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Association News

April 20th IVCA Educational Luncheon – Highlights of Online Companies: Chicago's Home Grown Successes

April 28, 2010 11:59 PM -

CHICAGO – It was a lively debate and enlightening discussion at the recent IVCA Education Luncheon sponsored by **Neal Gerber Eisenberg LLP**. The subject was Chicago online companies, and the distinguished panel included both investors and entrepreneurs.

IVCA Executive Director Maura O'Hara kicked off the proceedings by introducing **Lon Chow of Apex Venture Partners**, who suggested the topic and pulled together the panelists for the event. Lon opened the discussion with a few remarks...

"I came into the business in 1997, and spent the first 10 years of my career traveling between the two coasts. I didn't invest in a Chicago company until 2006, when I became an angel investor in Matt Moog's company. Through that involvement I became very exposed to the online community in Chicago. Today I'm involved personally or through Apex with eight online companies, all still pretty young."

He continued: "What I have come to recognize and appreciate is I always thought Chicago had an inferiority complex when it comes to comparing ourselves to Silicon Valley or Boston. I think there are a lot of pockets of good here, and I think online is one of those pockets. What we have here is great people."

Lon then turned over the proceedings to the moderator, **Michael Gray**, a partner at Neal Gerber & Eisenberg, the luncheon sponsor.

The panel included: **Brent Hill**, the head of Financial Services for **Google, Inc**. in the Midwest. **Matt Moog** is the Founder and CEO of **Viewpoints Network**. **Matt McCall** is a Partner in **New World Ventures** and **Portage Venture Partners**. And **Eric Lefkofsky** is President of **Blue Media, LLC.**

All the panelists experienced the internet business near its very beginnings, riding the wave through the bubble burst of the 1999-2001 period and emerging on the other side with new ventures, businesses, investments and success.

The discussion focused on the past, present and future of online companies in Chicago, and below are the highlights of the panel members comments at the luncheon...

Michael Gray: We want to look at the past. What were your experiences during the bubble and the post bubble hangover? What happened in that period for each of you and what did you learn?

Eric Lefkofsky: With some of the recent valuations of companies like Facebook, Twitter and Groupon and the like, have led people to think ‘are we in another bubble?' Having lived through first one rather intimately, there is no similarity. The euphoria at that time was just wild and such a land grab. It was so wide open and so many unknowns, that conventional business wisdom didn't apply. It was a race and we weren't sure where we were racing. That is a moment of time that is over.

Matt McCall: There are a lot of entrepreneurs and VC funds that are successful now because they experienced the disaster of 1999 and 2000. You will learn what works using the laws of gravity when you are in an absolute free fall, and you're thinking how did I get into this mess and I never want to be in pain ever again. That was the first thing a lot of us learned going through it. If you survived it, and came out the other side, you are a lot more mature now than you were going in.

The two lessons I learned was one, focus on the customer experience. If you are asking a consumer to change behavior or do something that is not natural to them, you're going to have trouble. That was the number one cause of death on the internet. The other lesson you need an inverse relationship between the amount of risk and the amount of capital going into a business. When you have high risk, low amounts of capital, and when you have low risk, lots of capital.

Matt Moog: The big lesson for me was that we raised all this money and hired all these employees and the infrastructure was so much more expensive than it is today. In 2000 we had 40 million in revenue and we lost 40 million. When the crash occurred, we has to let 250 people out of 400 go, and are revenues were cut in half. What was amazing afterward, is we only hired back 20 out of those 250 and were able to grow our income to 80 million.

It was a real lesson for me that throwing people and money at the problem is not always the solution. It taught me as a CEO not just to run with the euphoria and the excitement but to be honest with myself about do we have a reputable and scaleable business model. That takes longer, at least for me. The Midwest approach is to start slower, figure out the formula and get profitable, so you don't have to do multiple fundraising rounds as a way to grow.

Brent Hill: My experience in starting MVP.com, which originally was called Big Edge, was a lightning fast adventure. We went from business plan to Series A of a million and a half dollars very quickly. We were on the right path with our technology team, and partnered with a brick-and-mortar retailer, so we wouldn't have to invest a dollar of working capital to open the business. Our path changed when I went to a venture firm office in San Francisco, and they had Michael Jordan, John Elway and Wayne Gretsky lined up for promotional support, and that's what changed the profile to MVP.com.

We grew very quickly, shooting commercials with the best TV ad director in the business. We took maximum advantage of the athletes involved. We had John Elway at the Super Bowl and sponsored IMAX movies. That is something that none of us would do in the current state of the business.

After learning all that, the second time around with Feedburner it was the complete opposite. At its max, we had 30 employees at the company, but people thought it was a 100 person firm. We could have expanded, but we stayed focused on our core business and it played out pretty well.

My number one takeaway from the era is the importance of understanding customer acquisition costs. This was a decade before Google was in business, this was when you were signing the gold deal with AOL and the big portal deal with Yahoo!, those were the types of things that would expect to bring us customers, but at a fixed cost and not a variable cost. Anyone who lived through that decade has a much better understanding of customer acquisition as a function in their business.

Michael Gray: For me, it became a distinction between which people were good to work with and which people were not, and how people react when things are truly unraveling. You really learn got to learn what different people were made of.

[to the panel] **Are there any specific developments from that era that makes it more difficult or easier for companies in Chicago to succeed today?**

Hill: I think one of the things that is obvious from the era is that there is a lot of alumni that have stayed involved in the ecosystem in some way. Some are on their second or third start-ups, others have gone on to help Oprah Winfrey's interactive division operate better. So the alumni has gone on to help the Chicago interactive community in other ways.

Lefkovsky: I would say it has been terrible for Chicago. I think Chicago, more than Boston or New York, was almost waiting for the crash to happen. And then saying, ‘it failed of course.' We've been plagued by it. Even since we have this second city mentality when it comes to innovation and we're absolutely convinced that we don't build great technology here, we don't innovate, we don't change the world. We launch Big Macs and build railroads. Just as we were starting to get momentum, and then the downturn came, that's when people said ‘not here.'

This community does not foster innovation, you have to work extra hard here, because you don't get the same access to capital, talent and a communal willingness to let people take risks.

Moog: I guess I disagree, very respectfully. I've been to couple meetings with the mayor where he says get over this Silicon Valley vs. Chicago thing, we've got big successful companies here, innovative ones, fast followers and every kind. The good things about Chicago is you don't have the constant job hopping that other cities have. This is a huge advantage. I feel we've succeeded because we're in Chicago and we have close access to large potential clients, large agencies and a good pool of talent. The most important thing is talent. And the pool is here. Also if you have a successful venture you can raise money. I don't buy the argument at all that Chicago is not a good place to start an internet company.

McCall: What has been interesting, quietly underneath this, coming out of the ashes while the community overall said ‘see I told you, you can't do it,' the press pummeled everyone. The mayor went underground, everyone just abandoned us. Silicon Valley simply pulled out.

What came out of that was a series of serially educated teams, and noted the family trees here, the Orbitz team, the Feedburner team. We seeded a company last week, there are only five people on the team, but all five have twenty years experience and have been company founders for companies that have sold for between 400 million and 4 billion dollars. In Chicago, living here. We have talent here. I couldn't be more positive about this region, but you've got to cut through what people perceive to be the truth and what's really happening.

You have to earn it more here. We have rational, gritty entrepreneurs, and because you have to work so hard, that's what promotes the success. The customers are here. Every one of our first three successful companies were Midwest corporations. And it's the largest concentration of Fortune 500 companies in the United States is here.

Michael Gray: What other things can Chicago do concretely to be more successful in online business?

Hill: Good ideas and good people will get funded. The thing we need to do better in Chicago is the word ‘disruptive.' Groupon, Red Box are the type of disruptive businesses that brings customers to the average merchant. Those of the type deal we can do more of, good teams with good ideas, white board it and let's go.

If you have a business where access to media buyers and creativity types is important, Chicago has access to the four major ad agency holding companies have a significant presence, and they will make time for you if you have a great idea.

Lefkovsky: I love Chicago, but we have to first recognize where we are deficient. It's not that we don't have enough smart people or talent or all the essential ingredients. It's just that the community hasn't coalesced around in a way so that we can really compete. And if we want to be another New York we have to do that.

We have to throw tons of money at the problem. We need to throw 100 million at some technology projects, and other people have to throw money at it. We've done five technology deals since January, we'll do five or ten more this year, and we'll keep doing them. And hopefully that will spawn a lot of unbelievable stuff.

The media needs to embrace innovation and technology in new ways. They need to just honor it as holy and biblical and get behind every crazy idea even as it fails, so we as a Chicago business community start to embrace the people who takes chances and risks.

Moog: Chicago is a more practical and risk adverse culture. We need to figure out the entrepreneurs who are in local universities to stay here and sees them as a place that welcomes them and funds them.

McCall: Beyond money, we need the talent associated with it. Why I'm excited by what Eric's doing, is not just money, but it's money and then Eric telling them to take the business model this way, where you're kind of fostering and helping, that's how Silicon Valley was started. It's expanding on our number of successful entrepreneurs who really understand the eco-system and how to start businesses, and who also have money. When they put money in, they can also help make success.

There was a brief question and answer period after the panel discussion...

Q: Of all the elements of a successful entrepreneurial ecosystem – capital, competent entrepreneurs and business culture – where would you rank from best to worst those core elements in Chicago?

Moog: Everything is personalized. For me, raising capital was an absolute clinch. But I've heard that others, especially people just starting out, have problems with that. But my personal experience is that capital is readily available. The cultural issue is probably the biggest one, if you are trying to encourage people to leave their jobs and spend a couple of years to try and build something that nobody quite understands, can you really encourage that? They're here, and you can build it and quickly.

Lefkofsky: To rank them, Chicago has strong entrepreneurial talent. Access to capital is second strongest, it's there but needs to be there in way more volume. Culture is our biggest hurdle to overcome.

Q: You take about the 'white board,' but what specific advice would you have for someone who has the white board, is in Chicago, and wants to make a go of it?

Moog: One the biggest lessons I've seen lately is how inexpensive the infrastructure can be and how inexpensively you can launch. My advice if you are looking for a web based start-up, to develop the original version of it as inexpensively as you possibly can. Watch how people use it, what they're doing and look for opportunities on how to monetize it or grow it.

McCall: Know your strengths, I also say focus on the areas where you have passion and can focus on a market need. If you can slap your head and say, 'I can't believe there isn't a solution here.' And my number one criteria, what is the consumer experience like? If it's special, not only will it allow you sell your product easier, but they'll tell their friends. I other words, if you create a product that surprises somebody on the downside, you are screwed. But you design a product that surprises them on the upside, you are going to go viral at the end of the day.