



Caution puts limit on tech excesses

By David Gelles
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The excesses of the late 1990s technology boom created paper millionaires based on the most unlikely ideas. There was Pets.com, which raised almost \$100m while trying to convince people to buy cat litter online and whose sock-puppet mascot featured in an ad during the 1999 Super Bowl. And there was Webvan, which spent \$1bn trying to cultivate a market for grocery deliveries. Both shut up shop in 2000.

Ten years to the day after the Nasdaq hit its peak of 5,048.62 on March 10, 2000, the technology industry is learning to do more with much less. With the Nasdaq only recently having fought its way back above 2,000 to sit at 2,349 yesterday, Silicon Valley is a decidedly more sober place than it was a decade ago.

Gone are the days when dotcom start-ups spent millions of dollars for a Super Bowl ad slot and threw lavish parties to celebrate their initial public offering.

After a glimmer of optimism in the Web 2.0 era a few years ago, the recession put on hold any return to the glory days. A dearth of capital, a sense of frugality and a frozen IPO market are forcing entrepreneurs to make funding go further and wait longer for an exit.

The tech bubble was created by investors who believed that anything to do with the the Net would turn to gold. Nearly any dotcom business was able to gain funding and go public. In perhaps the most poignant sign of overreach, internet service provider AOL bought Time Warner in 2000, in what is regarded as the worst deal in history.

"Ten years ago, the bigger and bolder the idea, the more dollars would chase the idea," says Geoff Yang, founding partner for Redpoint Ventures, a venture capital firm that has backed the likes of Ask.com and Netflix. "What you found were a lot of ideas that were big and bold but that hadn't been proven."

The rising tide lifted many ships, making thousands of entrepreneurs

and investors fabulously wealthy. But when the bubble finally burst at the turn of the millennium, the majority of those companies were wiped out.

Silicon Valley has never fully recovered. Investment by venture capitalists - the grease that keeps the innovation engine running - has shrunk from \$100bn in 2000 to \$18bn last year, according to the National Venture Capital Association. That figure is unlikely to rise significantly in coming years.

And there are fewer people doling out money. The number of venture capital firms has shrunk from about 1,200 to 900 over the same period, and those that survive are unable to replicate once stellar returns. Yet while innovation continues apace, and entrepreneurs cannot help but be optimistic, their chances for an astronomical payday are few and far between.

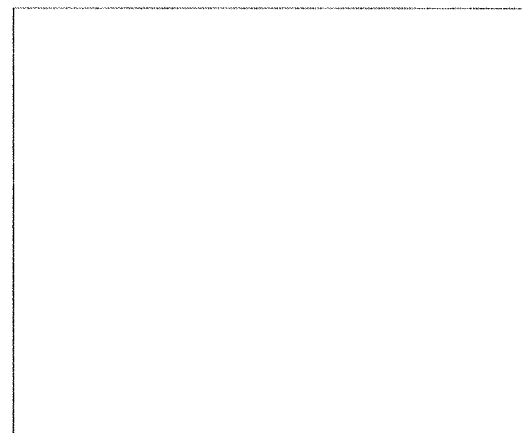
"This industry is much smaller today because of what happened 10 years ago," says Mark Heesen, president of the NVCA. "There's no question this industry is contracting and will continue to contract."

In the face of a shrinking industry, tech entrepreneurs today are a scrappy bunch - working on shoestring budgets, fighting hard in a crowded market, and decidedly more modest in their expectations.

Take David Lieb, who 18 months ago was a business school student growing frustrated by the task of entering the contact information of each of his classmates into his iPhone. A budding entrepreneur, he wondered if there was a way to tap two phones together and exchange contact information. Bump Technologies was born.

Mr Lieb, a former engineer with Texas Instruments, spent \$2,000 developing an application that let users swap contact details by "bumping" two iPhones together. Once available on Apple's App Store, Bump was an instant hit. Mr Lieb dropped out of school and moved to Silicon Valley.

Mr Lieb was able to scrape together \$45,000 to keep his company going. With several million downloads from the App Store, Bump attracted \$3m from Sequoia Capital, a leading venture capital firms.



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But 10 years ago, Mr Lieb might have been a millionaire on paper by now. Where the dotcom bubble made the simplest tech start-up a candidate for massive capital outlays, today's investors are more selective.

"VCs are much more aggressive in making sure there aren't 10 other companies doing the same thing," says Mr Heesen. "And you have much more realistic and better entrepreneurs today. There are better expectations on both sides of the aisle."

Yet the story of a company like Bump makes clear that, for skilled engineers with a good product, success is still attainable.

"Great companies are still being born today," says Ron Conway, a prolific investor and an early backer of Bump. "But it takes very little capital for a company to gain consumer traction."

With less money flowing, it is a good thing that companies like Bump are able to work on a shoestring budget. And at the same time, "the cost of building a business has gone down", says Mr Yang. "The drive down of commodity hardware, open source software, and infrastructure on demand has really driven down the cost of starting companies."

Though entrepreneurs may be scraping by, venture capitalists are still praying they make it big. It was IPOs by the likes of Pets.com and Webvan that delivered VCs those once-enormous returns.

But VC-backed IPOs, which numbered 270 in 1999 and 264 in 2000, are an endangered species. There were just six in 2008, and only 12 last year. "It's all about exits," says Mr Heesen. "Until you see a vibrant exit market it's going to be difficult [for venture capitalists]."

A vibrant exit market still seems a far off dream, although the rare company will be acquired for a princely sum. Facebook, Twitter and Yelp, which all seemed poised to go public last year, have publicly stated that they are not eyeing an IPO any time soon.

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