

Hit Based Businesses

From: Jorge E Ortiz S [jeortiz@interfibra.net]
Sent: Tuesday, June 22, 2004 9:08 PM
To: Lee Stein
Subject: **Interesting post from Venture Blog**
Lee:

Since you know the venture business AND the entertainment industries, you may find this perspective interesting:

<http://www.ventureblog.com/articles/indiv/2004/000670.html>

Silicon Valley and Hollywood Are Not That Different

Before starting my career in Silicon Valley, I was a strategy consultant working for a number of major Hollywood studios (see here for some of my writings on the music industry). Despite the fact that Hollywood and Silicon Valley don't really connect (except through Steve Jobs), business in both places is very similar - and very different from the rest of the country.

The reason is simple: both regions thrive on hit-driven industries, whether it be entertainment or high technology. A great deal of effort is expended on thousands of projects every year, but all of the money is made from a very few, high profile hits. Most of Hollywood targets consumers and relies on massive publicity, so it is more familiar to most Americans. Silicon Valley had a short burst of such publicity during the Consumer Internet craze, but for the most part remains tied to business press and trade publications, so the inner workings are more hidden from view.

The hit-driven nature of business leads to many similarities. Over the next few articles, we'll talk about the similarities as a way of exploring how the venture industry works. We'll begin with one of the most basic: why buzz is important to an early stage company.

Believing Makes It So

Both Silicon Valley and Hollywood are built on dreams - literally. There are a massive number of new plans for movies and startups floating about (trust me - I must see a tiny portion of them, and it's my full time job!). A tiny proportion of these will become funded businesses or movies. Most of them will die early from lack of interest - and it isn't because they are bad ideas. It is because the projects didn't manage to accumulate sufficient belief in their potential success.

Ideas aren't evaluated in a vacuum. It is an entrepreneur's myth that if an idea is good enough, it will stand on its own and generate enough interest to get funding. First-time entrepreneurs usually place too much value in the idea itself, getting fussy about NDAs and secrecy - same with producers and screenwriters. On the other hand, those reviewing the ideas have seen them all before. Roger Altman's movie *The Player* makes fun of pitch meetings in which movies are described only in terms of other movies - e.g., "Titanic crossed with Star Wars" or any number of other silly combinations. Any VC will recognize their own meetings in that movie as well - we use the same shorthand when describing companies to each other: "Google for blogs" or "Salesforce.com for supply chains". There are so many ideas, that by the time an idea gets funded we've usually seen it three times already.

Instead, it is the "virtuous circle" of belief that gets a company its shot. After all, it takes many groups to make a company successful: customers, employees, suppliers, managers, and financiers. For a startup, each group needs to be convinced of the support of the other groups. Customers don't want to buy from a startup that will run out of money, or fail to deliver because it doesn't have the engineering team it needs. Nobody wants to work for a company that can't get customers or funding. Nobody wants to fund a company that can't recruit. And nobody wants to give office space to somebody who won't be paying rent in another 9 months.

So projects in Hollywood and Silicon Valley get funded based on buzz. The more you hear about other people believing it will work, the more you believe it will work yourself. Getting all the people who need to believe in place doesn't make a project successful -- but it does give it a shot. The movie gets made, the company gets built, and gets its legitimate shot in the marketplace. The buzz doesn't guarantee success, but lack of buzz can guarantee failure by ensuring the project never gets off the ground, no matter how good it would be once it is launched.

This leads to an interesting conundrum: how does the buzz get started if everybody is sitting around staring at each other to see if others believe?

This is why it is so hard for outsiders to make an impact in Silicon Valley or in Hollywood. Insiders become expert at detecting the characteristics in a company that will lead other players to believe. It's no surprise that both places are highly networked with constant events & power lunches. Everybody is keeping tabs on the pulse of what others are looking for in projects these days so that they can look for the same things. (Who said VCs were like sheep?)

It is also no surprise that companies get funded in waves, just like similar movies are produced. Somebody in Hollywood greenlights a volcano movie, and suddenly everybody has to have a volcano movie in production. One VC invests in a social networking firm, and sud-

denly every major VC has to find some bet in the social networking area. It isn't irrational or lazy - VCs and studios really do need to have confidence that the pieces will come together. This is true even if you know ahead of time that the idea is less interesting than others you could invest in.

It's just the nature of beauty contest markets. Belief makes it so, but only if everybody believes together. Experienced entrepreneurs will tell you the early stages of their company are primarily about fostering this belief in all of the players back when you are selling nothing but an idea. It's not that different from a confidence game, actually, except in the intent to turn the belief into something tangible for everybody involved.

Coming Soon: Success Breeds Success