



Fish Where the Fish Are

by Tom Garland, ACT Venture Partners President

Many of you who know me know that I am a pretty crazy fly-fisherman. Recently, while wading on the pristine Trinity River in the bone chilling January cold in search of the increasingly rare Pacific run steelhead trout, I found time to reflect on my past four years at ACT Venture Partners. Much of that time has been spent in search of the illusive new market or customer on behalf of our ACT Venture Partners clients. Before I conjure up images of the Orvis catalog or Norman Maclean's classic "A River Runs Through It," it should be noted that despite spending countless hours on the stream incurring the wrath of my wife, who claims my gear and equipment budget may require a second mortgage, I've never actually caught a steelhead on a fly rod. So what keeps me coming back for more? I guess it is probably the same thing that drives entrepreneurs....the search for validation which is the subject of the next three guest musings.

*The first musing entitled "**Fish Where the Fish Are**" is about the preparation stage which involves planning for your customer validation fishing expedition. The second musing, "**Fishing Good.....Catching Bad**," is about how to get the most out of the limited time in customer waters. The third musing entitled "**All Fishermen are Liars Except for Me and You and Honestly I'm Not So Sure About You**" is about the post engagement stage in the customer validation process. Finally, "**Ain't Ever Caught One of Them Before**" is about validating truly disruptive technologies. Click here for more information on [ACT Venture Partners' Market Validation Practice](#).*

What is validation? When should it be done? Why is it so important? I wish I could say that most entrepreneurs start companies as a result of personally witnessing the pain or inconvenience of a work flow related issue. Armed with this perspective, they were inspired to create an inherently unique solution that gave birth to their new venture. Unfortunately that's rarely the case.

Most entrepreneurs start out toiling away in development labs of large companies continuing to push technology's inexorable march forward. When emancipated from the shackles of their previous employer, they naturally start ventures to commercialize familiar technologies and at best are distantly empathetic to a given customer's pain at a given point in time. As a result, we often see early stage companies who have developed technology in search of a problem to solve. To make matters worse, tomorrow's solution to today's problem may not be relevant when it finally gets to the market.

Market validation is more than getting "sound bytes" for the VC due diligence calls. Market validation is about listening. It is about talking to customers and channel partners and cycling their feedback into the product development process. It is about honestly testing market assumptions, hypotheses on customer pain thresholds and honest assessment of internal and competitive capabilities. It can exhilarate or devastate. Raw unfiltered feedback can cut right to the bone. It is never too early to start the validation process. Many early stage companies make the mistake of being way too far down the development curve before they start to engage customers. For many young ventures, validation can be a thinly disguised attempt to generate early revenue. These companies are past the point of no return in terms of making feature and schedule trade-offs based on the feedback and the iterative process is much less valuable.

Conducting market, customer and channel validation up front is likely to save development time later. Validation can accelerate the venture funding process and possibly prevent a big hollow "thump" sound when the 1.0 product hits the market and is not quite aligned with the needs of the customer.



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If you intend to stay in business past your 1.0 version, validation is a never ending process as markets, channels and competitors continually evolve as the dynamic equilibrium of the market is always in a constant state of flux.

What is the best way to get ready before you embark on your customer validation fishing trip? Below are some tips we've collected from some of the locals over the years who know the good fishing holes... think of them as best practices for pre-engagement validation.

- **Make certain you know what you are fishing for....**

One of the things I love the most about fly-fishing is the anticipation and preparation for a trip (often it is better than the trip itself). For days on end, I gleefully rummage through my fly-box and horde flies because you never know if the October Caddis is going to be a size 22 emerger or a size 14 Adult dry fly. Before I leave for the trip, I know what species I am going for. If I am going for steelhead, chances are my salt water tarpon flies are at home.

When early stage companies begin to engage customers for the first time, it is critical to understand the objective of the customer meeting. Often the object of customer validation may be for a Series A financing or possibly to get specific feedback for the Product/Market Requirements Document (PRD/MRD). These meetings are as different as night and day. The former is really about validating whether there is acknowledged pain and how acute it might be. If you are lucky and there is time available, you may get some high level opinions on competitive ways to solve their pain including feedback on your solution. Resist the temptation to launch into sell mode....listen and make sure your assumptions about the customer's pains are grounded.

Assuming the meeting goes well, have at least another few follow on discussions within a relatively short period of time to establish a relationship and increase the depth of the customer's technical understanding of your offering before you even think about using the customer as a funding reference. You would be surprised how often VCs tell us that a potential portfolio company used a customer reference for due diligence who faintly remembered the company's solution from the single 45 minute conference call 4 months ago! (Remember the IT executive has probably talked to dozens of vendors since your discussion.)

Getting feedback on feature and functionality for a PRD/MRD requires much more technical detail than validation for funding and, if possible, should almost always be done at a customer site at a time when a customer has the motivation, the time and the willingness to help. Try to involve as many functional constituents as possible on the customer side. Generally customers are willing to help you because if you execute you just might "scratch their itch."

These types of customer commitments are rare, and you should treat them like gold. Make sure their needs are representative of the larger market. Put them on your technical advisory board and include a stock honoraria if their company will allow them, and if not, make sure your advisory meetings are in Maui in February.

- **Tying One On**

"Tying one on" in fly-fishing does not mean a next morning hangover. "Tying one on" refers to fly selection to trick the trout into thinking the imitation bug is the real thing. The quality of the customer viewable materials is critical. Even if you are not quite real yet, you need to appear real to the customer with general product availability in the near term. The materials will make you feel tangible and will increase the chances of prospective validation candidates taking a meeting. Iterate on the materials after each meeting until you get closer to





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getting consistent feedback. This is a very important discipline and a never ending process.

There are a lot less IT folks doing a lot more with a lot less resources then there were a few years ago. If the customer senses you are not real and just siphoning their time to get educated, you will get labeled a "time waster." This will obviously reduce your chances of getting invited back when you do have something to say.

- **Before you get in the Suburban, do your homework. Get a stream report.**

Before I head out on a trip, I like to know what the action has been on the river I am going to fish. Are the flows high due to the storm? Is there an evening hatch? Have the steelhead started their upstream run from the ocean?

The same goes for customer validation. If you are working on a new VoIP solution, it might be good to know that the top tier financial services firm you are about to call just threw out the leading incumbent vendor for non-performance. Be prepared. Find an internal advocate or get on Google before the meeting and find out as much as you can about the customer's environment including incumbent vendors and the background of the individual with whom you will be meeting. At a minimum, you'll score points for being prepared.

As part of our market validation practice, we put together with our client our "wish list" of the titles, names and verticals of customers and partners we want to engage. The process of building a target database that everyone signs off on helps to build internal consensus and further define who the ultimate target customer will be.

Recent client engagements of what I would call category "cross-over" products such as Neoscale's storage security appliance that encrypts data in transit over the wire or the still stealth networking switch that also does per port security processing, may require multiple functional domain experts from a number of different areas to be present during the meeting. Without the right attendees, feedback may get distorted and could be an early indicator of a complex sales cycle. Strive to get full representation on the customer side and make sure that you involve key internal staff members such as the VP Marketing, VP Hardware and Software Engineering and the CEO in the meetings.

- **What happens on a fishing trip stays on the fishing trip.**

Okay, so you blew off the fishing trip and you went to Vegas. You get home and you want to make sure your fishing buddies are all saying the same thing to their significant others. Right?...we've all been there.

Centrify, an ACT Venture Partners client that has found a very clever way to unify access, policy and identity management across a multi-platform environment, has created a very neat internal positioning document that I particularly like. Think of it as a brief handbook for internal employees on how to consistently articulate the way Centrify wants to position itself externally. Even the lobby receptionist has the 25 word version down... which is impressive. The reason why this is important is that in early stage companies the paint is never quite dry on the positioning statement, and you really want everyone internally to consistently say the same thing whether it is to a customer or a VC.

- **What's in it for the fish?**

When I make that first cast, I know exactly what I am hoping to get out of the process, and when the fish rises out of the water for my fly I have a pretty good idea that it's looking to get fed.

What exactly does the customer get out of educating you? Entrepreneurs need to think through what the customer will get out of the interaction. They are giving you access to their most precious assets - their time and their insights. Most IT managers agree to customer validation meetings because they want to stay ahead of the technology curve. Their worst nightmare is to miss the next mega IT trend because they had their head



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down doing real work. Validation meetings are a time-efficient way to keep one eye on the business and one eye on what is coming next.

Mike Murphy, CEO of InQuira, a natural language enterprise search platform vendor, is the master at this. I have heard Mike's customers such as BellSouth, Honda and Mentor Graphics say things like "Mike spent the first two meetings trying to understand my problem which most vendors gloss right over so they can pound their chest about how great their product is." Even if customers don't buy InQuira's platform, time spent with a smart guy like Murphy talking about building world class customer experiences is well spent.

During the pre-engagement stage, I like to have the client write down their "Sacred Truths" before we talk to a single customer. These "Truths" are the basis for the company's existence and provide an outline to flush out the type of information we seek before we ever engage. The "Truths" should drive the customer viewable content to match the problem statement with the solution. The process of writing down the belief system generates great internal dialog in preparation for the quest. Documenting the "Truths" should also serve as justification for "tar and feathering" ACT Venture Partners if we leave a meeting and didn't dialog about them.

- **Ask a local or hire a guide.**

More than I would care to admit, I have tried unsuccessfully to fish unfamiliar waters on my own. While I flail away with my thousand dollar Orvis 9 weight rod (incidentally made from the same material as the Space Shuttle), some local walks into my hole with what looks like a pool stick with a piece of yarn and a chicken leg tied to it and pulls out more fish in ten minutes than I do in ten hours. I am not sure if it's that I am basically cheap (guides cost \$300 a day^[1]), or I am just stubborn and think I can figure it out. The reality is new unfamiliar waters always fish differently, and the quicker you can get a more familiar read, the more fish you'll get. Familiar guides accelerate the process.

There are many ways to do customer validation. From a past life, if you or your team have a strong network of contacts within a vertical market, senior IT staff will be more likely to return your calls. Due to the fact that many of us here at ACT Venture Partners have gray temples, over the years we have built up our ACT Venture Partners customer validation database to many thousands of IT contacts who are likely to take our call. We've done market, customer and channel validation quite a few times for our companies and for VCs, so chances are we may know the right target in the right vertical market who will take a meeting. This certainly doesn't guarantee success but will definitely make the process go faster with higher quality meetings.

A note of caution. Often companies use sales professionals to get the customer discussion started. Often these individuals are genetically programmed to attempt to close revenue even if all you have are PowerPoint slides! Inevitably, their enthusiasm (which makes them great sales people) converts the validation call into a sales pitch resulting in the validation candidate sensing what's coming and they clam up. Since our contacts know ACT Venture Partners' role is not to sell them but to extract and share data, they invariably open up more than the ACT Venture Partners client could ever imagine...all without selling!

Next month we'll talk about the trip itself and how to get the most out of the time you have in front of customers.... "Fishing Good...Catching Bad."

^[1] Moist ham sandwich and fish stories included...tip extra.

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Fishing Good....Catching Bad

Tom Garland, ACT Venture Partners President, continues with the second in his four-part series of guest Musings on Customer Market Validation.

The last guest musing, "Fish Where the Fish Are," was all about getting ready to engage customers for market validation. We've all seen the smug bumper stickers "A bad day of fishing is better than a good day at work" or "God doesn't subtract days from your life spent fishing." When driving behind these trucks I always wonder, "Are these people compensating for not catching fish or have they figured this thing out?"

Let's talk about some best practices to make your fishing trip better.

- **Get up Early and Stay Late**

The best fly-fishermen know the secret. Based on insect activity, trout feed early in the morning and just before sunset. When the sun is baking the water in the middle of the day, fish stay down and things get quiet. Most IT professionals are difficult to schedule especially in the middle of the day. So if you don't want your IT candidate to show up 15 minutes late, have to leave early while his pager constantly sounds during your presentation, try and schedule calls at the beginning of the day or at the end.

Be realistic and flexible about availability. It seems these days that everyone wants an audience with the same security IT professional employed in either health care or financial services who is particularly susceptible to getting pulled away unexpectedly.

- **Be observant**

Scout the river. Look around as things change throughout the day. One particularly memorable day, I was fishing a hole on the Pit River in Northern California in knee deep water when, unbeknownst to me, the hydroelectric dam a few miles upstream started gradually releasing water. I am a pretty focused fly-fisherman, and by the time I noticed what had happened, I was a football field away from shore in a strong current with water up to my armpits. Not fun and I would not recommend it.

Early in the discussion it is key to get the customer talking. Before you launch into your product presentation, take an audit of their environment and get context. Ask them to describe their environment or attempt to draw a topology diagram of what you think their infrastructure looks like. This is usually the ice breaker and important information will start to flow about their architecture, incumbent vendors and potential competitors. Be aware that some security folks in IT may not volunteer too much info on their infrastructure.

- **Be honest**

Let's face it. After spending thousands of dollars on gear and disappearing for weeks at a time, there are probably more socially redeeming activities you could be doing other than fly-fishing.

Be proactive. Take the offensive and address any potential landmines that are sure to come up. Talk openly about design trade-offs that you faced or even limitations of the v1.0 release. Customers will respect you for it. I love when a company is proactively armed with the slide entitled "Competitive Avoidance Strategies" because it shows you are not afraid to bring up competitors. You will almost always get some insight about would-be competitors that you didn't have before and by proactively bringing it up you will not be playing defense.

Reflect on the notion if you did not exist.... "How would customers solve this problem?" VCs cringe when an early stage company says "We have no competitors" and immediately process the words into "they have no market or they are totally naive."



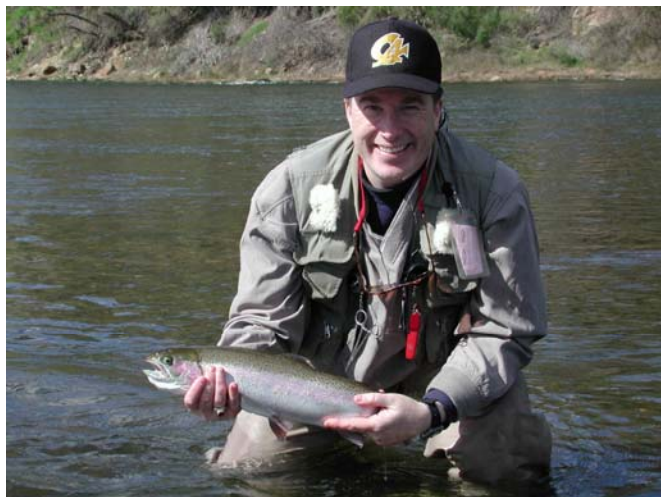
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I have had a few client situations recently where there was a well known problem with a number of alternative competitive solutions attempting to address the problem grouped around very similar approaches. However, these clients got a significant amount of mindshare from the customer because their solution was radically different than the clump of competitive solutions. Maybe it's the contrarians in all of us or it could be that the person you are speaking with has probably seen every vendor's slide set and they start to blur together. A solution that stands out from the rest of the crowd creates kind of a macabre fascination with IT professionals to see if this start-up is either really right or terrible wrong compared to the rest of the bunch.

- ***Match the Hatch***

This is fly-fishing secret code for throw a fly that looks remotely like the bug you saw splattered on your truck's windshield or flopping on the surface of the water being gulped by a steelhead. If the match is close... a fish might just strike.

Be humble. "This is what we think your problem is today but we are not sure. What do you think?" Get the customer talking early. Even if you are slightly off target, their corrective response or criticism is invaluable information for the next meeting.



Really listen to and concentrate on their responses. I continue to be amazed how often companies don't hear what is being said to them. In addition to listening to the spoken word, observe the body language and listen to what is NOT being said. When you see someone fold their arms and you hear, "Wow, you must be really smart because I understood 10% of what you just said. I am not sure we are a worthy customer... but Boeing would probably love this." This is a kiss off.

Some IT folks can be direct and others are experts in conflict avoidance. The latter group would rather avoid the debate with you and attempt to deflect you someplace else on a wild goose chase. Make sure you have your filter tuned to know the difference. Some entrepreneurs have an amazing gift to buffer only good comments and filter constructive criticism. Often ACT Venture Partners' role is to make sure everyone hears what is being said without reality distortion. Aggressively documenting these meetings is a good way to prevent this from occurring.

- ***Make a Good Presentation***

In customer visits, like fly-fishing, the presentation counts. Have your most articulate team member give the presentation. This does not mean your CTO has his mouth taped. A general rule of thumb...spend 50% of your time talking and 50% of your time listening and probing. I have seen many meetings where companies, obviously proud of their technology, spend 90% of their allotted meeting time on technical minutia and leave little or no time remaining to understand the customer's problem or get feedback. Technically drill down in follow on meetings if you earn the right to have another meeting.

The same thing goes for VC presentations. Keep it short and avoid bringing out the schematics for your product. VCs want to know how you are going to make them money and the sooner you get to this in your presentation the better.

- ***The Hit!***



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It's a beautiful thing...the right fly, the right cast and a beautiful fish arcs out of the water and strikes! Some customer meetings just go like that... right place at the right time with the right product and a customer actively seeking a solution to their pain.

When a customer says, "Where have you been? Finally!"...it doesn't happen that often, but when it does it is a beautiful thing. It is one of the reasons I love my job!

Please don't forget to probe about pricing. Recently, a client had a beautiful strike from an SVP of IT from a large, well respected Wall Street firm. However, due to the scale of the customer, it broke the company's shiny new pricing model. The company is still playing the fish as we speak.

- ***Catch and Release***

Most non-fisherman will question the sanity of someone who goes through all the effort and frustration to catch a fish and then let it go. For me, success is not defined as the catch ending up on my dinner plate but as a quick photo for memories and gently returning the fish to the stream in hopes of catching it again.

If a meeting does not go well because it's clear that there is not a problem or a good match, let the customer off the hook and do not subject them to endless power point about a solution to a problem they don't have.

Customer validation is the beginning of a long term relationship. When the meeting does goes well, I always like to verbally summarize what I have just heard. Partially it is to make sure I did not have my rose colored polarized glasses on, but also to allow the customer and our client to internalize what we have discussed. It is important to establish next steps if there are any. If you are looking for a VC reference, you may want to have additional discussions so the customer is comfortable when the VC calls and puts the customer on the spot by asking, "So, would you buy it?" I even like to give my VC customer reference a review "cheat sheet" email of all of the wonderful things they said in our meeting. If you want validation for your product requirements document (PRD), don't hesitate to get on a plane. Make sure the right players will be in the room to get representative feedback.

Often, when a validation meeting goes well, a customer will proactively ask to get on the beta program. Make sure they have a lab for testing and are willing to devote the resources to get the most out of it. More often than I ever think is possible, great validation meetings lead to unsolicited requests for betas. If the product does as promised...early revenue will often be the result. Little or no selling required.

- ***Watch out for Worm Dunkers***

Occasionally you are fishing a productive spot, and for whatever reason, there is another person (likely a local worm dunker) who is not very happy to see you.



Recognize this in the meeting. Often the person who is in the meeting may be responsible for creating the problem in the first place or may have just purchased the competitive solution you just railed against and their boss is in the meeting. There is not a whole lot you can do here, and it's key to get a sense of whether the person is just an influencer or a decision maker. If you were trying to sell this person something, it may be cause for lengthy debate, but since you are not (at the present moment) avoid the debate and try to make sure they don't pollute the discussion and negate feedback from others.

ACT Venture Partners has recently started doing videotaped, small IT focus groups with about a dozen participants around specific topics of interest to clients. It is very interesting to see the group dynamic when you get individuals with similar titles and backgrounds, but from different companies, in a room together. Focus groups are a great opportunity to conduct blind tests on different potential positioning concepts and evaluate perceptions about internal and competitive solutions.



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The third guest musing in the customer validation series, entitled "All Fishermen are Liars Except for Me and You and Honestly I'm not so Sure About You," will discuss what insights can be gained post engagement.

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All Fishermen are Liars Except for Me and You and Honestly ... I'm Not so Sure about You

Steelhead (and Salmon) are what scientists call androgynous fish. While they are born in fresh water, they adapt to also live in salt water as part of their migratory life cycle. Out of the 5000 or so fertilized eggs in their redd, only 300 will survive the many dangers from predators, pollution, drought, water diversion and worm dunkers. Against these odds, they innately follow their senses on the journey to and from the ocean only to return home to mate (once) and die. Any comparisons drawn between steelhead trout and entrepreneurs are for the most part purely coincidental.

In the last couple of guest musings "Fish where the Fish Are" and "Fishing Good...Catching Bad," we explored the pre-engagement and engagement stages of the customer validation process. We will now examine the post customer meeting phase.

- **All Fishermen are Born Liars**

My fishing buddy Trevor likes to say, "Nothing makes a fish bigger than the one that got away." He routinely divides in half the number of fish I tell him I caught and then discounts by 25% the size of the fish. I find myself telling my wife, "The fish was actually much bigger than it looks in the photo," (although, it's funny I always look the same size).

Possibly as a result of this, I am a big advocate of documenting customer meetings. There are a number of reasons for this. The first is that the process of transcribing meeting notes allows me to see trends that I might not immediately capture in the heat of the meeting. After multiple times of hearing quotes like "that's not the problem, this is..." my attention starts to peak. I like to build matrices with our "Sacred Truths" on one axis and every customer we talked to on the other axis. A quick scan of the rows will usually either yield a trend or an outlying data point depending on your perspective. It also can prevent instant memory loss, reality distortion from magnifying the positive and filtering out the negative. After a particularly bloody customer encounter, one of the founders of a client exclaimed to my disbelief, "Wow... they really loved the color of the box!"

Documenting customer meetings also provides a legacy to see how far you have evolved during the process of customer validation. Down the road this may be important to the new VP of Marketing or Sales. When the product is ready, they may want to follow up with the CISO at Goldman Sachs who was intrigued.

Finally, VCs know "All Fishermen are Liars..." In the due diligence phase, it is not unusual for our client companies to supply VCs with ACT Venture Partners' independent market validation reports. We are not J.D. Powers, but ACT Venture Partners' customer meeting summary documents tend to be pretty objective and will ensure that it didn't take 79 customer visits to produce those 3 perfect sound bytes. Some recent work with an exciting stealth company founded by a serial technical entrepreneur produced a very positive experience with Mohr Davidow Ventures' Jon Feiber and Donna Novitsky. The MDV team was a true partner in the validation process and had an insatiable appetite to consume the customer meeting analysis to probe more deeply into the opportunity while opening up their network as well.

- **Don't Shoot the Guide....**

Admittedly, after a fruitless (and expensive) day of guided fishing, I have been tempted to take out my '45. However after time goes by, I start to realize what Jimmy Buffet, the famous coral reefer philosopher, once said, "Hell, it could be my own fault."



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Most founders of start-ups are engineers and most engineers crave data. The trick is to diffuse the emotion out of the process and focus on what to do with what we've learned in the process. Our clients are intimately involved in the validation process. They write down their Sacred Truths belief system and their wish list of customer targets. They actively participate in the content creation process and the actual customer meetings. They are supplied with detailed post meeting write ups and analysis of what we have learned together immediately after each meeting. Somewhere during the process, a transferal of ownership happens which takes the feedback out of the realm of our opinion and into what the ACT Venture Partners client's customers truly believe.

People react differently to customer feedback. Many go through similar stages to what Dr. Elisabeth Kübler-Ross described in her landmark book "On Death and Dying" (Denial, Anger, Bargaining, Depression, Acceptance). This is not to equate getting negative customer feedback with terminal illness, but many founders go through a similar process when it comes to interpreting customer feedback. Many first time CEOs go through the stages very slowly as they get so entrenched in their own world view (based on their technological prowess and not on customer requirements). Sadly, it is often only after the company is shut down or the board brings in a new CEO that they finally accept it and can move on.

The faster an entrepreneur can process the customer feedback, the faster they can get to the most important question....the "Now What?" The right answer to this question will certainly impact engineering design decisions and product schedules while the wrong answer or ignoring the feedback could negatively impact the viability of the company. One of the best at assimilating and processing customer feedback is Ross Schibler, founder and Chief Technology Officer of Topspin Communications which was recently bought by Cisco. Topspin is the leading provider of programmable server switches whose channel partners include a few small companies you may have heard of (Dell, HP, IBM, NEC, Hitachi and Sun). Ross also founded Rapid City Networks and then sold it to Bay Networks. As a seasoned entrepreneur, Ross has the ability to unemotionally process customer feedback and make actionable decisions about product features and functionality based on the data which propelled Topspin through the five stages all in the same meeting.

One of the reasons why I love working at Acuitive is Mark Hoover. Mark has the uncanny ability (and 20 years of networking experience) to process recent customer data in real time and then sanity check it for consistency with his own career data points. Mark quickly gets to the "Now What?" With his legendary bed side manner, he can lift up the spirits of a founder by saying "The bad news is that your 40 targeted customers don't care much for your Swiss Army knife, but the good news is I think that you may just have the best Can Opener in the industry."

- **Size Does Matter....**

Hopefully, you have not had the good fortune of running across a California Fish and Game Warden while fishing. If you have, then you'll know these dudes don't mess around. If the fishing regulations call for only one adult steelhead over 24 inches in your possession, they won't hesitate to take your license, your gear and your truck if your prized catch is an inch short or your license is on the kitchen table.

Joel Jewitt, fellow Stanford GSB classmate and one of the founders of mobile platform provider Good Technology, once told me that there is no such thing as a vertical market for a start up. Joel's insight was that what looks like a single vertical market like financial services is really comprised of many small thin market slices (retail brokerage, equity trading, back-office, etc.) with diverse product requirements that can be difficult for a start-up to track and satisfy. The trick is to find as many slices that have enough in common to build a viable business and leverage your development.

I like what InQuira has done with their natural language enterprise search platform. They have targeted complimentary markets such as retail financial, retail telecom and retail automotive due to the fact that these complimentary slices all have what InQuira calls "well understood industry intents." With this leverage, InQuira knows how to focus their sales, marketing and development budget on a large enough market opportunity. Only after achieving significant revenue traction in known market slices, InQuira asked ACT Venture Partners to



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design a market entry strategy for other segments that exhibited similar characteristics to their core competency markets. There is no way to figure this out unless you talk to customers and understand their needs in complimentary verticals.

It is a fairly common practice for ACT Venture Partners to help companies quantify their Total Available Market (TAM) size, Served Available Market (SAM) and Share of Market (SOM) as part of the validation process. Despite enthusiastic responses from customers, be cautioned about having too narrow a focus. After the initial positive feedback, clients can be faced with the dilemma: to achieve a respectable revenue ramp they will need every customer with an installed base of 5000 VoIP phones deployed in a single location (all seven of them) or every existing geographically distributed SAN to buy the gateway appliance to make the numbers work. You don't want to be the undisputed leader in a zero billion dollar industry!

Resist the temptation to jury-rig the TAM/SAM/SOM model to make the numbers look straight up and to the right. While you might get funded, you will need to believe it yourself. Eventually, these expectations set in the funding process will have a big impact on the next four to six years of your working life.

- **Evaluate the dependencies**

You spot a huge steelhead slurping flies in a gin clear run across the stream and your heart starts pumping and your mind races...if you could just do a modified double-back haul cast into the wind to avoid the oak tree behind you and then bank your fly off the mid-stream boulder to have a chance at that fish...well that is a pretty big dependency. I hate dependencies where I can't control my own destiny.

Often this is the case with start-ups. The fate of your company is in the hands of someone else, such as a service provider or an OEM, and your success or failure may be highly dependent upon them. Often these companies know the leverage they have over start-ups and are not afraid to exercise it to get exclusivity, preferred pricing terms or even go to the Machiavellian extent of driving a vendor out of business to get access to IP. In the validation process honestly try and get a sense if your success is dependent on someone else. Soundpipe, a developer of private label low cost IP-PBXs, found that despite a 10X price benefit compared to comparable solutions from branded vendors, access to the distribution channel mattered as much (possibly more) than the product itself. Soundpipe was acquired by a public company (Comdial) and finally got access to the dealer channel.

Having spent over ten years in the proprietary hardware platform business, it is exciting to see the opportunities for start-ups being created as a result of the proliferation of low cost Linux compute nodes and the removal of many dependencies from proprietary platform vendors.

- **Keep your Eye on the Big Fish**



The harsh reality of the start-up world is often there is a really big fish swimming in the same hole as you. Whether it is Cisco in network infrastructure, security and telephony, Microsoft in anything related to the desktop, Network Appliance or EMC in storage, or Apple in consumer MP3 devices, being able to realistically anticipate the likely response to your market entry will increase the likelihood of your survival (or



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being swallowed up).

I was recently in a customer meeting where the CIO of a very well known financial institution was constantly one slide ahead of me during my presentation. After much head nodding (a good sign), I went for it and said, "You could have given the presentation instead of me. At the risk of going out on the limb it sounds like if company X had this product today you would buy it... right?" He replied to a dumbfounded audience of founders, "I love the product concept and you are two years ahead, but there is no way I would buy this critical component from a start-up. Cisco does not have this functionality today but it is on the Q4 2006 product roadmap." This factoid would have been good to know before start-ups burn through inordinate amounts of venture money trying to directly take on the Big Fish solely based on being cheaper or having some feature that the Big Fish didn't have at the current moment (nor did they for that matter despite impressive power point).

In recent years, corporate IT has gotten even more conservative. Frankly, they have been burned by too many start-ups. Without some extraordinary technological breakthrough based on proprietary IP or a "hair on fire" problem with an immediate solution only available from a start-up, taking on the Big Fish in their home pond is ill-advised.

Instead, I like Centrify's approach. Early on they began working closely with the Big Fish, which in this case is Microsoft. They have built a platform that integrates most flavors of UNIX and Linux into Microsoft's Active Directory so there is one directory structure for cross platform access, identity and policy management. It is a novel approach to the single sign on issue, yet leverages the fastest growing directory from the industry's most stable provider who is not threatened nor likely interested in supporting non-Microsoft platforms in Active Directory. When roughly 40% of Centrify's market validation customer meetings end up with unsolicited requests to be in their beta program, you know they have something. Now the Big Fish is asking to do joint customer calls because there is no threat, it fills a niche in their story, and furthers their mutual objectives.

Life is short. This beats banging up against a wall trying to figure out how to guerrilla market against the Big Fish who will attempt to freeze the market with their five year product roadmap while they play catch up.

So what happens when what you are working on is so disruptive that talking to customers is a futile exercise because your company will fundamentally change today's natural technology trajectory? We will examine validation for disruptive technologies in the final Musing in our series entitled, *"Ain't Ever Caught One of Them Before."*

Tom Garland is President of ACT Venture Partners. His market, customer and channel validation practice has helped match dozens of ACT Venture Partners' companies to his contacts with Fortune 1000 IT professionals in search of... the elusive customer. To contact ACT Venture Partners directly regarding its Market Validation Practice, email info@ACTventurepartners.com.



“Ain’t Never Caught One of Them Before”

Tom Garland, ACT Venture Partners President, concludes his four-part series on Customer Market Validation.

After the last three Musings on market validation, my friend Bob Cousins, a serial entrepreneur in his own right, chuckles and says, “Congratulations Tom, if some of the great entrepreneurs of our time read your Musings there would be no PC, no laser printer, no Ethernet or other countless discrete breakthrough innovations.” The final topic of the validation Musings series is about Validation for Disruptive Technology. How do you validate a market or product concept when your target customer does not understand the practical applications of your technology or perhaps they may fear its implications?

I recently had the pleasure of attending the US premiere of “BRILLIANT! The Blinding Enlightenment of Nikola Tesla.” The production has haunted me these last few weeks. Born in 1856 and emigrated to the US in 1884, Nikola Tesla was one of the most significant inventors of our time with dozens of inventions including x-ray technology, AC power, RF oscillators and robotics, just to name a few. For the non-Tesla aware reader, here’s the short version of his story: a brilliant young penniless immigrant inventor came to America; worked for the monopolistic incumbent vendor with too much at stake to jeopardize their cash cow (GE/Thomas Edison/DC Power); got screwed over by his employer; quit; formed new company to compete against former employer; developed superior product with no legacy technology (Westinghouse/AC Power); made fortune; serially invested in new research; lost fortune; went mad; died in relative obscurity; intellectual property confiscated by FBI upon death.



If Nikola were alive today, what would he have thought of my past three Musings on Market Validation? Probably not much, I suspect.

Smarter men than I have written countless business tomes on the topic of disruptive innovation, such as Clayton Christensen’s *Innovators Dilemma* and Andy Grove’s *Only the Paranoid Survive*. The basic premise is that enormous wealth generation opportunities get created when large successful incumbent vendors fail to capitalize on a new technology or business model, resulting in catastrophic consequences to their market share and possibly their viability. Large companies like AT&T ignore to their period or can’t get the organization to move fast enough to take advantage of a disruption like VoIP.

The Age of Incrementalism

Frankly, we have not seen much disruptive technology in the past five years. Customers just don’t seem to have much of an appetite for it as they recover from the hangover of technology over-indulgence in the era prior to this. Also, the funding climate and resulting capital structures for start-ups have not encouraged a “Think Different” mentality. With the IPO door locked shut, a good outcome was a base hit M&A transaction filling some missing feature that an established vendor lacked. As a result, the vast majority of ideas buzzing around Silicon Valley and other hot spots of Information Technology have been incremental and are easily validated or invalidated via the customer acid tests described in previous Musings.

Disruptive Signals

But, to a small degree at least, we seem to be coming out of the purely incremental innovation mode. That means that in some cases we need to apply techniques for validating potentially disruptive ideas that are quite different from the techniques for validating incremental ideas. Therefore, the first question you must ask yourself is “Am I disruptive or incremental?” in order to determine which playbook to operate from.



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It is “cool” to be disruptive, and therefore, there is a strong pre-disposition to filter facts and observations to convince yourself of that fact. But if you have an incremental concept and you manage it as a disruptive one, you will almost certainly make a series of strategic and tactical errors that will be fatal. Putting it in Geoff Moore terms, if you are entering a Tornado and are spending your time looking for Beachheads over Chasms, you are dead meat.

My definition of truly disruptive technology is when usage behavior is permanently altered forever.... for example, after a customer experiences a new solution and exclaims, “I will never do XYZ again.” Disruptions can permanently alter vendor landscapes and shake the customer’s status quo.

There are some indicators and questions to ask yourself that help determine whether your idea is disruptive or not.

- Is there a fundamental economic incentive present to adopt the disruption? (We mean 10x-100x better than today.)
- Do you believe that today’s market leaders have too much at stake and are inherently incapable or unwilling to “eat their children” to participate in the disruption?
- Are customers ready, willing and capable of changing their entrenched usage scenarios?
- Is there a shift in empowerment that gives new users unprecedented access to the disruption?
- If you are successful, will your mother or grandmother eventually hear about it and perhaps be impacted by it?

The goal of this Musing is not to conjecture on current technologies that fit the disruptive label, although I suspect that some forms of nanotechnology, grid computing, fuel cells, and wireless mesh networks may fit the label. I recently caught up with Paul Koontz, GP at Foundation Capital. Paul updated me on a company called DUST Networks*, one of his portfolio companies. DUST’s SmartMesh Networks uses very low power wireless sensors coupled with their wireless mesh networking platform for sensing and control applications. For example, imagine during an Iraqi fire-fight, an army helicopter sprinkles tiny nodes over a battlefield in a remote area to help track troop movements, update weather conditions and build portable communications infrastructure; imagine nodes measuring the sugar content of pinot noir grapes before a cold front hits; or imagine building automation, industrial monitoring and even remote security using the same platform. That all seems pretty damn disruptive to me.



WARNING: Don’t force fit the disruptive label. Yes, it’s “cool” to be disruptive. But not all disruptive ideas are valuable and certainly many incremental ideas are. The key isn’t to try and be in one category or another but to determine which you are in and then use the proper techniques for validating and developing the concept.

Disruption Validation

There is no science to validating disruptive technology. Frankly, sometimes it is a leap of faith and no methodology pontificated by a consultant like me is a sure thing. The problem is that often it is very difficult to validate in advance a truly disruptive technology because the customer has to experience the technology impact first hand and then have their behavior changed. The rules are all different since there are no known large incumbent vendors or other start-up competitors to emulate or critique. Much of validation is spent on education, anticipating behavioral or usage mode changes, probing and floating trial concepts to see what comes back. Zero time is spent on the length of the feature list and the list price. It is important to recognize that in certain cases a technology may be disruptive, but the customer may not be ready for it because they are unable or unwilling to be on the bleeding edge of the transition.

This often leads to “circular logic” where an entrepreneur who wants to be disruptive uses poor customer feedback as the evidence of the disruptive nature of his idea! The problem is that often this is also a symptom



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of a bad incremental idea. Again, this is why it is important to be objective about the disruptive/incremental label.

TIPS ON VALIDATING DISRUPTIVE TECHNOLOGIES

There Need to be Early Signs of a Market Somewhere

Let's not forget in the validation process, you are using other people's money which by definition is finite. The VC model just simply doesn't work unless there is some available market within a 24 to 36 month window.

Paul mentioned that the DUST board spends a lot of time developing a disciplined approach to validating potential market opportunities, so they don't get too far down the path ahead of the market and revenue. The initial market TAM (Total Available Market) does not have to be huge, but it does need to be an indicator. Technology often spills over from some other unrelated market and creates new and existing opportunities in unexpected places. Who would have thought that a DARPA grant to explore alternative communication systems in the event of a nuclear attack would have ultimately resulted in Amazon.com? In DUST's case, the founding team had been around the military and DOD applications from an academia perspective and recognized the commercial applicability of the technology before others had a chance to exploit.

The challenge for DUST is to filter the most relevant applications that will yield early revenue traction to grow or bridge to other markets that will drive sustainable revenue. In the beginning, validation will be both push driven (i.e. here is what we think is a good application let's go find someone to validate) and pull driven (i.e. sifting through the unsolicited inquiries from the outside).

Target the "Visionaries"

An important validation tip: have the wisdom to know whose opinions matter. In the case of a disruptive idea, the last people you want to talk to are operations people or others for whom the cost-of-change is a primary non-motivator. You need to talk to the visionaries.

Who are they? Where can I find them? A visionary is someone inside of a company who often has a high IQ, is strongly opinionated, possesses an innate ability to piece seemingly unrelated business and technical building blocks into a passionate vision, and, oh yeah, are often exasperated that others can't see how obvious their vision is. Visionaries are critically needed inside of big companies, but they can be troublemakers. They constantly question the status quo, much to the chagrin of senior management who are often focused on the next 90 days in the quarter. Perhaps the poster child for a visionary is Jim Clark, founder of SGI, Netscape, Healthon/WebMD, Neoteris, Shutterfly, etc. Jim saw the technical computing market as a niche and recent advancements in integrating graphics algorithms into commodity silicon were going to rob SGI of their stranglehold on the high end 3D graphics market. He single handedly dragged SGI kicking and screaming into the consumer and interactive TV markets with deals with Nintendo and Time Warner. Unfortunately, SGI could never see beyond their core markets which were evaporating. One memorable moment at SGI for me was getting Jim's idea on a project I had been working on for six months around developing a single board computer for kiosks and arcade machines. Jim, silent during most of my presentation, uttered seven classic words I will never forget, "This is a pimple on my ass." Given his next few jobs, I guess he was right.

Don't Ever Use PowerPoint

Virtually 100% of the time, Visionaries will be completely bored and will be writing on the white board anyway. I am not quite sure why this happens. It could be that Visionaries grasp the idea more quickly than most mortals; maybe it is a control thing; or maybe they subliminally think if you had time to make nice charts that you can't creatively think on your feet, hence making your idea, by definition, non-disruptive. At the end of most of these meetings, my head usually hurts because the meetings have a complete non-linear progression, and topics are fairly random. It is only until we meet again or we have time to reflect on what was said that the light bulb goes on.



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The key validation trick with Visionaries is to internalize their world view and assimilate other data points. If they are consistent, figure out a way to become aligned with them for your mutual benefit. This is a classic example of run as fast as you can to get out in front of the parade before it passes you by.

Lunatic Fringe or Early Adopters?

In my career, I have found Visionaries in government, military and university research labs working on applications ranging from GRID computing, scientific visualization and HPC. Often Visionaries migrate here because there is often access to funds, general avoidance of people in suits and fewer short term time constraints to produce results. The validation trick here is not finding these people. They are fairly accessible and often speak at conferences. The key is making sure they are a proxy for a real market in the future. An example of this tension is work being done on the massively geographically distributed cluster project called the TeraGrid project. This project is a joint effort between Caltech, Argonne National Labs, San Diego Supercomputing Center and the NCSA. Hopefully, this work will advance the commercial industries' understanding of how to scale low cost clusters and geographically distribute storage for applications like disaster recovery and pharmaceutical drug discovery.

Occasionally you do find large commercial companies with individuals whose job it is to think "out of the box" and have a longer term strategic view. Whether they are "Imagineers" or VPs of Next Generation Infrastructures, Directors of Vision, etc. treat them like gold.

One of ACT Venture Partners' favorites is Robert Keahey who is responsible for EDS' Technology Strategy and Architecture. Robert is a regular visitor to the Silicon Valley in order to keep his finger on the pulse of start-up activity. One of Robert's responsibilities is to make sure EDS does not miss a disruptive technology cycle and lose ground to IBM Global Services or some other large service provider to the Fortune 1000. Robert has helped champion Data Center Markup Language (DCML), which is a vendor independent XML based spec to increase data center automation, system wide management and utility computing. Robert's evangelism of DCML is a part of EDS' Agile Enterprise Framework and could have huge margin implications while offering unprecedented flexibility as a competitive weapon and avoid vendor-lock in. Another Validation tip: try and create disruptive technologies that make grand initiatives like utility computing real vs. "Market-structures." I like to think a part of my job is to help keep Bob's pipeline busy so ACT Venture Partners portfolio companies can fill some of the holes in the EDS vision.

If you can't find visionaries that share your vision, your idea may be in trouble or it may just be a bad idea or too far ahead of it's time. But even if you do find visionaries who share your view of the future, you are not out of the woods. It will be up to you to think through the market opportunity associated with a shared vision, because usually the Visionaries you find who share your vision don't care. Sometimes these people often only build exactly one of whatever they are working on.

Form a Federation of Disrupters

Many Visionaries are keenly aware of the work of their peers...sort of like how superheroes like Spiderman keep tabs on Superman and The Hulk's latest capers. A neat tactic is to get these Visionaries in a room together on a regular basis. This could be a formal Technical Advisory Board, an invitation only "Birds-of-a-Feather" at a conference (i.e. in the graphics industry every year at SIGGRAPH pow-wow) or even a focus group if you can find a geographically central location. Why this is important is that with a room full of respected peers there is a much greater chance of consolidation of ideas and collaborative constructive feedback which could be lost in 1-1 meetings.

Visualize Life after the Disruption and Work Backward

Many passionate start-up founders often take on the roll of hucksters, peddling their vision to anyone who will listen... normally at conferences or on trade show floors. Back to Tesla. Every now and again to demonstrate the safety of his DC power, Edison was known to use Tesla's AC power to electrocute a stray cat, dog or even



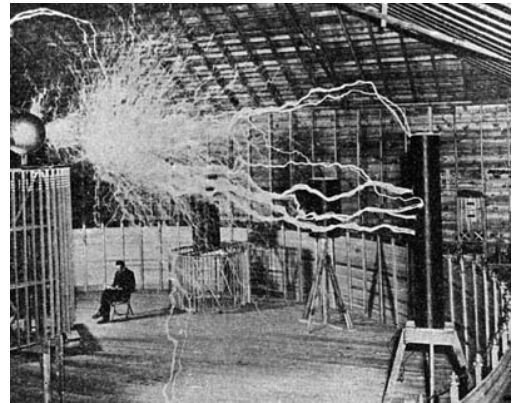
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Topsy the Coney Island Carnival Elephant. Even if the customer doesn't immediately understand the impact of the disruptive technology, it is critical to shape a vision of life after the disruption and make it as tangible as possible.



CAUTION: Killing something or using it on yourself is NOT recommended in the demo.

Visualizing the future may take the form of mock-ups or software demos that start to get the customers thinking about why they won't be able to live without your disruptive technology. Hopefully, over time they will realize that their incumbent vendor could not possibly satisfy this vision. Edison was incapable of embracing Tesla's AC Power because he had too much riding on harvesting his own patents for DC power.**



In 1988, John Sculley, former CEO of Apple Computer came to speak to my class at the Stanford Business School armed with a block of wood in the shape of what would become Apple's PDA (the Newton). The former soda pop marketer showed us a video called "Knowledge Navigator: A Day in the Life," evangelizing about how our lives would be transformed by our handheld personal digital assistant utilizing hand writing and speech recognition to manage our daily information, our schedule, our communications and our workflow. It should be noted that this was before the ubiquitous penetration of the World Wide Web, Palm Pilot, VoIP conferencing, Wi-Fi and even Windows GUI etc. As a student, it had a huge impact on me. I wanted to be a part of a company that was trying to make this tangible vision happen, so I went to work at Apple in the late 80s.

Visualizing life after the disruption will help you better understand who your target customer segments are.

A Giant Leap of Faith

The validation process for disruptive technology may or may not yield immediate concrete results. Hopefully, the validation process may de-risk or help to sharpen the original vision and may attract evangelists along the way.

Unleashing potential wealth creation opportunities is all about taking calculated risks and having the courage to step off the treadmill to pursue a dream or a vision. From Edison to Sergey Brin, most will fail and few will succeed. I am proud to be an American and live in a country where a penniless immigrant like Nikola Tesla has the opportunity to change mankind for the better for future generations. It has been one of the greatest honors of my life to play a small part in helping these dreamers validate their visions. Dream On.

*ACT Venture Partners has no affiliation with DUST Networks.

**An interesting footnote from Edison's showmanship was the invention of the electric chair.

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