Cisco Oral History Panel
Part One

John Morgridge and Don Valentine

Moderated by:
John Hollar

Recorded: November 19, 2014
Mountain View, California

CHM Reference number: X7309.2015

John Hollar: Let's start with part of the pre-history of Cisco. And Don, these questions are primarily for you. So by the time of the Cisco investment, you and Sequoia had made a lot of investments. And I'm wondering, what was it about the Cisco opportunity that really got your interest?

Don Valentine: In thinking about how to begin, I'm not sure if someone else will cover the fact that venture capital hadn't been invented yet. So the experience at Fairchild, which was the company I worked for-- they couldn't raise money. Arthur Rock, who became famous for raising money and for financing Fairchild and Intel, had 30 different organizations turn him down. And the amount of money that was needed to be raised was a million and a half dollars. Couldn't do it.

Someone decided to contact Sherman Fairchild of Fairchild Camera and Instrument, and he put up to the money that allowed Fairchild to be started with a million and a half dollars. And if you think about that goes back to about 1957. You had eight founders and a million and a half dollars. And they were going into the semiconductor business-- even then, a very expensive business.

OK. Enough for my version of the prelude. If you look at the companies that are listed here-- 3Com, Apple, Atari, Oracle, Electronic Arts-- four out of the five companies that you chose to list and ask about, all were microprocessor based. Microprocessors were vital to their creation.

I left Fairchild having had as a tutor, Bob Noyce-- the patent holder for the first kind of computer on a chip that was ever invented. So I have always felt I had an unusually significant advantage in knowing the future that almost no one else in the world had, with one possible exception-- one of the founders was Eugene Kleiner who, of course, was the Kleiner in Kleiner Perkins. And Eugene certainly had enough of a sense of the importance of it, but he was not anywhere near the customer and the application the way I was.

So Atari-- the first investment Sequoia made-- was microprocessor driven and had a very quick and unusual history of success. Apple, of course, was driven by a microprocessor. 3Com and Electronic Arts were derivative investments, from my point of view. We knew that the first personal computers needed, in some way, to be networked, although that word had not been invented yet. But they were one on one and couldn't talk to one another.

And I had the fortunate occurrence of meeting the guy who started 3Com-- who, interestingly, was an MIT emmigrant to the West Coast. And it was he who invented the Ethernet. And the Ethernet was the beginning of connectivity of small computers to small computers, small computers to big computers, which is what caused the trouble and a problem that only Cisco solved.

So here we have the beginning of a focused investment based on the existence of the evolution of the microprocessor. The one exception to that is the investment with Larry Ellison in Oracle-- totally a software company. Microprocessors didn't matter. They had a different opportunity. And it's amazing to me how these opportunities happen constantly in the last 40 years I've been in this business. There seems to be no end to the need for the creation of solutions to problems that were never known to exist before.

I think we'll talk about the opinion I had about Cisco. Because before John joined, this was a company located in a personal residence in the tony town of Atherton until the police shut them down. There were too many big brown trucks coming by every day picking up, since that was the factory and they were shipping out of the house. Neighbors complained, I'm sure.

And the company began with a very amusing beginning and they didn't let up in having unusual occurrences continuously. It's the only company I've ever financed where they had drive-by shooters leaving spent cartridges on the ground and holes in the building 'til the software developers said, please move us out of here. One of John's problems that he had to solve when it came along--I suspect a unique problem in the history of companies, never mind just Silicon Valley.

So it's a company rich in different kinds of unheard of phenomena. And I'm not sure when you want to go there. Is that enough on those five companies?

Hollar: Yes. Yeah, absolutely.

Valentine: The beginning of our lucky streak?

Hollar: Yes, it is. Let's talk now about Cisco and specifically how you got interested and involved with Cisco.

Valentine: John had a party last Wednesday sort of to celebrate a number of things, one of which was the people who were there-- some people who are there-- and it was very nicely done. And you had these old war stories, some of which were not told, and we were telling them to one another in the audience. It's the only place that, in addition to the drive-by shooting, I witnessed a fist fight in public in the company. So there were very heated people-- heated opinions.

Len and Sandy were introduced to me by one of the people at the party. And the person who preceded Sequoia, Ed Leonard was the attorney-- then a partner at Brobeck. And I believe he may have opened the Brobeck [Brobeck, Phleger & Harrison] -- a San Francisco firm-- had opened their office in the then partially discovered happening called Silicon Valley.

And he introduced me. And he said, I don't know whether I'm doing you a favor or not, but I'm about to introduce you to a company that have very, very different people in it and maybe only you can deal with the unusual nature of the founders. And that's when I met the five founders, three of whom don't get anywhere near the recognition that two of them did.

But there were other people. And these were all employees, as I remember, of Stanford University-- not students, not faculty, but employees. And I don't know that Stanford ever requested any ownership.

I don't know if that was ever negotiated or discussed. Maybe John can shed some light on that. But Stanford was very gracious about having employees starting a company literally in the shadow of the Hoover Tower and with things that they'd learned from other employees in other universities who had the same problem.

So maybe it's time to introduce the problem. The problem is called-- or was called, in those days-- a broadcast storm. What happened was IBM and most of the Seven Dwarfs-- and Hewlett-Packard, as an example, had opened offices east of Eden. And they manned those offices with minicomputers and with microcomputers or personal computers.

And the trick was to send information from the branch office back to headquarters. So on the West Coast, you have headquarters mainframes of different flavors and varieties, and packets of information were being sent from the East Coast. And these packets moved at light speed. So you have, going cross country, something that's coming as fast as possible.

And what happened was, there was no ability for the packet to recognize the terminal or the mainframe that they were supposed to lodge the data. And what you had are, technically, collisions of information at the wrong destination, called a broadcast storm. And it got worse and worse and worse as the people who ran the computer departments of corporations allowed personal computers and minis into their system. And this is the company, from our experience at Sequoia-- and we financed 1,000 companies-- that had a market demand the likes of which I have never seen.

Hollar: You said-- and there's a quote here-- that, "Customers were tearing the hinges off the door to get the product." So was that your experience?

Valentine: Yeah, I think John should take credit for that. But it was the nature of the size of the problem, which is one of those things we always look for-- what problem are we going to solve by backing a company? What's the solution that's needed out there to facilitate something working better?

And there are number of companies that were involved in creating the internet, not the least of which was a government agency called DARPA, which became ARPA. And what they wanted to do was link all the computer centers in the country-- universities, corporations-- and have an ability in case the Russians-- at that point in time, who were our nominal enemy-- did something like attacking us. And we had a way to communicate broadly around the country through this network being created by the government. Fortunately, as far as I know, it was only activated in practice and never activated in reality.

But that was the impetus for the creation of a particular protocol called TCP/IP. The last two letters were the critical ones-- Internet Protocol. And that was one of the things that the technical people at Cisco latched on to as being a partial solution to the broadcast crashes that were happening everywhere. Same opinion held, interestingly, by the founder of 3Com-- that this would happen and the networks of the world would have to get bigger and bigger and learn how to talk laterally as well as longitudinally.

And that's why I thought the opportunity was so fabulous at Cisco, because they had a product-- many people had products that were like a router but were not a router. And what really worked is Cisco's product was able to route that packet at light speed to the right destination. Switches were common, but switches couldn't do what Cisco's product did.

Now, when we financed the company, they had no building. They had no manufacturing with real manufacturing people and procedures. And they had this very dedicated, quite passionate group of people that managed to jerry-rig these things together and ship them to the initial customers who were equivalent employees of another university who had all the same kind of a fundamental technical problem. So maybe we should pause there and find out where you want to go.

Hollar: Let me ask you about this. Can you walk us through the sequence of how you determined you needed to bring in an experienced manager, how you found John, and that whole process?

Valentine: What was Chuck's last name? Do you know?

John Morgridge: Chuck--

Valentine: Was it Sudcliff?

Morgridge: Sudcliff. Chuck Sudcliff. He was a rent-a-president.

Valentine: Yeah.

Morgridge: By the month.

Valentine: When I arrived on the scene, they had five or six people-- really technically oriented, development oriented, but no one who really was interested in or knew anything about production, customer satisfaction. They were just people who recognized a horrifically technical problem and they were after it. And I didn't have a way to finance this company because in addition to not having any kind of a managerial presence, we didn't have a sales manager.

So the first things I did after we invested-- I had what John affectionately calls a rent-a-president. It was a guy that I knew who was a good listener. And he followed the instructions I gave him about renting him by the month to follow a set of instructions to get some order in this exploding opportunity. I also hired, as I prefer, an absolutely fabulous, killer salesman that was--

Morgridge: We called him the router barbarian. You either bought or it was scorched earth.

Hollar: What was his name?

Valentine: Jerry--

Morgridge: Terry.

Valentine: Terry Eger. And I don't know if he'll talk to you, but he will make a terrific character witness. John inherited the rent-a-president, who was very gracious about his tenure. And he inherited Terry, who was a booking machine-- just a wonderfully fabulous one on one salesman. And that's how we began.

And it was very clear that-- as is quite often true-- that among the founders, you have a lot of technical horsepower, but you don't have sales or you don't have manufacturing or you don't have marketing and you don't have a president. So we began a search. And we did our normal in-house search. We went to all the people we knew that might be interested and found out if they were candidates. And we engaged a search firm whose name was Schweichler

Morgridge: Yep.

Valentine: Lee Schweichler

Morgridge: Lee.

Valentine: Lee Schweichler. And he was on the job and he was the one who recruited John. Now, when I was doing the reference checks, I checked with a guy who I think lived, then, in the Boston area. And Stratus was a company in the Boston area, right?

Morgridge: Right.

Valentine: And I didn't know him well, but he seemed to know some of my peculiarities. So I called him and asked him about John, who was this-- what's Bill's last name?

Morgridge: Oh, Foster.

Valentine: Bill Foster.

Morgridge: And you knew him probably going back-- well, he tried to start his company out here, which was Stratus Computer. He was an HP alumnus.

Valentine: So I called Bill and I told him I wanted to have him give me a reference. Tell me about John. And he said, well, I don't know you well. And I'll tell you anything you want to know about John, but let me warn you about John.

First, he said, your personal reputation is being very cheap. He said, well, this guy is cheaper. That's a big positive for me. Second, do not let John ever buy the wine. You'll end up with half gallons of Ripple with screw top caps, which is not my favorite brand.

So he had told me two things about John. One was a caution that I've always followed. I never drank anything John bought. I either bought it, brought it, or didn't have any.

And that's how we began. I talked to the company that John was with on the West Coast. And we talked about this so I would remember Sam's last name.

Morgridge: Wiegand

Valentine: Sam Wiegand - Fabulous person. He had been at one of the other companies we were invested in called Tandem. At any rate, this was a company on the West Coast.

Sam gave John a great reference. And I had three finalists to talk with. And at that point in time, which was in the late '80s-- no, '87. We financed the company.

Morgridge: Yeah. '87, I think it was.

Valentine: My favorite question to ask presidential candidates was to tell me the most outrageous thing they ever did, at which time I stopped talking and waited. And the silence is a killer for a lot of people. And one guy got very flustered and said well, I've never done anything outrageous. I thought to myself, OK, you're dead. I'm not about to hire you.

Because this was a company that was going to require dealing with, as is often true of founders, very, very different kind of people-- very narrowly oriented-- but they knew everything about that subject. And anybody you brought in as president is not going to know anything about the subject by comparison to the depth of their knowledge, which is a matter of carefully learning what it's all about. Fortunately, John had come from a computer environment and this was a microprocessor driven world.

So you had to understand how computers work and you had to understand there was something about to happen call the Internet. And not a lot of people understood the Internet in those days. It hadn't been deployed. DARPA was sort of close to the vest with information on how they intended to deploy this and why. And John was the obvious candidate. Anybody who's cheaper than I am is a favorite candidate of mine.

Hollar: Do you remember how John answered the question, what's the most outrageous thing you ever did?

Valentine: I do not. And I was hoping--

Morgridge: And I don't either.

Hollar: That's a shame.

Morgridge: But I've done a lot of outrageous things, so--

Hollar: So John, at this point in your career, how did you first hear about the Cisco opportunity?

Morgridge: A chap that worked for me at Honeywell and subsequently at Stratus was called as a prospect for the job. And he didn't want to leave Boston and he referred Lee to me. So that was how the contact was made.

Hollar: Had you heard of Cisco?

Morgridge: I had not heard of Cisco, but I was a believer that someone was going to solve this problem. And we had just sold Grid to Tandy. And I had been approached by a lot of companies-- it was at the time when the in vogue thing were super minicomputers and all you had to do was raise $50 million to try and create one.

And I knew that wasn't what I wanted to do. And I knew that someone was going to come up to the solution for the problem that Don described. And so as soon as I heard about what-- I didn't understand the product technically, but I understood the product-- what it was targeting and what solution it was trying to create. So it was high on my list.

Hollar: How did you go about getting the information that you needed to make a decision about whether this was the right thing?

Morgridge: Well, I had seen the need-- both at Stratus and at Honeywell, prior to that-- for this kind of capability. And what I did is I asked-- after the job became real for me, I asked for the names of 12 customers. And I contacted the 12 customers.

I got through to eight. I asked three questions. Do you have Cisco equipment? Is it working successfully for you? And do you intend to buy more? All eight answered yes to those three questions.

Hollar: Were you shocked?

Morgridge: Pretty shocking. If you had done that for Grid laptops, you wouldn't have gotten that kind of a response.

Hollar: And how did you come to understand the core technology behind what Cisco was doing? Was that easy for you to pick up and understand?

Morgridge: I think anyone who had spent their life in the computer industry-- I had worked for a mainframe company. I had worked for a minicomputer company. I had worked for a laptop computer company. This seemed like a natural next step, tying all of those capabilities together.

Hollar: So Don has talked about this rare and high-spirited founding team. How did you first encounter-- well, let me back up. Before I ask you that, what had you heard at this point about the founding team and the situation at Cisco?

Morgridge: I really hadn't heard a lot. I knew they had come out of Stanford. I knew that they had operated out of their home, which struck me as clever and kind of pushy. And the fact that Atherton I don't think even permits restaurants, let alone a manufacturing capability. But they had a wonderful facility with a big circular driveway and a three car-- I mean, it was perfect-- very low cost.

Hollar: So I think we have come across-- I'm flipping over to page two if you're looking it, but if you're not, that's OK. I think we've come across, in some of the other oral histories that we've done as part of this, that there are many versions of the story of the first encounter that you had--

Morgridge: Depends on who tells it.

Hollar: Exactly-- with Sandy [Lerner] and Len [Bosack] [Co-founders of Cisco].

Morgridge: Right.

Hollar: So I'd love to hear both of you talk about that in your own words.

Morgridge: Well, certainly the encounter with Len was pretty conventional. The encounter with Sandy was more difficult because she was a different kind of a personality. And she actually had been the computer manager or network manager in the business school. And that may have colored her attitude toward MBAs.

Hollar: What was her attitude?

Morgridge: Well, she didn't have a high opinion of them. And I don't know the background that caused that. And I think they also had a difficult closing relationship with the university, because they were actually running a business on the campus and that's not generally acceptable to universities. You can develop there, but you don't take orders and do manufacturing and use, as has been implied, the university's credit for working capital. So that may have colored her--and that, of course, colored her feelings toward me because I was a graduate of that institution.

Hollar: What were each of them doing at that moment when you stepped into the company?

Morgridge: Well, at that point, Len was in charge of engineering. And Sandy had a broad scope of activities-- some formal, some informal. But she certainly ran-- she ran manufacturing-- or to the degree that it was being done.

And it was in a room smaller than this, actually. It was in the room about half this size when I arrived. And she had strong opinions in the whole area of marketing, documentation, customer relationships-- all of those were kind of either formally or semi-formally in her portfolio.

Hollar: Don, what are your recollections about their first meeting?

Valentine: Len, to me, was an introverted development engineer-- not much of a manager-- maybe supervisor was more fitting-- shy and somewhat hesitant. The only thing I found them very passionate about at one point in time was ensuring that we had enough cans of Dr. Pepper-- soda water. If you can be addicted to Dr. Pepper, he was addicted.

I was drawn towards Sandy because Sandy was very articulate, highly opinionated. And she had one opinion that really resonated with me. Because by now, Sequoia had financed enough companies-- enough computer companies-- that I knew that the product on arrival didn't always work and certainly was not user friendly. And the gem of the idea that she had was that we should have a customer advocacy capability and a leadership that ensured the customer was well taken care of, that the products were as advertised and worked wonderfully. And if by accident a customer had difficulty, we would rush to the scene and take care of the customer.

So she was different than anybody I had encountered in any of these other companies, all of which were computer companies, with a couple of software exceptions. And she was the leadership thinker and executor in this area. And in my opinion, it was well ahead of all of the other creative technical achievements that the companies had.

And I think, although I'm a decade out of touch with the details at that level, she created this atmosphere in a start up and I had never seen it before. And it was rocky roads when you're starting something new and you have to sell it to the other people. And if it weren't done the way Sandy had envisioned it, you heard about it.

So instant feedback from Sandy. No feedback from Len. So you had an unusual leadership partnership in that one was the source of unlimited numbers of ideas, often delivered at high decibels. And the other one was very soft spoken. And if, in fact, you had not done some kind of design thing the way he wanted it, you'd have a little quiet conversation about why and what it was all about.

But to me, she was a critical element in the launch of this company. And as things rolled out, I think among the other employees and the eventual management, I was viewed as her sponsor-- her supporter. And I never thought of it in those terms, but I did really become enamored with the concept of customer advocacy and the fact that Silicon Valley, historically, stunk in that area and is not a lot better now, especially since the products are immensely more complicated.

And it was interesting to me-- when I reflected on it, she was a lot like Steve Jobs. Steve was very tough on the products and the way they were designed. And if he didn't like the way it looked-- didn't like the way it felt-- he'd start over. And he also delivered the message at high decibels.

And they both had very creative beginnings to solving what should be conventional problems. When you buy a toaster, you plug it into the wall and you put the bread in and it works. Computers don't work that way, unfortunately, still.

Hollar: So John, how did you insert yourself into the organization as it stood then and begin to get at some of these issues?

Morgridge: Well, the first thing you do is you-- spent probably the first month or more meeting everyone. I'd already talked to the customers. The company was operating with a backlog. The challenge areas certainly were in manufacturing and also in engineering, in terms of having a schedule and meeting that schedule. Because as you grow, you need a more programmed kind of an existence. So I spent time finding out what their definition of winning was across all of those activities.

And certainly, one of the things that came out of it was the desire to do an IPO. I think that all the constituencies-- the venture capitalists, the employees, the founders-- had that as a goal. And by setting that as a goal, then there are a number of things that have to be done in order to meet that goal, not the least of which is a qualified team. And in a very fast growing organization, a qualified team is a little different than in one that's going to take five years to an IPO verses one that-- at that point, I think we were projecting -- I joined in the fall of '88. And we were projecting an IPO some time in 1990-- so a relatively short period of time.

Hollar: What were the revenues when you joined?

Morgridge: When I joined, the revenues for the prior year were, I think, $5 million-- maybe a little less. And the revenues for the prior quarter-- I joined in October-- were a million dollars. So they must have been less-- they must have been several hundreds of thousands for the prior year.

Hollar: How big did the two of you think, at that point, Cisco could become?

Morgridge: Well, I certainly thought it would be a multi-billion dollar company.

Hollar: Even at the very beginning?

Morgridge: Even at the very beginning. The need was so great. All you had to do was-- I had been in this industry for a long period of time.

And I was actually looking for this kind of an opportunity because I thought someone had to solve that problem. That was based on my experience at Grid. That was based on my experience at Stratus. To some degree, that was even based on my experience at Honeywell.

Hollar: And Don, how about you?

Valentine: Well, I think John had a better perspective than I, since in our closing negotiation to have him join, in addition to the other forms of compensation, he persuaded me to sell him shares at my price, which was the only price for preferred A that existed, and we did that. But the thing that I didn't hear carefully enough-- try to imagine. We're in a garage. More things don't work than do work. We had no management infrastructure.

And John softly told me-- and I didn't get it-- he said, I'm going to leave when we hit sales of a billion dollars. And I thought to myself, you've got to be kidding me. I won't live that long.

All these companies that I had financed previously, I never thought of them in terms of a billion in revenue. Because here we are, scrabbling along at a few hundred thousand dollars, and we had to build the entire company yet. So one of the things I also wanted to get in on the record was very helpful reference from Hewlett-Packard.

Morgridge: Yeah.

Valentine: Hewlett was using the product. And as I spoke with their technical people, they said to me-- and this is a rule of marketing as far as I'm concerned-- the world is made up of 80/20. 80% of the people will not know how to use the product. 20% of the people will know how to use the product and do not require a lot of support.

Find the 20%. Forget the 80% because they'll eat you alive in terms of holding their hand while they employ the router. And I've always believed that marketing premise and I've held every other company I was involved in to that test. Do not deal with the low hanging fruit unless they're really smart about what the product is.

Hollar: So you came to that test through HP's advice as the result of learning about Cisco? Is that the way this worked?

Valentine: Yeah.

Morgridge: They shipped the prototype to HP-- some prototypes-- with the idea that they would have them for some period of time and return them. They refused to return them. And HP, every quarter, was probably in the top five customers that we had. So they ultimately became a competitor or are a competitor, but they were a big customer early on.

Hollar: So what were the early business and technology decisions the you had to make, John, in order to get this thing going**?**

Morgridge: Well, I would say the first and major decision was-- I mean, there was a series of strategies that you set out. And particularly today, marketing, finance-- you can outsource engineering. Many companies do-- how you do sales-- a distributor versus a direct. So there are a lot of decisions.

And a couple of the early ones that we made-- number one, we decided we would not be an integrated manufacturer. If you're growing fast, it's easier to take over someone else's factory than it is to build one, staff it, and buy the equipment for it. So one of the very early decisions was-- and we were right on the cusp of the ability to do that. There were a few companies that were just starting to do it, but it was not the norm. And so we pushed that envelope very early on.

Hollar: Was that controversial?

Morgridge: No, because we didn't have a whole lot of manufacturing in place. A later decision not to get in the education business was more difficult because we had already started. But I had seen the DEC experience with doing in-house education and decided we ought to outsource that to our customers or partners. So that was another decision that we made.

In terms of engineering, I always thought it was mandatory to be internal, and likewise, service. Service at the start is always done by engineering. Actually, everything is done by engineering.

They're some of your key sales people in the beginning. And they're your key service people. And that's why we always had Dr. Pepper, because they were the first ones there and they selected it.

Hollar: That was the fuel?

Morgridge: The soft drinks.

Hollar: Yeah.

Morgridge: Well, there was a dependency that I really wasn't all that sensitive to.

Hollar: Ah. The customer advocacy point that Don made earlier, was that pervasive through all of that early growth period?

Morgridge: I think that it evolved in a relatively short period of time. Because the two founders were only with the company from its registration, which I think was in '86, and they only stayed a year after the IPO. And within that time, Sandy established that philosophy.

Sandy really was the driving force to create the company. And the person that she had to drive the most was Len. And she used the customer as the leverage to get Len to finish a product. Len was one of those engineers that could always think of a few additional things that we could add to the product to make it better. And oh, by the way, it may take another 30 days.

She'd say no. We have a customer that needs it now. Finish it and get it out. So she, to a large degree, was the kind of engine that caused it to happen. Len would not have caused it to happen in the same dimension.

Hollar: It seems you stayed on track toward that goal of having an IPO in that period that you encountered when you first got to the company. How did you do that?

Morgridge: Well, part of it was, as Don said, he had three requirements in his investments-- market, market, market. And we were blessed with meeting all three of those requirements. And it was a lot easier to run a company that had a backlog than it is to run a company that has no backlog. I was at Stratus Computer. We never had a backlog.

And our backlog at Cisco was the function of a number of things, not the least of which was it took AT&T 30 to 60 days to deliver a T1. And so if you ordered the equipment today-- you either ordered the T1 before you ordered our equipment, but if you ordered it at the same time, you guaranteed us a window before we had to deliver. And we used that window. We knew what our quarters were going to be because we always operated with a backlog. John Chambers has a bigger challenge because AT&T and the network have now caught up with its capability.

Hollar: A number of people, in the oral histories we've taken, have talked about how important-- how almost emotional the IPO was and what it meant to everyone. Can you talk a little bit about the offering and how that went?

Morgridge: Well, we had the typical road show. You need four things to do an IPO. You need three items that are up and to the right-- revenue, customers, and profits.

The fourth is something called the vision-- the vision thing. What is the vision? Because the market wants a vision because that helps them understand the size of the market. And so we had those.

We struggled most with the vision or satisfying the requirement for the vision. The other three, we had in abundance. So that was kind of why the IPO was successful. Don, fortunately, accepted the role of negotiating-- I think it was supposed to be the price. What it turned out to be was the wine that we served--

Valentine: Post offering.

Morgridge: Yeah.

Valentine: Morgan Stanley bought the wine I wanted.

Morgridge: Right.

Hollar: And what one was that?

Valentine: It was a Richebourg. It's a DRC Burgundy. But there's a point or two I want to get into that hasn't come up yet. For the IPO timing-- and John was not in agreement-- I wanted to introduce an asset to the company who would be a technical advisor on how to make a presentation.

Morgridge: Oh, yeah.

Valentine: And John said, I don't need that. I'm terrific at making presentations.

Morgridge: I didn't say that. I just said I don't need that.

Valentine: He said he doesn't need it. Jerry Weissman is the man's name and he's a former-- ex television producer.

Morgridge: Right.

Valentine: And he has a lot of experience. We were one of his early mentors in terms of getting him in front of our management teams. John was, to be charitable, willing, but not very.

Morgridge: Not excited.

Valentine: Not excited to go hear Jerry's pitch and maybe sign up for Jerry's treatment.

Morgridge: Right.

Valentine: And the net of it all was that after John's exposure to Jerry's approach, he had all the major management figures of the company all go see Jerry to help in their presentation style not only from a content point of view, but it turns out that-- and I've seen this for years-- technical people have a hard time dealing with an audience, locating their hands. And if they have, God forbid, slides, they turn their back to the audience. So they're now talking to the board instead of to the audience.

And Jerry did what was obvious. He got everybody sensitized about how to present and what the objectives were. And he's had a fine career counseling and he must've counseled dozens of Sequoia's companies.

Morgridge: We called him, affectionately, Mr. Packaging. And he had all the tips about not covering your privates, never pointing, always-- if you see John Chambers, he's always got his hand--

Hollar: The hand is open.

Morgridge: --open hand. Four by fours-- nothing on the chart longer than four words; no more lines on the chart than four lines. And we attributed it to him, after the fact, that he certainly had an impact on our offering, probably to the extent of an eighth of a point. But he was very helpful.

Valentine: My accounting would be a little more generous.

Hollar: OK.

Morgridge: Right.

Valentine: But I wanted to go back before the IPO timing. Because Cisco made a decision which has become the obvious decision of choice. The hardest thing in starting a company is the second product. What do you do next?

Morgridge: Right.

Valentine: OK. So we have this monumental problem that's killing everybody around the country-- around the world. And they come up with a router. And the router deals largely with few of the protocols that are flying through the ether.

And one of the things they did was figure out, in some kind of an analytical ranking, which protocols made sense to support. Was the DECnet important? And you'd go through the different kinds of computer transmitters because that's effectively what's going on. And they, little by little, selectively became able to deal with all of these different protocols with the basic router product that didn't have to have entire redesigns.

A lot of the companies we finance do not have that facility and don't anticipate it. And as a result, product number two is very difficult to birth. Software is easy to do that second product because the first product is release one. And you got to have release nine-- or in the case of Microsoft, release eight-- 20 years later. And you're still releasing part of the product forever.

Well here, they embraced the idea of being a multi-protocol supporter. Fabulously important decision. I don't think the world has ever recognized how important that was.

The second thing I wanted to get into the record-- and when John first articulated this, I thought he was maybe drinking some bad wine or something-- but we were not going to have any competitors. We were only going to have partners. And my question to myself was, well, we've got a company out there by the name of Wellfleet.

There's a number of people out there that are making the transition to routers from switches or trying to make their switches do some of the things that the router did. And the company was adamant. I remember attending a conversation-- what's the company that was physically very close to us? He was at the party last Wednesday night.

Morgridge: Yeah. Right.

Hollar: I have a number of companies listed here-- Cabletron, SynOptics--

Morgridge: SynOptics.

Valentine: SynOptics.

Hollar: SynOptics?

Morgridge: Andy Ludwick.

Valentine: Andy Ludwick. We had a meeting with Andy Ludwick and John explained that we're going to be partners. And Andy said, how can we be partners? We're competitors.

And yeah, we're competitors, but the real competitor's name is IBM or the real competitor's name is DEC. The real competitor isn't Cisco and SynOptics. An alliance between what apparently would become competitors would be beneficial in the short term. You work out the long term when you get to the long term.

The guys at Cabletron were very hostile to the idea, but they were hostile to everything as I remember. Remember the two guys at Cabletron? They were a Boston company. And this, to me, was also so counterintuitive that you didn't acknowledge competition. You acknowledged partners. And transactionally, they made it work.

Hollar: And how did that work?

Morgridge: We had what we called the Hub Club. There were a whole series of companies, SynOptics being one, but there was Cabletron. There was a company that-- there was 3Com. There was the company that 3Com bought that was out on the East Coast. There was DEC.

And what we did is we impregnated their hubs with routers. Now, as a practical matter, there weren't many of those sold. But what it did do is it gave us access to the real estate that they controlled, which was on each floor.

We were in the basement with a router. They were on each floor with a hub. And when switches came out, we'd already kind of encroached-- I mean, it was a great strategy.

And I met with those guys all the time, even with-- this is not from me-- but there was one of their competitors that referred to Cabletron as the junkyard dogs. Well, they weren't junkyard because they started their business cutting cable to length. I mean, that's how that business started. You could buy cable, but it all came in a fixed length. And so you had to-- but if you called them, they would cut it.

They bought a roll. And that's how they started-- the two of them-- cutting cable. And so they were, quote, "one of our partners." But it was a great way to get to know all your all your potential future competitors.

Hollar: Right. Yeah.

Valentine: And from my point of view-- slightly outside, looking in-- how better to approach existing or potential competitors and persuade them that we're partners?

Hollar: Right.

Valentine: And that was the key-- the persuasion-- which gets me to one other story. And I don't remember whether it was after the IPO or not. But the combatant was IBM. And the person's name was Ellen Hancock.

Morgridge: Ellen Hancock.

Valentine: And she was in London and she refused to see us. I think we ought to get that story a little fleshed out.

Hollar: Talk about that.

Morgridge: Well, we actually were very close to signing a deal with IBM. And we had actually convinced the people in Raleigh that this was a good idea. And it was kind of this same impregnation theory, which ultimately came to pass because in the end, they sold that business to us. Cisco actually bought that business from IBM.

But she just was so against it and said, we can develop the product. We don't need-- and she overruled the local management. And I don't know that it made-- it would've been, from our standpoint, just kind of a marketing plus to have had that relationship, in terms of selling our product to IBM customers. But as it turns out, we ended up taking that business anyway.

Hollar: Why did she refuse to see you?

Morgridge: I think she refused because she was just determined that they were IBM and that they could create their own solution.

Hollar: Hmm.

Valentine: See, the answer that I remember-- and I'm not suggesting--

Morgridge: They probably didn't like--

Valentine: I'm not suggesting that John's answer isn't the answer, but the answer that I seem to remember is Ellen Hancock said, one company has recently taken advantage of us at IBM and it's not going to happen again-- certainly not on my watch. That was Microsoft who took over IBM's personal computer business. Gates was so clever. He did it without a product. He had to go out and buy a junkyard dog product in order to have anything to offer them.

And she was infuriated by the fact that IBM had effectively given away a position that they would have dominated in the personal computer if, in fact, they didn't go about it in a panicky way that they did. And she blamed it all on Microsoft. So she was not going to allow another major area of business to be infiltrated and dominated by a competitor. Now, I remember the ultimate outcome slightly differently, also. What was the name of their network?

Morgridge: Well, they had a protocol-- actually we did that protocol for Boeing, although they never used it. I can't remember the acronym that they had for the IBM protocol-- AT something.

Valentine: We volunteered to go to London. Wouldn't see us. And the outcome-- Ellen had moved on and had a brief tenure as one of the many presidents of Apple-- different story.

I remember slightly differently that IBM at that point in time got so frustrated that they basically gave us their network-- then the biggest network extent, certainly in North America-- if in fact we would agree to hiring some employees in the East and taking care of the IBM customers that were part of the network, which was a huge, huge thing. They had so many employees. At one point in time, I had a quick count and we were about to take on more employees there then we had here.

This was really a big, big transaction-- a big win to assume a network of this size, with IBM's imprimatur on it. Ellen had gone to other pastures at IBM. I don't know what she was doing, but we were very thankful that it was not run from England anymore and it was not Ellen running interference, keeping us out of that business.

Morgridge: Cisco tried to develop that protocol. And we baptized a series of our engineers as IBM specialists. And we created that protocol and tested it, I think, in Mexico. It never quite performed very well.

And it was at that point that I said, where are the genuine IBM nerds? We want to go there. And it was in Raleigh. And that's why we went to Raleigh. We went to Raleigh to capture genuine IBM nerds to develop the product.

And of course, as a result of that, ended up greatly expanding our market. And Ford Motor Company was part of that whole scenario in that they had a large IBM network and they were a good customer of ours. And they said, why don't you go after this other segment? We'd be a better customer if you did.

Hollar: If you could get the IBM segments?

Morgridge: Yes.

Hollar: Before we leave the IPO period and that period immediately after it, I want to just talk about the decision by Len and Sandy to leave the company and how that all came about. Can you just talk about the sequence of events there and that story?

Morgridge: Well, I would say there were a couple of factors involved. Certainly, Sandy felt strongly about how the company ought to be run. And it was not only relative to my leadership. It was kind of, on various days, the leadership of others in the company.

And one of the things I've learned was that when I came on board, the employees were basically hired by Len and Sandy. And in the period of the year that followed in, quote, "building an experienced team," I hired all those people. And as a result, their relationship with Sandy was a different relationship and one that was probably less tolerant of her idiosyncrasies than the prior group of employees. And ultimately-- and Don can tell the story because I wasn't there-- they approached you.

Valentine: No. When they approached me, you were there, because I gave you the handoff, but--

Morgridge: Well, I was there, but I wasn't part of the group that came to see you.

Valentine: Right. No--

Hollar: There was a group the came to see, though?

Valentine: Yes, but just a little color. There was--

Morgridge: Not too much, Don.

Valentine: This was always a high decibel company where things were talked about in semi-public ways. And as I characterized Len, he was very soft spoken. But Sandy was quite direct and very specific and a tough grader.

And as John points out, there were progressively more people that she didn't know than she did know. And they became very intolerant of what I considered to be the author of an incredibly important aspect of the company-- the customer advocacy part of it. And I think it's distinguished the company for a long time in the early years.

Anyhow, I arrived in my office one day. I had made a prior stop and I didn't get there until about 10:30. And the receptionist said, the conference room is loaded with people waiting for you.

And there were, I think, seven Cisco vice presidents. And I just sensed that they were not there to celebrate my birthday or anything. They were looking very stern and convinced and a few of them, very red faced, as though they had been arguing among themselves.

And it was very quick. They said, look, we are not willing to take it anymore. These people now had some wealth. They had options. And it was working for them financially, but it was not working for them spiritually.

And they said-- and I think this is because they viewed me as her protector-- Sandy goes or we're all leaving. Now, I haven't had an experience prior to that or subsequent to that that was anywhere near as dramatic. And we talked a little bit.

I was trying to determine whether they were all of that persuasion. It's like a jury. I'm sure there were some people who felt more strongly than others, but clearly, this was a solid voting block.

So I said, does John Morgridge know about this? Yes. We talked to him before we came here. He sent us here. Swell. So I didn't know what my role was. I'm the chairman of the company largely for state occasions and choosing the wine.

So I called John and I said-- he says, I know what's happening. They already talked to me. I said, is there anything you want me to do?

And he said, no, I'll take care of it. We don't have any choice. Either the management team stays or Sandy stays. And that was intolerable because we now had a team of people that were really beginning to gel and work together and everybody was on the same page on the important issues. So they went trudging off back to Cisco-land.

And John had the distinct displeasure of having to deal with Sandy under circumstances that were less than friendly or ideal. But I did not go back with them. I could guess at the dialogue and I wasn't going to learn anything from the dialogue, so I didn't go. And John and-- I came from a company called Fairchild where the founders were called the Traitorous Eight. Well, we had the traitorous seven going back to the company and dealing with an unfortunate exit.

Hollar: What had led you to send them to Don?

Morgridge: I was tired of their complaints. And Sandy and Len, kind of by their own admission, were network, email people. And so it was a case of actual documented intrusion. And they also came-- at that point, Sandy and Len were in their, what, 30s, maybe?

And this group was-- there were probably some that were early 40s, but they were in their 40s and 50s. And I think the kind of-- and they'd all been in this industry for a long time. John Bolger, the CFO, long time; the engineering vice president, long time; Terry Eger had worked for IBM and he work-- although I don't think Terry was part of the group. He was out traveling, probably selling someone.

But at any rate-- and I think they just found it difficult being in that environment on a regular basis. I don't know. I don't know that I worked very well with Sandy, but I certainly didn't have trouble being around her.

Hollar: And can you talk about the conversation you ultimately had to have?

Morgridge: Well, the conversation I ultimately had with her was, I said clearly, you're, at some level, very unhappy. And your unhappiness-- I don't know if you want to live your life that way. And in addition to that, there's a lot of unhappiness amongst management relative to your activities. And I just think it's better if we recognize that and you departed.

And I said, you can do it on whatever terms you want. We actually left an office for Len and Sandy at the company, which they moved a lot of-- well, Sandy did-- moved a lot of very nice furniture into. And I don't know that she ever really used the office, but it was a reflection of that.

And I've not had any-- well, we did have direct conversations with her because we gave a chair-- we, Cisco, gave a chair at Stanford in the computer science department and invited them to attend the dinners that are associated with chairs at Stanford with the president at his house. And they came. That's another story.

Valentine: The chair, if I remember correctly, was in their name.

Morgridge: Yeah, absolutely.

Valentine: So it wasn't a Cisco chair.

Morgridge: No, it's not a Cisco chair.

[INTERPOSING VOICES]

Hollar: Yeah. Right.

Valentine: So it was done in the most favorable way you could think, in terms of recognition.

Morgridge: Yeah.

Hollar: I want to just do a time check because if you have to be somewhere at 3:00, John--

Morgridge: I got another 10 minutes.

Hollar: OK.

Morgridge: It's just up the road.

Hollar: We're not going to get through all of the questions that we had, so we'll--

Morgridge: Obviously.

Hollar: --we'll have to talk about having--

Morgridge: Incidentally, one question I do want to correct-- and I don't know where you got it--

Hollar: OK.

Morgridge: --is the statement, "I hear you're everything that's wrong with Cisco."

Hollar: Right. I skipped over that. I didn't ask that.

Morgridge: I know I'm not a great salesman, but I wanted to join this company. I would never, never say anything like that.

Hollar: Right. Yeah.

Morgridge: I mean, that's not how you close a sale, and I was trying to get Sandy to not say no. She didn't have to say yes. She just didn't have to say no. And I don't know if you know her very well, but that would've been--

Hollar: Inflamed the whole situation.

Morgridge: Whoa! Yeah.

Hollar: I get it.

Valentine: There has to be a footnote somewhere that they both left very, very wealthy.

Morgridge: Yeah.

Hollar: Yeah.

Morgridge: There would have been-- if they had held their stock-- of course, if we'd all held our stock-- they now would probably be as rich as Warren Buffett because they owned 25% of the company. The company's now valued at about $135 billion. At one point, it was worth a half a trillion. And they exited shortly-- the IPO was in February and I think they were out of the stock by a year later.

Hollar: Wow. Let's use the next 10 minutes to talk a little bit about your famous frugality, John. There are lots of stories about-- you've started it, in fact. You're known as cheap and he's known as even cheaper. So can you talk--

Morgridge: No, no. Not cheap.

Hollar: Cheap?

Morgridge: Frugal--

Hollar: Frugal.

Morgridge: --and always looking for the best deal, which I'm sure Don does.

Hollar: Yes. Right. So how did you bring that to Cisco? What are some of the things you did to--

Morgridge: Well, to start with, you had to understand that Len and Sandy were cheap. They were cheap. I mean, that's why they set the business up in their house, even against the rules. That's why they started the company and had the company operational on the Stanford campus. I mean, is there anything cheaper than that?

So that was my attribute that at least they understood and accepted. And so a lot of it's done by example. As I tell people, don't have a coach policy unless you like to sit in coach.

And I got complaints about coach. And I used to say, I'm a small person. I'm almost comfortable in coach-- not today, but I was.

And I've always had a feeling about big people, particularly when they get promoted. I said, if you look at the CEOs of Fortune 500 companies, I'll bet the majority of them are six feet tall or more. I said, this is my way of inflicting a little pain on big people.

And then we created a thing called virtual first class where I actually traveled first class and took photographs. And this was-- I mean, I'm dating myself. This was Pan Am to England with caviar when they used to serve it and they'd have the vodka or whatever in an ice cube. And so I told them, what I want you to do is visualize yourself in first class and you'll be more comfortable in coach.

Hollar: Did you give them photographs of first class that they could look at while they were…

Morgridge: Yes, of my flying first class. And we handed out eye patches and earplugs. So they still remember that.

Hollar: There was a story about-- was there a meeting at some point at which a row of coach seats on an airplane were--

Morgridge: Well, what I was demonstrating was-- this is back when there was excess capacity-- when they had bought these big airplanes and they couldn't fill them. And what I did is I demonstrated that you could, if you carefully arranged it, get five seats, put the armrests up, and sleep in coach. Because they were complaining about long distance travel and so I put five chairs on the stage and I lay down. And then we had the mantra of, we'll always try and upgrade you to the aisle. So it was-- and even today, business class is still a lot more expensive than coach.

Hollar: Yeah.

Morgridge: And I actually had some of the complainers run the numbers. And we were smaller then and did perhaps more-- on a relative basis-- more international travel.

Valentine: So I contributed to this concept of being cheap.

Hollar: Of frugality?

Valentine: Of being frugal. Sorry. When we had our conclusion conversation about John joining the company as the chief executive, I said the $3 million in the bank is mine. I want you to run this company and not spend my money, somehow or other.

That's just to make the customers feel confident that you have a real balance sheet and all the rest of it, but I have no intention for you to spend anywhere near the rate of my $3 million. So I tried to have the numbers in the treasury segregated in his head so that there was money he could spend and money he couldn't.

Morgridge: Right.

Valentine: Of course, that's an entire fiction.

Hollar: What are some other famous John Morgridge stories about frugality that you remember?

Morgridge: Well, the best story was-- I used to make trips to New York. And our competitor, Cabletron, while frugal for the employees, was not necessarily frugal for the two founders. So when they came to New York, they always had a limousine.

So I said, no limousines. We aren't going to-- so what they would do is we would go by subway. And strangely enough, they seemed to have us going from midtown to downtown to mid-- I mean, the appointments seemed to be logically created.

So I was down on Wall Street and I came out of the building. We had been calling, I think, on Morgan Stanley or someone. And they always have the limousines lined up. One of them had my name on it.

So I said, gee, this is terrific. So I go over and I said, I'm John Morgridge. And the driver took a subway coin and put it in my hand and he said, the entrance is right down there. [LAUGHTER]

But it was a reflection of-- I mean, I've got a lot of stories like that. I was on Northwest after a sales meeting and the stewardess comes down with a card that says, Northwest would like to upgrade you to virtual first class and here's a drink coupon. And it was one of our employees.

Hollar: Someone was--

Morgridge: No, no. It was one of our employees who had seen me.

Hollar: Well, it all clearly--

Morgridge: And then just this-- I mean, this is terrible. Just this week, I was at a football game at Wisconsin. And we're flying back and the guy behind me taps me on the shoulder and he said, I worked for you in Madison. And I'm here for the-- he was a graduate of the university and he had his son with him. And he introduced his son and so on-- 12-year-old kid.

And he looked down at me and he looked at my briefcase. And he said, is that one of the old Cisco laptop bags? And I turned it over and of course, it had the-- and he said, some things never change.

Valentine: But all the humor and jibing about John's frugality is-- it was natural. He lived it. It was not a two class company where John sat in the front and everybody else sat in the cattle section. John was just natively comfortable about not wasting money. And the company had terrific cash flows.

Morgridge: Yeah. Terrific.

Valentine: Terrific. I mean, a friend of mine who was in the hotel business looked at the balance sheet and he said, this must be a bank. No one has cash flows like this. And that's how you have cash flows like that-- by not spending, as well as creating gross margins that are high and being conservative about spending.

Morgridge: I've come to believe that gross margins are, to some degree, a state of mind. And I think Don believes that also. If you start accepting that you can only have a small gross margin, then you don't create a product that satisfies at a level that will permit a higher gross margin. And certainly, from very early days-- not basically from the founders, but from Don and some of our other early employees-- we created that idea that a gross margin of 65 or 70 was possible in this business.

Hollar: Do we have time to talk about the decision on stock options and the extent to which options are and were made available? Can we talk about that as the last section of this?

Morgridge: Well, of course the model at the time was to give them to engineering and very few others. Although actually, I was a little surprised when I came on board because there was one employee who clearly was a good salesman and had convinced-- normally, sales doesn't get a lot of options. They get commissions. But one of them, Terry Eger had over 5%, I think, of stock options.

But I was convinced that everyone should get stock options because I wanted to be able to ask anyone to do anything, anytime. And if they feel they have some portion of the ownership, I thought that would work.

I think it wasn't convention then. I think it's more convention now. They're broader based.

Hollar: Was it a competitive issue, then, to attract talent?

Morgridge: No. It was not a competitive issue.

Hollar: This was a compensation issue?

Morgridge: It was a-- they told an interesting story-- one of our early vice presidents of manufacturing told a story about when our options were underwater. And at a company meeting, which we had frequently, someone said, are we going to re-price the options? And I thought for a while and replied, why don't you quit and see if we re-hire you and then you'll get the lower option price? So we never re-priced options. And I think that was important because it said that we were confident of our future and that was a good message to give the employees.

Hollar: Yes.

Valentine: See, when I priced the company prior to financing it, I divided the company into thirds-- early employees, founders-- whatever you want to be called-- you get a third. I get a third. And the option pool is the third, for future employees, management-- whomever is justifiably qualified to get an option. And Silicon Valley's practice was always to give options out very broadly in startups.

Now, there is an incident-- and I'm trying to remember, first of all, whether I have the right company. But I don't remember her name. We had a bookkeeper that was a bookkeeper-- nothing more-- a young woman.

And she did what she did exceptionally well. She got options. When there were splits, she got more shares, more shares.

And at some point in time, she resigned. And I rarely ever do an exit interview with a bookkeeper, but I didn't understand-- because this was a valued employee. And I said to her, why are you resigning?

She said, well, I don't have a life. She said, I'm worth $8 million, but I have no life. And she left.

Morgridge: Yeah. The other thing we did is we had a table very early on of how many options employees at various levels got. And we never changed that number-- the number of shares they got.

What we did is in the first five years, we split the stock two for one every year. And as a result, no one ever calculated what share of the company they were getting, including the CFO that we hired. I was amazed that he didn't know-- I mean, we gave him shares that were quite generous based on history, but the stock had split so many times that he was getting-- his ownership had been reduced by a factor of I don't know what, based on the number of shares.

Hollar: But it didn't matter.

Morgridge: It didn't matter because they were only looking at the number.

Hollar: Exactly. Yeah, exactly.

Valentine: Over the years, when I was invited anywhere to interview, I would ask the person what they thought their equity compensation should be. And they always answered with a number of units. And I voted time and time again against hiring people in any business capacity who didn't recognize that they had to know the denominator in order to understand their compensation.

And they never asked the question. And if people were in some kind of important business category, I would vote against their hiring because they're dumb. And I don't think we can tolerate dumb people in critical positions.

Morgridge: It was great.

Hollar: Right. Right. Yeah.

END OF PART ONE

