Oral History with Paul J. Ferri

NVCA-Venture Forward Oral History Collection

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CHM Reference number: X8628.2018

National Venture Capital Association
Venture Capital Oral History Project

PAUL J. FERRI

Interview Conducted by
Carole Kolker, PhD
November 28, 2012
December 6, 2012

This collection of interviews, *Venture Capital Greats*, recognizes the contributions of individuals who have followed in the footsteps of early venture capital pioneers such as Andrew Mellon and Laurance Rockefeller, J. H. Whitney and Georges Doriot, and the mid-century associations of Draper, Gaither & Anderson and Davis & Rock — families and firms who financed advanced technologies and built iconic US companies.

Each interviewee was asked to reflect on his formative years, his career path, and the subsequent challenges faced as a venture capitalist. Their stories reveal passion and judgment, risk and rewards, and suggest in a variety of ways what the small venture capital industry has contributed to the American economy.

As the venture capital industry prepares for a new market reality in the early years of the 21st century, the National Venture Capital Association reports (2008) that venture capital investments represented 21 percent of US GDP and were responsible for 12.1 million American jobs and 2.9 trillion in sales. These figures, while significant, greatly understate the collective accomplishments of the venture capital industry.

I'm pleased to have initiated and given my early support to this project, which received support from NVCA, and is now funded by the Harvard Business School. I believe these oral histories will advance the understanding of the venture capital industry. This collection, along with Paul Bancroft's Bay Area oral history project at the Bancroft Library at the University of California, Berkeley, and Paul Holland's Silicon Valley project for the Western Association of Venture Capitalists, will add significantly to a growing body of venture capital memoirs available to the public sector.

A special note of gratitude goes to each interviewee who generously gave of his time while candidly sharing his memories. Their recollections bring to life the dynamic story of venture capital in the 20th century, providing a powerful perspective on the history of this industry.

Charles W. Newhall II

2013

VENTURE CAPITAL GREATS

A Conversation with Paul J. Ferri

Paul Ferri, a noted venture industry legend, was a founding partner of Matrix Partners in 1982. Prior to Matrix, Paul co-founded Hellman Ferri Investment Associates and served as its general partner from 1977 to 1982. From 1970 to 1978, Paul served as a general partner of WestVen Management.

Paul serves as a Member of the Board of Overseers of Columbia Business School and has served on the boards of numerous companies: Cascade Communications Corp., Sycamore Networks Inc., Stratus Computer Inc.; TechForce Corporation; ArrowPoint Communications, Inc. and Sonus Networks Inc. to name a few.

In February 2001, *Forbes* selected Mr. Ferri as one of the "Top 20 Venture Investors of all time and the "Best VC in Boston." Among other honors, Paul received the 2001 Massachusetts Telecommunications Council Award for "Venture Capitalist of the Year," and was elected to the American Academy of Arts & Sciences. In 2003, Paul Ferri was inducted into the Private Equity Hall of Fame, citing his work "in founding and helping to build Matrix Partners into one of the most successful venture firms in the industry".

Mr. Ferri holds an M.Sc. in Electrical Engineering degree from Polytechnic Institute of New York and an MBA degree from Columbia University and a BS in Electrical Engineering from the Cornell University. In considering retirement from Matrix, he says: "I'm stepping away – going to mentor young people who will take the firm to the next level."

The following is an interview with Paul Ferri, taking place at his office in Waltham, Massachusetts. Today's date is November 28, 2012. My name is Carole Kolker. A second interview is included, which was conducted by telephone and took place on December 6, 2012. These interviews are being conducted for the Venture Capital Oral History Project of Harvard Business School and the National Venture Capital Association.

THE EARLY YEARS

CK: *We're just going to get started here, since our time is limited. Paul, thank you for setting aside this time, because I know it's hard to find a chunk of time.*

PF: Well, and I basically live in Florida, so I'm only up here for three days this week.

CK: *Oh, my. Well, I might be able to follow up in Florida, because I think I'll be going down there. (laughter) That's your vacation time.*

PF: No, no. I spend the winter there. So I'm basically on my way out. I maintain I'm the oldest person in the United States that's made start-up investments up until three years ago.

CK: *Well, when I said to Rick Burnes that I was meeting with you, he says, "Oh, now you're getting to the real pioneers." (laughter)*

PF: I don't think Rick's made an investment for, I don't know, ten years, yeah, a while. I don't know. Did you talk to Dick Kramlich?

CK: *He's been interviewed, but I didn't interview him.*

PF: Dick and maybe I are the two people that are still somewhat active. Everybody else has been out of the business for ten, fifteen, twenty years.

CK: *I'd like to talk about how it's changed, but let's go back and we're going to start from the early years. And for the record, when and where were you born?*

PF: If we get on that story, it's a long — I was born in Rome, Italy.

CK: *And when did you immigrate?*

PF: My dad was, at a very early age, a world-renowned, high-speed aerodynamicist in Italy. We're all Italian, all from Rome. And you might remember Italy and Germany were fighting the Allies. When Germany occupied Italy, we went into hiding. The Germans were looking all over for my dad. Basically, looking for — I had a brother and a sister — looking for all of us as a way to get my dad. When the American Army entered Rome, June 2, 1944, the day after Rome was liberated, a fellow from the CIA knocked on my grandmother's door and said, "We're looking for Dr. Ferri. Where's Dr. Ferri?" We were hiding north of Rome. When the Allies got to where we were, they brought him to the United States in September '44, and the war didn't end until April '45. So he was probably the first scientist brought to the United States. And we didn't come over until two years later. So we were — my mother, sister and brother were on the first ship bringing non-military people to the United States. So we came to the United States.

They moved us to Hampton, Virginia, which is where the U.S. was doing this high-speed aerodynamics work. None of us spoke English. None of us knew anybody. We didn't know anything about — we just knew we were going to America, whatever America was. And so that's how we got to the United States. It's an amazing story. My father died as a young man. He was sixty-three. But it's an amazing story. I left out a lot of it.

CK: *Has this ever been written down?*

PF: Just this year, I published a book for my family about his life. He was well known worldwide in his field, which was high-speed aerodynamics. It's an area that very few people know much about.

CK: *Well, I said we were going to hear war stories, but I wasn't expecting this. Thank you. I'd love to hear the rest of it, but considering our time, we're going to move on. So you settled in Virginia.*

PF: Hampton, Virginia.

CORNELL UNIVERSITY, BSEE

CK: *And then did you go to school there?*

PF: Yeah, I finished grammar school in Hampton, Virginia. My dad moved to Long Island, New York. He became a professor at what is now NYU. He became eventually head of the Aeronautical Engineering Department at NYU. I grew up on Long Island, went to high school on Long Island, went to Cornell University for a bachelor in electrical engineering.

CK: *And what was your mother doing during this time?*

PF: She was a mother.

CK: *Right. Well, it was the forties.*

PF: Right. She basically raised us. My father was always super busy, worked all the time, had no hobbies. He worked, and he had dinner with his family, and that was it.

CK: *And you said you had a sister and a brother?*

PF: Right, younger. I'm the oldest of three.

CK: *How'd you all get along?*

PF: Well, my sister is a little less than two years younger than I am. We are close. My brother was five years younger than I was, and we were like in different worlds, because he was five years younger; but I graduated high school when I was sixteen, so I was in a different part of my life. We were really almost seven years apart in our real life, as opposed to five years, so it was different.

CK: *What were your interests as a child? Were you reader or were you more of a tinkerer?*

PF: I was actually neither of those. I did well academically because — not that I liked it. I was never one that did extra studying. I did it because I was expected to do well. And I did well. I was smart enough, but I never thought I was super smart — and particularly in the engineering world, the scientific world, you can tell when people are smarter than you. It's very easy to tell. There are people that just get concepts and understand complicated things very quickly. So I went to Cornell. Cornell was, I don't know, a 2,000 entry class, but they had a special program called the Engineering Physics, which thirty students enter. When I went to Cornell I was overwhelmed by how smart these kids were. There were kids that had graduated number one at Brooklyn Technical High School or Bronx High School of Science. dI didn't quickly realize, but I realized these guys are up here, brain power wise, and I'm okay, but I'm nowhere near where they — anyway, but I really didn't have a desire to be competitive with any of the people. I don't know why. I was young going to college. So eventually I graduated from Cornell.

CK: *Did you play sports?*

PF: I played some sports, yeah. I was very active in sports in high school, and I loved that. I wasn't that good at it, but I loved it. I played a little bit in college. They had a freshman team, basketball level. If somebody would've said, You could be number one in the engineering and physics class or you could be on the varsity basketball team, I would've chosen, I'd rather be on the varsity basketball team. But neither one of those things were possible.

CK: *What were the values in your home in terms of a work ethic, education, success?*

PF: We came over to the United States. I had one bag. We each had one bag. We had nothing. If you think back, we were moved to Virginia; we didn't speak English. I had finished third grade in Rome. The Italian elementary schools were — I assume they're more advanced at an early age than the American schools are, so I'd been learning fractions in third grade, and came over to the United States, and I was put back into first grade because I didn't speak English. They eventually moved me up to third grade. So I wound up repeating third grade. But our life was very simple. It was schoolwork and my mother put that pressure on that we were expected to do well in school.

CK: *So it was coming from your mother not your father?*

PF: No, no, my father worked all the time. I think back, I say, How did he do that all the time? But we came and we had nothing, right? And we were always outsiders in Virginia. If you think back, we were Italians, who were the enemy that the Americans had just defeated, and we were brought into this little — well, you're in Washington; you know Washington. Hampton is next to North Carolina. So we're in this little back — they'd never seen an Italian before. We were this curiosity. As a kid, you survive. You learn to speak English quickly. And you wanted to fit in to be like all the other American kids. That was what I remember as a kid.

CK: *Were there any teachers that were mentors in any way?*

PF: It's really odd. I have two master's degrees. I was just talking to somebody about it. Oh, I remember. President Obama said, "If you've been successful, there's a teacher that somehow…." I remember telling my wife, I said, "You know, if somebody said, 'Is there a teacher that you can remember that changed your life?' I can't think of one."

CK: *Interesting. A person?*

PF: No. I'm probably odd in that way, but it was just something. And I didn't do well in college when I started because it wasn't important to me. Why it wasn't important to me, I can't — I think back, I say, What the hell was I thinking? Anyway, but eventually I figured out I had to do well because I was wasting time. So I drove myself to do well and I did well in school.

CK: *Were you high energy?*

PF: I wouldn't say I was — I've been very successful at what I've done in my life. And I compare myself to people that I went to high school with, college with, and I say, Was I different than them? I don't think I was any different.

CK: *Were you competitive?*

PF: I'd say I am very competitive. I am very competitive. But I've gotten more competitive as I've gotten older and more confident, all those things that I didn't have. So I worked as an engineer at an aerospace company for seven years. I went to night school for seven years to get a master's degree in electrical engineering.

CK: *Were you working?*

PF: For Grumman Aircraft on Long Island, which made Navy airplanes and did the lunar module that landed on the moon.

CK: *How did you get that job?*

PF: Well, I got that right out of Cornell. I had worked at Grumman during the summers through college, so it was sort of automatic that I was going to go work there. How did I get in this business?

POLYTECHNIC INSTITUTE OF BROOKLYN, MSEE

CK: *I'm trying, but you're really helping me go along here because you're anticipating what I'm interested in. So you were at Polytechnic—*

PF: Polytechnic Institute of Brooklyn. That's where I went to night school for seven years to get a master's in electrical engineering. So I was working and going to school.

CK: *Then why did you change to business? Something happened.*

PF: That's very easy. My father was a world-renowned expert in his field. He didn't make as much money as the person who owned the Oldsmobile dealership in town. He loved his work and that was perfect for him. And I started out being an engineer. And I worked in an airplane hangar with 2,000 or 3,000 engineers just like me. We were rows upon rows. I could look down and there'd just be desk after desk after desk. And when you started out working at Grumman, there'd be a corridor here and there'd be desk, desk, desk. And when you started, you'd be the desk by the wall, and then as you moved up in seniority, you got to move. And then you became a little group leader, you got this desk by the corridor. And then when you became head of the whole group, you moved to this desk. About halfway through my master's degree, I said, I'm going nowhere with my life. I remember, I finished my master's degree and I told my boss that I was leaving; I was married, we had two kids. I'd saved enough money to go to business school. But I had no clue about anything. I just knew I didn't like what I was doing. I was going nowhere. Or I didn't like where I was going.

CK: *You didn't want that front desk.*

PF: Right, yeah. And when I told my boss I was quitting, he said, "Why? You're doing great. One day you could have my job." And I had to bite my tongue to not say, "That's exactly what I don't want. I don't know what I want, but I know I don't want to be here in seven years or ten years or something." So I debated going to law school or business school.

My father was totally scientific. Money was not of interest to him. I didn't find the engineering work I was doing satisfying to me. And I was okay to good at it. I wasn't exceptional, I don't think, but I wasn't absolutely the worst person there in engineering. So I'd say in that process I became more competitive, because I was going to night school for seven years. Everybody else didn't do that. So I always wanted to get ahead, whatever getting ahead meant. I didn't know, but I worked hard at it. So then I went to Columbia Business School.

COLUMBIA UNIVERSITY, MBA 1967-1968

CK: *And why'd you choose Columbia?*

PF: Versus Harvard?

CK: *Versus anything, I guess.*

PF: Yeah, that's another interesting question. I talked to some people and everybody said, Oh, you should go to Harvard. And I applied to Harvard. I got accepted to Harvard. And then it dawned on me, since I'd gone to night school, I said, I wonder whether there's any program that allows me to continue going to night school, where I don't have to quit? I don't know if they still allow this, but in those days Columbia allowed you to take night courses at a graduate business school and allow one semester's transfer worth of credits. So I went to NYU Stern Business School at night for another year. I got a semester's worth of credit. And I said, Well, I can go to Columbia. And Columbia allowed you to start any time and finish any time, and you could go straight through. So I could go for twelve months back-to-back and get an MBA versus Harvard. So I started Columbia Business School February ’67 and I graduated February ’68 with an MBA. Harvard, I would’ve started in September ’67 and I would’ve graduated June ’69. And I said to myself, There’s no way Harvard is that much better than Columbia. So I went to Columbia, and I did very well there.

CK: *What was exciting to you about it? There must’ve been something that finally—*

PF: I just thought the whole idea of going into New York every day — they were all things that I knew nothing about. I remember I took Accounting 101, and it was the hardest thing I've ever taken in my life. So I had taken nuclear physics courses and things that are really hard, and this was baby accounting and the whole notion of: What is an income statement? Why does the cash go over here on the balance sheet and liabilities go here? What the hell difference does it all make? It was a foreign language to me. But eventually I got it and eventually I did very well there. So when I was about to graduate, lots of people were interested in hiring me. And I interviewed with every kind of company known to man, from airlines to IBM, to all the accounting firms, to all the management consulting firms, because I still had no idea what I wanted to do. I had no idea. I was clueless about the business world. And airlines, Dow Chemical, Exxon, I mean every — When you look back, I don't know what I was looking for, but I didn’t know what I wanted to do. And everybody was interested in hiring me.

CK: *Was your engineering background a real asset for you?*

PF: Yeah, I would say. So, IBM, GE, they wanted people with an engineering degree and an MBA. So I was a natural for them. The management consulting firm McKinsey, Booz Allen, the same thing. In those days, it was rare for an engineer to go to business school, today it's commonplace. But in those days there were very few of us. And then there were these things called investment banks that I'd never heard of, that also were interviewing at Columbia Business School. I'll never forget it. This fellow interviewed me and he had what looked like a $3,000 suit and the suspenders and the cuff links and the two-tone shirt, his hair perfect. And I had my one suit on. He interviewed me and I said, Well, this guy will never be interested in what I know, because I didn't know anything. Anyway, so he said, "Well, we'd like you to come to Wall Street and meet the partners." I'd never been to Wall Street in my life. I'd never owned a stock in my life. I didn't know anybody who owned a stock in their life. And so I took the subway to Wall. He said, "Go to thirty-two Wall." He says, "And get in the elevator and the man will bring you up to the fortieth floor." So I'm going down. I'm looking at the numbers. I get to thirty-two Wall and this little, private elevator with a guy dressed in the Phillip Morris uniform, the elevator operator. And I go in, and we're going to the fortieth floor. And on the way up, I said, "I don't know what these guys do, but if they offer me a job, I'm going to learn how to do this, because this is much better than working with 4,000 other people." And luckily they offered me a job and I did that. It was an investment banking firm. My job was to be a security analyst.

LOEB, RHOADES & CO. 1968 - 1970

CK: *This is WestVen?*

PF: Nope, this was Loeb, Rhoades & Company.

CK: *And this is 1968?*

PF: This was ’68, February of ’68. And I went to Columbia Business School, so I started in February. The people in the class that started September before me were people that I graduated with. And those people include — and these names probably don’t mean anything to you, but Henry Kravis. You’ve heard of Henry Kravis, right? So he was in my class. Lee Cooperman, does that name mean anything to you? He runs a huge hedge fund. Mario Gabelli who runs Gabelli & Company, a huge mutual fund. And Art Samberg who was at one point running the largest hedge fund in the world. So those were my classmates. Art had gone to join a young, small firm called Weiss, Peck & Greer, that doesn’t exist anymore. Phil Greer started WestVen. And Phil wanted somebody — In those days, Phil had raised fifteen million dollars. Phil had had the Bank of America put sort of a stamp on Phil saying, This is a smart guy. We’re going to partner with Phil to help him raise money. So Phil, with the Bank of America, raised fifteen million dollars. And as I remember it, it was primarily from individuals. And I joined Phil as the junior guy on the team. This was 1970.

WESTVEN MANAGEMENT General Partner 1970-1978

By 1974, we had an annual meeting where it looked like everything we had invested in was a disaster, and Phil had to get up and say, "Well, we did this and it didn't work, and I take responsibility for that. And we did this and this didn't work." The famous name that was in there was Federal Express, which I can talk about for an hour. Many people know that story. And then I was involved with a company called Paradyne Corporation that doesn't exist anymore. So by 1974, we had theoretically, on our books, lost half our money people had given. I forgot what the numbers were, but say they'd given us ten million and we said it was worth five million. In '74 the economy was way down. Things turned around. WestVen wound up making respectable returns for our investors. And it was time to raise WestVen II. And Phil said, "Well, Paul, you can be the general manager of WestVen II. And WestVen was headquartered in San Francisco, but I was the only one in New York. So I worked in New York. And in those days, pretty much — not everybody, but the bulk — if you started a tech company in Massachusetts, you had to go to New York to raise the money. There was very little money here in Boston.

CK: *For startups?*

PF: For startups, early stage things, right. So there was something called American Research and Development, which was the predecessor to everything. So there was a company here called Prime Computer that was a big success. I met with them three times. They always came to New York to call on me, not that I had to visit them in New England. In those days, having money was really a distinguishing feature, and there weren't very many of us that were in the business. In those days, it was the Rockefellers and Bessemer and Whitney, these big, wealthy families. Phil was one of the first that raised outside pool. Anyway, things turned around. It was time to raise WestVen II and Phil said, "You can be the manager." You've never met Phil Greer probably, but Phil is this — I don't want to say overwhelming guy, but he runs whatever he's involved in. He may call me the general manager, but — I said, "Phil, you know that isn't going to work that way. I'm not going to be the general manager. You are going to." Anyway, we talked about economics and I said, "Well, what am I going to own of this?" He said, "Well, you can own what you owned in the first one." I said, "What? That doesn't make any sense to me. I did it here when I started because I didn't have any right to own any more than you gave me. But I've been here seven years and I think I'm entitled to *this*." I don't remember what it was. And he said, "Well, that's not going to be in the cards." So I said, "Well, then I'm not going to stay." And luckily I ran into a fellow named Warren Hellman. Have you ever heard that name? All right, so Warren was probably forty-two. He had been president of Lehman Brothers in New York. He had gotten fed up with living in New York. He was a big skier. He went up to Stratton Mountain, Vermont, every weekend in the winter. He started the Stratton Mountain School. His kids all went to the Stratton Mountain School. He had a daughter on the Olympic Ski Team.

HELLMAN FERRI & CO co-founder 1977-1982

CK: *Excuse me, but when you say you ran into him, were you introduced to him?*

PF: Well, somebody had given him my name. I didn't know Warren. Because, again, there weren't that many of us that were in the venture business. Warren wanted to start a firm in Boston to do three things: venture capital, investment banking, and money management. And he was the investment banker. He had also raised fifteen million dollars in 1977. And Henry Kravis tells the story that when he started KKR they went out to raise fifteen million dollars in '77, and he wound up raising seven or eight or something; they didn't get the fifteen. They went off and did that. Warren raised fifteen.

CK: *How was he able to do that?*

PF: Well, he had been president of Lehman Brothers, which helped. So Warren came from a very wealthy San Francisco family. Warren's family put in a million dollars. Lehman put in a million dollars. Through Lehman, he got an investment from the wealthiest non-royal family in Saudi Arabia. We got the Ford Foundation and Teachers Insurance. I think those were all our investors. And we did very well with that fund.

CK: *What venture capital firms were you working with at WestVen? Did you partner with any of the —*

PF: Well, it was sort of deal by deal. We invested in Federal Express with a firm called New Court Securities, Charlie Lea. Let me just think of the companies. Paradyne we had something called the Sprout Group out of DLJ. Who else was in there? Heizer Corporation, that was like the mega fund that started after– In those days, there were few opportunities, and the world was different than it is today. So we didn't partner across the board with anybody. One deal we did with Sutter Hill. Another deal we might've done with Sequoia. Or another deal might've been — Kleiner wasn't in the business in those days. But the bulk of our operations at WestVen were in San Francisco. So the bulk of the money was invested in California. I was an oddball by myself in New York.

CK: *It's kind of amazing how you were with Loeb, Rhoades for just two years and —*

PF: Just two years, yeah. That was the other thing. I figured out that being a security analyst was a non-job as far as I was concerned. Again, I went to my boss, I said, "I'm leaving. I'm going to go do something else." And he said, "Why is that?" So I go to Grumman Aircraft. They tell me, "We're going to make 22 of these kinds of airplanes this months and it'll be 25 next month and 32 the next month; and our gross margins are here, and they might go to here, and they might go to here." So what do I add to that process? I sort of reported to the world that that's what Paul Ferri thinks. That wasn't something that was satisfying to me. So I quit. I took a pay cut to go to WestVen. But I had the chance of getting an override on other people's money. That was huge for me. The whole notion that I had the potential to get more than my salary, that was huge. And it was an infinitesimal amount that I shared in, but it was way beyond what I'd ever dreamed of.

CK: *Did you feel like you were building a network at this time?*

PF: Not in those days. Not in those days. But we all knew each other, right. So whether it was Dick Kramlich or Bill Burgin who was at Bessemer or Neil Brownstein who was at Bessemer — they were both in New York in those days — Charlie Lea; Warburg Pincus had just started. There were probably fifty of us in the United States doing this thing called venture capital, but nobody knew venture capital; they had never heard of it.

CK: *Did you see yourself in some way as a band of brothers?*

PF: Yeah, it was certainly a more cooperative environment. So none of us ever did a deal by ourselves. We'd share a million-and-a-half-dollar financing, and we might do 300; somebody else might do 700; somebody else might do 500. And then, typically in those days, if we did the first round at a dollar a share, the next round a year later or two years later would be at $1.25 a share. And typically the first-round people would do less of that, and they'd bring in new investors in the second round and on into the third round. But the markups were modest markups compared to today's world. And we took turns. So we did a little bit of startup, a little bit of somebody else's second round, a little bit of somebody else's third round, we did some buyouts. And all of us did the same thing. So if you talk to Greylock or Venrock or whoever you talk to, we all did the same thing. And even when I joined Warren, which became Hellman, Ferri & Company, there was no strategy; there was no focus.

MATRIX PARTNERS co-founder - 1982

CK: *You didn't have a vision or a mission statement.*

PF: It wasn't required. And then, 1982, for a variety of reasons Warren wanted to move to San Francisco where he'd grown up, and he knew everybody in San Francisco. So the Hellman family — and Warren, then started Hellman, Friedman & Company; it's a big buyout firm. But Warren wanted to go to San Francisco, and he wanted me to go with him to San Francisco. I said, "Warren, we just moved here from New York. I'm not going home and telling my wife, 'I'm moving to San Francisco.'" So he said, "Oh, come on." And I said, "no." So I started Matrix, which was a follow-on to Hellman, Ferri. Hellman, Ferri, as a fund, might've been the best-performing fund that had ever been started at that point. And we had a unique compensation scheme that, depending on what our internal rate of return net to the investor was, as a rate of return increases, we got a bigger percentage of the profits. So we got paid nothing, but we were highly conscious of time. So we'd draw the money down. We wouldn't have any money sitting here. When we made an investment, we'd send you a note saying, "We're closing this investment Tuesday. Please send us your portion of this financing." And we had to recover all our expenses in determining what a profit is.

In the venture business or in any of these partnerships, determining what a profit is, — you would think it's easy to understand, but there are a hundred different ways to determine what a profit is. So we had to achieve real profits. You gave me a dollar, I'll give you $1.10 back; there’s $0.10 of profit. The other way is you give me a dollar and on this investment we invested $0.20 of it and we made $0.80 profit. I'll give you the $0.80. You still haven’t gotten your dollar back, right? So do you have a profit? But then we say we have these others things and they’re worth something. You would’ve had to have made a profit, cash back before we shared anything. But anyway, so we had this very complicated rate of return calculation. And we did very well with that fund. And some people, including some Harvard Business School professors, thought that that’s what motivated us to do well, that this increasing percentage of the profits is what drove us to achieve the superior performance. And I maintain it had nothing to do with it; it’s just that we did a great job making investments.

CK: *Do you remember what that first fund was invested in?*

PF: Sure. We were founding investors in a company called Apollo Computer that nobody’s ever heard of today. But it was the inventor of desktop microprocessor-based computers. We were founding investors of Stratus Computer, which was the first fault-tolerant computer of a generation. There was a company on the West Coast called Tandem Computer that Kleiner Perkins had done, and we were the founders — we were the only East Coast firm that was an investor in either Stratus or Apollo. We were early investors in Apple. But then we were also investors in a movie company. We were investors in Midway Airlines. We were invested in a competitor to Motel 6 called All Star Inns. Again, in those days, there wasn’t a requirement to be focused. You were just opportunity driven. Did we do any medical things? I don't think we ever did. We've never done any of that.

CK: *But you had some real winners here.*

PF: We did very well. I'm pretty sure it was the highest rate of return ever earned in the venture business. But it's funny because — so this sliding percent of the profit versus the rate of return, we only invested ten million dollars out of the fifteen because we had gotten so we were going to get the maximum profit sharing, and there was no incentive for us to invest more money, because then if we did a bad job with that it could drop down our rate of return. So we only invested ten million dollars, which today we write ten million dollar checks in one thing. We had a whole fund. Anyway, so that was '77, '78?

CK: *You said in '82, you—*

PF: In '82 we started a follow-on fund. It was called Matrix I..

CK: *Where'd you get the name Matrix?*

PF: I learned that it was not good to have your name on the door, because it always brings up issues that you're the new partner and you want your name on the door. So I said, "We're going to have a generic name, and then we don't have that issue." So we went to Matrix. And I went back with a fellow that I had worked with at WestVen by the name of Rick

Fluegel, who's my age. And he was always on the West Coast. And we decided that I would run our Boston office, and he would run our Palo Alto or whatever we were out there. And so we raised I think forty million dollars.

CK: *So Matrix was bicoastal from the beginning.*

PF: We might've been the first. There are pluses and minuses to being bicoastal, and we still struggle with that to this day. There are advantages and there are disadvantages. But we've had longer experience at doing that, I think, than anybody.

CK: *What's the disadvantage of bicoastal?*

PF: It's mainly a disadvantage for competing on the West Coast. We don't have critical mass on the West Coast. It's easier to not be big in Boston because we're a big presence in the Boston area. In California, we've never been a big presence. We've worked our way up. But when we're competing with Benchmark or Kleiner or Sequoia, our guys always think they're outgunned because they have more people out there than we do. So that was true then. It's still true today. The advantages are, to me, that we see what goes on, on both coasts. And we've taken advantage of that numerous times. The big example is we were co-investors with Mitt Romney in the first investment that he ever made at Bain Capital. And then he called me to fund Staples, which I turned down, so we didn't do Staples. And I paid attention. They opened one store outside of Boston, and I realized that was a big mistake that I had turned it down. So I called Rick. I said, "Rick, be aware. If anybody wants to start a company in this space on the West Coast, it's a good idea and you want to look at it seriously." So we wound up investing in a competitor called Office Club, which was then merged with Office Depot. And it turns out, our rate of return on that investment was better than the rate of return on Staples.

CK: *How do you see the difference between the East Coast venture culture and West Coast? Is there a cultural difference?*

PF: I think there's a lot of hype in our business and the West Coast, the Silicon Valley, has always had this air of superiority that the beginning and end of the venture capital world is in Silicon Valley. I've never bought that. And if you look at sort of long-term rate of return performance, all the better partnerships have — the investors are pretty much the same whether you look at Benchmark or Sequoia or Kleiner or us or Greylock; ninety percent of the investment dollars come from the same investors. So it's MIT, Harvard, Stanford, Michigan, Duke. Anyway, our rate of return at Matrix for twenty years was better than anybody that's headquartered in Silicon Valley.

CK: *Is doing business out there different than doing business here?*

PF: It's more competitive. And to me, the benefit of having a West Coast office is to compete out there you've got to be the best. Those are the best venture capitalists. But what it does for us is it allows us to bring that same standard of excellence that is needed to compete on the West Coast, to Boston. And that's what's allowed us to be successful. So

I said, “I want to have a team that if I move to Sand Hill Road with my team from here, I can compete out there.”

CK: *Why do you think they’re the best?*

PF: They have smarter guys out there. They work harder. And it’s just more competition always breeds better players. It’s much more competitive out there. And a lot of good ideas in the venture business get started out there, and we’re the first ones to bring them to Boston. So that helped us a lot. So things like entrepreneur funds. We were the first firm — and we’ve always been headquartered in Boston, and our West Coast office — it wasn’t a branch office but we raised the money here, we administer the investments here, we’re a Boston-based firm with a California office. So we brought entrepreneur funds. You know what they are? Where we’d invited friends of ours in the community to invest. So we’d raise a $125 million fund from the Harvard and Duke, and then we’d raise a seven million dollar fund that we’d offer to individual friends of ours who could help us find deals, evaluate deals. So we started doing that in Matrix IV maybe, something like that. And then we stopped doing it. And then a lot of people follow what we do in Boston. And I know that’s arrogant to say that, but that’s what happens. And then we stopped doing it. So everybody in Boston was doing the same thing. We stopped doing it because I felt that the returns we had generated in ’85 through 2000 were exceptional returns that were very difficult to ever duplicate. So I said, “I don't want to have all our friends find out that we’re now going to earn seven percent return for them. That’s not what they're expecting. And instead of creating goodwill, you're creating bad will." And a lot of people here kept doing it and wound up hurting. So we've generally been ahead of issues, certainly in New England. And having our West Coast office and knowing what goes on, on the West Coast helps us compete in Boston.

CK: *So, Paul, what made you think you were well suited for venture capital once you got your feet wet?*

PF: I don't know. I never thought about it that way. I just thought, "Somebody is giving me a quarter-point override on fifteen million dollars." That was what attracted me.

CK: *Is that what excited you? What excited you about the work that you were doing or motivated you?*

PF: When I started, it was I wanted to make money. I had no money. That notion that somebody — I'm not gambling, but I'm using other people's money. If they make a profit, I get a piece of it. It was just something I said, "Only in America could this happen." So that's when I started. Then after a while — it probably took me ten years that I could do this, in my mind. And I tell people, as I told you, in the engineering world I could tell you're smarter than I am. I have never met anybody in the business world that I say, "I can't compete with him." Nobody

CK: *What do you think has given you this confidence?*

PF: Well, a long record of success helps. But it's just having common sense and not getting carried away that you're a genius, which a lot of people in our business think, not only in our business but people that we back. They confuse being in the right place at the right time and doing a great job with being a genius. I've seen it over and over and over. And we have these discussions among our GPs here frequently. What do we look for in an entrepreneur? Who are the best managers that we backed? We make one new investment a month in a new company a month, and we probably have done that for thirty, thirty-five years. When you look back and you say, "who were the real stars in our portfolio," there aren't a lot of them. There are a lot of guys that did a great job because they were at the right place with a good idea at the right time. And in the whole technology world, other than Steve Jobs or Bill Gates or maybe Larry Ellison, there are not a lot of geniuses, in my view.

CK: *Along this period, once you got into finance, did you find any mentors in the business world?*

PF: I'd say no. I learned it on my own. I'd say Warren Hellman was great to me. He just died a year ago December. We were lifelong friends. And I would do anything for him and he would do anything for me. He was just a first-class human being. He treated me the best that anybody's ever treated me. And he invested in every partnership that we were in, that we did. I invested in everything that he did. He was a first-class human being, and that was important. He came from a very wealthy family. I did not come from a very wealthy family. But we had a great relationship.

CK: *Now, when you started Matrix, were you on your own? Did you take in a partner?*

PF: Rick Fluegel. So Rick and I started it. We were co-managing partners. And we did this for Matrix I and Matrix II. I would do the bulk of the fundraising. And we did not have a strategy. And it became clear to me as I went around and talked to investors and they'd be asking me about, "What's your strategy? And why are you going to be different? And why can you win?" So it dawned on me that — and we had done different things. So if you look at what we had done on the East Coast, they were mainly high-tech startups. On the West Coast, Rick liked doing buyouts and expansion financings and things like that in some tech but primarily non-tech things. The way we ran it was, I was responsible for our results; he was responsible for his results. And we'd put them together and we'd go to our investors and say, "Here's what our rate of return is." By the time Matrix III was getting funded, it was clear to me that the world had gone from capital being a differentiating function, so people had to find you, to capital becoming readily available and you had to have a reason why you were going to do better than the folks downstairs or in the next building. So we had to be very good at doing something. So the world changed.

CK: *Did you shift your strategy? What'd you do?*

PF: Absolutely. Well, I went to Rick. I said, "Rick, what we're doing has worked okay." It wasn't great. It worked okay, but it allowed us always to be top quartile in the performance numbers, and that got us funded each time." But I said, "This isn't going to continue to work. We have to be good at doing something." And I said, "Either you should run the firm or I'll run the firm, but we can't do what we've been doing. We have to all be doing the same thing." He invested in a pie company on the West Coast, right? And then they need more money and they were behind plan, and he'd have the team come here and I'd have to sit there and decide, What do we do with this pie company? And I'd say to Rick, "Rick, I don't know anything about the pie business. I don't know anybody in the pie business. I don't know whether the fellow who runs our pie company is A, B, C or D. So I don't bring any knowledge to help you make intelligent decisions. We need to get everybody doing the same thing so we can be smarter about what we do than our competitors." And he said, "Why don't you be the managing partner and we'll do what you want us to do?" So I said, "Great." We had been investing two-thirds of our money on the West Coast and one-third here. It wasn't a strategy, it's just the way it was turning out. And I said, "We're going to do just the opposite. We're going to be investing less in the more competitive West Coast." And it was clear to me that we were not — if you went and asked somebody on the West Coast, Who are the top ten firms? If you're a smart person and you want to start a company and you say, Who are the top ten firms, Matrix wouldn't have been on that list. Again, I thought the competition here was less than — our being good here was easier to achieve than to do it out there. So I said, "We're going to start investing here more." And it was all, in hindsight, it was a good time to be making that decision. It turned out infinitely better than I would've ever dreamed. So we owned the market here in startups for fifteen years. So everybody that's in business today in Boston, somehow we're responsible for their success. Either they co -invested with us, or because we couldn't take more money to invest, because what we do; we can't really manage more than $500 million partnerships. So to the extent some other university wants to give us money, we can't take it. We couldn't take it. So they said, Well, Matrix won't do it, but Charles River — or pick any other name. They said, "Well, Matrix has done very well, and we're going to be just as good as Matrix." So they got that money from universities.

CK: *Do you have a good story for me that always sticks in your mind? I know that Cascade was an early venture that really spun off. I don't know if that would be a story you'd like to share.*

PF: There are lots of stories, but what kind of story.

CK: *A challenge, something that kept you up at night, something that's instructive?*

PF: Well, the thing I tell all our guys that we bring in to be general partners here is that people say, "How do you get ahead in this business?" That's a question I get asked a lot. First of all, it's much harder today than it was when I started, because it's much more competitive. It’s much more efficient. And you have to bring value to your investment. Because our money is the same as Polaris’ money, we pay the same price. Nobody gives us a discount because we’re the great Matrix. So why are we going to be better than Polaris? We’ve got to give the smart entrepreneurs a reason why they want to do business with us. So to every general partner I said, “When you make an investment, don’t just focus on, ‘Are we going to make money on this investment?’ which is what everybody does. To me, it’s, If this investment is successful, will it lead to three other investments because of that? If it’s just one, you’re in the hit record business. You need to build a relationship with that team so that if somebody asks the president of Cascade, or whoever it is, There are three venture capitalists or five that are invested in your company, Mr. President. I want to start a company. Who should I go talk to?

Your job is to make sure that Matrix is the name that’s first out of his lips. And how do you do that? It’s not by being the easiest guy to deal with or agree with everything the president wants to do, but you’ve got to be the guy that if the president has a problem, whatever the problem is, the first person he’s going to call is you. If you’re the fourth guy that he calls, you’re not building that relationship that’s going to allow you to be successful in the future. And I'd say one of the frustrations I've had over many years is, to me, it’s crystal clear today that that’s what’s needed. So we’ve hired a lot of people here. The people we hire are uniformly smart, uniformly highly educated, uniformly high achievers. They work hard. But they don’t make us money. When people ask, “What do you look for in a venture capitalist?" I say, "I can't tell you. I don't know. I'll tell you after they've been here three or four or five years." But going in, everybody comes in and they all meet all these requirements. It's very hard to see what that magic ingredient is. And it's true in the industry. It's not just at Matrix. If people are honest with you — you look at the firms that have been successful, it's based on the individuals that are at the top of the firms, for the most part.

CK: *Can someone learn to be a good venture capitalist?*

PF: Well, that's part of the frustration. I managed to do it. A lot of others have managed to do it. But have we been successful at passing it on to somebody else? I don't think I have.

CK: *Is it an art, or is it a science?*

PF: Well, it's a combination of things. I'm on the board of Columbia Business School. The dean of the Columbia Business School asked me, "What is it that you learned at Columbia that allowed you to be successful in your business?" And I said, "Is there this magic ingredient that I got there? The answer is no." I was thinking and thinking. And he says, "It doesn't sound like there was any specific thing." I said, "That's probably right." Yes, I did learn accounting and finance and all these things that are important. But because you know these things, that doesn't translate into anything, right? It allowed me to get my first job in the venture business. And in those days, the pace was slower;

you could learn from your mistakes and other people's mistakes. Today it doesn't work that way. The pace is much higher. In those days, the firm might make three new investments a year. Today we do one a month. And we started an operation in India and another one in China. So if you do all the Matrix things together, we probably make thirty-five investments a year across the world.

CK: *You're saying you haven't found, in all the people you've hired, someone with that spark?*

PF: Well, no. I'd say Tim Barrows, who manages the firm today, has worked here his entire professional career. That's his only job he's ever had. He graduated from Stanford. He came here. I don't know, it's been twenty-five, thirty years. And he and I and Andy Verhalen have had a major impact in the success of the firm. But have we been able to replicate ourselves? We haven't done a good job of that. But I don't think any firm has. So it'll be interesting to see whether Mike Moritz pulls back from Sequoia, whether that continues. It's not an easy-entry business. People come into the business, they think they know everything, and it's not as straightforward as one thinks. It's a much harder business than people think. And they don't understand it until they've been in the business for five years or something like that. It looks like an easy business, but it's much harder. And you look at the firms that were the top firms twenty years ago. For the most part, they're the same firms that are the top firms today. It's very hard to move up in this pecking order.

CK: *What makes it so hard?*

PF: Well, when you think about it, you're a smart person, you want to start a company, and you go to a new firm or you go to Kleiner Perkins or equivalent. Why would you do business with a new firm? Here's Kleiner Perkins: We did this. We did this. We did this. We know this person. We know that person. And you'd have to be an idiot to go choose the new firm, unless there's some unusual characteristic about the new firm. But I maintain that — and I never believed this when we started, but I tell people today, "If we invest in your firm, the likelihood of your being successful is greatly enhanced." I know it's arrogant for me to say that, but when you think about the process, particularly in startups.

CK: *When you vet this new company, what are you looking for?*

PF: What I looked for and what we're doing today is different. The world has changed.

CK: *What were you looking for?*

PF: What I was looking for was very well defined. I tell people, "If Steve Jobs would've walked in here or Bill Gates would've walked in here to start those two companies, I would've absolutely turned them down.

CK: Because?

PF: Because they were weirdos. They didn't finish college; they were working out of their garage. We don't do those. We back people who have proven that they've been successful at — name the company: Intel, Cisco, Hewlett-Packard. They've achieved some level of success in a well-run company, and they know everything about their market segment, and they know what to do with a product opportunity that they think is unique, that they're uniquely positioned to see. So they're preselected and they're rational human beings. Facebook, would we have ever done Facebook? Probably not. That's what we did. That doesn't mean that's the only way you can make money. But as I've thought about it, we need to have a repetitive process. The more we can stick to that discipline, the better off our results are. So that's what we do. Kleiner Perkins sticks their necks out a lot more than we do. We didn't do any of the clean energy things. We talked about it a lot. I said, "It doesn't make sense to me. The people that we met did not have that pedigree of having been successful at a prior clean energy company. We're not doing any of those things."

CK: *How emotionally involved do you get in a startup or a company that you've backed?*

PF: Well, that's another good question that I tell our people here. My view is it's not our job to run anything. To the extent that you're running this, you're doing the wrong job. Your job and my job is to make sure the president we have in place is extremely capable and can do that job. We can help them interview people. We can give them our opinion as to, do we hire this vice president or this vice president? But at the end of the day, it's his call. You give him your input. We measure him or her versus the performance and the budget and meeting expectations and all those things. It's not our job to design the new product for them. I firmly believe that. I also firmly believe we are not visionaries. For people to say, Yes, this is the time to invest in windmills, or something, I think that's a fool's errand. And people who think they can see the future are kidding themselves.

CK: *When you're investing, what's more important, the people or the technology?*

PF: I'd say I weigh heavily on the people, but if it's a good idea and we get excited about the idea, I need to be convinced that we can work with the founders to bring in the right people. If they say: No, I'm Mr. Google, I want to run Google and I don't get along with those two guys. We wouldn't do the deal. I like to keep things as simple as possible, and it's been a good formula for us to do. We're highly repetitive and disciplined. And then we try to do the same thing in China. Actually, that's another interesting topic. So we started these activities there. They're new activities in essentially new economies. How do you staff those, and what do you ask them to do and so forth? We pass on our learned experience to them. Now, they make the decisions. I was on a panel with Dick Kramlich at an NVCA function four or five years ago, and we talked about how you expand the firm and do all these other things. And he had one view. And then I spoke and I disagreed with everything he wanted to do.

CK: *So what is your view?*

PF: Our deal is — so Dick made central decisions and everybody was a partner in the big NEA funds. We're, I think, just the opposite. We have separate economics for the people on the ground in China. We talk to them about what they're doing, what new investments they're looking at, what their strategies are. But at the end of the day they own the problem and they make the decisions. We are important advisors.

CK: *So you're teaching them how to do venture capital?*

PF: Right, remotely.

CK: *That's kind of like how Peter Brooke went around, in some way.*

PF: I've heard him talk. I don't really know exactly how he did it. People say, "Have you made any mistakes?" "Absolutely, we've made mistakes. But we always learn from our mistakes." And I am optimistic about being involved in those activities, in those countries. It just feels like the opportunities are huge. And I maintain that — people say, Well, it's not the right time to be investing in China or India. I say, Yeah, but you can't show up in ten years and say, 'Okay, now's the right time and now we're going to open an office.' We'll be way ahead of you by that time.

CK: *How do you find the people in China or India?*

PF: I'll tell you how we did it. We backed an entrepreneur here. We start companies in the back here, in our incubator space, which is not a big deal today, but it was a big deal fifteen years ago. We backed a young man who's now a general partner who works for us, who started a company that we backed. He sold it to Hewlett-Packard and now he's with us. While he was incubating here, I said, "Do you know anybody that you went to Harvard Business School with that was Chinese that you respected and had a high opinion of that I should talk to, because we're looking to try to do something in China." He said, "Oh yeah. You ought to go talk to so-and-so." I said, "Well, who is he?" He said, "He had the highest math scores in all of China for two years in a row." I said, "Well, that sounds pretty good to me." And we met him. His name is Bo Shao. We met Bo. We worked with him for two or three years and said, "Bo, your goal is to try to find us investments in China that we would invest in out of the U.S. fund, but, more importantly, we'd like to start an operation in China. We'd like you to see if you can find some people in China that are like you: very smart, very accomplished, very confident, that have had training in the U.S., have been successful in the U.S."

So he found the team. We put a team together. We found one person, then we found another person. We did the same thing in India. So I pay a lot of attention to what we do in China and India. I pay attention to what we do at the general partner level in the U.S. I don't pay as much attention to the investments we make in the U.S. I'm not as interested in that anymore. I'm available to talk to whomever wants to talk to me here, but I don't manage anything. And then across the hall we have a public equity investment partnership that I started, I don't know, ten years ago, twelve years ago, that I've hired somebody else. Not I've hired; he's run it from the beginning and he's done an excellent job. So I can stick my fingers in a whole bunch of different pies, which I enjoy doing, but I'm not responsible for anything anymore. It's very satisfying.

CK: *So you're backing off?*

PF: I definitely am. But I have the best job in the world, because I deal with interesting topics and interesting people. But I want to win. That's very important to me.

CK: *That's the one thing you said. Even as a child you were competitive.*

PF: And we talked about it in 2000 here. We had done so well. I'll give you some interesting facts. I had figured out that in the first three quarters of 1999, we had returned more money to our investors in the first three quarters of '99 than we had in the prior twenty-five years total. And we had done okay to well in those twenty-five. In nine months, we returned more than —I think it was either twenty or twenty-five years; it might've been twenty years. Let me just think. Yeah, it was probably twenty years. And I said, This is not the real world. This is the dot-com bubble. I don't know if you remember it. Then the fourth quarter of that year we exceeded what we did in the prior nine months. Then we were about to raise Matrix VI. And I went to Tim and Andy Verhalen, now in their mid-fifties at this point, so then they would've been, whatever – twelve years ago they were forty-two or something like that. And I said, “I think we ought to just shut our doors.” And they said, Why is that? I said, “We’ve done so well that this is all the stars aligned; everything was perfect for us. This is not the real world. And it isn’t going to be much fun. And money is pouring into our industry. Everybody is a venture capitalist all of a sudden. This is going to be a terrible business to be in. My preference — and I am twenty years older than they are, eighteen years older than they are. I said, “I don't want to have to struggle to make a twenty-million-dollar gain in an investment.” We had one company that I remember we had a dinner for them and I said, “This is the biggest gain we’ve ever had in one investment in the history of Matrix.” And two years later they were number ten on the list, they had moved down so far. So that isn't the real world. And I knew it wasn’t the real world, and I told all our investors.

All our investors, they would call me and they’d say, Paul, we’re looking at investing in Charles River VI, or whatever, at Harvard Management. And I said, “Peter, not only shouldn’t you be doing them, you shouldn’t be investing in us, because this is not going to be a good business.” Originally, I'm sure, he thought I was nuts. Ten years later, he understood. And it turned out worse than I would’ve imagined. So if you’re not in Facebook or Twitter or maybe Groupon at the right time, or something, it’s a difficult business; and it’s still too much money, in my view, and too many people, and you have to back less-experienced people than we used to back. So all the rules that we learned over forty years have sort of been thrown out the window. They don’t make any sense to me. I like competing in China and India better, because we compete with many fewer people.

CK: *You've answered the question how venture capital has changed since you got involved. Is it a different generation of venture capitalists today?*

PF: It's not clear to me. So we have these debates among ourselves. There are a lot of angels and a lot of new people. I said, "I've seen it before. There have been angels before. And I know they all come in at the wrong time." Oh, no, this time it's different. And we have this debate, what to invest in. It made no difference what price you paid to get into Groupon or Facebook because it's worth a hundred billion, or whatever the number is. "What are you focusing on the price for?" I said, "I guarantee you at some point it'll make a difference. It always has made a difference. And then the other debate we had: Is this the top or is this a wave that's just starting? Should we be paying up to get into these things because so-and-so is doing a lot of this? And I said, "We don't need to have this debate. This is a top, and I guarantee you it's no different than every other cycle we've ever been through. Whenever it looks like it's easy money, it's never easy money."

CK: *The paradigm hasn't really changed?*

PF: No, it's always the same. Some things change a little bit. The cycle might be longer. You might get lucky and you may pay $600 million to get into Facebook or something and it's worth more and you can get out. On the other hand, if that's all you're doing and you're wrong, then you're out of business. And no one is that smart.

CK: *So the risk is almost greater?*

PF: Yeah. To me the hard thing in this business is keeping a discipline when you've missed a wave. That's the hard thing.

CK: *Looking back, do you see venture capitalism as a romantic quest in any way? Do you see romance in this business?*

PF: No, but I think it's the best business in the world.

CK: *You do? Why?*

PF: Again, to our younger partners I'd make this point: "Yeah, you want to make a lot of money. I understand."

CK: *Do we have twenty minutes? What do we have?*

PF: No, I'm done. I have to quit. But again, if you want to call me next week and continue on, we can do it by phone. Let me just finish that point. So, why is this the best business? One: You can make a lot of money if you're in it a long time. It's not a business that you can get rich next year or the following year or five years. It may be ten years, it may be fifteen years. But if you continue to be successful at it, it's amazingly rewarding. But, more importantly, you're dealing with interesting people all the time. They're innovators that are people that are changing lifestyles in the world. You're dealing, for the most part, with people who have no net worth and you're helpful to them in building net worth for themselves and net worth for their employees. And you can be in the venture business and be relevant for a very long period of time if you're good at it, more so than if you start a tech company. The people who started Stratus Computer or Apollo Computer were relevant and important people in the eighties, but nobody knows who they are today. Whereas people that were in the venture business, to be relevant for forty years, thirty years, thirty-five years later. You're at the leading edge of product development or technology or capability. So there's no other business like that. You're not collecting the receivables for the hundredth time. You're not laying off employees. You're dealing with interesting personalities. So it's the best business. Sorry we had to cut it short, but something came up and I have to attend to this.

CK: *Okay. Well, thank you so much. I will call you.*

This is a continuation of an interview with Paul Ferri, by phone.

Today's date is December 6, 2012.

CK: *Okay, what I want to do is kind of start where we left off. What I wanted to ask you is to talk about board membership, because I know it's an important part of what you've done,* *and it also probably takes a chunk of time. So I'm wondering how much time you spend as a board member.*

PF: That's changed the longer I've been in this business, but when I started out in the business I absolutely had no belief that I could add value to the success of the company. I was reasonably inexperienced. And I would say, generally, every board that I was on when I started, I was the youngest person on the board. And I was on boards with some big-name executives from big companies. Over a period of time, I learned that just because they managed a big part of XYZ corp didn't suit them to be constructive directors for our little companies, which was a surprise to me. And I also learned that over the years in replacing CEOs. When I first started doing that, I looked heavily at if they'd managed 10,000 people; that was important to me, more so than looking inside the person to see what I thought his skill set to be. So I started out basically not knowing much about being a director or understanding what's needed for a good CEO to be successful. And over the years, that all changed a lot, being on the board, to the point that where I sit today, or where I have sat for the last ten years or something, I wanted smaller and smaller and smaller boards, so that my voice was going to get heard more often than if we had a ten-man board.

Basically I learned over a period of time that this notion of building companies from a small company to a bigger company to a bigger company, that I had more experience at doing that than anybody else that was going to go on my board. And I still feel today, that if somebody says, Who are the best outside directors you've ever had on your boards? They're very few, if any. I started out believing I didn't add any value to you if you had an idea and you wanted to build a company, to where the last ten or fifteen years, I'm absolutely convinced that if I'm on your board and we have a good relationship and you're going to listen to things that I think are important, the likelihood of your being successful is greatly enhanced by my being on your board. That doesn't answer your question, but—

CK: *It really expands on my question, which is exactly what I wanted. Do you feel like when you're starting with a company, are you giving twenty-five percent of your time or fifty percent?*

PF: It depends. And I have some thoughts on that also. I can tell you the advice I've given our Matrix general partners. Some of them listen to me; others don't. Everybody's style is different. As long as they're successful, I don't care. But my belief is that the strength and selling point that Matrix Partners should have for entrepreneurs is exactly that fact, that if a Matrix partner or general partner is on your board, the likelihood of success is greatly enhanced, because we have had, collectively — and it's true of the top-tier firms. If you say, Why do they do well over a long period of time? And why is it so hard for a new firm to pop in and be successful? That doesn't mean they can't get a big hit on something. But if you think of it, which I think we discussed, that I think this has to be a repetitive process. And the more we can define what we do and what we don't do it makes us much more valuable to the entrepreneur than just our money. To me, if we're competing for a deal with another firm, we generally wind up paying roughly the same price. We don't get a discount because we're the great Matrix. We pay the same price. And if we can't convince the entrepreneur why at the same price he should do business with us rather than our competitors, we have failed. Because I believe we're best suited, certainly in New England and increasingly in California, but as I mentioned earlier, I always thought the California VCs were better than the East Coast VCs.

I believe that if we are competing for a deal we want to be in, in Boston, and that individual doesn't choose us to be his investor, either that person wasn't who we thought he was, or, two, we've done a bad job in selling our skill set. Because I absolutely believe what I said, that if we're you're partner, the likelihood of your being successful over a long period of time is greatly enhanced. So I've, over the years, been able to build up a relationship with individuals who maybe didn't understand that on day one, but then as they've gone more and more and more issues and problems with us, they clearly understand it. Selling that to a first-time entrepreneur is difficult. But if we're dealing with mature people, we tell them, Here's a list of everybody I've ever been in business with. Here are their phone numbers. You call up any of them, including people that I've fired. And I can give you stories, which we don't have time to do, of people that we've fired as CEOs who have come back when they wanted to start another company and have come back to us because, even though they hated us at the time we fired them, they eventually saw that we're rational, fair, intelligent human beings, that we were more right on what had to be done than they were, so that they've been able to swallow their ego and come back to us to back them on their second company. That doesn't happen every day, but it has happened several times.

So getting back to: How much time do I spend? I probably spend less time on my boards than the other Matrix general partners. I don't like to get involved in all the details and the inner workings of the companies. I like to just work with the CEO and understand, in my mind, what he's good at and what he's not good at, and then give my opinions to he or she. If I think the sales VP, or the R& D VP, RN or the finance VP is not the right level of capability we need in the company, I will make that known to the president and try to convince them of that fact. And then what do is, to the extent we need to replace a VP, I want to be involved in that hiring process, because I think I have more experience. Most of our presidents are first-time presidents, so they've never hired a VP of sales; they've never hired a VP of finance. As I said, we make one new investment a month and have for a long time. We've hired more VPs and presidents than any human being ever has an opportunity to do in his lifetime. We've made every mistake in the book in that process, and hopefully we've learned.

So we have specific things that I look for today that wasn't what I looked for when I started in the business. If I had to hire a CEO when I was thirty-two years old, I would've been very impressed that this fellow ran a division of whatever — Amazon or whatever the relevant company was back then. Today, I've gone full circle, where I don't really care how many people you've managed. I want to be in business with aggressive, very smart, very driven leaders who I can have a conversation with about important subjects and he's going to pay attention to what I have to say. I don't have a lot of opinions on the features that the product should have, and I don't think that's important. If I have to figure that out, we've got much bigger problems. So I tend to work at a much higher level than my partners, and I think eventually, if they're going to be good in this business, I think they have to get where I am rather than where they start out being. Getting into this business, I think you have to get involved in a lot more details than I would get involved in today. And also, it's easier for me to understand today what's working in a company and what isn't working in a company than it is for somebody newer in the business.

CK: *So you would say that at one time you were more involved in the hand-holding, the operating, the strategy?*

PF: Yeah. I would talk to customers to try to understand what was wrong with our product or why we weren't selling enough. I don't get involved in talking to customers and haven't for a long time. And a lot of people do. They want to know: Is AT&T going to do this? How does it compare with the competition? I don't do that, but most people do. Because I've learned if I talk to somebody at Verizon about, What are the prospects for our product, they're not going to tell me, Oh, yeah, you're wired. Your company is going to get this job. They're going to give me a reasonably safe answer. And we've had partners, GPs at Matrix, that get involved in infinite details of the product and then they miss the big picture. So I get involved. I want to be very involved in setting the expense structure for the company for the coming year. I'm a stickler at reviewing that more than most presidents would like. And I also can be very critical of failure to perform, whether it's in product development, or achieving bookings, or spending too much money. I like to review all of that, and I think that's very important. I don't like when we revise our business plan for the year three times or four times. Again, if all of those things start to happen, to me it's a reflection that the person we have running the company isn't up to the job that's required. And my job is, if I believe that, to try to convince others on the board to change. Then I want to be involved in who we hire next. I want to be the lead person on who we hire next.

CK: *How do you, Paul Ferri, characteristically handle risk, personally, emotionally?*

PF: I think I'm very good at it. I don't go up and down very much. I'm always pretty much the same person.

CK: *Does any of this keep you up at night?*

PF: No. It used to. When I started out, it kept me up at night. I remember maybe '73, '74 or something like that, I inherited an investment from another partner, because I'd been through a mess at a company and I managed to figure out how to solve that problem. And I inherited his mess. And all of a sudden I was chairman of a public company that was in default on $150 million of bank debt. And I'd never — I didn't have five nickels to my name at that time. I remember I woke up in a cold sweat in the middle of the night like, What have I done? (laugh) This is insane. Me? I have to go negotiate with bankers? But anyway, eventually I got that solved. So you get more confident. I think I made a statement to you that I've never met anybody in the business world that I think is infinitely smarter than I am. Whereas in the technology world, there were many, many people who were infinitely smarter than I am. I think I have very good commonsense. I trust my instincts a lot. I'm super confident that my opinions are more right than others'.

CK: *What do you think has given you this confidence?*

PF: Well, I've done it a long time. And, just as an aside, at Matrix Partners we review quarterly every investment that we're in with the general partner who has responsibility for that investment. And we have detailed plan, expense structure. And you can see by looking at how often the companies make a plan as to who is doing the right job and who isn't. It's not that complicated. People who perpetually change their plans because there's this wonderful new opportunity that we have to pursue immediately, that's always to me, a bad sign. Our job with small companies is we have to be profitable in a finite period of time. And when they start spending more money in new areas, there's something that's going to come back to bite us. I've seen that over and over and over. So anyway, we review, I don't know, forty, fifty companies each quarter in our U.S. portfolio. I sit through the same number in India and the same number in China that we're involved in. I've seen the pattern over and over and over and over. After a while, even I get it. Again, I didn't start out this way, but over a long period of time I developed more confidence that I was more right than others that I'd been on boards with.

And again, the interesting thing to me is that, see, I am not the best salesman of me to a new entrepreneur, but I've had numerous, numerous people understand that what I might've told them five years ago that they regarded as total insane drivel was probably something they should've listened to. I tell them, "In my next life, I'm going to be a great venture capitalist, because I'm going to have all these smart people that will listen to me, when they didn't do it originally." But I don't have to be right all the time. I have to be right on important issues. And that's the other lesson I learned, that you can't criticize everything that you disagree with. You've got to save your ammunition for the important issues. And that's another lesson that a lot of young venture capitalists – they always want to prove to everybody else that they're smarter than everybody else. That's interesting but reasonably irrelevant.

REFLECTIONS

CK: *Did you ever stop and think you might've enjoyed or been successful in another area?*

PF: Well, early on in my career, I frequently toyed with the idea — particularly when I inherited a mess. I became chairman and CEO of two public companies, maybe three public companies that we had taken public and they had gotten in trouble. The playbook was always the same. We would have five, six, seven directors as we were getting ourselves in trouble. And then when we were fully in trouble up to our neck, somehow I always wound up with the responsibility of trying to figure out what to do. And several times I said, You know, maybe I should just do this and quit trying to be a venture capitalist and instead be CEO of this company. And luckily I never did that, but I was tempted several times. But that was thirty years ago. And in hindsight, it was a decision I shouldn't even have spent time thinking about. But it's the same point I make to our younger, general partners today. They think that they're missing, that they should be starting companies. And to the extent that they're in the venture capital business, they're not building their net worth as quickly as they might by starting a company and being successful. And that all could very well be true, but I tell people that if you want to be in the venture business, you have to think about why you want to be in the venture business, not because you're going to make more money than by doing something else. If that's your only driver, you're focusing on the wrong things.

To me, the reason why you want to be in the venture business is that I think it's the best business that one can be engaged in, in that you're dealing always with new technologies, new products, new opportunities. You're dealing with the best entrepreneurs in the world. And you can do this from the time you're thirty until — I'll be seventy-four in two weeks, and you can be relevant probably up until the time you're seventy or seventy-something. (laugh) And there's no other business that you can do that with. The people that were relevant in the technology world thirty years ago, you can't name. Yes, they have their day in the sun, but particularly in the technology world, it changes so quickly that unless you're Steve Jobs or Larry Ellison, most CEOs last ten or fifteen years and then they disappear. What they do, I don't know, but you don't ever hear of them again. And you're creating wealth for a lot of people in the company. You're creating some wealth for you. You're creating wealth for your investors. You're creating employment. It is the best job in the world.

CK: *Do you see it as a romantic quest in any way?*

PF: I'm not a romantic kind of person.(laughter) I'm a boring person. I'm always saying that. In a way, I think that's helped me a lot. So I'm not huge up and huge down. And it's a business that you have to try to think ahead of what everybody else is doing. And I think we discussed, so that if we miss a wave, which they occur in this business, you can't second-guess yourself. You've got to say, We missed it. Let's go on. Let's be awake the next time waves start. But don't do what everybody else is doing all the time. That's a strong belief of mine. If everybody else is investing in Facebook-like things, it's way too late for us to be focusing on that, or communications equipment companies. So let's do what's not popular today.

CK: *When you started Matrix, did you have a philosophy for Matrix?*

PF: No. I had no — the philosophy sort of started around the late ‘80s, I'd say, when Rick Fluegel and I had to come to grips with having a strategy and having as focus trying to be the best at doing something. Prior to that, it was just work as hard as you can to find the best opportunities, whatever they may be. And over time the industry has had to change. I think we talked about it. So some people moved up into the private equity world and others moved, as we moved, into doing very early stage things. And the cycles are different and there are pluses and minuses to having moved either way, but you had to move one way and be a specialist at doing something better than your competitors. We went from where we talked about that having money was a unique advantage to right now the world is flush with money and having money makes us no different than six other partnerships in our building.

CK: *I was wondering how venture capital has changed since you started in it. Is that what you see?*

PF: So we all compete with each other in some fashion. We don’t sit down and discuss with — Sequoia, Benchmark, Kleiner Perkins, Greylock, whoever you think the best firms are. We don't sit down and say, Well, how do you guys feel about what we ought to be doing? We pay a fair amount of attention at what they’re doing, from afar, because they’re smart people, and if there’s something that we haven’t picked up on— I would say quarterly we review every deal that’s been done in our sectors that we compete in. We look at whether we saw it, whether we had an opportunity to win the deal, or if we saw it and passed on it. I always feel good if we had the opportunity, even if we made the wrong decision, that doesn't bother me that much, because that's the nature of the business. But if we don't get a time at bat, then we're not doing our job. So we want to see every deal that's in our space that gets done, particularly by the better firms.

CK: *So are there any venture capitalists that you would comfortably say that you most admire? Over the years—*

PF: I hardly know these people. You probably know them better than I do. But I'd say the people that have done a good job are the Benchmark folks, Mike Moritz at Sequoia, John Doerr at Kleiner. I'd say over the last twenty years they've done the best job. That doesn't mean they haven't made mistakes just as we've made mistakes. But on balance, however they do it, their results have been great results. As I think we talked about, my philosophy is maybe — it's different from John Doerr's philosophy in that, to me, he takes a lot more risk than I would be willing to take. And we're probably more similar to Sequoia, again, even though we don't ever sit down and talk about what our philosophy versus their philosophy, but we tend to do similar types of things.

CK: *Are there personal rewards in this for you? Have there been personal rewards in what you've contributed through venture capital?*

PF: Financially, it's been great. Satisfaction, it's been great. The fact that our investors, who are the best investors in the world, respect our opinion is very satisfying. And the fact that I think, generally, we have been more honest with our opinions to our investors than others have, as far as saying we have problems or we're changing people. My belief is they trust us as much as anybody that they're invested in. And that's very satisfying. So not only have we delivered great results for them over a long period of time, but they regard us as trusted partners.

CK: *This trust and respect is something that you put a high value on for your company.*

PF: And that comes through many, many different ways to our investors. You've heard of clawbacks. Do you know what that is? So everybody always focused on clawbacks and, have we overpaid ourselves. I've always believed that we've always overpaid the limited partners before we shared in anything, until I felt comfortable that we had a safe enough kitty that no matter what happened in the rest of the portfolio, we were not going to be in a position where clawback calculations had to be gone through. So we've never had that issue with our investors. Arbitrarily, at the beginning of a partnership, when we're starting to return money to our investors, we have voluntarily said, We're not taking our share of this distribution, until we've overpaid them upfront at our expense, which doesn't endear me sometimes, or hasn't endeared me to our younger GPs. But my attitude is, we've developed, over a long period of time, this reputation with our investors that we look out for their interests. Yes, I negotiate hard with them when we started a partnership and we wanted the very best terms, but once we signed the deal, they could absolutely trust us. So that's a great position to be in. We don't have a franchise, but our reputation is very important to us. I think as long as you treat people fairly, both on the entrepreneur side and on the investor side, and you do a good job, that's the best place you can be in this business.

CK: *Well, I could cite now that perhaps this is one reason why you earned the "Best VC in Boston" in 2001, by Forbes: "One of the Top Twenty Venture Investors of All Time."*

PF: And those are all nice things, but they're not necessarily — to me, what I just said, our reputation with our investors. And our investors — the institutions are reasonably the same. The people involved in having made the decision change. The people that I knew thirty years ago, I'd say most of them aren't in the same seats at the same institutions anymore. But that reputation goes on for some period of time beyond just what our results show. So it's up to us to make sure that it continues. And if it continues, we couldn't be in a better place, from that point of view. And I think it's very important — that one can make [decisions] that are shortsighted, and frequently managing partners make the wrong decisions.

BEYOND VENTURE CAPITAL

CK: *Okay, Paul, just to wrap this up, tell me what you do when you take a break from all of this.*

PF: Well, I'm a very big family person. I spend maybe too much time with my family and my children and grandchildren. I am interested in their being successful.

CK: *And how many children do you have?*

PF: We have three children and we have seven grandchildren. I share in their success, and I want them to be successful at whatever they want to do. I want them to put forth their best effort at whatever they do. So to just do something mediocre is unacceptable to me. I'm sensitive to that could be overbearing, but so far it's worked fine. And the most important thing in my life is my family.

CK: *Is anyone following in your footsteps?*

PF: Nope, because I think it's a very difficult business. When I started in the business, I was very lucky and I managed, but the pace of the business was a lot slower. You could learn. You didn't have to make all the mistakes on your own. Today it's highly competitive, and you're competing against very smart people, in my view. So I've encouraged our kids to try to do things where you're not competing with the smartest people. And they've done great in doing that. But, more importantly, they need to do what they like doing, what they can be successful at doing, and what gives them satisfaction at the end of the day.

CK: *Well, I know you'd want to include their names, since this is your story.*

PF: My children's names are Michael, Paul John and Jessica, in that order.

CK: *I'm sure they've gotten some wise counsel from you — it sounds like.*

PF: Well, I've been privileged to learn — it's a business that you learn a lot. You deal with a lot of human beings if you're interested and I am. Again, in Matrix, we try to analyze: What kinds of people are we successful with and why? Is there a pattern that we can repeat? The issue of being a repetitive process has been huge to me over the last thirty years. Okay, thank you very much.

CK: *Okay, well, thank you so much. I've enjoyed this time with you, and I've learned a lot.*

PF: So in your next life you'll be much smarter. (laughter)

CK: *But you anticipated so many of my questions; I found that most interesting.*

PF: Again, as a final statement: When I started in the business, I didn't know anything. I'd never thought about any of these things. But over a period of time, it's led to thinking about: How are we better than the smart people that we have to compete with? Or how are we as good as the very best? To the extent you can make that more of a process it helps everybody. It's caused me to think a lot about it. I'm always interested in picking other people's brains about that. (I have somebody working on my lawn here! [background noise]) All right, thank you.

CK: *Okay, good luck to you.*

PF: Bye-bye.