

Star Gazer Bob Grady – Managing Partner for Carlyle Venture Partners

Bob Grady serves as managing partner for Carlyle's U.S. venture operation, Carlyle Venture Partners. In addition, Mr. Grady coordinates Carlyle's global venture capital group, which has over \$1.7 billion under management in five funds. Mr. Grady has an incredibly rich history both in finance and in politics, having served in the Presidential cabinet, among other things.

[start box] "When I'm looking to invest in the stars of tomorrow, I look on two levels. One is conventional analysis, is the market that they're addressing big enough to let this be a big company? Or does it exhibit growth characteristics that it will be big enough to be a big company? Will you be swimming with the tide at your back?

Two, is their product so special, so defensible, maybe it's protected because it's a unique design and it has IP protection, maybe they just have a jump on everybody with a great idea, but they'll have a franchise, and is it defensible?

Big, of course, the people. Especially the earlier you go by stage in venture capital, the more important the key leader or two are because most business plans don't turn out the way you finance them, but smart people figure it out and make changes along the way and make a better company along with you.

Those are the obvious things, but I would say there is another level at which we look at things. That is what I might call the "Aha! Factor." From an analytic perspective, what I mean by the Aha! Factor is the first thing I try to understand is, why is this product or service a no-brainer for the person who's buying it?

salesforce.com, is the perfect example. When I was a partner at Robertson Stephens, we had just done a Siebel implementation and, no offense to Tom Siebel, who I'm sure, is a great guy, but it was probably the greatest waste of money in the history of our firm. The classic Siebel sales force story is they sold us a license for \$5 million dollars that by the time they had finished upselling Mike McCaffrey, our lead partner, it was \$15 million. Then we spent another \$3 or \$4 million with extra products to implement the thing. Then it was rolled out to a couple of dozen people who didn't like it, and it was so cumbersome that no one ended up using it. It was basically on the order of \$20 million down the rat hole – sunk cost.

Coming right out of that experience about 6 or 8 years ago, I got to be friendly with Marc Benioff and he walked into my office and said, here's an idea: 90% of the functionality of Siebel at \$50 per month per seat. He didn't even need to say anything else. The light bulb went off, and I said, "Aha!" From an analytic perspective, maybe it's what Clayton Christensen calls "disruptive technology," can you deliver something that is a quantum better price? It might well be that it's not all the performance of the incumbent, but if you can deliver 80% of the functionality for 10% of the price, it's a great deal. Do you understand the compelling economic value proposition for the customer? If you cannot understand this, you should not invest.

There's an aspect of finding a product, idea or concept that everyone seems to be using or that makes your life so much better, the first thing you should do, this is what my professor Jack McDonald at Stanford taught me, turn that product over, see who made it and go invest in it.

I'm a runner. I started running in Nike shoes in the early '80's and about '84 or '85 I only would run in the predecessor to Air Max, they hadn't even invented air yet, and I said this is such a great product, I'm going to buy Nike stock. It was a great buy in 1985. I bought Starbucks Coffee stock after I was thinking this has got a lot of value if you're as addicted to coffee as I am, from Starbucks when I think it was 100 stores or something, and now it's many many thousands.

Blackberry had a great idea to take advantage of people like me. Jim Balsillie is a friend of mine, the CEO of RIMM. They gave Blackberries to who they thought would be opinion leaders, namely equity research analysts on Wall Street and leading investment bankers in the technology industry.

When I got my Blackberry around '97, '98, it changed my life. At that point, RIMM was already public, so I just bought the stock, but it was a great buy.

I walk around every day with a little notepad and think of ten ideas. I think chief on every investor's brain is probably the concept of wireless. The basic idea that everything everyone does in the world of computing and entertainment and life, is going to be done on a wireless platform by the majority of people in the world for the next several decades.

You just think of anything anybody does: search the web, play a game, organize their calendar, work on an application, whether it's a spreadsheet or writing something, watch television, they're going to do it on a mobile device.

I've been active in China for 20 years and it's amazing to see the changes. My sister lived there working with her husband in the US Embassy in the late '80's before you really saw the impact of some of the changes that are ongoing. At Robertson Stephens we financed Sinu.com and Asiainfo and a bunch of others. At Carlyle we have been active in China since the late '90's, and now we have 60 professionals working across Asia in buyouts, venture capital and real estate.

My simple thing with China is this: this is the single most important economic event in our lifetime, by far, the explosion in China. Nothing else has come close, or will come close. The reason that is true is it is the greatest expansion in living standards for the greatest number of people in the history of mankind. The American Press is finally waking up to it, in the last 5-10 years they missed a lot of the story, thinking that this was all about cheap manufacturing. This is not really about cheap manufacturing, it is about the empowerment of a huge number of people, and the opening up of a society that includes over 1.3 billion people.

Most of what we are doing in China is thinking about if we can make it in China, we should, because we are probably going to be distributing in China. We're trying to think that as a huge business culture and consumer culture grows in China, what products and services will be needed to make that culture live better, just as it does in the West today. So early on we invested in travel services. Chinese consumers had a little more disposable income, so the first thing they did was travel to other provinces, why? Because they could. We had an early investment in C Trip, it was a great investment. We sold not too long after the IPO and made 16-17 times our money. You could argue we should have stayed because the stock's been a five-bagger since the IPO. More recently we invested in Target Media which does advertising at the base of elevators. The first bet was a pure play bet. That company was the number two player and recently merged with the number one player, Focus Media.

Currently we are looking at things in a wide range of both consumer products and business services. We're also taking advantage of replicating many of the conveniences that you have in the business culture in the United States in the Chinese context. I do think that China is unique, and for an American investor, challenging, culture. Carlyle's model in China and around the world has been to take people of Chinese descent who are natives of Shanghai, Beijing, Hong Kong, let's say, and have natives of those cities be the people that staff our offices in those cities because they speak the language, they know the culture, they have a social history and know the other actors in that environment there.

From a public policy perspective, China's growth is a great thing for the United States. China, and other high growth areas and economies, including India, will be the engines of global growth for the next several decades. That growth is occurring in the context of a market orientation, of support for free trade, of openness to both Western investment and access for our products and to their products and vice versa. It is occurring in a peaceful context, it was a gradual transformation with an open and democratic and free market business culture. This is a fantastic thing for the United States of America that this has occurred in a way that China is in favor of the same international order and set of global rules for peaceful commerce that the United States has long advocated: free trade, open lanes, and just a general embrace of the notion that an open global economic culture is the best for all.

Those in the United States who want to saber rattle at China and who think that this is a terrible threat are sadly mistaken. This is a tremendous opportunity for the United States to participate in global growth for the next century. It may well be, it is indeed likely, it is indeed probability of 1 basically that sometime in the next handful of decades China will by GDP measures be the # 1 economy in the world. That's fine. We'll be # 2. If we're both growing at high rates and enjoying productivity growth and enjoying rising standards of living, that's a wonderful thing for the United States. We stand to be a principal beneficiary of that, and we should not lose sight of that.

You know, I think it's a great time to be alive. I think the one thing that's been a fantastic aspect, if you think of the last decade, even though we've had wild swings in asset prices, one thing that has not changed, that has been unyielding, and that is the pace of innovation. The fact that people are constantly thinking about how to do more with wireless, how to do more with energy, how to take the amazing advances in technology and apply them in the world of medical services, therapies, and diagnostics. What's a better model for selling software. There's just a million ways to build a better mousetrap and the

great thing about venture capital and growth stock investing is you're exposed to some of the most interesting people with the most interesting ideas anywhere in the world. So I wake up every day, and I just can't wait to meet the next five companies and get out there and play our little role in how to help change the world." [end box]