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Fuzzy Math

"Well, that was fun." Rex had just finished arguing with a California lawyer representing the union investors. "Looks like we're off to the races. But I've gotta tell you, I don't think I've ever met a more difficult, dare I say, unpleasant individual as this lawyer they're using."

"Well, you know lawyers," Craig grinned, and then got to the point. "Do they have the deal points right?"

"Yes, finally. In principle at least. But speaking of principles, you know what bugging me? It's not so much Seth Rossi and his finder's fee. It's this Quinton guy he introduced us to. I just don't know. We haven't really done anything with him yet, but I'm concerned."

"Rex, Quinton's news wire could be perfect." Craig saw the bright side, as usual.

"Right. It'd give us more credibility than issuing press releases, that's for sure. Anyway, maybe he'll come through, maybe he won't. I worry when guys get too clever. Do you recall him saying something about tax avoidance on stock in closely held companies after they go public?"

"Vaguely."

"He said you could put a collar on your stock by placing puts and calls on the same shares. Then you put the money in a trust and borrow it back from the fund. You pay interest on the money you borrow. But since the money isn't taken as income, you avoid paying taxes on it, and since you're paying interest on borrowed money, the interest is a write-off. So you spend the money, postpone your taxes, and leave it to your heirs to duke it out with the IRS."

Craig shook his head. "Sounds more like tax evasion than tax avoidance. This smells like the kind of thing that could land you in jail."

"I don't know if he was seriously proposing this, or was just trying to sound clever, but…."

"But…let's be careful around this guy."

"Remember what you said the day we started Value America?"

"Yeah. I told you it was supposed to be your job to keep the bad guys away."

"Well, my radar tells me you're three for three here. Quinton, Rossi, and Durn are all going to be trouble."

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One of the things that really rankled us was that when the venture capital round had cratered, the relationship with CapitalOne had disappeared along with the cash. So we were particularly eager to meet Derk Quinton's friend at Kessler Financial Services, a valued partner of financial giant MBNA. To this gentleman's credit, he had managed MBNA's co-branded credit card for Gateway Computers—the "Moola Card" (it's a cow thing).

As the discussions began, Craig explained that we were going to need a co-branded credit card. No problem. An installment plan for major purchases? Yes, we can handle that for you too. How about access to their customer data to help jump-start our custom marketplaces? Of course. Things got off to a promising start.

And then the rumors began floating through the grapevine. Craig and Rex were told some disturbing things about the head of KFS, Howard Kessler, from an investor. Should they pay heed to these stories? It was tough trying to figure out whom to believe. The guys hated making important decisions based on hearsay.

Then as the discussions progressed, Derk's contact made an unusual request. He asked that all communications about this transaction go to his home, not his office. The deal was to going to be directly with him, he announced. And the payment for his services, including Value America stock, would be going not to KFS but directly to his personal accounts.

Craig and Rex balked. This fellow was being paid by his employer to perform these very same functions. For him to moonlight the project was, they felt, unethical. Uncomfortable, they bailed.

Some time later, it should be noted, we found out that the rumors we had heard concerning Howard Kessler had been quite untrue. In reality, the man was a class act, completely worthy of the trust MBNA had placed in him. That revelation made one other fact all too clear: it was getting harder and harder to distinguish the good guys from the bad guys.

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I guess ol' Derk does have some contacts, Craig thought as he escorted the two executives up the stairway to the Attic. They were from Volpe Brown Whelan, one of the largest independent investment banks focusing on dot-coms. Quinton said he had placed a call to his friend Tom Volpe. We would learn later that it had actually been John Motley who had started the wheels turning, but today Derk was happy to accept the credit.

Mark McNay, the firm's senior investment banker, was one of the classiest Craig had encountered. It wasn't just "the uniform." They all wore expensive Italian suits and silk Hermes ties. It wasn't just his polished manners or the picture of confidence he projected. What impressed Craig was that the substance matched the image.

There are two sides to an investment banking house. On one side are the investment bankers. They put the deal together and manage the relationship. They work with the company, its accountants, and the lawyers preparing the S1 for SEC scrutiny as well. Mark McNay was such an investment banker.

On the other side are the analysts, who, as the name would imply, analyze the company to determine its viability and value. The analysts communicate with investors, write research on the firm, and explain the company's model to the investment community.

Naturally, nothing much happens unless both sides of the investment banking equation are in sync. That's why McNay brought his analyst along. Her name was Andrea Williams. A tall, slender African-American woman with a dazzling intellect, she was every bit as polished and apparently just as knowledgeable as her partner.

Craig ushered them into his office at the top of the cramped, poorly lit stairs. He gave them the grand tour of the store, outlined the company's five core concepts, explained the seven things that consumers want most, and discussed the four things brands need. He showed them just how close we were to being open for business.

He brought them up to speed on where we stood financially, including the union's commitment to fund a mezzanine round at a $100 million valuation. He explained how we intended to invest the money we raised—solving our remaining technical challenges, hiring more merchandisers, and getting our initial advertising campaign off the ground.

Mark peppered Craig with questions. Good questions, Craig observed—questions that told him the guy knew his stuff. "Amazon's the biggest player in the space," Mark said. "You have to pay attention to what they're doing. They're moving away from their dependence on book distributors like Ingram Media and Baker & Taylor. They're talking about building their own warehouses. Bezos thinks you've got to own inventory in order to satisfy the customer. Are you going to sit here and tell me he's wrong?"

"If that's where he's heading, yes. He's wrong," Craig said. "But look, Mark. Amazon's not being run by a retailer, or even by a manufacturer. It was founded by an investment banker. I know Bezos has built a hell of a site, but he apparently doesn't understand inventory. If he buys it, you watch, it'll be his downfall. His overhead will increase by fifteen percent managing inventory—oh, not initially, because of the GAAP rules on burdening inventory. With GAAP, Amazon will look more profitable while they're building inventory. But the rules will hammer them the first time they find themselves overstocked."

Mark nodded, as if he agreed.

"When you add the five to ten percent they'll need to manage the company to the five to ten percent they'll spend in advertising, and then add the fifteen percent they'll waste managing inventory, they've exceeded the twenty percent margin they're going to make selling books. I'll be amazed if they ever turn a profit, no matter how much volume they do. No, the way to achieve customer satisfaction, and ultimately profit," Craig concluded, "is to fine-tune the inventory-less model. That means using technology to enable distribution partners to ship orders quickly."

"Your ideas," Mark said dourly, "are counter to Wall Street's view."

"Yes, I know. Hopefully, they'll discover the truth before somebody gets hurt."

Mark changed the subject. "What about the fact that Value America has no agreements with the big Internet portals, Yahoo!, Lycos, Excite, or AOL? Nobody in your space has gone public without having their anchor and tenant positions locked up."

"Ask yourself, 'Whose brand do you want to build, anyway?' The way we see it, Mark, we could pay America Online five million bucks a year—well, we could if we had it—but that wouldn't build our brand; it would build theirs. No, we've got a better idea. We're going to use offline advertising, direct mail catalogs, newspaper, radio, and TV—not the Internet—to drive online sales."

"Nobody's ever gone public without a portal agreement."

"As you may have noticed, we aren't particularly interested in what's never been done."

"Uh huh," Mark said.

Andrea Williams watched the conversation as she would a tennis match. Back and forth. She was analyzing. That's what analysts do.

"All right, then," Mark continued. "Let's talk about your product presentations. They make you look like a content provider, not a retailer. Nobody does this. You're just going to confuse investors, you know."

Oh, that's not hard, Craig thought, but he said, "It doesn't have to be either-or. We have many reasons for creating these presentations, one of which you just touched on. Nobody else does them. We believe it's important to provide the kind of information consumers need to make better buying decisions. If we're the only place they can go and get the straight scoop, they'll come to us, and they'll buy from us.

"Beyond that, we want the best brands to be our partners. We call it 'having skin in the game.' We want brands to be invested in the solution we're providing on their behalf. We're forming symbiotic, mutually beneficial relationships, hundreds of them, ultimately thousands of them. That strategy is fundamentally sound. It's at the very heart of what online commerce should be all about—forming factory-authorized relationships to sell the best for less, not this convoluted notion that you're valuable because you give stuff away."

"Well, okay, let's say I buy that. What about this convergence idea of yours? You want to give people a choice of buying online or over the telephone. C'mon. Are you a dot-com or a 'ma bell'? This is never going to fly on Wall Street."

"It should. Think about it, Mark. Say you bought a refrigerator online, and you get it into your kitchen, and the door opens on the wrong side. What are you going to do? Peck away at your email, hoping somebody will respond? No. You're going to pick up the telephone! You'll want to talk to a real person who can solve your problem. Unless we move toward solutions that work in a converged world, we'll be old before we're even born."

"Well, I'm not sure…."

Andrea couldn't take it anymore. She slammed her palm down on the table. "Mark! Would you please just…shush up! This is the only model in this space that makes any sense. This guy understands what e-commerce ought to be. It's genius! Every one of his five core concepts is right on the money, including the one you haven't trashed yet, the one about being comprehensive. His idea about building the infrastructure to bring brands and consumers together is exactly how online retailing should work. I don't know what your problem is, but he's right."

Mark McNay rocked back in his chair. He had a big grin on his face. "I know that. I was just trying to see if our friend Craig here could stand the heat. Apparently he can. The Street's got a lot invested in the Amazon model, and his plan is radical—a whole new paradigm.

"You know as well as I do, Andrea, when other analysts hear this stuff, they're gonna come down hard on Mr. Winn. He's going to gore every one of their sacred cows, and they aren't going to take it lying down. People have made too much money to let somebody waltz in and prick this dot-com balloon. I just wanted to make sure Craig here could handle the pressure, that's all."

Andrea tried her best to give Mark a dirty look.

"Yes," Mark said, "I don't think we have to worry about your communication ability. You did a right fine job. Sorry about hammering you like that, but the Street's got a vested interest in their view. Normally my advice would be to keep low, not rock the boat—you know, don't point out the flaws in their reasoning. But I can't see that you have much choice. Everything you stand for flies in the face of what they believe."

Craig analyzed what Mark had said. "So if I run the company in accordance with their metrics, I'm dead because they're wrong. If I stand up and present the merits of our model, I'm dead because it's in their interest to say I'm wrong. Do I have this right?

"Yep, that's pretty much it in a nutshell."

"Sounds like a classic Greek tragedy. So where do we go from here?"

"We want to lead your IPO, that's where," Mark replied. "Damn the torpedoes." Andrea agreed, nodding her head. "We'll get a proposal to you. What are your revenue projections again?"

"Forty million for '98, a hundred seventy-five million in '99."

"So if we take you public in June of next year, which is probably the best timing, your forward-looking revenues will be a hundred seventy-five million. That means you'll earn a valuation close to that amount. Your comps are trading on forward revenues, you know. If things continue the way they're going, it could be twice that amount."

Twice $175 million was several times higher than the value of the current union round. It was even higher than their blue-sky buyout option of $300 million. Things were looking good.

"Before we get carried away," Craig said, "I have a problem. You need to know something about me before you sign up for what could be a suicide mission."

"What's that?" Mark asked.

"My last business, Dynasty, was a public company—a deal co-managed by Morgan Stanley and Salomon Brothers. Dynasty filed for Chapter 11 at the end of its fifth year."

"We know," Mark said. "We did our homework before we came. It's not a problem. Listen. OnSale's founder, for example, has a past far more checkered than yours, and his company is now public and doing well. The investment community wants to back people with battle scars, especially in the new frontier. This is no place for rookies or for people who don't know what it's like to lead, struggle, build something, make payroll. Besides, the way you handled yourself during Dynasty's fall should be worn as a badge of honor."

"Thank you, Mark, but if we're going to go out and do battle, I want you to know the whole story—no secrets, the unvarnished truth."

"We don't need to know anything more, Craig," Andrea said. "The very fact you thought it was important to volunteer this information speaks volumes."

It didn't normally work like that, of course. Investment bankers didn't often say such nice things. And they didn't usually make house calls on companies with fifteen employees either—especially ones hanging out in somebody else's Attic. On the other hand, impressing one investment bank did not an IPO make. If we were going to take Value America public, we were going to have to hit the road.

Companies getting ready to go public naturally endure more intense scrutiny than closely held "private" corporations. Value America was quickly getting to the point where we were going to have to have a real board of directors, something more substantial and broad based than Craig and Rex talking things over during lunch at the local Chinese restaurant.

Justin Caise was a natural choice to join Rex and Craig on the board. He was a respected attorney who had been a valuable ally for some time now. John Motley, too, had earned his place on our board with his timely introductions and tireless support.

ULIC's Rafe Durn would soon be in a position to command a seat on the board by virtue of his organization's timely and sizable proposed investment. Rounding out our brand new board of directors was Derk Quinton. His place on the board was based more on promise than performance. The United News Service connection was too tempting to ignore, and besides, Derk had asked—vigorously—to be included. After having taken credit for the Volpe Brown meeting, Quinton seemed to be a natural. He certainly looked the part.

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So it was that between John Motley's friends and one of Derk Quinton's contacts, an introductory road trip was planned. Winn, Scatena, Motley, and Quinton would make the rounds of all the big players. That would mean a trip to New York City's financial center, Wall Street. But it wasn't to start there. The journey would begin at Alex Brown, in Baltimore.

Dynasty, otherwise known as the University of Hard Knocks, was now history, gone but by no means forgotten. Craig could only hope that Mark McNay's intuition about the Street's attitude toward costly battles was right. Alex Brown's emerging growth analyst had covered Dynasty.

When they arrived, they found that the same analyst was still with the firm. Now, to their consternation, they discovered that he had become Alex Brown's analyst for dot-coms. The trial by fire had begun.

It quickly became obvious that the analyst remembered Craig, and unfortunately, remembered Dynasty all too well. But that wasn't the biggest problem. The analyst wasn't actually there. He was on the telephone. Couldn't make the meeting in person, something about the market acting up. That complicated matters. Value America, after all, was a visual sort of thing. How could one adequately describe the Mona Lisa over the phone?

They talked about old times, of course. To Craig's surprise, the analyst had no inclination to hold Dynasty against him. On the contrary, the way he had handled himself under pressure—making payroll out of his own pocket and working to the bitter end to salvage value for the shareholders, to the point that there were no lawsuits—was what he remembered most. Dynasty, strange as it seemed, had been miraculously transformed from a liability into an asset. The analyst understood that Dynasty provided the motivation to solve the problems that had brought it down.

But that in itself didn't mean the Value America team was able to make a dent in Alex Brown's armor. They left with the distinct impression that without the visual aspect of the presentation, they had failed to pique the analyst's interest. The fact that Alex Brown was in the process of taking another Internet retailer public didn't help much either. Nor did the day's record 500-point drop in the Dow Jones Industrial Average.

No go, apparently. But tomorrow was another day.

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Standing there on the sidewalk in the heart of New York's financial district, team Value America looked up at the tall buildings. The twin towers of the World Trade

Center dominated the skyline, like sentinels proclaiming this place to be the very center of America's economic soul.

"Looks like you're earning your stock options today, John," Rex said to Motley. "Four meetings in a row, with the best of the best. Ready, Craig?"

"I'm ready for them," he answered, still looking up. "The question is, are they ready for us?" Craig didn't want to worry his traveling companions, so he changed the subject. "Can you believe our luck? What happened to the market yesterday? It crashed, down five hundred points! These guys will probably be too distracted to pay attention."

"Biggest one-day point drop in the history of the Dow," Rex shook his head. "Boy, we sure know how to time these things."

"It remains to be seen if anybody is even going to show up for these meetings," Winn said apprehensively. "You couldn't blame them if they all said they've got more important things to do today."

With that, he looked at his watch. Six thirty. "We start in half an hour." Craig mulled over what was really worrying him. Goldman Sachs' lead analyst was one of the most respected, most credible presenters of dot-com gobblety-gook—the notion that popularity was more important than performance. With their colleagues at Morgan Stanley and Robertson Stephens, Goldman was responsible for the metrics, the corporate measurement criteria, upon which dot-coms were valued. Craig knew he was about to tell them that they were wrong. This, he thought, isn't going to be pretty.

Goldman Sachs wasn't the largest investment bank on Wall Street, but they were arguably the most prestigious. If Goldman Sachs elected to take a company public, especially as the lead firm, the company stood to gain instant legitimacy. And it was a given that the after-market support would be spectacular.

But there was a downside. Goldman Sachs had a reputation for under-pricing their deals—and they had good reasons for doing so. First, setting the IPO stock price conservatively assured that all of their deals would actually get done. But beyond that, these under-priced stocks invariably ramped up, making huge profits for their investors. The problem for the company going public was that less working capital was raised in the process. And raising working capital, for the company at least, was the whole idea. That's not to say we would have turned up our noses at Goldman Sachs. Oh, no. All they had to do was whistle.

The conference room was spectacularly situated on an upper floor in a corner suite overlooking the harbor. Lady Liberty stood out there, centered in the conference room window, with her torch lighting the way toward national prosperity, or so it was believed within these walls.

By seven o'clock, ten of the most influential people in New York were assembled. The Goldman Sachs team was led by Roth Latour, a brilliant investment banker, and by Rusty Kincade, one of the most famous Internet analysts on Wall Street. Kincade had written volumes on Internet commerce, and the guys had been hoping that he would attend the meeting. Craig had read everything he could find of Kincade's work, and he had weighed his presentation against what he knew of the analyst's thoughts.

As the financial experts filed in, the conference room took on the atmosphere of a sports stadium, although a gladiatorial contest is probably a more apt metaphor. Entrepreneurs versus Analysts—a fight to the death. Would the bankers give us a thumbs up or a thumbs down? A projector was brought in, and a large screen was unfurled from its recess in the ceiling. Goosebump time. If you're in business, presenting your company to Goldman Sachs is a good as it gets. So let the games begin.

As he began to talk about our five core concepts, Winn was all too aware that the first words that left his lips would probably manufacture a room full of enemies. As Mark McNay and Andrea Williams had discovered, our company followed no one's preconceived notions. Value America was more merchants and manufacturers than Internet geeks and investment gurus. We toed no man's line.

The truth was that there was very little "line" to toe, even if we had been of such a mind. Amazon.com was the poster child for e-commerce, and in the minds of the investment community in the fall of 1997, no one else was big enough to matter. There were portals, of course, and auction sites like OnSale were starting to appear, but in the pure world of "e-tail" at this time, Amazon was about the only game in town.

More to the point, Amazon had made these people rich. Their word was gospel. They were Wall Street's sacred cow, and we were about to fire up the barbecue.

"Ladies and gentlemen," Craig waded in, "Value America is driven by five core concepts—five principles that define who we are and how we operate. Each is based upon years of experience in the areas central to the success of online commerce—retail, brands, and the marketing and sale of consumer products.

"The first of our core concepts is comprehensiveness. We will sell products in over twenty categories, not just one, from computers and office supplies to appliances and home electronics, from sporting goods and toys to specialty foods. Value America will be the one place online where you'll find most everything you need for home and office.

"I realize that comprehensiveness is inconsistent with the model most analysts are touting. Clearly the most well-established company in our space is Amazon. They're a single-category store—just books. If success is to be measured by being like Amazon, then becoming King of the Niche would seem to be the right road to follow. I don't think so. I predict that even Amazon, whom I admire, will soon see the wisdom of our approach and expand beyond the sale of books into other fields. They'll be related at first—music perhaps. But soon they'll be adding categories farther and farther from their core business."

"I talked to Bezos just last week," Rusty interjected, "and he's committed to books. Jeff didn't say anything about being 'comprehensive,' as you call it. And as you acknowledge, his model is playing just fine here on Wall Street."

"Rusty, I believe that will change. But for now, let me give you three reasons for being comprehensive: scale, convenience, and comfort. It's going to cost a lot of money to build effective online systems, and even more to build a recognizable brand name in the virtual world. There's not enough revenue in one category to cover the costs. Profitability will occur sooner for a comprehensive store than it will for a niche player.

"Second, convenience. We can save people a lot of time by providing one convenient place for them to buy most everything they need.

"The third is comfort. Even though we know buying things online is safe, the general public is still worried about using their credit card. So there is something to be said for a store that has more of what shoppers want to buy. People don't want to give their addresses and credit card numbers to twenty different sites for twenty different kinds of products, especially when one store will have everything they're looking for.

“Convenience is a big factor in the success of traditional retailers. The world’s biggest retailer is comprehensive. WalMart sells everything from tires to t-shirts. Every shopping environment has a learning curve. A comprehensive store will have a decided advantage in the consumer’s mind over a collection of unrelated niche sites.”

As his audience endeavored to absorb the ramifications of his first point, Craig turned on the firehose again—giving them more information than they could swallow. “Our second core concept focuses on the communication of valuable information. In a moment you’re going to see our store. As we take our virtual tour, you’ll see that we provide far more product information than other sites. We’re committed to helping consumers become better buyers. The more they know, the more they’ll buy, the happier they’ll be with their purchases—and the less likely they’ll be to return them, saving everybody money.

“Most retailers stand as a wall between brands and consumers. We, on the other hand, act as bridge. Our mission is to be transparent—a conduit through which brands and customers can communicate and interact.

“Before Value America came along, brands were restricted to inefficient and ineffective ways of communicating the features and benefits of their products to consumers. A product’s package has limited space and capability. Quality sales help is a thing of the past. Have you ever asked the clerk at your local WalMart…come to think of it, you don’t have a local WalMart or anything like it here in Manhattan, do you? Have any of you ever shopped in a WalMart?” Craig asked. No one raised their hand or said a thing.

It suddenly became clear to him. How could these people purport to understand retail, much less position themselves as experts, if they had never even been inside the world’s largest retailer?

“Well, next time you’re out on the road, conduct a little due diligence. Go into a WalMart, veer left, and walk back to the electronics department. Ask the clerk what the megapixel rating of a digital camera means, or anything else for that matter. Try it sometime. You’ll find the experience entertaining. Like it or not, that’s what all of us online types are competing against—and it’s always a good idea to check out the competition.”

The crowd chuckled. The very thought of WalMart’s blue-collar image being competition for their dot-com superstars was, well, funny.

“The upshot of all of this,” Craig continued, “is that brands have no effective way to communicate to the customer why their products are better. The solution is our multimedia product presentations, like the ones you’re about to see. We research the products we sell, use them, and interview the brand’s most knowledgeable people, then share what we’ve learned. Brands love this, and they pay us to properly present their products in our store. In so doing they become our partners.

“But we’re not just a content provider. These presentations appear at the point of purchase, the best possible place. Wouldn’t you prefer to shop in a store where you could get the real story about a product—without pressure, without hype, on your schedule, and without leaving home? We’re using the Internet for what it was designed to do—share quality information.”

Craig looked around at his audience. This was starting to sink in. He saw a lot of head nodding, note taking, and spontaneous, involuntary smiles. “Some of you may be thinking to yourself, ‘All this information is going to take forever to download.’ And I’ll admit, if today’s 14.4 modems are as fast as the Internet is ever going to run, we may have overdone it. But compression techniques are improving, bandwidth is increasing, and modems are getting faster.

“All of which brings me to our third core concept: convergence. We are building Value America to work today and triumph tomorrow. When hockey legend Wayne Gretsky was asked why he was so good, he said, ‘I never skate to where the puck is. I skate to where the puck is going.’ That’s why we’re skating toward convergence. We believe that the productivity of the personal computer, the impact of television, and the communication prowess of the telephone will all come together—they’ll converge.

“That is why we record sound tracks for our multimedia product presentations, and why we produce video demonstrations that will be streamed in real time. Will it work at today’s 14.4 world? Not very well. Will it work tomorrow? You bet. And Value America will be ready when the technology arrives with the best multimedia content on the Web.

“For online retailers, however, the most important part of convergence is how you integrate the telephone into sales and customer service.” As he spoke these words, the smiles turned to grimaces. The thought of people helping people on the telephone was as blue-collar as shopping at a WalMart to those in this circle.

It was an Amazon thing again. Books are easy to ship, and they don’t break, so you don’t need customer service. You don’t sell them either, at least in the sense of explaining features. So Amazon had convinced everybody (on Wall Street, that is) that customer service call centers were passé—a victim of their superior technology.

“What if you live in a home without a Web-enabled PC? Today, that’s seventy percent of America. How are you going to buy something online in the first place? Folks, the telephone is essential to serving customers in the virtual world. And this will all become seamless in the converged world.”

Craig knew he was making an impact, but he also knew he was about to take a cattle prod to another of their sacred cows. “Now, the Web is getting to be a pretty crowded place. Every day, it seems, there are more places you can visit, get information, or shop. So how should we get the word out about Value America? He waited to see if anyone would rise to the bait.

Rusty Kincade knew the answer. This was a no-brainer. “Follow the lead of Amazon,” he said. “Get your anchor and tenant positions locked up on the big portal sites, Yahoo!, Excite, Lycos, and AOL.”

Oh God, Craig thought. How could such smart people be so out of touch with reality? It was as if their virtual world had no contact with the real one. “Ladies and gentlemen, let me introduce our fourth core concept. We are going to drive online revenues with offline advertising.”

Instant murmuring. It wasn’t done that way. You could see it in their eyes—this guy’s trouble. “I know that sounds radical to many of you, but please hear me out. You’ve been thinking of online stores the same way you think of portals. But they’re not the same. AOL and Yahoo! are media companies. Amazon is not. You should judge me

Craig saw their eyes starting to glaze over, so he retreated to more familiar territory. “Interestingly enough, Amazon started out with an inventory-less model, just like ours, only simpler, since they were dealing with a single great distributor, Ingram. And yes, I know they've begun talking about building warehouses. From what I hear, they say they're doing this in the name of customer satisfaction. Am I right?"

"Yes, that's true," Rusty said. "Bezos believes that owning inventory is necessary to satisfy the consumer. You know he's fanatical about satisfying the customer, don't you?"

"Yes, I am sure he is. So are we. But I respectfully submit that owning inventory is not the answer. It's the problem. I don't wish to be the bearer of bad news, but owning inventory will be Amazon's undoing. Jeff Bezos is a banker, is he not?"

"That's right," Roth replied. "He's one of us."

Winn took a deep breath and studied the room. "Folks, I've probably forgotten more about inventory, its costs and its problems, than anyone in the dot-com world knows. There isn't time to explain the consequences of owning inventory. For now, all I ask is that you envision the possibilities of a new paradigm. We can replace inventory with systems, and distribution centers with technology. We can build, in fact we have built, an electronic conveyor belt between factories and consumers. This is the real promise of the virtual world: linking supply and demand."

The analysts were awake again. Their sacred cow was once again bellowing. Craig didn't care. "Do the math," he told them. "It's my considered opinion that the numbers will never add up. Amazon will never turn a profit."

The analysts in the room were not happy with Winn's pronouncements. Strangely enough, their partners, the investment bankers, were pleased. They appreciated his business logic. Our team had managed to divide the room into warring camps, based solely on whose reputation would be trashed if we were right.

But few of them, whether investment banker or analyst, had ever gotten their hands dirty working in a business. They were naïve, having earned the right to be Goldman's golden boys merely by getting good grades in school. It was becoming obvious that dot-com euphoria was being built on a truly flimsy foundation.

Undeterred, Winn took them on a tour of the store. It was the same basic presentation he had given a hundred times. He knew beyond a doubt that his logic was flawless and his message was compelling. As he proceeded, the investment bankers became more convinced that he was on the right track, and the analysts grew more uncomfortable and antagonistic. It was starting to look like Verdun.

Craig had presented the store so many times, he could now do it on autopilot. It was during one of these hypnotic moments that Roth Latour's comment, "Yes, he's one of us," finally sunk in. It all dawned on him: Bezos is a banker, not a retailer. When he took Amazon public, he needed comps. There were no online retail companies with which to make a comparison, and offline retailers had less dazzling valuations—so portals, he must have thought, were perfect. They're valued more highly than gold; I'll use them for my comps. While simple and benign in itself, this idea started a catastrophic series of events that no one could have imagined on this day.

The partners patiently explained that with the economies and advantages of Value America's business model, taking us public would be good for Goldman Sachs. If our view of the virtual world was right, Goldman would have hedged their bet. Besides, an early IPO would put Value America on the fast track to becoming the first Internet retailer to turn a profit. And wasn't that—profitability—what it was all about? Craig assumed it was a rhetorical question. Turns out it wasn't.

"Mr. Winn," interjected Rusty Kincade, "Profitability isn't the issue."

"It isn't?"

"No," Kincade explained. "There's a whole new market dynamic in play, and profitability doesn't count for much. What counts today is market share, revenue growth, and first-mover advantage."

Team Value America tried hard to follow his logic.

"In this space, you're either number one or you're nothing. Investors aren't interested in number two."

"With your brand partnerships, you could become profitable sooner than others, a couple of years perhaps," Latour added. "But by that time, the market is going to be saturated with e-tailers like you—well, maybe not just like you, with your 'electronic conveyer belt,' slick presentations and such. But they'll be there all the same. They'll kick your butt in the revenue department and scoop up all the investment capital."

"In the new economy, it's grow fast or die," Kincaid concluded.

We had planned on growing like an oak tree, strong of root and thick of limb, able to weather any storm. And here were these guys, the acknowledged experts in the field, saying we had to be kudzu instead: grow like a weed.

Roth Latour spoke up. "Assuming you had enough cash to advertise, how much revenue could you generate next year?"

Craig quickly ran the numbers in his head. Strangely, he was not thinking about how much he could sell with an unlimited ad budget. He was calculating how fast the store could grow without hopelessly bogging down customer service. He knew that the bigger the number he gave Roth, the more interest there would be in taking us public, and the more we would be worth. He also knew this crowd devoured those that over-promised and under-delivered. And he knew they would write down whatever he said.

We had previously projected $40 million for 1998, easy from an advertising and revenue perspective. But more importantly, systems and customer care could handle the load. But there was a problem. The number was too small and too big. Forty million was tiny compared to the nearly two hundred million Amazon was projecting. And it was unbelievably large. How does a company grow from nothing to forty mil in its first year out of the chute? Craig said it anyway. "Forty million."

Roth showed no reaction. "And your revenues for the year after that, 1999?"

Rex, who had been quietly watching the drama, now spoke up. "A hundred seventy-five million is our projection."

"Gentlemen," Roth said, "the reality is that companies like yours are being valued on multiples of forward-looking revenue."

"Multiples," Craig tried out the word for size.

"As in more than one," Rex clarified. This was definitely a new and welcome concept.

"Yes," Roth replied. "Two, three times, who knows how high it will go. The point is, if you go public sometime in summer of '98, we'll use your hundred seventy-five million number…."

"Whoa, wait a minute," Craig said. "It's our philosophy to under-promise and over-deliver. Let's ramp up to, say, a hundred fifty million. That's twenty-five million less than we actually think we can sell."

"Okay. That would put your valuation at three hundred million dollars," Roth said. "If we take off the standard twenty percent pre-IPO discount, and another twenty percent to give our investors the bump they need, that puts the number around two hundred million. The IPO, with you on the road show, could be done at two hundred fifty mil, maybe two seventy five. You're a good speaker, and the store presents well. After you're public, that valuation should jump to somewhere between three and four hundred million dollars. That's the math du jour."

"I'll have a cup of that," Rex chuckled.

Rusty ignored the levity. "It's not about operating efficiencies, advertising productivity, or even profit. Right now the Internet is hot. It's all about growing fast and gaining market share. This is the way the game is being played."

"You've got a great model," Roth shared. "It makes a lot of sense, but you've got no chance of attracting any serious venture capital, or public equity, unless you start playing by the rules. Frankly, I can't believe you've made it this far without a venture capital round."

Winn and Scatena shared a look. Oh, let's not go there.

"Anyway, two hundred million, ramping to four, is about it."

We were practically broke, had twenty under-paid employees jammed into an Attic in a building we didn't own. The store wasn't even fully functioning yet. Two hundred million? Is that all? It was another surrealistic Alice-in-Wonderland moment. We were getting our reality directly from the lips of Tweedle Dee and Tweedle Dum.

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Later that day, Value America's team visited Morgan Stanley. It was a déjà vu experience. Craig had been all through Morgan's world before. He had great memories of Dynasty's IPO, memories of his first investor speech, when the stock had jumped in one hour from $12 to $18 a share. The pain was there, too. Morgan's analyst had since moved on, but Winn remembered him like it was yesterday. He had been awesome during Dynasty's Road Show, Craig's tour guide on a ride few get to experience—the incredible roller-coaster world of Wall Street's magical journey called an IPO. In the end, the analyst had bailed. Couldn't blame him, he thought. It wasn't his fault.

Our team was escorted into Morgan's large glass-lined conference room. Rex fired up the laptop and demonstrated the store. The reaction was pretty much the same—enthusiasm on the part of the investment bankers, wariness on the part of the analysts, and a new kind of math that said two plus two equals somewhere between seven and thirteen, depending on how fast you can add it up.

The really amazing thing was that they too came up with a valuation of $200 to $300 million if we went public in the summer of 1998. The new math was certainly friendly, Craig thought, even if it was a mass hallucination.

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Robertson Stephens was a San Francisco-based investment banking firm, but they maintained an office on Wall Street. Our gang was looking forward to meeting their lead analyst, Dale Dandridge, the man who had coined the term "e-tail." But the previous day's record stock- market decline had Dandridge distracted, harried, and more to the point, absent. Once more, we were faced with communicating the virtues of the store over the telephone.

The Mona Lisa? Well, she was an Italian girl. From Florence. In her late twenties when Da Vinci painted her in 1505. Brunette, having a really bad hair day when she sat for Leonardo. No sense of humor at all. She just sat there with her hands crossed, but Leo told her dirty jokes until he got one tiny smile out of her, and that's what he painted. Now that little smirk is the only thing anybody remembers about her. Explaining Value America over the phone was something like that. Inadequate.

Although no earth-shaking impression was made upon Robertson Stephens during that first encounter, they would later become our lead investment banker when we finally did go public. Never say die.

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Our visit to Union Bank of Switzerland had come about through a friend of a friend. It seems one Stan Garmin, a friend of John Motley in the office products industry, was a keen supporter of a European industry publication called OPI—Office Products International—whose publisher was Mike Jefferies, who in turn had ties with this European investment bank with an office in New York. They were supposed to have enormous worldwide cash reserves. It certainly couldn't hurt to talk to them.

Their Sam Abrams wasn't your typical investment banker. He was part analyst, part hustler, and part-time TV commentator. He introduced himself as a "shameless self-promoter," and their initial conversation seemed to bear out his assessment.

As introductions were made, he said to Quinton, "You look familiar."

Derk explained that he probably knew him from a student loan venture he had been involved in, a deal that had gained him some notoriety.

"Yes," Abrams said with a smile, "of course! I must tell you, Mr. Quinton, you're one of my heroes. I followed that whole thing when I was in school. What a performance!"

Well, he certainly seems impressed with our Mr. Quinton. I presume that's a good thing.

UBS's reaction to our store was unbelievably positive. They not only wanted to do a deal, they wanted to do it immediately. They had apparently never heard of terms like "coy" or "playing hard to get." They committed to an IPO right then and there. Sam said he and his firm would "crawl over five miles of broken glass to lead Value America's IPO."

Craig brought the discussion back into perspective. Enthusiasm was one thing, due diligence was another. "Gentlemen," he said, "why don't you send a team to Charlottesville? See what we're doing. If you're still impressed, write a letter of intent, explaining how you would handle the IPO. Tell us why we should choose UBS."

They did exactly that. They came, they saw, and for a moment it looked like they were going to conquer. They wrote a letter that said Value America was worth two hundred and fifty million casabas. Suddenly we were within shouting distance of the incredibly optimistic $300 million pipe dream we had used to cool off the union's ardor such a short time ago. The $100 million valuation for the current round was looking positively cheap.

The letter did not sit idly gathering dust. It proceeded with great haste to the nearest fax machine, where it was sent to Mr. Durn of the Union Labor Investment Company. Hey, Rafe, we thought you might be interested in this….

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The tour made one more stop before returning home. It had begun one Saturday at a car wash. John Motley had overheard a friend talking about his business with an upstart investment house called Freedman, Billings, Ramsey. In typical Motley fashion, John asked his friend for an introduction. Now, in an office overlooking the Lincoln Memorial, the boys encountered a different type of investment banker.

It was obvious they weren't on Wall Street anymore. FBR had a different style. It wasn't that they couldn't afford the thousand-dollar Italian suits; they just preferred blue jeans. They were hot, and they knew it.

FBR was on a roll, having just completed the IPO for a remarkable businessman, John Ledeky. The IPO for his United States Office Products had created a company poised to sell four billion dollars of pens, pencils, and paperclips annually. John hadn't built the firm; he'd bought it—sort of. More correctly, the companies that comprised USOP had bought into John's idea. Hundreds of regional office products distributors and related office supply and services companies sold their business for stock in USOP. If all went well, they stood to make millions.

The lesson to be learned, if only one had a crystal ball, was that the corporate life of an entrepreneur is a mere vapor, here one moment and blown away by the capricious winds of fortune the next. John Ledeky would be gone within a few short months of his company's multi-billion dollar coming-out party, replaced by a man named Tom Morgan, who would in turn…ah, but I'm getting ahead of myself.

The bankers and analysts at FBR listened to our pitch. They too asked to take us public.

The Motley crew had now seen seven investment bankers. The score was one no, three solid maybes (one of which would later change to a leading-role yes), and three yeses (one of which was punctuated by a melodramatic pledge to crawl over miles of broken glass). Not too shabby for a store that had yet to open its doors.

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john Motley seemed nervous, uncomfortable. John was a man of impeccable manners and unquestionable good will. He would never stoop to demeaning anyone, never say anything bad about a mutual acquaintance. But this was different. Seth Rossi had just finished bellyaching to John about how Derk had stiffed him. Seth evidently thought he was somehow entitled to a piece of whatever Quinton was going to get out of his relationship with Value America. While a provocative and tasty hors d'oeuvre, this admission was bland compared to the dish Seth served up next….

"Craig," John said shakily into the receiver, "I just don't know how to put this. I—I'm really uncomfortable saying anything about what I just heard, and it's nothing but a rumor. It might not even be true."

"What's wrong, John?" he asked.

Motley continued beating around the bush. “It’s just that I could never forgive myself if you found out, I mean, if it turned out to be true. But….” There was a pause that lasted for what seemed like eternity. John was really struggling with whatever it was. “But…I, I mean, there’s a rumor in town that says…Derk Quinton, well, Derk has spent some time in jail.”

“In jail,” Winn repeated.

“Yes, well actually,” John said, “in prison. But it’s just a rumor. You know how people love to conjure up vicious rumors about successful people. But you may want to check this one out, you know, just to be safe, especially with him being on the board now.”

He did check it out, calling Quinton himself, and asking him point blank. “Derk, there’s this terrible rumor going around. I’m sure it’s not true, but I’d be remiss if I didn’t ask.” Craig was more direct than John. “Have you ever been convicted of a crime? Have you ever spent time in jail?”

Derk was miffed. “Gimme a break. That’s ridiculous. Don’t you think I would have disclosed something as important as that? I don’t know who makes this stuff up….”

Craig was relieved and tried to smooth Derk’s ruffled feathers. “Okay, thanks. I knew it couldn’t be true.”

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“Listen, CL,” I said, “Take a couple of guys and go over to the new building. There’s a furniture truck there. Give ’em whatever help you can, and call me if you need more bodies.”

“Sure, Pop.” My son took off with the only two guys he could find who would admit to having a minute to spare. Half an hour later, he called me. “There’s a huge tractor-trailer rig here. It’s loaded to the roof with boxes. The drivers told me they weren’t going to unload anything. They’ve gone to breakfast!”

“How many guys are we going to need?” I asked.

“All of ’em!”

At least we were finally going to move out of the Attic, I reflected. Having twenty-plus bodies packed into a space that could reasonably hold six had gotten a little old.

Once we had received the checks from the angel investors Craig had signed a lease putting us into a 9,000 square foot building across town. He worked out a deal with some of the nation’s biggest suppliers of office furnishings to swap our Multimedia Presentations for chairs, desks, filing cabinets, and systems furniture. So here we were, entering the new economy by borrowing an idea as old as time, barter. We had been in business for almost two years. Now, for the first time, we were actually going to look like it.

The Yellow House, as we came to know it, would be our home during our most exciting period. But on that cool November morning it was a blank canvas—miles of empty space, the smell of fresh paint, new color-coordinated carpeting, and network wiring all over the place.

The truck out in the parking lot gave us our first hint of just how large our infrastructure needs had grown. Everybody dropped whatever they were doing in the Attic and pitched in. Technologists, writers, designers, and merchandisers all became stevedores for a day, unloading the big trailer, hefting boxes up the stairs, uncrating furniture, assembling chairs, and sorting hundreds and hundreds of module pieces for the cubicles.

With a bit of technical help from the furnishing manufacturers, we assembled the cubes and put the desks together ourselves. Craig had measured the place and drawn the schematic we used to lay out the furniture.

Working together, manual laborers all, we knocked it out, got it done. In a couple of days, it was home sweet home, not opulent by any means, but certainly businesslike and professional—a stunning contrast to the claustrophobic rummage-sale atmosphere of the Attic.

We would have enough elbow room for at least the next three months.

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Justin Caise was on the phone, talking faster than usual. Rex sensed that the change in Justin's demeanor meant something. "As I understand it, Derk Quinton was supposed to receive stock options if United News Service helped us get the word out on Value America," Justin started in.

"Uh huh," Rex said. "'Course, he hasn't done anything yet."

"Well, his attorney's pushing real hard. I've had some experience with guys like this. Whenever one of these tough-talking types tries to negotiate a one-sided deal, I get nervous."

Rex tried to envision where Justin was going with this.

"Anyway, on my own initiative, I decided to run a Nexis Lexis check on your buddy Derk. Are you near a fax machine, Rex?"

"No," he said, "but I can be. Why?"

"Give me the number."

Rex did.

"Go stand by the machine. You're not going to believe what I found."

Justin hung up, leaving Rex both puzzled and worried. He walked down a narrow hallway and stationed himself by the second-floor fax, right outside Craig's new office in the Yellow House. As Rex took up his post, he could see Craig through an internal window, talking on the phone. On cue, the fax machine started buzzing. Out came the first of thirty-five pages—the record of the Federal indictment and trial transcript of one Derk Quinton.

Rex turned white. Out spewed page after page of legal documents stating that Quinton had been arrested, tried, found guilty, and had spent time behind bars in a Federal penitentiary. The worst part was the nature of his offense.

About seven pages into the fax transmittal, Rex staggered into Craig's office. One look at his ashen face told Craig something was desperately wrong. "He's an ex-con!" Rex said through his teeth as he waved the fax pages in the air. "Derk Quinton is a felon. He's done time. And not for something simple like armed robbery or mass murder."

Craig's eyes grew large. "Oh, no…."

"Oh, yes," Rex said. "SEC violations. Securities fraud. Non-disclosure!"

"Oh, my God!" Craig gasped. "We just put a convicted felon on our board! We're dead, Rex. Dead."