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From My Perspective

The sad state of entrepreneurship in America: What educators can do about it

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ABSTRACT

Today's entrepreneurial scene suffers from dysfunctional startups, a sick venture capital industry, possibly misplaced adulation from the public, and other troubling developments. This Perspective documents a number of current issues in technology entrepreneurship in the USA (many of which apply in other countries as well), offers prescriptions for what higher education institutions can do before, during, and after students' periods of study, and notes some recent and forthcoming events that may, in conjunction with universities' efforts, ameliorate the situation.

1. A troubled scene

While responsible people work to implement the UN Sustainable Development Goals, and to stave off humanity's ecological suicide, young nerds in Silicon Valley write unimportant apps to do (as one genius Internet meme put it) "things their mothers used to do for them." The Elon Musks of the world – those who prepare for the long game while financing it with innovative products for today's market – are so rare as to be anomalies.

Today's entrepreneurial scene suffers from a sick venture capital industry, a number of imponderable illogics, and, maybe, misplaced adulation from students and the public. The ailments also include:

- "Frat-boy" start-up cultures that waste money and denigrate women and minorities (Wadhwa, 2014).
- Venture capital investors (VCs) with no management experience, attempting to micro-manage the companies they invest in.
- VCs who prefer to invest in – and then manipulate and bully – young entrepreneurs, when in fact more successful new firms are started by older entrepreneurs with corporate experience (The Ewing Marion Kauffman Foundation, 2017).
- Engineer-entrepreneurs with no knowledge of humanities or liberal arts – i.e., with no idea of what products society needs, or how their development projects will fit into societies and markets.
- Insufficient attention to data security. E.g., Snapchat (Ribeiro, 2014) and MongoHQ (TrendMicro, 2013).
- In many states and countries, government startup funding going to politically favored but unqualified entrepreneurs.
- Outright frauds like Theranos[1] and Pathway Genomics (Duhaime-Ross, 2015).

At present, 30% of all entrepreneurs in the U.S. are foreign-born and nearly 80% of all the intellectual property in the U.S. in the high-tech sector – telecomm, semiconductors, and life sciences – has its origins in foreign-born entrepreneurs (Angelos Angelou, quoted in Newlands, 2017). America is, at present, the world's font of innovation. As Bernie Sanders and Michio Kaku have both noted on YouTube, this flow of innovation depends on immigrant brains and initiative. Headlines like "Is Brand America Tanking?" in the *Forbes* business magazine anticipate an America that is less attractive to entrepreneurial migrants, and thus a less vibrant innovator.

New ventures seem focused on growth (in order to give VCs a quick and rich liquidity event), not on delivering superior customer value. Luckily, worthless online advice to startups like "Put your resources into customer acquisition over product" (Prajapati, 2017) is balanced by more sensible pundits. Anand Sanwal of CBInsights, for example, calls out the "bullshit culture" of catering to investors rather than to customers.[2]

2. Venture capital

Lazy VCs know they need to tap the innovation potential of smart people who do not live in San Jose, Seattle, or Austin, but they still insist that companies they invest in must move to where the VCs are.[3] Opportunities are lost. Civic-minded entrepreneurs, who want their companies to benefit their hometowns, are out of luck if their

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[1] https://www.theverge.com/tag/theranos.

[2] http://us1.campaign-archive.com/?u = 0c60818e26ecdbe423a10ad2f&id = ac6cb97638&e = 3c60089143.

[3] VC Dave McClure, interviewed by Caroline Fairchild in 2016 at https://www.linkedin.com/pulse/500-startups-founder-venture-capitalists-lazy-dont-caroline-fairchild/.

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hometowns are St. Louis or Flagstaff. Despite a flowering of innovation in Asia, for example, few US VCs are willing to invest in overseas startups.[4]

The unregulated US VC industry[5] attracts, well, people who are attracted to unregulated financial markets, with all that that implies. Suffice it to note that VCs spout insider jargon ("space," "unicorn," "pivot") to obscure the fact that they really don't know anything. They invest in what other VCs invest in – one entrepreneur called VCs "lemmings" – hesitating to risk money outside the box.

Their culture of morphing failure into virtue ("I'd invest in him again because now he's experienced; he knows how the game is played"), possibly justified in the past, has metastasized. Now no one is responsible for anything. Fisher (2017) calls Silicon Valley the "land of no consequences":

> "Venture capital comprises such a small portion of the portfolio of large [pension funds] that there is little impetus to care about where VCs distribute cash.
>
> "In the later stages, a startup will go public or be acquired and, even if it is horrible, the VCs… will cash out, leaving others—your mom and dad's pension fund—to deal with the fallout.
>
> "Where is the [institutional investor] who is coming forward and actually withdrawing money from a sketchy VC? Where is the VC who admits they propped up an unsustainable company—along with underwriters—in order to make money and flip the risk to the public market?"

VCs exert unreasonable pressure on their startups, implying that a less than billion dollar valuation, or not disrupting a trillion dollar market, is essentially failure. "Stratospheric expectations are killing fledgling startups," says Wickre (2017).

More than one successful entrepreneur has told me, "I will never start a VC-backed company again." I must add that I am acquainted with a few highly intelligent VCs. But I am convinced they are members of a small minority.

3. Strange contradictions

One of the contradictions of today's entrepreneurship scene, then, is that failure is simultaneously glamorized and forced. If an investor said to you, "You're not going to be a unicorn, we are withdrawing our money and shutting your company, sorry, come back again with your next idea," would you not recognize the con?

VCs perform financially no better than stock index funds, but with higher risk (Mulcahy et al., 2012). Chamath Palihapitiya, founder of VC firm Social Capital, goes so far as to call VCs "worthless" (CBInsights, 2017). He claims VCs are motivated "to get credit, [to get] a *TechCrunch* article, to get a press release." People are rewarded for "making good [Powerpoint] decks… not creating value." VC Eric Paley (2017) is equally blunt:

> "Venture capital should come with a warning label. In our experience, VC kills more startups than slow customer adoption, technical debt and co-founder infighting — combined. VC should be a catalyst for growing companies, but, more commonly, it's a toxic substance that destroys them. VC often compels companies to prematurely scale, which is typically a death sentence for startups."

Nonetheless – in another strange contradiction – the city of Albuquerque dangled a $15 million lure to bring a California VC firm to New Mexico.[6]

A third contradiction: With its $93 billion Vision Fund, SoftBank has become a leading power in VC investment. Although IPOs have tended to benefit VCs more than ordinary investors (see above), "the big fear voiced by some analysts is that SoftBank's large check book will help firms stay private longer, which would be bad for the IPO market" (Popper and Lopatto, 2015). This fear is groundless, for the sad reason that other VCs have already made it happen. (See the McClure interview noted in footnote 3.)

Moreover, the publically touted valuations of unicorns and near-unicorns are at odds with these companies' "true" valuations after preferred stockholder perquisites are accounted for. Gornall and Strebulaev (2017) write, "The average unicorn is worth half the headline price put out after each new valuation." The level of small print in which these perks are hidden smells of potential financial fraud.[7]

A unicorn's valuation – if not the value – may still be high. Nonetheless, there ensues a fourth contradiction: The unicorns are not unicorns because of their intrinsically high value.[8] Low interest rates, according to the editors of *Verge*, have given us an "ever-expanding bubble in startup valuations, fueled by an ever-expanding pool of increasingly less qualified investors…. [Due to] pitiful or negative interest rates… people with a lot of capital will pay almost any price for the chance to earn a meaningful return" (Popper and Lopatto, 2015). Indeed, "after five years of ever larger funding rounds, the market threw cold water on the party. From Dropbox to Square to Snapchat, a lot of 'unicorns' failed to live up to their sky-high valuations." Softbank's huge investments may create another bubble, as the companies the Vision Fund invests in experience significant "valuation bumps."[9] Nikkei Asia fears that Asia's exchanges will lower their quality standards in order to attract more tech IPOs.[10]

4. Healthcare: botching the opportunity

My students in healthcare management refused to sit in the same classroom with students from high-tech. "We are in a caring profession," they said, "The tech guys are looking only for profit. Talking with them is thankless." For their part, VCs early in this century shied away from healthcare because of the delays attached to FDA approvals. The culture gap has not narrowed in the ensuing twelve years. Again from the dialog of Popper and Lopatto (2015):

> What many firms seem not to understand is that though there are massive revenue opportunities in health care, "disrupting" patients' lives can lead to death. "Ask forgiveness, not permission" works fine in software. The medical field doesn't move as fast as the software industry because moving fast and breaking things is fine for things but not for people. The job of slow-moving bodies like the FDA is to keep companies from harming patients in their quest to get rich.
>
> The thing is, I'm not sure Silicon Valley sees the difference…. [Healthcare and life sciences are] undeniably a slower, riskier investment than the next photo-sharing app…. Disruption is more dangerous when it comes to medicine.

5. What should educators do?

5.1. Before students are admitted

Campaign to improve pre-college education in the USA, including science curriculum. Join the AAAS and other concerned organizations to push

[4] http://startuplawyer.com/venture-capital/flipping-your-international-startup-for-us-venture-capital.

[5] See Mifsud et al. (2010); Jickling and Murphy (2009). Singapore, in contrast, regulates its VC industry (Lim et al., 2016).

[6] https://www.abqjournal.com/1075943/nm-lures-silicon-valley-venture-firm-with-15-million-commitment.html.

[7] Gornall and Strebulaev's research was picked up by the *New York Times* and other news outlets.

[8] http://us1.campaign-archive1.com/?u=0c60818e26ecdbe423a10ad2f&id=83da300a37&e=3c60089143.

[9] Ibid.

[10] https://asia.nikkei.com/magazine/20171019.