Barons 2:

Radio Free Netpreneurs

James Kimsey • William Melton • Mario Morino • W. Russell Ramsey

Transcript of the June 18, 1997 Derek McGinty show on WAMU radio in Washington, DC. Follow up to the Potomac KnowledgeWay Netpreneur Program's Evening With The Barons.

Welcome to the Derek McGinty Show. They call Washington, DC, a company town, and that company is the federal government. Much of the business done here is done here because Uncle Sam resides nearby and there are those who say without the federal government Washington, DC, is a shell. But that might be less the case in the near future if my guests this hour have their way. The nation's capital is also one of the centers of the nation's rapidly expanding high-technology sector and, unlike in past years, the firms involved are not all making their money by selling to the federal government.

The expansion of the Internet as a means of commerce has opened the doorway for new jobs, new economic development, the growth of new companies and fast-moving firms in regions ready to make the leap. My four guests today say the DC area ought to be on the frontier of that. They have been dubbed "netpreneurs," for combining their business acumen with a sense of the possibilities inherent in all these new technologies.

William Melton is founder and CEO of CyberCash, he's trying to make it easy for you to buy things over the Net. You're probably already familiar with the VeriFone, which does credit card verification. We see that in action all the time. He was behind that, as well.

Mario Morino is founder of Legent Corporation. He is the current chair of the Potomac Knowledge Way Project, which is trying to network the right people together for high-tech business projects and is in the middle of hosting a special meeting about our topic today.

W. Russell Ramsey is founder and president of Friedman, Billings, Ramsey & Company (FBR), an investment banking firm specializing in raising capital for high-tech firm expansion.

And James Kimsey is the founder and former chair of American Online (AOL), the nation's largest online service.

I'm Derek McGinty. Call us at 202-885-8850. My guests have been dubbed by some "The Barons of the Beltway," and it is not, as some have said, a yuppie motorcycle gang. Gentlemen, welcome to the show. It's good to have the four of you here.

MR. McGINTY: *Let me begin by asking about Washington, DC, as a high-tech sector. People are familiar with Route 270 and the biotech firms that grew up out there. I guess there's a lot more to it than that, and I'll start with you, Mario Morino.*

MR. MORINO: Yes, I think there is, Derek. You have a major concentration in communications today—telecommunications right through wireless and DBS satellite bases that stretch from Lynchburg, Virginia, up through Maryland's 270 corridor. You have a growing concentration in the software and hardware areas. I think the emerging area is in content—information content, that ranges from healthcare information products coming out of the National Institutes of Health (NIH) to bioinfomatics, to content derived from the federal government information base, just to name a few examples.

MR. McGINTY: *Now, is there a critical mass here? Are there a certain number of firms, a certain number of things beginning to happen that you can start looking at the region and say, "Hey, this is a center of this sort of development," and has that happened here in the Washington area?*

MR. MORINO: Yes, it has, and I think it's not even near its a peak. It is just beginning. There is a study that was done two years ago by George Mason University that indicated there were over 2400 technology firms in this region. It stunned a lot of people when they realized the amount of revenue that was being generated by those businesses. There are 600-700 network-based and new media businesses that we are tracking at the Netpreneur Program and we're firmly convinced we are probably not even touching a third to a half of the total that are in this region right now.

MR. McGINTY: *Mr. Ramsey, as someone who works in the investment banking field, I'm sure many of these firms come to you for the cash to start up and maybe to keep going when their first operations don't yield profits right away. What's the sense you have of the region and how quickly it's growing?*

MR. RAMSEY: Well, I think all you have to do is look at the history of our firm which was also a start-up just a little over eight years ago. If you had asked me two and a half years ago, would we try to develop a practice around financing high-tech companies, I'd have said, 'Absolutely not. It's a world that is incredibly efficient. There is plenty of capital out there for all types of technology firms—hardware, semiconductors, across-the-board.' But that was before the emergence of the online world and the Internet.

It's clear—as you can see by pioneers like America Online, CyberCash and all the others— that it is a whole new world that needs capital. It needs new ideas. It needs a fresh look. It needs people who are willing to think out of the box, who do things differently. Being in the middle of that, with these 2400 companies probably ten minutes from our office, is an exciting opportunity.

MR. McGINTY: *Why this area, from your perspective?*

MR. RAMSEY: Well, as Mario said, this area is the center of communications. It's where all the major telecom giants either have major operations or are headquartered. It's where the whole base of the Internet was started, back with the original federal government funding. And so, just like any other area which benefits from regional people being there, it's spawned the start-ups of major corporations like AOL, UUNET and others. And it's increasing.

MR. McGINTY: *Mr. Kimsey?*

MR. KIMSEY: Well, I was born and raised here. That's why America Online is located here, so that happened to be an accident and serendipity rather than a process of logical forethought. But, in fact, Russ is exactly right. This has become a center for telecommunications and high-tech industries centered around telecommunications. I've bemoaned for a decade the lack of an infrastructure to support that, accountants, lawyers and so forth. I think all of that now is coming to pass. I think the community is developing into a "Silicon Corners," if you will. I think we are every bit a rival to Silicon Valley. There have been more high-tech start-ups in the Washington area than any place in the country except the Valley, and I think that speaks to all the points that Mario and Russ have made.

MR. McGINTY: *What do you think about the market in terms of investing and certainly in these sorts of firms right now. There was a time, a couple of years ago, when it was just so hot, maybe even a year ago, where, if it had "Internet" on it, everybody was interested. Then we saw your old company, AOL, have its problems with busy signals and there's other things that haven't come through as quickly as people thought they would. The Net is not making money the way people expected. Has the ardor cooled a bit now? Are people a little more nervous about it?*

MR. KIMSEY: Well, everything goes in cycles and nothing stays hot forever. It goes up and it recedes, and it comes back. I think it's an enduring business we all sit here witness to, and we've just begun to see the development of this phenomeno—and this medium, to be specific. I think we're in the last half of the first inning, maybe the top of the second.

MR. McGINTY: *So you really think this is still on the ground floor.*

MR. KIMSEY: Oh, absolutely. There's no question. The technologies that surround the development of this medium are only just beginning to show their promise. As you forecast them out, you'll be able to speak to a wall and it'll answer you, and point at things and they will respond. You'll be able to carry things around in your pocket that talk to you; you'll write on them, and they will translate that into the digital signal.

MR. McGINTY: *You know, I've heard all this before, though. We've been hearing this for a while now. Are we over-selling some of these promises by saying those sorts of things?*

MR. KIMSEY: Well, these technologies exist today. They're just buggy, too expensive, too heavy. You can't pinpoint with any accuracy when exactly these things will happen, but I think anybody even remotely associated with any of these industries knows intuitively it's going to happen.

MR. McGINTY: *Now, William Melton, let me get you into this. I mentioned VeriFone, which everybody knows about because, if you buy something with a credit card, they use it. What is it that you sense about the Internet as a medium for trade today?*

MR. MELTON: I think we can say that the Internet is advancing in something of a half-life of what previous industries have advanced. If you looked at the adoption rate of television over a 30 or 40-year period, if you looked at the adoption rate of the Automatic Teller Machines (ATM)—those things that you go to the bank and pull your money out of—ATMs have seen about a 20-year adoption rate. The VeriFone point-of-sale terminals, that's about a 15 or 20-year period. I think, on the Internet, we're seeing things go in about a half-life of that. We intuitively understand the promise of the Internet, that it makes geography go away. It makes, in many cases, time shift, if not go away. You can be any place in the world, anywhere, a few clicks of a button and you have the whole world at your fingertips.

Now, last year during the "hot" phase or the "manic" cycle, as you may describe it, everybody thought that maybe it would happen overnight—in six months or 12 months or eight months. It doesn't happen that fast. But it certainly is not going to take 20 years. It's in a period of three, five, eight or ten years, which is twice as fast as any major sort of technological phenomena adoption rate that we've ever seen before.

MR. McGINTY: *ATMs are such a ubiquitous technology, now. They've almost made travelers checks obsolete. You go to another place and you just use your ATM card. You wonder now, how did we live before these existed. Do you think we'll ever say that about the Internet?*

MR. MELTON: Oh, absolutely. In the early days of ATMs—unfortunately I have to admit that I was around during those days and I'm old enough to know that—the banks that were installing those large, expensive boxes in the walls of their banks spent millions of advertising dollars trying to figure out how to get people to use those things. We had . . .

MR. McGINTY: *And they broke down a lot.*

MR. MELTON: They broke. They had all the problems that you would think of. We had, at one time, what was called the 30% glass ceiling. In other words, it was common knowledge among bankers that we would never, ever get more than 30% of the population to use those things.

MR. McGINTY: *Really!*

MR. MELTON: It was just understood. Of course, today that would be laughable. But that's with the benefit of hindsight.

MR. McGINTY: *So you suggest that the Internet will come to that level of acceptance? You gentlemen agree with that?*

MR. MORINO: Yes, absolutely.

MR. KIMSEY: Absolutely.

MR. MELTON: Today, we're lucky if we have—Jim, your numbers would be better than mine—but we're lucky if we have possibly 15% to 20% of the US population really online today.

MR. KIMSEY: I think it's probably even lower than that, when you look at everybody that has a computer and a modem and a specific designated account. However, they're probably—through access—maybe 15% of the folks, but that leaves 85% who aren't.

MR. MELTON: And out of that, some of the industry is drawing the same conclusion about this 30% glass ceiling, that only 30% of the population will ever be the sort of educated techies who will use this new stuff. I would suggest that in ten years we'll look back and we'll laugh at that sort of a projection.

MR. RAMSEY: Derek, you mentioned the ATMs being ubiquitous. As a financier, I'd have no interest in the Internet if I thought it was going to stay the way it is today. But I think people are being too shortsighted if they don't recognize the power of what this communication medium is all about and the fact that the Internet will be fast, it will be ubiquitous and it will be dial tone. You don't pick up a phone today and say, 'I've just picked up an analog device, now I will connect.' No, it is dial tone. And the same thing will happen with the Internet.

You'll have browsers built into everything. People won't think about whether they're getting on the Internet or something else. That's just how they'll communicate. The power of the communication revolution which Mario talks about, is truly a transformation occuring around the Internet. It's not about technology; it's about the power of communication *around* the Internet. You already see that in America Online and others—really, America Online's the one building the brand.

MR. MELTON: If you think about the early days of the automobile, not many people drove, because they had to know how the carburetor worked and they had to turn the crank and it was . . .

MR. McGINTY: *It was too hard.*

MR. MELTON: . . . it was too difficult, exactly, and as Russ has correctly pointed out, people won't even think about what technology they are using, just as you don't think about what's under the hood of a car any more.

MR. McGINTY: *But you're saying it has to become a transparent technology.*

MR. MELTON: Exactly.

MR. McGINTY: *You have to be able to use it without being techno-whatevers.*

MR. MELTON: Yes.

MR. MORINO: It is about high technology in a lot of ways, but I'd argue it's much more about people and social dynamics at the end of the day. When you step back to look at the strengths of this region, what's moving today is the communications process. Think of the firms here—the MCIs, the LCIs, the UPIs and the ones which are just emerging left and right. The more traffic that occurs, the more the industry here will grow enormously.

Now, if you just step out to the five and eight-year cycle that Bill was talking about, and imagine that there is a degree of use, there's a degree of ubiquity. Look at the information content here in this region—our ability to package, to add context and knowledge—then consider the insatiable demand people have for information, for understanding, for context. I think that becomes the ultimate second wave of opportunity for this region.

MR. McGINTY: *Bill Melton, I wanted to ask you about the CyberCash phenomenon you've tried to create. You guys are doing what, about 10,000 transactions a day now or something along that line?*

MR. MELTON: At the end of our first quarter, that's what we were doing. We're obviously continuing to grow.

MR. McGINTY: *What do you think is the point you have to get to where you feel as though you've really broken through for your company, and what are the difficulties that are still standing in the way of having this sort of common currency of the Net that would allow us all to engage in the kind of trade you're talking about.*

MR. MELTON: Well, let me correct what might be a misperception. We do not create currencies. People that are down the street from here—the Federal Reserve and the government, you know, those folks who have guns—those are the ones that create currencies. We don't do that. In the physical world there are many kinds of payment instruments or currencies, all the way from the cash you carry in your pocket to checkbooks, debit cards and credit cards. All of those currencies, all those payment instruments, need to be migrated to the Net. That's our business—providing the technology that migrates the currencies, the payment instruments that you're deeply familiar with, to usability on the Net. So with that little clarification in mind . . .

MR. McGINTY: *Okay. Thank you, Bill.*

MR. MELTON: I don't want anybody with guns coming after me. I would say that it's obviously, again, a matter of getting to critical mass. And that critical mass has to come from content—the things that you want to buy on the Net, the critical mass of the tools in the hands of the consumers, the browsers that are equipped with security tools, on up to a general awareness of the availability of these tools. I would suggest that it will happen some time in mid to late '98. It it will become just understood, at least among those who are informed in this area, and then moving on in '99 and by year 2000 it will be as understood as ATMs are.

MR. McGINTY: *So two to three years, you're saying, we'll be in the midst of using this thing very, very, very significantly.*

MR. MELTON: As commonly as you use your ATM. Two and three years from now, you won't think of sending a check in the mail to your daughter who's away at college. You'll get on the Net and send her the electronic check through email.

MR. McGINTY: *Impressive. If it happens. What about the security concerns? I'm sure that's the first question.*

MR. MELTON: It's the first question, but actually, it's the least of all the questions. Security at this point has been largely resolved. We, and anybody that's serious about this, uses strong, industrial-strength security—security keys that are over a thousand bits long that are unbreakable with any technology we know of today. And they certainly can be extended to be longer keys if we need them. Security is not the issue. The issue is getting all the pieces working together, including understanding by the consumer.

MR. McGINTY: *And maybe that last part is the most important thing. The consumer understanding and trusting this technology. Can AOL fit in there somewhere?*

MR. KIMSEY: Well, this has been our raison d'être. We came to the marketplace with the consumer in mind. Obviously, the consumer ends up being the most important part of that equation. You can have all the technical elegance you want but if the mice don't eat the cheese, so to speak, you really end up with nothing, because ultimately you have to be commercially viable. In our case, that means the consumer has to accept it; and they will only accept it, as they've shown many times over, if it's affordable, easy to use and relevant to them.

MR. McGINTY: *Now, AOL has gone through its own changes with regard to making the consumer happy and also continuing to make money. You just went through this issue of going to an all-you-can-eat service and you've tried to go to more advertising. Do we have a sense on the Net yet, do companies have a sense, or advertisers have an understanding of how that's going to work and how these things are going to be priced and where is that technology?*

MR. KIMSEY: Well, we're obviously pioneering a new medium. Our sense is that, over time, transactions and advertising will pay the cost of this new medium, as it has in other new media. So, yes, we're moving in that direction. We have found that the pricing model we've got now works, and we just made a profit in our last quarter and expect to make a bigger one in the next quarter. But the first part of the strategy was to try and establish critical mass so that advertisers would understand that you've got lots of eyeballs that they can point at.

MR. McGINTY: *What's critical mass in your business?*

MR. KIMSEY: Well, we're eight and a half million subscribers. We're 53% of all the folks online, and so we're talking about dial-tone and online dial-up services. To the extent that we've got over half of that audience—eight and a half million people is bigger than most magazines, it's bigger than many of them put together—that's an attractive medium for advertising, and advertisers have come to understand that. You could see it in the recent transactions we've made where they gave us a lot of money up front.

MR. McGINTY: *Let's take some phone calls. Tommy in Arlington, you're on the air. Go ahead.*

TOMMY: *For an entrepreneur that's interested in trying to get something going, it's very tough to get introductions to venture capitalists (VC) in and around DC. People tell me I have to go out to the Bay area. I have partners. I've got a business plan. I've got a board of directors. I've got a lot going, but it's very tough to get in just over the transom to a VC if you haven't worked with them before. What do you recommend?*

MR. RAMSEY: Well. Obviously, the Potomac KnowledgeWay is doing a tremendous amount to promote entrepreneurship and utilizing the Web as a means to provide both a distribution mechanism to get your ideas and your business plan out to available funding sources. Mario probably can amplify on that.

MR. MORINO: Yes. There is a Web site you can come to today, the **Netpreneur Exchange** [http://netpreneur.org]. There you will see, first of all, a complete directory of online services for funding across the country, and we can put you directly in touch with 25 to 28 venture firms that are now located right in this region. We have a daily dialogue with those firms, Russ's Pegasus fund is an example. This kind of matching process has already been underway for two months.

MR. McGINTY: *You mentioned the Pegasus Fund. You put together a $25 million venture capital fund, didn't you, just for people like this?*

MR. RAMSEY: Correct. That's the the primary objective, to focus on businesses within the electronic commerce, Internet/Intranet sectors and telcommunications services; businesses which have ideas we think are going to benefit in this new environment.

MR. McGINTY: *So Tommy, it's your sense that people just won't even talk to you at all?*

TOMMY: *No, people will talk to me, but they have preconceived notions. I spoke with a gentleman who was uninterested because our proposal doesn't center on hardware. It's a service proposal that has to do with marketing. So because it wasn't hardware I couldn't even get in to give a presentation.*

MR. McGINTY: *Well, let Mr. Melton comment. Bill Melton, you wanted to say something?*

MR. MELTON: Tom, let me comment as an entrepreneur all my life. I've spent many days, in fact many months of my life, on my knees in front of VCs. My knees are bloody from all the hours I've spent in front of venture capitalists and the like, trying to raise funds. So I very much know where you're coming from, but I'd like to point out a couple of real facts that you need to recognize.

First of all, whether it's Friedman Billing & Ramsey or any other venture capital firm, they get literally thousands of plans a month. They have to have some filtering mechanism to get through and pick the wheat out of the chaff. And, frankly, the way that it happens is, to some extent, an old boys network. As much as I hate to admit that, all of us, as humans, rely on people that we know and trust. So what you really need to do is somehow figure out how to break into that old boys network, that sort of initial filter, and get to people who are known as peers in the network—this network of knowledge—and to get "recommenders." Certainly in this geographical area, people like those in the Potomac KnowledgeWay Netpreneur Program are there at various levels. You get more of those people with you and you get recommendations and you break through that barrier of inattention. Even with a poor idea, if you get some good recommenders on it you're going to get through and get in.

MR. McGINTY: *Good luck, Tommy. J.T. in Herndon, you're on the air, go ahead.*

J.T.: *I'm with a firm called the Partnership for a Networked Economy. One of the untapped resources in the DC area is the plethora of industry and trade and professional associations that are here primarily to represent the interests of their members to the government. Given that these groups have a wealth of content available about these companies and their capabilities, what role does the panel see for these groups to facilitate the adoption of business-to-business commerce or collaboration. Thank you.*

MR. MORINO: A key role, and in a couple different ways. At the higher level, the Netpreneur Program is looking at the various audiences we need to reach to inspire more netpreneurship. Associations, we hope will play a key part in that. A lot of it is educational. Our first qualification is to find those groups that are receptive to it. For example, we're working extensively with the real estate industry in associations here, because they are starting to see a change in their business base as a result of the network society.

The second avenue is to realize that in various sectors there is an opportunity for entrepreneurship based on intellectual capital. Again, the Netpreneur Program, is trying to work with associations, for example the American Library Association and other non-profit groups like Highway 1, to help them see that they have very important intellectual capital that is marketable. We have discussions underway today with the Information Industry Association, as an example, to develop an education program that will reach out to the people in this region who are content producers; to show them that the entrepreneurial opportunity exists today, and where this opportunity is going in the next five to ten years, as Bill indicated.

MR. McGINTY: *Let's go to Judy, who's in her car. You're on the air, Judy, go ahead.*

JUDY: *You were talking about how you expect to get more people on the Internet and what will bring them there. I consider myself a relatively computer-literate person. I've used email for ten years. I do a lot of my business financial transactions on the computer. It wasn't until two things happened that I suddenly got on the Internet and sought it out. One was that we got an Internet provider that had a flat fee—that was before AOL had its own flat fee—so we could be on the Internet for an unlimited amount of time and not worry about the additional charges.*

The second thing, though, was that we essentially had a hook to go there, and I think that's what people need. They need to have a hook. They need to go to the Internet because they can't find the information elsewhere or as easily. Last year our son actually died of SIDS. We received a tremendous amount of information from the SIDS Web Page and I received a tremendous amount of information from other SIDS parents who also are on the Internet. I found it absolutely amazing that I could speak to a person in Ireland three times in one day without the cost of trans-Atlantic calls or anything like that. So I think it's two things, I think it's the cost and the unlimited availability, and the hook that will get people on there. Now we are all over the place on the Internet. We love it, basically. And I'll hang up and hear your comments. Thank you.

MR. McGINTY: *Well, thank you, Judy, and I'm very sorry to hear about your son. I will note, however, that there are heads nodding around the table for just about everything that you said.*

MR. MELTON: Yes. Judy, I'd like to comment that as the Internet moves from the head to the heart, we will have made the transition. The Internet started out with the head. Libraries, academic scientists, for lack of a better word, "nerds," but obviously, on a day-to-day basis, as we're using this stuff to connect with family, with friends, with support groups to get information that is important to us on a personal level and strikes us at the heart, that's when the mass adoption will happen. It certainly has happened in your situation, and it's really great, the kind of mutual support that we can give each other over the Net.

MR. McGINTY: *I'm curious about the issue of bandwidth. If there's something else that may be standing in the way of greater adoption of the Net, it's limited by the amount of time it takes to download various pages and so forth. It's great for email but the bandwidth issues remains a problem, and I'm wondering what you guys think about how quickly that's going to be solved.*

MR. MORINO: Well, people have different opinions. I think it's short-term—short-term being a couple of years. Cable modems right now are driving speeds at ten times the speed of ISDN. You see a material difference in the usage, and I think what's around the corner in wireless is just going to blow the roof off the bandwidth issue.

MR. McGINTY: *Really!*

MR. MORINO: Yes.

MR. RAMSEY: Yes, and it's important to understand that these things get their own momentum and they move at speeds that you can never imagine. The question people should ask is not what commerce is happening over the Internet or what percentage of people are online, it's how many people come online and just don't want to go through the aggravation. But that's changing rapidly. A billion dollars used to be a lot of money. Even though now it's just dinner with Bill Gates, you have a lot of capital going in to make this bandwidth issue a non-event. The question which should be asked is, "How many people would be online if it was fast, ubiquitous, dial-tone and they could have access anywhere?"

MR. MORINO: Derek, going back to my background in the computer field, when I started with online networks in the mid-60s, the one thing that you could almost predict like a clock was that whenever you increased the speed of the network you actually increased demand. It's an inviolate rule, and it's still true. That's why we see so much promise going forward as bandwidth gets sorted out. You can assume that not only will it address the current demand and the latent demand, but we will actually create new demand for services.

MR. McGINTY: *Because it will be able to do much more.*

MR. MORINO: Right. Exactly.

MR. KIMSEY: We have empirical evidence of that on America Online. We started the company in 1985 as a Commodore-based service to use with 300 baud modems. Thinking back, it's amazing anybody ever used it. Thank God they did, but now that we're getting up to 28.8 speeds and beyond, as Mario pointed out, the number of people that use it has increased exponentially, and the amount of time they use it has increased. The average hours of usage per subscriber has gone way up—the all-you-can-eat pricing notwithstanding.

MR. McGINTY: *Harry in Falls Church, Virginia, you're on the air. Go ahead, Harry.*

HARRY: *I was at the event the other night. Tough to get up to the microphone and ask a question. It was pretty busy, so I thought I would take this opportunity. My question is about future revenue models for the Internet. As we know, there's a lot of ad-based stuff going on right now. AOL has stated that they want to generate more advertising revenue, and yet they also have a member-based revenue source. Obviously, CyberCash is interested micro-payment and things like that. I'd like each of you to comment on where you think, two to three years out from now, where's the revenue going to come from for businesses such as the one I would like to start.*

MR. McGINTY: *What kind of business are you starting there, Harry?*

HARRY: *It would be a community—a virtual community that would marry together buyers and sellers of corporate computer technology.*

MR. McGINTY: *That's interesting.*

MR. MORINO: Well, just as I did the other night, I make the qualification that there is a fundamental difference between those products that are aimed at a consumer market versus those for business. There's no mystery in the Internet products for business today because you clearly have clients who are willing to pay. They understand value and payment. The only question is to work out the various transaction issues, which is well underway. It will explode, and I think it could be one of the largest markets we've seen.

MR. McGINTY: *In fact, a few companies have completely abandoned the consumer market and just said, "We'll just go with business."*

MR. MORINO: Right. Well, it's a quick move today. Business is a receptive audience where you have more of a known commodity on both sides of the equation. On the consumer side, there are people here who can answer a lot better than I.

To Harry's question on the community ventures issue, I think in the next 18 to 24 months this might very well be one of the largest opportunities to move forward, especially for businesses engaging new communities. Books like Net Gain by John Hagel and Arthur Armstrong have discussed this. Where the revenue comes from in the community of interest model is still nebulous at best, but it's the AOL issue. It's audience aggregation. Once you have audience you can be a buyer or reseller of product, besides being simply an advertising vehicle. It opens up new channel. I think the trick in terms of community of interest is to make sure you're doing audience aggregation; that you have a channel to an audience that you can then use for various revenue sources.

MR. McGINTY: *Bill Melton, what do you think?*

MR. MELTON: Historically—you know, three years is a long history in the Internet—we've talked about two models, one being an advertising model and one being a subscription model. Certainly I think both are alive and well and will continue, though there may be a tilting toward the advertising model on the retail side as the advertising base grows. On the professional or commercial side, I think you're going to continue to play strongly in the subscription-based model.

A third model that we need to be aware of and, Harry, this might be more what you're going after—though I think there may need to be some advertising and subscription in yours as well—and that is what we would refer to as a transaction-based model, or more of a spontaneous interaction where you have many-to-many prior, unknown, non-related entities. Just as you would walk by a newsstand today and spontaneously grab something off the rack, that's a transaction-based model. All three of these models will exist. They are not competitive. They are cross-supplementary, and will exist at the same time.

MR. McGINTY: *Which one is going to be the most important for CyberCash?*

MR. MELTON: We are highly agnostic. Wherever money is spent, there we have an opportunity.

MR. McGINTY: *What do you think, Russell Ramsey? Is it your sense that the business side of this—well, what are you expecting from the consumers' side?*

MR. RAMSEY: Well, the consumer is going to be a major beneficiary in all parts of his or her life. Take, for example, finances. Today, the cost to distribute financial products is anywhere between a tenth and, in some cases, a tenth of one percent of traditional means. The Internet has allowed financial institutions to utilize this distribution channel to go beyond bricks and mortar. The impact is going to be that individuals will be able to conduct their financial life on one page with all their fees in one easy-to-read statement that's updated daily, hourly, in some cases by the minute. To give an example, today it costs the banking industry about $2.00 a transaction on average for individuals going into a branch office. The Internet takes that cost down to probably below 5¢. And . . .

MR. McGINTY: *And the bank will continue to charge you $2.00.*

MR. RAMSEY: Well, in fact, it won't because, like all market forces—remember, there are several banks now that just operate in cyberspace—the market will force these products to be bought at lower prices and the consumer will benefit.

MR. McGINTY: *Well, we'd like to think that. I note that even as the ATMs have become more ubiquitous, we're now paying up to $1.50 per transaction to use an ATM machine. It doesn't seem like the competition's forcing that price down too much.*

MR. KIMSEY: Senator D'Amato probably will, though.

MR. MELTON: Well, I think we're mixing a couple of issues here. What you're paying for when you pay a buck apiece for the ATM is the convenience—the ability to do it any time, any place. There you're talking about geographical convenience. Now, with the Internet remember what's happening. You're having the evaporation of geography. So you have all the banks, the entire 9,000 banks or 10,000 banks in the United States potentially sitting on your desktop. That becomes a slightly different environment when your closest ATM is a mouse click away.

MR. McGINTY: *Ah, so in other words, if I'm at an ATM machine I might not be able to get to another one that doesn't charge me, so there's not much competition at that particular moment . . .*

MR. MELTON: Or you might be too lazy to walk to one.

MR. McGINTY: *Right, exactly, but if I'm online and someone wants to charge me, then there's any number of others I can go to.*

MR. KIMSEY: There's nothing so efficient as the free market.

MR. MORINO: The enormous potential we face today is that the Internet is hitting so many market inefficiencies. When you have a market inefficiency, markets tend to move and close them.

MR. McGINTY: *I'm curious about the labor situation. I've been reading that a lot of companies in this region are, in a word, cannibalizing each other, fighting for programmers and other high-skilled people who can do the work that we're talking about. How's the situation there?*

MR. KIMSEY: Well, this has been a much lamented problem in the Washington area because we don't have the same large population of high-tech labor that they do, say, in Silicon Valley. I think the Potomac KnowledgeWay Project has initiatives going on in this direction, but I think both industry and the educational community understand this and will work together to try and open the spigot further and make sure that the community here expands to meet the demand.

MR. McGINTY: *Mr. Morino, is it your sense there's a labor shortage?*

MR. MORINO: Oh, there's a labor shortage, but realize that same labor shortage exists in Silicon Valley, it exists in Boston, it exists in Austin, Texas, today. There's nothing unique about the shortage itself. What's unique here is maybe the sheer volume in the demand that has been created. The very thing we're talking about in terms of the robustness of the economy is also driving that demand, which, in one sense, is a great opportunity. The hard part is dealing with it, but I think you'll see changes in a few ways. One is a lot of focus coming on educational institutions, and the Potomac KnowledgeWay Project is involved with many of them. But also, I think the greatest opportunity is that we have, to date, been somewhat unknown—a great secret to the rest of the country. I think a lot of kids are waking up to the fact that this is a pretty interesting place to move to.

MR. McGINTY: *Let's go to Mary in Washington, DC. You're on the air.*

MARY: *Hi, thanks. I tuned in late so I hope my comments are relevant, but I'd like to put a little bit of wet blanket on this. I've been using AOL Internet and I find that the number of ads coming in through the Internet are just increasing dramatically and I find it very annoying. I just want to deal with things that I want to deal with. I want to be able to pick and choose who I communicate with, and I have to delete ten emails every day of junk mail.*

MR. McGINTY: *That is starting to get a little annoying.*

MARY: *And also, it seemed like about six months ago they sent out a message saying that we could sign up for something to have the mass mailings screened out and I signed up for it. It's done nothing but increase. I have one other comment after that.*

MR. McGINTY: *All right. Well, hold on for a second and let James Kimsey speak to some of that.*

MR. KIMSEY: It's like building a wall at Alcatraz. No matter how high you build it, somebody will figure out a way to get over it. We at AOL are very concerned about "spamming," as we call it, the amount of folks that are sending out junk email. We've talked to legislators and government officials about the fine line you must tread between the freedom of speech and expression and the intrusion of those spammers on everybody's account at AOL. It bothers us for a number of reasons. It bothers our subscribers and it puts an additional load on our system.

The question about whether they have the right to do that or not is one that has not yet fully been answered. We've created a number of technology tools to try and block these spammers from loading up your email account with junk. Unfortunately for us, these spammers are also very technically adroit and our blockage techniques have been successful only momentarily until they figure out a way around them. We will continue our efforts to block them and we hope that over a period of time that we can reach some accommodation with regulators and so forth that will put at least a damper on that kind of activity.

With respect to ads that we generate, we're still trying to find the best way that our subscribers will understand that we've given them a fixed price, all-you-can-eat, and that's going to be subsidized with advertising and transaction revenue. In fact, we expect that over time that'll be the majority of our revenue. But we are looking for ways to make that an enjoyable part of the experience, as well.

MARY: *Well, the thing that we would want, I would think, would be the ability to tune into that or not tune into it.*

MR. McGINTY: *Well, see, that's the problem, of course. No one would choose to tune in to a bunch of ads if they didn't want to. If someone said, "You can watch television without ads or with ads," all of us would say we'd rather have without, but we like the idea that we don't pay anything for television.*

MARY: *Yeah, when you're watching television, you can get up and go get something to eat, so you don't actually have to watch the ad. In the newspaper, you turn the page and you don't have to read the ads.*

MR. MELTON: A simple question. If AOL were to provide a, say, a $40.00 a month service, all-you-can-eat with guaranteed no ads, would you subscribe to that as opposed to the $20.00 service?

MARY: *Well, that takes me to my next point. I was trying to get off of AOL and on to IBM because I heard it was much more efficient and also because it had a lot of sites overseas and I work overseas a lot. Apparently I was supposed to be able to download signing on through the Internet and I think AOL has blocked it. And even when I called an AOL technician to talk to them about it, they sort of inadvertently, quote, unquote, hung up on me.*

MR. McGINTY: *So now, you're saying that AOL has blocked you from downloading the software that would allow you to sign on to another online service?*

MARY: *Right.*

> **MR. KIMSEY:** No.

MR. McGINTY: *Any chance of that, Mr. Kimsey?*

> **MR. KIMSEY:** No. We wouldn't, nor should we. We wouldn't and we couldn't do such a thing.

MARY: *Well, then how am I not able to do this?*

MR. McGINTY: *Well, I don't think anybody here can answer that question. All right, Mary, thank you very much for calling. I appreciate that. This question about the advertising and the idea that you brought up, Bill Melton, about paying more not to have it, is that something that would actually be possible in the future?*

> **MR. MELTON:** Technically, I see no particular reason why it wouldn't be possible. I think, though, when consumers are really faced with that choice, I suspect that they will find the ads much less offensive than they claim them to be. I imagine there are some test markets that can be done and probably will be done to test that hypothesis.

> **MR. KIMSEY:** Actually, there's been a lot of research that shows that there's a lot of people who watch Home Shopping Network, that watch the infomercials on television. The public is not totally abhorrent to ads, they just don't like the ones they're not interested in. But to the extent that you want to buy a car, all of a sudden car ads have a special relevance. I think the beauty of this medium is it's going to have the capacity to funnel ads in which you might be interested. That's going to be the challenge that we and everybody in this medium faces. It has the capability now to be much more addressable and much more pointed and significant to the receiver. Hopefully, over time, it will make it a plus to the experience of being online.

> **MR. RAMSEY:** But that's the power of the Internet—it puts the consumer in control. If you don't like the ads, you hit the delete button. If you don't want to go at a certain time, you don't show up. If you don't like the site you're on, you go somewhere else by pointing your mouse. That is truly important in this communication revolution, by far the most powerful communication medium. It allows the consumer to totally control their destiny. If you want to be a couch potato, you can. But if you want to be interactive and proactive, it's in your control.

MR. McGINTY: *I'm curious. And all of you might want to address this question. Because of the speed with which things change on the Internet, it seems to me this has also affected the business cycle. You see companies come, grow really big really quick, and then shrink back down to maybe nothing and disappear; or maybe they sell and the owners go away rich or whatever. It happens very quickly. We saw it happen, for example, with Netscape, they're still around but they saw their price get really high, now it's back down a great deal. How has that changed the way netpreneurs operate compared to other business people?*

> **MR. MORINO:** That's not new. If I took you to the software industry, the exact same model occurred, you just didn't see it in the retail sense. It was never known to the consumer. I don't think it's new at all. There was a good article in the Washington Post this morning about two telecommunications firms that just merged into a $600 million company. The founders of one of the firms walked away with a big chunk of money. I think you'll see all three of those guys probably do something in the region again. We had the greatest comment from the Barons Evening. It came from a young fellow who started a company called Torso which was just acquired. His comment was, "You know, I went through a lot to get the company where it was. I thought I'd never do it again. What happened tonight, you guys really invigorated me. I'm going to do it again."

> **MR. MELTON:** I think one slight difference is that most of the rapid growth—getting merged, getting retransmitted into the system—heretofore has happened largely in the back alleys of the financial world; among venture capitalists and other supposedly "qualified" investors. Last year it started to happen where it hit the Street. That is, Wall Street took over the role in many cases of venture capitalist. You had these young companies going public in the full spotlight of Wall Street with the retail markets looking on. That's a bit new, and so it's a bit daunting to do some of the things that would normally happen in the nursery, protected by the mothers of the venture capital world, is now out in full public view.

MR. RAMSEY: Yes, but make note—don't mistake the difference between the power of communication and the impact that has on people and all the potential benefits and control that it gives, with the impact it has on business. The Internet blows apart much of the traditional business analysis, and it blows apart, in many cases, how businesses go about things today.

MR. McGINTY: What do you mean?

MR. RAMSEY: Anything that you distribute or sell today that can be distributed over the Internet puts the whole business in a different light. Whether it's World Book Encyclopedia, which has been made functionally obsolete, or other major corporate entities, they are threatened by the power of the Internet and by entrepreneurial start-up companies which can come up with a better way. It's accelerating the business cycle and, in many respects, it's what's keeping a lid on inflation.

MR. McGINTY: *So you think it's accelerating the business cycle out and beyond just the companies that have direct tie to the Internet. You think it's made the business cycle different everywhere.*

MR. RAMSEY: All businesses are impacted by the Internet, whether they know it or not.

MR. KIMSEY: And, in fact, these technologies are expanding and progressing at ever increasing rates, which accelerates the business cycle. So you've got the same sort of Darwinian imperative that applies, but it's just going to happen much more rapidly as these technologies advance. Then something that might have taken ten years to be obsolete maybe takes five or two, or, in some cases, a matter of months. Some company gets started with a great technology that seems relevant to everyone; starts to get itself established; and then here come some guys out of a garage that all of a sudden make their technology obsolete. They crater and the new guys pick up the prize.

MR. McGINTY: *Is it your sense that we really can have any idea of what this is going to turn into? And I say that because predictions have been notoriously off-target when it comes to this kind of technology.*

MR. MELTON: I think we're dealing with such a level of complexity that it is not possible to sequentially predict a simple cause and effect. Any second order growth curve starts over on the right hand side of the chart and turns upward into this fancy word that they call an "asymptote." That means it's going straight up, the rate of change is instantaneous—complete change, infinite change in a infinitely short period of time. That's just about the kind of growth curve we're talking about. Well, obviously, when you have that kind of rate of change, you end up with a change of state, and that change of state is not predictable by us mere humans.

MR. McGINTY: *On that note, I think that'll do it for us today. William Melton is the founder and CEO of CyberCash; Mario Morino is the current chair of the Potomac Knowledge Way Project; W. Russell Ramsey is founder and president of Friedman, Billings, Ramsey & Company; and James Kimsey is founder and former chair of America Online. They are the Barons of the Beltway. I want to thank the four of you for joining me here today. It's been a great conversation. We appreciate it.*