NOW WHAT?
WALL STREET

HOW DID WE GET HERE?

ERIC UPIN
MULTIPLE PROBLEMS

HOUSING LED RECESSION

OVER LEVERAGED FINANCIALS

FALLING ASSET PRICES

FROZEN CREDIT MARKETS

WEAK HOUSEHOLD BALANCE SHEET

GLOBALLY SYNCHRONIZED SLOWING EXACERBATING ALL OF ABOVE

FORCES OF INFLATION VERSUS FORCES OF DEFLATION
MARKET CYCLES ARE LONG

Source: Bureau of Labor Statistics, Dow Jones
DRIVEN BY PRODUCTIVITY AND CENTRAL BANK

Source: Federal Reserve, International Labour Organization
RESULTING IN FALLING INFLATION AND COST OF DEBT

U.S. inflation (annual year/year CPI change)

Yield on 10-year U.S. treasuries

Source: Bureau of Labor Statistics, Federal Reserve
FUELING A NATION OF CONSUMERS

U.S. current account / GDP


Source: Bureau of economic analysis
U.S. BUYS FOREIGN GOODS
FOREIGN COUNTRIES USE PROCEEDS TO BUY TREASURIES
DEMAND KEEPS LONGER-TERM RATES LOW
FOREIGN $s RECYCLED INTO TREASURIES
AS A RESULT, DEBT BALLOONED

Source: Bridgewater
DEPENDENT ON THE KINDNESS OF STRANGERS

Source: Bridgewater
LIQUIDITY AND EASING SPREAD TO HOUSING

Single family housing starts

Distribution of U.S. dollar mortgage originations

Source: Bridgewater, National Association of Home Builders
HOME PRICES GREW SUBSTANTIALLY ABOVE MEAN

U.S. real home price index

1900-1929
-1.2% annualized

1930 - 1997
0.7% annualized

1998-2006
8.0% annualized

Source: Robert Shiller
STRUCTURED PRODUCTS AND REGULATORY CHANGES COMPOUND THESE ISSUES

GROWTH IN SECURITIZATIONS

LEVERAGE ON THOSE STRUCTURES

INCREASED LEVERAGE ON BANK’S BALANCE SHEETS

OFTEN MIS-RATED BY AGENCIES

REPEAL OF GLASS-STEAGALL

REGULATORY CHANGES ENCOURAGING HOME OWNERSHIP
HUGE GROWTH IN DERIVATIVES

Outstanding amount of open positions in OTC derivatives markets

Note: Outstanding amount is not a pure measure of risk as some positions are netted and have collateral; U.S. GDP was $13.8T in 2007
Source: Bank for International Settlements
SIGNIFICANT EXCESS CAPACITY

World Fixed Investment (%GDP)

Source: Bridgewater
VERY TIGHT CREDIT

High yield spreads (basis points)

Investment grade spreads (basis points)

Source: Merrill Lynch
JAPAN MAY BE INSTRUCTIVE

Nikkei Index 1988 - present

Japanese discount rate

Annual real GDP growth

Source: Bank of Japan, Yahoo Finance
KEY THEMES

GLOBAL

SECULAR

NOT “NORMAL CRISIS”, WILL TAKE TIME

CREDIT NOT EQUITY DRIVEN

SIGNIFICANT RISK TO GDP GROWTH

POTENTIAL FOR GREATER REGULATORY REFORMS / SCRUTINY
OUR TAKE

MANAGE WHAT YOU CAN CONTROL
  SPENDING
  GROWTH ASSUMPTIONS
  EARNINGS ASSUMPTIONS

FOCUS ON QUALITY

LOWER RISK

REDUCE DEBT
MAIN STREET

WHERE ARE WE NOW?

MICHAEL BECKWITH
## THE U.S.: A NATION OF CONSUMERS

### THE CHANGING FACE OF THE ECONOMY

<table>
<thead>
<tr>
<th>$ TRILLIONS</th>
<th>1987</th>
<th>1997</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>TOTAL U.S. GDP</td>
<td>4.7</td>
<td>8.3</td>
<td>13.8</td>
</tr>
<tr>
<td>CONSUMER SPENDING</td>
<td>3.1</td>
<td>5.8</td>
<td>10.1</td>
</tr>
<tr>
<td>CONSUMER AS % OF TOTAL GDP</td>
<td>66%</td>
<td>70%</td>
<td>73%</td>
</tr>
<tr>
<td>DISPOSABLE PERSONAL INCOME</td>
<td>3.5</td>
<td>6.0</td>
<td>10.2</td>
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</tbody>
</table>

*Source: Bureau of Economic Analysis.*
EXPLOSION IN HOME OWNERSHIP

WAGE GROWTH & PERSONAL SAVINGS

PERSONAL SAVINGS RATE EVAPORATED

REAL WAGE GROWTH FELL

CONSUMERS BUCKLING UNDER DEBT

**HOUSEHOLD DEBT SERVICE RATIO**

**HOUSEHOLD FINANCIAL OBLIGATION RATIO**

DSR = DEBT PAYMENTS ON OUTSTANDING MORTGAGES AND CONSUMER DEBT/DISPOSABLE PERSONAL INCOME

FOR = ADDS AUTOMOBILE LEASE PAYMENTS, RENTAL PAYMENTS, H/O’S INSURANCE AND PROPERTY TAX PAYMENTS TO THE DSR

Source: Bureau of Economic Analysis.
MEWs BECAME THE NEW PIGGY BANK

MEW CONTINUES TO FADE…

Mortgage equity withdrawal, as a % of disposable income, 4-quarter moving average

Source: Haver, BEA, NAHB, Conference Board, EIA, Morgan Stanley Research.
FROM VIRTUOUS TO VISCIOUS CYCLE

MORTGAGE RESET
DELINQUENCIES/FORECLOSURES
PRICES FALL
MEWS DECREASE
CONSUMER SPEND FALLS
JOB MARKET ERODES
RECESSION

UNEMPLOYMENT SPIKES HIGHER

ON THE BRINK OF A RECESSION

CONSUMER CONFIDENCE AT MULTI-DECADE LOWS
Conference Board Consumer Confidence Index

ISM IS FALLING FAST
ISM Manufacturing & Non-Manufacturing Index

GDP IS POISED TO TURN NEGATIVE
Real GDP and GDP growth (YoY SA)

EARNINGS BEGINNING TO ROLL

EARNINGS DOWN 18% ON ESTIMATES MADE 12 MONTHS AGO

S&P 500 Rolling Earnings Surprise %
12mo Forward Estimates vs. Actuals

Grey shading represents US

V-SHAPED RECOVERY UNLIKELY

Current S&P 500 Consensus Actual and Expected Operating Earnings Growth (Weighted-Avg. % / Y/Y)

<table>
<thead>
<tr>
<th></th>
<th>CY00</th>
<th>CY01</th>
<th>CY02</th>
<th>CY03</th>
<th>CY04</th>
<th>CY05</th>
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<th>CY07</th>
<th>CY08E</th>
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<tr>
<td>Financials</td>
<td>5%</td>
<td>-10%</td>
<td>18%</td>
<td>25%</td>
<td>11%</td>
<td>5%</td>
<td>23%</td>
<td>-37%</td>
<td>-46%</td>
<td>109%</td>
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<tr>
<td>Consumer Discretionary</td>
<td>0%</td>
<td>-24%</td>
<td>33%</td>
<td>11%</td>
<td>28%</td>
<td>2%</td>
<td>9%</td>
<td>-10%</td>
<td>-16%</td>
<td>41%</td>
</tr>
<tr>
<td>Media</td>
<td>-1%</td>
<td>-6%</td>
<td>34%</td>
<td>12%</td>
<td>33%</td>
<td>28%</td>
<td>27%</td>
<td>15%</td>
<td>11%</td>
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<tr>
<td>Information Technology</td>
<td>28%</td>
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<td>0%</td>
<td>46%</td>
<td>43%</td>
<td>20%</td>
<td>12%</td>
<td>21%</td>
<td>10%</td>
<td>17%</td>
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<tr>
<td>Telecom Services</td>
<td>6%</td>
<td>-24%</td>
<td>-8%</td>
<td>0%</td>
<td>-8%</td>
<td>14%</td>
<td>17%</td>
<td>5%</td>
<td>-1%</td>
<td>10%</td>
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<tr>
<td>S&amp;P 500</td>
<td>17%</td>
<td>-17%</td>
<td>5%</td>
<td>18%</td>
<td>20%</td>
<td>15%</td>
<td>16%</td>
<td>-4%</td>
<td>1%</td>
<td>23%</td>
</tr>
</tbody>
</table>
ADVERTISING MARKETS ARE CRACKING

Source: TNS U.S. Advertising Expenditure Estimates
RETAIL/ECOMMERCE DETERIORATING

Source: US Census Bureau.
MOBILE IS NOT IMMUNE

Source: TNS U.S. Advertising Expenditure Estimates
TECH SPENDING DEPENDS ON ECONOMY


Drop in earnings in Dec 07 was partly due to financial services industry write offs.

Source: Bernstein Strategy Group; First Call
“IT spending is being more scrutinized now than at any point in the 2003 through 2007 timeframe … customers are showing more caution.”
- EMC, JUL 2008

“It’s now clear that this economic softness is continuing into September.”
- INGRAM MICRO, SEP 2008

“Market developments of the past several weeks have been dramatic and worrying to many businesses. These concerns triggered a very sudden and unexpected drop in business activity.”
- SAP, OCT 2008

AMAZON.COM & BUY.COM

Amazon.com Financial Performance '99-'05

- Strong business model
- Focus on core value proposition

Buy.com Financial Performance '99-'05

- Profitable growth
- Trim fat during lean times
• Tailor sales message to environment
• Take advantage of competitors’ weakness

• Understand your true customers
• Value of quick ROI and low cost
YOUR STREET

WHERE DO WE GO FROM HERE?

DOUG LEONE
UPS AND DOWNS ALWAYS OCCUR
IT IS DIFFERENT THIS TIME
RECOVERY WILL BE LONG
VENTURE FIRMS BRACE FOR CASH CRUNCH
Big investors turn away from VCs as the financial crisis takes its toll.
By Michael V. Copeland

“If you are a venture capitalist looking for a new limited partner, don't stop in here. Don't try and sell me on a new fund, and good luck trying with everyone else.”

“If you’re a second or third-tier venture firm trying to raise another fund, forget about it.”

“It will start first in private equity funds where there will be a substantial miss on capital calls. Then we'll see it next in venture capital.”

"If you are start-up that is not cash-flow positive you are in a tough spot right now. If you haven't figured out your business model yet you are in trouble.”

“It's going to be hard to get another round. You aren't going to get a second life this time."
NEW REALITIES

$15M RAISE @ $100M POST IS GONE
SERIES B/C WILL BE SMALLER RAISES
CUSTOMER UPTAKE WILL BE SLOWER
CUTS ARE A MUST
NEED TO BECOME CASH FLOW POSITIVE
INCREASED CHALLENGES

M&As WILL DECREASE
PRICES WILL DECREASE
ACQUIRING ENTITIES WILL FAVOR PROFITABLE COMPANIES
IPOs WILL CONTINUE TO DECREASE AND WILL TAKE LONGER
SURVIVAL

- Preserve Capital
- Cash is King
- Understanding of Market Uptake
- Customers’ Abilities to Pay
- Assessment vs. Competitors
- Need for Profitability
- Must-Have Product
- Established Revenue Model
OPS REVIEW

- ENGINEERING
  DECREASE HEADCOUNT FOR NEXT VERSION?
- PRODUCT
  WHAT FEATURES ARE ABSOLUTELY ESSENTIAL?
- MARKETING
  MEASURING & CUTTING WHAT’S NOT WORKING?
- SALES & BUS DEV
  GETTING RETURN ON EXPENSE INCREASE?
- PIPELINE
  REAL PROBABILITIES OF CLOSING DEALS?
- FINANCE
  WHERE CAN PAYMENTS BE DEFERRED?
  WHAT DEPARTMENTS ARE ESSENTIAL?
DEATH SPIRAL
SURVIVAL OF THE QUICKEST

DEATH SPIRAL

EXPENSES

TIME

10/08

COMPANY A

COMPANY B
NO ONE MOVES FAST ENOUGH

<table>
<thead>
<tr>
<th>OP EX % Y/Y</th>
<th>CY01</th>
<th>CY02</th>
<th>CY03</th>
<th>CY04</th>
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<tbody>
<tr>
<td>CSCO</td>
<td>-3%</td>
<td>-10%</td>
<td>-1%</td>
<td>9%</td>
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<td>EMC</td>
<td>9%</td>
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<td>-4%</td>
<td>31%</td>
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<td>ADBE</td>
<td>-2%</td>
<td>-1%</td>
<td>12%</td>
<td>18%</td>
</tr>
<tr>
<td>YHOO</td>
<td>-3%</td>
<td>14%</td>
<td>33%</td>
<td>57%</td>
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<tr>
<td>AMZN</td>
<td>-15%</td>
<td>-4%</td>
<td>10%</td>
<td>24%</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td><strong>-3%</strong></td>
<td><strong>-5%</strong></td>
<td><strong>10%</strong></td>
<td><strong>28%</strong></td>
</tr>
</tbody>
</table>
WHAT DECISIONS DO YOU PLAN TO MAKE?  VS.  WHAT DECISIONS DO YOU WISH YOU HAD MADE?
Douglas Leone

Sent: Monday, October 6, 2008 7:37 PM
To: Douglas Leone; Michael Moritz
Subject: mkt conditions...

Is this awful or what?

What is Sequoia’s take?

My attitude is batten down the hatches ... it is going to be a rough ride...

Any co without at least a yr of cash minimum in the bank is in trouble...in my opinion

Thoughts??

Here is what I sent to all my cos in april of 2000 and am dusting it off to resend again now!!

To: Portfolio CEOs
Date: 04/17/2000 05:24 PM
RE: Market Conditions Effect on Portfolio Companies

The down draft in the stock market sends us some obvious “signals” and we can’t help but mention them.

1. If you are in a funding cycle, you should raise your funding as soon as possible and raise as much as possible.

2. You must aggressively examine and pursue M&A opportunities (unless you have over 12 months of cash reserves!) to insure you have critical mass (including funding, customers, roldodex power, market share, cash, synergy, etc.).

3. Be realistic on valuations -- they will fall so be ready and willing to co-operate.

4. While it’s safe to say entrepreneurs have had negotiating leverage with the “down draft” in the market, the VC community will start exercising their leverage.
THE SOLUTION

PERFORM SITUATION ANALYSIS

ADAPT QUICKLY

USE A ZERO-BASED BUDGETING APPROACH

MAKE CUTS

REVIEW SALARIES

EMPLOY A HEAVILY COMMISSIONED SALES STRUCTURE

BOLSTER BALANCE SHEETS

BECOME CASH FLOW POSITIVE AS SOON AS POSSIBLE

SPEND EVERY DOLLAR AS IF IT WERE YOUR LAST
GET REAL    OR    GO HOME