Masters of Scale Episode Transcript: Peter Thiel

> **DARYL WOODSON**: Speed is not manufactured by how fast the feet move, but how much force per step.

REID HOFFMAN: That's Darryl Woodson, a personal coach to some of the fastest runners in the world. He trains Olympic athletes who have broken one world record, three national records and claimed 10 national titles. Darryl doesn't have a single training regimen for these Olympic medalists; each runner has unique strengths. Some runners, for example, seem to explode off the blocks. When Darryl sees that explosive quality, he lights a match under them.

> **WOODSON**: It starts in your head. The brain controls 100% of your muscle capacity. Sometimes a runner's brain functions a lot quicker than other people. It's more natural for them to just be explosive.

HOFFMAN: Now if any runner embodies this explosive quality, it's Natasha Hastings. She's a two-time Olympic gold medalist. They call her the "400-meter diva." And when it comes to starting off the blocks, she's a powder keg.

> **NATASHA HASTINGS**: My start is pretty explosive. I've even been asked, "Well, why do you start so fast?"

HOFFMAN: Natasha and Darryl spend a lot of time thinking about that first stride.

> **WOODSON**: The most important aspect of acceleration are the first two steps. That's what's going to manufacture the greatest power output.

> **HASTINGS**: One of the things that I always think about is those first few seconds, there's an energy system that you're never going to get back. So why waste it?

HOFFMAN: Now that's the plan that gets Natasha ahead of the competition. It takes natural talent, and training—yes. But also a very specific mindset. And I would argue a similar plan applies to Silicon Valley's fast-growing companies. They're built for explosive starts.

Peter Thiel—the founding CEO of PayPal and one of the Valley's sharpest investors—won't back a company if they don't have this kind of potential. He has to believe they can not only get *ahead* of the competition, but *break free* of it entirely.

> **PETER THIEL**: I do think that for a really valuable business, you have to at some point try to achieve escape from the competition. And so if you could scale incredibly fast, on the one hand, you have to race really hard to scale fast—but the benefit is that you're achieving escape velocity from the black hole that is hyper-competition.

HOFFMAN: I rarely agree with Peter. But in startups, we find common ground. I believe that if you want your company to scale, it's not enough to *beat* the competition. You have to break free of the competition altogether.

[Theme Music]

This is Masters of Scale. I'm Reid Hoffman, co-founder of LinkedIn, investing partner at Greylock, and your host. I believe if you want your company to scale, your goal is not to *beat* the competition. Your goal is to break free of the competition entirely.

In an ideal world, you do this by going where the competition *isn't*. You invent your own game and master it. But to be clear, this is more of an aspiration than a feasible goal. At best, you'll get a grace period—a fleeting moment when no one believes in your idea. And as soon as your idea takes off, watch your back. Before long, you'll find yourself where most businesses start: facing competition. Your goal? To break free.

That's what happened to PayPal—and I want to share that story with you, because it's easy to say, "I'll break free of the competition." It's quite another thing to be in the heat of the race, unaware of where your competition stands, or whether you're truly breaking ahead.

I wanted to talk to Peter Thiel about this, not only because he guided PayPal through those precarious early days, and went on to invest in company after company that embodied this idea. But also because he has some of the strongest opinions on competition—and, well, on almost anything—of anyone I know.

I first met Peter at Stanford, and right from the start, we clashed on a lot of issues.

> **THIEL**: It's always the joke we have Reid. Where you're the socialist and I'm the capitalist.

HOFFMAN: We were fierce young men back then. I'm pretty sure he saw me as a bleeding heart pinko commie. And I'm absolutely certain I saw him as a libertarian wacko who seemed to have sprung out of Ayn Rand's book, *The Fountainhead*, fully formed.

Our first dorm room debate pretty much consisted of us saying to each other, "You can't possibly believe that." And that feisty exchange continued throughout college through the founding of PayPal—and yes, as some of you might know, through the 2016 presidential campaign.

I've known Peter for three decades, and I *still* can't predict where he'll land on many issues. Who would've imagined that my former PayPal colleague would back Donald Trump? Not me. And yet there he was, at the Republican National Convention. Go figure.

I met Peter in August, and we sidestepped our political differences. If you really want to hear us duke it out, tweet us at Masters of Scale. We just might be able to arrange a follow-up interview. Peter, consider yourself on notice.

On today's show, we're going to shelve our political disagreements and consider one rare point of consensus—that the whole point of scaling fast is to *escape* your competition.

But Peter didn't always try to avoid competition. For most of his life, he *thrived* on competition—as he himself will tell you.

> **THIEL**: I was incredibly competitive in elementary school, junior high school. I remember in eighth grade, one of my friends wrote in my eighth grade yearbook, "I know you're going to get into Stanford four years from now. Four years later, I went to Stanford, and then I got into Stanford Law School, and I ended up at a top law firm in Manhattan. And it was sort of winning one competition after another.

HOFFMAN: So Peter has always had this competitive streak. But another thing you should know about Peter is he also has a *very* serious contrarian streak—and those two qualities don't sit comfortably together. On the one hand, he wants to race against his peers. On the other hand, he wants to stand apart from them entirely. For most of his childhood, he let his competitive nature get the best of him.

He was a champion chess player. He trounced his peers in class rankings and LSAT scores. At last, he had reached his competitive nirvana: law school. And then?

> **THIEL**: Maybe I was attracted to law school because it was very precisely rank-ordered. It was a thing you could go to next after undergraduate. And the paradoxical thing that, when you compete very intensely, you do get to be very good at the thing you're competing on. But then, you often don't ask enough critical questions about whether the thing you are competing on is really worth doing.

HOFFMAN: Good question. Peter didn't have an answer, so he just kept competing. He clawed his way to the top of the class. Then he landed a job at a prestigious law firm.

All the while, that question—"Is this worth it?"—still gnawed at him. And as his career reached new heights, he had a sinking feeling: he wasn't winning. In fact, he felt trapped.

> **THIEL**: It was this very strange place, the law firms. From the outside it was a place where everybody wanted to get in, on the inside it was a place where everybody wanted to get out. When I left after seven months and three days, one of the people down the hall from me said that he had no idea anyone could leave this quickly, and that it was possible to escape from Alcatraz.

HOFFMAN: All that work—all that *winning*—had landed Peter in a prison of his own making. And like any inmate, he began to question his life choices. Then it dawned on him, the root of his problem was an obsession with winning. Who cares how anyone measures up to their peers? Competition, he decided, is for *losers*.

I'm not overstating his argument. He really says that.

Google the phrase "competition is for losers," and the top results all point back to Peter Thiel. There's his Wall Street Journal op-ed, headlined: "Competition is for losers." He said it to me too.

> **THIEL**: By the time I was at Sullivan and Cromwell, five years before we started PayPal, I came to question conventional competition. I thought that a lot of the conventional ways people competed resulted in too many people doing conventional things, and then you end up in very competitive dynamics—and then even when you win, it's not quite worth it. So you might get a slightly better-paying job than you otherwise would, but you sort of have to sell your soul. And so that doesn't seem like a very good economic or moral tradeoff—and the kinds of things like that, that happen with conventional competition.
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> By the time we started PayPal, I was focused on, "How do we compete very intensely—maybe to avoid competition altogether?"

HOFFMAN: I often disagree with Peter, but I have to say, on this point, he's spot on. Competition will make you, at best, a winner in a losing game. If you really want to scale a business, *escape* the competition. Change the playing field. Hang up your jersey. This applies to businesses as well as individuals. Don't try to beat the competitors at their own game. You have to invent a new game—and master it.

And that's precisely what drew Peter to the idea of online payments. It was 1998. Everyone wanted to sell stuff online, but no one had an easy way to pay for that stuff. Peter saw an opportunity to essentially *invent* the Internet's cash registers.

> **THIEL**: By the time we started PayPal when I was 31, I was focused on doing something entrepreneurial, doing something that strictly speaking, other people were not doing. There's this question about financial cryptography. Could you start a new currency? Could you start some new secure financial product? And so that was sort of the intellectual set of ideas that we were very interested in exploring. And then we were also very focused on getting to scale as quickly as possible. How do you get it to grow by word of mouth? Reid, you and I had many late-night conversations about virality and exponential marketing.

HOFFMAN: After talking with Peter, I realized that his *memory* of PayPal's early, experimental days was of a solitary, heroic struggle to make online payments a reality. But the fact is, we weren't alone for long.

EBay had emerged as the leading online marketplace for selling, well, everything. Their power sellers flocked to PayPal; they caught us by surprise. Who were these users? Not at all the ones we imagined.

> **THIEL**: The way I remember it was the initial reaction was quite negative. It's like, "Wow, this is the junkiest stuff being sold on the Internet, and it's so bad for our brand to be affiliated with all of this."

HOFFMAN: Entrepreneurs, take note! Your first users are often not at *all* what you imagined. They're often less glamorous, and fewer in number. Don't be too quick to judge them. They may prove more valuable than they initially seem. And Peter changed his tune on the eBay sellers very quickly.

> **THIEL**: In retrospect, it turned out to be this incredibly tight community, a new use case where the alternatives were much worse. The alternatives were typically using a check which would take seven days to clear. And because people were both buyers and sellers on eBay, it had a natural sort of fluidity to the whole thing—where the money went from one PayPal user to another, and stayed inside the system. It turned out to be quite powerful. I'd say within three to four months of it being used on eBay, something like 30% percent of the eBay power sellers were using PayPal.

HOFFMAN: EBay executives were miffed to see us ambushing their checkout counter. Granted, we made their users happy and accelerated the sales cycle on the site. But, who were we to siphon off eBay's business? So began a very strange dance between frenemies.

It kind of reminds me of those unusual animal pairings that you see on a nature show. It's an old story—I can almost hear David Attenborough narrating the scene.

> **"ATTENBOROUGH" VOICE**: The remora eel fastens onto the whale shark by means of a disc-shaped organ on the top of its head. Once secured to its host, the eel may hitch a ride across the vastness of the Pacific Ocean.

HOFFMAN: Incidentally, scientists are still debating whether the remora eel has a parasitic, harmless or beneficial relationship with its host. That pretty much sums up PayPal's relationship with eBay in the early days. In the long run, though, Peter saw trouble.

> **THIEL**: That was a deeply uncomfortable place to be, though. So I mean it worked but it was uncomfortable because we were the cash registers, and you had a different

company that ran the store and they were trying to figure out how to get their cash register machines to work. And if they ever figured it out we'd be in real trouble.

HOFFMAN: We knew we were in trouble when eBay bought a rival online payment service called Billpoint, and directly integrated it into eBay. So much for Peter’s grand escape from competition. Things were getting heated. But when I remind Peter of this massive threat, to my surprise, he shrugs it off.

THIEL: We were certainly not alarmed about eBay initially, because they had not yet launched the Billpoint product—it got launched after we got started. They bought the company, but they hadn't done much with it yet.

HOFFMAN: I remember it a bit differently. EBay scared the dickens out of us—and yes, even Peter—because I distinctly recall him asking me to sell the company to anyone who would buy it for $600 million dollars.

HOFFMAN: I remember our conversations. You were actually at that time fairly concerned about, people think we have this really valuable thing, but we haven't established it yet. It's a house of cards right now. This whole thing could blow over. There was a six-to-12 month period where you had me essentially seeing if anyone would buy the company.

THIEL: Right.

HOFFMAN: And so it's like, “Will anyone buy this?”

THIEL: Right.

HOFFMAN: “OK, go look for buyers.” There's a funny untold story around if VeriSign had upped their bid by $50 million dollars, they may have actually owned PayPal, right?

THIEL: Yes. It's hard to say what would have happened, but certainly there was a lot of uncertainty around all these things. The name was a good name. It was a friendly name. You know, how could you go after poor little PayPal? It was just this friendly little company that was helping customers.

The remarkable thing, in retrospect, was how robust it turned out to be. Maybe the kind of countervailing advice I would try to give would be that you should try to always do something where there's an intense use-case, where the customers really like what you're doing—and that will protect you up to a certain point.

HOFFMAN: Peter makes a fascinating point here. On the one hand, he says avoid competition. On the other hand, he seems to concede that competition is tolerable, so long as your customers have an intense attachment to your product. And it may sound like he's contradicting himself—he isn't.

Here's how he sees it:

> **THIEL**: There are companies that are purely competitive, they do not make any money—think a restaurant. You never want to be in the restaurant business.

HOFFMAN: I'm sure right now you're thinking of a restaurant that makes money. Suspend your disbelief for a moment and hear him out.

> **THIEL**: And then there are businesses that do not compete—they are monopolies, and they do very well. And even though this is not the way people want to talk about it on the inside, you always want to have a monopoly on the inside.

HOFFMAN: You're probably thinking, "Don't we regulate monopolies out of existence?" Well, yes, the unscrupulous kind. Most people associate monopolies with the robber barons of the late 19th century. You know the type—wearing a top hat, chomping on a cigar and lounging on a pile of moneybags. Peter, on the other hand, sees monopolies in the here-and-now. They're camouflaged as competitors. Look closer, he says, and you'll find that even the most classic examples of competition are not what they seem.

> **THIEL**: You could say that Coke and Pepsi compete very intensely. On the other hand, you could say that they're somehow quite differentiated from a brand—so that in practice, different people prefer Coke or prefer Pepsi, and there actually is a much smaller set of people who view them as interchangeable products. I think measuring how much actual competition is happening is not always a straightforward thing to do. Because just as people want to have monopolies, they want to also downplay them—and so they will suggest that they're facing enormous amounts of competition everywhere, whether or not that happens to be true.

HOFFMAN: Once you think of a monopoly as simply an absence of competition, you might start noticing a few yourself. What's a patent, if not a monopoly backed by the government? And what about those companies that monopolize a market by pursuing a wildly original idea? Elon Musk's SpaceX is pretty much the only company on a mission to send people to Mars. Anyone want to take him on? No? Well, that's precisely what spurs Elon onward and upward.

You have to invent a new game—seek out a fresh, new field. But you don't have to go to Mars to discover new terrain. We sent our producer, Dan Kedmey, to perhaps the most competitive landscape on earth—the bakeries of Manhattan's West Village—to see how a baker breaks free of the pack.

UMBER AHMAD: I'm actually trying to get into a remarkably crowded market. People will look at this and think that I'm crazy. You can't swing a dead cat without hitting a bakery.

HOFFMAN: That's Umber Ahmad, founder of Mah-Ze-Dahr Bakery. You can swing a dead cat from her front door and hit Patisserie Claude, with its legendary croissants, or Dominique Ansel Kitchen, where the "cronut"—that's half croissant, half donut—was born. Competition doesn't get tighter than that.

AHMAD: And so I said, "All right, there has to be a point of differentiation." If if there isn't an opportunity in a crowded market, then Ford and GM and Toyota and Mercedes and Tesla and all these other people wouldn't exist in the same market. There is always opportunity, and I believe that very strongly. I don't believe that you have to be the singular owner of a market in order to be successful.

HOFFMAN: Umber knew what she was up against. She's a former Wall Street banker, and she knows how to hedge her bets. So she started selling baked goods online.

AHMAD: I said, "How do I minimize my costs?" And rather than build a million-dollar space, and build a huge kitchen and all these things, and hope someone will show up, I said, "Let me figure out if there's even traction here." And so I started with an online business.

HOFFMAN: Once she had repeat business, she gained a toehold in a coffee shop.

AHMAD: And I said, "Where are the people that I care about; where are my customers shopping today? Where are my customers living?" I went to those brands, and I said, "I want to work with you." And one of the first brands was Intelligentsia Coffee. So that was my first wholesale contract.

HOFFMAN: And then she took to the skies.

AHMAD: I was approached by JetBlue Airlines. So JetBlue had just introduced Mint service—it's like their first class. At the end of the contract, we were packaging pastries for 22,000 passengers a month. So that, for me, was also a really great way to do two things: test a large brand partnership, and also figure out what customer conversion looked like—if we could get customers to convert to us directly through a partnership like that. So I kept trying to find the partnerships which would gain me access to the customers that I wanted to become my own.

HOFFMAN: Along the way, she discovered her point of differentiation. She would never make anything as newfangled as a croissant crossed with a donut—leave that to Dominique Ansel. *Her* bakery ever-so-subtly elevates the familiar flavors from childhood.

> **AHMAD**: What we really want to do is to have whispers of new things in the pillow of something that is familiar. A great example of that is our spinach and feta hand pie. It's kind of like our version of a grown-up Pop-Tart, but it's savory and it's made with sauteed spinach and Greek feta. But then I season it with za'atar. Za'atar is a spice that is used very commonly in the Middle East, and so it's somewhat unexpected when you bite into it—because you're not sure, you're like, “What is that flavor?” And then you think, "Gosh, it elevates thi,s and it kind of intensifies the experience of the pastry in a way that I wasn't expecting."
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> Some of my favorite comments from customers are, "This reminds me of my grandmother," or "this thing that I grew up with," or, "I was on this vacation, and you're taking me back and you're helping me remember and experience that." And for me, that's my dream—because what happens then is I've now created a link, and I’ve created a connection with you, and I've got you.

HOFFMAN: She’s got you—as much as a baker can capture a customer. At the very least, she can go on scaling her business, even as the baker next door invents the hottest new thing since sliced bread. For her, the goal isn’t so much to break free of the competition, but to differentiate enough that she carves out her own mini-monopoly. How much do you have to differentiate? It depends—on the size of the market, the speed of your competition, and your own aspirations for scale. How big do you want to be?

Umber knows exactly who her competitors are. All she has to do is look at the storefronts around her. At PayPal, it wasn’t so cut and dry.

eBay *appeared* to be our true competitor. And as a startup founder, you’ll often hear potential investors asking, “Isn’t some gargantuan company on the verge of doing whatever it is you’re doing?” The presumption being that with all of their money and talent, they’ll squash you.

But the reality is, your most dangerous competitors are rarely the big guys. The big guys, like eBay, are hesitant to storm the field and fumble alongside you. A fumble for PayPal risked blowback from a few thousand users. A fumble for eBay, however, could anger users in the millions, and draw the watchful eye of government regulators. And even if eBay were willing to take those risks, why would they burn so much creative energy on the online equivalent of a cash register? Think about it—they’re building the store, a global marketplace for online commerce. So what if a little company is hijacking the checkout counter?

So while we were wringing our hands over eBay’s new payment system, we also were encouraged to see that they took more than a year to roll out Billpoint.

And now we get to one of Peter’s key ideas on escaping competition. It’s the central idea that drove not just PayPal’s success, but nearly every successful scale company.

THIEL: We needed to achieve escape velocity. We needed to grow so quickly that it would discourage anybody from even trying to compete with us. And so if you could scale incredibly fast—on the one hand, you have to race really hard to scale fast, but the benefit if you do it is that you're achieving escape velocity from the black hole that is hyper-competition.

You could start in something that's very competitive, but then over time, get to a place that's less and less competitive. Amazon was incredibly competitive. But over time, it's becoming more and more of the retail monopoly. And that's why people value the company so highly—because when they look into the future, they envision Amazon having destroyed all other retail stores and making all the profits.

HOFFMAN: Now this is a big idea: escape velocity. How do you know you're hitting it? Peter has a formula.

THIEL: I used to have this equation on the PayPal whiteboards: U sub T=U sub 0; E to the XT—where U sub 0 is the initial users, U sub T is the users at time T, and E to the XT is the exponential growth factor. And X is, if you get X up, the exponent rises even more quickly.

HOFFMAN: Yes, he did just recite that equation off the top of his head. You don't have to understand any of it. The equation simply helps Peter detect whether users are growing exponentially. It comes down to what Peter calls "the X factor." Translation: watch for exponential growth.

THIEL: The X factor in the exponent was growing at about something like seven percent a day—and even when you start with only 24 people, the compounding dominates. And so, you go from 24 to 1,000 by mid-November. We were up to 13,000 by end of December '99. By early February of 2000, we were up to 100,000. By mid-April of 2000, we were up to a million.

HOFFMAN: If you're wondering how Peter remembers every date and every metric from 17 years ago, your guess is as good as mine.

Maybe it's because the daily movement of those numbers hinted at a radically altered future for our company. Exponential growth is simple to grasp, but really hard to believe in. The sooner you can detect it, the better you'll understand whether you're hitting escape velocity. Think about the moment Peter detected our blistering growth rate. We had only 24 users. Every day, they grew by seven percent. If the trend held, we could break free of every competitor in the span of a few years. In short: eat dust, eBay.

THIEL: There's an Einstein line—it may be apocryphal, maybe Einstein didn't actually say it—but it's to the effect that compound interest is the most powerful force in the universe. And so there was this question, “How do we get some sort of powerful compounding to work?” And we concluded that linking money with email, and maybe giving people some money to accelerate the process, would really get it started. It made for a very crazy ride.

HOFFMAN: This underappreciated rule of compound growth is why Silicon Valley seems to spawn so many overnight successes. It’s why investors pour hundreds of millions into a wisp of a company. So long as your startup is hitting escape velocity, anyone who understands the power of compound growth will keep funding you. And most of those investors tend to reside in Silicon Valley—because they’ve seen compound growth with their own eyes, and they believe it.

Take, for example, the time that Peter and I invested in Facebook. We weren’t blown away by Mark Zuckerberg’s pitch, as we recalled.

HOFFMAN: I don't know if you remember two features of that meeting which were pretty funny. Zuck's grown into his articulateness; he's very articulate now. But back then, there was a lot of staring at the desk, not saying anything. So, what are the right words to say? Well, Zuck didn’t say very much. The second part is, remember he said, “Well, if you don't like this one, I have this other business, Wirehog.”

COMPUTER VOICE: Wirehog was a file-sharing service created by the Facebook founders.

HOFFMAN: Do you remember the peer-to-peer file distribution?

THIEL: Yes.

HOFFMAN: Get rid of that!

THIEL: Not interested.

HOFFMAN: So why did we invest? The X-factor. Facebook expanded from one college campus to the next at a speed that was unprecedented among his competitors, like Friendster or MySpace. We still had a million questions about whether the network could ever break out of college campuses and spill into the wider world, but there was no denying that Facebook’s user engagement was unreal. If memory serves me right, when Facebook launched to a new college campus, within six weeks 80% percent of the students were essentially using the service. And by using the service, I mean they checked it more than four times a day. That X-factor mattered more to us than whatever Mark said—or didn’t say—about his business.

> **THIEL**: The story I always tell was that you always have this Shark Tank image of this—and, "What did they say," and, "What were the right magic words to use to get money?"
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> And I think the answer was much more that the two of us—and maybe you, more than me—had done our homework for at least a year, maybe a decade before that, and were primed to invest. And that's actually what you want to be able to do.

HOFFMAN: Suppose you've hit escape velocity. User growth compounds by the day. Investors back you in round upon round of financing. You've mastered a game of your own making.

Now, the pressure is on to not just gain a competitive edge, but to escape the competition entirely.

The very same force that enabled you to secure huge sums of capital will compel you to spend at an alarming rate. If you want to break free of your competitors, get ready to burn money.

> **THIEL**: We had a burn rate north of 10 million a month from March to September of 2000. That was pretty uncomfortable.

HOFFMAN: Yes, you heard that right. We spent upwards of $10 million dollars a month. You might think that making sure your business has a steady stream of cash should be a priority. But when you face intense competition, you often have to *spend* to leave your competition far behind. And you might have to spend a *lot*.

In Silicon Valley, competition can be downright lethal. Think all of the late '90s search engines. Remember AskJeeves? HotBot? Infoseek? Direct Hit? Then Google comes along, and it was like, "Nope, that's it. No soup for you."

And that's just the nature of the game. The stakes are neatly summed up by my favorite line from the movie Glengarry Glen Ross: "First prize is a Cadillac Eldorado. Second prize is a set of steak knives. Third prize is you're fired." Except in Silicon Valley, it's usually first prize is the whole Cadillac dealership, second prize is you're a footnote in history.

And that's one reason Peter agreed to run a costly experiment that was pretty much unheard of at the time. Most companies paid advertisers to reach users. We took a more direct route—we paid the users themselves. If an existing PayPal customer referred our service to a friend, they each got $10 dollars online cash, on the house. Peter wasn't exactly gung ho about this idea.

Here's why he decided to pay users, despite his misgivings.

> **THIEL**: We had to get to scale as quickly as possible. And if we didn't get to scale, maybe somebody else would beat us, and we wouldn't achieve escape velocity. And we

didn't know that there would still be a rapid organic growth, even when we stopped giving customers the referral bonuses, for example. And then similarly, I also thought that we either could get to scale or figure out our business model. So we should get to scale and then see if the business model worked, rather than see if the business model worked and then scale it.

HOFFMAN: Yes. And burn rate, and exponentiating, free credit—

THIEL: It was exponentiating. Certainly there were no revenues yet.

HOFFMAN: Because the funny thing is there's a flip side, which we'll go into in a little bit, of the positive exponential curve. But the negative exponential curve was one of the things that we were also—

THIEL: Well, there were both. It was exponentially growing users, and exponentially growing costs.

HOFFMAN: Yes, exactly.

HOFFMAN: Plenty of wildly successful businesses defer profitability for years. Amazon chugged along for roughly two decades, ignoring the occasional gripes from Wall Street that their whole operation seemed to be a money pit. In fact, they were breaking free of their competition in one retail sector after the next.

You'd think just as PayPal was hitting its stride, we'd also rest easy. I wish. At no point did we say to ourselves: "Relax, Peter. We've hit escape velocity. Sign that $10 million check already." In fact, we worried without end.

Our concern was grounded in a humbling truth: escape velocity is not a fixed speed. It's always and forever relative to your competitors. Your fastest competitor determines how hard you hit the gas.

Peter suspects the majority of Silicon Valley startups could gun it a little harder.

THIEL: Post-2000, the main post-mortem was that you shouldn't scale too quickly. And you had to do it fast, but not too fast. And if you think about businesses that have failed because they scaled too quickly, there have been very few post-2000—I think there have been a few companies I can point to in the last one or two years. So perhaps as of 2015-2016, people finally got over the hangover from '99-2000. But if you think about scaling, there's obviously a lot of businesses that scale too slowly. You'd expect there to be a lot that are scaling too fast—and it's striking how few have scaled too fast in the last 17 years.

HOFFMAN: So how quickly can a competitor sneak up on you? Brian Chesky, the co-founder and CEO of Airbnb, has a cautionary tale. Now, Brian invented a wildly new game that was so strange, he really didn't have a single competitor.

If you listen to Masters of Scale regularly, you may recall my initial response to Airbnb—and the idea that strangers would open their homes to other strangers.

> **HOFFMAN**: Oh, someone's going to rent a couch or a room from someone else? Who are the freaks on both sides of that transaction?

HOFFMAN: Bear in mind, this is coming from the guy who *invested* in Airbnb. Fortunately, the people on both sides of that transaction weren't freaks at all. And now you can find them in just about every city around the globe. Brian and his co-founders had basically invented the eBay for extra rooms and empty homes. And as the new mover in that space, Airbnb scaled fabulously. Brian thought he had hit escape velocity around the middle of 2011. They had users. They had investors. They had no competitors. And then, as inevitably happens, they did.

> **BRIAN CHESKY**: And then all of a sudden, we had gotten cloned. So we had to expand really fast internationally.

HOFFMAN: By "cloned," Brian means websites that had cropped up across Europe and Asia, that looked and worked a lot like Airbnb. They were backed by a behemoth of a company, Rocket Internet, based in Germany. Brian recognized the competitive threat, thanks to some sage advice from Michael Moritz, a partner at the venture capital firm, Sequoia. Brian and his co-founders invited Michael to their headquarters to discuss Airbnb's expansion strategy. Back then, Airbnb's "headquarters" was just a dingy apartment with a no-shoes policy.

> **CHESKY**: We make him take his shoes off—it was the funniest thing. He's like, "What?" He's used to going to these offices; he has to take his shoes off in our apartment to meet with us. We had to get advice from him. We had two choices for international expansion—we could either go to the football cities, or international expansion. The football cities are basically, where in the United States are like small, medium to large cities with a football team?
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> And we can expand to St. Louis, and Baltimore, and Boston, Chicago. Or we could do something else. Michael Moritz said, "Plant flags." "What does that mean?" He said, "Pick the most important markets in the world, and imagine you lost them. Which ones couldn't you lose?" And we thought, "London, Paris, Barcelona"—we kind of stayed in Europe, Asia was maybe a later chapter. "Rio." And so we started planting flags.

HOFFMAN: I saw just how quickly Brian planted flags across Europe. He literally hopscotched from one European capital to the next, scrambling to get users on his site.

Ultimately, a wildly original idea only buys you a grace period from the competition. As soon as it works, you have a target on your back.

And in the early 2000s, PayPal was an increasingly juicy target for eBay. They did all sorts of things to rattle us, like a promotion with Visa that made it free for sellers to accept payments from credit cards. And who knows? Maybe one day they would have just booted us off the site.

That day never arrived, and it's because we found the ultimate escape plan. We sold PayPal to eBay for $1.5 billion dollars, and got out of the online payments competition. Why?

If you ever do invent a new game, fumble through it, master it, grow it at an exponential rate, hit escape velocity—even after all of that, you might still come crashing back down to earth. There's a much older adage that you should always have in the back of your head: If you can't beat 'em, join 'em.

And after all that hard work, it can a bitter pill to swallow. Just sell your company? We still question the decision.

> **HOFFMAN**: Do you have any additional thoughts on whether or not selling to eBay was a good idea or not?
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> **THIEL**: Well, I think it was still the right idea, because there were so many regulatory constraints on the business, and we were not really achieving escape velocity from eBay. You know, eBay was growing fast. We were growing on eBay. So we're growing maybe 100% percent annualized on eBay. And so to diversify away from eBay, we had to grow the non-eBay business by more than 100% percent a year. And I think that was extremely hard to do.

HOFFMAN: We'll never know whether eBay would have gained on us. Maybe we could have achieved escape velocity. Or maybe we could have held out for more growth, or a higher bid. The PayPal founders to this day have differing opinions—and I don't claim to have the right answer.

But one thing we did learn from that experience is that competition is just a drag. As investors, Peter and I both look for that founder who aspires to break free as much as possible. As Peter says, he always comes back to a fundamental question: will this founder reshape the future?

> **THIEL**: I've gone back and forth over the years how much is the people, versus the technology, versus the business strategy. But if you ask people what they are trying to do, and if it's not that ambitious, and if they're not trying to win in that significant a way, that's probably a relatively bad sign.

> And then, of course, if it's ambitious, then you have to calibrate how realistic it is—and maybe it's always a little bit unrealistic. There's a lot of calibration around that, but there's something around that that I think is very underestimated, where the future is the future that we will. We decide what future we wish to create. And if you want to ask what kind of future is going to happen in a given company, you just ask the people—and they will tell you, and you all need to do is ask.
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> **HOFFMAN**: So my version of that is you have a very ambitious future, you have an ambitious goal, and you at least have a plausible theory about how you get there. It's not just, “We will get there.” It's, “This is what I recognize the path looks like, these are some of the risks, these are some of the techniques.”
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> **THIEL**: Yes, that's a good one. The bad patterns tend to be either no ambitious future, or winning the lottery—ambitious desires, but no pathways.

HOFFMAN: These people who want to reshape the future, but also understand how hard it is to get there, and plan accordingly—they’re exceedingly rare. Most of the things you imagine about the future are wrong. And that’s why people tend to vie for excellence on the same well-worn playing field. There’s a deep comfort in knowing the rules of the game—and no harm in it, either, if that’s your thing.

But if you stop for a moment and realize that you can’t find a single member of the herd you aspire to be, then perhaps that’s the first sign that you’re ready to break free of the competition. And to that I say: “Game on.”

I’m Reid Hoffman. Thanks for listening.