PITCHIT FINTECH STARTUPS PODCAST NO. 69-DAVID McDONOUGH

Welcome to PitchIt, the fintech startups podcast, one founder, one startup, one investor at a time. I'm your host, Todd Anderson, Chief Content Officer, Fintech Nexus.

(music)

Todd Anderson: Thanks again for tuning in to this week's episode of PitchIt. I sat down with Commonstock Founder & CEO, David McDonough. Commonstock is a social network that amplifies the knowledge of the best investors, verified by actual track records for signal over noise and David describes it best during our conversation when he talks about the fact that investing has been democratized, but the flow of information has not.

Commonstock is really aiming to change that dynamic by providing investors with their file information and track records. David and I talk about the rise of the retail investor, the impact of the various meme stocks and kind of everything that went on with them, the perception of the markets overall, payment for overflow, crypto, raising capital and much, much more.

Before we begin the episode, please take a minute to rate the show and provide feedback. I take listener comments and feedback very seriously and don't forget to join us in Miami on December 13th and 14th for Fintech Nexus LatAm, this is LatAm's premier fintech event.

Without further ado, I present Commonstock's Founder & CEO, David McDonough. I hope you enjoy our conversation.

(music)

Welcome to the podcast, David, how are you?

David McDonough: Fantastic, thanks for having me.

Todd: Of course. So, I'd like to start off if you could tell the audience a little bit about yourself, your professional background before you started Commonstock.

David: My name's David McDonough, I am the Founder & CEO of Commonstock, I sort of stumbled into it not in the traditional pathway. Graduated in 2008 into the first financial crisis and all my friends went to Wall Street and realized well, I need to learn how stocks work so I was actually coaching tennis and squash trying to save money for medical school and in the process we started a little investment club called Team America Recession Please or TARP.

Todd: (laughs) A different tarp than the.....

David: Yeah, exactly, the original and fell in love with trying to understand markets and companies and business and realized the potential there, that was the original genesis. I would go on to get an internship at a VC fund and made some technology investments, turned myself to code, went to work at Google, got better at coding, started building this side project in 2015/2016 as Robinhood and

Coinbase started to take off where I could share knowledge with my friends because I taught myself about markets through the Internet and through friends and realized as these platforms were taking off that we now are able to, you know, we democratize access to capital markets, but we hadn't democratized access to the knowledge side.

And so, I bludgeoned to death the term democratize anything, but I wanted a way to make it easier to learn from smart people and to be able to verify who actually knew what the hell they were talking about. So, I started building Commonstock and it started taking off as a side project so I left Google in 2017 to build it fulltime and here we are.

Todd: Now, had you always seen yourself as a founder eventually? Obviously, this problem you kind of fell into, as you said, but did you eventually see yourself as a founder or was that never the path and it was really this issue, the first TARP that you created with your friends that kind of began your journey as an entrepreneur and founder.

David: You know, that's a great question that I wish you will ask more. I always wanted to be a founder, right, I was, from the very beginning, wanted to be an entrepreneur. I remember being an analyst at this VC fund doing diligent calls, sitting in a windowless backroom and talking to these founders in San Francisco. Again, this is like 2009/2010 when it wasn't as mainstream as is now and it just seemed like to coolest job ever and realized then okay, eventually at some point I want to do this, but, you know, I was a Biochemistry major, I didn't have any of the tool kit so I very thoughtfully spent the next ten years getting jobs that would build different tools for the tool kit, part of it was finance, now it's the venture side.

The next part of it was operations, you know, operating and managing at Google along with learning to code and getting better at the actual technical side and so I didn't want to rush into it, I didn't want to found something for the sake of being a founder, but I knew eventually I would want to be and I think that approach worked. I think the common mistake people make is just trying to come up with an idea and forcing it, but I, instead, wanted to wait until I found something that I was willing to spend the next 10 years/20 years of my life dedicated to and not rushing into that idea, but making sure that when that idea did hit, I was in the right place, right time and also had the right skills to be that founder and that, so far, has worked really well.

Todd: Tell us more about Commonstock, what you guys are building and ultimately who you see as your target customer.

David: Yes. So, we are building a social network for the stock market and crypto and you can think of it like Reddit or Twitter where you can link your actual brokerage account and so you can verify your holdings, your performance, you can verify and give people alerts, get alerts when people trade in real-time and get contacts and tell people why you're buying or selling, calls, for example. The idea behind all of these is, you know, I sort of predicted a lot of the GameStop saga and that retail was going to go mainstream before it actually happened, I was directionally correct. I don't think I had accurately really realized the magnitude by which retail markets were going to go mainstream and the problem that I saw was that there were all these drifters and snake salesmen on Twitter and everywhere else anytime you combine money and social networks you really get all scammers. As anyone twitted about Bitcoin knows you'll get all these bots and I realized it was very important, specifically for this industry, to try to weed out and amplify the voices that actually know what the hell they were talking about.

So, that's what Commonstock does, it's a network that amplifies the knowledge of the actual best investors and the smartest traders. Our target users are self-directed investors usually on the more intermediate to advanced side is where we're aspirationally targeting so you're trying to build, this is another overused term, a Bloomberg terminal for Main Street where people can't or don't want to spend money on a full Bloomberg terminal, but want a place to share ideas, get insights and unique data that you can't get anywhere else and find good ideas validated by people actually putting their skin in the game.

Todd: How do you avoid, you know, some of those scammers, some of the bots on your network say versus a Twitter and avoid it becoming something similar?

David: Yeah, actually, some background. The team I worked on for the longest at Google was the Anti-Spam and Anti-Fraud Engineering Team and this was, again, back before it was cool or really a big thing. So, I brought a lot of those learnings to Commonstock and this was built from the ground up to prevent that situation and so we have a number of different tools at our disposal proactive and reactive moderation, but really, it all comes from incentive alignment. And so, we've structured this in a way that makes it really impossible to spam or create bots that annoy people at scale because you can only have so many brokerage accounts, right, and we built this, you know, if you look at Reddit or Twitter and I love these platforms, but they incentivize engagement over quality or accuracy, for example.

So, for us, we built the incentives from day one to not necessarily incentivize engagement which would incentivize people saying extreme or controversial things, but incentivize quality and accuracy. And so, we have the broker linking layer that lets us validate using numbers and math. Does this person know what they're talking about, have they outperformed the market over the past year or are they very clearly..... we can see in their broker data and you don't have to link the brokerage at all, but if you do link a brokerage and you outperform the market, we are going to amplify your content more than those that do not link their brokerage or who links a brokerage and is clearly like losing all their money trading penny stock or shit coin crypto.

Todd: You mentioned obviously the overuse of the term democratize, but do you think stock trading and investing today is democratized?

David: I do, and I think it's a massive net positive, I think it's going to be really interesting to watch. I don't think people really appreciate the long arch of progress and I think there's a lot of volatility and a lot of initial reaction to this influx of retail investing and it's all net positive. Some of the behavior doesn't look ideal and to be clear, there's, you know, when you go into certain subreddits, the conspiracies around GameStop and (inaudible) and, you know, it's pretty wild to see just even the conspiracies around payments overflow, it's just kind of insane to see. And so, I think, generally, society, as a whole, and especially financial and capital markets weren't prepared for what happens when you get this new rapid influx of information liquidity and so we have democratized access, but we haven't democratized the knowledge side.

And so, that's where, to answer your question, having a lot of, you know, 14-year old’s, 18-year old’s, 25-year old’s all involved in markets is a massive positive. They may initially not know what they're doing or not invest the way that Warren Buffet invests, but they're learning and making these mistakes, understanding things at the age of 18 that otherwise they would have waited until 35 or 40 to start learning. In fact, I always say that 18-year old’s know who the Chairman of the Fed is, that alone is a remarkable shift.

Todd: (laughs) Oh, yeah.

David: Like I can tell you for a fact, when I was 18, I was not concerned with monetary policy.

Todd: (laughs) Yeah.

David: I think that's where it gets exciting is this generation will have a 10-year head start on financial health and that'll really start to play out over the next decade as they start to come into founder-age, creator-age, whether they start companies or whether it changes their employment prospects, their financial health as they create families, etc.

Todd: You reference the GameStock saga and obviously a lot of the noise around that was, you know, was there these secret deals going on in back rooms that either help stop the bleeding of one firm versus another. Does the information flow and the advantages of the big investor of Wall Street, does that still tilt as badly towards the Wall Street firm and have we or have you, has the market made a bit of a dent in that, were starting to even out, but obviously the scale still isn't equal.

David: It's not equal and I don't know that it ever will be equal nor split necessarily. I don't think it's fair or even healthy to say retail investors are entitled to all of the same exact tools, right. It wouldn't be fair for me to say, I deserve a Bloomberg terminal, but I think it depends on specifically on what you're asking, I think the data or I think the exciting part of capital markets is that it's all there, it's possible to find all the same date. We all play on this even playing field, it's about the resources and the time to get that data or find that data and anybody who works hard enough can get access to that. You know, if I'm a regular self-directed investor and I don't have access to the alternative data that a hedge fund might use to see if parking lot is full at Walmart at scale, they might use satellite imagery, I might just have to just go and sit in a Walmart or call a few hotels, but I can work my way up to a affording that.

I think, I'd draw distinction is just because institutions have access to more resources doesn't make them inherently evil, like we have this concept today where there always has to be a bad guy, right. When GameStop happened at the pause trading, there was nobody evil, there was no bad person in the scenario. We had such a rapid influx of treat activity focused on one specific asset that the regulatory framework that we created, Verdant and Ziz, was immediately not enough and it was not an evil thing, it was just like wow, we never could have possibly, in a million years, predicted this would happen. We made it a requirement in the capital requirements 3X and we, in this case, needed it to be 6X type of thing so I think understanding that different resources is not inherently evil is I think the incredible thing to understand.

Todd: Is payment overflow, you know, what are your thoughts on it. Obviously, some in Congress have taken it up as if it's this one, that it's a new thing, which obviously it is not, if anybody understands anything about this type of market, it's not there like everybody essentially uses it, not just Robinhood who made the headlines for it. But what are your thoughts on it and should it be adjusted or regulated further by either legislators or those in the SEC or whatever agency might oversee some things.

David: Yeah. This is one that I think is just so fascinating to me, makes me sometimes feel like I'm taking crazy pills (Todd laughs) because it effectively enables us retail investors to trade for free.

Todd: Exactly.

David: They pay like a cent or half a cent per share or per trade and we actually get price improvements, you know, it's all net positive. There's a very, very small sliver of people who are retail investors, who might like the high frequency trading at crazy volumes on which case it might me more, slightly more expensive for them, it might be very arcane specific instances which are fractions of a percent of the total market where it can be not the best approach, but they can pay fees to get a specific different type of execution.

I can't fathom the fact that it's even controversial because it’s like what is the alternative, by the way, yeah, we should have more sunshine as always, more transparency, more insight into best bids and all of that would be great. I'm not saying that we shouldn't have more transparency, more openness, but again, it’s like we're looking for this bogeyman where most people don't realize, I don't think who are complaining, that when I started investing with E-Trade, I had to pay $10 per transaction and now, I have to pay maybe a penny. I can't fathom, people are like we need to get rid of this free thing and go back to paying $10 per trade.

Todd: You would think with all the focus on, you know, especially those in Congress on like overdraft fees and banks gouging customers with secret fees, something that eliminates the fee would be heralded versus thrown under the bus for some other reason.

David: You would think it’s free, (Todd laughs) I can’t wrap my head around it. Again, I’m not saying there’s no room for improvement, it’s just that we are to watch this thing turn into a bogeyman when it’s just like a basic, very amazingly beneficial, one of those rare things that actually creates a “win, win, win” for brokers, market makers and the end-users just to benefit.

Todd: In terms of buying actual stocks, a stock of Amazon or Facebook or whoever or some of these blue-chip companies, they’re still generally pretty expensive for the everyday trader who wants to maybe play around. Obviously, you guys are catering to a bit more sophisticated person, but what have you thought of the impact of fractional investing to give even the smaller trader a chance at owning pieces of companies and getting involved earlier, has that had a big impact on the overall retail push and what are your thoughts just generally on the fractional trade?

David: I think it’s amazing and it’s a very good thing because, as you said, it does create an on-ramp for more people to get involved in owning Amazon or Apple that’s not quite as expensive. I always go back to this mindset that I have, right, my opinion is that the value of investing is, you know, secondary value is the notional increase of the amount of dollars in your account. The primary value is having skin in the game and because of that you learn about markets and capitalism and business and the things that drive the economy.

I bought a few shares of Tesla in 2012 and by no means is that enough for me to retire, it doesn't move the needle at all in terms of my finances or economics, but just having skin in the game means that I'm super interested in Tesla and how car companies work and how the economy works and this is why I started Commonstock is because what I've personally experienced is it doesn't really matter whether you have $10 or $100 or a million dollars.

Just having any exposure makes you interested in learning and improving and that is, over the long haul, more valuable to you than, you know, I may have made $1000 or $10,000 on those Tesla shares, but the insights and the knowledge that I got, because I had Tesla shares, is worth an order of magnitude more than that notional dollar value. And so, I think fractional shares unlock that for a wider audience of people and that is, in the long haul, super valuable.

Todd: How big or potentially detrimental could a recession be on the retail wave that we've seen the last couple of years and is there a risk that some of those retail investors won't come back or that kind of retail will fade for this the time being.

David: There's definitely a risk that things will fade and it will drop off and I shared a chart during the GameStop saga when we raised our Series A to our internal team, like it's going up like this and I can assure you that at some point it will come down. The thing about retail though is when you look back at……I feel almost fortunate at this point to have lived through multiple corrections and recessions because we look back at 2000, 2001, 2008, even 2020, what happens is retail is extremely volatile as a purchase spin.

You have your money in an account and you may step back, you may not stop checking your account for a time, but what happens afterwards is market starts correcting and will go back up, it's very cyclical and retail will return and it'll start returning in droves. It's really more of a living, breathing thing, people don't generally put money into the market and then literally never come back to it. And so, for us, it's more of a time and a seasonal approach to….just like crypto winter, the original form of that was just retail winters and usually shorter and usually are paired with market performance and so as long as companies are prepared for this season, it'll be summer again, if you want to use that analogy, and you just need to be at the right place at the right time to capitalize on that.

Todd: Is crypto, in your estimation, more dangerous than regular stocks, I mean, does it need more guard rails than say the typical stock market or is it just another asset? It might be a bit more volatile today, but trading crypto shouldn't be viewed as that much different than say trading a stock?

David: Trading crypto is absolutely more risky, more volatile. I'm a crypto bull, in general, I'm excited about some of the opportunities in crypto, but I think crypto specifically is……we live in a very different capital market world right now than has ever existed before because of the way that information spreads. And, you know, if you think back in 2008 even, Facebook was just getting started, Twitter, Reddit, but we really didn't have the information liquidity that we have now where it becomes so much easier to coordinate, it exacerbates cycles more quickly and so human nature is going to do what human nature does and it's going to create this massive pipe cycles and pumps.

You have to realize that in an unregulated way it's just human nature left to its own devices and then it just compresses the wavelength of those cycles so you have to know that and also we're in the early innings of something where there is no regulation or very little, very few social or cultural norms around it, you have all these scammers and drifters and there's no way to prevent it. There's maybe 5% of crypto projects are really great and healthy and the rest are things that are crazy over levered or outright scams or Ponzi schemes, it's so nascent we haven't been able to flush those out of the system and it's possible that those drifters could overcome the entire thing and it never announced anything.

It's good to have like a call option on crypto and have a very, very small amount, in my opinion, exposed to, like I didn't have anything in crypto and I've been buying the recent dip to keep it around under 5% of my total portfolio because if crypto does turn out to be the world currency and Bitcoin and Ethereum go up 100X then that's great, I'll capitalize on that, it can be game changing for the portfolio. If it goes to zero and I lose 2%, that also doesn't affect me so it's sort of an asymmetric risk, but also an asymmetric risk profile upside and downside that as long as you take that approach versus putting all of your money into crypto, it can be a healthy thing, but you've to understand that risk profile.

Todd: What's the biggest lesson that you've learned about Commonstock since launching?

David: The biggest lesson that I've learned about Commonstock, but I think more in general, is the time and effort that it takes to build something truly great and scalable and of value and I think this is more about company formation. The time and effort and the challenge involved in creating Amazon or Apple, it became in vogue or trendy or just common misconception that you can just spin up like an Instagram and sell it overnight in a year with five people. The reality is that Amazon's stock price went down 95% at one point back in the day, right. That is staggering and you can't fathom the culture inside Amazon at that point, like how could it not be doom and bloom and knowing that it takes five, 10, 15, 20 years to build anything of value. And especially today, when I see something get overnight economical success, it takes off, the only guarantee I know is that it's going to come crashing down, at least in the consumer space.

Todd: Yeah.

David: You can build for the pipe cycle, that really quick win, but you don't have anything to back it up, that's going to be short-lived and when it comes crashing down you can actually be in a worse place than if you built a slow, steady, healthy thing. You can't build a tree, you know, a redwood in a week, it takes years. That and like just the intellectual and psychological challenge around building a startup, 95% of the challenge, in my opinion, is psychological and emotional, the actual coding and designing, marketing, that's the easy part. It's managing humans, managing people, managing their mindset while the world explodes in both directions around you, both upwards and downwards, that's a large part of the challenge.

Todd: Biggest regret since starting Commonstock, if there is one.

David: My biggest regret is going to be a boring one, I don't have a single big regret, it's more of a…..my regret is always optimizing for speed over quality and sacrificing a threshold of quality, whether it is in hiring, hiring is where it really manifests as the biggest mistake. You know, you feel all this pressure as a founder to move fast and deliver results immediately. And because of that, you can end up, you know, initially spun up massive teams of contractors that built the foundation of the code in the wrong way, we had to rebuild and re-factor. Those are the things that can be short term wins, but long-term massive losses, sometimes almost triple the company, not sacrificing quality in your threshold for what great looks like in the interest of speed.

Todd: Best piece of advice you received since launching?

David: One of the best pieces of advice that for a while didn't seem correct was Sarah Tavel at Benchmark and this was before GameStop. As we were starting to take off, we were in this climate where lots of other startups were spending money or just lending money on fire buying up and that was what….you know, money was free, as what VCs were all rewarding, it was extremely tempting to…I was talking to Sarah, we hadn't raised our Series A yet, was saying, in watching all these sub-par, you know, copycats or people in our space just buy their way to artificial growth, inflating their numbers, it's not real, but it looks good, they're pumping up their fluff metrics, can I just do this, we have money now, can I just spend like a million dollars and buy a bunch of users.

And she talked me off the ledge, especially in consumer and social networks, where that would have probably killed the company, in fact, it killed a lot of our copycats that did that because you are creating a community of real bonds and anytime you flood that with low quality or artificial users you end up breaking the bonds of that organic community. An organic community is extremely hard to build, but it's insanely powerful if you do build it. The artificial one, where you receive a million examples of these now, can look good at first and you see that manic growth, but as nature comes crashing down because it's all fluff and artificial and then you're kind of screwed.

And so, on the surface the advice was, stay out of your own way and, you know, stick to your guns which for me is I want to build this the right way, not because I feel external pressures from investors to meet some deadline or build a bigger goal immediately and that can often be myopic and shortsighted. We'll build it in the right sustainable way, it will be painful for a while, but in the long term how you win. A bit of a ramble there, but that was some of the best, concrete advice I got.

Todd: How big is the team today and what does the team look like, engineers, product, what's kind of the make-up of the team and where it stands today?

David: It's primarily engineering, but we try to keep a small lean team because I think that's really, at our stage, how you can remain nimble, but you can create outsized returns and an outsized company where common knowledge was bigger is better, even I fell into this trap. A lot of other startups fell into this over the past few years, you know, over hiring and they can end up slowing you down enormously. So, we're still under 50 people, somewhere between 30 and 50 and the vast majority are engineers building and now, we're starting to build out design and marketing teams, but for the most part, all engineering data, frontend, and backend.

Todd: You mentioned the Series A a couple of times, how was investment appetite when raising the round and if another founder picked up the episode, what kind of advice would you give them if they were looking or going out on a fundraise today?

David: Our Series A happened during an exogenous market shock which is GameStop which created a pretty massive tailwind. I've done a lot of the legwork before as I saw that heating up so I had done all the prep work and was ready to execute on it at the opportune time.

Number one advice would be create some macro tailwind that…where VCs like we need to place a bet on this asap, it becomes obvious to everybody else. That's not really doable within founder's control necessarily and so in lieu of that you can still create your own momentum, whether that's through marketing, growth, doing all the legwork to, you know, six month/eight months ahead of time, understand where your product will be, where the market will be and make sure you sequence things, start relationships, start sending out intros and start the conversations so that when you start to hit your stride, and ideally external macro conditions line up, you're in the sweet spot where you can create a lot of market pressure and dictate terms.

Todd: So, we have just a few minutes left, I'd like to end a little bit lighter. Do you have a favorite book and the last book that you read?

David: Just a cliche, but "Shoe Dog" is one of my all-time favorites and the last book that I read which I'm currently reading is "Crossing the Chasm," it's a book about the software companies needing to go from early product market fit with like their innovator group, the initial users, there's a huge leap that you have to go through from that user to mainstream adoption. That's where Commonstock is, it's a great place to be in, but it's hard, it's not intuitive, I recommend that people read that, it's been really interesting.

Todd: Founders, obviously, a lot of them get to the point of almost burning themselves up, what do you do to unwind and kind of step away and take a few minutes?

David: Not so good at that. I have an art freak hobby, I think we've missed label burnout. Burnout is having to work hard on something that doesn't give you energy, in my opinion.

Todd: Prove your point.

David: I work insanely hard on this, 120 hours plus a week, but I love it and it gives me energy so that's where I'm even surprised myself that I'm not burned-out on this because it's not about how hard you're working, it's about what you're working on. So, if you find something that gives you energy, you're sort of immune from burnout, you know, when I have to do a bunch of paperwork and admin, as the team knows, I hate that (Todd laughs), that'll burn me out in a second. So, you know, photography and then I go for runs.

Todd: Do you have a favorite sport or sports teams that you root for?

David: Got into Formula One five or six years ago, where you drive to survive and that's been really fun. And I also am a huge well, American football fan so the Washington Commanders, although they're terrible (Todd laughs), now more European football, soccer, calling Leeds. My girlfriend is from Yorkshire, near Leeds so have adopted that, some Americans and the US National team ahead of the World Cup.

Todd: Do you have a favorite vacation spot?

David: The beach. My family grew up going to Martha's Vineyard and Nantucket so New England beaches, I'd say, kick on.

Todd: Final question, biggest inspiration in life?

David: Saving the best for last (Todd laughs). Biggest inspiration in life, what inspired me the most, what drives me is having the most impact possible on the world in a positive way. And so, when I think of inspiring people, I actually think of some of the titans of industry Bezos, Phil Knight, even Elon, despite some of his current antics, Zuckerberg, people who are able to will things into existence and change the way things operate, ideally for the better. You know, I have a lot of feedback on things they'll do differently, for Elon and Zuckerberg specifically, but like Phil Knight I think is a good example of a big inspiration for me.

Todd: Well, David, I appreciate your giving me a few minutes here today. If someone picked up the episode, they wanted to reach out, find Commonstock, how can do so, how can they reach out to you guys?

David: Yeah, commonstock.com, there's an app in IOS and Web App so commonstock.com, sign up and you can DM me right away.

Todd: Alright, well, thank you very much, David, continued success to you and the team.

David: Thanks so much, Todd.

(music)

Thank you for listening to the latest episode of PitchIt, the fintech startups podcast. I encourage you to take a few minutes to write a review or rate the episode. Both ratings and reviews help us to improve the show for future episodes. If you're interested in learning more or would like to be considered for a future episode, please reach out anytime. My email is todd, t o d d @fintechnexus.com and until next time.

(music)