

2009

The Flight of Angels



*'Bootstrapping' may be the only
funding strategy for startup companies*

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About the Author

Henry Gregor, has over 30 years experience working in corporate America; he has held numerous technical, marketing, and sales management positions in a variety of industries.

Henry's background in Fortune 100, Fortune 500, and startup companies has given him the experience and skills needed to help companies deal with enhancement and growth. He has been on startup teams in six companies; he was the founder of a direct-marketing and telecom services company.

His present companies, StrategicVisions& Evaluations Plus, specialize in business and management consulting, aligning strategies with human assets. They are strategic partners of Profiles International Inc.

Henry has experience servicing a variety of industries, from high-tech to blue-collar. He has been on the front end of many revolutionary products, like flash memory. He has also enabled numerous Strategic Alliances; one led a Fortune 100 company to create a \$1B operating division.

Henry has authored numerous articles and papers and his first book: "**Business Genesis – A Strategic Approach to Starting a Business**", he is a very able presenter with a commanding customer presence.

He graduated from the University of Strathclyde (UK) with a B.Sc and then from Syracuse University with a Masters in Electrical Engineering, and worked on an MBA at Portland State Univ. He holds CEng and MIEE accreditations and recently became a Certified Behavioral Analyst (CBA)

Flight of Angels

The current economic crash may force 'Bootstrapping' to be the primary funding strategy for many startup companies, for the next few years.

Where would startup companies be without Angel Investors? We will find out in 2009! In 2007, 258,200 angel investors pumped \$26 billion into 57,120 companies?

The [Angel Capital Association](#) recently conducted an Angel investments survey; half the respondents believe they will receive more investment requests in 2009 than in 2008. However, 60% of them said the number of investments and the dollars will decrease in 2009.

If the reduction in dollar amounts available is in keeping with the runoff in the equity markets, there will be 40% to 50% less Angel money available in 2009. Angel liquidity, like yours and mine, has been devastated by the current unprecedented economic downturn.

Sweat Equity

The downturn is forcing Angels to invest more carefully! Deals will still be made, but they will be fewer in number, and happen less frequently. Despite the expected dearth in Angel (and VC) moneys, the entrepreneurial minds in our population are still clicking away. They will continue to come up with great ideas and the desire to start new businesses.

The situation requires startup companies to exist on founders and other's funds, and 'Bootstrap' their way to generating revenues; possibly all the way to breaking-even! Bootstrapping is a way for entrepreneurs to utilize other people's money in order to grow their company. OK, it may not be actual money but it is people's time and their expertise, and time is money. It is very common for engineering teams to be made up from 'Bootstrappers', working for 'sweat equity' in the startup company.

Bootstrapped Financing

Bootstrapped financing, in effect, is a means of financing a startup company by innovatively acquiring funds, or other assets, without raising equity through traditional sources, banks, etc.

The traditional 'direct' approach for many entrepreneurs is to get moneys from their family members, or friends, or from the sale or mortgage of their own assets, or even credit cards.

There are positive and negative aspects to Bootstrapping. On the positive side, waiting as long as possible to consider equity financing gives the entrepreneur a better chance of retaining more ownership in his/her company.

Angel or VC Moneys

Waiting for funding may actually raise the probability of obtaining Angel or even VC funds. Limited funds limits the performance and success a startup can achieve, and/or determines its solvency. Angel moneys (and VC \$s) is often invested later in a startup's growth cycle.

Waiting until a company is further developed, gives an entrepreneur greater control in running a company. There will be fewer questions and less monitoring pressure from investors.

In effect the new company can be more flexible and agile and be better positioned to deal with the ambiguities that all startups face. Investor involvement and monitoring often forces a 'strategic rigidity' (see author's article, "Underperforming Corporations").

Types of Startups

Success or failure in Bootstrapping as the predominant funding strategy is dependent on a variety of factors, some of which may not be within the sphere of control of the entrepreneur.

Factors such as the business environment, or ambiguities and the awareness of how the 'type' of company (being started) affects the success (or failure) of a new company, is often a 'don't know' for entrepreneurs.

This Author, in his book "*Business Genesis – A Strategic Approach to Starting a Business*" describes five types of startup businesses:

1. Life-Style Businesses
2. Evolutionary Businesses (Corporate Spinouts, etc)
3. Venture Funded Startup Businesses
4. Revolutionary Startup Businesses
5. Corporate Revolutionary Businesses

Each type of business requires a different funding strategy. Life-Style businesses for example are almost always Bootstrapped (about 95% of all startups in the US). And the others, and variations of the other types, present differing funding and Bootstrapping challenges.

Startup Growth Phases

Startup companies have three phases of growth; 1) internal, 2) external (market), and 3) 'GAP' growth; i.e. the GAP is the potential growth opportunity space/time between internal growth, and growth in the market. Bootstrapping efforts 'in the GAP' may provide some 'market growth' opportunities for a new company.

When the business's activities cross-over into the 'market space', Bootstrapping opportunities decrease greatly. Generally, businesses that have, or are developing an end-product (not a service), usually have specific Bootstrap issues to deal with.

Most Bootstrapped businesses use sweat-equity labor to design, engineer and/or manufacture their products. The concept of sweat-equity works fine for engineers and internal marketing and sales, or finance but many other types of labor don't have the personal luxury of being able to work for free. And external marketing people and companies all want to get paid!

Time to completion is also a very important factor in the successful use of Bootstrapping. Sweat-equity labor usually has an undeclared tolerance for how long it can wait until a startup is at the stage where it can pay wages. This time will vary as a function of the individual but success in less than two years would not be an unusual expectation.

That Special Case

Businesses developing services or applications for the Internet, that are using Bootstrap self-funding techniques, can grow in both phase 1) and phase 2) simultaneously. Internet service/application/software companies can actually grow in all phases at the same time!

There may not be a 'GAP' for businesses developing Internet Services or Applications! They develop their App' or Service while operating in the target medium using its technology.

These companies would fall into the 'Type 2' category (above), similar to a spinout; they are in effect extending the capabilities provided to an existing market. Bootstrapping is a very effective strategy for Internet/Web based startups!

An important area of consideration for a Bootstrapped Internet company, like others, is the time to success, or to when wages can be paid. Internet companies can actually be category 1, 2 or 3 (above). Many of them 'are' lifestyle companies, providing incomes to the founders but some of them eventually received VC funds and grow to be giants, Yahoo, eBay, etc.

The Bootstrap GAP

The GAP is a time or activity period in which Bootstrapped labor and other techniques can be used effectively to generate revenues and operational growth.

The GAP comes between a startup's first growth phase, 'internal', and the second growth phase, 'external'. Bootstrapped self-funded companies may actively use the GAP period to Bootstrap revenue growth and generate cash.

Some companies will have little or no chance of creating cash for themselves in the GAP! Consumer-product companies could face this issue.

Bootstrapped companies must accept lower performance targets, and develop strategies that will allow them to gain traction in their target markets; strategies like 'targeting and tailoring' an offering to a niche market.

When the GAP is in Play

Knowing when the GAP is in play is very important for all startups.

1. Is the target market \$s > 100 times the total capital available?
2. Is the business consumer-product based?
3. Will the end- product sell for > \$1000?
4. Is the business developing Web based products or services?
5. Are current operational costs > 50% Bootstrapped?

If you answer in the affirmative to questions 2 or 4 the GAP is not in play for you; if you answered in the affirmative to question 2 you need to develop a special strategy of how to get your product to market; Bootstrapping will not work! If you answered in the affirmative to question 4, Bootstrapping will work just fine for you in all stages of your business development.

Answering in the affirmative to questions 1, 3 or 5 means that the GAP is in play for you! You need to develop a strategy that will allow you to Bootstrap your way to making sales! Answering in the affirmative to 3 means that Direct Sales strategy might work for you. All others should think about Niche Marketing or developing a Strategic Alliance.

Using the GAP

A company's ability to use the GAP will also be a function of its 'type'!

Type 4 companies (from the definition above 'Revolutionary') will have a tough time utilizing the GAP; the requirement to create awareness and to create a markets requires cash. These companies must develop strategies that will generate revenues in as short a time as possible.

Companies selling high price capital goods will find it easier to use the GAP in their growth strategies. The very nature of their product will force them to target, and they will have little need for mass marketing, they can use direct sales effectively to generate revenues.

If the GAP is in play (or not) startups must manage their moneys to maximize its potential and benefit. The best way to do this is to control finances using 'Zero Based Budgeting'; this forces continuous attention to managing cash usage and to operating on a project basis.

Bootstrapped Businesses Marching Orders

- Determine the 'type' of startup being launched
- Develop a Zero Based Budgeting process
- Determine if the GAP is in play
- If the GAP is in play, develop a GAP Strategy
- Consumer-product companies should develop a 'niche' strategy
- Revolutionary businesses should develop a 'strategic alliance'
- All businesses should develop Post-GAP revenue objectives