Universiteit Utrecht

Climate-KIC Scout Report - Australia

The value of start-up communities

November 2013
Henk Steinz (henk.steinz@climate-kic.org)
Frank van Rijnsoever (f.j.vanRijnsoever@uu.nl)
www.climate-kic.org
@ClimateKIC

About this report

This study is part of the Climate-KIC Innovation Scouts program. Climate-KIC is Europe's largest public-private partnership, working together to address the challenge of climate change. An important part of Climate-KIC's efforts is to facilitate entrepreneurs in bringing new ideas and technologies to market that mitigate climate change. It does so by providing funding, training, and access to a network of academic institutions, governments, corporates, and investors.

As Innovation Scouts, we study (a) what makes entrepreneurial ecosystems work, and (b) the lessons we can learn from other programs that, similarly to Climate-KIC, aim to accelerate (clean tech) start-ups. We do so by collaborating closely with and interning at local key stakeholders, such as start-up incubators. Our results are shared with the rest of the world, thereby providing value for Climate-KIC, local stakeholders, and the world wide start-up community.

This document contains the key findings of the research performed in Australia from February – July 2013 and has a specific focus on the value of start-up communities for entrepreneurs and the start-up ecosystem. In Australia we studied the young and quickly growing start-up scenes in Sydney and Melbourne and the emerging start-up scene in Canberra. We visited 17 organisations in Sydney, Melbourne and Canberra that support start-ups, including the leading incubators, accelerators, co-working spaces and investors. We performed 53 (53 minutes average) qualitative interviews with entrepreneurs, facilitators and other stakeholders and met and spoke with many more people in the start-up scene at several events.

In this report we present eight important lessons about start-up communities.

It is important that communities:

- select the right people;
- are open to new members;
- encourage learning from peers;
- give motivation and inspiration;
- are diverse, but not too diverse;
- consider different stages and needs.
- are big, but not too big and;
- host events;

In this report we will start with (1) setting the Australian start-up scene by providing some background. We will (2) discuss the most important lessons learned and (3) present some interesting models to accelerate start-ups.

1. The Australian Ecosystem

In land area, Australia is one of the largest nations, it is however very thinly populated with only 23,1 million inhabitants (in 2013) of which most live in cities. There is thus a limited national market. Most start-ups we interviewed see Australia as a perfect test bed for their product/service, however to seriously scale the company they have to look at bigger markets. English speaking countries belong to the usual suspects and the US is the prime suspect. The US and especially Silicon Valley is the place where everybody looks at because it is seen as the most exciting place with the right conditions.

Not many entrepreneurs express their interest to expand their business to continental Europe. In Australia Europe is not known for its flourishing start-up ecosystem and the barriers to entry are perceived as too high. Europe is a collection of (small) markets; there is no European wide introduction possible at once (one can argue this is the same in the different states in the US). The language barrier makes it hard to validate a market without local partners. Also the European financial crisis makes Europe a less attractive place to settle. Growing economies in South East Asia and South America seem more interesting to Australian start-ups in that respect. Australian tech start-up success story Atlassian is an exception to the rule. They opened their third office (after Sydney and San Francisco) in Amsterdam because of its good tech community, central location in Europe and outstanding language skills.

Australia has seen nothing but economic growth the past twenty years, averaging 3,5%. The mining boom has been a great contribution to this growth. With 1,6%, inflation is under control (CPI)(2012) and unemployment is relatively low 5,6% unemployment (2013). It is therefore not strange that Australians belong to the wealthiest people on earth ($222.000 highest median wealth in the world in 2011) and come in second on the Human Development index, just after Norway. The necessity to start a new venture is thus very low. Comfortable jobs with high salaries (and high costs of living) are said to hold people back to become a full-time entrepreneur.

Although Australia has a rich history of small- and family businesses, it is not common for high potentials to start a new venture. Society encourages the more traditional careers that include a university degree and a corporate job. Some say that Australia suffers from the 'Tall Poppy Syndrome', which means that high achievers are resented, cut down or criticised because their achievements or ambitions elevate them above their peers. However, the emerging start-up scene attracts more and more entrepreneurs.

Australia has a relatively small and young start-up scene but it is growing very fast. Experts in the start-up community say that there was virtually no start-up scene 5 years ago and actually only really started growing fast and becoming more vibrant since 2012. By February 2013 there were 62 co-working and collaborative workspaces, incubators and accelerators spread over Australia.

The immaturity of the start-up scene translates most clearly to the lack of available funding. Seed funding is alright, also because of several available grants. Follow up funding can be more difficult but is available for the right companies. However, to raise a serious series A most start-ups look abroad, typically to the US.

The main reasons that there is so little series-A investment in start-ups in Australia is said to be the risk averseness of investors and the safer investments options available such as mining. With an average interest rate of 5,4% from 1990-2013 and a stable low inflation, even a savings account has a reasonable -and definitely safer- return on investment.

It has to be noted that the different cities under study (Sydney, Melbourne and Canberra) have their own and notably different start-up scene. Most important and obvious difference is the size of the scene which relates directly to the city sizes; the biggest being Sydney, closely followed by Melbourne and Canberra being the smallest of the three with respectively 3.641, 3.371 and 356 thousand inhabitants. More subtle differences are in the sense that Sydney is the most transactional and self-praising and Melbourne as well as Canberra are more relational and modest slash less good at communicating their successes.

2. Lessons learned

Below are eight of the lessons that we have learned about the value and the success factors of a start-up community. We see a start-up community as a group of entrepreneurs that are tied to each other by an incubator, accelerator or co-working space. Although this could also be virtual communities, we focus on communities in an office environment where start-ups work alongside each other.

It is important that communities…

- **select the right people.** Some communities have a thorough selection procedure. By curating the people that become part of the community, you can influence the culture, homogeneity and quality of the community. An important characteristic for a valuable community member is the willingness to contribute to the community by sharing knowledge, expertise and experience. People who only want to take should be avoided, as this community manager explains: *"A big part of our being here is also protecting the community because there're so many people that would come in to a place like this and go, "Hey, you have a bunch of developers here and I need developers. Introduce me to these developers." And it's like, "No."* Some communities use a trial period to find out if there is a good fit between the entrepreneur and the community. If there is no good fit, the community facilitator can ask the unwanted member to leave. In self- selective communities this process is much more organic. The community as a collective attracts and rejects new members on the basis of how they fit. Therefore the first group of people in the community is determinative for the characteristics of that community.

- **are open to new members.** This is important to determine if the community selected the right people and to let the new member come to full potential. Too Large and close communities can be intimidating to new members, which would hamper interaction. Some communities use a 'Buddy System'. New members to a co-working space or incubator can sign-up for a buddy that introduces them to the others in the community. Ideally the buddies work in the same industry or have a similar business. Through his buddy, the new member quickly becomes familiar with the values, customs and other members of the co-working space or community.

- **encourage learning from peers.** An important value that entrepreneurs extract from a community is the informal knowledge sharing. Start-ups face similar problems and solve them, they make mistakes and they learn from them. By sharing this knowledge not every start-up has to find the same solution, or make the same mistake again. This accelerates the process of building a successful start-up. *"You learn from them and you get inspired to keep persevering. To see everyone pushing their product, facing the same problems, you can talk to them about it. Almost every day we try to meet with some company in the building to figure out something about our business which we need to know. Like manufacturing for example, how to protect your IP and manufacturing in China."* Peers are also important for bouncing of ideas and get feedback from. Knowledge sharing relates to both technical and business knowledge. A coffee corner is always a good place for informal knowledge sharing. For example, York Butter Factory actively facilitates this in their café style area.

- **give motivation and inspiration.** Apart from having peers around to learn from, it is also important to have peers around for motivation and inspiration. Entrepreneurs often describe building a company as a very long and lonely journey. Seeing other start-ups having successes on their journey can give a boost, as this entrepreneur explains: *"Because it's not easy to slug it out as an entrepreneur so it's good to see, it's encouraging when other people in the space are doing the same thing and they achieve like milestones and wins."* Thereby, a community can function as safe haven from Tall Poppy Syndrome, because the entrepreneur is surrounded by like-minded people. Entrepreneurs also indicate that there always is a bit of healthy competition with other firms which makes them want to run just a little bit faster. It is important to share a common goal; building a successful start-up. Therefore a community needs a large majority of driven entrepreneurs and not too many service providers (lawyers, accountants, etc.) that see the community as potential customers.

- **are diverse, but not too diverse.** To be able to learn from peers and get motivation and inspiration, the community needs to have the right diversity. If start-ups are too similar, there is a chance of unhealthy competition (i.e. competition for the same customers) and this will hamper the knowledge sharing for fear that ideas get stolen. If start-ups are too divers, they become unable to relate and learn from each other. Most communities consider this in the selection of new members. For instance the company has to be a tech start-up, but can't be a competitor of one of the start-ups that is already part of the community. This ensures a sort of common sense of belonging and an 'us together against the world' culture, as this entrepreneur explains it: *"Here it feels like we are actually part of a bigger team. That's an important thing for start-ups, the culture aspect. Sometimes we feel like [the incubator], sometimes we feel like [the start-up] as an individual business."*

- **consider different stages and needs.** Besides building company culture, different start-ups in different stages of development have different needs. Early stage start-ups that are in the business development phase are probably better off in a vibrant community as can be found in a co-working space. There they meet new people, meet partners, learn, get inspired, receive feedback, get motivated and get referrals. Start-ups that are in the next phase where they build their product don't need the 'distractions' that a community can bring, they need to focus, build and sell. Successful non-EU start-ups that come to Europe are more likely to need market introduction than product development. Climate-KIC should be able to assist in network (partners, suppliers, customers, funding) and knowledge on the local way of doing business. Small start-ups can benefit from working in the supporting culture of a community. However, when the company grows bigger it can also hamper the development of own company culture. This is the point when start-ups outgrow their community. As this entrepreneur explains his experience with first a larger start-up an now a smaller start-up: *"First time around we built up to 20 people pretty quickly and you built your own culture, you need to be in your own office, you need to be on your own. But when we are with 3 people like we are now, you need to be somewhere where there is a culture around you, where you can absorb that."*

- **are big, but not too big.** Large communities create economies of scale and have a larger network. It also brings legitimacy, i.e. when being an entrepreneur is out of the ordinary, as it is to some extend in Australia, a community of like-minded people justifies entrepreneurship as a career path. This also attracts more entrepreneurs, investors and other stakeholders which benefit the entrepreneurial ecosystem. However, when communities become larger, you come to a point where not everybody knows each other anymore. This reduces the sense of belonging and trust. We saw that, in larger communities, community managers play an important role in facilitating in what would otherwise happen organically in smaller communities. If the community grows too large, it becomes too big a distraction for the entrepreneur to know everyone and keep up with what they are doing. Thereby the entrepreneur risks missing out on opportunities to learn and collaborate. A community manager can facilitate those valuable connections. This community manager explains: *"So my job here I'd say is to greet everyone and to get to know everybody on a personal level so that I know what everyone is about, what their interests are, what they're passionate about, what they're good at, what their skills are, in that way the more people I meet, the more I could introduce people".* Also organising small events like communal lunches and informal drinks foster those interactions.

- **host events.** Start-up camps, weekends and hackathons. Many, if not all, of the co-working spaces and incubators host these events where (aspiring) entrepreneurs build a start-up in one weekend. These are important events to build and support the entrepreneurial community. It can be an easy first introduction for people who think of becoming an entrepreneur and it brings likeminded people from different disciplines together. It can even be a feed to the incubator.

3. Interesting models to support start-ups

There are a numerous organisations that support start-ups in Canberra, Melbourne and Sydney. We will now discuss some interesting organisations and their models:

Lighthouse Business Innovation Centre: connecting people

Lighthouse provides business advice, education, training, mentorship and networking opportunities to help start-ups in the Australian Capital Territory (ACT) commercialise their ideas and grow their companies. Lighthouse tailors their approach to meet the specific needs and current stage of business development. Lighthouse is supported by the ACT government and Epicorp, the former incubator in Canberra. Because of the financial support they are able to offer most of their services for free, which makes them quite unique. Apart from the knowledge and expertise they are able to share, their big strength is in their connectedness. They have close relations with the government funding agencies, Capital Angels, the universities, other research institutes and industry and that enables them to connect entrepreneurs to the right people. Especially in Canberra where the start-up scene is not as developed as in Sydney or Melbourne this is extremely valuable.

Lighthouse supported this research by hosting Henk Steinz. He was able to work with them as part of their team whilst performing this research. They made an important contribution by facilitating, sharing their knowledge on the Australian start-up scene and making the all-important referrals.

ATP Innovations: economies of scale

From a clean-tech perspective, ATP Innovations is the most interesting incubator. ATP is Australia's biggest incubator with >300 people working in approximately 45-60 companies. ATP focuses on deep tech, such as bio-tech and clean-tech. The entrepreneurs in ATP are typically somewhat older and more experienced than the entrepreneurs in web/app start-ups. When a start-up is selected they can hire office space, receive mentoring and coaching and get access to events. In return ATP asks rent at commercial rates (or higher) and a 1-5% equity stake in the start-up. ATP is important for the network and credibility of the start-ups. They have good relations with government funding agents and Sydney Angels, which through good coordination increases the success of funding applications.

Ignition Labs: provide the necessary push

There are two accelerator programs running from ATP innovations; Startmate and Ignition Labs. In both these accelerators there is an investment in the start-up and intensive coaching over a three-six month period in return for equity in the start-up. Ignition Labs is a niche incubator in deep-tech. They ran a clean-tech round in 2012 and a med-tech round in 2013. Apart from the obvious benefits of an accelerator program (investment, coaching, exposure, peer support, credibility, etc.) the accelerator works as a huge validator and confidence booster for the founders of the start-ups. *"With an accelerator it is something that you've been working on and you need the stamp of approval from an accelerator to stop consulting and work on the business full time. It makes me confident that I got picked by these* *twenty people[…] I might fail, but hopefully I get enough traction. But people can't tell me I was a fool, because I was picked. That's a big part of the accelerator value proposition."*

Acceleration programmes are typically about three-six months and end with a pitching tour around Australia and the US. The pitching tour provides exposure for the start-ups, network building and possible follow on funding. Thereby it is a moment to work up to and get motivation from.

Pollenizer: co-found and enable entrepreneur to focus

Pollenizer is constantly changing its model, taking into account the lessons they learn on the way. Pollenizer uses a co-founder model, i.e. they become a co-founder in the start-up and thus work with the company in an intense way and take a corresponding equity stake. That also means that they can only work with a limited number of companies at the same time. The investment is high, as is the potential return on investment.

For example: A founder can come into Pollenizer with a business idea but no technical skills. Pollenizer will then find a co-founder with supplementary skills in their team or in their network. Thereby the Pollenizer team will take care of the 'distractions' such as finance, legal and even design so that the founders can focus on the core. Another option is that the founders of the start-up are tied to a full time job and that Pollenizer will find a whole team, including CEO to run the start-up. The original founders can take a seat on the board.

Because of the limited number of start-ups at a time, the intensity of working with the start-up and the associated resources invested, it is not attractive to spend too long on one company. It is their aim to build assets as good and as quick as they can and make an exit to be able to reinvest those resources in a new start-up.

Fishburners: homogeneity by niche and selection

Fishburners is a niche co-working space especially for tech-entrepreneurs and one of the largest in Australia. The requirements for renting a desk is that you work on a tech start-up and if the company has employees the founder has to work from Fishburners as well. Start-ups, inside as well as outside the co-working community, are supported by events like meet-ups, Startup Weekend and Hackathons, but most importantly by the community itself. There is a culture of sharing knowledge, skills and experience. Co-workers who would only use Fishburners and its members without giving back to the community are not accepted.

The York Butter Factory: provide the right ecosystem

The York Butter Factory (YBF) is a co-working space for digital media and web entrepreneurs. The co-working space is operated by the Venture Capital firm Adventure Capital. YBF is part of the ecosystem that the founders build around Adventure Capital. The idea is that aspiring entrepreneurs come in through Silicon Beach, join a Startup Weekend hosted by YBF, than maybe start co-working there and if things go well get funding through Adventure Capital or Aurelius Digital, the related Angel group.

The co-working space provides Adventure Capital with insight in how the start-ups perform before they make the decision to invest or not. By providing the start-ups with the right ecosystem and contributing to the broader start-up scene in Melbourne, Adventure Capital also want to increase their deal flow.

Sydney Angels: enable investment

Sydney Angels is an Angel group; a network of High Net Worth Individuals (HNWIs) that invest in start-ups. Angel investors can be very important for a start-up. Angels usually invest in start-ups that operate in an industry they understand and feel comfortable in, typically because they have a background in this industry. Besides the financial investment, the angel can bring his expertise and network into the start-up, often by taking a seat on the board. There are also investors that are appealed by the investment opportunities in early stage ventures but lack the ability or confidence to make the investment themselves or don't have the time to assess the companies or sit on their boards. Those type of investors can invest in Sydney Angels' sidecar fund. If two or three Angels in the network decide to make an investment, the sidecar fund can match those funds or invest a percentage of that amount. Investment in the sidecar fund automatically leads to a diverse investment portfolio.