Ventureburn survey sheds light on SA's tough, but pioneering startup industry

By Jacques Coetzee

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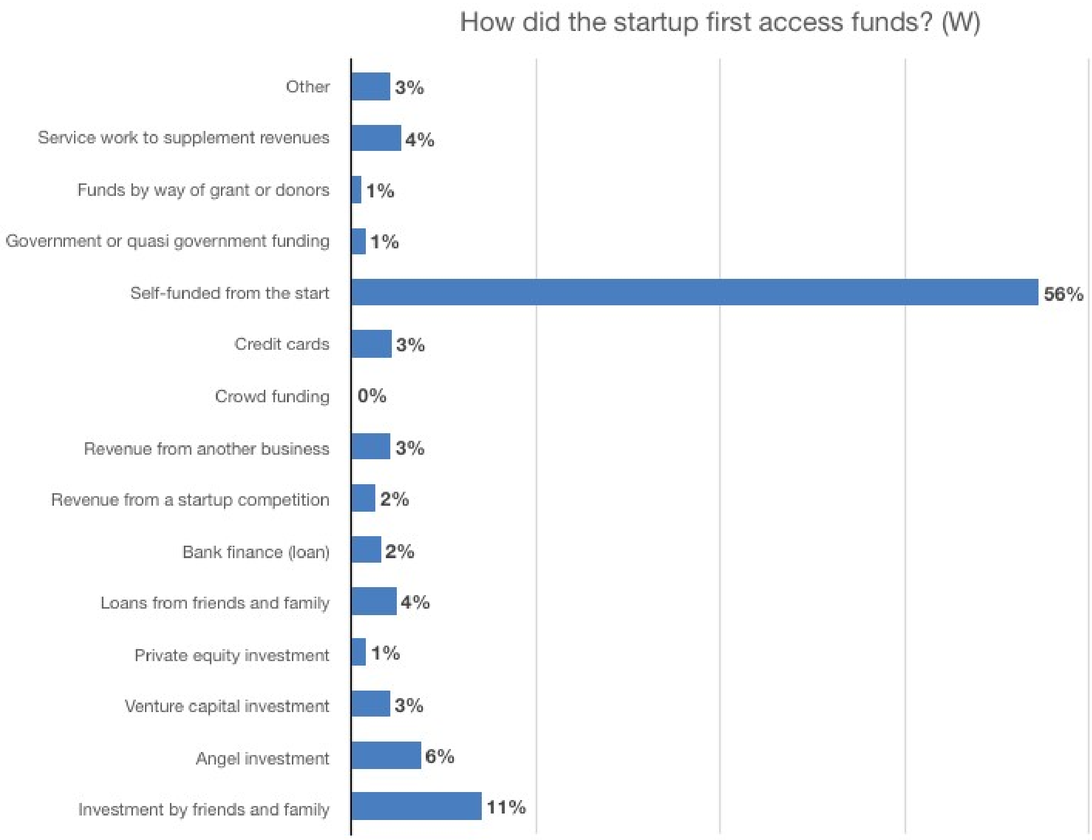
South Africa's Startup industry isn't always as glamorous as it's sometimes made out to be, according to a new survey by Ventureburn. Employees and founders of startups are often paid below-market salaries, get close to zero benefits and are subject to high-pressure environments. Moreover, just 17% of startups are profitable, with only three percent of startups making it to the sought-after venture capital investment stages.

But this begs the question: why is creating and working for startups an increasingly popular option? Although entrepreneurs will make it big if their startup succeeds, making money doesn't appear to be the primary driver for many of them. The survey reveals that entrepreneurs are generally driven by the need to 'innovate', 'be a pioneer', or for reasons of 'personal development'. Many also start their own fledgling companies because they have spotted a 'gap in the market'.

These are the findings of a new Ventureburn survey, which aims to reveal the 'true picture of SA's startup landscape'. Another key finding of the survey is that the startup industry has seen a surge in black entrepreneurs, more than that recorded by any other startup survey to date.

The Ventureburn Startup Survey partnered with First National Bank (FNB), investment advisory firm Clifftop Colony and analytics company Qurio to poll just under 200 tech startups. Each of the startups was asked 42 questions, ranging from funding, the profile of their founders, to their revenues and the everyday challenges they face.

The survey defines a tech startup as a company with annual revenues below R20 million, and staff numbers of anywhere between 1 and 100. The survey sample size assumes a population of 5,000 tech startups in South Africa, with a 95% confidence level and a seven percent margin of error.

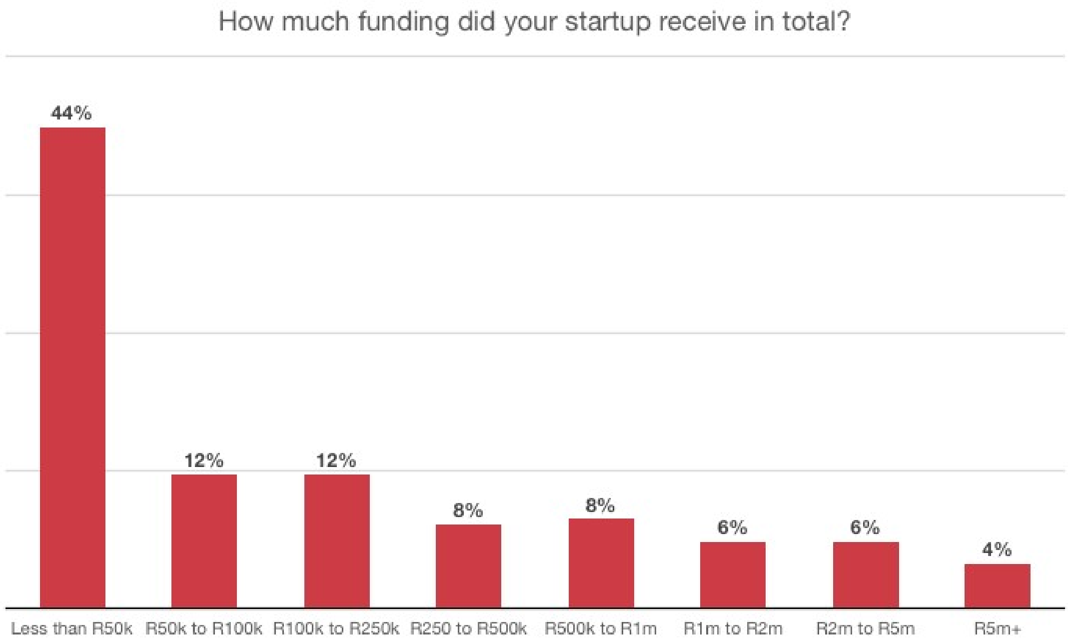


Bootstrap nation: funding one of the biggest challenges

Funding has always been one of the biggest challenges in South Africa's startup space. Various reports from Ernst & Young to the Omidyar Network would tell you that a lack of financial support is crippling the country's entrepreneurs. The survey confirms that this is still very much the case.

Nearly half (43%) of all South Africa's tech startups find access to funds their biggest challenge. Bootstrapping remains the most popular way to raise initial funds (56%), followed by investments from friends and family (11%), which is in line with the "friends, family and fools" investment adage. But just because they're friends and family, doesn't mean they're fools. This group is more likely to invest directly than hand out loans (4%).

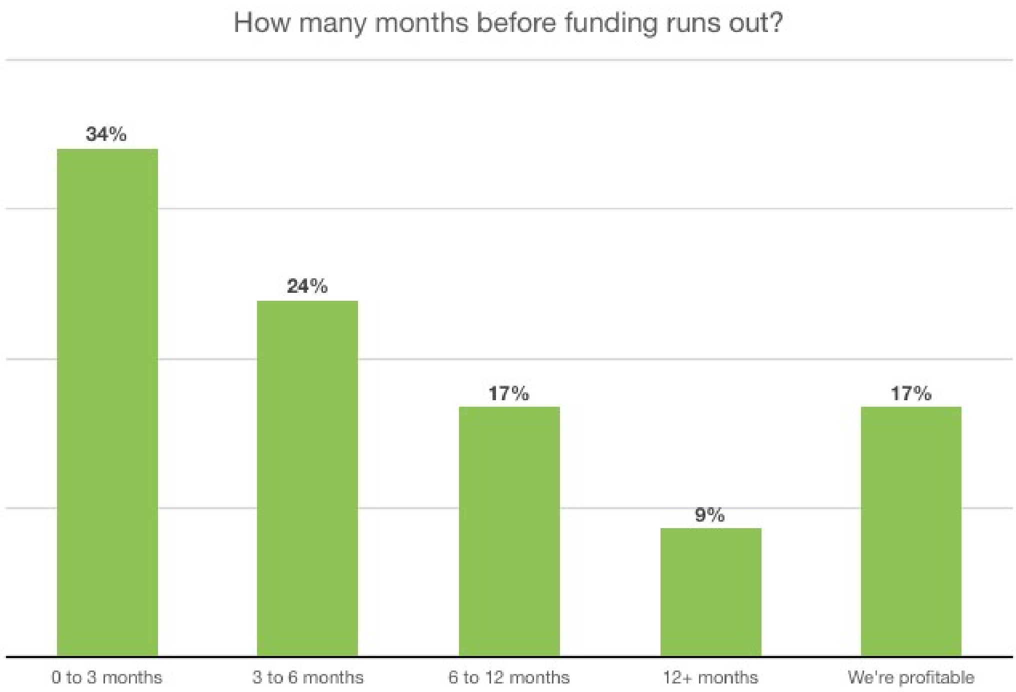
While angel investors, venture capitalists, and private equity firms grab all the headlines, the survey suggests that very few go on to make it to these rounds. In fact, just three percent of startups make it to the venture capitalist stage in their funding evolution.



Interestingly, credit cards (3%) are more popular than bank loans as funding channels. Bank loans are one of the least popular sources of funding (2%), which comes as little surprise given the perception that banks are well-known as a "no-go" as a source of funding to startups.

While crowdfunding often grabs the headlines as a funding option, the survey indicated that this type of funding is simply non-existent in South Africa, with exactly zero entrepreneurs indicating that they've used this as a funding source.

Even when startups do get investment, the amounts aren't generally that large. The bulk (44%) of the country's startups received investments totaling less than R50,000.

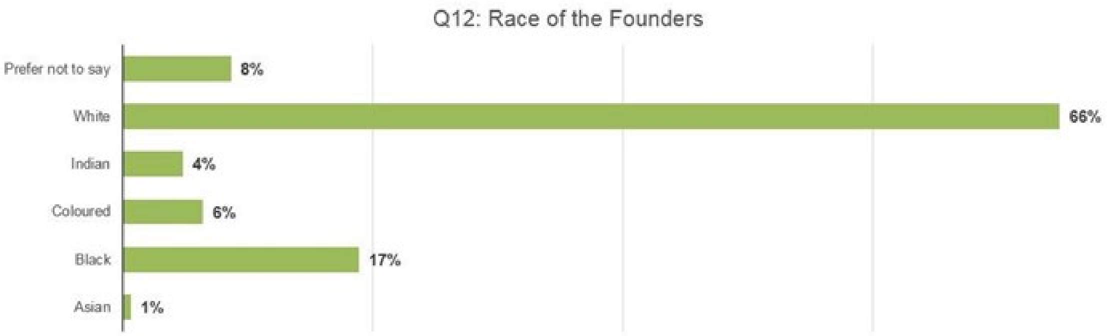


Despite the apparent propensity for bootstrapping, only a third of the companies say they are not looking to raise funding within the next three years. Of those looking for funding, most (45%) hope to raise between R1-million and R25-million within this period. A select few (6%) want a R25-million-plus payday.

Although the survey indicates that very few go on to make it to the venture capital, angel investor, and private equity investment rounds, just over a third of startups indicate that they hope to tap these for future investments.

A question of revenues

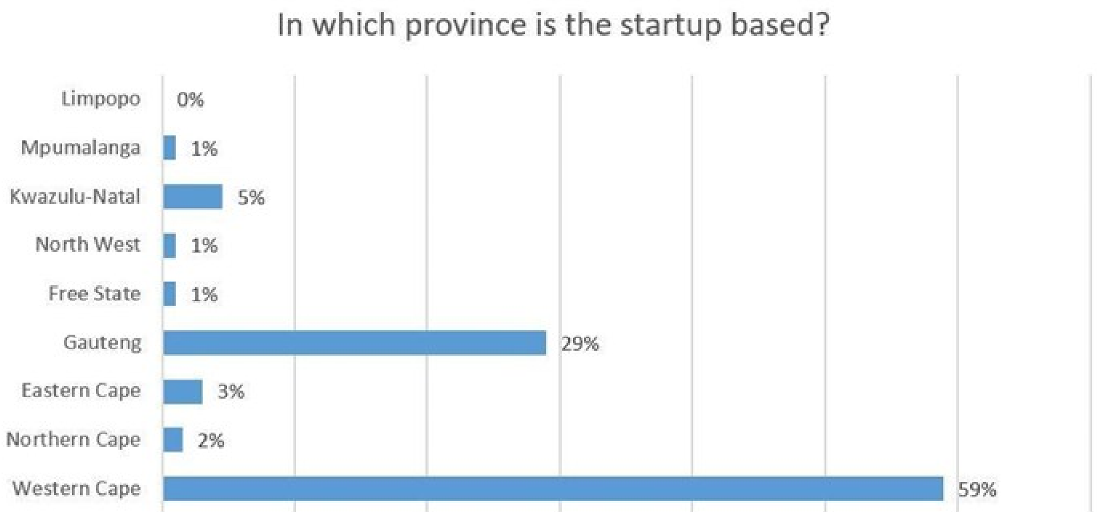
People might not get into the startup game to make money, but without revenue, a business is dead in no time. For an alarming number of South African startups this is a looming reality. A sizeable 75% of startups said they would run out of funds within the next 12 months, with 58% of those indicating they won't last longer than six months.



That makes sense when you consider that just four percent of startups generate more than R5 million in annual revenue. The vast majority meanwhile (58%) bring in less than R100,000 a year. A further 30% of the startups generate revenues between the range of R100,000 and R1-million per annum.

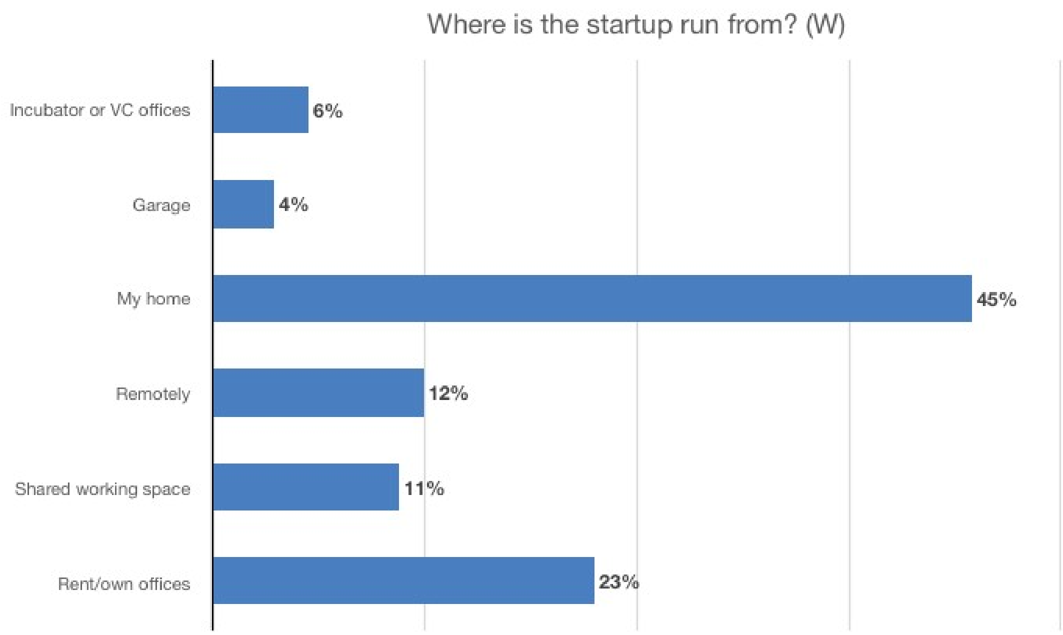
Startups are becoming more diverse

It looks like the "white, male" face of the South African startup space may be on its way to becoming more diverse, according to the survey results. The survey indicated that 17% of startups in the country had black founders. This is a significant increase from a national survey undertaken by the Silicon Cape Initiative in 2012 where just over six percent of startup founders were black.

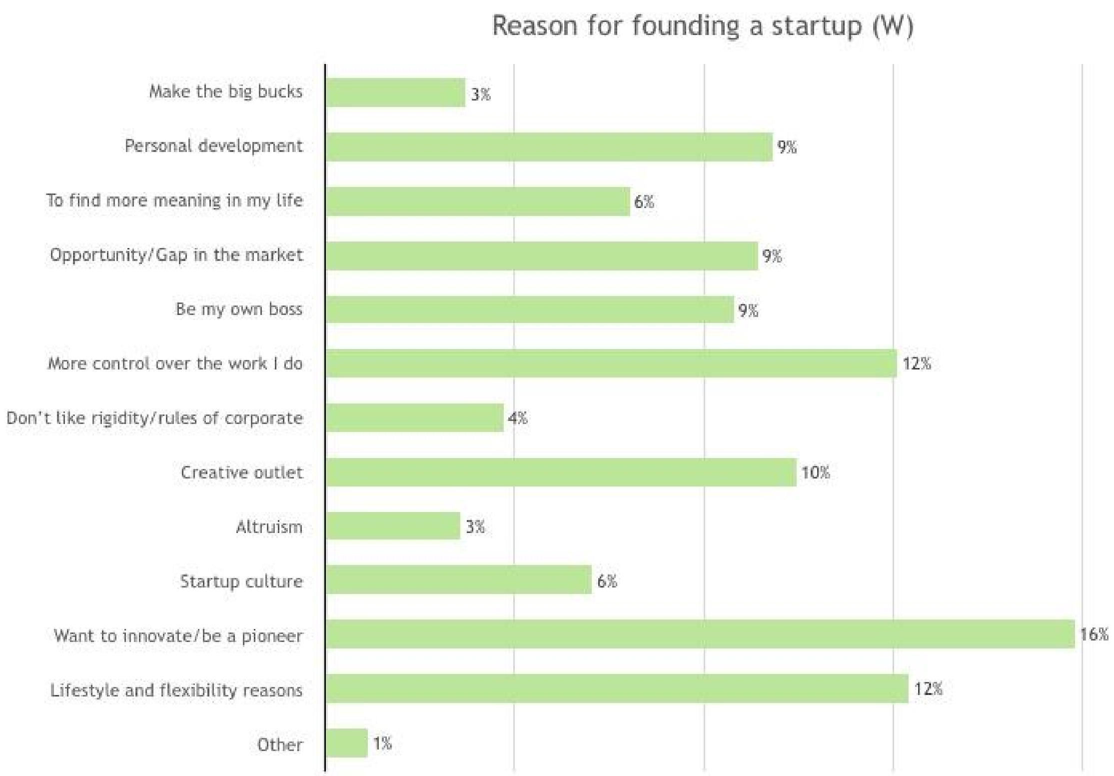


More still needs to be done when it comes to achieving gender parity, with the survey indicating that only six percent of the country's startups have female-only founders. By comparison, 68% of startups have male founders while 27% are run by combined male and female founder teams.

The Western Cape is often referred to as South Africa's Silicon Valley or the "Silicon Cape". The survey substantiates this claim as nearly two-thirds of the country's tech startups are based in the Western Cape (59%), followed by Gauteng (29%) and KwaZulu-Natal (5%).



Just under half (49%) of startup founders prefer to work from home or their garage. That's in line with the image of some of the world's most renowned startups beginning life in people's kitchens, lounges or garages. The next most popular place to run a startup from is an office (23%), with 12% running their companies remotely.

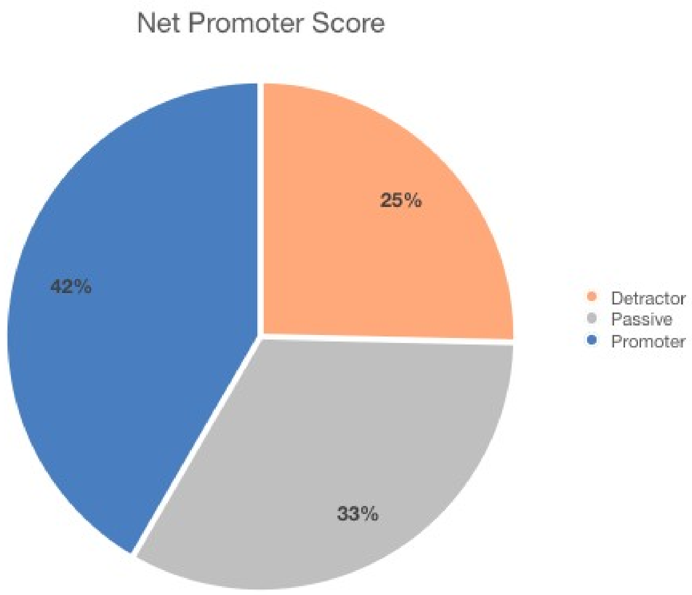


BEE compliance amongst startups is low. The majority of companies surveyed are non-compliant or do not know their status. Just under a quarter of startups are Level 4 compliant, which is not surprising considering this status includes companies with less than an annual turnover of R5-million or those less than one-year-old.

What gets startup founders ticking?

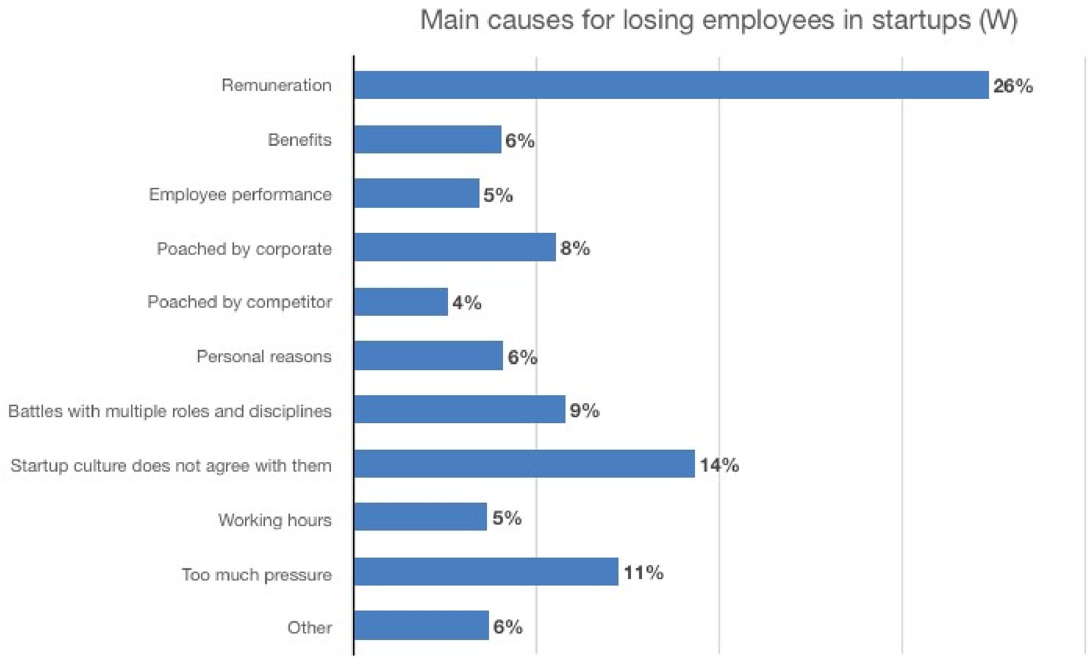
While multi-million dollar investments and funding rounds get a ton of attention, they aren't actually the reason most South African founders start their businesses. The survey found that the need to "make the big bucks" (4%) are not the most popular motivators in the industry.

Tech startups are instead driven by the "want to innovate", "be a pioneer" (15%) and to find "opportunity", or exploit a "gap in the market" (17%). The next most popular motivations for creating a startup included "personal development" (9%), "be my own boss" (9%), "lifestyle/flexibility reasons" (9%), "creative outlet" (8%) and "more control over the work I do" (8%).



This question has been weighted according to how many options were chosen by respondents. The more options chosen, the less they count.

Seventy percent of startup founders have a corporate background and only four percent of those would consider going back. Despite the obvious stresses, only 25% of the entrepreneurs would not recommend the "startup lifestyle" to other people. Some 42% consider themselves promoters of this lifestyle with a further 33% sitting on the fence.



Employees struggle with wages, startup culture

While entrepreneurs are overwhelmingly positive about startup life, things are decidedly less glamorous for their employees. Nearly 40% of tech startup employees are either volunteers or get paid salaries that are below the market average.

That seems like a recipe for disaster given the survey's finding that remuneration (26%) is one of the main reasons for losing employees in a startup. This is followed by "startup culture does not agree with them" (14%), "too much pressure" (11%), "battles with multiple roles and disciplines" (9%).

	"Successful"	Other
Kind of business		
Service orientated business	67%	31%
Have own product or IP	24%	47%
Business type		
B2C	21%	61%
B2B	79%	38%
Age of business		
Over two years	58%	23%
Biggest challenges		
Raising enough funds/access to capital	12%	49%
Method of funding startups		
Self-funded from the start	72%	53%
Reason for founding a startup		
Opportunity/Gap in the market	9%	19%
Lifestyle and flexibility reasons	12%	8%
More control over the work I do	12%	7%

"Successful" startups are classified as those turning a profit. Out of all the respondents, 17% of the companies fall into this category. "Other" indicates startups which are currently not profitable.

If you're looking for a pension you probably won't find it at a tech startup. None of the companies surveyed offer pension plans. Medical aid isn't all that common either, with just two percent of companies offering it as a benefit. The most standard office benefits are those of "coffee" and "lunch and office perks" (18%).

One way startups can look to solve the issue of low pay is to reward employees in company shares -- a trendy method of remuneration in Silicon Valley. Yet only eight percent of South African startups reward their employees in shares.

What makes a 'successful' startup?

If you could bottle the secret to startup success and sell it, you'd probably be one of the richest people on the planet. The survey sheds some light on what the most successful startups have in common. Ventureburn looked at what the profitable startups were doing differently from the rest, and found the following:

• While the majority of all startups surveyed have their own product or IP (43%), the profitable companies surveyed tend to be service-oriented. Some 67% of the companies reporting profit "sell hours". This may be due to two major reasons. One, that startups that have their own IP (and which have the potential to be bigger, more scalable business than service startups) are not initially profitable in the early stages and take a long time to show profitability. Or two, and controversially, it may also show that South Africa's market is more conducive to service startups rather than IP-play startups which are the type of startups more prevalent in Silicon Valley.

• Most (58%) of the profitable companies surveyed have been operating for more than two years.

• Motivated by gap/opportunity in the market doesn't necessarily mean profit. Likely more challenging pursuit.

• Of all the startups that reported profitability, 72% are self-funded, adding weight to the belief that lean and efficient operations from day one forces companies to perform. This is followed by bank loans (6%), "investment by friends and family" (4%) and "loans from friends and family" (4%).

• Only nine percent of successful startup founders are motivated by "opportunity" or a "gap in the market" compared to 19% of those non-profitable. "Lifestyle and flexibility reasons" (12%) and "more control over the work I do" (12%) are the most popular drivers among successful startup founders.

Finding focus: where are SA's startups putting their energy?

"Think global, act local" has become something of a buzzword in the startup and marketing world. But are South African entrepreneurs following through?

The survey found that only 15% of the startups focus on the global market. The South African market is the most popular, with 65% of startups focused locally, while 13% are taking on the African continent. Developed markets like North America (2%) and Europe (3%) have low appeal.

The majority of startups (41%) plan to dominate their target markets, with over half estimating those markets to be worth more than R100-million per annum.

If they're to achieve that dominance, marketing is crucial. But startups often don't have money for this, leading to the rise of the growth-hacking phenomenon. This holds true in South Africa, with most startups reporting that they rely on "word of mouth" (24%) or their "personal networks" (19%), which are the cheapest forms of advertising.

A further 12% of the startups surveyed say they use "organic social media" content while nine-percent rely on "paid social media advertising". Fewer startups indicate they look to conferences and events (8%) and PR and media interview (7%).

Stuart Thomas, Matthew Buckland and Graham van der Made contributed to this article.