Italian Startuppers, Time to Polish Your Act

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IN ITALY, THERE IS A DEARTH OF INVESTMENT IN STARTUP COMPANIES. NEW ENTREPRENEURS SHARE PART OF THE BLAME, THOUGH, BECAUSE THEY OFTEN PRESENT UNSUSTAINABLE BUSINESS MODELS, SHAKY TEAMS, AND MODEST GROWTH AMBITIONS TO INVESTORS. TO REVERSE THE TREND, LET'S START FROM THE TOP

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Working with Italian startuppers, I often hear that they have trouble finding people (angels) and entities (funds) prepared to invest in the early stages of a firm's life, when the business model is not yet consolidated, and revenues (if any) are still low. Startuppers who feel unlucky to have their fledgling companies based in Italy have a point. According to EY/AIFI data, Italian investment in startups in 2015 amounted to less than €100 million in 2015. By comparison, German, British and French funds invested more than €5 billion. This big difference in capitalization, liquidity and cash flow puts Italian startups at a disadvantage, also because their venture capital is mainly local. But the fact that investment deals are not done through specialized actors, such as institutional investors and business angel networks, does not necessarily mean the money is not there.

Italian companies, even established ones, heavily rely on private financing and banking loans. The problem is that these channels are hard to reach for startups. However, while Italian startuppers have grounds to complain, it is also true they are doing themselves no favors by not doing the things that would make them attractive in the eyes of the few Italian angel investors that do exist. Three are the most common errors that Italian startups do.

First item on the list has to do with unsustainable business models. There is a widespread misconception that the money of investors is needed to cover structural losses in the business. This isn’t true. A startup looking for an investor must present a sound business model and organizational structure which comfort the view that the business is sustainable. If the cost of acquiring a new customer is €30, the startup must show that revenues per customer exceed that figure. Otherwise there is no margin for growth. Often, a startupper will claim that the difference between cost of acquisition (CPA) and earnings (lifetime value) is to be financed by investors. This is an error: investors put their money in financing growth.

Second, the lack of a committed team. A business achieves results and creates value through the execution of ideas, and the implementation of strategies and action plans. For this, motivated people are needed. The value of a startup lies not in the idea, but in its execution. Often startuppers instead present to investors while they still lack a full, motivated and strong-willed team. Maybe a startup hasn’t yet found a good coder, or the sales person has another full-time job and cannot devote 100% of his worktime to the startup. In a business like that people won’t invest, because it does not deliver results.

Third, the potential market is too small or growth ambitions are too modest. In other words, Italian startuppers tend not to think big. An investor will invest in a business that’s realistic (i.e. that has sustainable unit economics and a solid team), only if there’s also the opportunity of big returns. Such returns cannot be expected from a market generating €30,000 in the first year of sales, €80,000 the second, and €150,000 the third. This is a business with no great pretensions. No matter if a startupper asks an angel investor for fifty thousand, five-hundred thousand, or a million euros, the business should be able to deliver a return that is 5 to 10 times the capital borrowed.

In conclusion, we can lament the predicament of startups in Italy, but since we still make many mistakes that, unlike structural problems, it’s in our power to correct, let’s start by fixing fix what we can.