

# START-UP –FINANCING IN FINLAND

Case: Funding opportunities and best practices in utilizing them for new ventures based in Jyväskylä

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Abstract <p>This thesis was assigned by Protomo Jyväskylä. The aim of this bachelor's thesis is to examine start-up companies and find ways to help them realize the possibilities to finance their companies in all stages of the process.</p> <p>The reasons for the research are to create value through different types of financing. The thesis is aimed at start-up companies to help them through the process providing background information on different local and national support organizations.</p> <p>The research focused on the seed, 1<sup>st</sup> round and 2<sup>nd</sup> round of financing, problems and solutions. Research results include steps which entrepreneurs should take to have the best possible chances of receiving financing from an investor. This information was collected through qualitative research using interviews in person, on Skype or over the phone.</p> <p>The research reveals multiple sources of funding and support available in Jyväskylä. It also informs the reader on the interests of investors and advises future entrepreneurs on what to do and not to do.</p>		
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Tiivistelmä <p>Tämän opinnäytetyön toimeksiantajana toimi Protomo Jyväskylä. Opinnäytetyön tavoitteena on tutkia miten start up -yrityksiä voitaisiin auttaa ymmärtämään erilaisia rahoitusmahdollisuuksia yrityksen kaikissa vaiheissa.</p> <p>Tutkimuksen perusteena on luoda yritykselle arvoa erityyppisillä rahoitusmahdollisuuksilla. Opinnäytetyö on kohdennettu start up -yrityksille ja työn tavoite on toimittaa yrityksille taustatietoa erilaisista paikallisista ja valtakunnallisista tukiorganisaatioista.</p> <p>Tutkimus keskittyi siemen vaiheeseen, ensimmäisen sekä toisen kierroksen rahoitukseen, ongelmiin ja ratkaisuihin. Tutkimustuloksista tulevat esille vaiheet, jotka yrityksen tulisi käydä läpi, jotta sillä olisi parhaat mahdollisuudet saada rahoitusta. Nämä tiedot kerättiin tekemällä kvalitatiivista tutkimusta haastattelemalla rahoittajia sekä yrittäjiä henkilökohtaisesti, puhelimitse sekä Skypen välityksellä</p> <p>Tutkimus tuo esiin useita rahoituksen ja tuen lähteitä Jyväskylässä. Se myös informoi lukijaa rahoittajien kiinnostuksista ja neuvoo tulevaisuuden yrittäjiä asioissa joita kannattaa tehdä ja joita kannatta välttää.</p>		
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# 1. INTRODUCTION

During the autumn of 2012, the author decided to go forward with his long term desire to conduct a research concerning the financing of a start-up company. Some friends of the author have built their businesses from an idea to an actual company. It seemed interesting to know how this is possible and the results of the thesis could even help others to avoid financial barriers. After beginning the research the author soon realized the overwhelming amount of available data on the subject and defined it strictly to include seed, 1<sup>st</sup> and 2<sup>nd</sup> round of financing. The first part of this thesis focuses on the descriptive, secondary data collected from dozens of different sources. The author wanted to add the possible support organizations as the research suggested it would be wise for a start-up to use such services.

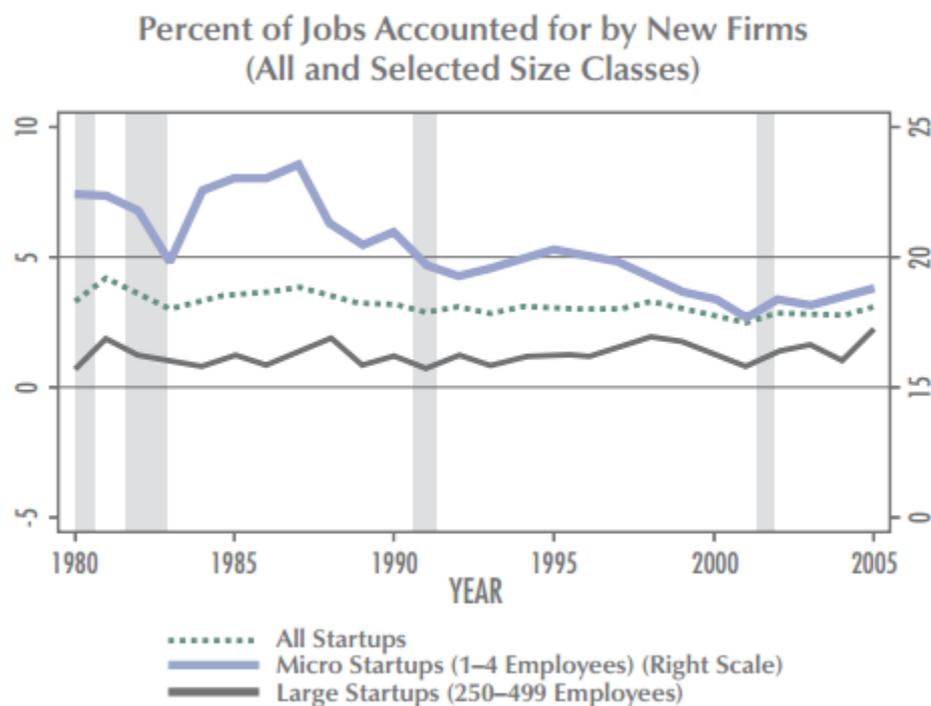
The need for such a research was great as the moment the author told other people about his idea; he received a lot of feedback for the usefulness of such a study. That is why the author decided to have a slight focus on the Jyväskylä region.

The regional discussion about new innovations fuelling the national economy is ever growing, and the discussion has encouraged more and more people to create new products and enterprises. Many of these enterprises have failed in their road to success, growing the need for support organizations in Finland. In the latter part of this thesis the author uses a normative, primary data based, research methods in attempt to help future enterprises.

## 2. RESEARCH FRAMEWORK

### 2.1 Research Problem

The purpose of the research was to explore how to create more value for each start-up. Furthermore, how this value could be turned into words in a pitch and how this value would be better appreciated by a potential investor. The problem today is the declining number of start-ups each year. As shown in from Figure 1, the total number of jobs has declined by about 20% from the best years during the late 80s. Reasons behind this decline are unclear. A recent paper by Teresa C. Fort suggests the most recent decline is due to the 2008 housing price bubble.



**Figure 1: Total number of Jobs Accounted for by New Firms (US. Government Consensus Department, 2005)**

## *2.2 Research Questions & Objectives*

The research questions are quite straight forward and linked to the objectives.

- What kind of financing options are there?
- How to make sure more start-ups survive the “valley of death”?
- What are the start-ups doing wrong and how to spark more investment from Angel Investors and Venture Capitalists?

The objective of this thesis is to increase the number of start-up companies that receive funding. Whether the funding from a private or the public sector, the aim is to give financial advice to people who are becoming entrepreneurs. Another objective is to prepare start-ups for the 1<sup>st</sup> and 2<sup>nd</sup> round of funding by Venture Capitalists (VCs), Angel Investors and syndicates.

### ***2.3 Research Methods***

The Interviews used were standardized and tailored for the study with strict questions directed to a specific group of people. The general set of questions did not work as a template for all focus groups. Both parties, Investors and Start-ups, were interviewed anonymously. This was done because the VCs did not want to be held liable by their supervisors for revealing some information normally not available for the start-ups. It was important to interview the investor because they are the ones who actually know what is going wrong in today's start-ups. Investors know more about start-up financing than most paid advisors as they have to go through several hundreds of companies a year.

After seeing what kind of an approach works best for a start-up from the investor's point of view, it was clear to the author: questionnaires and interviews were the perfect approach for tackling the research problem. "Descriptive method aims to describe the nature of a situation as it exists at the time of the study." (Travers, 1978) Descriptive qualitative research was done for the background information mostly through company websites, brochures and guide-books. After the research the author found out that descriptive study was a good way to find information. "Descriptive research is an effective way to obtain information" (Monsen, E. 2008, p. 5)

The author collected data from a total of 4 Venture Capitalists, 2 Business Angels and a representative from one of the government funded investment companies. Furthermore the author collected data from 8 start-ups and 1 spin-off enterprise. The author will not reveal which entities were parts of the research as the data collection was done with the promise of anonymity and

trust. These people were chosen for the interviews through recommendations by Protomo, personal connections and networking. The primary data was collected and analysed as normative data to provide help for future entrepreneurs. According to Jacobs (1961) a normative study aims to form our "good values" into ideas. Normative studies are often combined with empirical or descriptive studies to provide a good base for analysis. (Williams 1986, 140-144)

## 3. BACKGROUND

### *3.1 Definition of a Start-up*

A start-up usually means a company, which has just started, but sometimes it is not an actual company yet. They can be defined in a few ways, but the easiest is to take a look in the growth of the company. The whole business activity of an enterprise focuses on growth. (Laukkanen 2007) Another way to define a start-up company would be through growth of revenues, but it is not as firm of a definition as growth. Eurostat defines a start-up company to have at least 10 employees and the number of employees must increase at least by 20% per year for the next 3 years. (Harri Lehtovaara, 2013)

Figure 1, in chapter 1, shows the importance of a start-up company as they generate around 20% of the US total jobs. This figure can be used as a benchmark for any other country as the USA is the one of the few countries with such statistics easily available.

### 3.2 A typical Lifecycle of an Enterprise

A typical start-up company has 5 stages. Every enterprise starts from a problem or a lack of product in the market. Figure 2 illustrates the normal lifecycle of a start-up enterprise. This lifecycle begins when the founders of the enterprise start to work on their idea. At this point the new entrepreneurs are in the valley of death. By many studies it is the toughest area to get through in an enterprises' lifecycle as they are not generating any revenues, but instead they are already using capital to fund the early stages of an enterprise. Until a start-up makes its first sales, the enterprise's revenue will turn more and more negative. At this point the seed capital from Angel investors plays a key role in turning the revenues positive.

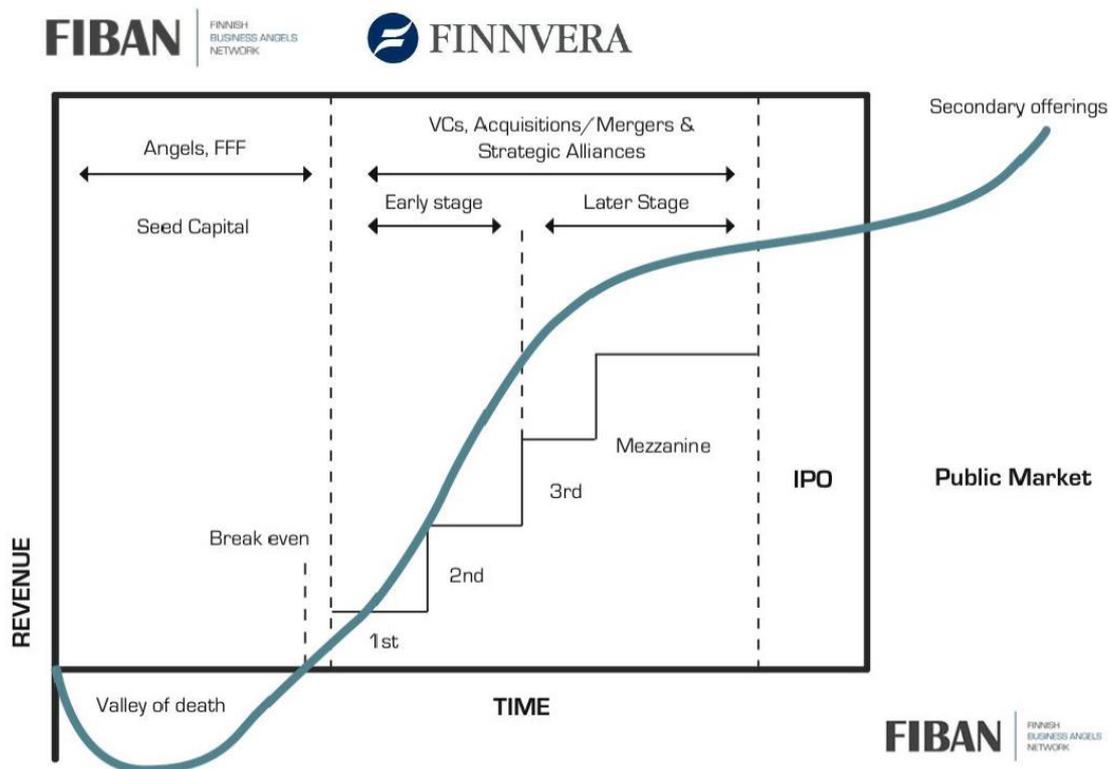


Figure 2: Stages of a Start-up company (FIBAN, Business Angel Activity in Finland 2012)

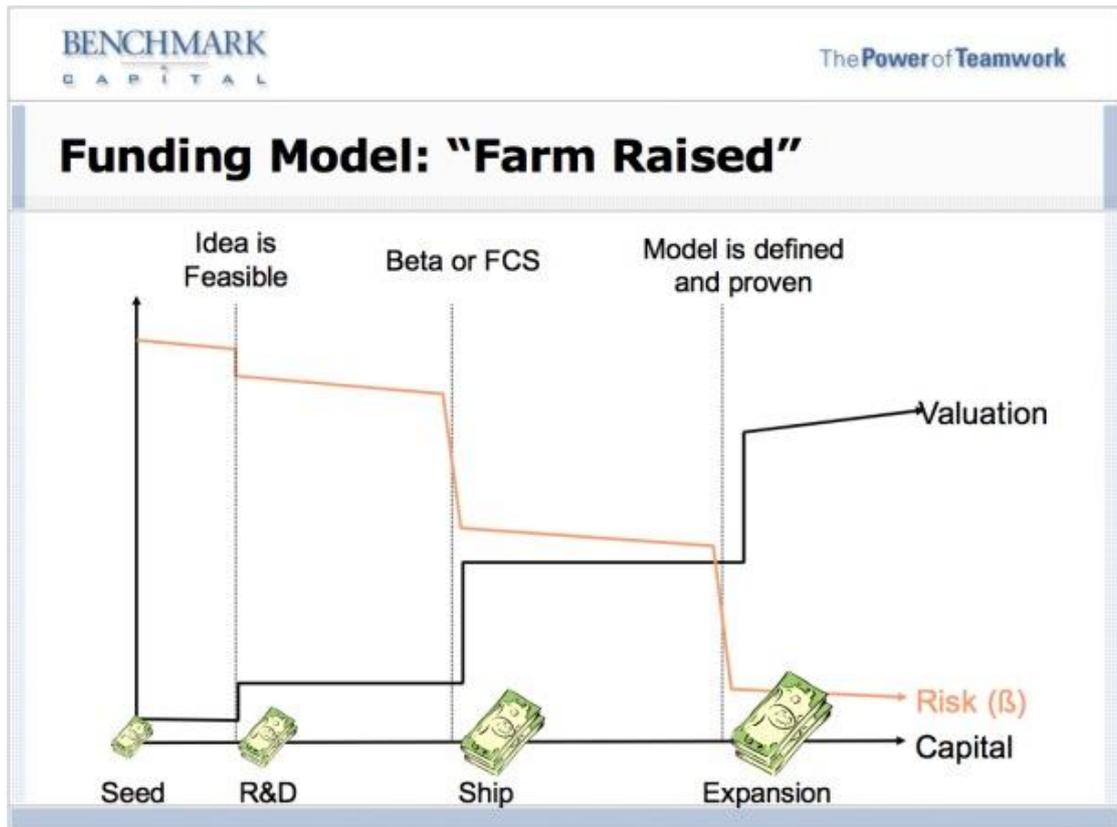


Figure 3: Funding Model: "Farm Raised" (Conor VC, 2012)

Interviews with Venture Capitalists revealed that after the enterprise has breakeven it has officially survived the valley of death. Once an enterprise has survived it enters the seed money stage. Figure 3 illustrates the different stages with piles of money. In the seed stage an enterprise does not need a big pile of money to fund its operations, but in Venture Capitalist's eyes the risk of losing that small pile is still very high. A start-up should have some revenues at this point. In Figure 2 1<sup>st</sup> and 2<sup>nd</sup> round of funding equal to the R&D and Ship in Figure 3. Venture Capitalists' interviews revealed that most enterprises ask for funding at the end of the valley of death with no revenues or even just before the idea is feasible. Often the risk is too high for them and the enterprise receives no funding. Venture Capitalists most often try to operate in 1<sup>st</sup> and 2<sup>nd</sup> round of funding for best risk-to-reward ratio.

When an enterprise starts to expand it sometimes requires a 3<sup>rd</sup> round of funding. At this point the enterprise is already well established in its region, but wants to expand its operations to other markets. Afterwards an enterprise reaches mezzanine state where it is already engaged in several markets. Interest increases and then the enterprise face the inevitable decision to go public. IPO, Initial Public Offering, is the final step in an enterprise's lifecycle as after that it can be freely traded on the stock market.

### *3.3 Path to an enterprises' value*

This section briefly introduces the different methods of funding an enterprise. We will go through public and private funding, take a brief look at most of the support organizations and alternative ways of funding. According to many investors interviewed, value does not always result from money or even from a good idea. Instead, the best value for an enterprise comes from within, the people make the enterprise what it is, and without the people and their passion the start-up might not have started up at all.

#### 3.3.1 FFF - Family, Friends and Fools

All the companies studied had used this sort of funding in the very beginning and yet, it is the most often overlooked in scientific studies. The prime source of equity for your first month or even a year is, or at least should be Family, Friends and Fools or FFF for short. FFF means basically all of the money a person can pile up from the people around him. It could be a neighbour, uncle or a Christmas bonus.

#### 3.3.2 Starttiraha

Starttiraha refers to the sum of money given to an individual to start up a company. The purpose of this government aid is to support the individual during the time he or she is not earning any money from the start-up. It can be paid for up to 18 months, and it ranges from 32.46 euro/day up to 51.94 euro/day depending on the case. (MOL 2013) Often an entrepreneur goes

through an entrepreneurship course through a TE-office. Anyone can apply for the Starttiraha, and it can be done easily online or directly at a TE-office. (MOL 2013)

### 3.3.3 Protomo

Protomo is a relatively new support organization in Finland. Protomo is a business development community for start-ups in Finland, but they also offer a small amount of funding for certain companies. They help you with setting up your company; partner your business with a pool of talent available to help you. (Protomo 2013) Protomo makes an idea commercially viable with the start-up enterprises, which will at the end, stand on their own feet. Protomo's goal is to provide support with local and networking services. (See Figure 3) They provide new start-ups with facilities where they can work on their project. They provide support in pitching your idea to potential investors through experience and the support of the community. The services of Protomo are free, but potential advisory services are paid.



**Figure 4: Protomo support circles**

Protomo will sign a Non-Disclosure Agreement with all its community members, stating that everything you hear on the Protomo premises is confidential. That is a great legally binding contract that brings the community together. Protomo also makes a plan with all the new start-ups and signs a contract including all the small details you wouldn't even think about yourself. It helps starting entrepreneurs to take the first legal steps of their company, protecting their intellectual property and thus making sure one of the founding members does not run off with the business idea. (Personal research, 2013)

### 3.3.4 Luotsi

Luotsi is a part of the support group in the same way as Jykes, Protomo or Uusyrityskeskus. What makes Luotsi different is that it is supposedly has all of the regional support services under one roof. Luotsi offers a comprehensive

set of support measures for existing companies struggling to expand.

Uusyrityskeskus in the Central Finland region works as a part of Luotsi, under the same roof which fits its slogan “all of the services you need under one roof”. (Luotsi 2013) It even has links on the website to the start-up guide made by Uusyrityskeskus.

### 3.3.5 Jykes

Jykes is one of the localized, county owned economic development companies. The goal of Jykes is to develop the Jyväskylä region to be more international and successful. Jykes owns a subsidiary called Jyväskylä Innovation, which is a development company centred around on technology companies and innovation. (Jykes 2013) Jyväskylä Innovation works closely with Protomo and other support networks in the Jyväskylä region to offer a wide range of expertise. (JKL Innovation 2013) Jykes aims to help Jyväskylä Innovation in internationalization of companies. (Ilmarinen 2010)

### 3.3.6 Suomen Yrityskehitys

Suomen Yrityskehitys or “Finnish company development” is a support organization that operates in the Jyväskylä region. It has formed a contract with Jykes to provide business incubator services until the end of the year 2014. (Yrityskehitys 2013) Suomen Yrityskehitys was founded in 2005. It was meant for innovative and growth-oriented business clients. Yrityskehitys offers advisory services in terms of market research, business planning or mentoring. (Yrityskehitys 2013)

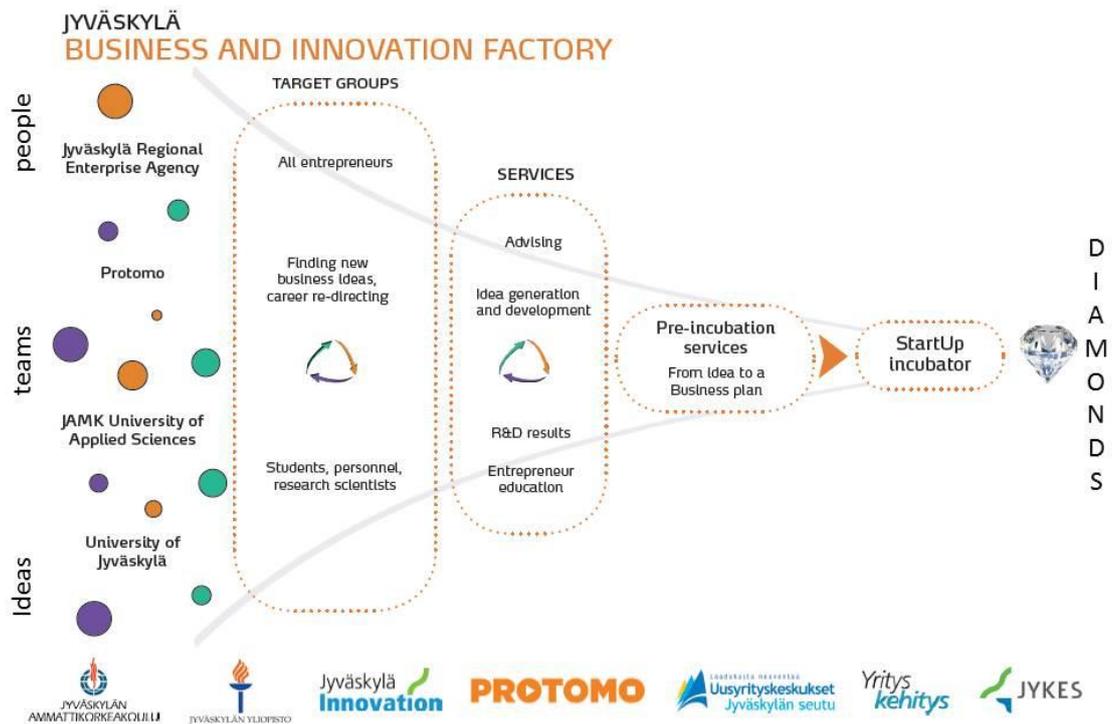
### 3.3.7 Uusyrityskeskus

The New Entrepreneur Agencies (Uusyrityskeskus in Finnish) are part of the support network created in 1989. It is not a government agency, but it works very closely with the government, big companies, funds, and other localized business incubators and organizations. The main objective of Uusyrityskeskus is to provide free information and expert advice for anyone aspiring to become an entrepreneur. Uusyrityskeskus boasts with a staggering number of 104 251 new companies set up since 1989 and only 10% of those companies have stopped within the first 2 years. In the first five years only 4% of the clients of Uusyrityskeskus went bankrupt. (Uusyrityskeskus 2013)

Uusyrityskeskus has a branch specialized for women called Women's Enterprise Agency. Their goal is to encourage women to become entrepreneurs. It is funded by private enterprises and the Ministry of Employment and the Economy. (Kärki 2013, 28-29)

### 3.3.8 Jyväskylän Yritystehdas

Yritystehdas is a new organization combining Protomo, Jykes, Suomen Yrityskehitys, Uusyrityskeskus, University of Jyväskylä and Jyväskylä University of Applied Sciences. This is basically what Luotsi has tried to achieve, but this time they have brought the local two universities in. (Yritystehdas 2013)



**Figure 5: Jyväskylä Business and Innovation Factory**

Jyväskylän Yritystehdas, or “Jyväskylä’s Business and Innovation Factory” in English, is exactly as the name states, a factory. It gathers all of the entrepreneurs and young students with ideas around the same table. The factory supports them with financial and practical advice. Once these target groups have been formed and sufficiently in the correct ways the idea is further refined in a pre-incubator. At the end of the factory a business plan is drafted and the project is moved to the start-up incubator. The end result should be diamonds!

### 3.3.9 Finnpartnership

Finnpartnership is a Finnish, nationwide, support organization. It provides financial and advisory support for any project regardless of business sector. It focuses on establishing business connections between Finland and developing countries listed by the OECD. It provides matchmaking services across all of the OECD developing countries. Finnpartnership offers all of its services for free. Finnpartnership covers up to 70% of travel expenses for SMEs during their project to a developing country. (Finnpartnership –website, 2013)

### 3.3.10 Finnfund

Finnfund is a Finnish development finance company. They offer long term finance in ventures with a Finnish interest. These ventures are strictly situated in developing countries and Russia. Finnfund is a very similar organization to Finnpartnership. Companies from any sector can apply for Finnfund financing. Enterprises are encouraged to contact Finnfund as early as possible to formulate a complete project plan. It is highly recommended for enterprises targeting a developing country to work with Finnpartnership and Finnfund. (Finnfund –website, 2013)

### 3.3.11 Keksintösäätiö

Keksintösäätiö, or “Foundation for Finnish Inventions” in English, is a foundation that according to their website “Screens and evaluates inventions and innovative ideas generated by private persons and start-up companies”

They are situated in Otaniemi, Espoo and they provide funding for private individuals and start-ups. The money received from Keksintösäätiö is called “Development money” and the main purpose of this money is to develop a product or service. (Uotinen 2013, 24) The money from Keksintösäätiö is basically a loan for 12 years, which you will have to pay back in full.

### 3.3.12 Sitra

Sitra usually funds projects that promote well-being and sustainability, but sometimes they also fund start-up companies in their 1<sup>st</sup> and 2<sup>nd</sup> round of funding. In 2012 Sitra, The Finnish Innovation Fund started a special fund called “Start-up –fund. It will hold Start-up Sauna business incubator events in the future and Slush-Conferences. Slush conferences are leading start-up conferences in Northern Europe and Russia. They often have high-end key speakers such as Prime ministers and CEOs of multinational companies. (Sitra 2013)

### 3.3.13 TEKES

TEKES is the most important public funding organization in Finland. (TEKES 2013, 4) They funded 65% of well-known Finnish innovations between 1985 and 2009. Out of the 50 fastest growing technology companies in Finland 47 were TEKES clients. The English for TEKES is Employment and Economic Development Centre, and its main objective is to increase the national GDP through innovation. (TEKES 2013, 4-18)

TEKES is deeply integrated with universities and polytechnics to fund research projects. It is publicly financed by the Finnish government. ELY centres work closely with TEKES as they provide TEKES funding through the nationwide network already established by ELY centres in Finland (Ilmarinen 2010)

#### 3.3.14 ELY –Keskukset

ELY –Keskus, Centre for Economic Development, Transport and the Environment in English, is a government organization. In total there are 15 ELY centres in Finland. Each of these centres work locally to support the founding of an enterprise, advisory services and funding. (Kiviranta 2013) ELY centres receive funding from the Finnish government and from the EU. Funding is available for start-up enterprises but also for existing enterprises to help them expand and develop. (ELY –Keskus, 2013)

ELY centres offer a variety of courses for start-ups to attend, some of which are free. These courses might help an enterprise to get a global view of the markets (Globaali -course), formulate a business plan (PK-LTS –programme) or help to plan investments (Balanssi –program). (Uotinen 2013) ELY centres a similar kind of funding to Finnpartnership in terms of Valmistelurahoitus. It is given enterprises conducting research with a global scope.

#### 3.3.15 Commercial Banks

Interviews with start-ups revealed that most of them had used commercial banks as one of their primary sources for funding in the seed stage.

Commercial bank is a term used for all banks that give out loans, accept deposits and at least some kind of basic investment possibilities. Commercial banks give out loans to start-ups and the loans are backed up by the Finnish government through Finnvera or by the entrepreneurs themselves. (Uotinen, 2013)

Some enterprises might adapt cash flow financing as a strategic decision. It is a way of a loan from a bank to generate cash flow prior to selling anything. It is often given out on estimated revenues.

#### 3.3.16 Finnvera

Finnvera is a government run organization providing financing in the seed and growth stages of an enterprise. Its objectives are to increase exports from Finland, increasing the number of start-ups and to support enterprises when there are changes. (Finnvera, 2013) Finnvera operates mostly by granting or backing loans for companies. It gets the funds from the financial markets. (Kärki 2013, 19) Finnvera is also ECA, the official export credit agency. An enterprise seeking for financial aid from them doesn't have to decide what kind of support it needs, but rather Finnvera will tailor its financing model to for the needs of any enterprise. (Lehtovirta 2013, 31)

Finnvera guarantees loans in several ways. The most modest type of guarantee is called Pienlaina, "Small loan" in English. It can be provided for anyone even if the enterprise is receiving a different type of funding from

Finnvera. Pienlaina is always between 5000 and 35000 euros. A company must employ at most 5 people to be eligible for Pienlaina (Finnvera, Pienlaina 2013) Another guarantee Finnvera uses is called Pientakaus, "Small guarantee" in English. Most of the time a company might not even know of Finnvera's involvement as they apply for a loan at any bank and the bank talks with Finnvera. (Lehtovirta 2013, 33) In Pientakaus, the company receives the funds from the bank and not from Finnvera.

Finnvera has a subsidiary called Veraventure Oy, which focuses on Venture Capital -like activities, but it also funds during the seed stage of a company.

### 3.3.17 Suomen Teollisuussijoitus

Suomen Teollisuussijoitus or TESI for short is "Finnish Industry Investment". It was established in 1995 and currently employs 29 people. (TESI -website) TESI is a Finnish government run organization, which means that they will nearly always syndicate with someone on their investment. (Interview with TESI) They invest in companies directly during the A & B round of investment, which means stages 1 and 2. They also do investing through various funds, but no seed investing. TESI takes a minimum of a 10% stake in a company when investing, but never a majority share, and often a membership on the board of the enterprise comes with it. (Interview with TESI)

### 3.3.18 Crowdfunding

Crowdfunding is a new source of funding for companies. It was started originally by ArtistShare in 2000, where artist could be funded by the fans. The success 6 Grammy awards spurred the rise of Crowdfunding websites in the late 2000s, most notably IndieGoGo and Kickstarter. I will use Kickstarter as an example. The basic idea of a Crowdfunding website is “pay first, get product later”. The website is full of enterprises trying to accomplish something extraordinary. In Kickstarter an enterprise puts up photos or a video of the project it is trying to accomplish. It puts up the number of capital it needs and the time in which it needs to get the capital. (Niznik-Klocek, 2013)

Kickstarter works up in ladders to provide any micro investor with the most appealing package for the best price. A video game is the perfect example of a funded project in Kickstarter. For 10 USD you might get your name in the credits of the game. For 30 USD you will get the game when released. 40 USD will get you the game and a beta access to the game. Paying 200 USD or more might get you to design a piece of playable content. Crowdfunding is not popular in Finland, but with a certain type of business it could be the perfect opportunity.

### 3.3.19 FiBAN & Business Angels

FiBAN is a Finnish Business Angels Network. The network covers about 450 angels around Finland. Before 2012, Finnvera also had business angel activity, but it has since moved to FiBAN in 2012. There is very little business angel literature available from Finland.

Business angels are individuals with interest in a specific business sector. They form a consulting enterprise through which they invest. Business angels are as the name states: angels. Often angels are involved in the seed stage of an enterprise. Business angels are extremely well connected and integrated with the community. The easiest way to approach a business angel is through the support network. Incubators and pre-incubators such as Protomo, Suomen Yrityskehitys and Jyväskylän Yritystehdas have connections with several Business Angels.

According to an Aalto University study Finnish business angels have a net worth between 1 and 5 million euros. To receive funding from a business angel: an enterprise must spark the angel's interest and prove its' potential. Business angels are syndicate investors which mean they invest as a group of business angels. In many cases business angels invest with other business angels to reduce and distribute the risk of investing. (Lyytikäinen, 2012, p. 5-6) Business angels do not only provide capital to keep the enterprise going, but also operational mentoring. Most business angels were entrepreneurs prior to being angels. (Mäkinen, 2013, p. 9-11)

### 3.3.20 Venture Capitalists

Venture Capitalists are the sharks of the start-up financing world. Venture Capitalists differ from business angels in couple of ways, but most importantly for the sheer amount of capital they have to invest. As already mentioned in the previous chapter, business angels have a net worth of up to 5 million euros, but the Finnish Venture Capitalists can have several funds

each worth over 100 million euros. (Personal research, 2013) They have a reputation of making deals that are not mutually beneficial, and according to several start-ups interviewed; they should be used as a last resort for raising capital. (Personal research 2013) In reality, this is not the case. Venture capitalists have the money to fund any kind of project, but they are very reserved when they invest.

Valuation is extremely important to Venture Capitalists and Angel Investors. Value of an enterprise is very often different for different people. Valuation serves a few purposes. It provides the buyer with information on the highest number he should pay. For the seller it provides the lowest possible value for the enterprise. Sometimes valuation is done by looking at an enterprise's book value, simply looking at Assets – Liabilities. For example an enterprise with total assets of 100 million USD and total liabilities of 40 million USD would be valued at 60 million USD. It is extremely difficult to show the true value of a company in the seed stages. Venture Capitalist interviews revealed that a start-up is worthless to them until it makes its first profit.

## 4. RESEARCH RESULTS

### *4.1 Data collection*

Data collection was started in autumn 2012 and it ended in autumn 2013. Primary data was collected by conducting interviews and questionnaires during autumn 2012 and spring 2013. As already mentioned in chapter 2 the data was collected from several different people totalling: 4 Venture Capitalists, 2 Business Angels and 1 Representative from one of the government funded investment companies. In terms of entrepreneurs the author interviewed 8 start-ups and 1 spin-off enterprise. The author will not reveal who took part in these interviews.

Most of the research was done in a Technopolis -Moneytalks Event. The money talks event is an event held multiple times yearly by Technopolis and it is the place where companies and investors can meet. Its purpose is finding funding and networking. The event had pitches from several companies and few introductory talks from investors. Most of the attendants were start-ups with a 15 minute 1-on-1 sessions with VCs. The author decided that qualitative data was the easiest type of data to analyse. Secondary data was collected from Protomo Jyväskylä through interviews and discussions with start-ups, from corporate websites of support organizations (mentioned in section 2) and from business angels through interviews on Skype.

## *4.2 Interests of investors*

One of the various objectives of the research was to find the reasons behind the investor's actions. Venture Capitalists interests are purely financial, but surprisingly almost unanimously they told the author about a willingness to invest. Some of the VCs interviewed revealed that the wrong VC is bad for you, instead when an enterprise is at a stage where it needs money from them they should consider the options. The right partner for an enterprise is more valuable in the long run than the wrong partner with more money.

Business angels and the governmental organization had different motivators. The governmental agency interviewed had profitability as a motivator, but also the Finnish law as they were obliged by law to improve Finnish business climate. Angel investors had a more humane approach. They responded with the usual "Capital efficiency" –story as all other investors. Furthermore they need to have an actual interest in the company, they want to help and they seek excitement in seeing the enterprise take shape and blossom. One of the angels said "Money is not my motivation or fuel. Even FIBAN (Finnish Business Angels Network) has a motive to repay the society."

### *4.3 Stages of investment*

As this paper has already covered, an enterprise needs funding at different stages of its life. The author found through research that enterprises are different and there is concept which would apply to all enterprises. All of the interviewed enterprises had used their own money for seed capital. Nearly all of them had received some funding from TEKES and ELY centre.

Not many of the organizations listed in chapter 2 were mentioned which surprised the author. Finland has an abundance of support organizations ready to help anyone wishing to become an entrepreneur. This is a big dilemma among the Finnish start-ups. Either Finland has too many support organizations and they should be unified or the enterprises looking for funding aren't looking in the right place. The latter was confirmed after interviewing the Venture Capitalists. Venture Capitalists said: "Start-ups look towards them us too easily for investments. It is almost as if they think we have the money to spend on every little company. Instead, they should develop their company first and prove their ability to make profit."

#### *4.4 Chances of receiving funding*

The research shows the chances of receiving funding from a Venture Capitalist are very slim. The chances are between 1/1000 and 5/250. The number of funding decisions per year and the number of applicants put the average percentage figure between 0.1% and 2%. (Interview results, 2013) The author believes it is not because of the low chances, but rather because of the timing when enterprises apply for the funding. One VC said: "We do not come to MoneyTalks –type events to make funding decisions, because the companies we want to invest in do not come to MoneyTalks. The companies we really want to invest in have others offering them money too." (Interview results, 2013)

Chances to receive funding from governmental agencies are relatively higher as any enterprise is eligible for Starttiraha. TEKES and ELY centres are known to give out seed funding in an early stage. Funding through Finnvera backed bank loans is also relatively easy to get.

### *4.5 Importance of Pitching*

During the research made for this paper, pitching was highlighted several times. In its core, pitching is the answer to the question “How to make the listener interested in my enterprise?” Pitching is how you present your enterprise to a potential investor.

There is not much scientific research done on pitching and this paper will not cover all the elements of pitching, because this paper focuses on generating value for an enterprise, not on how to present that value to an investor.

When asked the Venture Capitalists to describe the process from a pitch to a funding decision, most of them replied in a similar fashion. The enterprise has to know where it is financially and strategically. It needs to know where VCs are financially and strategically. Most importantly the enterprise has to have proven something, most often by breaking even or otherwise financially, before a Venture Capitalist will even consider funding. They replied “Numbers do not lie: if a company is making losses for 3 years with 0 sales it is no good” when asked about what do they specifically look in numbers before investing.

Venture Capitalists also replied with a rather interesting thought: “A successful enterprise will be able to pitch his enterprise anywhere anytime. Imagine if you were an entrepreneur on a holiday in Italy and you would happen to walk into an elevator with Donald Trump, one of the wealthiest people in the USA, what would you say? A successful entrepreneur would pitch his enterprise in the short 30 second journey and get Mr Trump interested.” When asking the entrepreneurs “How have you developed the

pitch?" the author was surprised. 90% of the enterprises had no pitch training and none of them had a third party create a pitch for them. Nearly all of the enterprises said to have made up the pitch themselves and practiced it internally before going in front of investors.

#### *4.6 Build a Dream Team to survive*

In this section we are going to take a look at a Dream team model, formulated based on opinions from different investors and enterprises. This section was formulated to answer one of the research questions: “How to make sure more start-ups survive the “valley of death”?” Two things in this Dream Team - business model are above anything else. Firstly the team behind an idea has to speak the language of the customer. The team needs to have the passion to create something out of nothing and furthermore have the passion and courage to show the world how great it is, not to forget a sense of critical thinking. The team needs to complement each other and have the competences to make an idea into a finished product. Several sources pointed out that the team needs to have a strong management structure and a very good sales & marketing department, because without sales there is no revenue.

Second, equally important, factor is scalability. It does not matter how great the idea, concept or product. If it cannot be scaled, it becomes worthless. A Venture Capitalist always looks for the ability to scale the start-up. Scalability is simply: “If one fast-food restaurant runs smoothly and makes a profit. We should be able to have 100 restaurants across the country running smoothly and making a profit” (Interviewed VC, 2013)

One of the business angels said: “You should not attempt to re-start milk production, but instead create something to “destroy” an existing market” Furthermore a Venture Capitalist noted “I do not want to invest in the fifth twitter, I’d rather invest in the first something” Investors look for patentable products. They try to see the potential in the product by looking at the team

who has invented it. "Track record" is extremely important to the investor. A brief history of an enterprise tells the investor what has happened before, what problems the enterprise might have had. They want to understand the idea of a business, even though they are only looking for capital gains.

Other things investors also look for include the following: Differentiation, marketing concept, competitiveness potential, potential momentum and "things that lower the risk level" (Interviewed Angel Investor, 2013)

### *4.7 5 Rules, 5 Steps & 5 Suggestions*

These 3 sets of 5 were designed to answer one of the research questions:

“What are the start-ups doing wrong and how to spark more investment from Angel Investors and Venture Capitalists?”

The 5 golden rules for start-up companies are designed based on the feedback and suggestions of interviewed start-ups. These rules include some things which should be avoided, but also some things which should be done to ensure an easier life for a start-up.

1. Real entrepreneurs never give up. If you want to make it, then make it! This was highlighted by one entrepreneur interviewed as the start-up he was involved now was his second.
2. “Double your capital from TEKES.” –said an entrepreneur when asked “What would you do differently?” TEKES can provide funding for an enterprise, which can effectively double a starting capital.
3. In Finland Business Angel investors are no match for an international angel. If an enterprise cannot find suitable angel from Finland, look elsewhere. Russia and Germany have a high amount of Business Angels. (Lyytikäinen 2012)
4. Be ready to pitch: anywhere, anytime. Make sure every pitch is better than the previous. Practice the pitch within the support network. Once an enterprise has received an angel investor, practice the pitch with him.

5. Conduct a feasibility study. Get feedback from customers as early as possible. Try the product with actual customers as much as possible. “Feedback is important in the early stages as it provides a psychological effect of success.

Investors were asked a question “How would you fund your company? What is the best way to do it?” Interestingly they answered with a similar 5-step plan to fund a company.

1. Step 1 was unanimous across all of the investors. Use your own capital. Working without pay has to be a viable option for some time if an entrepreneur wants to make it. Enterprises should try to push it as far as they possibly can with their own capital, only then they should go to step 2 and get governmental financing.
2. In seed stage, all of the investors suggested to get some capital from TEKES and other government agencies. Furthermore they suggested thinking big from the beginning. Forming an enterprise with a global focus and scalability is vital. Further along the lifecycle of an enterprise: these some of the traits VCs look for in a potential investment.
3. Business Angels were placed in the middle of a financing lifecycle of a company by most of the investors. Some suggested that business angel funding could be used in a relatively early stage, even in step 1 and 2. This is most often the first step of an enterprise where external non-governmental funding is needed. It was suggested by an angel investor

that also finding the right angel is important. Knowledge and experience of an industry means making it through to the next step. The aim of this funding should be to finalize a product, test it in the field and launch it to the market.

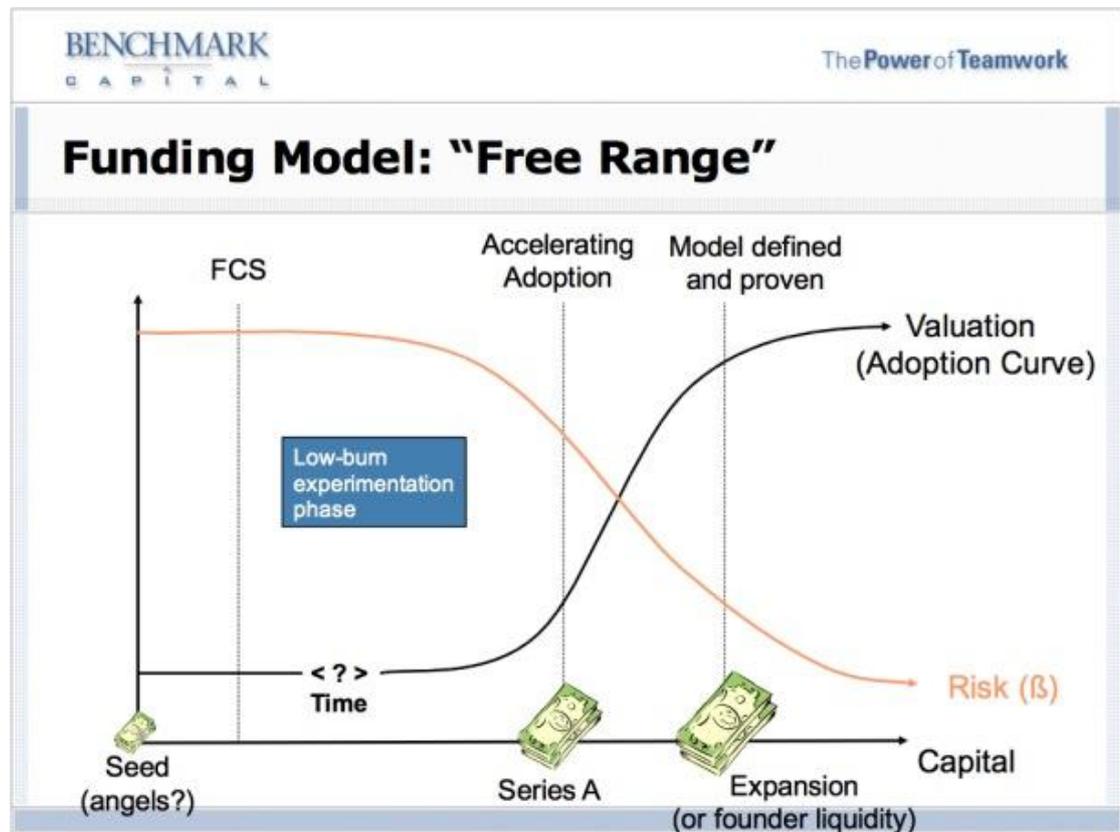
4. Veraventure or other sort of bank loan was suggested as the fourth step of funding for start-ups. This half-step in the funding process is necessary, because at this point most of the enterprises have not generated enough revenues to survive, but the enterprise is growing at a steady rate. It is not ready for Venture Capital, because it has not reached its breakeven point.
5. Venture Capitalists are the last step of the puzzle. They want a half-ready company to invest in with a good future ahead of it. The amount of capital they can provide at this point will be enough for expansion to different markets or cities. This is why Venture Capitalists look for scalability in the companies they invest in. They want growth in the next 18 months, because they want to exit the investment as soon as possible for as big of a profit as possible.

Interviews conducted were drafted in a way to allow flexible answers to questions. In the author's opinion a critical question was asked from the entrepreneurs "What would you do differently in terms of finance?" responses were astonishing. Nearly half of the enterprises said "Nothing.", which in the author's eyes seems very strange. A conclusion can be drawn from their answers – many companies think they know about financing a company and they think they have done everything as they should. This

poses a problem: Where is the ability for self-critical thinking? Here are a few key suggestions to keep in mind when starting a business.

1. Keep a close eye on the news in the start-up world. Look for events where investors are. Do not go rushing in and talking to a Venture Capitalist when you have an idea. Take it one step at a time and talk to the right people at the right time.
2. If possible create an enterprise with a team of professionals from different fields. "No sales = no manufacturing - no manufacturing = no sales." (Interviewed Venture Capitalist, 2013)
3. Network with other entrepreneurs at every chance you get. The more connections an enterprise has the more people know about the enterprise. The more people know about the enterprise the more customers an enterprise has. More you sell, more want to buy a share of you.
4. Take a close look at a website: [www.rahoituskone.fi](http://www.rahoituskone.fi). It is something the author found during the research. It is a website through which a start-up or an established enterprise can look for funding. It is very easy to use and it has a filtering possibility to leave the best possible options.
5. Do not be afraid to be an early adopter. Most of the start-ups today "invent" something that has been invented before. It is just a matter of who builds an enterprise faster, runs it better and sells more. (City.fi – blog, 2013)

### 3.8 Problems in financing



**Figure 6: Funding Model: "Free Range" (Conor VC, 2012)**

Earlier, on page 7, we covered the funding model for a typical enterprise. Today the investors face a different problem: fewer companies are typical. Internet has revolutionized the typical business model in a way Venture Capitalists had not foreseen.

The revolution has happened in the requirement for funding. A seed capital required for a two man software micro enterprise is much less than the seed capital required for a new manufacturing enterprise. This surfaces a problem for Venture Capitalists. As seen from Figure 6, the ladder up to valuation and eventually an Initial Public Offering is not a ladder. An ideal enterprise for

rapid growth might lurk in the “Low-burn experimentation phase” for years until a Venture Capitalist finds it.

Another big problem in financing is start-ups trying to jump a step or two on the ladder and falling down. More than one Venture Capitalist complained about the number of companies they go through every year, some of which do not even have a name for the company. The author hopes this thesis will decrease that number of enterprises.

## 5. RELIABILITY AND VALIDITY

The purpose of this research was to help start-ups in receiving funding and to increase the survivability rate. Qualitative research conducted was the best approach to tackle this problem. However the sample size, both entrepreneurs and investors, could have been larger. Answers in the qualitative study were surprisingly similar and in the author's opinion the research is valid. The research results can be generalized to any other city in Finland. The author had no previous knowledge of the researched subject which means his personal opinions were formed during the research.

The reliability in terms of data collection is good. It was a conscious decision not to record the interviews in listenable or viewable format. This was done simply to protect the enterprises' best interest and the investors' integrity. The results are relatively time-bound and the background information might be obsolete after 10 years. However the author believes the research results will help entrepreneurs for much longer than that.

Lastly to consider is the language. For some enterprises the author was forced to conduct the interview in Finnish. The author is not familiar with Finnish business terminology as he studied it in English. It might have an impact on the validity of the research. However the author works now in the United Kingdom and is a Finnish citizen proving a sufficient knowledge of both languages. Glenn mentions in his handbook of Research Methods: "Validity cannot exist without reliability." (Glenn, J. 2010)

## 6. CONCLUSIONS

The research studied the different methods of financial and advisory support the Finnish government provides. Furthermore the study focused more on the problem of creating actual value for an enterprise through these support networks. This paper covered these support networks in section 2.

It is important to make the distinction between these government funded support networks and the private funding options discussed in the latter part of this research paper.

Simple conclusions can be drawn from this research paper and from the amount of research conducted. Firstly the seed stage –funding is easy to get in Finland. It is relatively easily accessible through FFF, ELY centres, TEKES and Business angels.

Secondly Finland is filled with different support networks all claiming to do the same thing: provide facilities, advisory services and expert planning. This support network is extremely extensive and good, but it is, at the same time, exactly what is wrong with it. The network of government –supported agencies, incubators, pre-incubators, start-up events is simply too big. It is not appropriately unified under a single decision-making body or even a single name. This creates confusion and, in some cases, it might even be paralyzing for an enterprise.

Lastly the image of Venture Capitalists is distorted. Often people do not see the facts. They are very careful about when they invest, but when they do, they do it big. They are still sharks, but not the kind of shark one should be afraid of.

## 7. SUGGESTIONS FOR FUTURE RESEARCH

Further research should be done in pitching as the author feels it is underrated by enterprises of today. The author would like it to be researched further, for example “How pitching affects the chances of receiving finance?” Second area of research is valuation. The author researched valuation for the purposes of this research, but due to limitations made in the beginning of the research was not able to put as much focus on it as it required. There are plenty of valuation books by renowned authors, but very little research has been done how to improve valuation in the later stages of an enterprise? Business Angels were researched for this paper, but there are no thorough research papers done on business angels alone. The author would like to see a research about the roots of a business angel, what sparked them to help others and what keeps them going today? Interesting research topic including the Venture Capitalists could be to determine “When is the right time to exit an investment?”

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## 9. APPENDICES

### Appendix 1

#### List of questions: (Investors)

- 1) What is your Company? Company figures, Portfolio at the moment
- 2) What kind of companies do you invest in?
  - a) In which stage?
  - b) Ideas, new companies, existing/"old" companies
- 3) Why/what do you invest in companies? What's in it for you?
  - a. Board membership?
  - b. Typical share-% of a company that you invest in?
  - c. Only for profit?
- 4) Where do you find the companies you usually invest in? Pull or Push?
- 5) I'm doing my thesis about start-up financing, what do you think is the best way to finance a start-up company? How would you do it?
- 6) Do you offer funding to all companies? Is there a specific industry that is more appealing today to investors in general and especially to your company?
- 7) How do you differentiate between the good companies (Teams & Ideas) and the ones that are risky?
- 8) Do all companies accept your proposals? Why?
- 9) Your best investment so far? Dream Team?
- 10) Please, describe the process: From first pitch you hear to funding decision.

Appendix 2  
Original list of questions to Start-ups

Startupeille:

- 1) Mikä tilanne: Idea, Koska perustettu? Liikevaihto? Mitkä ovat tavoitteet tulevaisuuteen Suomessa ja kansainvälisesti?
- 2) Onko rahaa haettu aiemminkin (mutta ei saatu)?
  - a. Mistä? Montako tapaamista ja mihin saakka päästy?
  - b. Miten pitch kehittynyt, kuka kehittänyt? Onko haettu apua pitchiin kolmannelta osapuolelta, jos on niin mistä?
- 3) Onko saatu aiempaa rahaa
  - a. Milloin, mistä, minkä verran
  - b. Omat rahat?
- 4) Paljonko valmis luopumaan omistuksesta?
- 5) Mitä tekisit toisin?
- 6) Mitä jos ei tulekaan rahoitusta? Plan B?
- 7) Mihin rahoitusta?
  - a. Kasvu
  - b. Investoinnit
  - c. Idean jatkokehitys
  - d. Muu?

## Appendix 3

### Translated list of questions to Start-ups

#### List of questions: (Start-ups)

- 1) Situation: Idea, Company founded? Revenue? Goals in Finland and abroad?
- 2) Have you tried to get money elsewhere (but haven't received it)?
  - a. Where? How many meetings? How far have you got?
  - b. How have you developed your pitch? Who has developed it? Have you had any help developing your pitch from a third party, if yes where?
- 3) Have you received previous investments?
  - a. When? Where? How much?
  - b. Personal capital?
- 4) How much are you willing to give up of your company?
- 5) In terms of financing, what would you do differently?
- 6) What if you won't get the funding you need?
- 7) What do you need the funding for?
  - a. Growth?
  - b. Investments?
  - c. R&D?
  - d. Other?