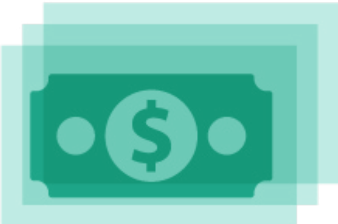
Capital Access

Why it matters to startups:



Access to capital is perhaps the most critical barrier startups face when launching. The average startup launches with roughly $78,000, often cobbled together from a mix of personal loans and family savings. While angel investing and venture capital represent attractive options for certain startups, only about one percent of startups launch with angel funds and an even smaller percentage with VC funding. These statistics are even worse for underrepresented founders. Controlling for differences in credit scores, small businesses with underrepresented founders report higher loan denials, pay higher interest rates, and are more likely to be denied credit than white-owned businesses. And those small business owners are more likely to rely on personal funds and personal credit than white owners. Put plainly, diversity in the startup community is not yet reflective of U.S. society, and underrepresented founders are at a stark disadvantage when accessing capital.

Key takeaways:

- Startups are one of the U.S. economy's main net job creators, and policymakers should consider the unique circumstances facing startups when formulating policy, especially economic relief policy in response to the COVID-19 pandemic.
- Most startups rely on a patchwork of funding sources outside of traditional venture capital.
- Policies should make it easier for startups to access capital and open up capital markets to allow more people to participate in funding early-stage companies.
- Difficulties with accessing capital are especially relevant to underrepresented founders, including women and founders of color.

What policymakers can do:

Policymakers must continue to improve the regulatory environment in which startups operate to raise capital. While the Securities and Exchange Commission has recently made changes—including a limited expansion of the definition of accredited investor, lifting the limit a company can raise through crowdfunding, and increasing the offering limits for Regulation A and Rule 504—policymakers should continue to seek out ways to best enable startups to raise capital effectively. Policymakers can also address capital access issues with federal funds, including streamlining federal grant processes, directing federal funds to incubators and accelerators, and supporting organizations that provide valuable support, resources, and programming for startups. And policymakers should specifically prioritize equalizing access to capital for underrepresented founders, including through incentivizing venture capital funds to be allocated to diverse founders, ensuring access to Small Business Administration resources, and identifying and rectifying discrimination in bank lending. Congress should also work with the new administration and with the startup community on its stated goals of creating a Small Business Opportunity Fund to direct funds to state and local initiatives that provide venture capital to qualifying businesses, and amending the Community Reinvestment Act.

Startup Spotlight on Capital Access

DivInc
(Austin, TX)
Preston L. James, II, Founder and CEO

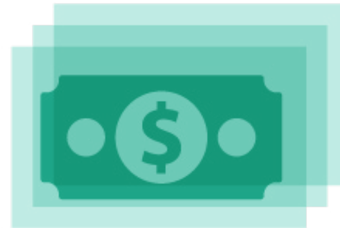
DivInc is a nonprofit that connects entrepreneurs of color and women founders with mentors, connections, opportunities, and resources

"If we look at this from a socioeconomic perspective, we need to empower people of color and women by providing them with equitable opportunities. When you look at women—and specifically women of color—they are by far the fastest growing entrepreneurial demographic in the United States. We need to create policies that fully support women."

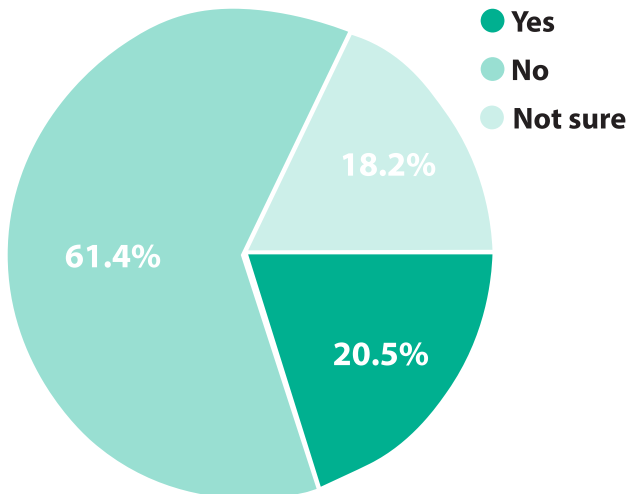
The Pandemic and Capital Access

The COVID-19 pandemic has brought with it even more financial uncertainty for many nascent companies. While some venture capital backed startups have been able to weather the pandemic well, other startups are in continued need of government assistance. Though the Paycheck Protection Program (PPP)—as created by Congress in the Coronavirus Aid, Relief, and Economic Security (CARES) Act—provided a lifeline for many struggling businesses, initial efforts were confusing and limited, and subsequent efforts to extend and expand PPP are not enough to ensure long-term viability of America's startup ecosystem. According to an Engine survey, while many startups received government assistance amidst the pandemic, including Economic Injury Disaster Loans (EIDL) and PPP loans, more than 60 percent of respondents indicated the financial relief was insufficient. And a plurality of startups responding indicated that more relief was needed before the end of 2020 or they would risk shuttering their doors. Startups further indicated that policymakers needed to consider a broader range of reforms beyond PPP loans in thinking about long-term relief.

To ensure startups' ability to weather the pandemic, policymakers must consider the unique needs of the startup ecosystem as Congress crafts relief programs. Though Congress took quick action early on in the pandemic by implementing the PPP, many startups did not qualify, or were not sure if they qualified for PPP loans because of the program's focus on payroll costs and rules that effectively excluded startups with venture capital backing. While Congress has renewed PPP and is allowing for second draw loans, policymakers must also consider targeted, long-term recovery proposals, including creating a dedicated startup fund, a tax credit for angel investors, long term, low-interest loan options, and incentivizing venture capital funds to be directed to more diverse founders. Given that startups success leads to net job creation, it is imperative policymakers ensure that startups have the long-term tools they need to survive.



In a survey, startups that received emergency relief through a federal program were asked if the amount of emergency funding they received was enough to support their business operations amidst the pandemic.



Startup Spotlight on Capital Access

Bitwise Industries
(Fresno, CA)
Jake Soberal and Irma Olguin Jr.
Co-Founders and Co-CEOs

Bitwise is a startup focused on increasing workforce opportunities for diverse workers

"We disproportionately have early-stage companies led by women and people of color that do not have the safety net that later-stage companies often do. The federal government was right to move quickly on Paycheck Protection Program (PPP) loans during the pandemic. From our view, however, there should have been multiple bursts of that funding from the beginning of the pandemic until now. Without PPP, though, I think you would have seen a larger number of early-stage companies wiped out in communities like Fresno."