

# The Rise of Startup Studios

WHITE PAPER

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# Acknowledgements

This white paper was written with input from innumerable individuals we could never begin to thank. But, we'd like to start by thanking all of the studios who are part of the Global Startup Studio Network. Next, we thank everyone who read and commented on the various drafts of this document, including Chris Collins, Sergio Marrero and others.

## About GSSN

The Global Startup Studio Network exists to connect hundreds of startup studios around the world. Through GSSN, studios share ideas, expand their networks, promote their portfolio companies, and raise capital for their portfolio companies.

We're leading a revolution in the way startups are created. Through increased collaboration between studios, we will increase the success rate of studio-born startups. As a result, GSSN will improve the health and awareness of startup studios globally, making the studio model the gold standard for startup creation.

In June 2018, Boulder Bits, a startup studio in Boulder, Colorado (USA) created the Global Startup Studio Network (GSSN) in an effort to connect the hundreds of startup studios around the world and provide them value in their growth. Outside of creating GSSN, Boulder Bits was best known for creating SmartCapital, Bear Systems, and Zizmos, its most successful startup spin-offs. Jesse Lawrence, Sarah Phillips, Jake Hurwitz, Pam Narowski, and Kristin Fulton played an instrumental role in the creation of Boulder Bits and all of its portfolio companies, and this team is fully credited with the content and data shared in this white paper.

In late 2018, GAN (GAN.co), a highly curated community of independent accelerators, partners, and investors, began providing informal expertise and advice to Boulder Bits and, in early 2019, the Boulder Bits team unfortunately needed to cease operations due to health issues on its leadership team. Shortly following, they approached GAN to formally ask if GAN would be interested in taking over operations for GSSN.

Now, though still a separate organization, GSSN is fully owned and operated by GAN and its team and GSSN is excited to move the studio community into its next phase—no doubt working alongside studio leaders to see the industry continue to grow and evolve.

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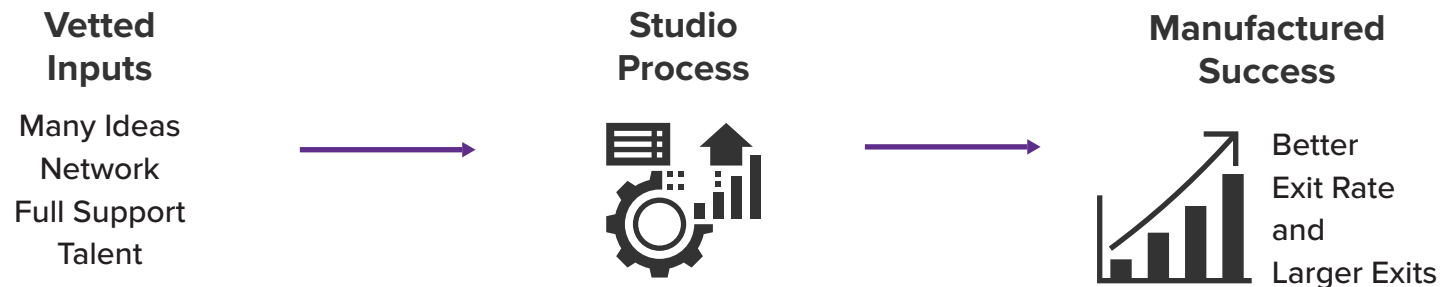
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# Executive Summary

Startup studios—or venture builders—are proliferating at an increasing rate. Ten years ago, there were fewer than a handful. Today, there are more than 200. These unique companies create startups, infusing time, effort, and cash in exchange for startup equity. They bring in founders to operate the

startups and support them with services like legal, HR, and fundraising. In other words, startup studios are factories that produce startups. In exchange for human and financial capital, studios retain a portion of the equity in the companies they create.

## STARTUP MANUFACTURING



Even three years ago, studios ran into significant resistance from venture capitalists, angel investors, limited partners, entrepreneurs, and the media. In this white paper, we explain how and why

entrepreneurs and investors are increasingly turning to this lesser-known startup model. It is part of the long-term, macro trend of investors moving upstream toward the inception of startups.



# Introduction

Startup studios create companies the way that factories might create high-priced widgets: efficiently, systematically, and for the greatest monetary upside. In this white paper, we discuss the norms of startup studios and variance between them. Like any process, startups can be manufactured. The goal of any manufacturing process is to produce more valuable outputs with fewer lemons. Typically, better supply chain and

better manufacturing processes result in better outputs. Or, in this case, more valuable equity. Studios are inherently different than accelerators because they work on a project as early as the problem-identification stage, on through scaling, whereas accelerators typically support external companies and teams for a short duration. Greater involvement from studios results in studios retaining more equity.

## AVOIDING FAILURE

We all know that startups are hard to grow properly and they fail roughly 80-90% of the time<sup>1</sup>. There are millions of ways that startups can fail, often at great expense to those

involved. Here, we list the top 20 reasons independent startups fail<sup>2</sup>, organized into the five categories identified by Bill Gross of Idealab as the key sources of success<sup>3</sup>:

<b>Team</b> 32%	<b>Idea</b> 28%	<b>Funding</b> 14%	<b>Business</b> 24%	<b>Timing</b> 42%
Incorrect team	Poor market fit	No funding/ investor interest	Legal challenges	No market need
Lose focus	Pricing/cost issues	Ran out of cash	Didn't use network	Product mistimed
Disharmony among team/investors	Poor UX		Outcompeted	Failed geographical expansion
Lack passion	Poor marketing		Lacking business model	
Ignore customers			Failure to pivot	

This table lists the key factors in startup failure, according to CB Insights, categorized by the top five startup success factors listed with the percentage correlation with success, according to Bill Gross' TED Talk<sup>3</sup>.

1. Duffy, James. "Startup Failure Rates: 3 out of Every 4 Venture-Backed Startups (75%) Eventually Fail." More Than Accountants, 13 Dec. 2018, [www.morethanaccountants.co.uk/start-up-failure-rates-3-out-of-4-venture-backed-startups-eventually-fail/](http://www.morethanaccountants.co.uk/start-up-failure-rates-3-out-of-4-venture-backed-startups-eventually-fail/).

2. "The Top 20 Reasons Startups Fail." CB Insights Research, 15 Mar. 2019, [www.cbinsights.com/research/startup-failure-reasons-top/](http://www.cbinsights.com/research/startup-failure-reasons-top/).

3. Gross, Bill. "The Single Biggest Reason Why Start-Ups Succeed." TED, Mar. 2015, [www.ted.com/talks/bill\\_gross\\_the\\_single\\_biggest\\_reason\\_why\\_startups\\_succeed](http://www.ted.com/talks/bill_gross_the_single_biggest_reason_why_startups_succeed).

Interestingly, the leading source of success—timing—is often not accounted for by many startup founders, but is accounted for by studios. The evaluation of timing is a key process in the validation that startup studios perform. Prior to modern accelerators, entrepreneurs would have to pay for a network to help them solve problems like

those listed above. A lucky few would garner venture capital (VC), which usually comes with a high-end network capable of steering the team away from danger. Venture Capitalists were the original startup investor-network hybrids.

## EARLY & CONSISTENT INTERVENTION

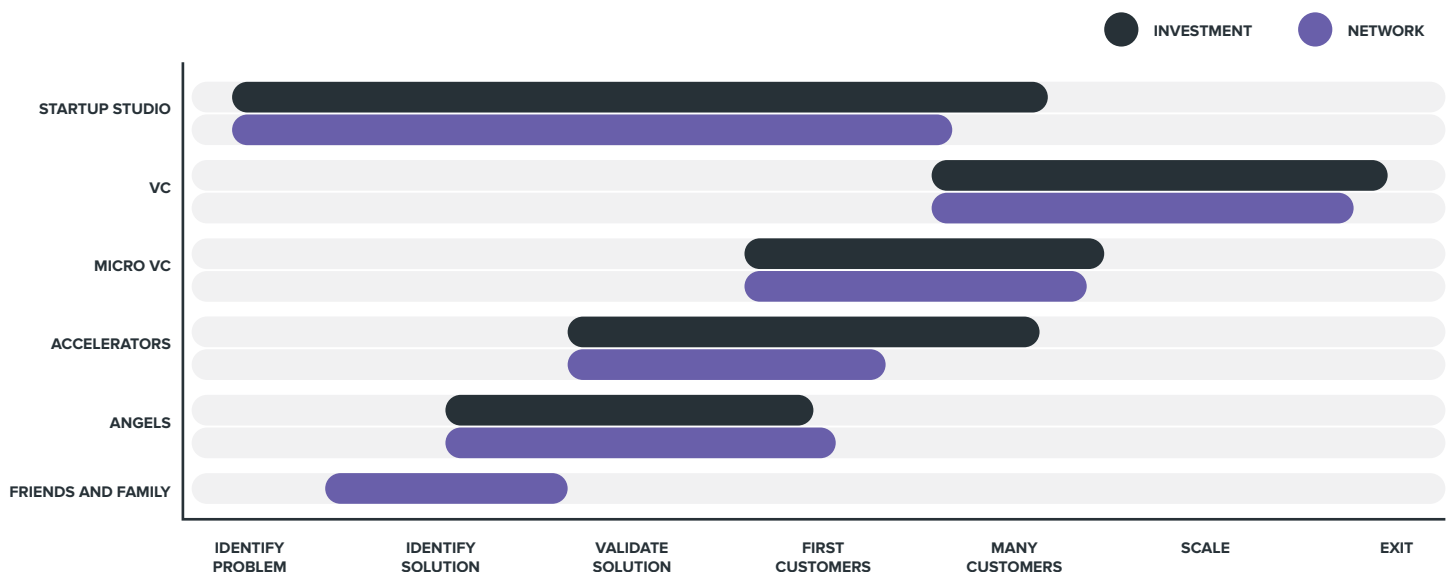
Startup accelerator data from the last decade has repeatedly shown that providing a support network at an early stage drastically increases a startup’s odds of success. Data from Mattermark and others clearly demonstrate that startups that participate in accelerators exit through IPO, acquisition, or merger four times more often<sup>4</sup>.

The startup studio model is a natural progression of pushing investment, process, and networks upstream toward the inception of

startups. For two decades, studios have been asking these questions:

1. How can a team systematically validate startup ideas sooner?
2. Who is the optimal team to execute on a project? What support is needed to win?
3. How can we offload repeatable work to help founders focus on scaling their company?

## VALUE-ADD FOR STARTUPS



4. Cremades, Alejandro. "10 Startup Accelerators Based On Successful Exits." Forbes, Forbes Magazine, 12 Sept. 2018, [www.forbes.com/sites/alejandrocremades/2018/08/07/top-10-startup-accelerators-based-on-successful-exits/#6ea6cf6b4b3b](http://www.forbes.com/sites/alejandrocremades/2018/08/07/top-10-startup-accelerators-based-on-successful-exits/#6ea6cf6b4b3b).

The benefits of early intervention are clear, and break down into the following processes:

**Logistics**

Legal, accounting, human resources, taxes

**Product-Market Fit**

Experience, tools, partners, network

**Development**

In-house developers, outsourced, talent acquisition

**Branding/Marketing**

In-house talent, outsourced, talent

**Investment**

Studio fund, active investor network

**Domain Expertise**

Access to industry experts

**Best Practices**

Process, structure, prioritization

Many tasks required to form and run a fledgeling company are distracting and can bog down even the best of entrepreneurs.

However, an abundance of these tasks are common and repeatable. It is the goal of most startup studios, therefore, to streamline the above processes and reduce friction for founders by taking over some or all of these tasks, freeing founders to focus on innovation, leadership, and scaling.

For example, legal documents can make or break a company. Intellectual-property or human-resources mishaps can land a startup in court. Paying lawyers 20% of a new company's runway is a painful way to fail. On the product side, providing an experienced mentor can help entrepreneurs pivot the right amount rather than missing opportunities or spinning in circles. Similarly, connecting founders with investors and mentors early can help founders get on the right fundraising track and stay there. Assistance and processes in each of these areas can make the difference between exit and bankruptcy.

In the following sections, we describe the differences between types of studios, the evolution and growth of studios, the benefit of the studio model, and the changes we expect to see from studios moving into the future.



# Studio Model

Startup studios create companies like factories create widgets. They invest time and money into a repeatable process that outputs valuable companies. The goal is to sell every studio-born startup at a large profit. The inputs to create a

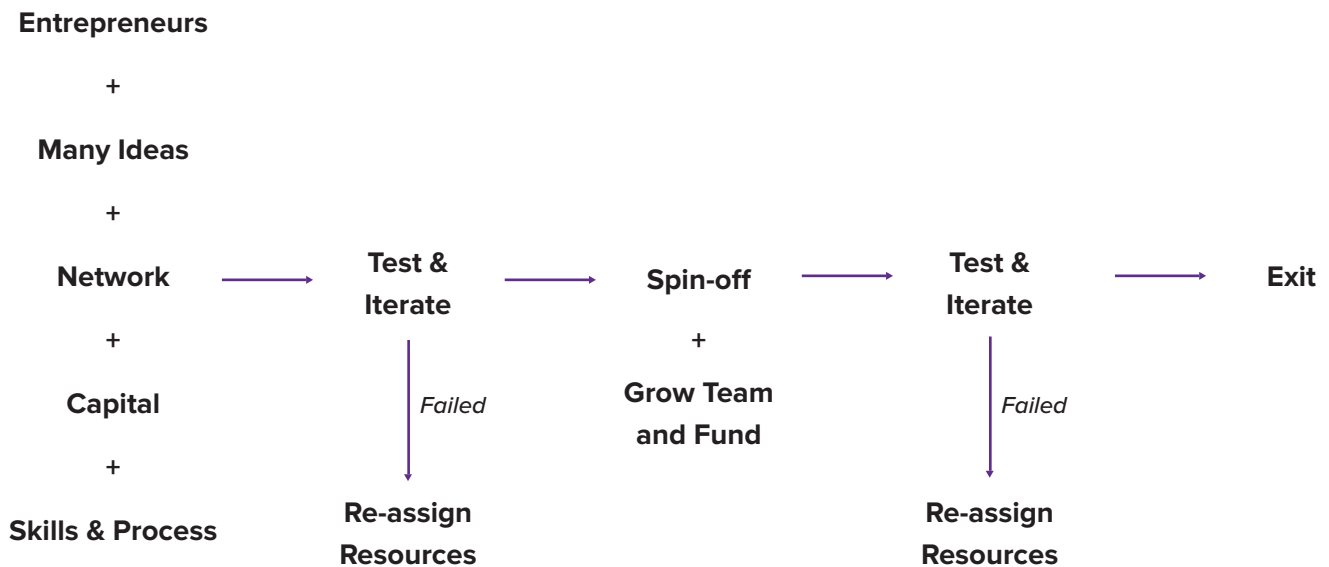
startup are ideas, team, capital and support. Better inputs result in higher-quality outputs. If a studio assembles a great team around a great business idea, far more value is created than with either a bad idea or the wrong team.

## THE PROCESS

As we've already mentioned, process is the core of what makes studio-born startups different than independent startups. One of the most important aspects of process is the decision-making methodology of how and when to allocate and re-assign talent, capital, and support to various projects. The whole point of a studio is to iterate quickly over many ideas to connect a team with the best possible company where everyone can win.

The image below illustrates that you can build many proto-startups in parallel, see how good they are, and reassign the team if a particular proto-startup doesn't work out. If everything works, then you can launch the startup into the next stage of growth and funding. Studios typically don't spin off their startups until after they have been validated sufficiently.

## STUDIOS SUCCEED OR RE-ASSIGN RESOURCES

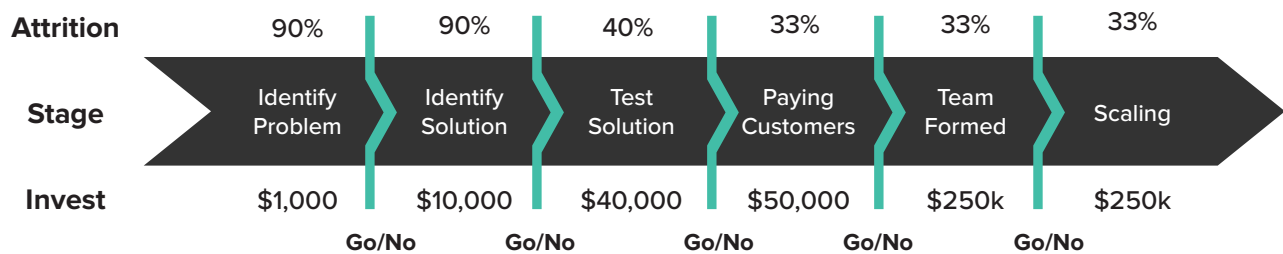




## STAGE GATES

The stage gate is a core process for nearly every studio. A stage gate is a hurdle that founders must overcome in order to continue<sup>5</sup>. For example, within a studio an entrepreneur can only found a company if they segment the market, identify customers excited to pay for a solution, test and observe an unfair advantage, and accomplish a hundred other similar tasks. Each task may result in a “go” or “no-go scenario

for a given project. When a team hits a “no-go,” the team can start working on another project. Each stage gate de-risks the project for everyone involved, resulting in a higher chance of success for those that pass the stage gate. Projects receive increased funding and resources as they pass stage gates.



This figure shows an example of major stage gates. While the specific stage gates and cost per gate may differ from studio to studio, almost all studios have some form of go/no-go process. Further, the order of the stage gates may shift from project to project. For example, if a project starts because a customer approaches the studio with the goal of paying to have a problem solved, it reduces risk faster.

The advantage of having multiple clear and defined stage gates in an iterative process is that the team can be objective about success and failure. If you don't define success, then the team fails to understand the overarching goal.

5. Wise, Sean, and Brad Feld. Startup Opportunities: Know When to Quit Your Day Job. John Wiley & Sons, Inc., 2017.

## ITERATION VS. SELECTION

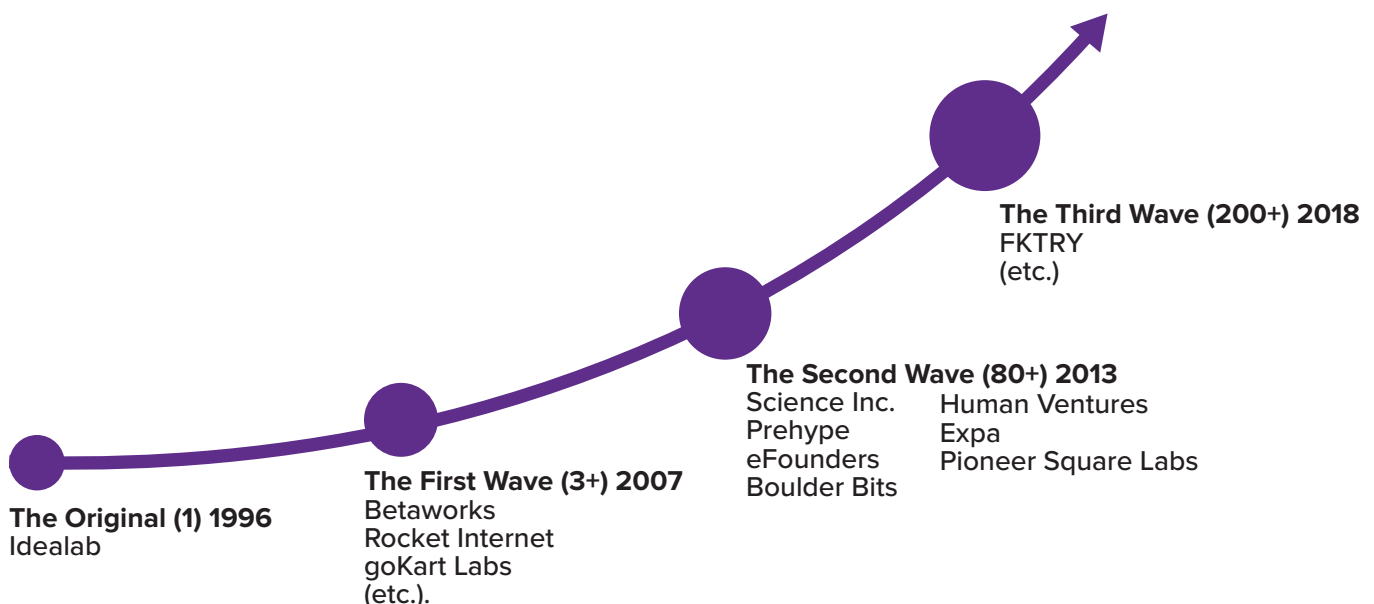
The lean startup model can result in endless iteration on a single project. From the studio's perspective, iteration alone is inefficient. A startup that fails after five years is much more expensive than one that fails after five weeks. The studio model truncates the iteration process with stage gates, but allows for iteration over many projects. Studios apply the Lean Startup

iterative approach of "learn, build, measure" at the portfolio level, not just within projects. Iterating over projects and selecting the winners is a more efficient way to reach success. Rather than progressive iteration, the studio process is a combination of entrepreneurial iteration and investor selection.

## HISTORICAL PERSPECTIVE

Business innovation has no true historical starting point. Major inflection points for business innovation include Richard Arkwright's mechanized factory (1767), Ford's assembly line (1913), and Bill Smith's six sigma (1986). The modern accelerator was invented in 2005 by Paul Graham, and quickly innovated on by David Cohen and others<sup>6</sup>. Most people are unaware that the startup studio model pre-dates the

accelerator. Bill Gross formed Idealab in 1996<sup>7</sup>, nearly a decade before Paul Graham invented the accelerator. While Gross was way ahead of his time in 1996, he borrowed from the rapid innovation methodologies that Safeguard Scientific pioneered from the mid-to-late 1900s<sup>8</sup>. Unlike accelerators, which blossomed nearly overnight, it took another 11 years before the next wave of studios came along.



6. "Startup Accelerator." Wikipedia, Wikimedia Foundation, 6 Mar. 2019, en.wikipedia.org/wiki/Startup\_accelerator.

7. "Idealab." Wikipedia, Wikimedia Foundation, 10 Nov. 2018, en.wikipedia.org/wiki/Idealab.

8. "Our History." Safeguard Scientifics, Inc. - Experience Growth., www.safeguard.com/value/our-history/.

## STARTUP STUDIO TIMELINE

The concept of startup studios began with Idealab in 1996. Since the 2007 economic downturn, the studio model has proliferated. The variation in studios has grown along with the number. Over the last decade, we've seen 5000% growth in startup studios. In 2013, there

were approximately 80 studios. Today, there are well over 200, yielding 250% growth in just five years. Based on the expansion of the studio model in the last three years, we project another doubling by 2023.

## DIVERSIFICATION VS. CONCENTRATION

Practicality tells investors to invest broadly across startups because startups are known to fail all too often. While an accelerator may gain a dozen new portfolio startups every year, studios typically spin out only two to four startups a year. Spinning out a portfolio company from a studio requires more capital, compounding the lack of diversification. To compensate for this increased risk, many studios take much more equity.

Diversifying investment across many companies via an accelerator model means a greater chance

of landing a “winning” company, but that likely means a decreased “win” when it comes to the size of return. Alternatively, while there might be higher risk in investing in a small number of companies coming out of a studio model, return potential is extremely high.

To compensate for reduced diversity compared to accelerators, studios must concentrate more heavily on a few winners.



## NAME CONFUSION

One of the challenges in talking about startup studios is that they go by a variety of names. Here are a few.

Name	Overall Rank	Use Rank	Relevance Rank	Category Rank	Identify Rank
Startup Studio	1	2	1	1	1
Startup Factory	2	1	2	2	3
Venture Builder	3	4	4	3	2
Company Builder	4	3	3	4	5
Venture Studio	5	6	5	5	4
Startup Foundry	6	5	6	6	6
Startup Nursery	7	7	6	7	7

We analyzed the online frequency of use of the above search terms, the frequency each term was predominant in the search of the other terms, the number of times the search term was associated with the overall category described in this white paper, and the number of times that studios/factories self-identified with the term. We use the term startup studio because of overall rank order—even if it's not the most used search term.

This lack of consistent language is just one of many examples demonstrating a lack of awareness, consensus, and understanding of the model itself, even among studio founders. This is one of many reasons a white paper such as this one is so essential to the industry—galvanizing everyone around more specific language and educating the public on what we mean when we talk about startup studios will not only serve studios themselves, but entrepreneurs, investors, and the public.

## PUBLIC VIEW

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Studios remain widely unknown among the public and investors. While Google searches for the term “startup studio” have remained constant over the past 14 years, the term “startup accelerator” and “startup incubator” have nearly tripled over the same time, according to Google Trends.

On the other hand, one reason for the growth in public awareness for accelerators is that they are public-facing. Demo days are popular events in startup hubs like Silicon Valley, Boston, New York, Austin, and Boulder. Studios don’t have demo days, so they are far less focused on and effective at promoting the good deeds of their portfolio companies among the general public.

## DATA BIAS

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As we’ve already noted, studios produce far fewer startups than accelerators accelerate, and even less compared to startups that exist “out in the wild.” Fewer than a handful of studios are more than a decade old, which means that most of the data—particularly on successful unicorn exits—comes from a very small number of early studios. A studio that formed less than five years

capitalists and avid angel investors to be completely unaware of this class of startups. Anecdotally, around half of investors will admit to being unfamiliar with startup studios. We informally surveyed entrepreneurs to find out how many could confidently describe different types of startup services. After unbiasing the data, we found that studios were only understood a quarter as often as incubators, accelerators, and VCs.

In our research, we even found startup studios that were unaware of the existence of other entities like them. We spoke to multiple people who wanted to create a studio, but didn’t know what to call it. Taken altogether, it’s clear that studios are underrepresented in common startup culture.

ago, spinning out two portfolio companies a year, would have too few mature startups to measure anything but vanity metrics. The fact that a studio may not spin out a portfolio of thirty startups for 10 or 15 years is frustrating to investors. Investors don’t want to spend a lot of money without big numbers to back up their decisions. This is why we look at data from multiple studios.

# Types of Studios

Just like with VC's, accelerators, and incubators, there are a variety of different types of startup studios. The primary drivers of differentiations are the source of the ideas, talent, and capital. Here is a brief overview of the primary startup studio models:

**Venture Builders:** Venture Builders are studios where the main focus is on creating companies from the ground, up. Venture Builders typically invest off the studio's balance sheet to cover ideation, validation, and early salaries. On average, they provide around \$250k of launch capital for each portfolio company. This capital serves as a bridge to a future seed round. *Examples: Idealab, Science Inc., Human Ventures, and Pioneer Square Labs.*

**Agency Builders:** Agency Builders typically bring cash in through a fully functional digital agency or dev shop, and use the proceeds to spin up their own products and startups. Or, they leverage their agency resources to jumpstart an existing team in exchange for a mix of equity and cash. Their agency work provides a unique perspective on market trends and unmet needs. These builders often have deep expertise in either advertising or software development. *Example: Colab.*

**Venture Capital Labs:** VC Labs are typically a startup studio attached to a larger VC firm. Typically, the VC fees and carry pay for the operations of the lab and may act as the source of capital for the portfolio companies. *Example: Primary VC.*

**Accelerator Studio:** These studios behave as a hybrid between an accelerator and a studio. They tend to have rolling start dates, long engagements, and greater funding like a studio, but bring in outside fledgeling companies like an incubator or accelerator. *Example: 500Labs*

**Corporate Studio:** These studios are either formally or informally supporting innovation at larger corporations. The funding source is typically a single corporation or in conjunction with the studio. The studio leads the problem/solution process within the parameters of the corporate goals. Often, the corporation can provide powerful assets such as IP, distribution channels, know-how, or be an early customer. *Examples: BCG Digital Ventures, Mach49, PreHype, and Ideo Colab all partner with corporations.*

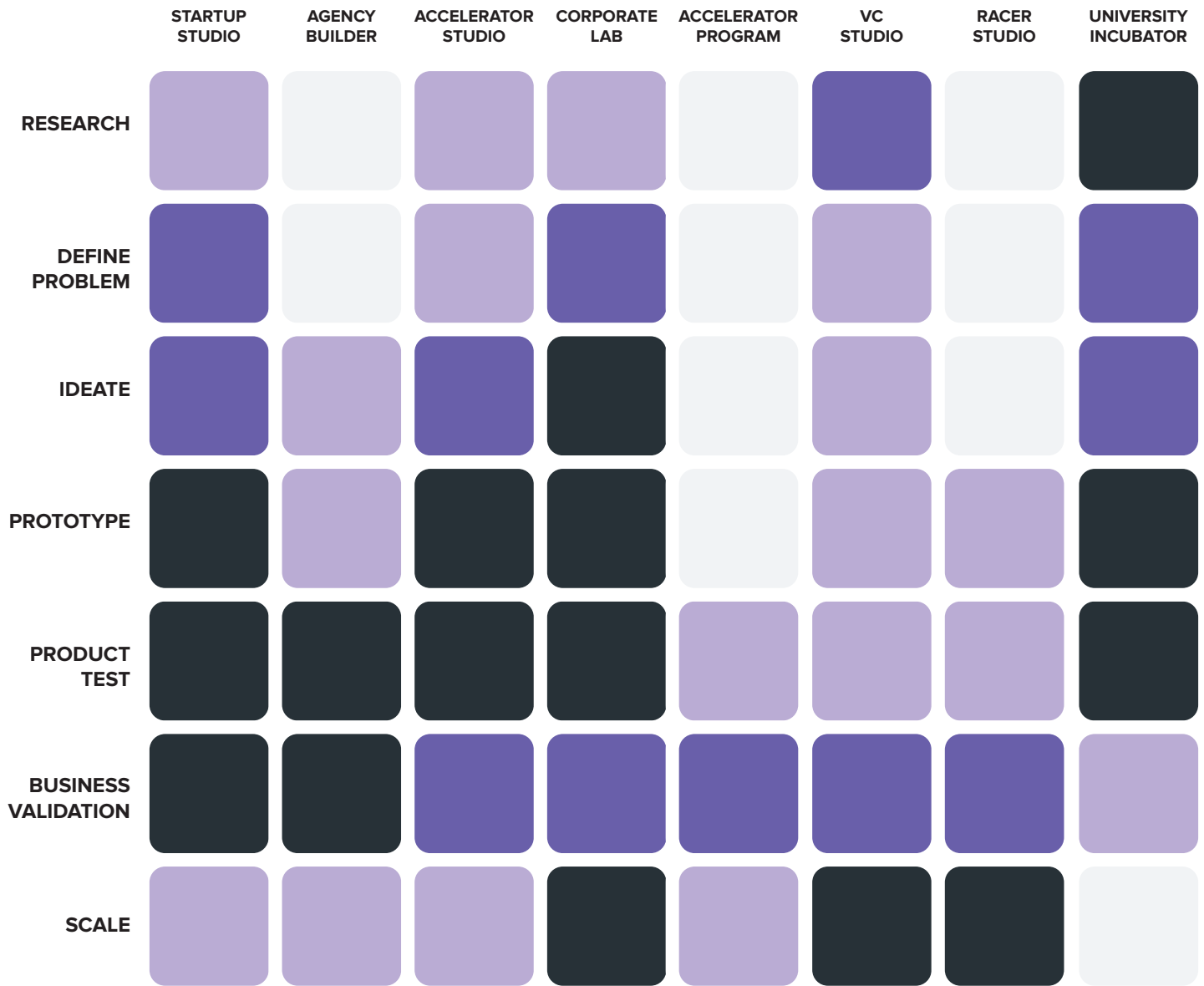
**University & Government Studios:** These studios commercialize the IP generated from universities and government labs by building technology companies. They work closely with the office of technology transfer and academics to build viable businesses. *Examples: UCLA Anderson Venture Accelerator and Fed Tech.*

**Loose Structure:** When we started this research, we were surprised to learn that some venture builders didn't have structure or process surrounding their methods. These studios consist of a loose group of entrepreneurs who work together to spin up companies. They bring their partners and teams together informally, but do so repetitively. *Examples: Elon Musk's suite of startups and Bam Ventures.*

**Racer Studios:** Racer studios seek to identify great startups and emulate them often in different geographies. These studios are extremely lean because they don't require as much innovative research. Emulation is much faster and cost effective. *Example: Rocket Internet.*

**Hybrids:** Not surprisingly, studios exist that blur the lines or have a unique operating model. *Examples: Prehype, 10.10.10*

## PRIORITY AND INVOLVEMENT



This chart shows the rough priority and involvement that different types of startup engines impart into startups. Dark means higher priority and involvement. Light means lower priority and involvement.

# Studio Attributes

Studio type plays a large role in determining the different aspects of a studio. Here are common attributes:

## Founding Team of the Studio

The founding team greatly shapes the culture, practices, and leadership strengths of the studio.

## Experience

Most studios are founded by very experienced startup founders (such as Expa - founded by Garrett Camp, the co-founder of Uber). Their past experience helps them replicate future success in their portfolio.

## Fame

Some studios are founded by famous celebrities. Famous studio founders help draw talent and network to the studio. Most of these enterprises have less apparent structure, but typically have more structure than one might imagine. For example, Combs Enterprises, lead by Sean “Diddy” Combs, has systematically built and promoted a series of companies over the past decade.

## Process

Some studio founders are more process-driven, giving them the ability to reproduce underlying tasks more efficiently than others. As an example, FKTRY is a studio that provides systematic value through brand, product, growth & organizational design.

## Creativity

Other studio founders are more creative with respect to business models, giving them the ability to generate more innovative solutions in various different industries. An example of this is Idealab, a studio that has worked on everything from robotics to pay-per-click to candy.

**Access to Money:** Studios don't exist if money is lacking. The amount of money can limit studio resources. There are two primary ways studios have

access to money: internal to the studio, and through control of side funds. Most studios have access to one or both. The major difference is the amount of funds in each.

## Internal Coffers

Studios with more money in the bank can fund their portfolio startups with more seed funding and later funds. Larger funds can support more startup portfolio startups and pay larger salaries to attract top-tier talent. Studios with prior large exits can afford to overcome a few years of lesser productivity, which can happen when only producing a handful of companies per year.

## Side Fund

Many studios raise an additional VC fund to either support the portfolio companies they spin out, startups in the local startup ecosystem, or startups in a particular vertical. More funds to support spun-out portfolio companies comes with obvious benefits. Investing in outside startups has the benefit of providing greater visibility into outside practices, state-of-the-art community.

## Location

Every studio is limited and benefited by the regional talent, resources, and culture surrounding the studio's headquarters. Access to less expensive talent, larger talent pools, and/or lower real-estate costs can shape a studio as much as the founding team or access to money.

## Network

Some founders have larger, and more influential networks than other studios. The type of network also changes. Some focus more on growth while others focus on funding. For example, access to top-tier VC's can accelerate growth at a later stage.

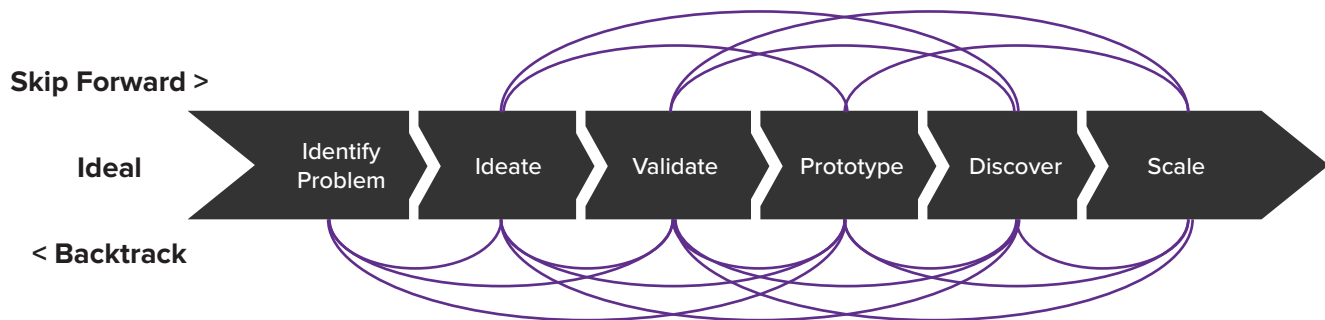


# Zero-to-Exit

Design thinking is great for the “Zero-to-One” stage, as described by Peter Thiel<sup>9</sup>. Going from nothing to something is a challenging endeavor. However, payday for founders and investors only happens if the startup exits. Therefore, studios must have an exit in mind from the beginning. Therefore, it’s critical to plan from “Zero-to-Exit.” Studios start working on a startup as early as the problem identification phase, and help through IPO. The concept of “Zero-to-Exit” is far more complex than “Zero-to-One,” requiring multiple

interconnecting systems for success. In the image below, the process is simplified. Each activity, such as validating a product feature interacts with other activities, such as funding or prototyping. The challenge is to identify the ideal path and backtrack as few times as possible.

Professional startup operators and supporters can drastically reduce the number of missteps, which results in more successful startups.



9. “Zero to One.” Wikipedia, Wikimedia Foundation, 31 Jan. 2019, en.wikipedia.org/wiki/Zero\_to\_One.

# Verticals vs. Breadth

It should come as no surprise that some verticals focus narrowly on a particular industry, while others span industries. There are advantages

and disadvantages to both narrowly and broadly focused studios.

Focus	Pros	Cons
Narrow	Deep industry expertise can be recycled for multiple projects. Network and investment are aligned with the portfolio companies.	Individual industries suffer from episodic economic downturns, resulting in times of plenty then times of scarcity.
Broad	There are more potential problems to choose from, resulting in more opportunistic startups.	It can be more costly to spin up startups without deep industry knowledge, which is harder to have across disciplines.

A studio’s focus may be dictated by an industry partner, the primary LP’s in the studio, access to local talent, or the studio founders areas of

expertise. Clearly corporate labs and university studios are dependent on the IP available from the feeder institution.

# Studio Structure

Most studios are created by professional entrepreneurs or investors. Unlike the portfolio companies they spin out, studios are designed to invest in stock. Therefore, studios are usually designed to be more tax-efficient with less concern for scalability.

The majority of studios in the U.S. take one of two forms: either an LLC (limited liability company) or a subchapter S corporate (S-corp), though some take the form of LLP or similar.

**LLCs:** LLCs are well-known and often-used investment vehicles in the U.S. because they provide pass-through taxation of a partnership with the limited liability of a corporation. LLCs provide the ultimate in flexibility and ease of operation.

**S-Corps:** Standard corporations can elect "pass-through" taxation by applying to the IRS for status as a Subchapter S Corporation. These entities are limited to 99 U.S. owners and require greater corporate structure and management.

The structures and agreements get more and more complex from there. Partnerships, contracts, and subsidiaries all play roles in different types of institutions. Some studios

have separate subsidiaries that have different functions (e.g., VC, development and marketing). Others are subsidiaries of holding companies.

## SIDECAR FUNDS

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Many studios also manage sidecar funds to invest in the portfolio startups or external startups. These funds are usually structured similar to any other fund, where the management company is also a studio. In other cases, the major players of the fund create a separate entity. In either case, certain tensions exist between the fund and the studio.

### Fund Time Commitment

Studio managers are busy people. They have few spare hours for anything but creating new companies, scaling companies, maintaining investor relationships, and following up on old deals. Fund managers are also busy people, vetting possible deals, executing on new deals, maintaining relationships with limited partners, and following up on old deals. As you can see, many of the activities overlap, allowing the same person to hold two positions. In fact, having a large fund can reduce a studio's time commitment except during fundraising years.

### Sidecar Fund Conflicts

Fund and studio managers have a responsibility to their investors to maximize return. While the general conclusion is that funds and studios maximize the returns by working together, there are subtle differences in responsibilities that could lead to conflicts of interest. This is

particularly true when the investors in the fund are partially or wholly different from the investors of the studio. Here are a few examples:

1. A studio may have sunk costs in a flawed portfolio company, and may wish for the fund to invest more cash to keep it afloat.
2. It is in the studio's interest to increase the valuation of portfolio companies to reduce dilution of the studio's equity, whereas the fund wants lower valuation to get more equity.
3. Fund managers that run a studio may pass up investments in external startups in favor of known entities, even if the external deal is better from all empirical measures. It may cost the joint fund-studio manager too much time to do external diligence.

We state these possible conflicts in order to be thorough, but generally conclude that any jointly-managed studio and fund would be short-sighted to allow such conflicts to interfere with day-to-day operations. Sophisticated investors have no tolerance or forgiveness for mismanagement of funds, and violation of such trust would eliminate the likelihood of follow-on investment in either entity.

## OWNERSHIP

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Studios may have a variety of different ownership structures. Obviously the studio founders take a large cut of equity. Initial studio investors may, as well. The initial investors may be individual LP's, family offices, or VC funds. The value of ownership in a studio usually stems from the studio's ownership of its portfolio companies. One invests in a studio because of the anticipated growth of the portfolio.

### Early Stage

When a studio is founded, they fall somewhere between two extremes: extremely funded to extremely underfunded. Well-funded studios are usually those like Expa, where the founders have had large wins in the past and can operate with expenses exceeding \$30M a year. These studios usually have large up-front costs and don't operate as efficiently, but crank out top-notch startups that more than pay for the high burn. The underfunded studios often operate off of the funds from the more modest successes of the founders' prior exits. If the founders' prior endeavors were bootstrapped, they likely don't have a large VC network to extend their cash. These studios often struggle to ramp up as quickly or have exits as large, but operate at such efficiencies that less sizeable wins still account for extreme growth. Numerous studios have launched with funds as little as \$250,000 per year.

### Intermediate Stage

Studios that have operated several years fall into the successful category, failed category, or the wait-and-see category. It often takes several years for portfolio companies to exit. It is easy for studios to run out of funds before a major exit. It can be hard to tell the difference between the "failed" and the "wait-and-see" categories. Studios with large exits typically don't need additional investment. Studios in the wait-and-see category may struggle to raise funds until they find an exit.

### Later Stage

By seven years in, studios fall into the successful or failed category. A studio either has a portfolio of companies valued at a large multiple of the investments or they don't. Some studios still exist in name at this point, having had a large brain-drain toward their biggest winner. Others have just folded, with the team scattering to the wind. Those with successes typically see some change in management. Often, the original founder will have taken "sabbaticals" running one or more of the portfolio companies throughout the time. Later-stage studios typically have great investor networks and don't struggle for investment—even if they had during for the first five years of their studio's operations.

# Success and Failure

A discussion of startup studios would be incomplete without a review of success and failure. As a baseline, we compare the successes and failures of studio-born startups with those of accelerated startups and independent, venture capital-backed startups. The hypothesis is that investment-network-supported startups have greater success rates at earlier stages.

We consider these key factors as relevant for evaluating startup performance:

1. What percentage of the startups are no longer operating?
2. What percentage of the startups have exited?
3. What is the size of the exit?

## DATA

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Before describing the results, we describe the data collected by the Global Startup Studio Network and affiliated organizations. We aggregated data from studios as well as publicly and privately available datasets. We analyzed the data for successful exits, failures, and investment size.

To learn more about GSSN, visit the [GSSN.co](https://GSSN.co) website. Because startup failure and exits may take five or 10 years, we focus on portfolio companies formed more than five years ago. Because half of all studios were formed within the past five years, we cannot evaluate those studios properly yet.

## FAILURES

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If a startup ceases operations, founders, studios, customers, and investors lose out. Therefore, failure rate of startups is a key indicator for comparing startup methodologies. Failure doesn't necessarily provide lower ROI for investors. Investors typically don't get any return from a startup unless the startup exits. On the other hand, a successful startup that doesn't exit is far better for a founder than a startup that fails.

**Exit rates of elite studio-born portfolio companies are approximately 30%, but may be as high as 50%.**

**Caveat:** The challenge with identifying failure rates is that not all information is made public. It is far harder to track failures than it is to track successes. There are far more discrepancies between available records, more missing websites, and far fewer public releases than with exits or operating.

## EXITS

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In general, the best way to have a positive IRR from a startup investment is an exit, whether IPO or corporate acquisition. Of course there are investor buyouts that occur during later rounds, but an exit is the gold standard for investors. Investors, studios, employees, and founders all benefit from startup exits.

**According to our research, seed-stage investments for startups created by top-tier studios are more likely (34%) to result in an exit than the average Series D investment (27%). Accelerated startups are marginally less likely to exit (21%) than a Series D investment, and a third less likely to succeed than studio-born startups. Based on personal communications, some studios, such as Betaworks, boast a 50% or higher success rate.**

## UNICORNS

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Unicorns are startups valued greater than US\$1B. The number of unicorns has risen over the last two decades. **To date, over 4% of all startup unicorns were created by only three startup studios.** We expect this number to change rapidly as the total number of unicorns grows.

**Elite venture builders and racer studios can create startups with more than a 4% chance of becoming a unicorn.** Studios with these exit rates include Idealab, Rocket Internet, Science Inc. and Betaworks. In the first years, several studios created portfolio companies that went on to reach unicorn status. For example, Science Inc. created Dollar Shave Club within a year of their formation.

# Evolution of Studios

Back in 1996, when Idealab began, there was no such thing as on-demand server farms like AWS, few people understood rapid prototyping, and only a few people understood design thinking. The common information that's currently available today online wasn't yet available. Studios had a huge advantage; they could pool computational resources, utilize a few key individuals who understood newer best practices, and draw capital under one roof.

The first wave of follow-on studios started when web 2.0, on-demand server, and smart phones were on the rise. Few people understood or even knew about the impact these new technologies would have. The timing was ripe for success. Meanwhile, there was an economic downturn, and lots of great talent were soon to be looking for a job. These studios benefited from prior relationships, pre-secured funding for their early-stage startups, and an expanding pool of talent. At this point, accelerators were still in their infancy, so there was no competition to the talent draw.

By 2011, early data showed that studios could win spectacularly, and the second wave of

studios were launched. By this point, best practices, lean startup, social marketing, web hosting services, and API-driven development were in full usage by experienced startups, but public knowledge of these tools was still limited. The challenge became convincing excellent entrepreneurs to join studios rather than go-it-alone or through an accelerator. Competition was on the rise.

Jump ahead to the third and fourth waves of studios, and we have acceptance of the lean startup model, mobile-first mentality, and on-demand everything. Best practices are described all over the web for anyone to read and anyone can find the right information. The problem isn't access to information; it's distilling the right information and applying it correctly. Network is still critical, and the web still struggles to provide strategic advice.

Studios are currently proliferating at a rate of over several studios a month, suggesting a doubling of the number of studios within two years. If the rate of proliferation follows recent trends, we expect to see a tripling in the number of studios by 2023.



# Why Now?

The obvious question we've asked is, "Why is the studio model expanding rapidly now?" As with any shifting tide, there's a series of contributing factors. We break these factors down into the following categories:

## Success

Success stories are spinning out of studios.

## Community

The larger pool of studios are catching people's eyes.

## SUCCESS

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Successes like Hims, which spun out of Atomic, and Dollar Shave Club, which spun out of Science Inc. during its inaugural year, catch the attention of the media and investors.

## COMMUNITY

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When there were only a few studios, operating as internally-facing startup factories, it was hard to tell what the studios were doing. Unlike accelerators, studios don't usually have outward-facing events like demo days. So, until a few years ago, unless you were in a studio's network, you didn't know that studios existed. With the third and fourth wave of studios, the number of blog posts about studios started increasing. Press reports became more common. Studios started to

## Costs

Prototyping has never been faster, reducing costs.

## Talent

The tech and startup talent pools are much larger.

## Failure

Failure rates haven't changed among wild-born startups.

## Ideas

Increasing number of business ideas and validating businesses at a faster rate.

There is nothing like success to help a community garner support. While skeptical, investors can't deny that the model works—at least in some cases.

reveal more and more information about themselves to compete with accelerators. More recently, studios have formed a global community—the Global Startup Studio Network—to connect with other studio leaders, share data and learn best practices, pool any related resources in order to help entrepreneurs thrive, and to help educate the public and generate more press around the startup studio model.



## COSTS

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Costs for prototyping are progressively declining, making it increasingly easy to rapidly prototype. While the same is true for everyone, studios are organized for the sole purpose of early-stage experimentation.

Experience, rigor, and pipeline matter. Studios can evaluate hundreds of business ideas in the time it might take a founder on her own to evaluate 10.

## NEW STARTUP HUBS

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With over two decades of talent expansion in tech startups, the talent pool has hit critical mass for startup hubs all around the world, not just in hubs like Silicon Valley (Atomic, Data Tribe), New York (Expa, Human Ventures), Tokyo, or Boston. In the second and third wave of startup studios, we've seen increasing U.S. expansion into secondary startup hubs like Boulder (Boulder Bits), Cincinnati (Differential), Guadalajara (Agave Lab), Helsinki (Founders),

and Indianapolis (High Alpha). Worldwide, the proliferation is expanding beyond European hubs to places like Bangkok (Alpha Founders) and Cape Town (Far Ventures). However, studios cannot succeed without the necessary talent, so studios often draw talent from the more expensive tech hubs because they provide instant network for seasoned entrepreneurs looking to achieve more with lower costs.

## FAILURE

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Interestingly, for the past 20 years, the long-term failure rates of independent startups haven't changed significantly. Despite the proliferation of lean startup and low-cost tools for entrepreneurs, failure rates are still just as high as they were a decade ago<sup>10, 11</sup>. One reason is that, without a strong network, startups simply fail. While the media loves to portray startups as the vision of a singular

individual, in reality, they're a group effort. Additionally, failure of VC's to increase the odds of success can frustrate investors.

Through the success of accelerators, startup experts are increasingly recognizing that the main way to reduce failure is to move the hard work and benefits of network to earlier stages.

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# Looking Ahead

Looking ahead at the future of studios, there are some clear indicators of what is to come. For example, with the recent inception of the Global Startup Studio Network, there's now a central place for studios to collect data, expand their networks, and learn from each other. We're seeing a rapid shift from anecdotal data to statistically relevant studies on startup studios. This shift will not only highlight best practices, but also shines a spotlight on the value of studios to investors, founders, and the global economy.

We're already observing increased investment into studios as a whole and on a per-studio basis<sup>12, 13</sup>. Barring any major downturn in the global economy, this trend is likely to continue. Investors are looking for new and creative ways

to invest in early-stage companies, seeing the growth they're capable of. Investors have learned that picking winners isn't as good as supporting winners with bigger and better networks, thanks to the increased availability of data out of companies like CBInsights, Crunch-Base, and Mattermark.

Through the plethora of new data available and increased inter-studio communication, we're starting to see a convergence on process, and divergence on focus, branding, and strategic advantage. With studios collaborating more, studios will become more competitive about how they attract talent, differentiate themselves, and define a network.

12. Eakman, Lindel. "Our Investment in High Alpha." Foundry Group, 27 Aug. 2018, [www.foundrygroup.com/blog/2018/07/our-investment-in-high-alpha/](http://www.foundrygroup.com/blog/2018/07/our-investment-in-high-alpha/).

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# Glossary

## Accelerators

Accelerators source startups for their cohort-based, mentorship-driven and short-term programs that provide the resources needed to help accelerate the growth of startups within their community. Accelerators take a smaller share in a larger number of 10-20 startups that go through each program.

## Angel Investor

An angel investor (also known as a business angel, informal investor, angel funder, private investor, or seed investor) is an affluent individual who provides capital for a business startup, usually in exchange for convertible debt or ownership equity.

## Board Seats

Studios often have rights to appoint one or more position on the board of directors of the portfolio companies they create. This helps align the studios and portfolio companies toward the greatest growth.

## Demo Days

Demo days are days where accelerators open their doors to investors, mentors, and community to present their portfolio companies. Startup studios rarely have demo days because startups spin out at different times and are not often capable of monetizing on the effort of pitching at the same time.

## Equity

Equity refers to the shares issued by a company. Equity is often used to indicate the amount, or percentage of shares owned in a company.

## Exit

A startup exit is where the startup and investors sell their stock, typically in an initial public offering, an acquisition, or a merger. Exits are the primary manner by which startup investors realize return on investment.

## Exit Rate

The exit rate is the fraction of portfolio companies that exit as an IPO, acquisition, or merger. Because exits are the prominent way by which investors realize return on investment, the exit rate is a good indicator of portfolio performance. In venture capital, the majority of returns are made from one or several outsized exits. Many exits providing small ROI may not yield significant portfolio ROI, whereas one giant exit may return enough to yield a larger ROI.

## Deal Flow

Investors often use the term “deal flow” to refer to the funnel of investment opportunities they have access to. A VC may look at thousands of startups and invest in 10. A studio will look at thousands of concepts, test dozens of projects, and invest in a few portfolio companies.

## Failure Rate

The failure rate is the fraction of portfolio companies that stop operating without an exit. Because failure typically results in little or no return on investment, failure rate is an important metric for measuring early performance of a portfolio. In venture capital, the majority of returns are made from a few outsized exits, so early failure rate may not be indicative of the ultimate ROI of a fund.

## Founders

Typically in the studio environment, founders refer to the founders of the portfolio companies, not the founders of the startup studio or venture builder.

## Incubators

Business incubators help create and grow startups by providing them with the support, financial, and technical services needed to expand. An incubator recruits startups already created and hosts them without taking a significant stake in each company. Studios and builders internally generate the

business idea, create the startup, take a substantial share in the company, and drive the company's development.

**Limited Partner**

A limited partner, or LP, is a partner in a company or venture who receives limited profits from the business and whose liability toward its debts is legally limited to the extent of his or her investment. LPs are the investors in a venture capital fund.

**Portfolio Company**

1) A company created by a startup studio. The studio typically retains equity in the subsidiary company, ranging from minority to majority ownership. The studio may invest further to obtain more equity or retain pro rata ownership.

2) A company invested in by an investor. In the studio context, a portfolio company may mean that the company was created by the studio or that the studio's venture arm invested in the the startup. It can be confusing.

**Seed**

Seed money, sometimes known as seed funding or seed capital, is a form of securities offering in which an investor invests capital in a startup company in exchange for an equity stake in the company.

**Series A (B, C, D, E, ...)**

A Series A round is the name typically given to a company's first significant round of venture capital financing. The name refers to the class of preferred stock sold to investors in exchange for their capital. Later investment rounds are labeled with subsequent letters, B, C, D, E, and so on. Typically, later rounds are larger, spurring additional growth. Later rounds may dilute earlier shareholders in percentage of ownership, but the goal is to increase the value of company much more than the dilutive effect at each stage.

**Side Fund**

A side fund is a venture fund managed solely or fractionally by the studio/venture builder. The side fund may solely invest in studio-born startups, in external startups, or both. Side funds infuse cash into

portfolio companies and fees often help support management of the studio.

**Startup Factory**

A company that creates startups in parallel. Thanks to its infrastructure and resources, startup studios increase a startup's chance of success and optimize its creation and growth. (Also See: Venture Builder, Venture Studio or Startup Studio.)

**Startup Studio**

A company that creates multiple startups in parallel. Thanks to its infrastructure and resources, startup studios increase a startup's chance of success and optimize its creation and growth. (Also See: Venture Builder, Venture Studio or Startup Factory.)

**Studio-Born Startup**

A company created by a startup studio or venture builder. This is a specific case of a portfolio company.

**Success Rate**

The success rate is the fraction of startups in a portfolio that succeed. Success can be measured in several ways, the most prominent of which is the fraction of startups that are still operating after some number of years. Investors are more interested in exit rate, which measures the fraction of startups that exit over the cycle of a fund.

**Venture Builder**

Another term for "startup studio." A company that creates multiple startups in parallel. Thanks to its infrastructure and resources, startup studios increase a startup's chance of success and optimize its creation and growth. (Also See: Venture Builder, Venture Studio or Startup Factory.)

**Venture Capital**

Venture capital is the capital, or money, invested in a project in which there is a substantial element of risk, typically a new or expanding business.

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