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CITY INCLUSIVE ENTREPRENEURSHIP NETWORK

Venture Capital for Black-Owned Startups

What is a startup?

While the definition of a startup is ever-changing, there are two characteristics that differentiate it from a ‘traditional’ business: growth and disruption. Startups are companies designed to grow very quickly. They also often try to disrupt an established industry through innovation (e.g., Uber’s rideshare model vs. the taxi industry). This is different from a ‘traditional’ small business, which is more likely to prioritize stability and sustainability, not sector domination or disruption.[1]

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To finance exponential growth, a startup will require some form of external capital. Early-stage funding usually comes from friends, family, or personal finances—with angel investors or venture capitalists providing funding as the startup grows. Though these later methods differ slightly, the transaction is mostly the same: money is given to help the startup’s business operations in exchange for equity, or a percentage of ownership in the business.

Venture Capital vs. Angel Investors[2]

VENTURE CAPITAL (VC)

- VCs are a type of business or private equity firm
- They invest pooled funds from Limited Partners (LPs), as well as their time to support a startup (portfolio company)
- They will usually have a portfolio of startups they believe have the highest growth potential
- They provide capital in exchange for startup equity

ANGEL INVESTORS

- An angel investor is an individual
- Like a VC, angels are offered equity of the startup in return for their investment
- Angel investors are often other entrepreneurs who use the money they've earned to finance other startups (as opposed to a pooled funding source like a VC)
- Angel investors do not typically invest more than $1 million

What is Equity[2]

In short, equity is a "stake" in a company. It refers to the number of shares of the company a person or entity (employee, investor, co-founder) owns.

Why venture capital?

When an individual has a new idea or technology for a business, they may not have an established lending relationship, wealthy friends, or family financing to rely on. This is a familiar experience for many Black founders who, no matter their own financial status, tend to be less visible to affluent investors.

Moreover, there are stark demographic contrasts between those who receive startup capital and those who don't, along racial, ethnicity, gender, and location lines. Entrepreneurs from similar geographies or backgrounds as VC or angel investors have easier access than those who are from more financially disadvantaged backgrounds.[3]

The lack of capital to Black founders not only prevents these businesses from reaching their full potential, but it also has devastating effects on the U.S. economy. According to Accenture, this funding gap caused the country to lose $67 billion in business opportunities between 2016 and 2020.[4]

> **“Receiving $50k, $100k — and sometimes more — from family and peers is not part of the average Black founder’s journey. Personal loans, credit, and day job salaries often serve as a substitute for readily accessible capital from their social network.”**
>
> **James Norman**, Harvard Business Review

What can local governments do?

While not yet abundant for Black founders, venture capital is a critical financing method for businesses deemed too ‘new’ or ‘risky’ by typical lending institutions. Since VC is a way of securing both financial and human capital, venture capitalists have specific expectations in return for their investment: growth rate, business timelines and return on investment are some examples, to name a few.

Furthermore, founders must navigate a complex universe of terms and conditions to determine whether they are prepared to meet VC investment. Various training resources for traditional borrowing, whether from a bank or a community development financial institution (CDFI), exist. Yet similar support services for venture capital are less common.[5] Before committing themselves fully to VC financing, startup founders must first understand the fundamentals of VC investment, and if it’s appropriate for them and their business.

NLC’s City Inclusive Entrepreneurship (CIE) Program partnered with Collab Capital, an Atlanta-based VC, to support cities through the Ownership and Optionality commitment. This commitment seeks to promote and build the infrastructure for early-stage Black-owned companies to access the capital, networks, education, and mentorship opportunities they need to grow.

NLC and Collab Capital worked with five cities to identify innovative, Black-owned businesses and either support them in applying for investment via Collab Capital’s profit-sharing model or match them with larger suppliers for guidance and mentorship. In all five cities, economic development staff worked with entrepreneurial support organizations with deeper connections to local diverse founders.

How Washington D.C. and St. Louis, MO are closing the financing gap for Black founders

Through CIE, Washington D.C.'s Office of the Deputy Mayor for Planning & Economic Development (DMPED), saw an opportunity to complement their existing work by utilizing the expertise and network of Collab Capital. Recognizing that mentorship was the first step in supporting their entrepreneur system, DMPED's Senior Tech, Equity & Inclusion Manager Joycelyn James looped in the Coalition for Nonprofit Housing and Economic Development (CNHED) to tap into their prominent anchor institutions collaborative.

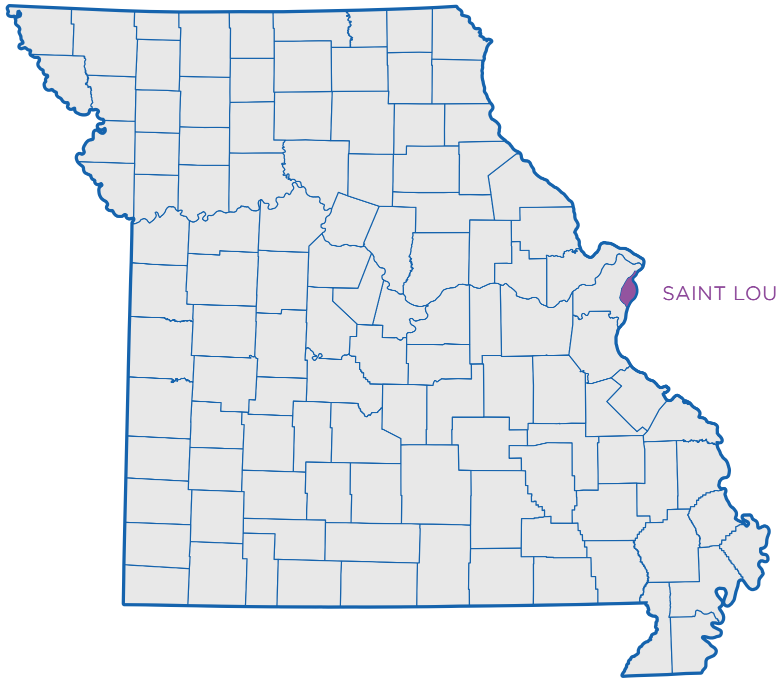
Since startups usually need a verifiable track record and proven business model to secure venture capital, DMPED and CNHED created a way to forge mentorship relationships with 11 prominent anchor institutions committed to supporting the growth of local minority-owned business enterprises (MBEs) through procurement.

So far, the team has made significant progress in building capacity for founders of color, getting them ready for their next stage of financing by:

1. **Connecting** Collab Capital to the BLCK VC DMV network to share insights about penetrating the D.C. market
2. **Creating** a Guide to Small Business Financing, as well as an RFP Response Strategy Toolkit
3. **Identifying** Cedar Hill Regional Medical Center, a $375 million, 136-bed, full-service hospital project as a large contracting opportunity (scheduled to open in December 2024)

"The economic health of a community doesn't lie in its business failure rate; it lies in its business formation rate. Venture capital is one of the biggest barriers to business formation."

Stephen Glaude, President and CEO Coalition for Nonprofit Housing and Economic Development (CNHED)



In St. Louis, Missouri, Mayor Tishaura Jones' office committed to supporting WEPOWER's efforts in connecting Black founders to VC and mentorship. WEPOWER has already begun developing a database of all Black- and LatinX-owned businesses, and VP of Community Wealth Building Yoni Blumberg has identified five of those to connect to Collab Capital for future investment conversations.

Blumberg and the WEPOWER team have also organized workshops where more established enterprises share their story and tactics for winning large contracts with earlier-staged businesses. For example, Pure Catering is the only registered minority-owned catering business in the state of Missouri and is designated as a "Preferred Caterer" in 15 major venues around St. Louis.[6] In addition to catering banquets, weddings, and other special events, Pure Catering provides nutritious meals for several government daycares, city shelters, summer camp programs, the Missouri History Museum café, and all of St. Louis' Head Start programs. By inviting co-owner Tim "The Caterer" Eleby to speak to their recent cohort, the startups in WEPOWER's network were given examples of how they can establish the traction VCs and other investors look for.

Conclusion and key takeaways

Access to capital is necessary for startups to succeed, and venture capital allows for a quick infusion of cash that may not be accessible elsewhere. Though a powerful financing method, founders should proceed carefully before pursuing venture capital. Local leaders and support organizations should systematize resources so more capital, mentorship, and education are available to Black entrepreneurs. This approach would not only benefit Black business owners, their families, and communities, but also the U.S economy as a whole.

- **Recognize Black founders as their own entity.** Identifiable sectors get resources, yet Black founders still have a long way before becoming an accommodated asset class. If we can see Black founders as a concrete part of the larger ecosystem, it will be easier to allocate attention and resources.

- **Ecosystem builders must understand the limits of their expertise.** City leaders should recognize when other entities are better connected to diverse founders than they are. Partnering with trusted partners in this space helps build founder relationships.

- **When elephants fight, the grass always loses.** The ecosystem which serves minority businesses tends to be more fragmented with fewer resources and should be shielded from competition between internal players as best as possible.

Endnotes

1 https://launchvic.org/files/LV-Startup-Guide.pdf

2 https://www.businessnewsdaily.com/4252-venture-capital.html

3 https://www.transparentcollective.com/who-we-are.html#/

4 https://www.accenture.com/us-en/blogs/accenture-research/how-to-improve-diversity-at-the-enterpriselevel-invest-in-black-led-firms

5 https://news.crunchbase.com/news/something-ventured-funding-to-black-startup-founders-quadrupled-in-past-year-but-remains-elusive/

6 https://wepowerstl.org/you-have-a-future-in-this/