FEATURES

Finding Cockroaches: Identifying Dynamics Of Becoming A Cockroach Startup In 2023

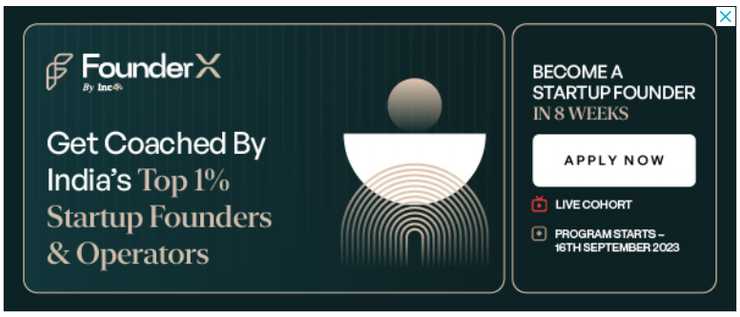
09 Feb'23 | By Meha Agarwal

- The year 2021 could have been a course correction, with more focus on cockroach startups that do not blow up money and refrain from being extravagant
- Given their lean and profitable nature, cockroach startups may not make themselves available to investors, say VCs
- Cockroach startups have a natural ability to survive in any macroeconomic, regulatory and competitive environment

"Chaos breeds innovation, and cockroach startups have the highest tendency to survive amid chaos," Ankur Bansal, cofounder and executive director, BlackSoil Capital.

If there is one lesson that the stakeholders of the Indian startup ecosystem could have learned early on is what led to the collapse of the dotcom bubble in the US between 2001 and 2002.

For the uninitiated, the dotcom bubble in the US collapsed between 2001 and 2002 when the tech-heavy NASDAQ tanked more than 75%, burning billions of dollars of investor money.



The major reason behind this crash was the heavy infusion of VC money into internet-based startups, which failed to emerge profitable or even generate sustainable revenues. Pertinent to mention here is that such fad-based investments, at one point in time, bloated the valuations of US tech stocks, which eventually came crashing down.

Does it ring a bell!

If not, the Indian startup ecosystem is in a similar state of affairs. After the peak pandemic year of 2020, the year 2021 could have been on a course correction, with more focus on cockroach startups that do not blow up money and refrain from being extravagant. Instead the year saw the entry of 44 unicorns to the club in the same year, the highest so far. Not only this, despite the funding winter of 2022, the year added another 21 unicorns, skyrocketing the total unicorn count to 108 in India.

At the same time, we saw most unicorns across sectors posting heavy losses in FY22 and resorting to layoffs [now reaching 21K+] to minimise their costs in FY23. Also, as per one of Inc42's October 2022 report, around 10 startups are in danger of being locked out of the unicorn club due to the ongoing fluctuations in the dollar-rupee exchange rate.

> "Whenever there will be excesses in any economy, there will be a cooling off period which is also known as the funding winter. We saw excesses globally in 2009 and again in India in 2016 and then in 2021, when startups received funding without too much merit. Due to the excesses in 2021, and realisation of the same in 2022, 2023 will most likely bear the brunt of the actions that startups will have to take, to stay afloat," said Yagnesh Sanghrajka, cofounder & CFO, 100X.VC.

Dynamics That Will Push For Cockroach Mentality In 2023

Higher sentiment toward consolidation

Especially among startups that have raised a lot of capital but haven't yet built a sustainable business.

Increased competition

Small handful of startups that are doing incredibly well, with strong growth and excellent economics will move aggressively to capture market share.

Revenues are likely to decline

Especially for startups that primarily sell to other startups and tech companies.

Consumer discretionary spending will be fragile

Many founders recognize this and are aggressively right-sizing their startups to be consistent with the new revenue reality, reducing their net burn.

More pivots

Sectors characterised by high marketing costs to acquire customers and unsustainable unit economics are expected to pivot.

More collaboration

Through a collaborative approach, startups can benefit from corporate funding, resources, and customer access.

Source: Industry inputs

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Where Are My Cockroaches?

Although it is not going to be easy to find cockroaches from a plethora of other startups in the Indian ecosystem, investors, we spoke with, have hinted at the sectors and business models that could be fostering them.

Sector-Wise Search For Cockroach Startups

In general, whichever sectors historically required high amounts of capital in the early stages to grow will be the first ones to realise the importance of capital efficiency.

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According to BlackSoil's Bansal, any sector can have the emergence of cockroaches, but they are often seen in industries that are characterised by:

- High volatility and uncertainty where traditional business models are challenged
- Have limited access to capital (as such startups rely on their own resources and creativity to sustain and succeed)
- Disruptive technology to create opportunities and challenge established players

Look Out For Cockroaches: Key Sectors On Investors Radar In 2023

Sectors with high probability of producing cockroach startups

Deeptech, Spacetech, Agritech, Media and Entertainment, Real Estate Tech, Cleantech.

Sectors which may see more pivots

B2C Ecommerce, Online travel, Grocery delivery, Fintech, Edtech, Consumer services.

Sectors which may see more collaborative approach

Fintech, Healthtech, Agritech and Real Estate.

Sectors which may focus more on profitability than valuation

Fintech, EdTtech, Ecommerce, Consumer services.

Source: Industry inputs

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Searching Cockroaches In Business Models

Instead of specific sectors, Abraham Thomas, currently the venture partner at Merak Ventures, likes to think of cockroach startups in terms of business models.

Some business models depend on easy access to capital to grow. They have high fixed costs, large capital commitments towards product development, highly leveraged balance sheets, unfavourable cash cycles, and expensive customer acquisition practices. Startups with such kinds of business models will struggle in 2023.

Conversely, startups which are frugal and asset-light and efficient in their customer acquisition and service delivery should find it easier to survive, and that's where he expect to see lots of cockroaches emerging. It doesn't matter what sector they're in.

> "As investors in deeptech, spacetech, tech-enabled enterprise, or similar categories, we have observed that you can be extremely frugal and efficient even in an area that requires a lot of R&D and genuine innovation. It all comes down to having a culture and DNA of moving fast and doing more with less," Thomas added.

Stage-Wise Search For Cockroach Startups

Startups that can monetise early, speed up their product features and start charging their customers will become cockroaches and be able to survive in 2023 and beyond, even when there is a funding drought.

> "In 2023, we may see more cockroach startups at seed stage as the mortality in this stage is the highest," 100X.VCs Sanghrajka highlights.

Sharing his point of view, Blacksoil's Bansal said, it is also prudent to categorise them based on why they are called cockroaches – a high survival instinct.

> "A cockroach startup is an ideal fit for an investor who wants to delve deep into the startup world. However, given their lean and profitable nature, these startups may not make themselves available to investors," he added.

How Can You Become A Cockroach In 2023?

Cockroaches have the innate ability to survive in the direst of situations. According to Blacksoil's Bansal, this instinct is derived or achieved by a startup through its ability to survive with minimal funding (largely bootstrapped), high attention to profitability (EBITDA +ve), pre-identified and a well-catered captive market, low or highly calculated cash burn, spending less on fixed assets such as an office, low CAC, and not underpricing the product (direct or in-direct), dreaming to monopolise some day.

Other imperatives to note are that cockroach startups have a natural ability to survive in any macroeconomic, regulatory and competitive environment. An example of a perfect cockroach startup will be one that would hardly get impacted by any change or volatility in any of the aforementioned environments.

> "Among other things, becoming a cockroach startup is all about building a culture of frugality and speed; focus and discipline and cornering from non-essential goals to concentrating on what's critical. It entails clear-eyed honesty and commitment. The founders of cockroach startups don't fool themselves about their product, market or finances, rather take necessary steps to survive and thrive," Merak's Thomas said.

Key Areas Startups Should Focus On To Become Cockroach Startups In 2023

Product-market fit :

Startups need to ensure that they have a product or service that meets the needs of their target market. This involves understanding customer needs and developing a product or service that addresses them.

Scalability :

Startups need to focus on building a product or service that can be sold at scale, with minimal marginal costs. This will enable them to grow quickly and efficiently.

Revenue generation :

Startups should focus on generating revenue as early as possible. This will allow them to fund their growth and pay their bills.

Cost management :

Startups should focus on managing their costs, so that they can survive even in difficult economic environments.

Adaptability :

Startups should be able to adapt quickly to changing market conditions, customer needs and technology trends.

Strong team :

A strong team with diverse skills and experiences is crucial for startups to navigate the challenges and uncertainty of the startup journey.

Source: Industry inputs

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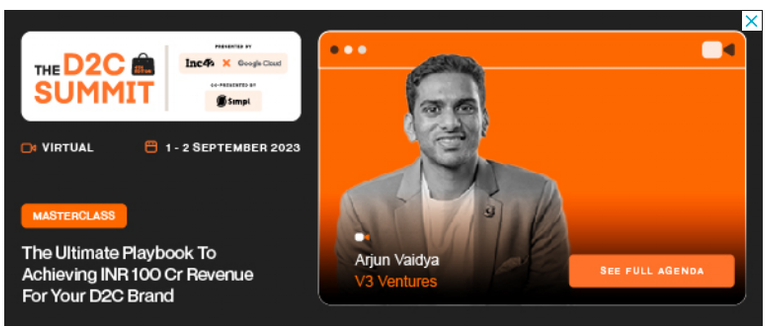
According to experts, to build a cockroach startup, founders will have to stay true to what they're building and be prepared to commit to that journey.

Further, what is going to change in the Indian startup ecosystem is the environment of easy capital availability and lavish growth trends. Amid this, the founders who will create sustainable startups will be the ones to roll up their sleeves and build a business that is resilient to external shocks and largely independent of investor capital.



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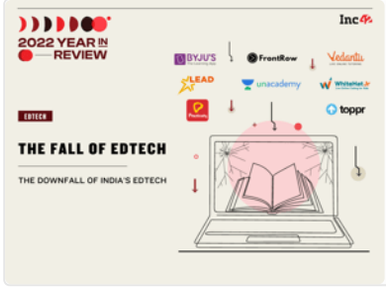

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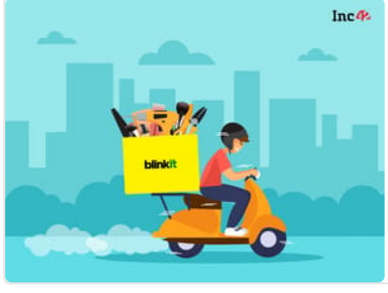

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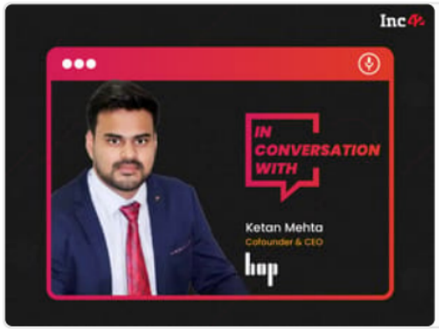

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