

Workshop on Start-up Exits: Modalities, Impacts and Policies

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Organised by the OECD Centre for Entrepreneurship, SMEs, Regions, and Cities (CFE) and ICSB

What's the issue?

On average, more than half of new business start-ups in OECD countries exit the market within 5 years of incorporation.

Start-up exits are often misunderstood as failures. However, there are many kinds of start-up exits, including private acquisitions, public listings (IPO), and voluntary liquidations, not just bankruptcies, and exit can represent success as well as failure. Moreover, failure itself can result from a range of chance factors as well as from strategic or operational errors. And even when not successful, exits can be a source of learning for the entrepreneur that can help them to re-engage and generate new successful ventures.

There are potential opportunities from exits if policy can facilitate the founders to restart or invest in other entrepreneurial ventures. To design policy effectively, governments need a better understanding of the nature of start-up exits, of what founders go on to do following exit, and of the barriers that exist to entrepreneurial recycling.

This workshop, organised by the OECD and the ICSB, looks at the issues, focusing on two, quite different, broad types of exits. At one end of the scale, there are rapid-growth scale-ups, or blockbuster entrepreneurs, characterised by the sale of the business by the founder. The exiting entrepreneur can then potentially re-use their experience, networks, and capital in new ventures as serial entrepreneurs, investors, or mentors. Such recycling can be encouraged by a range of policies, including taxation regimes or matchmaking with new entrepreneurs or investor groups or other ecosystem actors. At the other end of the scale, there are standard entrepreneurs whose businesses close but may be successful in subsequent entrepreneurial projects. Here policy can assist in various ways, for example with early intervention or insolvency regimes that help manage the exit in an orderly and timely way and by the offer of business advice and finance for restart.

Presenters and moderators

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Introduction

Roberto Crotti (OECD)

Are start-up exits failures?

The OECD has launched an initiative to better understand current issues and policies for start-up exits and entrepreneurial recycling. Start-up exits are often mistakenly equated with failures, but they may also represent success. Furthermore, even in the case of a failure, the entrepreneur may leave with learnings that are important for future entrepreneurship.

A basic distinction can be made between the highly successful exits of start-ups that rapidly scale-up and are sold, with the founders potentially reinvesting in new businesses, and less dynamic start-ups where the exit may result from failure, but where there is potential for second-chance entrepreneurship.

The modalities of scale-up exits include private acquisitions or trade sales, special purpose acquisition companies (SPACs), public listings (IPO), and buyouts (by management or employees). Often, these entrepreneurs use their newly acquired capital and experience to create further ventures (Montanaro et. al. 2021). This can lead to continual innovation and venture creation in a process of serial entrepreneurship. In addition, the entrepreneurs may make investments in their local entrepreneurial ecosystems, for example by investing in or mentoring other up and coming start-ups or helping develop leadership to conceive and broker new collective actions for the ecosystem.

Second-chance entrepreneurship often relates to unsuccessful exits, where the exit routes may involve voluntary liquidation and bankruptcy. However, restarts by the founders can benefit an economy, through the re-injection of the knowledge, experience, contacts, and resources that entrepreneurs built through their first venture attempts, and the application of entrepreneurial learning to new projects (Shepherd et al., 2000; Starr & Bygrave, Politis, 2005).

What are the potential modalities of exits and subsequent activities?

There are few data sources that track start-up founders during and after their exit. However, data opportunities have recently been improving. Available data include the OECD's Structural and Demographic Business Statistics, which provide aggregate information from business registries on business creation and exit; the NCVA/Pitchbook Venture monitor, which tracks venture capital investments/disinvestments in start-ups; Crunchbase, which tracks start-ups and how they exit (acquired/closed/IPO); and the Global Entrepreneurship Monitor, which surveys entrepreneurs on reasons for quitting and gives information about business continuation after exit.

Entrepreneurs' career options after exiting include:

- i. Continue being an entrepreneur, either by either developing new ventures in parallel with existing businesses (portfolio entrepreneurship) or by starting a new venture after ending another (serial entrepreneurship).
- ii. Use the financial gains from a successful exit to become a business angel or venture capital investor.
- iii. Stop being an entrepreneur (retire or find regular employment).
- iv. Entrepreneurial philanthropy (Mason and Brown, 2014, DeTienne and Robb, 2016, Clayton et al., 2021).

What are the policy questions?

Several policy questions are still open. These questions include:

- i. To what extent do exits represent failure or positive aspects of the development of the enterprise and/or the entrepreneur?
- ii. What can be done to encourage successful entrepreneurs to re-engage in entrepreneurial ventures?
- iii. Can policy be effective in helping entrepreneurs to restart after a failure?
- iv. To what extent do foreign venture capital (VC) investments, and foreign corporate takeovers of start-ups that give VCs an exit, encourage the outward relocation of start-ups/founders and limit reinvestments in the origin ecosystem, and what should be done about it?
- v. To what extent do insolvency regimes limit re-engagement of entrepreneurs after a bankruptcy event?

The importance of insolvency regimes for second-chance entrepreneurship

Insolvency regimes can be costly and time consuming for exits, both in terms of bankruptcy regulations and contract enforcement procedures through the judiciary ([OECD 2016](#)). This may discourage business re-entry. There is certainly evidence in general terms that the quality of insolvency regimes can affect start-up rates ([OECD 2016b](#); [Lee et. al. 2011](#), [Prusak et. al. 2021](#)).

In theory, insolvency regimes should aim to:

- i. incentivise the restructuring of viable firms and the liquidation of non-viable ones at low cost,
- ii. balance the interests of the parties involved to ensure an equitable resolution without discouraging future risk-taking by investors and entrepreneurs,
- iii. provide for a timely resolution of insolvency.

The main difficulty is finding the right balance between implementing fast and low-cost procedures and protecting the rights of all stakeholders.

The OECD has created a composite index that measures the effectiveness of insolvency regimes. The tool combines thirteen dimensions: 1. Availability of discharge and time to discharge (i.e. the number of years a bankrupt must wait until they are discharged from pre-bankruptcy indebtedness); 2. Extent of exemptions of assets of the debtor that are not directly linked to the business (e.g. the family house or a spouse's assets); 3. Early warning tools (e.g. training and financial counselling to companies), 4. Extent of pre-insolvency regimes (e.g. the possibility of discussing creditor options for restructuring), 5. Special procedures for SMEs (e.g. simplified or pre-packaged in-court proceedings or the possibility to have instalments in the payment of administrative costs), 6. Creditor ability to initiate restructuring, 7. Availability and length of stay on assets, 8. Possibility and priority of new financing, 9. Possibility to "cramdown" on dissenting creditors, 10. Treatment of management during restructuring, 11. Degree of court involvement, 12. Distinction between honest and fraudulent bankrupts, 13. Rights of employees. ([OECD 2018](#)).

Many countries have introduced reforms to their insolvency regimes that may be effective in facilitating second chance entrepreneurship as well as promoting start-ups and scale-ups generally. For instance, in 2019, the European Parliament and European Council approved the Amendment (2019/1023) to the Directive on Restructuring and Insolvency, which includes:

- i. common principles on early restructuring tools, which would help companies to continue operating and preserve jobs.
- ii. rules to allow entrepreneurs to benefit from a second chance through a discharge of debt; and

- iii. targeted measures allowing Member States to increase the efficiency of insolvency, restructuring and discharge procedures.

EU Member States are called on to transpose this into their own legislation.

Overall, the latest edition of the OECD insolvency framework indicator shows that, across the OECD area as a whole, some countries have progressed significantly while others moved backwards in improving insolvency regimes between 2016 and 2022 ([OECD 2022](#)).

Exits and re-engagement, statistical evidence from GEM data

Jonathan Levie (University of Galway)

The Global Entrepreneurship Monitor collects information on business exits by asking individuals if they have sold, shut down, discontinued, or quit a business they owned and managed (including self-employment) over the past 12 months. These data help shed light on the reasons why entrepreneurs exit and whether they re-engage in entrepreneurship after exit.

The questionnaire enables us to distinguish between entrepreneurs who quit and close the business and those who quit but the business continues. In a pooled sample of 32 OECD countries surveyed from 2015 to 2019, among those who quit and closed the business, the main reasons for quitting were unprofitability (30%), personal factors (16%), access to finance (13%), and another job or business opportunity (9%). Among those who quit but the business continued, the main reasons were personal factors (21%), unprofitability (15%), another job or business opportunity (12%), and an opportunity to sell the business (12%). During the COVID pandemic years from 2020 to 2022, 27% of those who quit and closed the business cited the pandemic as the main reason for closing, compared with 16% of those who quit but the business continued.

In terms of re-engagement, data show that 58% of those who quit but the business continued, and 43% of those who quit and closed their business expect to start a new business within three years, while only 17% of non-entrepreneurs expect to do so. There are however significant country variations. Notably, in European countries, both business exits and re-engagement are relatively low, while in North America and Latin America both business exits and re-engagement are high.

Education, income, and gender affect exit strategies and re-entry propensities. In terms of exit strategies, high-income males (across all education levels) are more likely to quit a business that continues relative to high-income females and low-income males with low education levels. The latter groups are more likely to shut down their business as they quit. Re-entering intentions exhibit a U-shaped relation with education. Males with high or very low levels of education tend to re-engage more than males with middle levels of education. Among females, highly educated entrepreneurs tend to re-engage less than men, suggesting that many potentially capable female entrepreneurs re-engage less than we might otherwise expect.

Potential policy implications from these data are:

- i. Since re-engagement is relatively more likely among lower-educated entrepreneurs, there could be training opportunities for them to improve their business management skills.
- ii. Higher post-exit disengagement rates among highly educated females suggests that gender affects the likelihood to quit and not re-enter. Policymakers need to better understand what role gender and other demographics play in exit dynamics.

Recycling from unsuccessful exits, evidence from Swedish and Australian data

Anna Jenkin (University of Queensland)

Data from Sweden and Australia show that it is important to distinguish between start-up failures and small business failures, because differences in their latent business models influence their causes of failure and their post-failure outcomes.

Start-ups' business models emphasise scalability. They tend to: i. focus on revenue growth rather than profitability, ii. have few tangible assets, iii. be amenable to investment, and iv. be driven by a founding team who separate their personal finances from start-up finances. The main cause of start-up failure is the exhaustion of investment runway before reaching a positive cash flow and a lack of product-market fit.

Small businesses' business models tend to focus on profitability, use tangible assets, often use self-funding (at least of half of sampled SMEs have business loans with personal finance guarantees), require employees, and emphasise maintaining a positive cash flow. The main cause of small business failure is declining cash-flows, often driven by a combination of simultaneous negative events.

Based on post-exit information from a sample of 140 start-ups in Australia that went through the same commercial accelerator programme, just under half (67 start-ups) were still active six years later (with seven of these being "high growth" with 20 or more employees), three of the start-ups had sold and the remaining half (70 start-ups) had shut down after 4 years (on average). Among entrepreneurs who shut down, 20 had founded a new business. Among these restarters, there is a high incidence of serial/portfolio entrepreneurs. The business they closed is just one of the many they are working on. Approximately 50% returned to paid employment. In some cases, the start-up experience translated into well-paid employee positions that value innovation management skills. Qualitative data show that formal shut-down can take up to 3 years after founders decided to stop working on their start-up. This means that a share of formally active start-ups is already on a shut-down trajectory.

Small businesses' post-failure information is available from a sample of 265 founders in Sweden who had owned and operated a business that went bankrupt. Over a half of these SMEs founders returned to paid employment after closing their business, about a third restarted, and about 20% was unemployed. Even among those who re-started or could find new employment, almost half claim that their financial situation has worsened after they shut down their failed business.

There is a human dimension to unsuccessful exits. In start-ups, even if registered as a corporation or limited liability company, shutting down the business generates a high level of stress and disappointment. In small businesses, stress levels and exhaustion can reach extreme levels, especially when shutting down the business converts into high personal debt. Stress levels increase even further when the decision to shut down is delayed. Even after the business stops operating, it can take several months and up to two years to deal with the administrative aspects of closing the business, adding to the personal stress levels.

Both pre-exit and post-exit policy interventions can be considered to support recycling from unsuccessful start-up exits. An important pre-exit policy could be the creation of systems (e.g. help lines) that help start-ups in identifying when they are on a negative trajectory so that they shut down before they hit their "rock bottom".

Post-exit policy interventions could include reducing the administrative burden of closing a business, improving access to unemployment benefits, and introducing programmes that can support the entrepreneur in re-building. For instance, the Australian ABERA's Restart Smart programme provides motivation, coaching,

recommendations, and support to entrepreneurs who shut down their business, as well as connections, links, and introductions for restart.

Recycling from high-growth start-up exits

Ross Brown (University of St. Andrews)

There are relatively few high-growth start-ups, but they can generate a large impact on entrepreneurial ecosystems when the founders exit, whether through firm merger, acquisition by another firm, or liquidation.

High-growth firm exits produce “harvest events” that can be exploited in their local entrepreneurial ecosystems particularly when they concern equity-funded, high-tech start-ups. For example, this may involve the movement of talent into other entrepreneurial ventures locally, reinvestment of the proceeds of sales into new local businesses, or exploitation of ideas or intellectual assets that were not carried over in new businesses.

In some cases, the cashed-out founder re-invests in other start-ups locally either directly or as a business angel or venture capitalist. An example is Gareth William, who invested in over 20 other new ventures in Scotland after selling his start-up firm Skyscanner, which was one of Scotland’s technology unicorns. Many of the former employees of a start-up exit may also start up new ventures in the same location, as in the case of the demise of RIM (Blackberry) in Waterloo, Canada. Entrepreneurial know-how can also be transferred from exits to other firms in their entrepreneurial ecosystems through mentoring and advice by founders to new businesses and by transfers of knowledge as employees move to new firms.

A policy implication is that support to high-growth start-ups can be beneficial for the entrepreneurial ecosystem, even if the firm exits. However, some experts suggest that the government should have a minor role in entrepreneurial recycling, while others are in favour of an active public role.

A possible active policy role is for policy makers to provide longer duration or larger value investment support to retain the high-growth start-up firm for longer. This could see it grow more and put down more local roots. This helps respond to the problem that the local recycling benefits of exits may be limited if high-growth start-ups cash-out too soon.

A second possible active public role could be matchmaking to help cashed-out founders find local start-up entrepreneurs for re-investment.

Winslow Sargeant (Genaesis):

Ecosystem actors may also be advised to encourage leaner start-ups amongst technology and equity-based ventures. Lean start-up involves a methodology that tests the appeal of minimal viable products and collects feedback from different customer segments. This allows the enterprise to shorten its product development cycles and rapidly discover if a proposed business model is viable. Lean start-ups could be expected to be more efficient, less likely to exit with big losses, and more likely to recycle quickly into new firms.

Conclusions and next steps

The workshop collected initial views and information on start-up exits and entrepreneurial recycling, taking a first step towards identifying policy issues and possible areas for intervention.

Two important conclusions from the workshop are:

1. Exit should not be seen as failure. Many exits are not due to financial difficulties and many entrepreneurs who quit a business start again.
2. There is some space for policy intervention to support recycling. For example, helplines and advice could help firms to identify the best time to exit, regulatory changes could ease administrative aspects of firm shutdown to support restart, and recycling of high-growth starts could be encouraged by matching cashed-out founders with emerging start-up opportunities.

More understanding is needed of issues and policies in this area. For example, there is not yet full understanding of what public policy could do to foster lean start-ups. Another issue is whether acquisitions of start-ups by foreign multinationals harm the host ecosystems and what policy makers could do to minimise adverse effects without discouraging investments. A third issue is how policy could support second-chance entrepreneurship, for example with better insolvency processes and support to founders for rebuilding. A fourth issue is why some demographics appear more likely than others to quit and not re-enter.

Acknowledgement

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The OECD Centre for Entrepreneurship, SMEs, Regions and Cities provides comparative statistics, analysis and capacity building for local and national actors to work together to unleash the potential of entrepreneurs and small and medium-sized enterprises, promote inclusive and sustainable regions and cities, boost local job creation, and support sound tourism policies.

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