

Startups surviving a slump: What it takes to make it through a downturn

By Louis Lehot, Esq., Foley & Lardner LLP

JULY 25, 2023

Startup entrepreneurs are the ultimate risk-takers, innovators, and disruptors no matter the economy, and no matter their stage of growth, economic slumps, and downturns pose unique challenges. Leanly capitalized pre-revenue startups will struggle to get their minimum viable product into commercial shipment without a healthy seed capital market.

Companies that have established that they can ship products and get to one million dollars or recurring revenue will need a Series A financing to scale or hyper-growth mode. Post-Series B or Series C companies will struggle to raise the next round or exit without maintaining strong double-digit growth in recurring revenue or if they can't do it without burning bonfires of capital.

History shows that startups that figure out how to survive and thrive during challenging times will dominate during the good times.

When market conditions become challenging, startups in every stage of growth face struggles to stay afloat and maintain their trajectory. We are seeing this play out now, with funding hard to come by and exit plans unable to get liftoff. These can be scary times for companies just getting off the ground, and many startups will fail in these market conditions.

But history shows that startups that figure out how to survive and thrive during challenging times will dominate during the good times.

Whether they pivot their business model, come up with a new and innovative solution, or capitalize on some new emerging trend, startups will need to adapt. Here are just a few examples of startups that found a way to succeed during challenging times. Notably, most of these launched during or after the 2008 recession, proving that sometimes great success can come from the most difficult situations.

Airbnb: Founded in 2008, Airbnb initially struggled and then flourished during the 2008-2009 global financial crisis. As people looked for affordable travel options, Airbnb's platform, which

allowed individuals to rent out their homes or spare rooms, gained popularity as a cost-effective alternative to hotels.

According to a Tanston.com article,¹ in 2007, Brian Chesky and Joe Gebbia found themselves struggling to pay rent for their San Francisco apartment. They decided to turn their spare room into a bed and breakfast for attendees of conferences in the city. This led to a platform connecting homeowners with spare rooms to travelers searching for affordable accommodation.

Square: Founded in 2009 by Jack Dorsey and Jim McKelvey, Square created a mobile payment solution for small businesses. During the economic downturn, their services gained popularity among small merchants seeking convenient and affordable payment processing options.

Groupon: Founded in 2008, Groupon's daily deals platform offered discounts on local services and products, appealing to consumers looking for cost-saving opportunities during the recession.

Venmo: Launched in 2009, Venmo provided a peer-to-peer payment solution that gained traction during the economic downturn as friends and family sought an easy and quick way to split bills and share expenses.

These examples show that successful startups during a downturn often address changing consumer needs, offer cost-effective solutions, and leverage emerging trends in the market. Their ability to adapt and provide value in challenging times contributes to their resilience and success.

Let's explore some key factors that contribute to a startup's ability to weather a slump and emerge stronger on the other side.

Adaptability and flexibility: One of the fundamental qualities that enable startups to survive a slump is their ability to adapt and remain flexible in the face of adversity. Successful startups understand that change is inevitable and are willing to pivot their strategies, products, or services to meet evolving market demands. Resilience has been described as the ability to recover quickly, but recovery alone is not an adequate goal. Organizations, resilient at their core, bounce back better and even thrive.

Cost control and managing burn: Prudent financial management becomes even more critical during a slump. Startups must prioritize cash flow management, optimize expenses, and ensure adequate

reserves to sustain operations during lean times. Building a buffer can provide a lifeline during a downturn, allowing startups to continue operating and seize opportunities when competitors might be forced to shut down. Continuously challenging expenses and doing more with less is a virtue in any economy.

Focus on core competencies: Startups focusing on their core competencies and key value propositions tend to fare better during a slump. It's easy to get distracted and attempt to diversify too quickly or enter unrelated markets during challenging times. However, successful startups stay true to their vision and strengths, doubling down on what they do best.

Prudent financial management becomes even more critical during a slump.

By focusing on their core offerings, startups can maintain customer loyalty, reinforce their unique selling propositions, and streamline operations. This targeted approach enables them to allocate limited resources more efficiently and effectively, increasing their chances of survival and subsequent growth.

Embrace innovation and continuous learning: Innovation is the lifeblood of startups, particularly in challenging times. Successful startups embrace a culture of continuous learning and innovation, fostering an environment where experimentation and creativity are encouraged. By actively seeking out new ideas, exploring emerging technologies, and staying ahead of the curve, startups can identify novel opportunities and differentiate themselves from competitors.

Additionally, startups should maintain strong lines of communication with customers, soliciting feedback and adapting their products or services to meet changing needs. Engaging with customers and understanding their pain points allows startups to tailor their offerings effectively, ensuring continued relevance and customer satisfaction.

Resilient leadership and team: Leadership plays a vital role in navigating a startup through a downturn. Resilient leaders possess a clear vision, inspire their teams, and remain steadfast in the face of adversity. They effectively communicate the company's goals and instill confidence in their employees, fostering a sense of purpose and determination. Leaders must maintain transparency, offer support, and motivate the team to persevere during challenging times.

Furthermore, startups should ensure they have a cohesive and agile team capable of adapting to changing circumstances. Hiring the right talent, fostering a collaborative culture, and empowering employees to contribute to problem-solving can make a significant difference in surviving a slump.

While economic slumps can be daunting for startups, they also present opportunities for growth and resilience. By operating leanly and focusing on the principles that will drive them forward, startups can survive and emerge stronger, positioning themselves for long-term success.

Notes

¹ <https://bit.ly/4778axw>

About the author



Louis Lehot is a partner with **Foley & Lardner LLP**, where he is a member of the private equity and venture capital, mergers and acquisitions, and transactions practices as well as the technology sector team. He advises entrepreneurs and their management teams, investors, and financial advisers at all stages of growth, from garage to global, and helps them navigate liquidity. He is based in the firm's Silicon Valley and San Francisco offices and can be reached at llehot@foley.com.

This article was first published on Westlaw Today on July 25, 2023.