Forbes insights

Midwest Rising:

Accelerating The New Tech Migration

IN ASSOCIATION WITH

MICHIGAN ECONOMIC DEVELOPMENT CORPORATION

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Introduction

From Detroit to Houghton and Ann Arbor to Grand Rapids, Michigan's startup ecosystem spans the entire state and covers a variety of industries. Fields like life sciences, cybersecurity, mobility, logistics and artificial intelligence are richly represented in the Wolverine State's startup scene. Universities that serve as research powerhouses, coupled with Michigan's considerable investments in launching new startups from the ground up, have also helped the local startup scene thrive.

The Covid-19 pandemic has put considerable strain on virtually every industry. But how has Michigan's growing startup scene fared during such an unprecedented climate? And which areas will drive its future? In this report, a partnership between the Michigan Economic Development Corporation (MEDC) and Forbes Insights, we assess what drives companies to Michigan and what challenges and opportunities lay ahead—based on the views and experiences shared in a survey of 505 executives and professionals from global enterprises.

SECTION I

The Effect Of The Startup Ecosystem

Michigan's reliance on the auto industry has faded in recent years, with new jobs surfacing in industries like medical devices, advanced manufacturing and technology. Michigan business leaders see the state's economic revival as directly linked to the diversification of its economy and startups as being the key driver of that change.

"Michigan's historically been so dependent on auto and advanced manufacturing that it's really essential that we leverage the fact that it doesn't matter where you are anymore, you can start a startup anywhere," said Patti Glaza, senior vice president and managing director of Invest Detroit. "Really continuing to invest in the diversification of our economy, I think, is probably the most important factor."

In recent years, Michigan has emerged as one of the fastest-growing startup powerhouses in the Midwest. According to an analysis of Pitchbook data, the state received 250% more startup investment between 2013 and 2018—a total of $1.4 billion—than it received in the five years prior ($577 million).

Mark Burton, MEDC's chief executive officer, said the state's growing tech hub is vital to its economic future. "There is no doubt that the innovation, and the ingenuity of high-tech startups throughout our state will continue to play a key role in helping Michigan emerge from this outbreak and put us in a stronger position," he said.

Startups, and the wealth of new ideas they generate, will continue to play an important role in the year ahead, the survey finds. The vast majority, or 87%, of executives agree that the new technologies, products and services generated by the startup ecosystem will continue to have an impact on legacy businesses. A total of 84% of executives polled believe that startups will continue to have a profound impact on society.

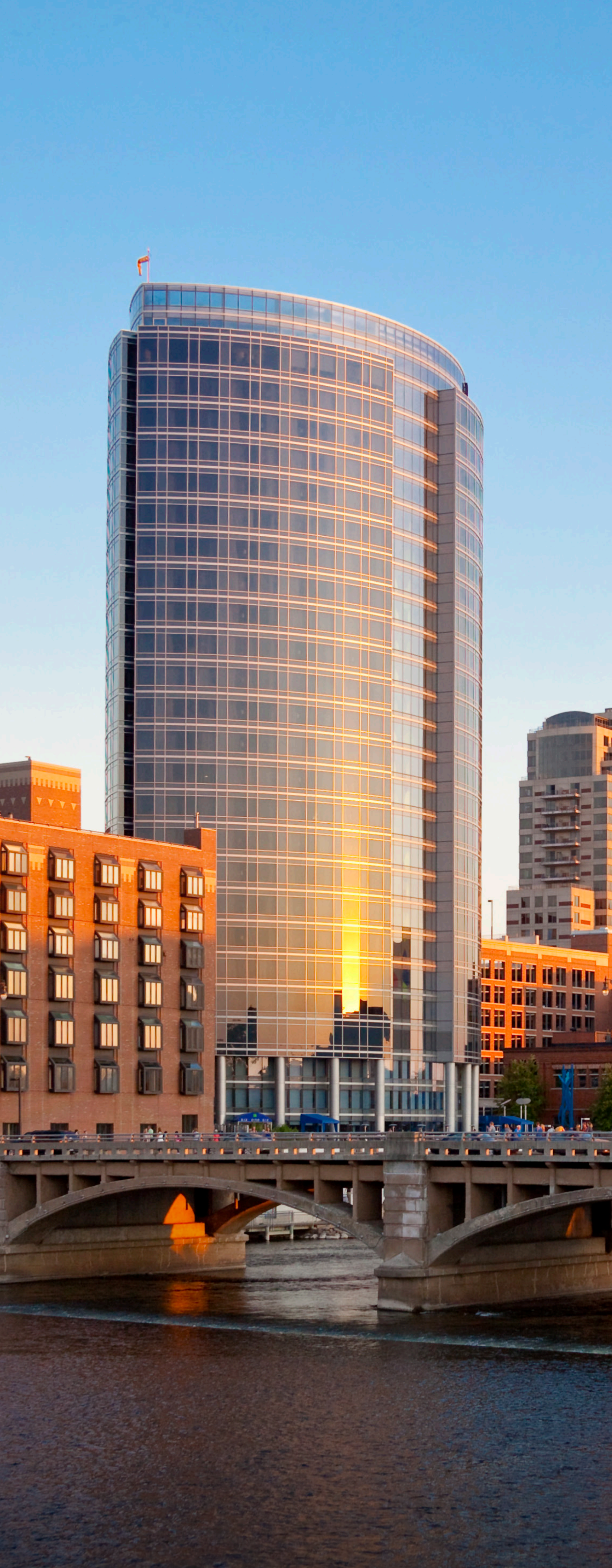
Just as the Covid-19 pandemic has taken a toll on most industries, it has also posed a challenge to startups. For the most part, VCs during the early months of the pandemic put a halt to investing as the market remained volatile. A total of 74% of executives agreed that economic uncertainty due to the pandemic has changed the course of startups. A significant number of executives (65%) also believed that the pandemic posed a threat to future innovation and entrepreneurship hubs.

David Corcoran, CEO of Ann Arbor-based startup Censys, witnessed the abrupt change to VC investment priorities firsthand. After Censys closed its first seed round last year, Corcoran said the plan was to start fundraising for the company's first Series A in early 2020. Unfortunately, the pandemic set the company off course. "All the VCs out there, basically in March and April, were doing damage control," he said. "They weren't really thinking about new investments unless it was something already in flight."

As the economy began to show signs of recovery in May, VCs began investing again. In August, Censys was able to raise a $15.5 million Series A. "The good news is that we were able to cut a deal with our existing investors," Corcoran said. "They already knew us, they saw the progress we've made, and they've seen what we've done over the course of the last year or so. And so while [raising the Series A] took us a bit longer than we had hoped, we got it done."

Despite the new hurdles stemming from the pandemic, executives are optimistic about their future. Investors and business leaders have noticed a positive turn in events, with the pandemic increasing the need for certain goods and services. A total of 73% of executives said that the Covid-19 pandemic is accelerating the pace of innovation.

"The needs of these startups, the problems they were solving, didn't go away because of Covid," explained Glaza.



Adapting To Uncertainty

- While venture capital funding briefly halted during Q1 due to uncertainty surrounding the pandemic, it has since recovered

- Before the pandemic, VCs were more selective about investing in tech startups that specialize in artificial intelligence and machine learning due to the overuse of such terms

- During the pandemic, VCs are looking closely for startups that they believe will be resilient in a new type of environment

- A shift to remote work may allow Michigan-based startups to recruit from outside the state or country, but will also lead to many people relocating from the coasts to areas with cheaper costs of living

- Tech startups have proved to be especially resilient during this time, due to their embrace of remote work and demand for their services

SECTION II

Advances In Remote Work And Mobility

Mobility and an accelerated virtual transition will no doubt impact startups. A total of 82% of executives believe that advances in transportation and mobility will continue to impact business profoundly, and slightly more (86%) believe advances in the field would continue to impact society. Most executives (83%) feel that advances in transportation and mobility are raising the bar for what it means to be competitive in today's workplace.

Investors saw the success of Michigan's industries as dependent on how well they keep pace with the future of mobility. "We've always been reliant on automotive, among others, agriculture, and there's med tech. And so those three industries have really been the core, and I'd throw advanced manufacturing into the auto sector," said Glaza. "Those industries have to keep investing and evolving. It's important to try and make sure that as mobility evolves, these industries are evolving with it."

MEDC has focused on mobility as one of the most vital areas of growth in Michigan's startup economy.

"When it comes to startup technologies in this mobility space, we look to jump on those as quickly as possible and begin to find partners for these startups to be able to test its proof of concept," said Burton.

As the region benefits from its strengths in the mobility space, startups can also take advantage of a major shift in the workplace landscape: remote work and the flexibility it offers. Only 47% of executives feel that remote work was vital to their companies before the pandemic. Now, 87% of leaders say that remote work has become vital to their companies.

Many companies and workers who resisted remote working before the pandemic have now been forced to undergo a virtual transition. Some in this group may choose to continue working remotely in the future, due to the flexibility and cost savings.

"So before Covid, I thought remote work couldn't work. I wasn't a big fan," said Glaza. "I thought that everybody really did need to sit in the same room together. I've changed. I think technology has come far enough now where you can simulate people feeling like they're in the next room."

Executives believe a transition to a remote workforce will bode well for the future success of companies, including early-stage startups. A total of 81% of executives believe that remote work will lead companies to be more productive and innovative.

If one hoped to build a large software company in Michigan before the pandemic, investors may have asked if founders would be able to find the right talent to build their workforce. Corcoran believes a transition to remote work has opened the door for Michigan companies to hire the most talented workforce, regardless of location. Meanwhile, the company's local employees will benefit from the state's business-friendly environment.

"I think we've all proven that we can work remote. So I think you can start an absolutely giant company in Michigan," said Corcoran. "I don't think it necessarily needs to be in Ann Arbor; it could be in Traverse City, it could be anywhere in Michigan. You can have an office for the people who are local and you can have a very distributed workforce that's all over the world, and I think you can make it successful."

Corcoran isn't alone in this optimism. A total of 84% of executives believed that as work becomes more virtual, innovation hubs will begin to thrive in new places. A total of 82% of executives believe that society will shift to more virtual engagements. Early-stage startups that may have been drawn to Silicon Valley or New York City due to their excess of tech talent and proximity to investors now have more options. A majority, 81%, of executives believe that remote work and advances in mobility would allow new cities and regions to emerge as startup powerhouses. And the same number feel that remote work would result in the workforce of startups being spread across a distributed network of places, rather than a specific city or location.

During this transition, Michigan stands at a unique advantage due to its tech-forward and innovative talent pool. The state is home to notable research universities—and it ranks in the top 10 for net tech employment, net tech jobs added and share of workers in the tech industry, according to CompTIA's 2019 Cyberstates report.

SECTION III

Michigan's Innovative Culture

Michigan's abundant tech workforce and innovative culture will drive its future growth. When asked to pick the top two most important attributes that would make Michigan an attractive hub for innovation, executives pointed to its growth in tech jobs and efforts to support emerging technologies. The largest number of executives (51%) said that Michigan's Office of Future Mobility and Electrification, which focuses on scaling up emerging technologies and businesses, was an important attribute in the state's attractiveness as a hub for innovation.

Such innovation wasn't put to rest during the pandemic. In order to meet an urgent need for personal protective equipment for the state's healthcare workers, MEDC Pure Michigan Business Connect program created the Covid-19 Emergency Access and Retooling Grants. The program awarded more than $1 million in grants to small manufacturers willing to shift gears and produce critical health supplies, from masks and gowns to oxygen concentrators for ventilators.

Population shifts due to the pandemic will likely lead to many seeking to relocate from coastal cities. Such transplants will likely benefit from a state that already has an existing innovation and entrepreneurship ecosystem. Three-quarters believe that the pandemic increased the value of being located in a region with a strong innovation and entrepreneurship ecosystem, and 73% agree that the pandemic increased the value of businesses located in less densely populated areas.

"I think [... Michigan] has a lot of advantages. Certainly the educated workforce. The IP and innovation that's spinning out of universities," said Glaza. "The state itself has really prioritized investment in entrepreneurship. The state has invested a significant amount of dollars in accelerator programs, in pitch competitions, in venture funds trying to make sure they're helping seed and propel our startup ecosystem."

73% agree that the pandemic increased the value of businesses located in less densely populated areas

SECTION IV

The Challenges Facing Startups

Slightly more than half (55%) of executives surveyed believe that startups will face significant challenges in the future. These executives were divided as to what form these challenges would take. A quarter (25%) feel that the number of startup powerhouse regions or cities would decrease, and that the density of such regions would disperse. A total of 26% of executives say that industries in which startups are involved would become less diverse. More than 3 out of 10 executives say that consumer spending on startup-driven products would decrease as a result of the pandemic.

But a significant group (30%) of leaders believe that startups will thrive and become more robust as a result of such unprecedented circumstances. Only 12% believe that the startup ecosystem will not change significantly.

A resounding majority (78%) of leaders say they had great confidence that society and business can aptly manage the challenges and risks associated with the pandemic. The same number of leaders say they had great confidence that society and business could manage the ethical and legal risks associated with the pandemic.

VCs will likely be more selective about the startups they choose to invest in and especially attentive to whether new companies can thrive under unpredictable conditions. "I will say that VCs became more choosy on what they were investing in. I think the standards are just different. You might see them as higher," said Corcoran.

The adaptable nature of startups will likely pose an advantage in the future. "Doing a startup is all about resiliency, and you're just constantly changing, and darts are getting thrown in there and you're dodging them," said Corcoran. "So, there's nothing more unpredictable than a global pandemic."

Burton said MEDC will continue to encourage investors. "We have and continue to encourage our venture capital and angel investor community here to consider using its dry powder," he said. "Continue to support entrepreneurs and technologies by injecting much-needed capital into the ecosystem right now."

SECTION V

The Appeal Of Higher Education And Livability

When asked to list the top three traits that allowed a city to maintain a strong talent pool, many leaders mentioned livability and quality of life. The largest number of executives (45%) believe that the livability of a city, including access to cultural institutions and walkability, played a top role in maintaining a strong local talent pool.

The state's livability is well known to its nearly 10 million inhabitants, whether they be city dwellers or reside in its many suburbs. Detroit's entertainment scene includes year-round festivals, four major professional sports teams and a number of top-rated museums. Michigan has made concentrated efforts toward smart growth and increasing mobility. For example, construction of The Hudson, a $1 billion "city within a city," is underway in downtown Detroit.

A total of 43% of leaders list advances in transportation and mobility as an important factor in retaining a talented workforce. Investment in higher education was also a popular choice among the leaders polled, with 42% listing it as an important trait in retaining a talent pool.

The state's fastest-growing areas are the suburbs and townships outside of Grand Rapids, Detroit, Lansing and Kalamazoo. Between 2010 and 2017, 53 percent of Oakland and Kent counties' growth was in semi-rural communities just outside the suburbs, according to an analysis of 2018 population estimates by the U.S. Census Bureau.

Michigan's cost of living is also 10% below the national average and ranks as the fourth most affordable state in the country. Living in San Francisco will cost you 62% more when compared to living in Detroit. Not to mention Michigan is surrounded by four of the five Great Lakes, boasting more freshwater coastline than any other state.

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SECTION VI

The Draw Of Innovation-Friendly Policies

Executives say that innovation-friendly policies (40%), business-friendly regulatory environments (40%) and low costs of operating a business (40%) are all leading characteristics of the Midwest that make it attractive for innovation. Michigan's cost of living is 10% lower than the national average, and it ranks as the fourth most affordable state in the nation. The state ranked 12th in the Tax Foundation's 2020 State Business Climate Tax Index—one of only two states in the Midwest to be in the top half of rankings. The state's favorable tax climate, as well as low cost of living, makes it an attractive site for growing new businesses.

Finally, regions that welcome new growth and promote entrepreneurship are expected to thrive more than others in the future. Four in five execs agreed that cities or regions that welcome and promote innovation and entrepreneurship will thrive more than other areas. Michigan has a steady track record of supporting local entrepreneurs through efforts such as MEDC's Entrepreneurship & Innovation initiative, which helps tech startups access funding and expert counsel. The state is well primed to continue to be a hub for innovation and growth in the future.

Conclusion

Michigan's status as a startup hub has shown clear growth over the years. As the state moves toward a more resilient future, executives and startup leaders should consider the region's many advantages. From a community that fosters innovation to a quality of life that attracts top talent, Michigan has the elements for a vibrant entrepreneurial ecosystem. As companies craft their strategies for the path ahead, they should take notice.

Learn more about Michigan's entrepreneurship ecosystem.

Methodology

The data in this report is based on a Forbes Insights survey of 505 executives in the United States conducted in July and August 2020.

Eighty-two percent of responses represent the C-Suite, including 20% from CEOs, 15% from CIOs, 14% CFOs and 11% COOs. The remaining 18% are Vice Presidents at their organization. Executives represent a range of sectors, led by technology (16%), financial services and banking (15%), manufacturing (15%), healthcare and life sciences (11%), automotive (10%), construction and infrastructure (10%), and consumer goods (8%). All come from organizations with at least $100 million in annual revenues, with 39% coming from firms with at least $1 billion in revenues.

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