



eHATCHERY[™]
a technology incubator



UNK
COLLEGE OF BUSINESS
& TECHNOLOGY





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Overview

The Ewing Marion Kauffman Foundation’s research has revealed that net job growth occurs in the U.S. economy only through startup firms.¹ Furthermore young high-growth firms, comprising less than 1 percent of all companies, generate roughly 10 percent of new jobs in the U.S. in any given year.² Unfortunately, most young high-growth firms are drawn to major urban areas due to financial resources, human capital, and lifestyle considerations. Major IT accelerators like TechStars and Y Combinator focus on technology clusters and large population centers where costs are high and expectations are higher for the next “homerun” investment. Entrepreneurs submit their ideas to these accelerators, a small number are chosen to participate, and often the companies must move to the location of the accelerators.

The traditional technology startup/accelerator model relies heavily on tech clusters such as Silicon Valley, Boston, or other large urban areas with a university presence. This provides excellent support for businesses that can be quickly built, scaled, and sold, but only a very small number of viable business opportunities fit this model. Few receive funding and even fewer are ultimately successful long term. Interestingly, the strength of the technology cluster approach is also one of its major weaknesses. By focusing billions in funding (\$11.2B in Silicon Valley and \$3.6B in Boston in 2012³) the costs of starting a business in a technology cluster has increased dramatically. From \$70/sq.ft. office space to six figure salaries and lavish perks for technicians and recent graduates, only well-funded entrepreneurs and businesses are able to compete for the resources necessary to be successful in this environment.⁴

Other regions and cities have attempted to recreate these technology clusters, trying to drive the same level of investment and concentration of human capital to spur their local economies. While a handful of these may achieve some degree of success, they will continue to find it difficult to beat the existing powerhouses at their own game (funding/talent/infrastructure). Because of funding limitations or profits margins that fall short of a typical VC minimum, these entrepreneurs and their businesses do not fit the technology cluster mold. These situations, therefore, present an untapped opportunity. *These entrepreneurs can be successful if given a lower cost area and access to reasonably priced talent, but only if they are provided with support and guidance to develop their businesses and sustainably grow within these communities.*

¹ <http://www.kauffman.org/newsroom/u-s-job-growth-driven-entirely-by-startups.aspx>

² <http://www.kauffman.org/uploadedfiles/high-growth-firms-study.pdf>

³ <http://www.technologyreview.com/news/517626/infographic-the-worlds-technology-hubs/>

⁴ <http://www.technologyreview.com/news/516501/in-innovation-quest-regions-seek-critical-mass/>

The concept behind this initiative is to develop and pilot an approach to technology entrepreneurship that incorporates the lessons of Silicon Valley, but takes a fundamentally different approach that focuses on the strengths that more rural communities can bring to the table. These include lower costs of labor and infrastructure, a strong pool of college and university graduates who want to live where they have roots, a labor force with a strong work ethic, and access to ideas and experience that are underrepresented in technology ventures such as agriculture. Rather than competing with technology hubs for the same entrepreneurs and startups, this program will focus on viable businesses and models that would otherwise have been non-starters.

Background & Partners

Xpanxion was one of the pioneers of using a rural approach to global development and has helped several startups across the country to quickly and cost effectively, bring their products to market – a key factor when working in a market with limited human and capital resources and a limited window of opportunity. Xpanxion brings fifteen years of software development expertise and has been an active participant in Atlanta’s technology startup community.

Invest Nebraska is collaborating with the University of Nebraska at Kearney, Buffalo County Economic Development Council, and Xpanxion, LLC to develop and pilot this eHatchery Initiative.

- Invest Nebraska is a private, non-profit venture development organization focused on assisting and investing in start-up companies in Nebraska. The organization also supports those communities and regions in the state that want to build entrepreneurial ecosystems based on their respective strengths and abilities.
- The city of Kearney is located in central Nebraska and is the county seat of Buffalo County, Nebraska. In 2011, the population of the city was 31,174, including the headquarters of one publically traded corporation (The Buckle, Inc.; NYSE:BKE) and one global software company (Xpanxion);
- Buffalo County Economic Development Council supports and promotes responsible and sustainable economic development in Kearney and Buffalo County;
- The University of Nebraska at Kearney has a diverse student body of nearly 7,100 students from across the globe with over 170 programs of study. The University has a strong internship program that requires undergraduate participation, along with a College of Business and Technology;

- Xpanxion is a private software engineering firm with offices in Atlanta, Georgia; Loup City, Nebraska; Kearney, Nebraska; Ames, Iowa; Manhattan, Kansas; and Pune, India. A key component to their business model is the establishment of rural hubs that provide US-based business understanding, software development lifecycle expertise, and independent software testing locations. Clients of Xpanxion include: InterContinental Hotels Group, The Weather Company, Red Hat, TravelPort, Cox Media, American Cancer Society, and Nuance Communications (for a complete list go to www.xpanxion.com/clients).

Advancing High-Growth Entrepreneurs: The eHatchery Initiative

The eHatchery Initiative will identify six potential high-growth businesses focused on software solutions for businesses or consumers. The collaborative partners will leverage Xpanxion's business network in Atlanta and across the country to identify the potential opportunities. Entrepreneurs and businesses will be evaluated based on the idea, business plan, the entrepreneur's domain knowledge, and the overall fit with a rural model. Selected companies will be those that can introduce a product to market quickly and can demonstrate an existing demand for their proposed product.

In order to capitalize these six participating startups, two early-stage funding programs exist in Nebraska. The Business Innovation Act Prototype Grant provides a \$50,000 grant to a potential high-growth company to assist in the development of a prototype product or process. This grant must be matched 50 percent by the company unless the project is a value-added agriculture company in which case the grant must be matched 25 percent. Companies apply to the Nebraska Department of Economic Development for consideration and will generally be notified within two weeks. Alternative funds also exist for building the prototype from Invest Nebraska's capital re-use program.

Once a startup completes the prototype, follow-on capital is available to commercialize the product or process through the Nebraska Seed/Commercialization Fund Program or the Invest Nebraska Angel Sidecar Fund Program. Through both funds, Invest Nebraska co-invests between \$50,000 and \$500,000 in Nebraska companies along with other private investors. Two organized angel groups exist in Nebraska. KAAPA (www.kaapacoop.com) is an angel investment group of over 330 accredited investors, all agriculture producers. The Nebraska Angels (www.nebraskaangels.org) is a non-profit mutual benefit corporation comprised of 60 accredited investors from the Omaha/Lincoln areas organized to exchange information about investment opportunities in early-stage and emerging growth companies with ties to the state of Nebraska. Other private investment groups in Nebraska focused on high-growth businesses include: TreeTop Ventures (www.treetopventures.com) Dundee Venture Capital (www.dundeeventurecapital.com) and Prairie Ventures (www.prairieventures.com). Significant pre-seed capital and follow-on capital, from public and private sources, exists in Nebraska for high-growth companies.

The eHatchery Initiative will have two primary elements:

1. Startup Facilitation - version 1.0: 120 days

1. Market Analysis – Leverage the Xpanxion client network and the Invest Nebraska corporate partners to assist with initial customer identification, market potential, and scalability;
2. Product Development - Launch version 1.0 of the software product in 120 days or less with the assistance of software developers from Xpanxion. The participating startup will also apply to the Nebraska Department of Economic Development for a \$50,000 prototype grant to assist with its operational and development expenses;
3. Customer Acquisition – Release the product commercially and evaluate feedback for version 2.0.

2. Educational Artifacts and Student involvement

1. University of Nebraska at Kearney Courseware – Develop the methodology and approach of launching version 1.0 within 120 days, which will be documented and collected for the purpose of creating course material (i.e. courseware) to be used as instructional materials for entrepreneur classes at the University of Nebraska at Kearney;
2. University of Nebraska at Kearney Internships – Involve students from the University of Nebraska - Kearney early on in the process of product development. These students can learn in a real environment the stresses, successes, and setbacks of starting a technology company. Once the internship ends, the company may decide to keep the student as a part-time employee and/or hire the student upon graduation.

Internships will be multi-disciplinary since it takes more than technologists to develop a successful business. Possible intern roles will include software development and testing, marketing, accounting and finance, and general business. Working within actual startups will give students the opportunity to make meaningful contributions to the success of the business, gaining valuable experience and an appreciation of the challenges and opportunities of entrepreneurship.

Case Study for the eHatchery Initiative

In November of 2012, Tom White decided to start his third company. He previously founded and sold two IT companies: Carthage to WAVO in 2009 and Vocada to Nuance Communications for \$51 million in 2007. Tom realized that there was no way to effectively store, update, and retrieve healthcare provider information within a healthcare system. This problem created a waste of resources and time as providers searched for contact information for other doctors treating the same patient. The solution developed by Phynd, Inc. (pronounced “find”) will pull data from internal hospital databases, along with the databases of state licensing agencies and educational institutions. The company’s value proposition is to automate and manage in the “cloud” the capture, cleansing and distribution of provider engagement (contact) information as a “source of truth” database across a health care institution. The benefits of the system are a reduction of costs, the improvement in compliance, and the increase in operational efficiency. Phynd mitigates the catastrophic impact on patient safety from poor

communications (the cause for 70 percent of all accidental deaths in a hospital) and improves readmission rates that cost hospitals \$12 billion annually.

When Tom needed to discuss his business model and the IT applications he called Paul Eurek, CEO of Xpanxion, who had helped him build out the software for Vocada. Mr. Eurek encouraged Tom to consider starting his business in the small rural college town of Kearney, while allowing him to maintain his residency in Dallas, Texas. The attraction to Kearney was a highly educated workforce, experienced IT software developers and architects, and low cost of doing business. What Kearney did not have was the type of ideas and innovation Tom could bring to the equation as a result of his previous entrepreneurial experiences. Tom agreed to start his company in Kearney, and initially applied for and received a \$50,000 Prototype Grant from the State of Nebraska Department of Economic Development. Upon completion of the prototype, Tom raised \$1.4 million in angel financing outside of Nebraska and leveraged a \$500,000 equity investment from Invest Nebraska through the Nebraska Seed/Commercialization Fund Program. Metrics for Phynd at the end of 2014 included:

- 5 employees in Kearney with an average wage of \$54,000 (the median household income in Buffalo County is \$44,379);
- Signed contracts with 6 hospitals, including Yale University Health System of New Haven, Connecticut;
- 10 part-time employees receiving an average of \$10/hour;

As the company ramps up production in 2015, forward looking projections include hiring:

- 20 part-time employees at \$10/hour;
- 5 IT Specialists at an average wage of \$80,000;
- 4 Lead Generation Specialists at an average wage of \$50,000; and
- 3 Customer Support Specialists at an average wage of \$40,000.

Launching an enterprise-class technology company from concept to market in such a short timeframe is considered exceptional in any market; to do this in rural Nebraska proves the right pieces are in place to successfully replicate this accelerated start up model.

The eHatchery Initiative is intended to advance high-growth entrepreneurs by providing them with the business model and mentor support to establish their businesses in a rural community. The primary advantage to entrepreneurs is that the lower costs of the rural model will attract those entrepreneurs and investments that would otherwise be priced out of the technology cluster market. Once started, they will be able to stretch their funding dollars further, giving them a better chance of commercial success and rapid growth. By their nature, technology and software companies have the ability to grow very quickly, but only once they have developed the product and intellectual property which can then be produced at scale very cheaply. This Initiative will focus on teaching startups how to reach their first commercial release quickly and inexpensively so that time-to-revenue is accelerated and adjustments can be made based on customer feedback before their R&D budgets are fully consumed.

Presently, the rural technology startup approach has been successful as previously discussed in the Phynd Technologies example. However, this initial case would not have been possible had it not been for the assistance from a private company and the collaboration of public and private organizations. By formalizing and standardizing the approach, developing the tools and templates, and providing a mechanism for entrepreneurs to engage the community, this pilot initiative will attempt to establish Kearney as a community that is not only attractive to technology entrepreneurs, but also brings wider attention to rural communities in general as potential entrepreneurship destinations.

Proposed Metrics and Deliverables

The metrics used to evaluate the high-growth companies include:

- Customer contacts
- Sales
- Number of jobs created
- Average salary of jobs created
- Follow-on capital raised (equity, loan, grant)
- Income taxes paid (federal and state)

During the first 120 days, each high-growth startup is expected to conduct a market analysis. This analysis would include first customer identification, market potential for the product, and scalability of the business. During this phase, the startup is also expected to develop and launch version 1.0 of the software product. Following the first 120 days, the startup is expected to release their product commercially and evaluate feedback for version 2.0 in anticipation of customer acquisition.

Risks and Contingencies

A pilot initiative has inherent risks, especially when one such as this is proposed in a rural area outside of the conventional metropolitan area. Seeking interested high-growth entrepreneurs wanting to start their business in a rural area could prove challenging. But serial entrepreneurs know that controlling costs with limited capital is imperative, especially when building a prototype prior to commercialization. The Nebraska Seed/Commercialization Fund Program and the Invest Nebraska Angel Sidecar Fund Program also incentivize entrepreneurs to start their business in Nebraska in partnership with an international software firm like Xpanxion.

This proposal also depends on utilizing Xpanxion's network to seek out the potential ideas and high-growth entrepreneurs. Their network would include past and current clients, Angel/Venture Capital firms the company has worked with in the past and business contacts in the Atlanta area. Leveraging Xpanxion's network has already resulted in one company, Phynd Technologies, starting its business in Kearney. A contingency plan is already planned should it become challenging to recruit the eight companies to Kearney during the one-year grant period. These steps include: identifying promising research at the University of Nebraska with commercial potential that requires an information technology component and conducting a startup idea competition in Atlanta and/or Dallas with the prize of mentor services and capital once the startup locates to Kearney.

Expected Outcomes at the Conclusion of the Initial 2-year Period

At the conclusion of the grant period, Invest Nebraska and its partners would expect the participating companies in eHatchery to have a completed prototype, first paying customers, and follow-on investment from angel investors. The program will also produce courseware of the methodology and approach of launching version 1.0 for a software company in a rural area.

Rural areas in this country are isolated, but not because of geography. The internet has broken down these barriers, allowing residents greater exposure to new ideas and technology. What is often missing is the understanding of the problems facing customers nationwide, especially other businesses. This program is an innovative approach to connect entrepreneurs with a rural skilled workforce under the supervision of a seasoned entrepreneur and international software company. At the end of the grant period, Invest Nebraska and its partners believe this model can be replicated, bringing high-growth entrepreneurs to rural areas and exposing a technology workforce to the environment of a technology startup.

Proposed Budget

Invest Nebraska is requesting a \$300,000 grant over a three-year time period to pilot the eHatchery Initiative. This Initiative requires a part-time executive to organize the operations of the Incubator. This person will have experience working in an IT startup environment and a general understanding of the key aspects of a startup business. These aspects include product development, marketing analysis, and first customer acquisition. Another significant component of this position will be identifying and coordinating mentors for the various high-growth companies. These mentors will come from the Xpanxion and Invest Nebraska networks. If this pilot program proves successful at the end of the three-year period, Invest Nebraska would leverage its private and public network to continue funding the eHatchery Executive Director position.

The Buffalo County Economic Development Council has outlined an agreement with the City of Kearney and Xpanxion to provide commercial space for the eHatchery Initiative. This open commercial space is suitable for startup companies and allows for collaboration among partners. The global development resource identified in the proposed budget is the “secret sauce” used to develop Version 1.0 for each participant, allowing them to develop a prototype of their product, identify their market, and pursue first customer acquisition. The educational materials are the documented methodology and approach of launching version 1.0 within 120 days. Once the materials are finalized at the end of the grant period, these documents will be used in the entrepreneurial classes at the University of Nebraska-Kearney. Eventually, these course materials could be used at other college campuses in rural areas as well as urban areas. The travel expenses will be used by the participating companies to sign first customers during the customer acquisition phase of the Startup Facilitation.

eHatchery Initiative - Proposed Budget	
eHatchery Executive Director	\$ \$ 100,000
Invest Nebraska Administration	„5 50,000
Facility and Equipment	20,000
Global Development Resources	20,000
Educational Materials	20,000
Prototype Grant Match (\$10,000 per company)	60,000
Travel	<u>30,000</u>
Total	\$ 300,000

Proposed Timeline

The proposed timeline assumes that an award announcement is made in May 2015 and Invest Nebraska begins the pilot project in July. The timeline is as follows:

July 2015

- Interview and hire the eHatchery Initiative Executive Director.
- Identify the contacts within the Xpanxion network.

August – November 2015

- Identify, contact, and interview high-growth entrepreneurs with the goal of having three startups locate to Kearney and begin version 1.0 over the next 120 days.
- Identify appropriate coach/mentor for each company from the Xpanxion and Invest Nebraska networks.
- Identify interns from the University of Nebraska at Kearney interested in working for this first class of companies.
- Require each company to apply for the State of Nebraska’s Prototype Grant (up to \$50,000 to assist in developing a prototype product or process).
- Organize and sponsor a central Nebraska community reception for the eHatchery participants and mentors, highlighting the companies and their achievements to date.

December 2015 - January 2016

- Assist the first class in working on version 2.0 and identify first customers.

February – May 2016

- Identify, contact, and interview high-growth entrepreneurs for the second class of the program with the goal of having three startups locate to Kearney and begin version 1.0 over the next 120 days.

- Identify interns from the University of Nebraska at Kearney interested in working for the second class of companies.
- Require each company to apply for the State of Nebraska's Prototype Grant (up to \$50,000 to assist in developing a prototype product or process).
- Organize and sponsor a central Nebraska community reception for the eHatchery participants and mentors, highlighting the companies and their achievements to date.

June – July 2016

- Assist the second class in working on version 2.0 and identify first customers.

August 2016

- Develop and write the curriculum for the coursework to be used in the University of Nebraska-Kearney entrepreneurial classes. The coursework will be based on case studies of the participating companies.

About Invest Nebraska

Invest Nebraska Corporation ("Invest Nebraska") is a not-for-profit 501(c)(3) venture development organization focused on advising and investing in potential high-growth entrepreneurs in Nebraska. As an entity with a statewide mission, Invest Nebraska receives operational funding from the Nebraska Department of Economic Development, the United States Department of Treasury, the United States Department of Agriculture – Rural Development, the Nebraska Investment Finance Authority, and individual donors.

For entrepreneurs seeking capital, Invest Nebraska operates two funds. From the Nebraska Seed/Commercialization Fund Program, Invest Nebraska invests \$50,000 - \$500,000 in Nebraska companies that are seeking to commercialize a product or process. The Nebraska Department of Economic Development allocates \$2 million per year for this program. All invested funds must be matched 1:1 by the private sector. Invest Nebraska also operates the \$3.8 million Invest Nebraska Angel Sidecar Fund Program, investing between \$50,000 - \$500,000 in Nebraska companies with a required 1:1 match from individual angels or angel funds in Nebraska. All returned capital from both funds will be re-invested in future Nebraska high-growth companies, creating an evergreen fund for the benefit of Nebraska's entrepreneurial ecosystem.

For entrepreneurs seeking advice, Invest Nebraska:

- evaluates potential new concepts;
- assists with the evaluation of business plans, marketing plans and raising capital;

- provides guidance in building a management team, business structure and financial forecasting;
- assists with developing an effective investor presentation;
- assists with obtaining funding through federal grant programs; and
- works with research universities to encourage spin-outs.

Invest Nebraska is governed by a strong twelve member Board of Directors representing both public and private entities, bringing various backgrounds and experiences to the organization. Current members include:

- Dr. Michael Dixon – Invest Nebraska Board Chairman, President and CEO of UNeMed Corporation; UNeMed is the technology transfer organization for the University of Nebraska Medical Center;
- Mr. Paul Eurek – Founder and CEO of Xpanxion, LLC
- Mr. Dennis Wiederholt – Principal and Chief Financial Officer of DLR Group
- Mr. Richard Baier – CEO of the Nebraska Bankers Association and former Director of the Nebraska Department of Economic Development;
- Mr. John Decker – President of Smith Hayes Financial Services and owner of MBA Suppliers, Inc.
- Mr. Dan Curran, ex-officio member – Director, of the Business Development Division, Nebraska Department of Economic Development
- Mr. Ben Harris – Chief Financial Officer of Nebraska Heavy Industries II, LLC
- Mr. David Milligan – Founder and Principal at Milligan PC LLO and former advisory board member to Kiva.org
- Mr. Ken Moreano – Executive Director of the Walter Scott Technology Center
- Mr. Sylvester Orsi – Partner at Baird Holm, LLP
- Ms. Jackie Ostrowicki – Assistant Vice President, University Affairs/Director of Marketing & Strategic Communications, University of Nebraska

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