To fail or not to fail?

Startup success prediction based on historical data

APPS UCU Data Analytics Final Project, Spring 2019

Sofiya Hevorhyan
Iryna Popovych

INTRO

Many people try to predict startups success: big companies like Amazon, Microsoft or Facebook do it to know whom to buy at a right time, venture capitalists do it to earn money. Most of them do some analysis, but still rely on pure intuition. Individual decision makers make errors due to their bounded rationality. This assumption considers the capacity of the human mind for solving complex problems as rather constraint.

BUSINESS OBJECTIVE

Investment strategies for start-up companies are usually based just on intuition or past experience. The question we pose here is,

Can we perform some analysis that can be used to identify relevant factors and score prospective startups based on their potential to be successful?

We decided to try complex approach for this problem and do analysis that will include many different factors and won't be biased.

DATA

We have a dataset from CrowdAnalytiX that represents startups and covers information about various aspects of company, cofounders, investments, industry, activities of company, details about employees and technologies used.

Here is the link to dataset with information about 472 startups each having 116 characteristics.

You can take a look at data dictionary for descriptions of variables.

OUR PLAN

Data Preparation

- Data cleaning
- Missing value treatment
- Outliers treatment

Data Exploration

- Graphical exploration
- Hypothesis testing
- Principal component analysis

Feature Engineering

- Feature creation
- Determining feature importance
- Variable selection

Modelling & Results

- Building logistic regression models
- Interpretation
- Comparing different results

- Data transformation
- Missing value treatment
- Outliers treatment

1. Data Preparation

Data transformation

Missing value treatment

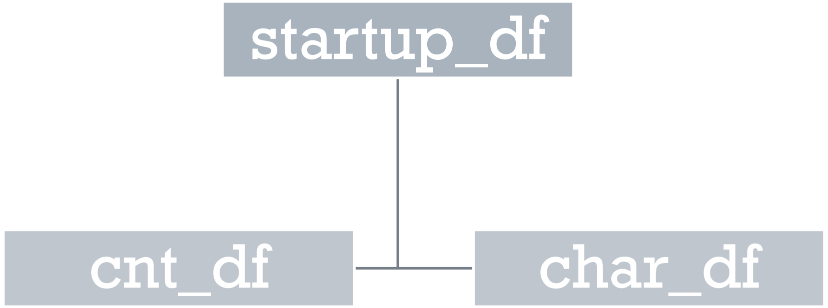
Outliers treatment

- We transformed strings to numerical, date, or factors where possible.

For example, the column Average.Years.of.experience.for.founder.and.co.founder transforms from to

High	3
Low	1
Medium	2
High	3
…	…

- We separated numerical and text data to make it more comfortable.



Data transformation

Missing value treatment

Outliers treatment

- We defined percentage of missing values for every column.

```
mis_val<-sapply(startup, function(x) sum(is.na(x)))
percent_mis<-as.data.frame(round((mis_val/nrow(startup))*100,1))
```

- We separated all the rows with more than 40% missing not to use them in modelling.

```
# keeping only variables with less than 40% missing
new_var<as.character(pcnt_mis_var$variable[
                                which(pcnt_mis_var$Percent.Missing<40)])
new_startup<-startup[new_var]
```

- By doing this, 3 variables (columns) with lots of missing values were gone. On top of that, we reduced number of incomplete cases (rows which have missing values) by 56.

```
sum(!complete.cases(startup)) - sum(!complete.cases(new_startup))
-----→ 56
```

Data transformation

Missing value treatment

Outliers treatment

- We calculated 10, 20, ….. 100 percentiles for every variable (column). Then created a function that replaces outliers with NA's using interquartile range rule.

  Outliers here are defined as observations that fall below Q1 - 1.5IQR or above Q3 + 1.5IQR.

```
remove_outliers <- function(x, na.rm = TRUE, ...) {
        qnt <- quantile(x, probs=c(.25, .75), na.rm = na.rm, ...)
        H <- 1.5 * IQR(x, na.rm = na.rm)
        y <- x
        y[x < (qnt[1] - H)] <- NA
        y[x > (qnt[2] + H)] <- NA
        return(y)
    }
```

- We cleared outliers, and after that used k-Nearest Neighbor to fill missing values.

```
cnt_df <- kNN(cnt_df, imp_var = FALSE)
```

- Graphical exploration
- Hypothesis testing
- PCA

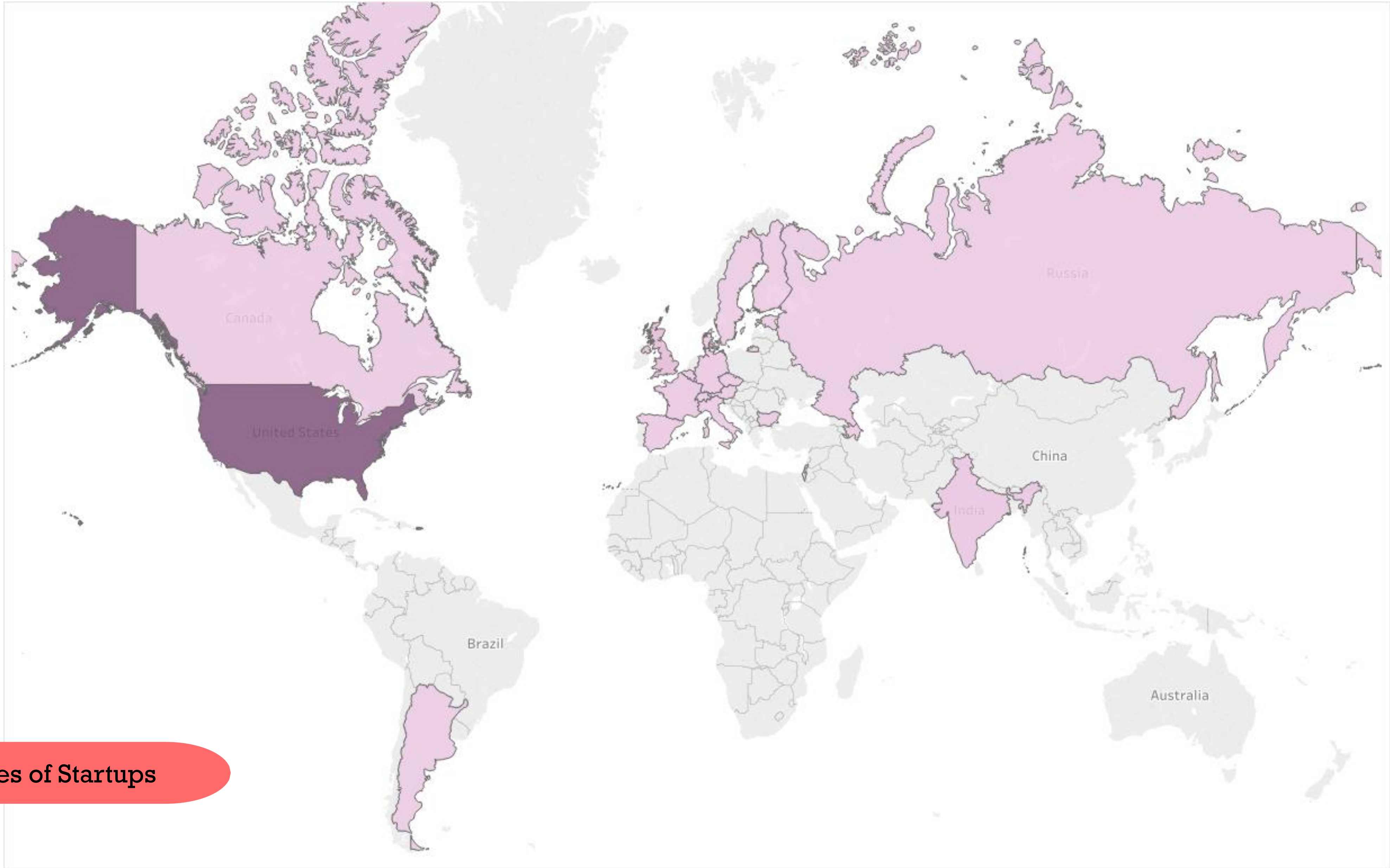
2. Data Exploration

Graphical exploration

Hypothesis testing

PCA

472 startups from **22** countries



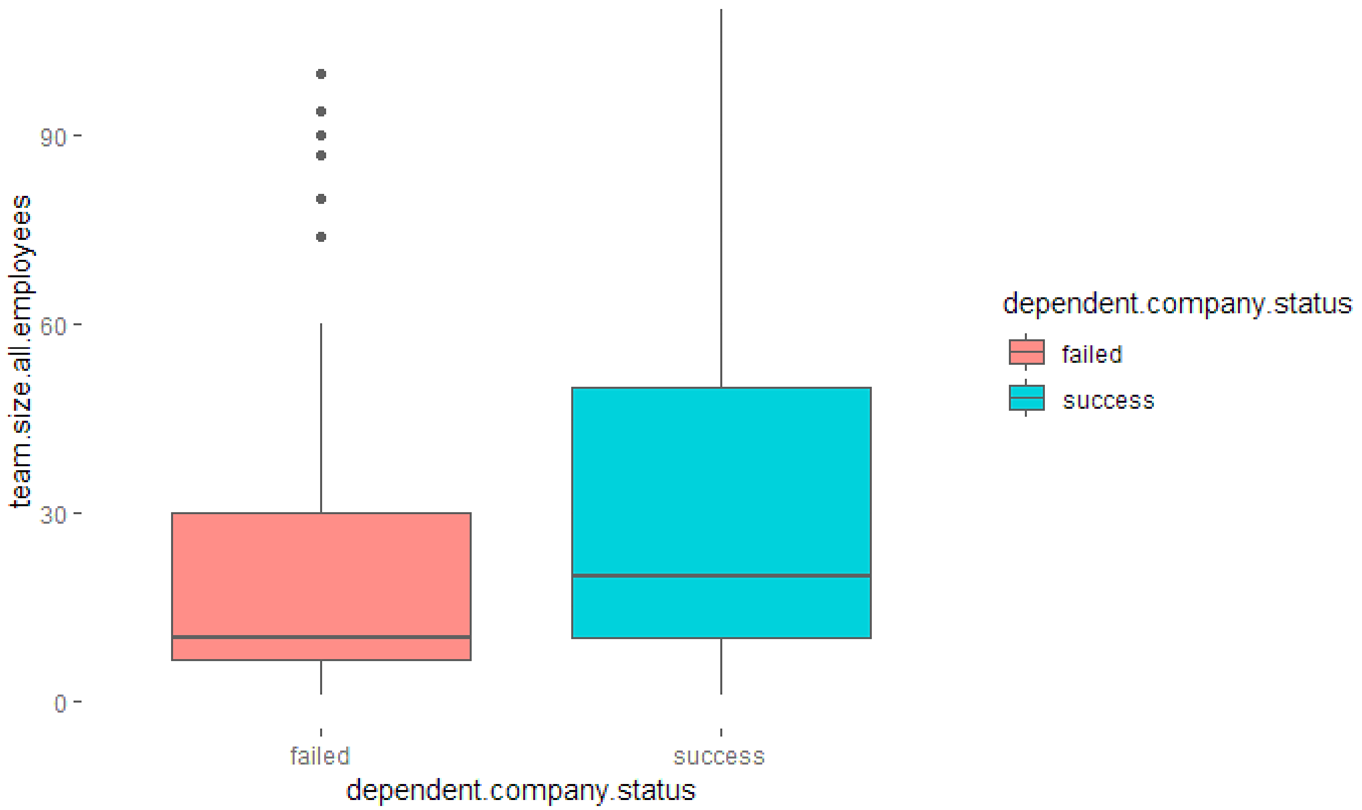
Countries of Startups

Graphical exploration

Hypothesis testing

PCA

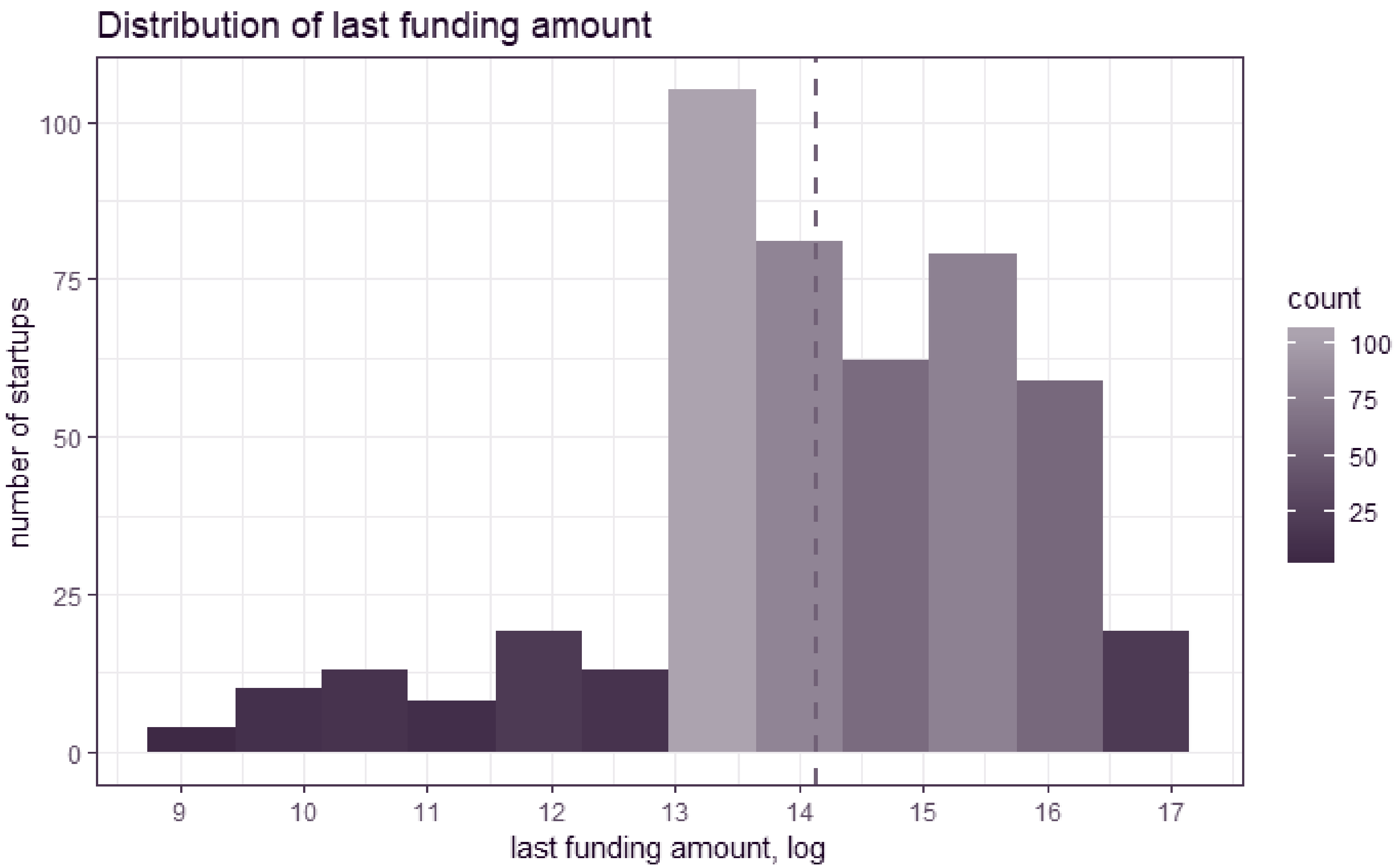
Company status by size of the team



Graphical exploration

Hypothesis testing

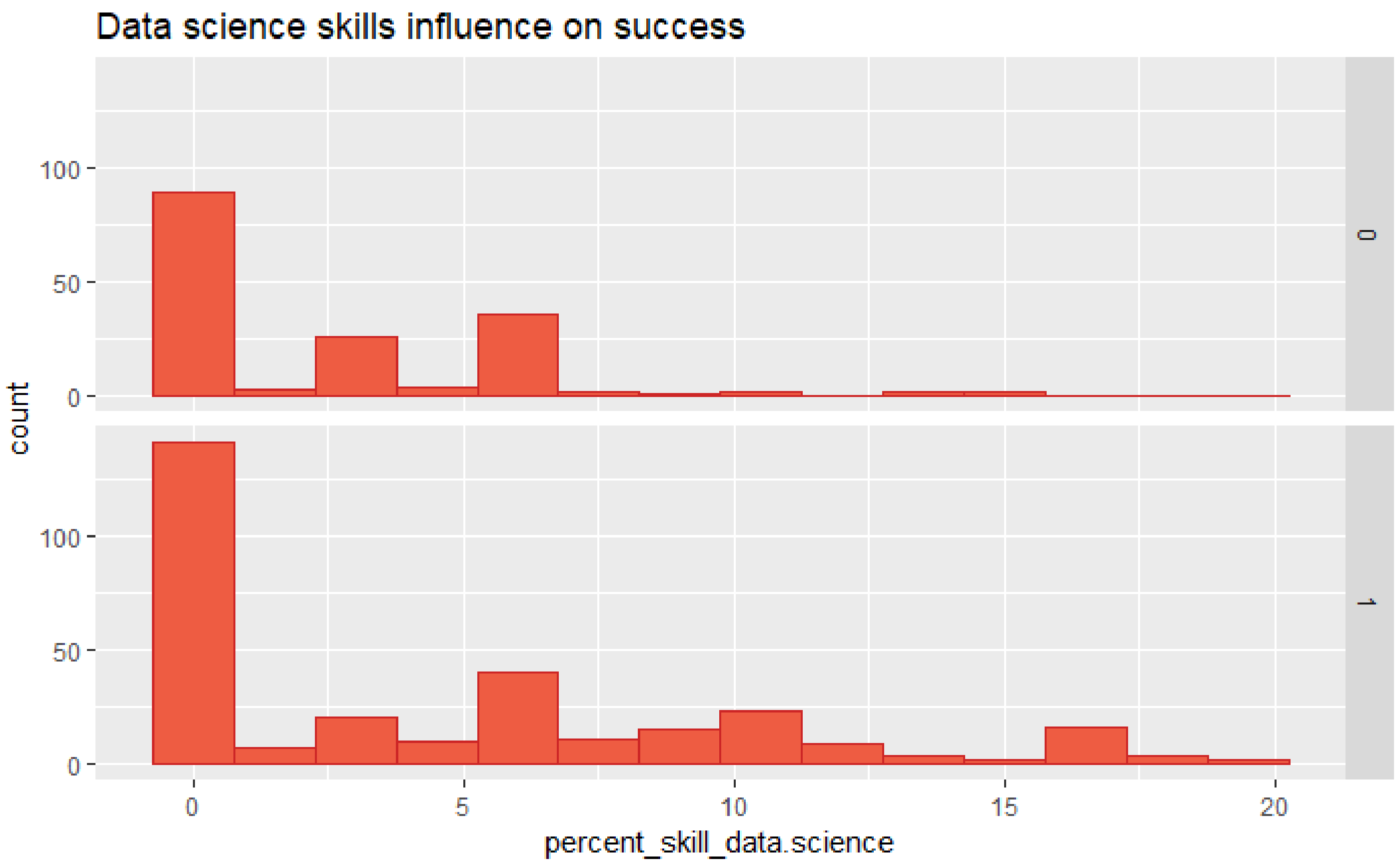
PCA



Graphical exploration

Hypothesis testing

PCA



Graphical exploration

Hypothesis testing

PCA

- We used ‘T-test’ for testing difference in mean of an independent variable to two categories of dependent:

Let's see if team size is an important feature or nor -- compare mean team sizes of companies who succeeded and who did not.

```
# t-test for checking difference in mean
t.test(team.size.all.employees~dependent.company.status, data=cnt_df)
        Welch Two Sample t-test

data:  team.size.all.employees by dependent.company.status
t = -3.4997, df = 341.26, p-value = 0.0005276
alternative hypothesis: true difference in means is not equal to 0
95 percent confidence interval:
 -11.29195  -3.16608
sample estimates:
mean in group 0 mean in group 1 
       20.44311        27.67213
```

Here we can reject the null hypothesis of equality with a strong p-value of 0.0003, so, we can choose “Team.size.all.employees” for modeling.

- We also used “Chi-squared test” for testing interdependency for a categorical variable and dependent categorical. We used it to decide whether to use variable in modeling or not.

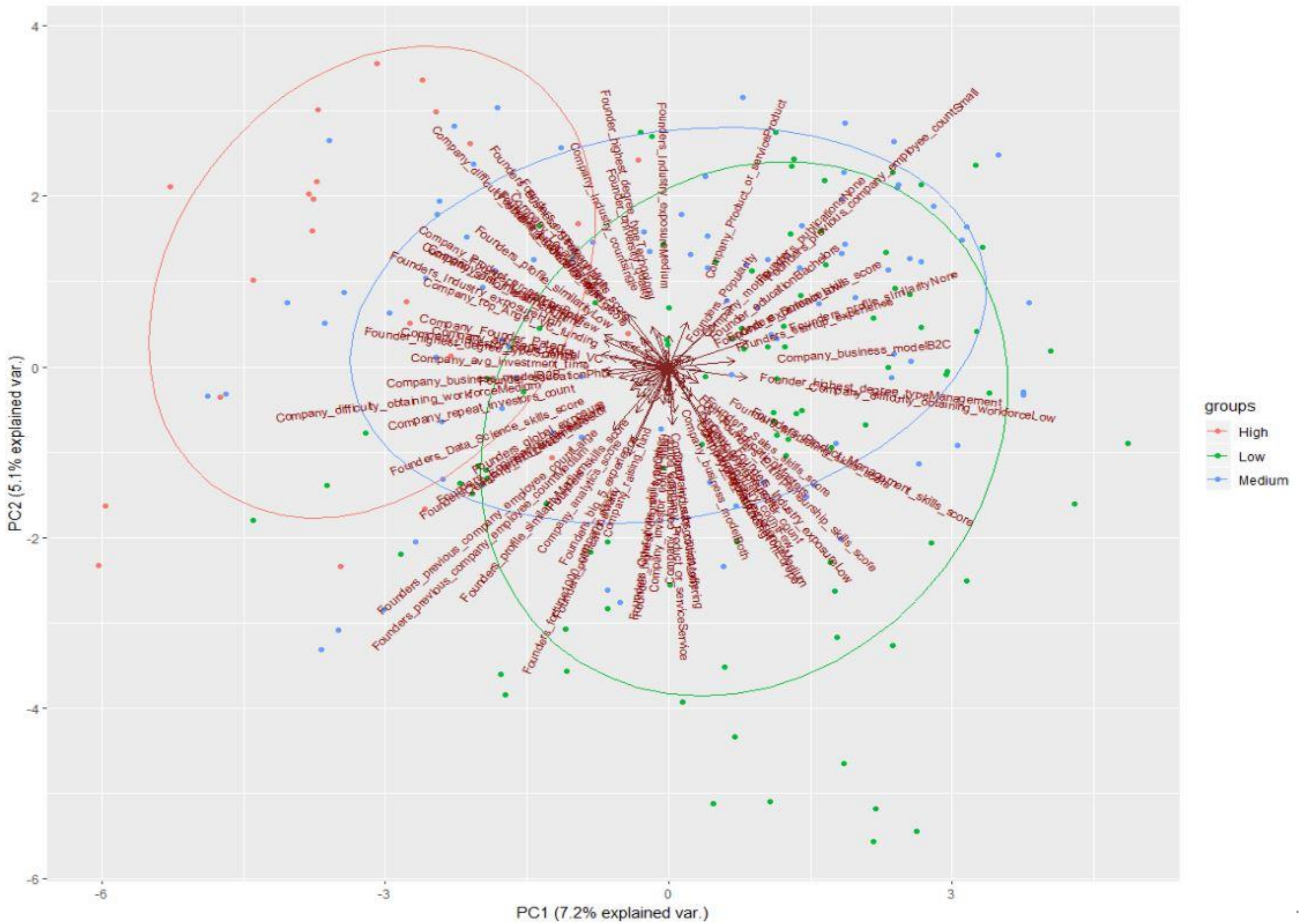
Graphical exploration

Hypothesis testing

PCA

In our case it was very useful to try Principal Component Analysis as a feature selection techniqu for modelling. PCA projects the entire dataset onto a different feature subspace.

In the figure below you can see what we got after calculating the rotation matrix.
It is clear that first principal component explains 7.3% of variance
and second component explains 5.1% variance.



Feature creation

Determining importance

Variable selection

3. Feature Engineering

Feature creation

Determining importance

Variable selection

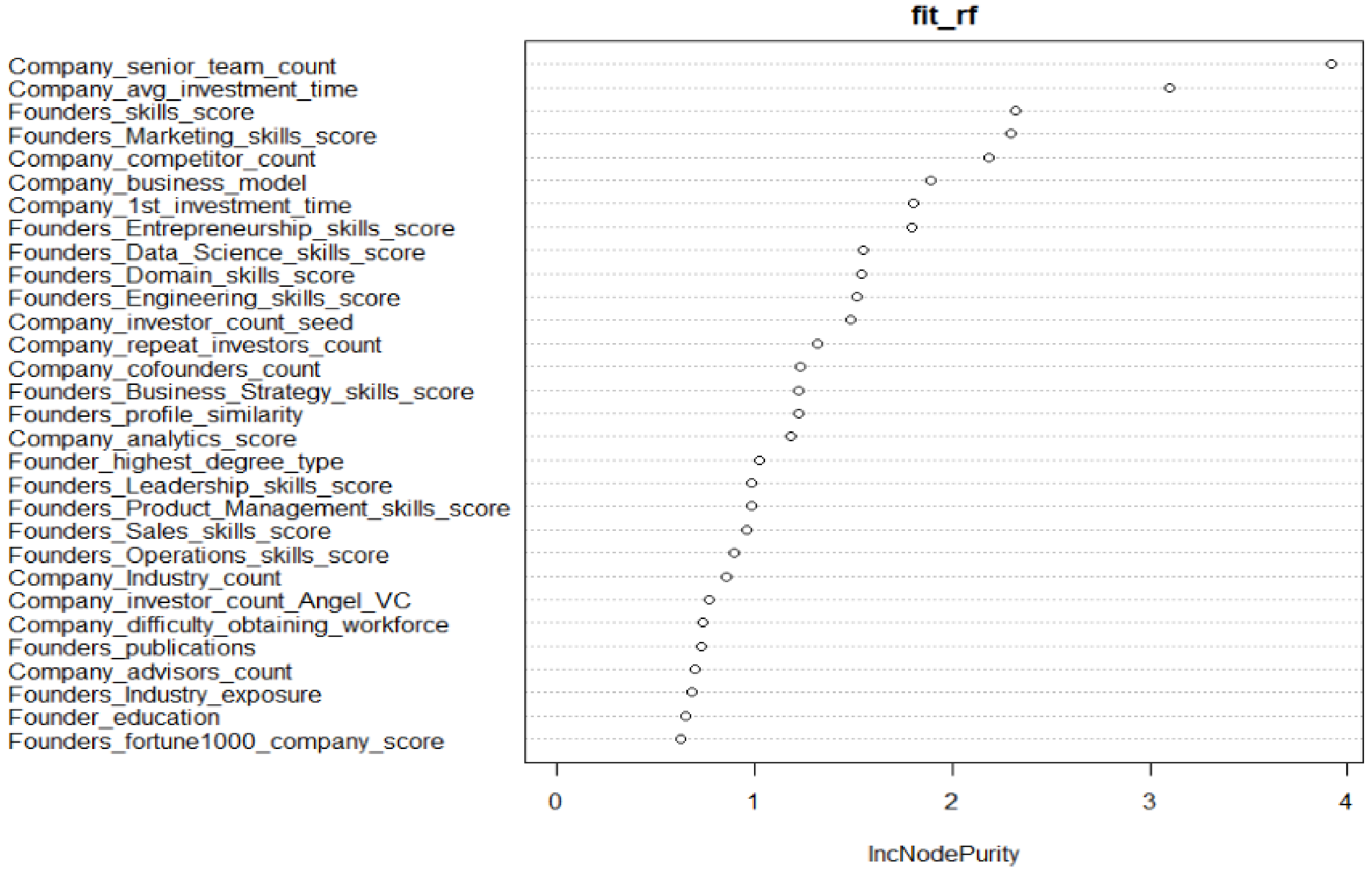
- We created additional features in given data to make it more meaningful which will help in analysis / modeling.

  - For example, variable "Investors" has list of investors for the company separated by 'pipline' symbol. We can create 'Count.of.investors' variable which will help in analysis.
  - We can also create some ratios to reduce number of variables. For example, we created lastfunding.amount vs. age of company ratio, as these two variables are dependent.

- We needed to select features for modeling, because we aren't able to use all of them.

- One of the ways to prove if the feature is meaningful and can be used in modelling is performing hypothesis testing for correlation, dependence etc., which we mentioned earlier in 'hypothesis testing' section.

- After analyzing different ways of determining importance, we decided to use random forest to select the most relevant features.



Feature creation

Determining importance

Variable selection

Feature creation

Determining importance

Variable selection

- One more approach that we sed for variable selection is Information Value.
  - Information Value (IV) for logistic regression is analogous to correlation for linear regression.
  - Information value tells us how well an independent variable is able to distinguish two categories of dependent variables.
  - We selected variables with IV of 0.1 to .7 for modeling.

```
# selecting variables with good information values
var<-IV[which(IV$InformationValue>0.1),]
var1<-var[which(var$InformationValue<0.7),]
final_var<-var1$Variable
```

Logistic regression

Comparing results

Interpretation

4. Building a model

Logistic regression

Interpretation

Comparing results

- Remember? We need to predict whether company will succeed or not:

```
startup <- read.csv(file="./data/CAX_Startup_Data.csv", header=TRUE,as.is=TRUE)
head(startup)
```

	Company_Name <chr>	Dependent.Company.Status <chr>	year.of.founding <chr>	Age.of.company.in.years <chr>
1	Company1	Success	No Info	No Info
2	Company2	Success	2011	3
3	Company3	Success	2011	3
4	Company4	Success	2009	5
5	Company5	Success	2010	4
6	Company6	Success	2010	4

6 rows | 1-5 of 116 columns

Dependent variable

Logistic regression

Comparing results

Interpretation

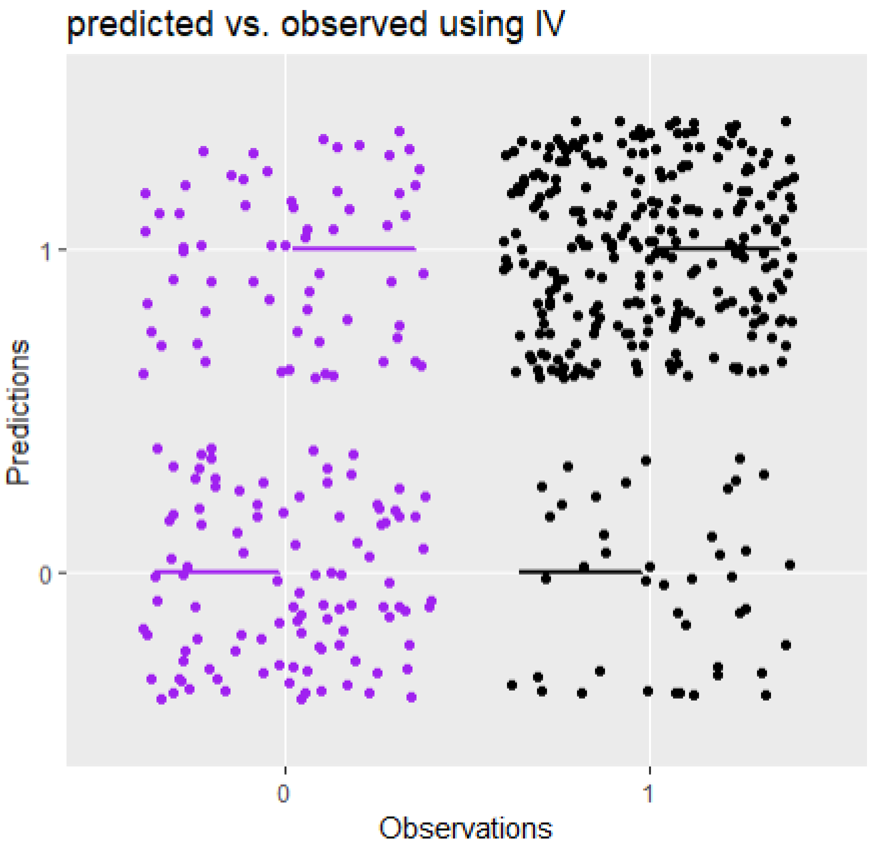
- We used different approaches to select predictors for the final model for our project.
  - randomForest + caret, varImp()
  - Information value
- After that, we've built different models with these groups of features, including one mixed group, and compared results.
- Here, we present the model that appeared to be the best one. You can take a look at other models in the R-Notebook of the project with re-executable code.

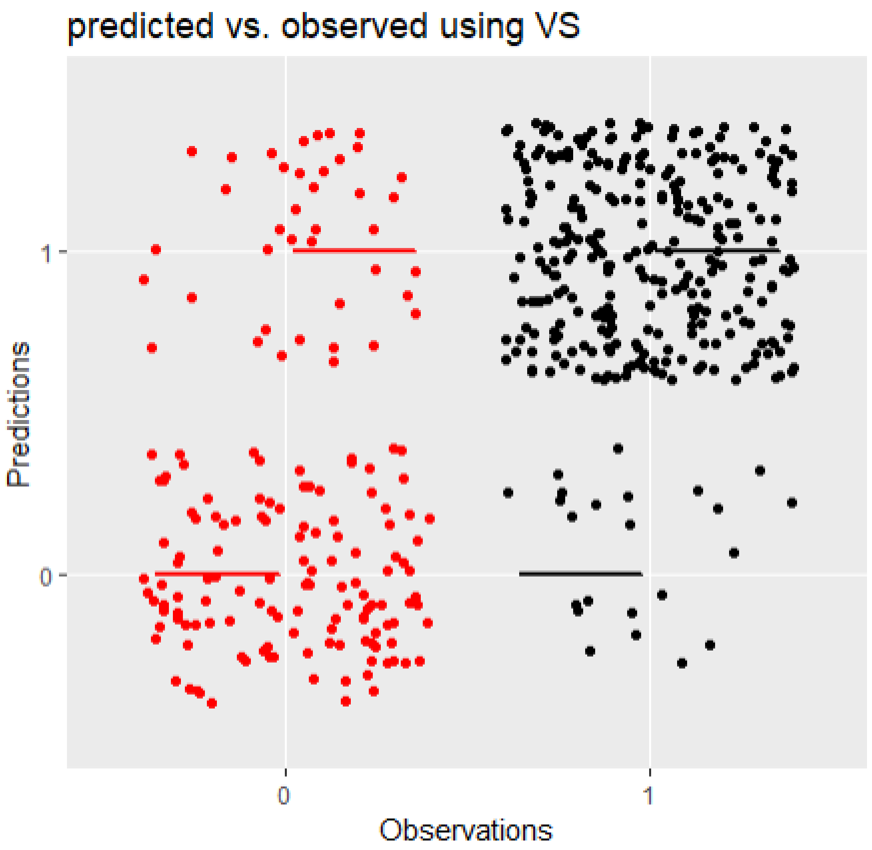
```
Coefficients:
                                     Estimate Std. Error z value Pr(>|z|)    
(Intercept)                         -3.559649   1.207424  -2.948 0.003197 ** 
percent_skill_data.science           0.136885   0.031212   4.386 1.16e-05 ***
number.of.investors.in.seed          0.697207   0.151188   4.612 4.00e-06 ***
team.size.all.employees              0.010010   0.006220   1.609 0.107553    
percent_skill_leadership            -0.092485   0.036339  -2.545 0.010925 *  
percent_skill_engineering            0.021718   0.008258   2.630 0.008539 ** 
number.of.co.founders                0.263153   0.118278   2.225 0.026090 *  
experience.in.fortune.500.organizations 1.271004   0.339622   3.742 0.000182 ***
last.funding.amount                  0.200215   0.087595   2.286 0.022272 *  
percent_skill_sales                  0.145185   0.042586   3.409 0.000651 ***
renown.score                        -0.143344   0.046112  -3.109 0.001880 ** 
percent_skill_operations            -0.147242   0.055933  -2.632 0.008476 ** 
---
Signif. codes:  0 '***' 0.001 '**' 0.01 '*' 0.05 '.' 0.1 ' ' 1

(Dispersion parameter for binomial family taken to be 1)

    Null deviance: 613.39  on 471  degrees of freedom
Residual deviance: 435.52  on 460  degrees of freedom
AIC: 459.52
```

Logistic regression

Comparing results

Interpretation





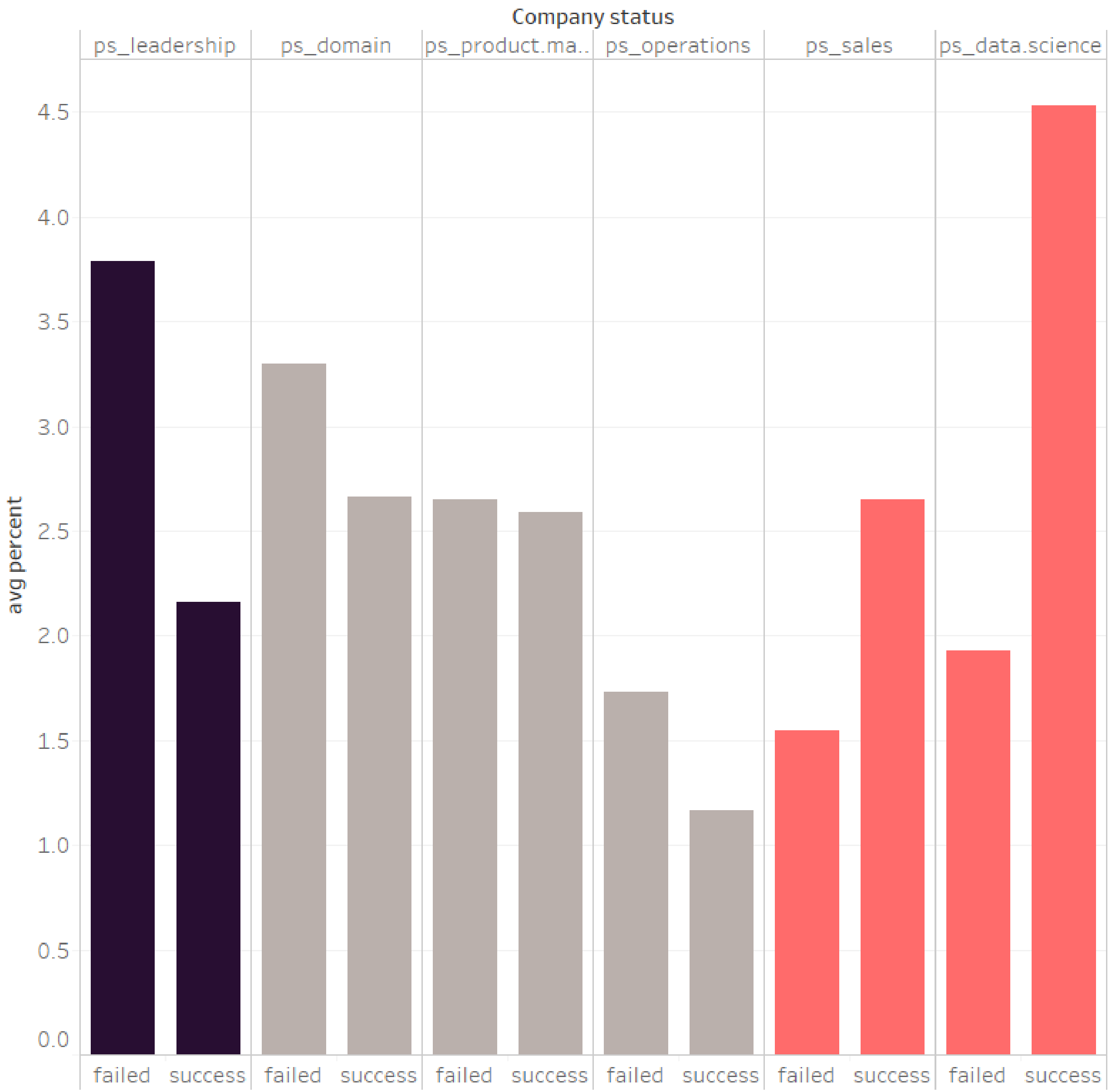

```
                Reference
Prediction   0   1
         0 103  42
         1  64 263

               Accuracy : 0.7754
                 95% CI : (0.7351, 0.8123)
    No Information Rate : 0.6462
    P-Value [Acc > NIR] : 8.087e-10
```

```
                Reference
Prediction   0   1
         0 127  23
         1  40 282

               Accuracy : 0.8665
                 95% CI : (0.8325, 0.8959)
    No Information Rate : 0.6462
    P-Value [Acc > NIR] : < 2e-16
```

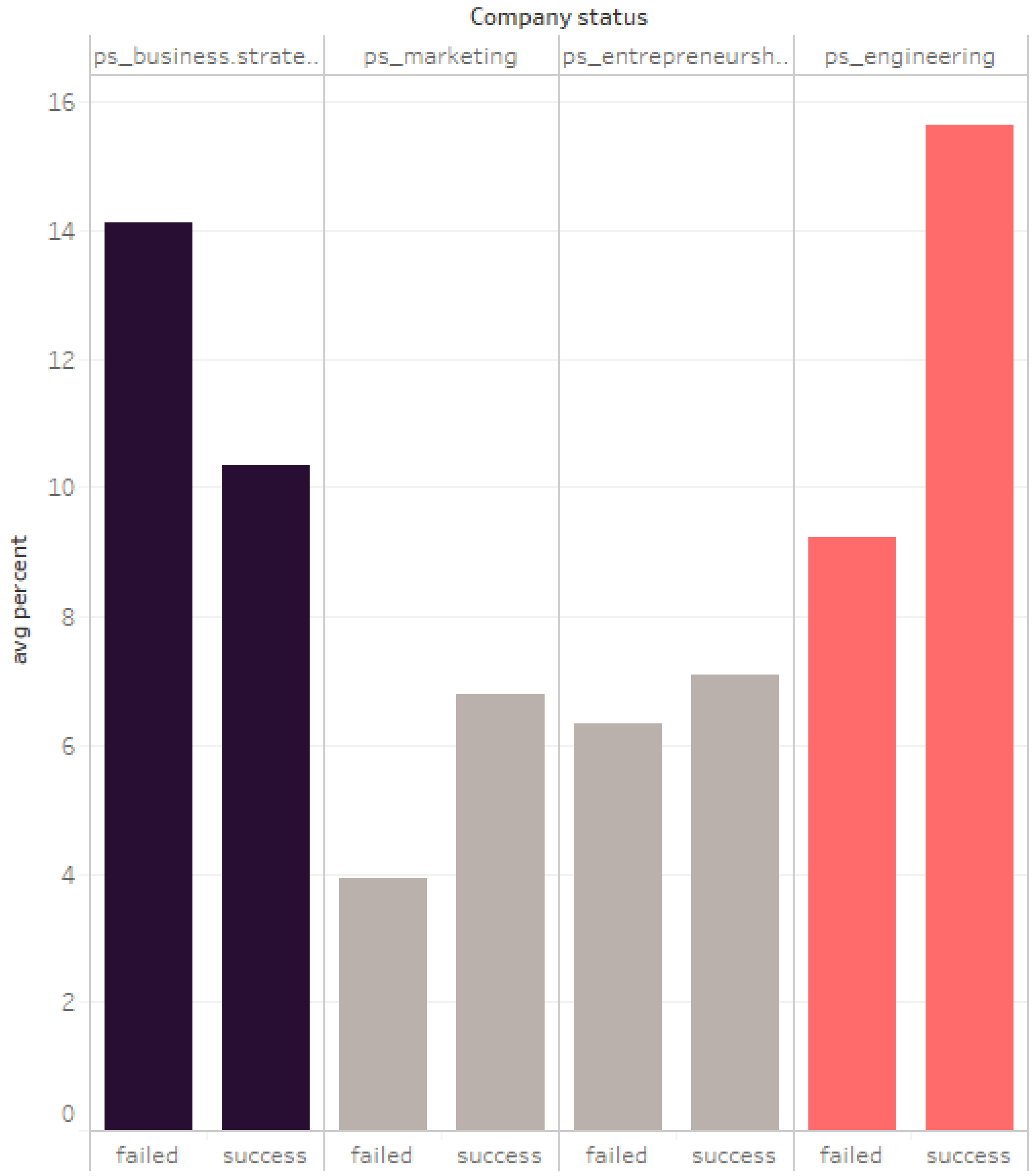
Comparison of Confusion Matrix for models with Information Value methods and Variables Selection method

SO, WHAT'S IMPORTANT?

Data Science and Sales are the most important skills, whereas Leadership is not that important.



Besides Engineering and Business Strategy, marketing can also have relevant impact but this feature is not significant for the model

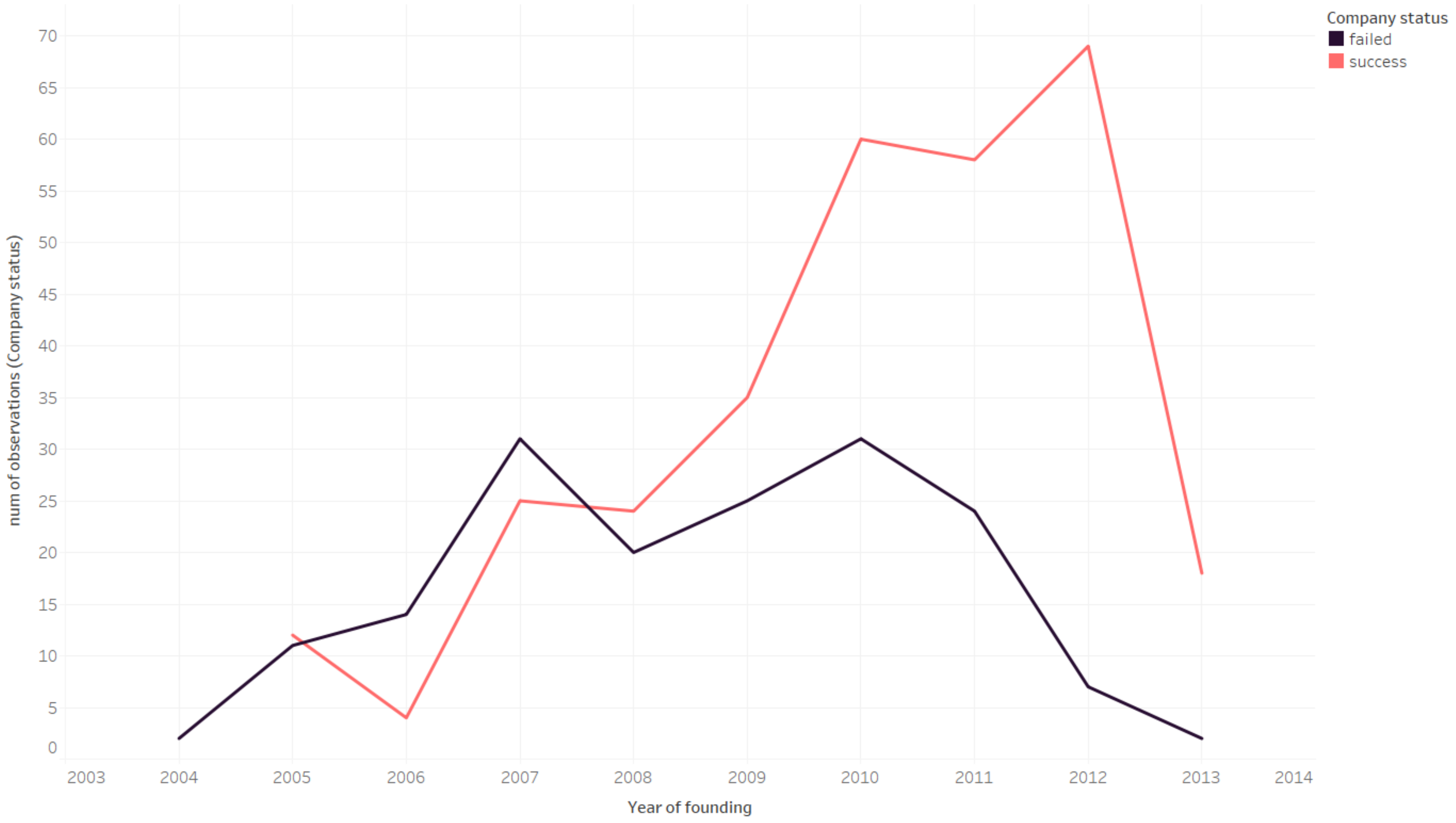


The most important skills of startups

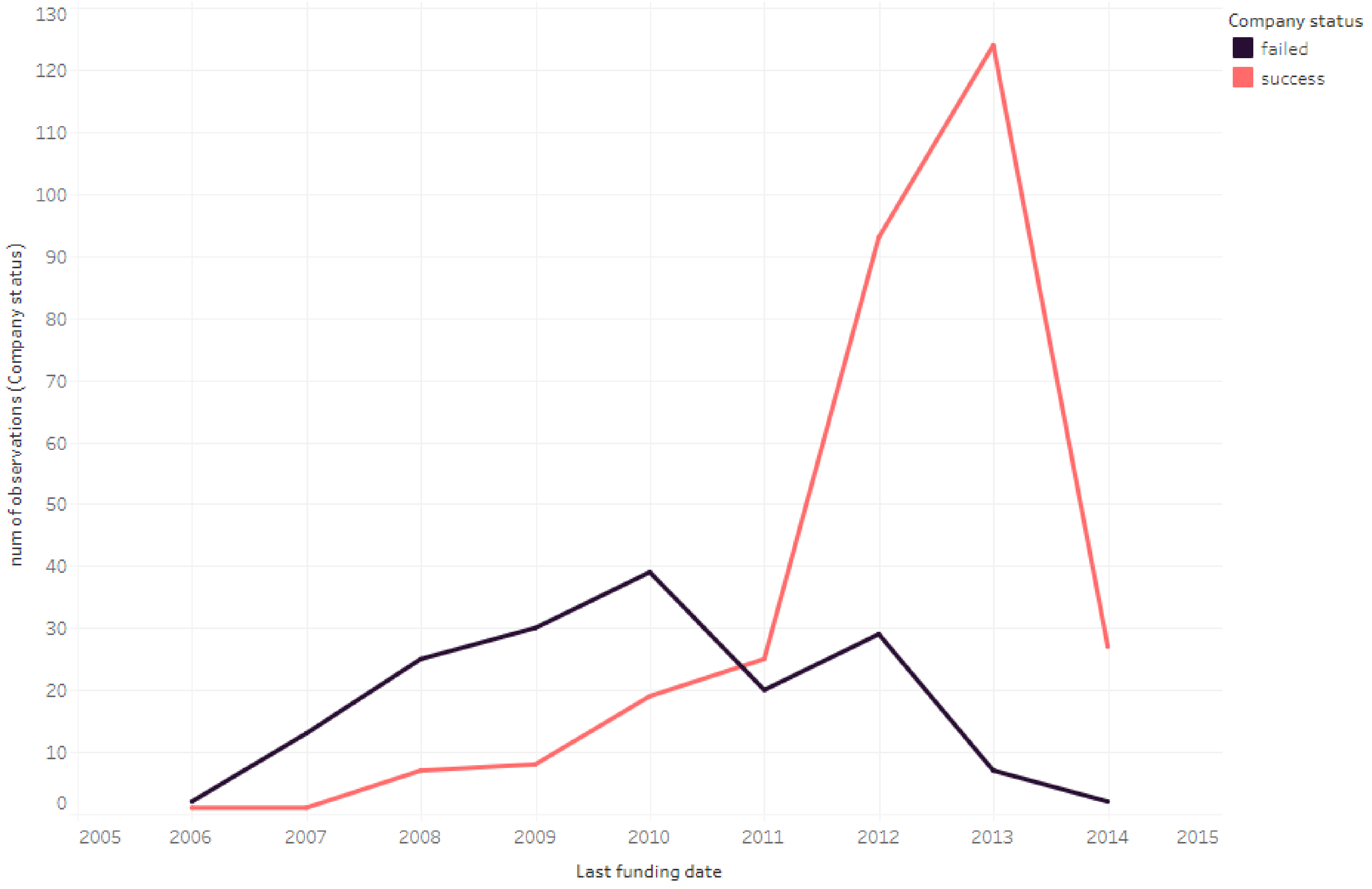
(as we concluded from regressions)

- Data Science, ↑
- Sales, ↑
- Engineering, ↑
- Business Strategy, ↓
- Leadership, ↓

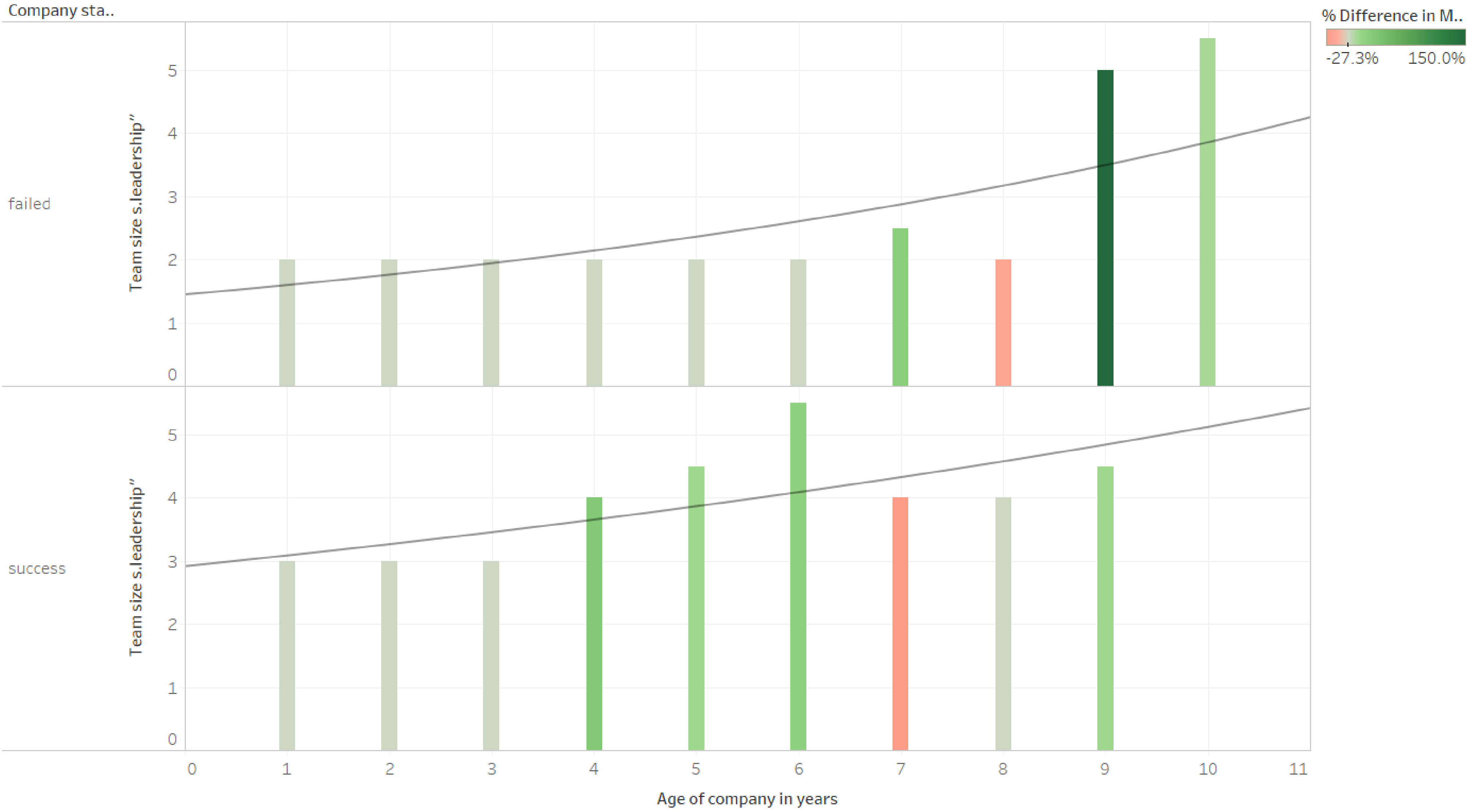
Distribution of failed/success by year of founding.



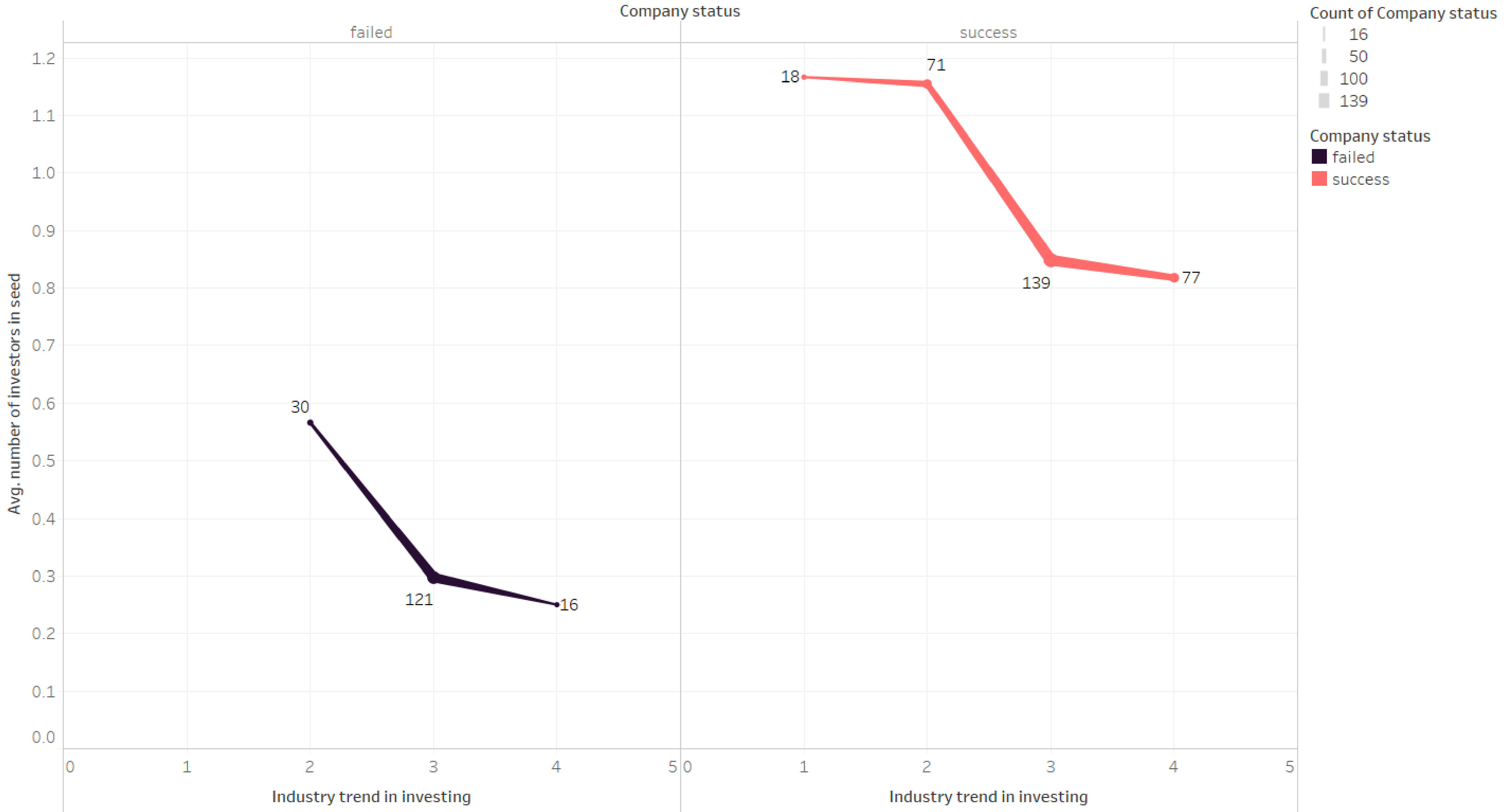
Relation of last funding of failed/success



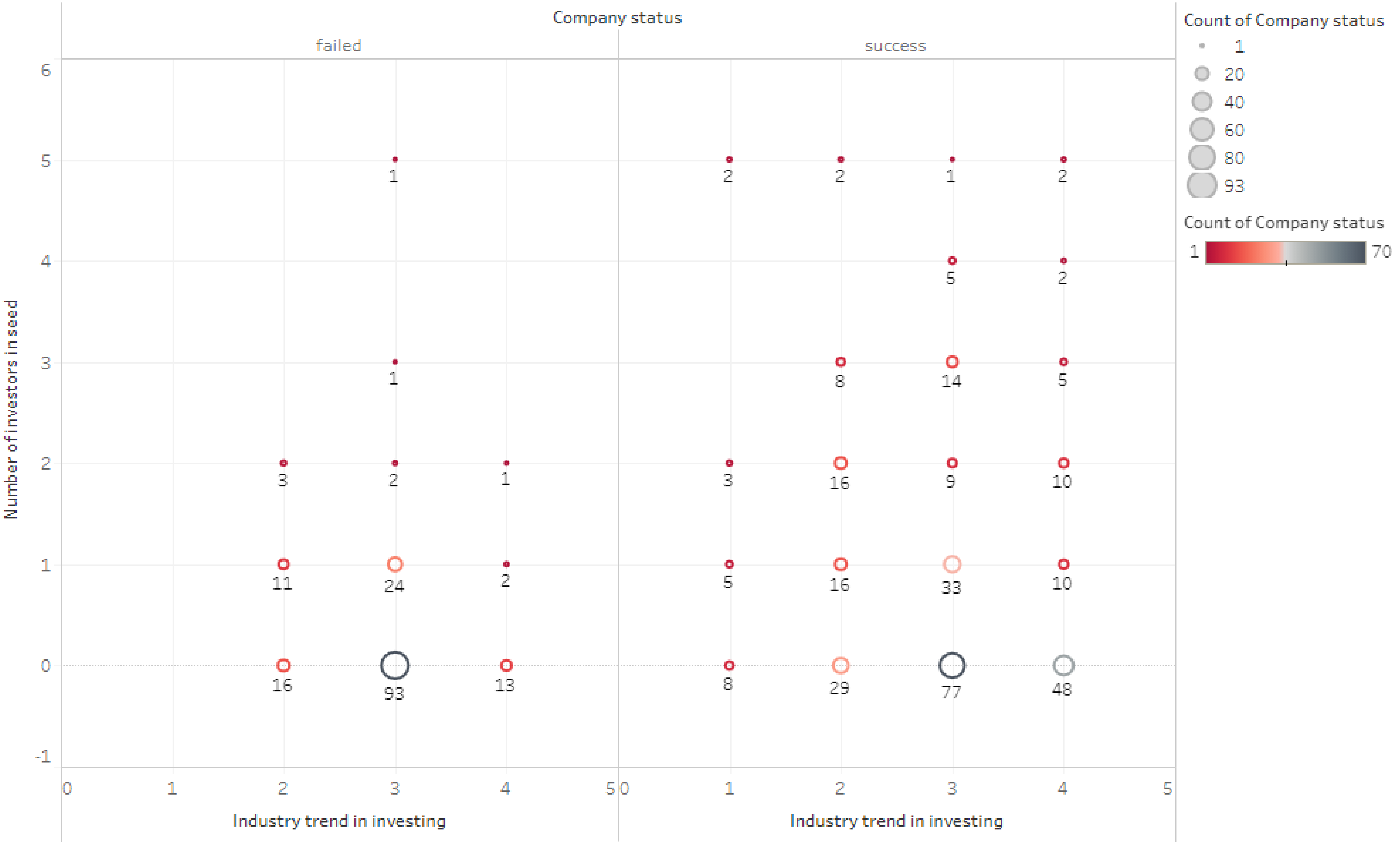
Growth in % of startups across years (grouped by failed/success)



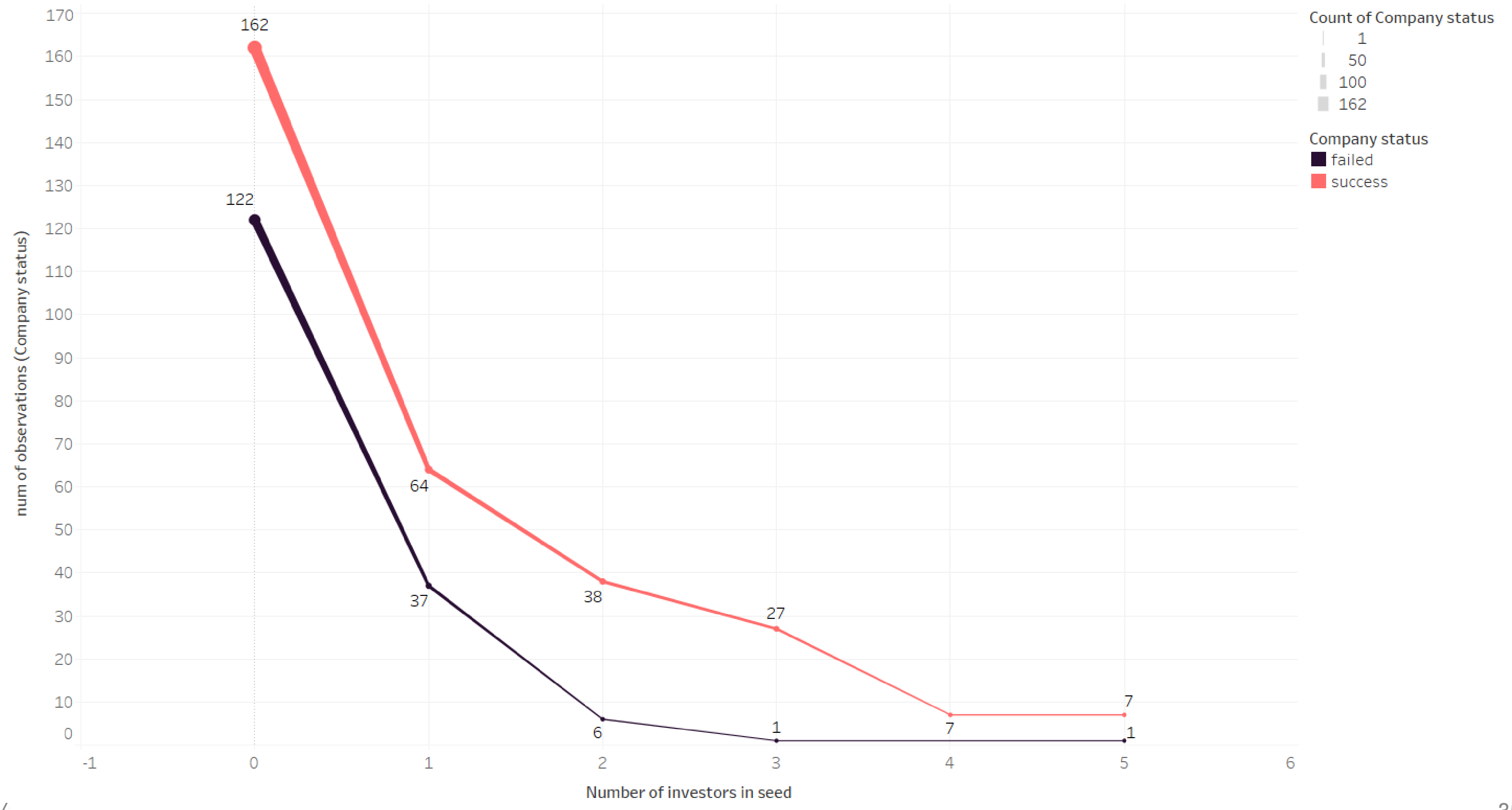
Avg. seed investors at failed/success in different industries



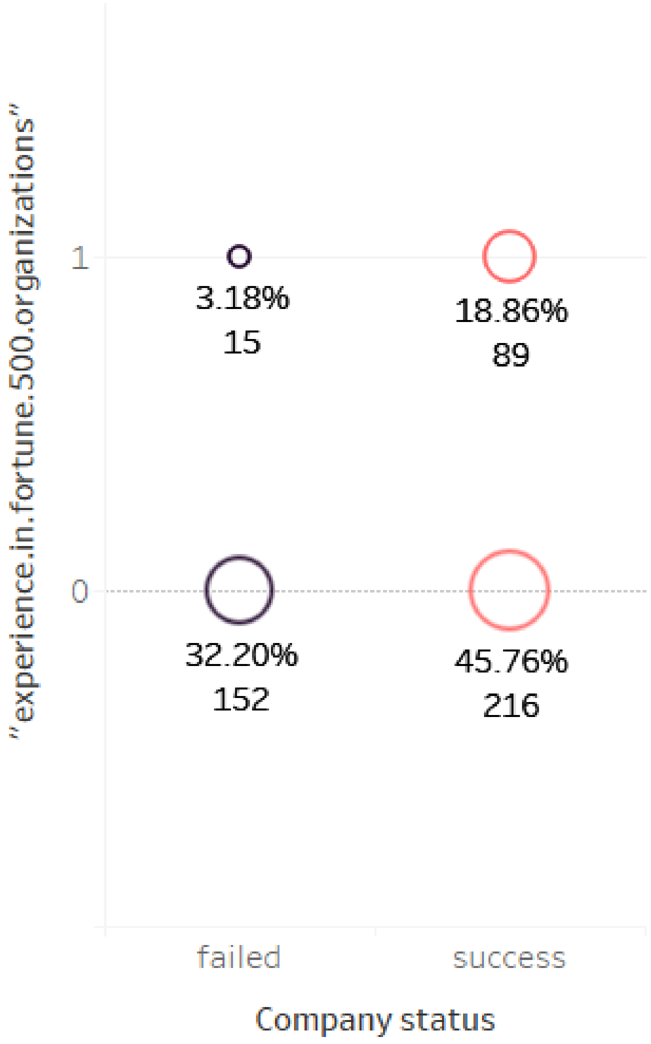
Num of seed investors at failed/success in different industries



Distribution of seed investors at failed/success startups



Relation btw experience in Fortune 500 and failed/success



CONCLUSIONS

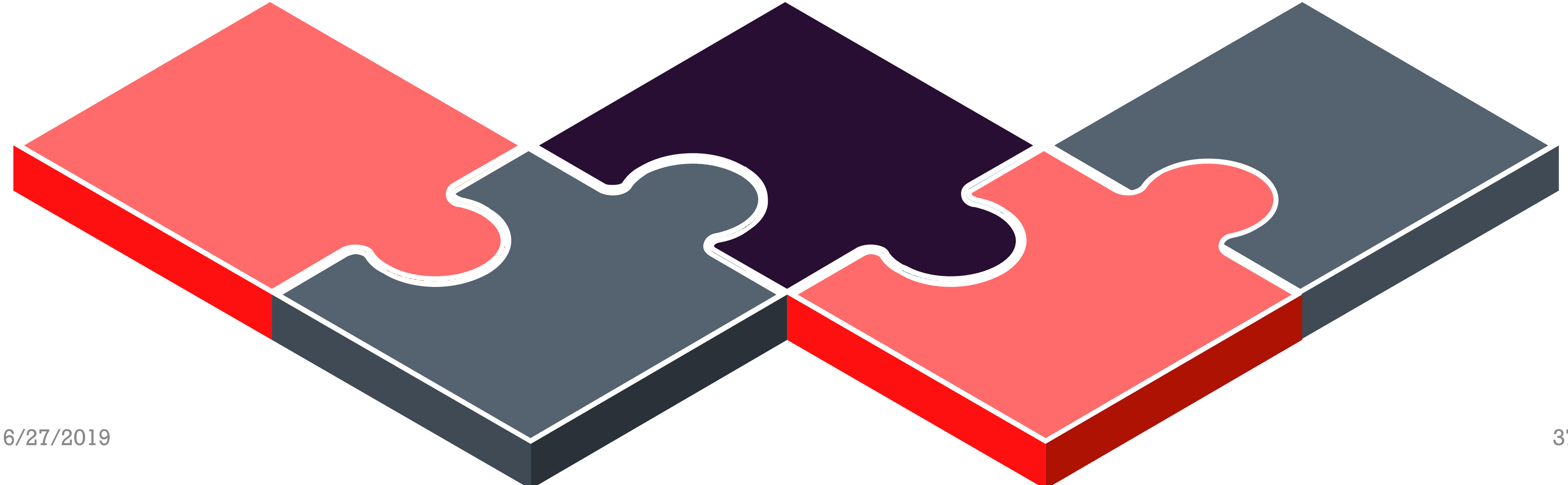
A Data cleaning and preparation is a hard work. It takes time.

B It is important not to overlay too much value onto visualization before modeling, as soon as it can biased

C We learned some new techniques for working with wide datasets.

D Feature selection was the most important part of our work. We used different methods, and tried to compare them to choose best.

E We have a piece of text data which we left untouched. We plan to work with text and multi-stage factors in the future.



CONCLUSIONS

- **A** Number of investors in seed
- **B** Team size senior leadership
- **C** Data Science
  Engineering
  Sales
- **D** Business Strategy
  Leadership
- **E** Experience in Fortune500
- **F** Last funding date

AUTHORS

Iryna Popovych

Sofiya Hevorhyan

LINKS

/DataAnalysisR

link to dataset

THANK YOU