

EIGHTH EDITION

LAUNCHING NEW VENTURES

An Entrepreneurial Approach

KATHLEEN R. ALLEN

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An Entrepreneurial Approach

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The world we live in today is vastly different from the one that existed when I wrote the first edition of Launching New Ventures in 1995. The most notable difference is the prevalence of smartphones and social media. Nevertheless, I would argue that the future of the United States, and certainly the world, still lies with entrepreneurs who start the innovative businesses that create jobs and produce products and services to fuel the economy. For the foreseeable future, we will live in a world characterized by a high degree of uncertainty, an accelerated pace of change, and the impact of social media on everything from politics to business to culture. While there are benefits to these changes, there are also enormous risks. Entrepreneurs are comfortable with risk because they can calculate probabilities and outcomes for the risks they face. Uncertainty, on the other hand, has no probabilities associated with it; it can't be calculated or predicted. To survive in a world of uncertainty, entrepreneurs must develop businesses that are fast, lean, adaptable, and flexible. Whether a new venture operates in the online world, the life sciences, manufacturing, or services, entrepreneurs need to compress the product development timeline, get to an early prototype quickly and cheaply with the minimum number of features needed to meet the customer's requirements, continually refine their business models, and find ways to get traction as fast as possible. An uncertain business environment means more than ever that the winners will be those who launch businesses as entrepreneurs in the true Schumpeterian sense of the word: disrupting what has gone before, looking for the unexpected, and creating new value.

The evidence for the benefits of entrepreneurship is clear when we study its impact on society and on the economy. However, the evidence is not so clear when we look at entrepreneurship in the academy. As educators and practitioners, we assume more benefits than we can actually quantify. In the preface of the sixth edition, I referred to an important article written by one of the early leaders in the field. It bears repeating here because the problem persists. Researcher and Professor Dale Meyer wrote about the field of entrepreneurship as a discipline in a provocative article for the Journal of Small Business Management called "The Reinvention of Academic Entrepreneurship." He lamented the lack of rigorous metrics for measuring the impact of entrepreneurship education on students and society, the heavy reliance on neoclassical economic paradigms, and the blurring of the boundaries between entrepreneurship and small business management. He called for more emphasis on creative, self-organizing processes that entrepreneurs employ to craft complex, adaptive business systems. I wholeheartedly agree with Meyer's assessment. Today, the term entrepreneurship has been diluted by overuse in contexts that have nothing to do with new venture creation. Entrepreneur is being co-opted by everyone, including the media, to describe what is more traditionally referred to as a small business owner, a successful musician, or an effective product manager. The rationale for this dilution is that if you think like an entrepreneur, you're an entrepreneur. I believe that this rationale confuses entrepreneurship with creativity and innovation. In every edition of *Launching New Ventures*, I have attempted to remain true to the Schumpeterian view of the entrepreneurial process as "creative destruction." Now, more than ever before, the world needs entrepreneurs, in the strictest sense of the word—those who challenge the way we think about business, who create innovative business models that solve new problems, and who excel at sense-and-respond processes in the face of great uncertainty.

With all the knowledge we now have about how to operate effectively in a global market, how to build successful companies with extraordinary valuations, and how to innovate, we still have so much more to learn. And that is perhaps why so many of us enjoy the field of entrepreneurship because it is messy, chaotic, and in a constant state of change. We are continually challenged to revise our ideas—what we knew to be true—in the face of almost daily changes in the countless variables that affect the complex launch and growth of a new business.

Launching New Ventures, Eighth Edition, represents the most current thought, ideas, and practices in the field of entrepreneurship. In fact, ever since its first edition, Launching New Ventures has endeavored to extend the boundaries of what we know about entrepreneurship and to celebrate the uniqueness and creativity of entrepreneurs.

CONTENT, ORGANIZATION, AND UNIQUE COVERAGE

Launching New Ventures is organized around the process of creating a startup, from the creation of an opportunity to the validation of that opportunity to the launch of the business. It is designed to help readers organize and plan for venture creation by mentally (and sometimes physically) engaging in the various activities that entrepreneurs typically undertake. This book has never sought to be all things to all people. It has a very specific emphasis on pre-launch activities—those things that entrepreneurs do to prepare to start a business and secure their first customer. The reason for this emphasis is that the decisions made to prepare a business for launch will have a significant impact on how successful that launch is. So this book explores activities such as opportunity creation and feasibility analysis in more depth than the average book on entrepreneurship. The book also takes a distinctly entrepreneurial view of new businesses as opposed to a small business perspective. In a complex, global world, new business owners, whether their business might be the next Google or simply a small restaurant, need to think like an entrepreneur. They need to be opportunity-focused, innovative, growth-oriented, and constantly looking for new ways to create and capture value for customers.

Part One introduces the foundations of entrepreneurship and entrepreneurial opportunity, which are important to understanding the decisions that entrepreneurs make, the environment in which they make those decisions, and the tasks they must undertake before starting a new company. In Chapter 1, readers will learn the nature of entrepreneurial ventures and how they are distinct from other types of businesses as well as the role of entrepreneurship in the economy. Chapter 2 dispels many myths about entrepreneurs and helps readers understand the characteristics and behaviors that work for and against entrepreneurs. Readers also

learn about the entrepreneurial mindset, which is so critical for a successful startup. Chapter 3 introduces the subject of opportunity and how entrepreneurs create and shape opportunities for themselves.

Part Two addresses the heart of entrepreneurial activity, the testing of a business model through feasibility analysis. It opens with Chapter 4, "Analyzing the Industry and Market" where readers will learn how to study an industry, the environment in which the new business will operate, and follows that with a discussion of how to effectively conduct market research to understand customer needs and levels of demand. Chapter 5 focuses on the design, development, and testing of a business model as well as how innovation happens in all the components of the business model. Chapter 6 explores the way entrepreneurs develop products and services; it considers product development using lean methodologies, prototyping, and the minimum viable product. Chapter 7 considers ways to protect a startup's assets through intellectual property rights. Chapter 8 looks at how to build an effective founding team and also discusses how to determine what gaps in experience and expertise may exist in the management team and how to compensate for them with such solutions as strategic alliances and independent contractors. Chapter 9 closes this part by addressing the startup resources entrepreneurs must gather and how to calculate the required capital and other resources needed to launch the venture and operate it until it achieves a positive cash flow from the revenues it generates.

Part Three deals with business design, those activities that take place once you know you have a feasible venture. It begins with Chapter 10, which describes how to move from a feasibility analysis to preparing a business or execution plan. Chapter 11 deals with the design of an entrepreneurial company, considering how entrepreneurial businesses are organized, how entrepreneurs determine the best business location, and how they develop their initial human resource capability. Chapter 12 focuses on how products and services are produced and addresses issues related to planning the startup operations of a new business, such as production, quality control, customer service, outsourcing, and managing the supply chain. Chapter 13 looks at the legal form of the business and discusses the advantages and disadvantages of sole proprietorships, partnerships, and corporate forms. Chapter 14 deals with the role and implementation of the startup marketing plan and how to promote new products and services effectively with limited resources. It pays particular attention to the role of social networks and search engine marketing. The chapter also addresses personal selling and customer relationship management. Chapter 15 explores the increasingly important topics of vision, ethics, and social responsibility. The value system of a new business shapes the culture of the business and the image it will have to live up to as it builds its reputation. Readers will be challenged to define a vision for a new venture based on the values they believe to be important. They will also gain a greater understanding of the need for ethics and social responsibility in any business. Part Four explores planning for growth and change in the new organization. It begins with Chapter 16, which looks at how to fund a startup as well as a rapidly growing venture, including the cost and process of raising capital, venture capital, and the IPO market. Chapter 17 deals with exploration and exploitation growth strategies for entrepreneurial ventures. It also pays particular attention to growing by going global and concludes with a discussion of harvest and exit strategies.

SPECIAL FEATURES IN THE EIGHTH EDITION

The eighth edition contains a variety of features of value to instructors and readers.

- 1. Chapter Objectives highlight the key topics for each of the chapters.
- 2. The digital version contains inline activities that enable students to check their understanding of important concepts as they move through the chapters.
- 3. Arguably, the biggest change is the MindTap platform, which offers students a new way to engage with their course material and offers instructors easier ways to assess students' understanding of the materials.

NEW TO THIS EDITION

The following are the major changes to the eighth edition.

Overall Changes

Examples and data have been updated.

Chapter by Chapter Changes

- ➤ Chapter 1: All statistics have been updated, as well as the inclusion of the most recent market trends: artificial intelligence, augmented reality, synthetic biology, and genomics.
- > Chapter 2: All data have been updated.
- ➤ Chapter 3: The chapter title, Creating Opportunity, underscores the proactive nature of opportunity for entrepreneurs. They don't wait for opportunity; they create it. The chapter has been updated with new data and reorganized to make it more concise.
- ➤ Chapter 4: The chapter opens Part II on feasibility analysis and has been structured with more bullet points to highlight key learning and facilitate reading.
- ➤ Chapter 5: A new quote was added as the lead-in to the chapter. It provides a new way to explain the difference between a user and a beneficiary. The chapter is more concise.
- ➤ Chapter 6: In addition to updating examples, the chapter features a new chapter section and associated figure on product development trade-offs as well as an in-depth discussion of the minimum viable product.
- ➤ Chapter 7: This chapter is devoted to intellectual property and ways to protect the startup's assets. All statistics and laws have been updated with current examples.
- ➤ Chapter 8: This chapter is about the founding team. The chapter incorporates important research on founding teams conducted by Noam Wasserman and addresses the issue of entrepreneur scalability.

- Chapter 9: This chapter goes in depth on the process of determining startup capital. It offers readers inline activities to sharpen their understanding of business metrics, customer value, and sales forecasts.
- ➤ Chapter 10: This chapter opens Part III on business design by discussing the preparation of a business plan. The chapter also includes a new approach to the elevator pitch. New inline activities help readers understand adoption patterns, customer value, and social media strategies.
- Chapter 11: The chapter treats the critical areas of location decisions, hiring, and stock with a number of new inline exercises.
- ➤ Chapter 12: This chapter focuses on startup operations and includes new inline activities that test the reader's understanding of supply chains and manufacturing.
- Chapter 13: This chapter focuses on legal forms of organization. All laws have been updated and new inline activities test the reader's understanding of legal concepts.
- ➤ Chapter 14: This chapter deals product adoption/diffusion and marketing strategies and tactics. The social media metrics section has been enhanced to reflect the latest tactics. The chapter has been completely refreshed with new examples.
- ➤ Chapter 15: This chapter closes the part on business design and is now the chapter on ethics and social responsibility. The entire chapter has been refreshed with new examples.
- ➤ Chapter 16: This chapter focuses on how to fund startup and growth Using new inline activities, readers can sharpen their skills in money basics, investment capital, and the valuation of startups.
- ➤ Chapter 17: This chapter combines the topics of growth and change because they normally occur together. The chapter data have been updated and the chapter includes new inline activities that check the reader's understanding of the material.

SUPPLEMENTAL MATERIALS

On the Instructor Companion Site, you'll find everything you need for your course in one place! This collection of book-specific lecture and class tools is available online via www.cengage.com/login. Access and download PowerPoint presentations, test bank, and more.

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PART

ENTREPRENEURSHIP AND OPPORTUNITY

CHAPTER 1: Understanding Entrepreneurship

CHAPTER 2: Preparing for the Entrepreneurial Journey

CHAPTER 3: Creating Opportunity

THE ROAD TO STARTUP

Simplified



Find a Problem Make sure it's significant and

compelling



Engage with Potential Customers

Observe Listen Focus on problems



Develop

The solution in a physical forma prototype.
Test it with customers



Build the Product and Get It Ready to Sell

Include feedback from customers in the design and development



Develop and Test the Business Model

How will you make money? If necessary, who do you know who can contribute capital to your business?



Look for Partners

Who can share resources and help you get to market faster?



Develop a Marketing Plan

What is the best way to reach customers?



Decide on the Legal Form for the Company?

How to split equity? Roles and responsibilities



Hit the Market and Learn If Your Business Model Works

Get market feedback and revise if needed. Retest the model



1

UNDERSTANDING ENTREPRENEURSHIP

"I think a good entrepreneur has a very clear grasp of what the goal is, an unwavering sense of the goal, an utterly agile approach of getting there."

—JOHN KATZMAN, CEO NOODLE EDUCATION

CHAPTER OBJECTIVES

- Define entrepreneurship.
- Explain the role of entrepreneurship in economic growth.
- Distinguish entrepreneurial ventures from small businesses in terms of their purpose and goals.
- Describe the evolutionary history of entrepreneurship.
- Identify today's broad trends in entrepreneurship and technology.

t the age of 16, Jan Koum and his mother fled their Ukrainian homeland to the United States. A self-taught programmer, he eventually spent nine years at Yahoo! where he met Brian Acton who would become his co-founder of WhatsApp, an app that provides open and free access to people to communicate via text messages. In 2014, Facebook acquired WhatsApp for \$22 billion and that transaction remains the highest price paid for a venture-backed startup in history. The WhatsApp story goes a long way toward explaining why so many people want to become entrepreneurs. While the lure of success and wealth is enticing, the reality is that most entrepreneurial businesses do not end up like WhatsApp. In fact, WhatsApp is only one example of what success looks like in the world of entrepreneurship.

What is **entrepreneurship**? From one of the earliest definitions of entrepreneurship, proposed by Austrian economist Joseph Schumpeter, we learn that entrepreneurship is a form of "creative destruction." Breaking down old ways of doing things to create new value.¹ Another definition by Harvard professor Howard Stevenson embodies the essence of what entrepreneurship is: The process by which individuals—either on their own or inside organizations—pursue opportunities without regard to the resources they currently control.²

This definition suggests that entrepreneurship is more than simply starting a business; it also encompasses a mindset or way of thinking and a set of behaviors. That way of thinking is usually opportunity-focused, risk taking, innovative, and growth-oriented. Although entrepreneurship is still most commonly thought of in the context of starting a business, the entrepreneurial mindset can be found within large corporations, in socially responsible nonprofit organizations, and anywhere that individuals and teams desire to differentiate themselves and apply their passion and drive to executing a business opportunity. Entrepreneurship is not unique to any country, gender, race, age, or socioeconomic sector. Entrepreneurs can be found in some form in every country, in every age group, and (increasingly) in women as often as in men. The entrepreneurial fever does not distinguish between the rich and the poor; in fact, it touches anyone who has the passion to be self-employed or anyone who is determined to be independent and to take charge of his or her life. The entrepreneurial way of thinking can be understood and practiced, and the skills and behaviors of the entrepreneur can be learned and applied. The only characteristic of entrepreneurs that is arguably intrinsic is passion, the drive to achieve something. Passion cannot be taught or practiced; it simply exists when the right elements come together—for example, when an entrepreneur creates a business opportunity and devotes his or her full attention and resources to bringing it to life. Passion is found in successful people in all disciplines—great musicians, artists, writers, scientists, and teachers. It is what drives a person to go beyond expectations and to be the best that person can be.

This chapter explores entrepreneurship as a phenomenon and lays the groundwork for the skills and behaviors that are fundamental to the remainder of the text.

THE ROLE OF ENTREPRENEURSHIP IN THE ECONOMY

To understand the role that entrepreneurship plays in the economy, it is important to describe the process that entrepreneurs undertake as they create and exploit opportunity. Figure 1.1 depicts a view of this entrepreneurial process. As displayed, you can see that it is not a linear process but rather something more like a dynamic system with complex moving parts.

- ▶ Phase 1: Entrepreneurs initially work to find a significant problem or need in a market or an industry. Then they do preliminary research to understand the industry, the potential market, and any issues they might face in the areas of intellectual property, regulation, or in product development in the case of a technology solution. They then develop hypotheses from what they've learned.
- **Phase 2:** Here entrepreneurs focus on validating the hypotheses they have made about the customer, the solution, and the proposed **business model**. The results will ultimately provide important information about potential sources of revenue and major drivers of cost.
- ▶ Phase 3: When the activities in Phases 1 and 2 give entrepreneurs sufficient confidence that their business is feasible, it's time to consider the design of the business and to create a plan for its execution. This means having the right team and partners in place as well as choosing the best time to launch the business.

Figure 1.1 illustrates the phases of The Entrepreneurial Process.

The successful execution of the entrepreneurial process results in a new venture; however, the process of testing and validation continues as the new business responds to a dynamic environment that includes all the variables external to the business that can impact its growth. Some of those external variables include the economic environment, competition, new laws and regulations, labor supply, and sources of capital. As the leader, an entrepreneur essentially plays two roles—that of the catalyst, initiating and driving the process, and that of a ringmaster in a three-ring (or more) circus, managing the process through all its changes as the business grows.

This complex entrepreneurial process provides many benefits to society. Chief among these benefits are economic growth, new industry formation, and job creation. The following sections offer some insight into these contributions.

1.1a Entrepreneurs Spur Economic Growth

Early economists recognized that technology is the primary force behind rising standards of living³ and that technological innovation would determine the success of nations in the future. Technological change happens when an entrepreneur identifies:

- 1. New customer segments that appear to be emerging
- 2. New customer needs

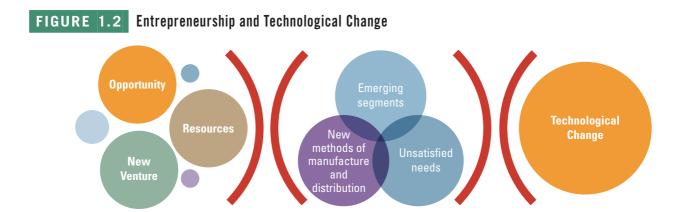
FIGURE 1.1 The Entrepreneurial Process

Phases	PHASE 1: Environment, Discovery and Opportunity	PHASE 2: Business Model Development and Testing	PHASE 3: Business Design, Planning, and Execution
RESEARCH	Critical Industry Forces Suppliers, Rivalry, Barriers to Entry Threat of Substitutes Trends: Technological, Political, and Social	Value Proposition: The Solution Applications Product/Service Offerings Benefits to Customer	Business Process Flow Customer Acquisition to Delivery Business Activities
	Market: Pains/Problems Market Size and Growth Competition Trends	Market Size and Growth Competition Addressable Market Segments	
	Intellectual Property, Regulatory, and Technology Validation Patent Decisions, Regulatory Impact Technology Platform Development Field Tests and Pre-Clinical tests Technology Validation	Operations Manufacturing-Operations Plan Marketing Plan Management Plan Contingency Plan Execution Plan	
MES	Revenue Sourc Number o Ty Si Speed to	Strategic Partners Independent Contractors Strategic Alliances Investors	
OUTCOMES	Cost and Profi Ty Si Impor	Launch Strategy License Start a Business Sell Joint Venture	
	Startup Capita		
EXECUTION	Managem Board of Dire Expertise, Expe	Market Timing When to launch	

- 3. Existing customer needs that have not been satisfied
- 4. New ways of manufacturing and distributing products and services. (See Figure 1.2.)

Identifying these needs offers the opportunity to invent new technology solutions that change the way we do things or to improve on existing products, services, and business models.

Economic Growth



Entrepreneur

1.1b Entrepreneurs Create New Industries

Customer Needs

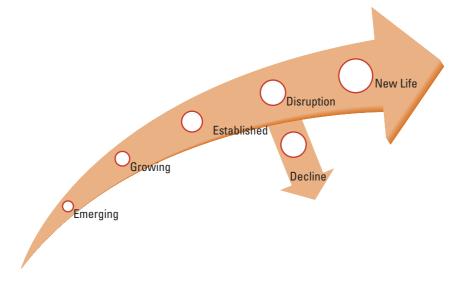
New industries are another important outcome of entrepreneurship and technological change. An industry is simply the people and companies that engage in a category of business activity such as semiconductors, medical devices, or food services. New industries are born when technological change produces a novel opportunity that enterprising entrepreneurs seize. For example, Apple's iPhone, introduced on January 9, 2007, spurred the development of the mobile app industry, which is now one of the fastest growing sectors in the broader software industry. It is expected to grow 270 percent by 2020 reaching \$189 billion in sales.⁴ The iPhone itself was an innovation built on the know-how of many earlier inventions. Nevertheless, Apple saw the opportunity to change the way we use phones by essentially putting a very powerful computer into everyone's hands and then encouraging developers to create unique programs exclusively for the device.

Industries don't last forever. Much like humans, they have life cycles—they're born, they grow, they decline, and they die. Figure 1.3 depicts the generic life cycle of an industry. The earliest stage of an industry is a time of rapid innovation and change as young firms struggle to become the industry standard-bearers with their technology. As these entrepreneurial firms achieve noticeable levels of success, more and more firms desiring to capitalize on the potential for success enter the industry. As the industry grows, it generally becomes more fragmented as a result of so many firms competing for position. Then, at some point consolidation begins to occur as the stronger firms begin to acquire the smaller firms and the weaker firms die out. Eventually, the number of firms in the industry stabilizes and the firms mature. If innovation in the industry ceases to occur, the industry output may actually begin to decline. However, if new, disruptive technology is introduced, the industry may now have a new platform on which to innovate and grow again.

1.1c Entrepreneurs Create Jobs

Entrepreneurial ventures are responsible for job creation that is disproportionate to the net total new jobs created in the United States over the past 25 years. The U.S. Small Business Administration (SBA) defines a small business as one with fewer than 500 employees, which by many standards is not very small and includes

FIGURE 1.3 The Industry Life Cycle



both high-growth technology ventures and small "mom and pops"—quite a range indeed. Over the past two decades, startups have accounted for about 40 percent of new jobs while the expansion of existing companies accounts for the remaining 60 percent of new jobs.⁵ In all, 62 percent of net new jobs come from small businesses; small businesses comprise 99.9 percent of all businesses.⁶ It is important to note, however, that the vast majority of net new jobs created by the small business sector are created by a few rapidly growing young firms called **gazelles** or high-impact businesses. These young businesses generally have sales that double over a four-year period with employment growth of two or more times over the same period.⁷ It is also interesting to learn that there are 29.6 million small businesses in the United States, 80 percent of which have no employees.

Given that we do business in a global marketplace, it's important to know something about international entrepreneurship. The annual *Global Entrepreneurship Monitor* employs samples that represent about 75 percent of the world's population and 90 percent of the world's GDP. The study divides countries into three groups based on where the country stands in terms of growth and they look at early-stage entrepreneurial activity.⁸ In the 2016/2017 report, they identified three categories of countries: factor-driven, efficiency-driven, and innovation-driven.

Factor-driven economies rely on unskilled labor and the extraction of natural resources for growth. Here businesses are normally created out of necessity so these countries tend to have very high entrepreneurial activity rates relative to other types of economies. Examples are India, Zambia, Iran, and the Russian Federation. Early-stage entrepreneurial activity rates are generally below 15 percent.

- **Efficiency-driven economies** are those growing and in need of improving their production processes and quality of goods produced. Examples are Argentina, Egypt, Croatia, and South Africa, although the highest entrepreneurial activity rates were found in Ecuador at 33 percent.
- **Innovation-driven economies**, which are the most advanced, are where businesses compete based on innovation and entrepreneurship. Examples are the United Kingdom, Singapore, Israel, and the United States. The highest levels of entrepreneurial activity are found in Australia, Estonia, the United States, and Canada at about 17 percent.

One consistent finding is that across all type of economies, there are more people in the 25- to 34-year-old age group with intentions to start a business and entrepreneurship is a highly regarded activity and career path.

THE NATURE OF ENTREPRENEURIAL STARTUPS

Entrepreneurial ventures and small businesses are related, but they are not the same in most respects. Both are important economically but each provides different benefits and outcomes. Schumpeter described entrepreneurs as equilibrium disrupters who introduce new products and processes that change the way we do things, while small-business owners typically operate a business to make a living. Examples of small businesses are small shops, restaurants, and professional service businesses. They form what has been called the **economic core**. In some cases, they're known as lifestyle businesses or "mom-and-pops," not only because they tend to stay small and geographically bound, but more because their owners make a conscious decision to remain small. As a result, they tend to be slow growing and often replicate similar businesses already in the market.

It should not be forgotten, however, that even high-impact ventures start small. The difference is that the high-impact entrepreneur's goal is not to stay small.

In general, high-impact entrepreneurial ventures have three primary characteristics. They are:

- Innovative—the venture brings something new to the marketplace.
- > Value-creating—the venture creates new jobs that don't draw from existing businesses and serve customer needs that are currently unserved.
- Growth-oriented—the entrepreneur sees the business growing to a regional, national, or global level.

Choosing what kind of business to start is very important, because that choice influences all subsequent decisions and determines what kinds of goals you are able to achieve. For example, if you intend to grow a business to a national level, you will make different decisions along the way than if the intent is to own and operate a thriving restaurant that competes only in the local community.

1.2a Risk and the Entrepreneurial Venture

It's impossible to talk about entrepreneurial ventures without considering the effects of risk as risk is an inherent part of the entire entrepreneurial process. With more information and validation from the market, the impact of risk changes over time.

Much of new venture risk occurs early in the creation process. Borrowing a term from product development, we can call the period of time prior to launch and startup the *fuzzy front end*, which simply means that the activities undertaken at this point are often unclear and subject to change as more information is obtained. The fuzzy front end has been modeled in economic terms. Simply put, the amount of investment an individual is willing to make in a new product—or, in this case, in a new venture—is a function of the probability of its success, the value of that

success, and the cost of failure [Inv = f(PS + VS + CF)]. A change in any one of these values will alter the economics of the bet.¹¹ **Nascent** entrepreneurs use the time spent in the fuzzy front end to calculate the probability of success as an entrepreneur; what that success will mean in terms of return on his or her investment of time, money, and effort; and what the risk or cost of failure might be. Because these risk estimates are highly subjective, it's important for entrepreneurs to gather sufficient information and test the business model to reduce that risk as much as possible.

The intent to start a business is not in itself enough to make it happen. Due to the challenging nature of the endeavor, many potential entrepreneurs drop out of the process as they move from intention to preparation and then to execution. ¹² Many times they discover just how difficult it is to start a business or the business they want to start isn't feasible.

1.2b New Business Failure

The SBA reports that about half of all new businesses will survive five years or more, and approximately one-third will survive 10 years or more. Therefore, it appears that survivability tends to increase with age. But wait, maybe not. Statistic Brain, a research institute, found that 50 percent of all U.S. companies fail after five years and 70 percent after 10 years. Operhaps survivability isn't about longevity. In any case, it's important to learn why failure happens.

There are several reasons for new business failure:

- 1. Entrepreneurs often start businesses with a solution looking for a problem. In other words, they haven't identified a real need in the market with customers willing to pay for a solution,
- 2. The solution is not necessarily unique or compelling. In other words, it is often a "me-too" solution that does not offer anything different from what is already in the market. Furthermore, entrepreneurs often do not communicate the **value proposition** effectively to the customer, and/or
- 3. Entrepreneurs often haven't identified and tested a business model that actually works.

All of these factors lead to failure. But beyond these factors, young firms have a higher chance of failure because they have to divert their scarce resources away from the critical operations of the company in order to train employees, develop systems and controls, and establish strategic partnerships.

Failure is a fact of life that must be dealt with. What matters is that you minimize the cost of failure and have a plan to recover quickly.

WHY ENTREPRENEURSHIP IS WHAT IT IS: A BRIEF HISTORY THAT YOU NEED TO UNDERSTAND

The United States was founded on the principle of free enterprise, which encouraged entrepreneurs to assume the risk of developing businesses that would make the economy strong. However, it was not until the 1980s that the word *entrepreneur*

ıĸ

came into popular use in the United States, and an almost folkloric aura began to grow around men and women who started rapidly growing businesses. These formerly quiet, low-profile people suddenly became legends in their own time, with the appeal and publicity typically associated with movie stars or rock musicians.

Today's entrepreneurs are no different. Elon Musk has changed the game for the space industry by creating a lower-cost solution for sending cargo and satellites into space. Under the leadership of Jeff Bezos, Amazon.com completely disrupted the brick-and-mortar retail industry. Entrepreneurs such as these shake up the economy and change the game for everyone. They look for unsatisfied needs and satisfy them. Figure 1.4 summarizes the entrepreneurial evolution that has taken place since the 1960s, paving the way for an innovation economy that is the envy of the world.

1.3a The Decades of Entrepreneurship

In the *mid-1960s*, gigantic companies were the norm. General Motors in the 1960s was so large that it earned as much as the 10 biggest companies in Great Britain, France, and West Germany combined.¹⁵ Lacking competition from Europe and Asia, U.S. companies enjoyed unrestricted growth.

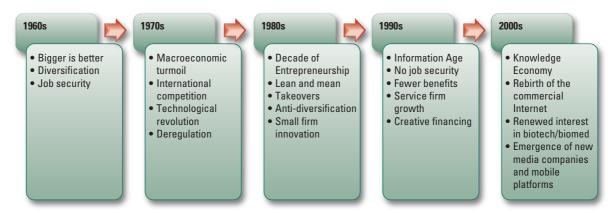
The *1970s* saw the beginnings of three significant trends that would forever change the face of business:

- 1. Macroeconomic turmoil
- 2. International competition
- 3. The technology revolution.

Macroeconomic Turmoil: The 1970s Vietnam War economy brought:

- **I**nflation
- Devaluation of the dollar
- Food prices skyrocketed as a consequence of several agricultural disasters.
- ▶ The formation of OPEC sent gas prices up 50 percent.
- ➤ Interest rates rose to a prime of 20 percent producing a major recession and an unemployment rate of 10 percent.¹6

FIGURE 1.4 The Decades of Entrepreneurship



International Competition: By 1980, one-fifth of all U.S. companies faced foreign competitors that had far more favorable cost structures with much lower labor costs. Imports, particularly in the automobile and machine tools industries, were suddenly taking a significant share of the market from U.S. businesses.

Technology Revolution: The introduction in 1971 of the Intel microprocessor, the Mits Altair personal computer in 1975, and the Apple II computer in 1977 started a technology revolution. Microprocessors succeeded in rendering whole categories of products obsolete—such things as mechanical cash registers and adding machines, for example—and effectively antiquated the skills of the people who made them.

By the *early 1980s*, business was in terrible shape. The Fortune 500 saw a record 27 percent drop in profits.¹⁷ Large mills and factories were shutting down; manufacturing employment was declining; and yet, ironically, productivity remained the same or actually increased. New, smaller manufacturers were still generating jobs—and not only manufacturing jobs, but service jobs as well. How was this possible?

To become competitive, the smaller, more flexible, entrepreneurial manufacturers had hired subcontractors who could perform tasks such as bookkeeping and payroll more efficiently. These service firms developed to support the needs of the product sector, but they also inspired the creation of other service firms. The 1980s became known as the Decade of Entrepreneurship. On the heels of the emergence of Silicon Valley and its legendary entrepreneurs, the mainstream press began to focus on business activities, creating many popular magazines such as *Inc.* and *Entrepreneur*.

Responding to this entrepreneurial drive, big businesses began to restructure and reorganize for a new way of doing business. More than perhaps anything else, the 1990s were characterized as the Information Age. The commercial Internet emerged midway through the decade, and suddenly global competition and resources were more readily available than ever before. The Internet made entrepreneurship and the ability to compete alongside large established companies in the same markets a reality. Furthermore, with more and more jobs being shipped overseas, employees learned that job security was no longer a fact of life. U.S. companies quickly discovered that their competitiveness lay in the control of information and new ideas, and clearly the Internet was to play an important role in this new view of the world. The late 1990s brought the "dot com" bubble and the rush of the venture capital community to position itself for what appeared to be a new way of doing business. At the same time, the interest in non-Internet-related technology was waning as investors saw a much quicker return on their investment in the world of e-commerce.

The new millennium ushered in what many referred to as the **knowledge economy**, brought about by increased globalization and the competitive shift to more "knowledge-based economic activity." In the new economy, the primary resource was knowledge rather than raw materials and physical labor and the emergence of significant entrepreneurship capital supported the development of new business models that monetized knowledge. The knowledge economy of the early 2000s was also described by low-cost competition from Asia and Central and Eastern Europe that came about when transfer costs were driven down in the telecommunications and computer sectors, making it easier and less expensive to move

capital and information. Consequently, most routine tasks in production and manufacturing were now more efficiently accomplished in low-cost locations.

Renewed interest in non-Internet-related technologies was one of the results of the dot-com crash of 2000 as investors turned to solid technologies that could be protected through patents and developed a growing interest in green tech, biotech, and biomedical devices that spread into the second decade of the new millennium.

CURRENT ENTREPRENEURIAL TRENDS

In the previous edition of this book (2016), major trends were (1) digital anonymity, (2) domestic manufacturing, (3) big data, and (4) the lean startup movement. Those trends continue; but for 2018 and beyond, research firms like Gartner, Forrester, and Deloitte see some key technology trends that will be the foundation for the next generation of entrepreneurial businesses. They are summarized here.

1.4a Intelligent Technology

Artificial intelligence (AI) as a technology has been around a long time, but today its potential is beginning to be fully realized. It is arguably the most important platform technology today.¹⁹ AI is about machine-learning solutions targeted toward completing a specific task such as driving a self-driving car in a controlled environment. In general, AI augments human decision making and enables us to take advantage of skills like facial recognition, diagnostics, and many other tasks that can be automated and executed faster and more reliably than a human could do. In the consumer market, Siri, Alexa, and Google assistant are current examples of AI voice recognition. In the not too distant future every app and service will incorporate AI in some capacity such as analytics.

1.4b Digital

The digital world will see increased capabilities in areas such as the following:

- > Immersive experiences. Mixed realities that include augmented reality and virtual reality will blur the lines between the real world and the digital. The user will interact with objects in both the digital and real world. You are already seeing these immersive experiences in such things as video games, manufacturing, medical training, and military simulations.
- ▶ Digital Twins. A digital twin is exactly what you might think it is—a digital replica of a human or real-world entity. Using connected sensors and endpoints, we can now conduct advanced simulations, operations, and analysis via a digital twin.

1.4c **Disruption**

Some technologies will exponentially transform the way things are done. For example, we are seeing advances in **synthetic biology** and **genomics** using technologies like CRISPR, which enables editing of and making changes to the genome

of living cells. Soon we may be able to correct for genes that give someone a higher chance for, say, Alzheimer's disease. Another area of disruption that will lead to new opportunities is quantum computers, which are enormously powerful machines that process information differently from the computer you're currently using. They can untangle complex structures and potentially enable us to discover new medicines and materials.

LOOKING AHEAD: THE ORGANIZATION OF THE BOOK

This book is divided into four sections that reflect the key elements of the entrepreneurial process.

1.5a **Part One**

- ➤ Chapter 1 serves as an introduction from a macro perspective to the field of entrepreneurship and the environment in which entrepreneurs start new ventures today.
- > Chapter 2, another foundational chapter, explores the entrepreneurial journey from the entrepreneur's perspective, a micro perspective, and helps you prepare for this journey by dealing with the human side of entrepreneurship as a mindset and a way of life.
- ➤ In Chapter 3, the process of entrepreneurship begins and we look at how opportunities are generated through the development of creativity and problem-solving skills.

1.5b Part Two

➤ Chapters 4 through 9 explore feasibility analysis for new ventures in detail by examining the various types of hypotheses and tests that entrepreneurs use to determine the conditions under which they can launch their businesses. They include all the areas of the business that must be researched and understood in order to increase the chances of a successful launch.

1.5c Part Three

Chapters 10 through 15 focus on the elements of business design and operations, and they address how to develop a business plan or execution strategy for the startup. Chapter 15 also introduces ways to incorporate ethics and social responsibility into the business.

1.5d Part Four

- ➤ Chapters 16 and 17 recognize that any successful business undergoes growth and change.
- ➤ Chapter 16 looks at how to fund startup and growth as well as architect a harvest strategy for the entrepreneur and any investors.
- **>** Chapter 17 explores how to plan for growth and change.

Entrepreneur skills are key not only to economic independence and success but to business survival. The marketplace puts a premium on creativity, initiative, independence, and flexibility. Entrepreneurs who develop those behaviors and display those characteristics will be more likely to succeed.

2

PREPARING FOR THE ENTREPRENEURIAL JOURNEY

"Success isn't permanent, and failure isn't fatal."

-MIKE DITKA, PROFESSIONAL FOOTBALL COACH

CHAPTER OBJECTIVES

- Dispel myths about entrepreneurs.
- Understand the many pathways to entrepreneurship.
- Appreciate the challenges and opportunities of entrepreneurship.
- Prepare to become an entrepreneur.

ntrepreneurship is a personal journey that begins in the mind of an individual. But it is much more than that. From an entrepreneur's motivation to start a business to the decisions made about growth, customers, facilities, employees, and the exit from the business, everything comes down to people and their needs and motivations.

For example, entrepreneurs quickly learn the importance of people when they try to put together a founding team. Assembling the right team can, more often than not, make the difference between success and failure. It is very difficult today to start a new company as a solo entrepreneur; mostly because any single person rarely has all the knowledge and skills required to move quickly and make the decisions that will lead to success, so assembling a great team is more critical than many entrepreneurs believe. This chapter explores the personal journey to entrepreneurship, what it takes to become a successful entrepreneur, and the many ways to approach entrepreneurship throughout a career.

SAYING GOODBYE TO STEREOTYPES

Given the frequency with which entrepreneurs are discussed in the media, it is not surprising that stereotypes have developed around them. Not all of these stereotypes are flattering, and most are simply false. In fact, research has failed to identify that stereotypical entrepreneur. There are no psychological or sociological characteristics that can predict with any certainty who will become an entrepreneur or who will succeed as an entrepreneur. This section attempts to dispel some of the major myths surrounding entrepreneurs so that your entrepreneurial journey can begin on a solid, factual foundation.

2.1a Myth 1: It Takes a Lot of Money to Start a Business

One false assumption about entrepreneurship is that it takes a lot of money to start a business. Nothing could be further from the truth. For example, Lori Bonn Gallagher parlayed her love of travel and finding unique jewelry into a multimillion-dollar business. Starting with \$1,000 worth of samples of handblown glass jewelry that she discovered in France and a successful selling strategy, Gallagher secured a deal with Nordstrom to begin selling her imported jewelry in the United States. Today her jewelry is designed at her headquarters in Oakland, California, manufactured in Bali, and sold in retail outlets such as Nordstrom, Discovery Store, and Boston's Museum of Fine Arts museum shop (www.loribonn.com).

2.1b Myth 2: It Takes a Great Idea

Most of the great businesses that have been successful for at least 50 years—companies such as Walt Disney, Sony, and Merck—didn't start with a great idea. They started with a great team who simply wanted to create an enduring company. Usually it's not the idea but the execution plan that makes the business a success. Marc Benioff did not invent software as service, but his company Salesforce .com found the pain in hosted solutions and removed it. Instead of having to buy

applications to handle each function in the business, companies can access hosted services that can be customized to meet their specific needs. Benioff's success was not a great idea but rather solving a big problem with great execution.

2.1c Myth 3: The Bigger the Risk, the Bigger the Reward

Students of entrepreneurship often hear that risk is correlated with reward—the greater the risk taken, the greater the reward expected. Certainly, it appears that investors hold that point of view. But *risk* is a relative term, and the goal of most entrepreneurs and investors alike is to reduce the level of risk in any venture. In fact, investors *expect* entrepreneurs to do what it takes to reduce the risk for them such as testing the market, acquiring the first customer, and investing some of their own capital in the business; and no one expects the business to be worth less because risk was reduced.

2.1d Myth 4: A Business Plan Is Required for Success

There is no question that lenders, investors, and others want to know that you have done your homework before they're willing to risk their capital. It is also true that an operating business that wants to secure a loan from a bank will likely have to produce a business plan. But many entrepreneurs have started highly successful businesses without having a formal business plan in place—including recognizable companies such as Pizza Hut and Crate and Barrel that have survived for decades. Others have launched websites and been "in business" within a day, making money within a couple of weeks. The current thinking is that for most entrepreneurs to test a business idea, you need to get in front of customers. To grow a business, you need a plan. The issues of the business plan will be presented in more depth in Chapter 10.

2.1e Myth 5: Entrepreneurship Is for the Young and Reckless

Many people believe that if they haven't started their first business by the time they are 30, it is too late. They think that the energy, drive, resources, and risk involved are suitable only for the young. Nothing could be further from the truth according to the latest research on the topic. The Ewing Marion Kauffman Foundation reported that in 2015, 24 percent of startups were founded by entrepreneurs between 55 and 64 years old. Furthermore, the percentage of entrepreneurs aged 20 to 34 declined from 34.3 percent in 1996 to 25 percent in 2015. Surprisingly, today the ages of entrepreneurs are fairly evenly distributed across all the decades.² What this suggests is that entrepreneurship can be a lifetime endeavor.

2.1f Myth 6: Entrepreneurship Cannot Be Taught

This myth is a corollary to "Entrepreneurs are born, not made." Both are wrong. There is a lot about entrepreneurship that can be taught, including specific skills and behaviors. People who don't naturally have the skills of a successful entrepreneur can certainly learn and apply them. Management guru Peter Drucker asserted,

"The entrepreneurial mystique, it's not magic, it's not mysterious, and it has nothing to do with the genes. It is a discipline. And, like any discipline, it can be learned." Scholarly research over a number of years has supported that claim. In fact, a 2008 twin study by Nicolaou and Shane using 870 pairs of identical twins and 857 pairs of same-sex fraternal twins to study entrepreneurial activity, found that entrepreneurs are about 40 percent born and 60 percent made. The born part was not deterministic but rather explanatory; that is, their results pointed to strong evidence for the effect of environmental factors, including genetics, on entrepreneurial propensity. Practically speaking, the born part is what cannot be taught: the passion to persist and achieve as well as the willingness to take risk.

PATHS TO ENTREPRENEURSHIP

Entrepreneurs are as varied as the kinds of businesses they start and the precipitating events that led them to become entrepreneurs in the first place. In general, people start businesses either out of necessity or driven by opportunity. In the United States, opportunity-driven entrepreneurship is far more prevalent than in efficiency-driven or factor-driven economies such as Brazil and Uganda, where entrepreneurship frequently happens out of necessity.⁵ Entrepreneurs typically choose the startup process when:

- 1. Industry entry barriers are low.
- 2. When there is a lot of uncertainty in the job market.
- 3. When investment capital is plentiful.
- 4. The opportunity they seek to exploit involves a **breakthrough** or disruptive technology that will make previous technology obsolete.

There are many paths to entrepreneurship, and in the following sections we briefly look at four broad categories that differ from the traditional path: the home-based entrepreneur, the serial entrepreneur, the nonprofit entrepreneur, and the corporate entrepreneur.

2.2a The Home-Based Entrepreneur

It might sound strange to refer to a home-based business as entrepreneurship. And in most cases, you would be right because many of these are hobby businesses, consulting, and freelance-type businesses that don't grow or hire a lot of employees; but many others are entrepreneurial ventures that compete in the same arena as brand-name businesses with large facilities. Technology has made it possible to do business from virtually anywhere, so entrepreneurs don't have to work in traditional office spaces to start or run businesses. Moreover, home-based business owners can tap into more resources than ever before from their desktops or mobile devices to locate help for any problem they may be facing.

According to the Small Business Administration, as of 2014, 52 percent of small businesses were home-based. Given that there are about 28 million small businesses (fewer than 500 employees), that's 14,560,000 home-based businesses.⁶ Many

entrepreneurs with aspirations to grow their businesses start from home to save on overhead and reduce the risk of startup. Once the concept has proved itself, they often move out to acquire facilities and other resources that will support the growth of the company and the addition of employees. Some of the more famous businesses that started out home-based are Apple, Hershey's, Facebook, and the Ford Motor Company.

2.2b The Serial or Portfolio Entrepreneur

Many entrepreneurs enjoy the pre-launch and startup phases so much that when those activities are over and running the business takes center stage, they become impatient to move on to the next startup. It's the thrill of starting a business that keeps them going; they prefer to leave the management issues to someone else. An entrepreneur who starts one business and then moves on to start another is called a *serial entrepreneur*. Often these entrepreneurs start another business that builds on the experience from the first venture or builds on a specific expertise that the entrepreneur possesses or has acquired through a previous venture.

An entrepreneur who owns a minority or majority stake in several ventures is called a *portfolio entrepreneur*. Portfolio entrepreneurs often create a lot of churn in their portfolios as they seek out new business opportunities that link to their existing businesses. They tend to be constantly on the hunt for new opportunities. Certainly U.S. entrepreneur Elon Musk is in this category, having co-founded PayPal, then going on to found Tesla Motors, Solar City, and SpaceX.

2.2c The Nonprofit Entrepreneur

Today many enterprising people are turning to nonprofit types of ventures to realize their entrepreneurial dreams. Nonprofit, socially responsible businesses typically focus on educational, religious, or charitable goals. They generally seek tax-exempt status so that they can attract donations from companies and individuals who believe in their mission. Contrary to popular belief, nonprofit businesses can and should make a profit, but that profit must stay within the company rather than be distributed to the owners. Jennifer Staple-Clark founded Unite for Sight in 2000 while she was a sophomore at Yale University. The nonprofit is now a leader in "providing cost-effective care to 2.5 million of the world's poorest people, including more than 99,000 sight-restoring surgeries." Chapter 12 explores nonprofit ventures in more depth from a legal perspective.

2.2d The Corporate Entrepreneur

Entrepreneurship can also occur inside an existing organization. Known as corporate entrepreneurship, this phenomenon is now regularly studied by the research community; and increasingly, large organizations are finding it necessary to provide for entrepreneurial activity to remain competitive. Corporate ventures are distinct from other types of projects that large firms take on. For one thing, they generally involve innovation and activities that are typically new to the company so the risk of failure is high. There is also a high degree of uncertainty around such projects, so

they are often managed separately from core business activities. Recognizing that it is nearly impossible to reengineer and redesign an entire organization to be more entrepreneurial, many companies have chosen from several models to simulate the entrepreneurial environment required for innovation to occur:¹⁰

- ➤ Opportunistic Model: Most companies start their efforts to be more entrepreneurial with an opportunistic model. They wait for project champions to emerge and suggest new business opportunities. Then they decide if they want to move forward and provide some support.
- **Enabler Model:** Google is an example of an enabler model company that sprinkles resources throughout the organization to encourage innovation and entrepreneurship at all levels while establishing clear criteria for the selection of opportunities to pursue.
- ➤ Advocate Model: An advocate company acts like an evangelist, assigning ownership of a project or new business creation and providing modest seed funding to test it. DuPont, a global conglomerate, uses this approach to generate new sources of growth for the company.
- ▶ Producer Model: Some companies like IBM and Cargill establish formal organizations with dedicated funds and significant autonomy. This approach used to be called a skunkworks, dubbed so by Lockheed Martin when it originated the idea years ago to develop its stealth fighter jet.

Those who choose the corporate entrepreneurship path will need to align with key decision makers in the organization; work with only the best, most motivated people; and do any job needed to make the project work.

This book is not intended to address the specific needs of corporate entrepreneurs, but recognizing opportunities, conducting feasibility analyses, and developing execution plans are as relevant in the corporate environment as they are in a startup.

THE CHALLENGES AND OPPORTUNITIES OF ENTREPRENEURSHIP

One could argue that in the current startup environment of business **incubators** and startup **accelerators**, the first thing on entrepreneurs' minds seems to be what they have to do to raise money. However, based on years of research, this book argues that entrepreneurs create opportunity first from unmet needs or unsolved problems in the market and only then do they gather the resources to exploit that opportunity, unusually through a new venture.

Entrepreneurship is not for everyone, no more than any other endeavor is Table 2.1 presents an overview of the challenges and opportunities that come with choosing entrepreneurship as a career path. When reading the table, it is important to ask yourself if you would be able to deal with such a challenge and also if the opportunities of entrepreneurship are meaningful to you and compatible with your life goals. You may come up with even more challenges and opportunities than are presented in the table, but these are the most common.

2.3

TABLE 2.1

Challenges and Opportunities with the Entrepreneur Career Path

CHALLENGES	OPPORTUNITIES
Finding the right business opportunity	Becoming independent—taking charge of a career
Needing to work, often without pay, for long hours	Creating wealth
Facing uncertainty and high risk	Doing well while doing good—the potential for social entrepreneurship
Needing to make major decisions, often that affect other people's lives	Working in a business environment that the entrepreneur creates
Relying on other people for expertise and resources	Doing something the entrepreneur is passionate about
Having no previous experience on which to rely	Making a difference
Facing failure at some point	Creating new jobs
Finding the right people to help grow the business	Supporting the community
Raising capital and other resources	
Dealing with a sense of isolation and disillusionment	

The lead-up to the launch of the business is a very exciting time. Everyone wants to see the entrepreneur succeed, so encouragement and support are never lacking. But beneath that excitement lurks a painful reality: many entrepreneurs are surprised at what running a business day to day is really like. They have no comprehension of how difficult it is, and so often there is a feeling of being overwhelmed. This is one reason starting a business with a team makes sense; the difficulties and the work can be shared.

For all the challenges associated with entrepreneurship, the opportunities seem to outweigh them. To succeed at anything requires a higher-than-average amount of self-discipline and perseverance. Entrepreneurs don't give up easily, and they tend to stick doggedly to a concept until something or someone convinces them that it's time to move on to something else. That persistence is one important reason why entrepreneurs ultimately succeed.

One reason why entrepreneurship is such an interesting and exciting field is that it is constantly changing. It is well known that the greatest, most innovative ideas occur at the edge of chaos when things that aren't normally associated with each other are brought together in new ways. Opportunity is rarely found in stable, predictable settings, so potential entrepreneurs must learn to embrace change and uncertainty and be prepared to take risk.

PREPARING TO BECOME AN ENTREPRENEUR

Starting any business, large or small, requires a tremendous amount of time, effort, and resources. Therefore, it usually makes sense to start a business that has the potential to grow large and provide a good return on that investment, rather than spend the same amount of effort on a very small business that yields only a single job. In fact, research supports that notion that starting a small business exposes you to more risk because you are typically undercapitalized, poorly managed, and undifferentiated from competitors.¹¹

FIGURE 2.1 Preparing for Entrepreneurship



How, then, does an entrepreneur increase the chances for success? Through preparation. There are a number of important steps that you can take to increase your chances of success in entrepreneurship. Figure 2.1 displays these steps, and we discuss them here.

2.4a Find a Mentor

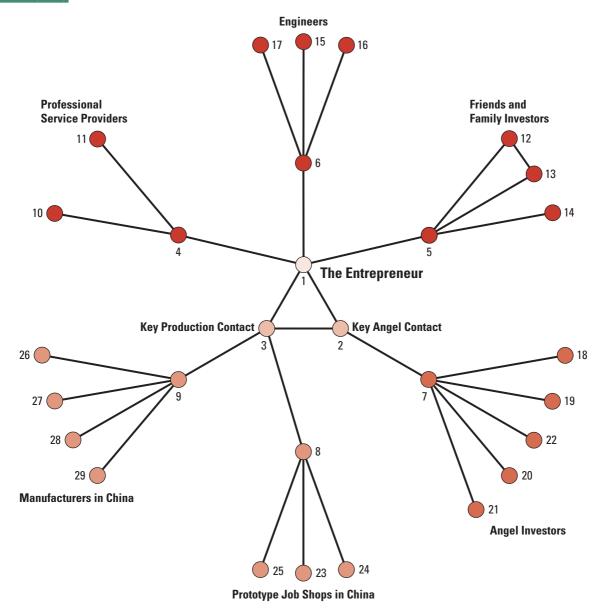
One very specific task that an aspiring entrepreneur can undertake to prepare for success is to find a mentor—that is, someone who is leading the type of life that you envision for your future and who can be your guide and sounding board as well as champion and gateway to people you would otherwise not have been able to meet. Vivek, an Indian entrepreneur, discovered that he had become so passionate about the product side of his computer hardware business that he had stopped listening to the good advice he was being given about the need to diversify his product line. It was not until his business was facing failure, something that is viewed very negatively in India, that he sought the guidance and wisdom of a *guruji* or mentor. The mentor helped Vivek understand that it was his own ego that was standing in the way of his success in finding the right path for his business.¹²

2.4b Build a Professional Network

Networking is the exchange of information and resources among individuals, groups, or organizations whose common goals are to mutually benefit and create value for the members. Entrepreneurs do not act autonomously but, rather, are part of social networks with which they interact.¹³ These social networks consist of strong and weak ties. *Strong ties* are your close friends and family members whom you know well whereas *weak ties* are your acquaintances and business contacts. These weak ties play an important role in the entrepreneurial process because entrepreneurs typically move forward faster with the help and support of weak ties who are not biased by a prior history with the entrepreneur. That is why entrepreneurs rely on their weak ties for objective advice.

Building a large network with credible partners and maintaining the connections in that network will be important to your success. However, how do you achieve a large but meaningful network? You accomplish this by connecting with network brokers who serve as gateways to other networks. These brokers, or opinion leaders, exert influence between groups or networks. Figure 2.2 depicts such

FIGURE 2.2 Brokering across Networks



brokering. The entrepreneur in this example initially has a network of family and friends as well as a network of professional engineers. Outside of these networks, the entrepreneur knows only two people: an angel investor and a production person. However, these two people are well connected into communities with which the entrepreneur has no experience. In effect, they are opinion leaders who serve as the gateways to those new communities and can make the appropriate introductions to provide the entrepreneur with instant credibility. Now it's easy to see why the adage "it's who you know" makes sense. Rather than spending an extraordinary amount of time trying to find all the required contacts, it would be more efficient and prudent for you to figure out who is the gateway to your community of interest and endeavor to meet and cultivate that relationship.

Networking is discussed in the context of building a startup team in Chapter 8.

2.4c Learn About Entrepreneurs

One of the best ways to prepare for entrepreneurship is to learn as much about it as possible by reading magazine articles, books, blogs, and newspapers, and—most importantly—by talking to entrepreneurs. University entrepreneur programs, local chambers of commerce, small business development corporations, and industry events are also great sources for meeting entrepreneurs.

2.4d Understand Personality and Business Preferences

Although we have dispelled many of the myths surrounding entrepreneurship in this chapter, it is a fact that there are barriers to becoming an entrepreneur that should not be ignored, and many of these barriers relate to the entrepreneur's personality and preferences—likes and dislikes. Research has uncovered six factors that serve as barriers to people becoming self-employed as entrepreneurs: (1) lack of confidence, (2) financial needs, (3) startup logistics, (4) personal or family issues, (5) time constraints, and (6) lack of skills.¹⁵ The questions in Table 2.2 reflect these factors and others that should be considered as well. They will help you understand more about what you like and dislike about business. The questions are posed as a definitive yes/no choice to force you to think about these questions independent of any particular opportunity being considered.

Launching a new business requires tremendous amounts of time and energy, as well as a great deal of support from family and friends. During the early stages of a new venture, resources are limited and you must wear many hats. This can be immensely stressful, so it is important that you be in good health and opti-

TABLE 2.2

Entrepreneur Personality and Preferences Questionnaire

1. Are you a self-starter?

2. Are you able to work for up to a year with no income from the new business?

3. Do you stick with a project until it's finished?

4. Do you frequently abandon a project when you grow tired of it?

- 5. Do you enjoy working with other people on a regular basis?
- 6. Do you enjoy traveling for business purposes?
- 7. Are you comfortable with pressure (i.e., deadlines, fast-paced work environment)?
- 8. Do you enjoy working with people from other countries?
- 9. Are you comfortable hiring people you believe are smarter or more experienced than you are?
- 10. Do you enjoy being in an office at your desk for most of the day?
- 11. Are you comfortable in selling situations?
- 12. Are you comfortable asking for money or other resources?
- 13. Are you comfortable with debt?
- 14. Is security important to you?
- 15. Do you have time to devote to this new business?
- 16. Are you comfortable with unions?
- 17. Are you willing to work in a government-regulated environment?
- 18. Do you have the support of your family to start a business?

ИП

YES

mal physical and emotional condition. It is often said that entrepreneurs start businesses to be in charge of their lives. The reality is that after you start your own business, you might find yourself working more than you ever did for someone else. The major difference is that because you are building something you own, it doesn't feel like the work you are accustomed to; instead, you are bringing to life a new business that reflects *your* goals and values.

Here are two additional things to consider:

- ➤ What kind of lifestyle are you striving to achieve? Not all businesses support the kind of lifestyle that some entrepreneurs want to lead. Is travel important? Is having a large home and all the things that go with it a requirement? Is achieving a balanced life with plenty of time for family and friends important? If so, starting a business that requires a lot of travel or puts you at the mercy of demanding clients probably won't provide that balanced lifestyle.
- ➤ How important is your work environment? Entrepreneurs who love the outdoors should probably not start businesses that require them to sit at a desk all day. Entrepreneurs who don't enjoy working with people should probably not start businesses that are labor-intensive or involve numerous daily interactions with the public. It is a good idea for future entrepreneurs to take a step back and contemplate their ideal work environment. What does this environment look like or "feel" like? What would spending a day in this environment entail?

2.4e Improve or Acquire Critical Skills

Because entrepreneurs operate in a world of uncertainty, the ability to analyze a situation, extract the important and ignore the superfluous, compare potential outcomes, and extrapolate from other experiences to the current one is vital. Entrepreneurs also regularly have to weigh options in complex situations.

- ➤ Making Decisions. People who have a difficult time making decisions or who regularly find that they make poor decisions will probably not be successful as entrepreneurs. Making effective decisions is a critical part of the everyday life of an entrepreneur and is a skill that must be developed and exercised carefully.
- **Embracing uncertainty and ambiguity.** Both are essential to creating opportunity and to launching a new business. We live in uncertain times and it's likely that will not change. Entrepreneurs view uncertainty and ambiguity as opportunities to discover a need or problem that no one else has seen.
- ➤ The devil is in the details. Entrepreneurs who proudly claim that they leave the details to others while they focus on the vision are telling the world that they don't participate in the inner workings of their own business. Details matter, and although entrepreneurs should not be micromanagers as the business grows, they should be well aware of the status of critical numbers in their business, and they should make their presence known among employees on a regular basis. Table 2.3 lists some of the skills that you need to hone to be effective at starting and growing your business.

TABLE 2.3

Critical Entrepreneurial Skills

ANALYSIS AND CRITICAL THINKING	WRITTEN AND ORAL COMMUNICATION
Calculated risk taking	Story telling
Embracing uncertainty and ambiguity	Vision
Opportunity creation	Persuasion and negotiation
Organizational and time management (details)	Decision making
Resource gathering	Leadership and people management

- ➤ **Storytelling.** A compelling story about the founding of the business, how the need was identified, and why customers will choose to buy from your company over others will help you raise capital, find strategic partners, and build a board of directors. Entrepreneurs, therefore, must become skilled storytellers, crafting tales about who they are and how their new venture and its resources will benefit customers, investors, and society.
- ➤ Leadership. Today it takes a team to succeed and a leader who can inspire others to motivate and lead as well. Entrepreneurial leadership, like any effective leadership, is a balance of passion and pragmatism. It is the entrepreneur's passion that launches the business and keeps it going through the early days when survival is often in doubt. But a different kind of leadership is often required once the business has survived and has entered growth mode—a more pragmatic style of leadership that can deliver the right systems and controls to keep the venture on course. Sometimes the founding entrepreneur is equipped to take on this type of leadership. Other times, it will be necessary to hand the reins over to someone else. This topic is explored in more depth in Chapter 16.

2.4f Study an Industry

One of the best ways to discover an opportunity is to study an industry in depth, perhaps even work in the industry for a time. An industry is a group of companies that are engaged in a similar or related field; for example, the computer industry consists of all the businesses that provide parts, assembly, manufacturing, and distribution for computers—essentially all of the businesses involved in the value chain for computers. The value chain is discussed in more depth in Chapter 4. The best opportunities come from your experience and knowledge of an industry, a market, or a type of business. Since opportunities are not limited to products and services, studying an industry offers the prospect of identifying opportunity anywhere in the value chain of that industry.

When all is said and done, business is about relationships—with partners, with customers, with investors, and with suppliers. Successfully building relationships requires honesty and integrity. It requires giving value and delivering on promises. Your core values are the foundation for the business and are always reflected in the business and in how customers are treated. Integrity is something that you must guard more carefully than anything else because you cannot afford to taint or lose it. Chapter 3 explores how entrepreneurs cultivate ideas into business opportunities.

CHAPTER

3

CREATING OPPORTUNITY

"The greater danger for most of us lies not in setting our aim too high and falling short; but in setting our aim too low, and achieving our mark."

-MICHELANGELO

CHAPTER OBJECTIVES

- Use design thinking approaches to understand opportunity.
- Understand the nature of creativity and the creativity process.
- Learn how to develop creative skills.
- Experience how to find and frame problems.
- Understand the innovation process and the types of innovation.

deas are a commodity; everyone has them, dozens of them every day. "I think I'll go to a movie." "If I use this screwdriver, I can pry open the lid." "I think I'll take a vacation." We're all idea generators, but what distinguishes entrepreneurs from others who have ideas is that they know how to extract value from those ideas and turn them into opportunities that have commercial potential. Fundamentally, that is the difference between an idea and an **opportunity**. An opportunity can turn into a business.

This chapter uses the principles of **design thinking** to frame a discussion around creativity, opportunity, and innovation. Design thinking is a process and approach that looks at the world from the customer's perspective. It can be thought of as groups of related activities that move from inspiration (creativity) to ideation (opportunity development) to implementation (innovation and commercialization). Moreover, this chapter is organized to address these aspects of design thinking in precisely that order. Figure 3.1 displays these activities as well as the questions associated with them and the types of exercises that help to develop design thinking skills. In its most simplistic definition, design thinking uses techniques and tools to:

- 1. Define a problem
- 2. Create and consider multiple options
- 3. Refine those options through iteration, and
- 4. Settle on a winning solution.

At the heart of design thinking is a deep understanding or **empathy** with what people (customers) want. That level of empathy requires entrepreneurs to embed themselves in the world of the customers they are trying to serve so they can see needs from the customer's perspective.

British anthropologist Jane Goodall is the foremost expert on chimpanzees. How did she achieve that distinction? She embedded herself with a community

FIGURE 3.1

Entrepreneurship and the Elements of Design Thinking

Creativity/ Inspiration

What is true? What if?

Visualization
Mind Mapping
Journey Mapping
Brainstorming
Observation

Opportunity/ Ideation

What is possible?
What problem is being solved?
Are there customers for a solution?

Observation
Understanding/empathy
Problem framing and
solving
Concept development

Innovation/ Implementation

How do we know? How can we test? What sets us apart? Which solution works?

Rapid Prototyping Hypothesis testing Launch to learn

3.

of chimpanzees in Tanzania for 30 years, observing them and gaining their trust. This type of deep understanding or empathy can only happen when you take the time to dig into a problem. Now we are not suggesting that it's necessary to spend years attempting to understand your customer's problem, but your chances of coming up with a great opportunity increase with the amount of time you spend trying to understand the need.

A number of characteristics are associated with design thinkers. Don't be concerned if you don't have all of these characteristics as you can develop them over time.

- **Empathy:** are you able to view the world from many different perspectives and do you notice things that others don't?
- **Integrative thinking:** are you able to recognize all the contradictory options there might be in solving a problem and come up with solutions that greatly improve existing solutions?
- **Optimism:** are you able to assume that there is always a better option than what is currently available and do you have the persistence to go after it?
- **Experimentation:** are you willing to iterate on ideas hundreds of times in search of the best solution?
- **Collaboration:** are you an interdisciplinary thinker and are you knowledgeable in more than one field, for example, engineering and anthropology? Can you work with others to achieve a goal?

Let's look at the components of the design thinking process in more detail to see how they are used to turn an idea into an opportunity.

CREATIVITY AND INSPIRATION

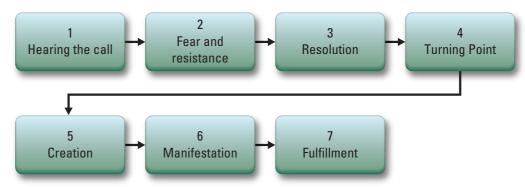
What does creativity have to do with entrepreneurship? Everything! **Creativity**, the ability to use your imagination to come up with original ideas, enables entrepreneurs to differentiate their businesses from competitors so that customers will notice them. Creativity is the basis for invention, which is discovering something that did not exist previously, and innovation, which is finding a new way to do something or improving on an existing product or service. Creativity is also fundamental to problem-solving.

The creative process is difficult to study because it generally deals with a person's internal thought processes, which are often not apparent even to the person being studied. One of the earliest descriptions of the creative process came from Wallas, who had studied famous artists and scientists and from that identified four stages in the creative process:

- 1. Preparation: looking at a problem from a variety of perspectives;
- 2. Incubation: letting the problem lie in the subconscious for a time;
- 3. Illumination: the discovery of a solution; and
- 4. Verification: bringing the idea to an outcome¹

FIGURE 3.2

The Seven Stages of the Creative Process



Source: Adapted from Norman Seeff Productions.

A more recent and very insightful view of the creative process comes from photographer and documentary film producer Norman Seeff, who identified seven stages that individuals or teams go through as they move from the beginnings of an idea to the fulfillment or final outcome (see Figure 3.2).²

Stage One

Stage One is the honeymoon phase. The new idea is born and it brings with it all the possibilities for what it can become. The idea is usually an "aha" moment; in other words, the idea suddenly appears as if out of nowhere.

Stage Two

The possibility stage is often followed by Stage Two, fear and resistance, which normally arises from an individual's previous experience with failure. It is common for people who have experienced failure—and who haven't—to consider what might go wrong this time.

Stage Three

Stage Three is reached when an individual has reconciled the major fears associated with the idea and has addressed enough of the unknowns to feel comfortable moving forward.

Stage Four

Stage Four, the turning point, is when the individual or team either makes the commitment to move forward despite not having all the answers or gives up on the dream.

Stage Five

Stage Five represents the implementation of the action plan to turn the idea into reality.

Stage Six

Stage Six is the outcome of the creative effort in the form of a new product, a new business, or whatever outcome has been defined.

Stage Seven

Seeff's process also has a Stage Seven, which represents the emotional fulfillment of the original dream at Stage One. If Seeff's process is overlaid on the entrepreneurial process of identifying an opportunity and starting a business, typically a team effort, it is clear that Stage Seven is a demonstration of the full emotional commitment of the team to each other as individuals and to the new venture as a whole.

Seeff believes that emotional commitment is essential to the successful completion of a creative endeavor because the creative process is fraught with many challenges that must be overcome before the dream can be realized. This belief that emotions are a key part of the act of creation was born out in his experience with teams at the Jet Propulsion Laboratory in Pasadena, California, working on the Mars Rover project. After two spectacular failures in 1999, the demoralized Mars Polar Lander team was faced with creating a new solution in time for the next window of opportunity in 2004. In interviewing the team, Norman Seeff realized that if he could tap into the team's emotions, he might figure out why the 2004 mission was a success despite all odds against it. What Seeff ultimately discovered was that for the duration of the project, the team became a family who believed in each other as much as they believed they could achieve the mission. In an "aha" moment, they were inspired to use the successful parts of the previous failed missions to innovate a new vehicle and means for safely landing on the surface of Mars.

3.1a Challenges to Creativity

Creativity tends to occur naturally if one lets it, but entrepreneurs often unintentionally erect roadblocks that prevent them from following the creative path. These roadblocks are generally of two main types: environmental and personal.

Environmental Challenges

Entrepreneurs are often so busy that there is little time to pause and reflect on what they need to do to exercise their creative skills. Today we are all bombarded by a constant stream of information pushed to us by our mobile devices. Some research has found that we are actually less productive today than we used to be. One of the biggest contributors to lowered productivity is multitasking. A study published in the *Proceedings of the National Academy of Sciences* surveyed 262 students about their media consumption habits. They then took the 19 students who multitasked the most and the 22 who multitasked the least and conducted additional tests. The findings revealed that in every test, those who spent the least amount of time simultaneously e-mailing, texting, talking on the phone, and surfing the Internet performed substantially better than those who spent the most amount of time doing such activities.³

These findings make sense when you consider that the subconscious is the part of the brain responsible for discovery. If the thinking parts of the brain (left and right hemispheres) are constantly active, the subconscious is unable to supply the creative power it was designed for. Entrepreneurs need to set aside some time each day to let their brains free-associate or perhaps to do something creative that is unrelated to work. The simple act of turning off the e-mail notification button

or turning off the smartphone can cut down on distractions and open the door to new ideas.

Personal Challenges

Design a creative environment

"Confidence is the expectation of success." Those who expect to be successful generally are willing to exert the effort, spend the time, and expend the money to achieve it. The need for ideas to be acceptable or seem rational to others is a significant roadblock for some entrepreneurs; however, rationality is not a prerequisite either for innovative ways to seize opportunities or for receiving a patent on an invention. The inventor of patent number 2,608,083 probably thought he was being rational when he invented the Travel Washing Machine, a portable, mobile appliance that is mounted on the wheel of a vehicle and washes the driver's clothes as he or she motors down the road. Unfortunately, the motorist has to jack up the car first to install the device and, for optimum results, cannot travel faster than 25 miles an hour. Ridiculously, irrational inventions notwithstanding, many of the products in use every day—the Internet and the mobile phone, to name two—would not have come about if the people who invented them hadn't had the courage to go against the general thinking of the time. Here are three important actions you can take to increase your confidence as a creative individual.

- 1. Set manageable goals that create small wins when they're achieved.
- 2. Spend time learning everything you can about your new business idea to reduce some of the risk of entrepreneurship and build confidence.
- 3. Learn when to stop improving on an idea or planning a business and start moving into action mode.

Table 3.1 provides an overview of some effective ways to develop creative skills and remove roadblocks.

Minimiza distractions

TABLE 3.1 Developing Creative Skills

Design a creative environment	Ninimize distractions. Spend time in quiet contemplation—make thinking a habit. Pay attention to where you are when you feel creative. Move out of your comfort zone to try new things.
Log ideas	Maintain a journal of thoughts and ideas. Go back to your journal periodically for inspiration.
Put the familiar in a new context	Look for opportunity in the places you frequent. Pick a product and come up with new application for it. Identify a negative event (i.e., economic downturn) and brainstorm why it may be a positive.
Take advantage of your personal network	Who in your network can connect you with people doing very different things from what you're doing? Do you have a diverse network of people who can connect you to new communities of people? Entrepreneurs need networks for every aspect of their businesses.
Visualize something	Try visualizing what the world might look like in 50 years based on what you know today but not limiting what is possible. Visualize where a technology like mobile phone or social networking is going and what that might look like in the future.

3.1b Tools for Creativity and Inspiration

When you generate new ideas, it's important that you not limit yourself or criticize the ideas too soon. The reason is that either praising or criticizing an idea at this point might shut off the flow of additional ideas or confine the direction of thought too early in the process. Instead, apply these three rules of thumb:

- If you're in a group, start by generating ideas individually first.
- Initially, go for quantity of ideas over quality of ideas.
- **>** Capture every idea no matter how outlandish it may seem on the surface.
- Piggyback on ideas by taking several ideas and creating new combinations and modifications, but do this only after first generating ideas at the individual level.

When you start by generating ideas individually, the number and quality of ideas improve and it's easier to determine which ideas are the best.⁵ Why not just brainstorm as a group? Because it will result in something called *group think*. All the ideas will start to look very similar to each other. Doing individual brainstorming first produces about three times as many ideas per unit of time and these ideas are generally of much higher quality.⁶

Next, we'll briefly summarize some excellent exercises that you should consider using to get your creative juices flowing and generate great ideas.

Brainwriting

Brainwriting is a form of brainstorming that is often used to make sure that everyone on the team feels comfortable offering up ideas. There are a number of ways the exercise can be accomplished, but essentially, it's about getting ideas down on Post-it® notes and then organizing the ideas and creating themes, followed by putting together ideas that don't normally go together.

One of the common sources of new inventions is the ability to connect things that don't normally go together. Leonardo da Vinci saw a connection between the branches of trees and the potential for a canal system in the city of Florence, Italy. He verbalized this connection as a metaphor: *canals are tree branches*. Nature has often served as the metaphor for an invention, including Velcro®, which was inspired by the sticky burr, and the entire field of nanotechnology, which was inspired by plants.

Visualization

Visualization is being able to paint a picture of what you're seeing through graphics and words that also reveal patterns in the masses of ideas you generate. Mindmapping is one effective way to visually lay out numerous ideas and begin to organize them. If you search the Internet, you will find free software tools to help you do mindmapping. However, paper and pen work just as well. Start with a central idea and then branch out with derivative ideas.

Journey Mapping

Journey mapping is also an excellent way to understand customers' current experiences with a problem and existing solutions. Figure 3.3 presents an example of a simple journey map for a generic consumer product that depicts all of the touch