

# CHAPTER 1

## What Is a Startup?

**T**he word *startup* has become an increasing part of the popular lexicon in the past few years. While it has been around for a while, it has recently become ubiquitous for those discussing entrepreneurship and new company creation. But not all new companies are startups.

There is a big difference between two types of entrepreneurial endeavors: (1) local businesses, also called SMEs (small- and medium-sized enterprises) or lifestyle businesses; and (2) high-growth companies, often referred to as *startups* or *gazelles*,<sup>1</sup> a term first used by David Birch in 1979 and refined in 1994 to refer to companies with a minimum of \$1 million of revenue that were at least doubling in size every four years.

Local businesses are what they sound like. These are the businesses that you find in your city whose customers are close to the business, such as the corner grocery, local bookstore, nonchain restaurant, or locally owned gas station. Occasionally these local businesses start to expand and turn into multigeography businesses, resulting in a large enterprise, but many are local businesses for the duration of their existence.

In contrast, high-growth companies rarely have a local focus. While they are often started in one location, and, at inception, usually only have a few people involved, the founders of these companies aspire to grow quickly, independent of geographic boundaries. Their customers are all over the world, and regardless of whether the company ever expands geographically, the business is rarely constrained by geography.

In the United States, until recently, all startups were referred to as small businesses. This is a historical artifact of the U.S. Small

Business Administration, commonly referred to as the SBA. Until 2010, the U.S. government didn't differentiate between types of entrepreneurial businesses. Thus, the SBA was helpful to some companies but useless to many others, especially the high-growth ones. Government at all levels (federal, state, and local) didn't understand the potential impact of startups as a separate class of company, so all small businesses were lumped together.

In 2010, President Barack Obama announced Startup America<sup>2</sup> and thus the word *startup* catapulted to the forefront of everyone's mind. Through the support of the Case Foundation and the Kauffman Foundation, the Startup America Partnership was launched. This was a private partnership that executed a three-year plan, chaired by Steve Case (the founder of AOL) and led by Scott Case (unrelated to Steve), to define, support, and spread the message of startups throughout the United States.

Today, a startup is recognized as something distinct from a small business. For the definition of startup, we turn to the czar of customer development and grandfather of the Lean Startup movement, Steve Blank, who has coined what we think is the best definition for the term: A startup is a temporary organization formed to search for a repeatable and scalable business model.<sup>3</sup>

Let's break down Steve's definition and explore the different parts:

*A temporary organization:* A startup does not last as a startup. It either goes out of business or succeeds in finding a solution that customers are willing to pay for.

*To search:* The goal of a startup is to explore, test, and validate an unmet need. This definition recognizes that the startup lifecycle is finite.

*Repeatable and scalable business model:* Initially, all startups are based on assumptions, with the goal of iterating until the assumptions have been validated. Once the business model has been proven and the startup is self-sustainable, it is no longer a startup.

Steve says this in another delightful way: "A startup is not a smaller version of a large company."<sup>4</sup> Instead, a startup is a series of experiments in search of a scalable business.

## How to Use This Book

Our goal with this book is to help you figure out in advance which ideas are worth experimenting with. While this book is intended to be read from beginning to end, we have organized it so that you can read each chapter independently. We want to provide you with a structure to evaluate the idea you have in a formal and comprehensive way while allowing you to quickly think about the key issues that will come up.

We aren't trying to create a new methodology for starting a company, nor are we trying to replace approaches like Lean Startup. Instead, we are taking a step back and engaging earlier in the process. This book is intended to be read before you read *The Lean Startup* or participate in a Lean LaunchPad process. We'll provide plenty of context around different approaches and resources for getting your business off the ground, but our primary focus is in helping you with the prestartup, or the opportunity evaluation phase, when you are still deciding whether to put energy into the startup.

In addition to our perspectives, we've included examples from entrepreneurs and the investors who funded them at very early stages. Many of the examples are of companies that have grown substantially. By going back to a point in time near their inception, you can get a sense of how and why the entrepreneur and the investor decided to pursue the opportunity. Other sidebars include expert analysis from practitioners or academics of some of the more important elements in the opportunity evaluation process.

Our primary professional focus is in investing in high-growth startups. Brad's experience, through Techstars and Foundry Group, is primarily in high-tech companies. Sean's experience, through *Dragons' Den* (Canada's version of *Shark Tank*) and his own investing, is primarily in consumer products. To make this book applicable for anyone interested in starting a company, we've used examples from each of these domains.

## Who This Book Is For

We wrote this book with first-time entrepreneurs in mind. However, we have received feedback from experienced entrepreneurs that this book has been helpful to them while thinking through their next opportunity.

As entrepreneurship engages a wider range of younger people in our society, we see a dramatic increase in entrepreneurial activities from high school and college students. This book is aimed at them and is intended to be used as a part of an entrepreneurship curriculum.

This book is for educators, particularly those teaching entrepreneurship and opportunity recognition and evaluation courses. If you are a teacher whose students often ask, “How do I know if my idea is worth pursuing?” then this book is for you.

This book is also for friends and family who support the entrepreneur on her complicated and challenging journey. If you are an entrepreneur, you can use it as a source of dialogue with your spouse, your siblings, your parents, and your children.<sup>5</sup>

This book is for fans of *Dragons’ Den* and *Shark Tank*. If you have wondered how the judges choose which companies to fund, you’ll enjoy this book.

This book is also for investors, especially angel and early-stage investors, as they try to better understand a new business. In the same way that the entrepreneur can use this book to help shape an opportunity, an investor can also use these concepts to help evaluate an opportunity.

Most of all, the book is for all those who have a passion for entrepreneurship, especially those of you who know that only the very best opportunities deserve your blood, sweat, and tears. Ideas may be worthless, but your time, energy, and focus are not. Friends only let friends work on great opportunities.

## Notes

1. John Case, “The Gazelle Theory,” *Inc.*, May 15, 2001, <http://www.inc.com/magazine/20010515/22613.html>.
2. The White House’s Startup America homepage, <https://obamawhitehouse.archives.gov/economy/business/startup-america>.
3. Steve Blank, “What’s a Startup? First Principles,” Steve Blank’s blog, January 25, 2010, <http://steveblank.com/2010/01/25/whats-a-startup-first-principles/>.
4. Steve Blank, “A Startup Is Not a Smaller Version of a Large Company,” Steve Blank’s blog, January 25, 2010, <https://steveblank.com/2010/01/14/a-startup-is-not-a-smaller-version-of-a-large-company/>.
5. Don’t forget your pets, especially if you have a rubber duck. For more perspective on the value of talking out loud to yourself, see [http://en.wikipedia.org/wiki/Rubber\\_duck\\_debuggin](http://en.wikipedia.org/wiki/Rubber_duck_debuggin).