

1

Understanding the Entrepreneurial Process

“Monopoly is the condition of every successful business.”

Peter Thiel, Entrepreneur, investor co-founder PayPal

OBJECTIVES

- Place entrepreneurship in today’s context.
- Understand what differentiates an entrepreneur from others.
- Classify different types of entrepreneurs.
- Explore what control means to you and the choices it affects.
- Understand your strengths and limitations.
- Understand the spider-web model for small companies.
- Learn how to network and use mentors.
- Learn how to contain stress.
- Describe the five stages in the entrepreneurial process from opportunity analysis to scaling the venture.
- Learn the key growth issues for an entrepreneur.

CHAPTER OUTLINE

Introduction

Profile: Wayne McVicker—A Typical Entrepreneur

An Entrepreneurial Perspective

Commonly Shared Entrepreneurial Characteristics

Types of Entrepreneurs

The Need to Control

The Spider-Web Model

Finding Early Mentors

Managing Stress

The Five-Stage Entrepreneurial Process

The Growth of Entrepreneurial Companies

So Why Become an Entrepreneur?

Developing Your Entrepreneurial Management Skills

Summary

Study Questions

Endnotes

Worksheets

Introduction

No sector of the economy is as vital, dynamic, and creative as entrepreneurship. For the past thirty years, the impact of entrepreneurs and small-business owners in the creation of new ventures has been felt in virtually all the world's mature as well as developing economies. The startling growth of entrepreneurial ventures forms the heart of our changing economic system as more employees work for these owners than for any other sector of the economy. In the United States today, the number of employees in small and entrepreneurial ventures is growing faster than in any other sector of the labor force, and there is no sign of a reversal in this trend. The Global Entrepreneurship Monitor states that as much as one-third of the differences in economic growth among nations may be due to differences in entrepreneurial activity. A key factor affecting the U.S. economy is the annual creation of 600,000 to 800,000 new companies, which produces many new jobs.¹ Entrepreneurship—the process of planning, organizing, operating, and assuming the risk of a business venture—is now a mainstream activity. Starting a business is never easy; it requires a special blend of courage, self-confidence, and skills—all of which determine the success or failure of an enterprise. The Internet has fundamentally changed the way entrepreneurs can flourish. It not only provides up-to-date market and technology information but also offers many useful support networks to entrepreneurs. Business schools everywhere *teach* the fundamentals of entrepreneurship, which were not even part of the curriculum until the 1990s.^{2,3}

Throughout this text, you'll read about entrepreneurs from many types of businesses. Their stories will help you explore possible paths for building your own successful career. You'll also have the opportunity to assess your present career profile and strategy and contrast them with the approaches these entrepreneurs have developed. The career choices and paths you take are deeply embedded not only in relationships but also in individual characteristics and valued outcomes. The path you follow will be based on a collected set of skills, knowledge, abilities, and experiences, as well as the recognition of unique opportunities. At the end of this chapter, we lay out the five-stage roadmap that every entrepreneurial start-up must navigate before success is achieved. Often, it is difficult to even see the road, let alone know where you are. But keeping the roadmap in mind will help you in your decision making along the way.

Profile: Wayne McVicker⁴—A Typical Entrepreneur

Wayne McVicker, originally trained as an architect, first had the idea of starting a company while working for Varian Corporation in California. The idea to create a new and transparent way to market complex medical equipment did not get much support within Varian, so together with another employee, Jeff Kleck, he started Neoforma. (Interestingly, more than 60 percent of ideas for start-ups come when working for someone else!) They did this with full knowledge of their employer. At first McVicker worked out of his home, while still full time at Varian, but eventually he untied the knot. Using loans from family members, his home equity, and retirement and college funds, he started building the company. He was fortunate to meet Jack Russo, a local attorney who took Wayne and his partner under his wing. Jack gave them a little money and introduced them to some local successful entrepreneurs who eventually invested in Neoforma. The company grew rapidly, continually putting Wayne and Jeff under stress to find money, people, and advisors. They made a number of common mistakes, including wrong hires, chasing fruitless initiatives, not delegating tasks, and gradually losing control of their company as venture capitalists and new managers entered the picture. Despite these trials and tribulations, the passion that Wayne and Jeff had to make health care better carried the company through to a public sale of stock and an eventual purchase by a group of large health-care companies. After a short breather to get over the years of intense activity and stress, the founding partners started another company, Attainia, to do an even better job at opening up the health-care market. Using the lessons learned from Neoforma, they were better equipped to avoid most of the start-up traps. Recently, Jeff and Wayne have handed over the management of Attainia to Jack McGovern and are exploring new start-up opportunities.

“As professors of entrepreneurship, we are often asked if it is possible to ‘teach’ someone to be an entrepreneur. My response is that you can’t teach someone to acquire the drive, the hunger, the passion, and the tenacity to pursue an entrepreneurial path. However, give me someone who has such ‘fire in their belly’ and we can help them to develop critical entrepreneurial skills which will guide them along their journey.”

Alex Denoble
Professor of
Management and
Director of Academic
Entrepreneurship
Program, San Diego
State University
Entrepreneurial
Management Center

An Entrepreneurial Perspective

The word *entrepreneur* came into English use in the seventeenth century from the French word *entreprendre*, which refers to individuals who “undertook” the risk of new enterprise. Early entrepreneurs were also “contractors” who bore the risks of profit or loss, and many were soldiers of fortune, adventurers, builders, and merchants.⁵ Early references to the *entrepreneur* spoke of tax contractors—individuals who paid a fixed sum of money to a government for the license to collect taxes in their region. Tax entrepreneurs bore the risk of collecting individual taxes. If they collected more than the sum paid for their licenses, they made a profit; if not, they lost money.

Today the definition of *entrepreneurship* includes more than the mere creation of a business; it also includes the generation and implementation of an idea. Understanding this team concept is critical if you wish to be a successful entrepreneur. The idea of a sole individual being able to take on enormous risks, attempt innovations, leap without the appropriate background research, and succeed by working long hours and persevering at all costs is no longer relevant in today’s global economy. Entrepreneurs also communicate effectively not only to their teams but also to external “stakeholders” such as investors, bankers, and corporate partners, who are necessary components of their growth path.

Commonly Shared Entrepreneurial Characteristics

Entrepreneurs share a number of characteristics.⁶ Often these seem to be paradoxical or even mutually exclusive, which highlights their first key attribute:

- They have the ability to deal with ambiguity. They are comfortable with making decisions based on apparently conflicting and incomplete information. They do not need to nail

down every detail, yet they can apply analytical skills when appropriate and necessary. They are also comfortable in complex situations; indeed, they can spot opportunities from what may seem to others a chaotic environment, often using an innate intuitiveness to extract patterns not obvious to competitors. Operating in fuzzy-edged gray areas is natural to them.

- They are self-starters, optimists, perseverant, energetic, and action-oriented.⁷ What to others may seem a fatal blow is an opportunity for entrepreneurs to learn, pick themselves up, and see a new opportunity. Threats are turned into great new ideas.
- They are persuasive leaders, people-oriented, natural networkers, and communicators. Habitual entrepreneurs involve many people—both inside and outside the organization—in their pursuit of an opportunity. They create and sustain networks of relationships rather than going it alone, making the most of the intellectual and other resources people have to offer, all the while helping those people to achieve their goals as well. They lead by example rather than dictating.
- They are often creative and highly imaginative.
- They passionately seek new opportunities and are always looking for the chance to profit from change and disruption in the way business is done.
- They tolerate risk, but great entrepreneurs temper risk with reality.
- They work with urgency but balance this with a focus on long-term goals, too.
- They focus on execution—specifically, adaptive execution. People with an entrepreneurial mind-set *execute*; that is, they move forward instead of analyzing new ideas to death.
- They are open to change and do not hang on to old plans when they are not working. But they pursue only the very best opportunities and avoid exhausting themselves and their organizations by chasing every option. Even though many habitual entrepreneurs are wealthy, the most successful remain ruthlessly disciplined about limiting the number of projects they pursue.

These skills clearly conflict with the old idea of an entrepreneur being a loner coming up with new, out-of-context inventions in the basement without having the personal skills to create a valuable and exciting business.

ROADMAP

IN ACTION

Entrepreneurs possess recognizable skills, many of which are embedded within us all. Understand these to uncover hidden traits, and develop them sufficiently to become a successful entrepreneur.

Many entrepreneurial skills do not apply only to starting a company, but have broader applications to other career paths and, indeed, to the way one deals with many of the personal challenges in one's life. As the world becomes more complex and job security in large organizations is no longer the norm, the ability to create and successfully build your own opportunities is vital. Therefore, even if you do not decide to start your own company (at least not yet), the lessons learned throughout this book will help you in whatever you do.

Types of Entrepreneurs

Until recently, people tended to think of the world of work in distinct categories. Most people worked either in someone else's business or in their own. The distinction between being an employee and being an entrepreneur was clear.

The rapid changes in the economy over the past two decades have blurred the lines between traditional employment and entrepreneurship. What counts now are portable skills and knowledge, meaningful work, on-the-job learning, and the ability to build effective networks and contacts, whether through teams or through the Internet. Many people now follow less predictable and even zigzagging career paths.

The distinction between managing your own operations and working for others has become blurred. Owning your own business may be a lifetime pursuit or just one part of your career.⁸ Some people, called *serial entrepreneurs*, start, grow, and sell several businesses over the course of their careers. In any case, to be successful, you must develop the appropriate skill sets, strategic plans, and management team to enhance your possibilities of survival.

There are several different approaches to identifying entrepreneurial types. Ray Smilor, in his book *Daring Visionaries*, recognizes three kinds of entrepreneurs: aspiring, lifestyle, and growth entrepreneurs.

1. *Aspiring entrepreneurs* dream of starting a business; they hope for the chance to be their own bosses, but they have not yet made the leap from their current employment into the uncertainty of a start-up.
2. *Lifestyle entrepreneurs* have developed an enterprise that fits their individual circumstances and style of life. Their basic intention is to earn an income for themselves and their families.
3. *Growth entrepreneurs* have both the desire and the ability to grow as fast and as large as possible. These firms are the most dynamic job generators in the economy.

Within these categories, there are three subtypes that have grown in importance over the last few years. So important, in fact, that we include two “special topic” chapters on the book web site for students who wish to specialize in these areas—Chapter 13, Special Topic: Social Entrepreneurship (available from instructors); Chapter 14, Family Businesses (available from instructors).

Social entrepreneurs are individuals with innovative solutions to society's most social problems. They are ambitious and persistent, tackling major social issues and offering new ideas for wide-scale change. Rather than leaving societal needs to the government or business sectors, social entrepreneurs find what is not working and solve the problem by changing the system, spreading the solution, and persuading entire societies to take new leaps. They often seem to be possessed by their ideas, committing their lives to changing the direction of their field. They are both visionaries and ultimate realists, concerned with the practical implementation of their vision. Social entrepreneurs present ideas that engage communities that have aligned aspirations.

Technology entrepreneurs have ideas triggered by developments in science and engineering. They usually have a strong education in those fields, an advantage that opens up opportunities for them that others might not see. Building ventures around new technology requires specialist knowledge in economics, markets, and social science, in addition to the purely business skills that other entrepreneurs master. Technology entrepreneurs must understand where their ideas fit into a complex environment, and learn that the best technical solutions do not always end up as the leader in the marketplace. *Family-owned businesses* comprise nearly 90 percent of U.S.-based companies and employ over 60 percent of the workforce. Such companies have unique management and governance issues, and these are explored fully in Chapter 14 (available from instructors).

One of the major mistakes entrepreneurs make when starting out is *not* to closely question what they want to be “when they grow up.” Choosing the path of a lifestyle company creates certain advantages and disadvantages that must be carefully considered. If the goal is to employ maybe twenty or thirty people, to create a comfortable lifestyle for yourself and family members, and to retain control of the company, then the lifestyle path is for you. However, this imposes certain limitations on how you can fund the company. This path eliminates the possibility of selling part of the company for cash to pay for growth. A lifestyle company will not provide a way for investors to get a return on their investments through the sale of their ownership positions in the company. Not being honest with yourself at an early stage about control and lifestyle issues will lead to serious and unpleasant conflicts with investors if you take money from them and do not provide them a way to “exit” their investment.

ROADMAP

IN ACTION

The ambitions of entrepreneurs vary widely in scope. Understand your personal aims before embarking on an entrepreneurial journey.

Growth entrepreneurs, on the other hand, are much less driven by control or lifestyle. They recognize that to grow quickly, they will have to sell parts of their companies to raise cash. These investors will apply various levels of control. The aspirations of the founder and the investors are aligned; they both want to build a valuable company and sell it either to an established company or to the public via an initial public offering (IPO). The entrepreneur is willing to trade control for growth and wealth creation.

There is a third route, however—a lifestyle company that manages to grow fairly rapidly without taking in outside investors. These companies are a hybrid between the lifestyle company and the high-growth equity-financed company. We call these “growth bootstrapped” companies. In most cases, entrepreneurs do not plan it this way. They may start off as a lifestyle company and find that they can generate enough interest for their products or services that they can grow using the cash that they generate from sales. Or they may be in a place where there is little or no access to equity funds or their business does not match the industry knowledge and interests of investors.

It is important for you to think carefully as you decide if control and lifestyle are what drive you or if it is growth, visibility, wealth, or perhaps fame that fuels your ambition. Moving between these two different paths is difficult for reasons explored further in Chapter 9.

The Need to Control

The first decision that an entrepreneur should make is whether personal lifestyle and control are more important than growth and eventual wealth creation. If you believe that the idea for a new business is your baby, identify with it, believe you are the best person to grow the opportunity, and cannot conceive of handing the reins over to someone else, then a lifestyle choice is best. On the other hand, if you wish to grow the opportunity into something that is going to change the world and share the responsibility rather than control the venture, then a different set of options are open. Understanding how important control is will affect your willingness to share the management responsibilities and fundamentally impact your financial options.

ROADMAP

IN ACTION

Many problems that occur in entrepreneurial companies can be traced to conflicts over who controls what. Be completely honest with yourself on this issue *before* involving others.

Partners: Many well-known and highly successful companies were started by two or more partners: for example, Jobs/Wozniak at Apple, Hewlett/Packard at HP, Brin/Page at Google, and Allen/Gates at Microsoft. Studying successful companies shows that there is a lower chance of failure when there is more than one founding partner. This is not surprising, as one person is unlikely to have all the experience or personal attributes that are required to meet all the challenges. As we will see in the Neoforma master-case, Wayne and Jeff complement each other in ways that enable them to weather some heavy storms. On the other hand, having a partner who turns out to be incompatible can be fatal to the company.

Additionally, right from the beginning, any value that is created is immediately halved if there are two founders. There is a balance between increased likelihood of success and dividing the eventual wealth or cash flow. You should carefully consider on which side of this divide you feel more comfortable. Worksheets at the end of this chapter and Chapter 9 will help you think through this process. If you feel that sharing the opportunity with a partner is best, you must carefully consider what personal values and ambitions are needed in a partner. Once an outline profile is prepared, the chances of meeting the right partner increase.

Hired Managers: Unfortunately, many companies fail because the founders do not confront their management limitations. It is one thing to have an idea, a passion, and the ability to get to the first sale of a product; it is another to build a strong organization with all the trappings of a larger company—human resources policies, structured training, international cash management, distribution channel development, and so on. The personal attributes of those who create the original idea and have the risk profile and passion to get a company off the ground are usually very different from the skills that are required as the company matures. It is rare indeed to find a first-time entrepreneur who can take it all the way. It is so rare, in fact, that most venture capitalists refuse to invest in companies in which the founder is not open to the idea of stepping aside at the appropriate time. You need to be brutally honest about your own limitations. First-time entrepreneurs have little or no experience and are often too optimistic about their own capabilities. In many cases, they can provide the vision and passion for a new opportunity but soon become overwhelmed as the company begins to take control of them, rather than the other way around. Bringing in new managers with more experience can often be a painful but necessary step; learn when to hand over to others before it is too late.

In the master-case, Wayne and Jeff accept from the very start that they are not the ones to take it all the way and, in fact, work hard to find their replacement. Even so, they have a really hard time handing their baby over to a stranger. There are two issues here: (1) Can you personally accept that it is time to step aside? (2) Can you do this without undermining your replacement? We have seen many companies fail from the inability of the entrepreneur to confront these issues. They take the company down with them still in the captain's cabin.⁹ Certainly, if you are someone wanting to retain control, you should pay careful attention to your abilities to manage growth and seek guidance when the time calls for it.

Financing Options: If control is more important to you than wealth creation through sharing, you will have to limit your financing options to the so-called bootstrapping methods, bank loans, and the emergence of crowd-funding and forgo using true investors to provide funding

for your company. This limitation may well restrict the growth rate of your business but can retain your ability to make all the key decisions, both good and bad. These two fundamentally different financing options are so important that we discuss them in Chapters 8 and 9.

Opportunity Selection: If control of your own company is important to you and you are somewhat risk averse, you would be better off starting with a smaller opportunity. If, on the other hand, you are someone who is comfortable with sharing decisions and ownership, you may follow a more ambitious plan in which you intend to grow your company quickly with the help of one or more partners, outside investors, and advisers.

The Spider-Web Model

The skills needed to run a small company with few resources are completely different from those required in a larger firm. In the early stages, the organization is more like a fragile spider's web, as shown in Figure 1.1; an attack that breaks one or two of the supporting threads could be fatal. An established company is more as a fortress with many specialized and organized troops ready to defend the enterprise, but a start-up has no legal department to deal with lawsuits, no head office to write checks, no cleaning service to clear the drains, and so on. The entrepreneur has to do it all, particularly in the first attempt, with no experience of being a multitasking, always-on-duty spider!

Finding Early Mentors

If the entrepreneur has limited experience and limited internal resources, then help from outside is necessary. Entrepreneurs must learn to be good listeners and find good advisers who can help make difficult decisions. Entrepreneurs need to develop networking skills and uncover and penetrate networks of possible partners, mentors, customers, investors, and others. Of course, the Internet has become a great place to immerse yourself into social networks through such web



FIGURE 1.1
A Fragile Spider's Web

sites as MySpace, Facebook, and LinkedIn. However, the interactions that such virtual media elicit can be rather superficial and lack some important factors required to establish personal business networks. Networks function largely on trust, which takes time to develop and often requires lengthy, face-to-face discourse in a variety of situations. This trust becomes one of your personal assets and can be used to navigate networks through recommendations.

ROADMAP

IN ACTION

Entrepreneurs require good mentors, who are best found through networking. Identify highly connected people, and build trust with them.

There has been a lot of interest over the past few years in trying to understand the dynamics of network growth. Much of this work has been triggered by the Internet, which has fundamentally changed the way interconnectivity operates. The concept of “scale-free networks” has evolved.^{10,11} In order to understand the implications of this concept, consider the following pair of easily recognized maps.

The U.S. interstate roadmap is typical of a network in which connectivity is made only to nearest neighbors. As shown in Figure 1.2, the network can grow incrementally because each link is a link between more or less equal intersections. The airline map is fundamentally different. Although having a similar number of nodes, some, the hubs, have a much higher connectivity than others. If I wanted to meet someone by chance, then standing at any of the interstate intersections would have a nearly equal probability. However, the chances are very different between, say, the airport concourses in Atlanta, Georgia, and College Station, Texas. Networks that are characterized by a few nodes with very high interactivity and many that are not often visited are referred to as scale-free. The Internet is one such network. Certain web addresses, such as Yahoo!, MSN, Google, and Amazon, are hubs; nearly everywhere else is “remote.” Scale-free networks can be very powerful tools for developing new ideas and markets, a topic we will return to in later chapters.

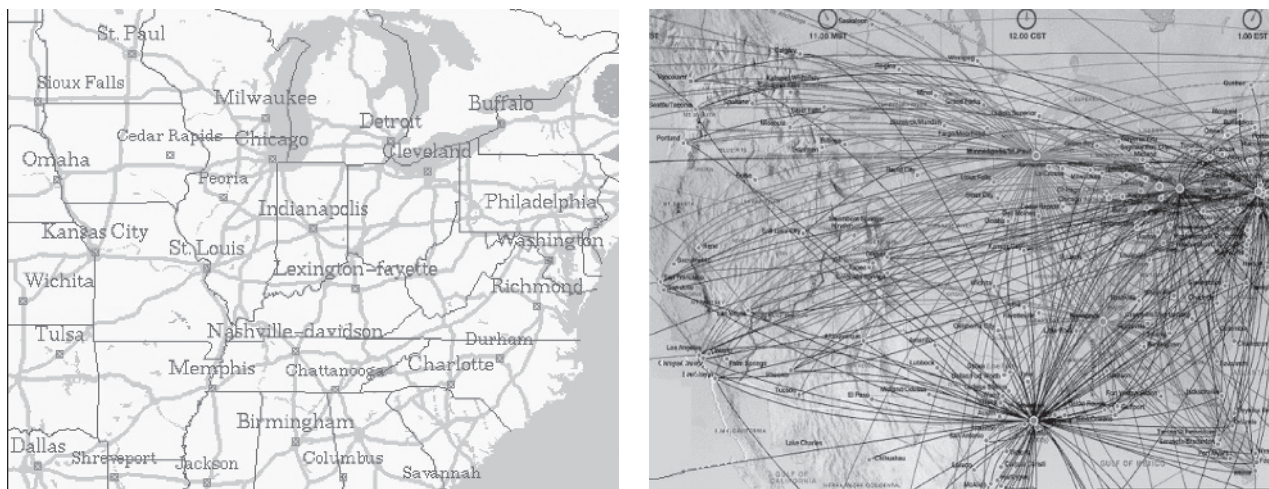


FIGURE 1.2
Comparison of U.S. Road and Airline Networks

Entrepreneurs who wish to access know-how and help can apply these valuable concepts. As you will see in the master-case, Wayne and Jeff used networking extensively when they were getting started. They learned that there are certain people who are “hub-like,” whose business life depends critically on personal connectivity. Professionals such as attorneys, accountants, bankers, salespersons, and venture capitalists all depend on their network to find opportunities. Farmers, teachers, and shop owners do not. Therefore, you should identify the “connectors” in your field and locality and arrange to meet and talk to them about your plans. Start very early because you need time to build trust and respect before they are likely to devote much time to helping you directly or recommending you to their own network. You will be surprised how often people are willing to help you if you are open and honest with them. You should not seek mentors who always agree with you. Make sure you have one or two who challenge your decisions constructively.

Managing Stress

Being a 24/7 entrepreneur running from one broken spider thread to another can easily distract you from making rational decisions. You become emotional rather than practical when choosing your actions. This is not helped by the fact that starting a company is not just a job; it is a passion, a dedication, even a life. The company can easily become all consuming, the only thing you think about, day and night. The swings from ecstasy to despair shown in Figure 1.3 come all too often and unexpectedly. Not surprisingly, therefore, every entrepreneur—without exception—has experienced conflicts between his or her personal life and the company. It is too easy to become so completely engrossed in the venture that you neglect your friends and family, and your own physical and mental health. This is dangerous as you lose balance in your judgments, forget to seek ideas and mental stimulation except within the confines of the company, and allow emotion rather than logic to guide decisions. In the worst case, you bury yourself in an isolated cocoon away from the social comforts that

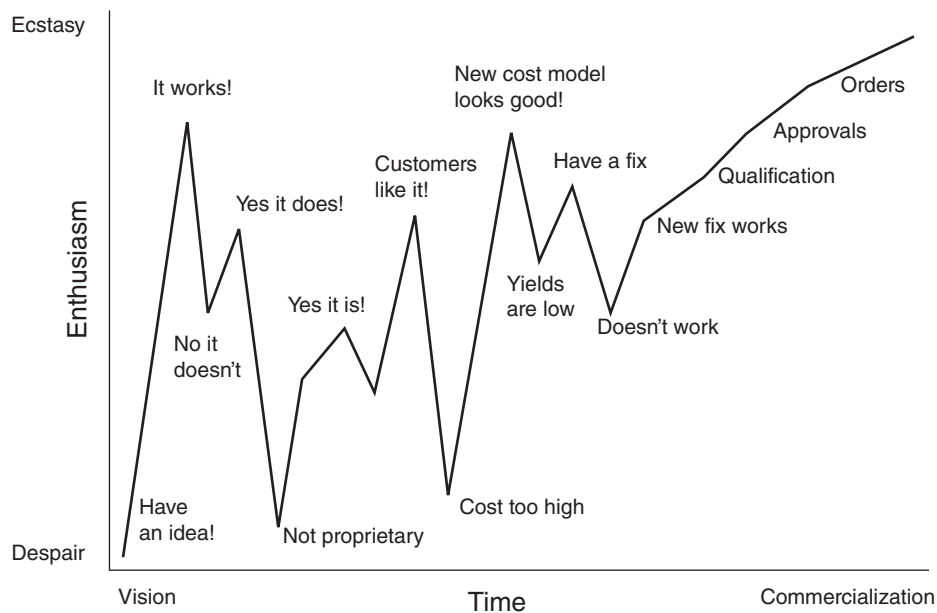


FIGURE 1.3
The Ups and Downs
of a Start-Up

could actually help you through the periods of stress. You need some tools to help you avoid this common trap:

- Before taking action, ask yourself, “How can I work smarter, not harder?”
- Get advice on time-management techniques.
- Plan some personal time with friends and family and stick to them.
- Try to have your workplace at least twenty minutes from home. This seems to be the right time span for you to mentally unlatch yourself from the company.
- Find someone you trust outside the company with whom you can discuss stressful situations to help you tone down emotional content.
- If you have a business partner, work on ways you can help each other through the tough times. Take time to talk before the relationship breaks down.
- Think about your own behavioral patterns and build in some slack time just to think.
- Force yourself to listen to friends and family about their lives; don’t talk about just the company all the time. They may have interesting things to talk about, too.
- Delegate whenever possible, even if you think you are the only person in the world able to do the work.
- Try to see the funny side when things look really bad.

Contact your local chapter of SCORE (www.score.org) to find a retired, experienced executive who will help you on many of these issues for free and plug you into a valuable network. Balancing your personal and business lives is similar to walking a tightrope, and it is very easy to fall off.

An entrepreneurial life is inevitably stressful. Manage the different sources of stress effectively.

The Five-Stage Entrepreneurial Process

Entrepreneurs can increase their chances of success if they understand, follow, and implement the basic five-stage entrepreneurial process described in this section. These five stages, summarized in Figure 1.4, form the backbone of the entrepreneurial process. Each of the key stages includes a main focus activity, discusses tactics for completing tasks, and identifies the estimated amount of time required for each stage. Costs are provided for each activity, which can be used to plan budgets. We will also analyze the risks inherent in each stage and make suggestions for reducing potential problems. Additionally, we have provided assignment worksheets to help you through each stage of your entrepreneurial journey.

Stage 1: Conducting Opportunity Analysis

The basic objective of this stage is to define the criteria that would make a business opportunity worthwhile. In this stage, the founder identifies the opportunity and creates a *vision for the company*. If there is no vision for the venture, the new idea is just a dream. Chapter 2 discusses the role of innovation in the economy and how entrepreneurs can learn to innovate new business concepts, as well as how you screen these business ideas and opportunities. The opportunity has to be embedded in a sustainable business model. All entrepreneurs must create a business model or framework that enables the new company to retain the value of its efforts. Otherwise, they can be quickly eroded by competition such that profits decline. Using a number of stimulating examples, Chapters 3 and 4 illustrate how it is possible to apply innovation to the overall business, not just to new products or services, and how to create a sustainable, highly profitable business that

Stages	Focus Areas	Worksheets
Stage 1 Conducting Opportunity Analysis (Chapters 2, 3, and 4)	<ul style="list-style-type: none"> Innovate and create the vision Identify and evaluate new venture opportunities Develop business modes Conduct customer discovery and secondary market research Develop early product testing 	2.0, 2.1, 2.2, 2.3, 3.0, 3.1, 3.2, 3.3, 3.4, 3.5, 3.6, 4.0, 4.1, 4.2, 4.3, 4.4, 4.5, 4.6, 4.7, 4.8
Stage 2 Developing the Plan and Setting up the Company (Chapters 5, 6, and 7)	<ul style="list-style-type: none"> Establish venture goals and objectives Prepare concise business Select corporate structure and determine other legal requirements Protect your intellectual property 	5.0, 6.0, 7.0
Stage 3 Acquiring Financial Partners and Sources of Funding (Chapters 8 and 9)	<ul style="list-style-type: none"> Ascertain funding requirements and bootstrap early development and operations Secure early-stage funding Prepare for later growth investment options 	8.0, 8.1, 9.0
Stage 4 Determining the Resources Required and Implementing the Plan (Chapter 10)	<ul style="list-style-type: none"> Preparing financial statement for your venture Identify and monitor key performance metrics Hire and manage your venture team Create an innovative culture 	10.0, 10.1, 10.2, 10.3, 10.4
Stage 5 Scaling and Harvesting the Venture (Chapters 11 and 12)	<ul style="list-style-type: none"> Prepare communications for investors and other major stakeholders Develop strategies for scaling the venture Decide best exit strategy for founders 	11.0, 12.0, 12.1

FIGURE 1.4
The Five-Stage Entrepreneurial Process

will retain its value and be an attractive opportunity for investors and, eventually, purchasers. In these chapters, we show how the market research can be used to build value and how information on customers' behaviors can be mined to build barriers to competitors.

We'll also discuss various techniques that are used to evaluate the different categories of opportunities. Specifically, we'll look at the following:

- Evaluating business ideas (determining the idea's value and relevant factors, as discussed in Chapter 2)
- Building the vision, conducting market analysis to sustain a competitive advantage, and learning how to think big (as discussed in Chapters 3 and 4)
- Preparing a competitive analysis is covered in Chapter 4. Here, we describe how to undertake competitive analyses, determine marketing strategies, develop a pricing scheme for your products or services, and use the Internet to identify and engage with customers. This stage usually takes at least a year because it details the pricing and sales strategies required.
- Developing and testing an early product offering, commonly called a minimum viable product (discussed in Chapter 3).

Stage 2: Developing the Plan and Setting Up the Company

In this stage, some ideas are discarded, and strategies are documented and converted to an outlined business plan. The focus at this stage is not on producing a fully-fledged business plan but on documenting the main concepts for the company and the route planned for its growth. Increasingly tools such as the Business Model Canvas in Chapter 3 are being used to convey the key elements of a business plan. A fuller business plan is a vital yet dynamic document for the company; however, rarely does a newly formed company precisely follow its original plan. In addition, any plan must be tailored to the audience for which it is intended. For example, when raising money from investors or banks, one version might be required; when selling the company either to another corporation or to the public, other versions are needed; and, of course, a plan is needed to guide your management team as the company grows. There is a trend toward shorter, more concise business plans that helps when producing versions for specific audiences. Because the business plan is such a vital tool for the entrepreneur, we have devoted a full chapter to just this topic (Chapter 5). Chapter 6 describes how many entrepreneurs dedicate thought and planning to starting their businesses and determining the structures of the companies. Others establish their companies without much regard to how the business should be structured. Regardless of the amount of forethought, one of the most important decisions to make is how to legally structure a business. The legal form of the business proprietorship—C-Corporation, S-Corporation, partnership, or limited liability company (LLC)—should be determined in light of the business's short-term and long-term needs. We'll examine the pros and cons of each of these business structures as well as how to prepare a checklist to start a business.

Don't give up. Don't ever give up. And when things look worst, just don't give up.

Richard Foreman,
*former president and
CEO of Register.com*

For those companies that have a unique technology, or business model, it is important to understand how these can be protected. Chapter 7 explores the value of intellectual property and how to file patents, trademarks, and copyrights to gain a competitive advantage in the marketplace. The chapter provides an explanation of these forms of intellectual property (IP) and guides you toward effectively developing, protecting, and promoting your own IP.

Stage 3: Acquiring Financial Partners/Sources of Funding

Armed with a well-conceived plan, the next challenge is to focus on acquiring funding either through bootstrapping, finding financial investors and partners, or using crowd-funding. In most cases, entrepreneurs may not be aware of the many financing options available that would best meet the needs of the business. Therefore, it is important to know the expectations and requirements of various sources of funds.

Chapter 8 focuses entirely on funding a closely held company in which the founder(s) wishes to remain fully in control of the company. Control restricts the company from certain sources of money, and the entrepreneur must creatively bootstrap the company to keep ownership positions from outsiders. Bootstrapping is a vital skill for all entrepreneurs; therefore, this part is also valuable even if the intention is to seek outside owners by selling equity, or shares, in the company at a later stage. Early-stage funding sources include self-funding, family and friends, angels, banks, and government sources. Each potential source has certain criteria for providing financing, and these criteria are the focus of this stage. To increase the chances of success, we'll specify what sources are available for early-stage funding and discuss the requirements of financial partners. Chapter 9 discusses sources for growth funding. We'll look at using private placements, attracting venture capital, and securing sources of debt financing. The chapter ends with different valuation methods and how much of the company to sell, at what price, and for what percentage of the deal. We'll also explain the risks involved in financing in terms of timing and the emotional stress and patience required.

Stage 4: Determining the Resources Required and Implementing the Plan

Entrepreneurs are asked to plan operations and evaluate decisions using financial accounting information. An understanding of managing financial operations will contribute to the success of the entrepreneurial business. Chapter 10 discusses financial statements; how to analyze these statements; and how to prepare budgets, ratios, and cash flow forecasts. We also describe the importance of identifying and monitoring important performance indicators for new ventures as they relate to revenue growth, customer acquisition, profitability, and funding requirements.

Additionally, Chapter 10 covers the important issues regarding people management. Finding, interviewing, training, incentivizing and managing, and, yes, even firing, are important skills you need to build a culture for success.

Stage 5: Scaling and Harvesting the Venture

Chapter 11 provides you with a vital skill that all entrepreneurs need, namely, how to communicate an opportunity concisely and compellingly to new employees, investors, partners, and customers. An idea has no value unless others understand its potential, become excited about being involved, and are willing to participate enthusiastically in the venture. Here, you will learn about the different forms of communications, including video methods as well as how to prepare for a presentation, and what is expected at each stage of relationship development.

Finally, Chapter 12 highlights the methodology, procedures, and options available for entrepreneurs to scale the venture or consider an exit strategy. We'll discuss how to sell an equity stake to a partner, sell the business, transfer ownership to family members or employees, merge with another company, and implement a leveraged buyout. We'll also discuss planning for a public offering that offers an option to sell a portion of the venture and scale the business for growth. The objective of this chapter is to help entrepreneurs identify the best exit plan and be in a strong position to manage the process.

The Growth of Entrepreneurial Companies

Despite the growing prominence of entrepreneurship, understanding of its key features and development stages lags. Mainstream media coverage frequently emphasizes the most unusual successes, creating misconceptions about the nature and evolution of most successful entrepreneurial firms. In theory, entrepreneurship includes several sub-disciplines, including small businesses, businesses owned by women, high-technology start-ups home-based businesses, family-owned businesses (refer to Chapter 14), and those focused on a social mission. Businesses in these groupings have received the most intensive study.

Relatively little research has been done, however, on the distinctive features of growth companies. This is an important point because in many aspects entrepreneurial companies are indistinguishable from small businesses until they enter a "growth" phase, during which they are transformed into an almost entirely different entity. An entrepreneurial firm is one that grows large enough to influence the environment and, thus, become a pacesetter. Yet we cannot use growth alone to evaluate the real pacesetters, as 86.7 percent of all U.S. businesses employ twenty or fewer people.¹² The past fifteen years have been years of tremendous growth for entrepreneurial companies and for the individuals who make them thrive. During this time, entrepreneurs such as Bill Gates, Andy Grove, Steve Jobs, Meg Whitman, and Jeff Bezos have captured the public imagination and dominated the business news.

The reasons for this trend in entrepreneurship are clear. Each year at least 700,000 new businesses are started in the United States, and of these, a small portion turn out to be the fast-growth companies that propel the economy forward. Each year, this small set of businesses creates a disproportionate share of the new jobs and fuels the economy in numerous ways. Some of the best investment opportunities for the next decade are first innovation: Big Data, artificial intelligence, robotics, cybersecurity, privacy, and genomics. Second is people: aging, silver economy, Gen Z, Gen Y, millennials, education, inequality, everything that has to do with demographics. Third is Earth—everything having to do with our planet: climate change, food security, water, waste, renewable energy, and energy storage. These are the megatrends that will impact our lives.

The Growth Period

Most businesses “start small and stay small.” On the one hand, the business may not offer any productivity improvement and, therefore, may have no significant potential for entrepreneurial growth. On the other hand, even if a business does have growth potential, the business owner may prefer to grow it to only a certain point. As we mentioned earlier, not all entrepreneurs want to grow their businesses. Many entrepreneurs work toward the goal of growing the business to a certain level to provide a relatively steady stream of income and employment. The true challenges for these entrepreneurs and small-business owners are to avoid burnout from the daily operations and keep the entrepreneurial spirit that drove them into business in the first place.¹³

What distinguishes an entrepreneurial company from a small business is the ability of the venture owner to maneuver successfully through the transition stages necessary to handle distinctive periods of growth. In many cases, the growth period comes right from the start and is part of the initial vision for the company. In other cases, the growth period comes later or appears to arrive out of the blue. Each year, a certain number of small businesses make the transition to become entrepreneurial growth companies. One thing these growth companies usually have in common is an entrepreneurial mindset.¹⁴

Entrepreneurship Roller Coaster

Of course, life is not so predictable that you can follow each step in this book without being confronted with surprises, challenges, and disappointments. Indeed, one of the most important attributes of a successful entrepreneur is the ability to keep going under duress. Figure 1.3, adapted from *Commercializing New Technologies* by K. Jolly from an original chart from R. J. Skaldic, shows the ups and downs of a typical start-up from the original vision or idea through to commercial success. The challenge for the entrepreneur is to manage the periods of despair as well as celebrate the ecstatic events. As you follow the Neoforma story, you will be able to clearly identify many “ups and downs.”

ROADMAP

IN ACTION

The entrepreneurial life is unpredictable, challenging, and often stressful. Practice how to handle uncertainty effectively.

So Why Become an Entrepreneur?

With such a roller coaster life, you might ask, “Why undertake such an uncertain journey?” People become entrepreneurs for many reasons. Some people are attracted to the perceived independence and freedom from the politics and restrictions of corporations. Being able to do your own thing, make your own decisions, and exert greater control over your working environment are attractive alternatives to the conformity—real or imagined—associated with life in a big company. Some may hit a plateau, see that they are blocked from further promotions, or recognize that they are not progressing as rapidly as they would like, and these conditions become motivating factors. We even tell our students that they should view being fired not as a negative, but as the trigger to start something exciting. Other people believe that building a company can provide them with opportunities for sustained growth and mobility. For others, starting their own company provides them with the flexibility they seek in their lives. And of course, for many, entrepreneurship offers a vehicle for creating huge financial rewards.

Developing Your Entrepreneurial Management Skills

The failure rate of start-ups is very high. According to Timmons and others,¹⁵ the failure rate of new companies is 24 percent within the first two years and 80–90 percent within the first ten years. However, most companies fail not from focusing on a bad idea or even having insufficient funds; they fail because the founders are confronting complex management decisions without experience or knowledge of the tools to make them. Throughout the book, we include sections on management issues that are aimed at providing you with an understanding of the unique personal challenges that an entrepreneur faces, especially in their first company adventure. You will examine your own strengths and, yes, weaknesses, and learn management skills to deal with the major decisions you will have to make.

Starting a company can be very stressful, with tremendous demands on your time and energy. This can take a toll on your personal life and affect friends and family in ways that are painful. You need to be honest with yourself and those near you so that the appropriate balance between your personal lifestyle and your new company can be struck.

You will be able to consider some of these important attributes and skills by completing Worksheet 1.0 at the end of this chapter.



SUMMARY

The definition of an entrepreneur has evolved over time as the surrounding economic structures have become more complex. Today, *entrepreneurship* is defined as the process of creating something different by devoting the necessary time and effort; assuming the accompanying financial, psychic, and social risks; and receiving the resulting monetary rewards and personal satisfaction. Before embarking on an entrepreneurial journey, you should take some time to reflect on your own attributes, particularly your need to be in control. This will help you identify an opportunity and create a plan of action that is suited to you and increase the likelihood of success. The entrepreneurial process

consists of five stages: (1) conducting opportunity analysis, (2) developing the plan and setting up the company, (3) acquiring financial partners and sources of funding, (4) determining the resources required and implementing the plan, and (5) scaling and harvesting the venture.

The study of entrepreneurship has relevance today not just because it helps entrepreneurs better fulfill their personal needs, but because of the economic function of new ventures. More than increasing national income by creating new jobs, entrepreneurship acts as a positive force in economic growth and social benefits by serving as the bridge between innovation and application.

STUDY QUESTIONS

- Q.1** What are the three types of entrepreneurs? With which do you most identify?
- Q.2** What is the difference between technology and social entrepreneurs?
- Q.3** Describe five common entrepreneurial personal attributes.
- Q.4** If you start a company, will you expect to always be in control, or will you be willing to share control with others if that will help the company grow and make all the participants wealthier? Describe your reasons for your choices.
- Q.5** What is the spider-web model? How does it apply to start-up companies?
- Q.6** What are the five stages of the entrepreneurial process?
- Q.7** What are the growth issues entrepreneurial companies face?

ENDNOTES

- Findings by the Entrepreneurial Research Consortium, a publicly and privately sponsored research effort directed by Dr. Paul Reynolds at Babson College, indicate that seven million adults are trying to start businesses in the United States at any given time. The Global Entrepreneurship Monitor, a joint research initiative by Babson College and the London Business School and sponsored by the Kauffman Center for Entrepreneurial Leadership, was launched in September 1997 to analyze entrepreneurial activity, its impact on national growth, and those factors that affect levels of entrepreneurial activity.
- See Dale Meyer, plenary address at USASHE on February 15, 2001, "Changes in Entrepreneurship Curriculum." Courses in entrepreneurship are now taught at nearly one thousand colleges and universities. Entrepreneurship education programs for youngsters in the K-12 age range now exist in more than thirty states. The YESS!/Mini-Society entrepreneurship curriculum has been accepted by the U.S. Department of Education's National Diffusion Network as being effective in both acquiring knowledge and improving attitudes toward school and learning. In addition, according to the Global Consortium of Entrepreneurship Centers, the number of U.S. universities having such centers has grown from 50 to more than 250 in less than ten years.
- See Marilyn Kourilsky, "Entrepreneurship Education: Opportunity in Search of Curriculum," Kauffman Center for Entrepreneurial Leadership, 1995.
- See Wayne McVicker, *Starting Something* (Palo Alto, CA: Ravel Media, 2005), available in paperback and in digital format.
- For a more complete discussion of the evolution of the term *entrepreneur* and theories of entrepreneurship, see "Theories of Entrepreneurship Historical Development and Critical Assessment" in *The Oxford Handbook of Entrepreneurship*, ed. Mark Casson, Bernard Yeung, Anuradha Basu, and Nigel Wadeson (Oxford: Oxford University Press, 2006), 33–56.
- See Alex F. DeNoble, Doug I. Jung, Sanford B. Ehrlich, and Mark Butler, "A Paper on Entrepreneurial Self-Efficacy: The Development of a Set of Measures and a Preliminary Test of Their Properties," Entrepreneurship Management Center, College of Business Administration, San Diego State University, 1999. Paper submitted on September 23, 2001, at Babson Research Conference.
- See Ray Smilor, *Daring Visionaries* (Holbrook, MA: Adams Media Corporation, 2001), xxiv–xv. Smilor is the president of the Foundation for Enterprise Development and former vice president of the Kauffman Center for Entrepreneurial Leadership.
- A breakdown of types of lifestyle entrepreneurs can be found at the U.S. Department of Commerce, "Statistical Abstract of the United States," Bureau of the Census, Washington, DC, 2008. This report also provides a wealth of data on the state of entrepreneurship in the United States.
- For a discussion of the problems that arise when founders are unable to give up control and hand over the reins to more experienced managers, see Noam Wasserman, "The Founder's Dilemma," *Harvard Business Review* 86, no. 2 (February 2008): 103–109.
- Two introductory books on how social networks can enhance businesses are David Silver, *Smart Start-Ups: How Entrepreneurs and Corporations Can Profit by Starting Online Communities* (Hoboken, NJ: Wiley, 2007); and Larry Weber, *Marketing to the Social Web: How Digital Customer Communities Build Your Business* (Hoboken, NJ: Wiley, 2007).
- An excellent introduction to the changing world of networks can be found in Albert-Laszlo Barabasi, *Linked: How Everything Is Connected to Everything Else and What It Means* (New York: Plume Press, 2003).
- See U.S. Department of Commerce, "Statistical Abstract of the United States," Bureau of the Census, Washington, DC, 2008, for a wealth of data on small firms.
- See William B. Gartner, Barbara J. Bird, and Jennifer A. Starr, "Acting as if: Differentiating entrepreneurial from organizational behavior," *Entrepreneurship Theory and Practice* (Spring 1992): 13–27.
- See Rita McGrath and Ian MacMillan, *The Entrepreneurial Mindset* (Boston: Harvard Business School Press, 2000), 2–3.

15. It is extremely difficult to obtain reliable data on the failure rate of start-ups; see www.businessweek.com/smallbiz/news/coladvice/ask/sa990930.htm. However, a good summary can be found in Jeffrey A. Timmons and Steve Spinelli, *New Venture Creation*, 7th ed. (Princeton, NJ: McGrawHill/Irwin, 2006). For a more

theoretical discourse on small firm failure, see: Robert Cressy, “Determinants of Small Firm Survival and Growth” in *The Oxford Handbook of Entrepreneurship*, ed. Mark Casson, Bernard Yeung, Anuradha Basu, and Nigel Wadeson (Oxford: Oxford University Press, 2006), 162–193.

WORKSHEETS

Worksheet Assignment 1.0: [p. 17]

Assessing Your Entrepreneurial Characteristics. You can use this worksheet to rate and reflect on some of the important characteristics needed to navigate the entrepreneurial journey.

Best Practices

Entrepreneurship is sometimes discussed as the ability to deal with apparent conflicts and find a balance between differing conditions and personal attributes. Here are some examples to consider.

- **Ambiguity—Planning.** Start-up companies are usually exploring new opportunities where data, details, and the environment may be largely unknown. Yet without a plan, managers do not have a basis on which to make decisions. Yet the discipline of a business plan that is required is rarely followed.
- **Creativity—Discipline.** Many, though not all, start-up companies are based on a new idea or an innovative solution to an existing need. However, if everyone is creating new things all the time, then nothing will actually get done.
- **Urgency—Patience.** Entrepreneurs are driven people. Yet real advances take longer than planned—always.
- **Flexibility—Organization.** The need to respond rapidly to changing circumstances, new ideas, opportunities, and threats with limited resources requires a great deal of flexibility and the ability to change direction quickly. But as the start-up grows, it is impossible for the founders to control everything and make all the decisions. An organizational structure must be put in place, which inevitably begins to prevent just the flexibility that is needed for success.
- **Risk Taking—Risk Management.** Entrepreneurs are usually risk takers, yet too much risk does not create a successful organization and certainly may turn away investors.
- **Short Term—Long Term.** Every day presents a new challenge and possible change of direction, yet you must not lose sight of the ultimate goal.

NAME **Your Name**WORKSHEET **1.0 Your Entrepreneurial Behaviors and Skills**INSTRUCTION **Rating Scale: How frequently do you exhibit this behavior/skill? 1 - Rarely to 5 - - - Very Often**

► BEHAVIORS AND SKILLS	RATINGS	ACTIONS TO DEVELOP
1. Desire and Passion: When I start a task, I have the passion and drive to succeed.	1 2 3 4 5	
2. Tenacity: I have the stamina to tackle challenging problems.	1 2 3 4 5	
3. Ability to Thrive on Uncertainty: I prosper in an environment with many questions and few answers.	1 2 3 4 5	
4. Determination and Resiliency: I continue to work on a task during hard times and recover quickly.	1 2 3 4 5	
5. Accountability: I take responsibility for my own success.	1 2 3 4 5	
6. Persuasiveness: I articulate my ideas convincingly to others.	1 2 3 4 5	
7. Self-Discipline: I can do the tasks necessary to succeed, whether pleasant or unpleasant.	1 2 3 4 5	
8. Self-Confidence: I believe that somehow, I can solve whatever problems arise.	1 2 3 4 5	
9. Ethics: I deal with others with honesty and integrity.	1 2 3 4 5	
10. Problem Solving: I anticipate and troubleshoot problems.	1 2 3 4 5	
11. Networking: I make connections with others and build relationships.	1 2 3 4 5	
12. Risk Taking: I pursue ideas, despite risks.	1 2 3 4 5	
13. Innovation: I challenge the status quo in pursuit of new ideas.	1 2 3 4 5	
14. Regulation: I pause without immediately reacting in difficult situations.	1 2 3 4 5	
15. Attention: I am easily distracted when working on a task.	1 2 3 4 5	
16. Focus: I stay focused on what is happening in the present.	1 2 3 4 5	
17. Flexibility: I adapt to challenges and change direction as needed.	1 2 3 4 5	
18. Awareness: I pay attention to how my emotions affect my thoughts and behavior.	1 2 3 4 5	
19. Attentiveness: I rush through activities without being really attentive to them.	1 2 3 4 5	
20. Communication: I listen attentively, focusing on other person fully without distraction.	1 2 3 4 5	

► SUMMARY ACTIONS

- Based on the above ratings, what actions do you plan to take to enhance your entrepreneurial behaviors and skills?
- Start with three areas that you would like to work on and set a timetable to review your progress.

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