Patterns of Entrepreneurship Management

Fifth Edition

JACK M. KAPLAN | ANTHONY C. WARREN

WILEY

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Students past, present, and future who will learn
to change the world for the better

Preface

Working in a corporation, or even a smaller business, does not prepare you for the challenges, long hours, social sacrifices, and financial commitments involved in being an entrepreneur. If you know that your future goal is to become an entrepreneur, how can you truly understand the rewards and pitfalls of this choice? How do you acquire the information and skills needed to support you in realizing your goal? This book provides just that—the necessary information you need to get you started as a successful entrepreneur, even in today's ultracompetitive, hostile, turbulent, and global business environment.

We have had the privilege of teaching entrepreneurship courses for more than fourteen years—Kaplan at Columbia Business School in New York and Warren at Penn State. During this time, students, alumni, investors, small companies, and business colleagues have sought our advice regarding the topic of entrepreneurship. Both of us, being entrepreneurs ourselves, have also had the opportunity to gain extensive experience. Professor Kaplan served as the president of Datamark Technologies, a technology marketing company engaged in loyalty and electronic gift card programs, and Professor Warren was a founder of several companies and was a venture capitalist for a number of years. We also stay active as entrepreneurs, Kaplan having cofounded "Robotics Systems & Technologies, Inc.," a hospital automation company, and Warren, "Halare Inc.," a networked telemedicine company. Thus, not only are we both in touch with the most recent academic research findings and best practices regarding entrepreneurship, but also we have firsthand experience in starting and building companies. We hope to impart our practical knowledge and counsel directly to you through this book and its associated web resources.

Why This New Edition

Patterns of Entrepreneurship Management, Fifth Edition, supports a greatly enhanced interactive learning experience that addresses the challenges, issues, and rewards faced by entrepreneurs in starting and growing a venture. When we were asked to produce a fifth edition by our publisher, we believed that it would be a relatively easy task. As it turned out, the world of entrepreneurship is changing so rapidly that many of the topics in this new edition were not even on the horizon just three years ago. We have seen enormous changes in the investment climate, stunning new applications for social networks, and the evolution of new business models to fit this changing environment. Many of the chapters had to be completely rewritten. Also, in talking to our colleagues at a number of universities, we were asked to address three new special topics in entrepreneurship.

The first is *crowdsourcing*, which has grown enormously since the last edition. We invited Professor Marion Poetz from Copenhagen Business School, an expert in this field, to co-author a chapter on this topic.

Second, family-owned businesses play a major role in most economies. They have unique and challenging management issues. We devote a new chapter on this topic written by Dr. Isabel C. Botero from Stetson University. The Internet has revolutionized sales and marketing strategies for small businesses. Adjunct Professor .Jeremy Kagan from Columbia University has joined us to add content in Chapter 4 on the tools now available in digital marketing. Special thanks to Elizabeth Lott , Columbia EMBA 2014 and entrepreneur for the Tiny Updates, and canvas model example in Chapter 4.

Finally, Dr. Jack McGourty, also from Columbia Business School, has added to the discussions on the canvas model process and structure and the minimum viable product strategy.

In the last edition, we introduced the concept of "special topics in entrepreneurship" to enable teachers to design courses that address unique needs of students who may wish to focus on one type of venture. The first two topics were social and technology-based opportunities. To these we are adding the above-mentioned "family business" chapter. We have placed all three special topic chapters on the book website. The textbook, which covers all required core course materials, has two brand-new chapters—crowdsourcing and digital media marketing. All other chapters have significant revisions to bring them up to date. Still, this edition has kept the popular theme on *managing* a start-up. The authors have spent many years both as entrepreneurs and teachers and passionately believe that entrepreneurial skills can be acquired only by actually confronting the problems that challenge every entrepreneur. This text and accompanying website, therefore, differ from others in that they challenge students with real situations and examples on which they can practice the broad range of skills required to start and build a company in today's complex world. Throughout this book you will find tips on how to become a successful entrepreneur as well as issues to avoid.

The web projects and cases that accompany this book focus on the successes and failures of entrepreneurs and offer valuable business plan examples and assessment tools. Other outstanding features that the book offers are as follows:

1. *Focus on Real Entrepreneurs.* Throughout the text, we relate the material to real entrepreneurs, helping you understand how entrepreneurs position their companies to meet the various marketing, financial, and technological challenges. For example, each chapter starts with a short profile of an entrepreneur that illustrates the key issues that will be covered. These engage students as they immediately see the relevance of the chapter and are intrigued by an actual case chosen for its learning impact.

2. *Management Track.* This *learning track* is embedded in the book. The failure rate of new companies is 24 percent within the first two years and 80–90 percent within the first ten years. Most companies fail not because they are focusing on a bad idea or having insufficient funds, but because inexperienced founders are confronting complex management decisions without knowledge of the tools to make them. The *management track* is based on a real company, Neoforma, which constitutes a *master-case* for the entire book. Wayne McVicker, one of the founders, reported, in a diary form, the entire company history from concept to eventual sale, covering every conceivable management challenge that all entrepreneurs inevitably face. His book, *Starting Something,* became the basis of a new management course at Penn State. Students were so enthralled that we decided to enhance the materials. We took a film crew and interviewed many of the key characters—founders, investors, mentors, key hires, and even family members—who gave their personal views on many of the key management decisions that transpired. McVicker has agreed that we can embed elements of his book with the videos into this edition of *Patterns of Entrepreneurship Management* to provide a rich experience for students on the key management issues in entrepreneurship. We believe this is the first attempt to address important entrepreneurship management topics within a textbook. The materials have now been used with great success at many universities around the world, and we are pleased to incorporate them into this edition to greatly enhance the learning experience. Management topics are revisited in many of the remaining chapters with appropriate student exercises structured around the video materials on the book's website.

3. *Finance Track.* The book contains a complete set of materials covering entrepreneurial finance for non-finance majors. Every entrepreneur at some time needs to raise funds to grow the

company. Many make fatal mistakes early on because they haven't clearly thought through the personal implications imposed by the source of these funds. The issues of control, lifestyle, risk tolerance, and ambition all determine this choice. This book is the first to differentiate funding sources between closely held private businesses and high-growth equity-funded companies, and these are dealt with in two parts of Chapter 8 on financing. Understanding these two mutually exclusive routes for companies can save a lot of heartaches for entrepreneurs and their supporters. Additionally crowdfunding is covered in Chapter 5 and Chapter 9 describes how to manage funds carefully once they have been raised.

4. *Case Studies.* In addition to the master-case based on Neoforma, most chapters include a shorter case study that looks at a potential entrepreneurial opportunity. Answering the case study questions allows you to think critically about the various aspects of launching a business. Several case studies touch on important aspects of business such as setting up the management team, financing for early and growth ventures, and expanding ideas into viable business opportunities. Longer cases appear on the website, which provides additional interactive materials.

5. *From Idea to Opportunity. Patterns of Entrepreneurship Management* is not merely a concept-oriented textbook. Through powerful examples, cases, and exercises, students explore important "soft" issues such as how to continuously innovate, design sustainable business models, and create a culture in their companies that will increase their chances of success as they launch a new enterprise.

6. *Innovation and Technology Venture Framework. Patterns of Entrepreneurship Management* stresses the importance of innovation and technology. Throughout the book are sections devoted to creating a framework for screening ideas, thinking about strategy and business models, determining the capital and resources required, attracting management talent, and preparing the plan to ensure that practices are accepted and implemented effectively.

Organization Of the Book

The book has been designed to support seven different courses in entrepreneurship:

1. *Introduction to Entrepreneurship* teaches the student about the basics of the field, including the personal aspects of entrepreneurs, opportunity identification, and structuring. This course often includes teamwork in which students identify their own business opportunities and work them up into business plans and presentations to investors. For this course, some of the more detailed topics in management and finance can be omitted. Chapters 1–7 contain the core content.

2. *Entrepreneurial Finance* is a subject that is rather different from corporate finance, which is taught in most business schools. Chapters 8 and 9 provide a complete set of materials for such a course, with supporting readings taken from elsewhere in the book, especially Chapter 5's sections on crowdfunding.

3. *Entrepreneurial Management* is based on the master-case and the other management cases in the book. This is an experiential course and is best run in a seminar format.

4. *Business Planning* is covered extensively in Chapters 3, 5, and 6 with supplementary content in other chapters.

5. *Social Entrepreneurship* is supported by most of the chapters in the book but is enhanced greatly by the Special Topics in Chapter 12 on the book's website devoted entirely to this topic. This chapter covers the legal and taxation issues associated with social ventures as

well as the unique classes of business models and management skills that are required for such ventures.

6. *Technology Entrepreneurship* requires extra material to supplement that in the rest of the book. Chapter 13, on the book's website, has been developed from a highly successful course at Penn State designed specifically for scientists and engineers wishing to explore a career as an entrepreneur.
7. *Family Business Management* is covered in Chapter 14. This new addition to the content is found on the book's website.

The book covers three roadmap phases of entrepreneurship. Each chapter has been written to help students learn specific tasks needed to complete it with defined deliverables. A fourth section on the book website contains special topics in entrepreneurship.

Part One, "Getting Started as an Entrepreneur," includes six chapters that establish the foundation for starting a venture, from understanding the personal attributes of an entrepreneur, developing ideas, and recognizing business opportunities to exploring business models, preparing a winning business plan, and setting up the company. The master-case, Neoforma, is also outlined in the first chapter. Chapter 1 introduces the concept of entrepreneurship and emphasizes the entrepreneurial process and the steps to becoming an entrepreneur. Chapter 2 explores the role of innovation and its importance. Students learn techniques to become creative in developing new business ideas by building their own framework for analysis of situations. Chapter 3 is devoted entirely to the study of business models, providing students with frameworks for business model design with illustrative cases. Chapter 4 discusses how to analyze markets and potential customers and how to conduct a competitive analysis and create a marketing plan for the venture. Digital marketing methods are covered in detail. Chapter 5 covers the new field of crowdsourcing which has opened up entirely new ways for entrepreneurs to develop opportunities with limited resources. In Chapter 6, we cover business planning and in particular the new *lean plan* models. Chapter 7 describes the various forms that ventures may take as well as the processes of actually forming a company.

Part Two, "Funding the Venture," constitutes a complete module on entrepreneurial finance. It describes the many ways start-up companies can access the resources they need, including funding at different stages of growth. Chapter 8 has two parts: the first examines the methods entrepreneurs use to raise early-stage funding when their plan is to retain control of the company and make it a "lifestyle" business. These techniques, referred to as *bootstrapping*, are also important for entrepreneurs who later choose to grow a larger organization. Sources include friends, family, government grants, partners, and banks. The second part explains growth-funding sources from angel investors and venture capitalists whereby the entrepreneur sells shares in her company where ultimate wealth may be traded with loss of control. This extensive chapter is supplemented with the first part of Chapter 9, which teaches the fundamental financial management systems that should be installed early on in a company's development.

Part Three, "Building and Exiting," focuses on three functions that must be developed as the company begins to grow. Chapter 9 covers the management of two key resources: money and people. Here students learn the key skills in building and managing a team, including the establishment of a strong culture; finding, hiring, and even firing the right employees; and learning how to manage ambiguous conflicts of interest and ethical dilemmas. This chapter also describes key legal documents that a company will use. Chapter 10 will equip students with the skills needed to communicate an opportunity to different audiences, including customers, investors, bankers, and employees. No entrepreneur can be successful without the ability to communicate passion and drive to those who can help her reach her goals. Chapter 11 describes the exit strategies entrepreneurs may wish to consider, including selling the business, going public, being acquired, or transferring ownership to employees, family members, or a chosen management team.

Part Four consists of Chapters 12, 13, and 14 which can be found on the book's website, These cover three special topics for students with a particular interest in social-, technology-, or family business-oriented entrepreneurship. These topics are dealt with in considerable depth but may be valuable to all students through their enlightening examples for analysis. For example, Chapter 13 includes the complexities of intellectual property and its management.

Supplements

If instructors wish to incorporate all or part of the "management track" into coursework, then students can access the Neoforma casebook on the book's website. This is a shortened version of the full text of *Starting Something* by Wayne McVicker. Students may want to read the full version if they seek an even richer insight into the life of an entrepreneur. In addition, for instructors, the website provides access to a test bank, PowerPoint presentations, sample cases and business plans, answers to end-of-chapter questions, and financial and legal templates you will need to set up a business. The website can be accessed at www.wiley.com/college/kaplan.

The website gives students access to a variety of resources:

- Additional case studies that allow students to review key entrepreneurial concepts.
- Audiovisual presentations by entrepreneurs, venture capitalists, successful students, and the Neoforma characters.
- Sample business plans. These plans are divided according to market and stage of development. Downloadable plans are available for students.
- Case summary reviews.
- Downloadable legal documents. Students can download sample legal agreements, including stock and shareholder agreements, consulting contracts, and employee option plans, among others.

About the Authors

Jack M. Kaplan is an adjunct professor of entrepreneurial studies at Columbia Business School and of Smeal College of Business at Penn State University. He has taught the entrepreneurial courses for Launching New Ventures, The Business Plan, and The Entrepreneurial Manager. During his career, Kaplan started and managed three successful companies, concentrating on smart card technology, health-care information systems, and loyalty marketing programs. He was president of Datamark Technologies, Inc., an entrepreneurial business venture engaged in electronic gift card and loyalty marketing programs. Ceridian, a Fortune 500 company, acquired the company in November 2005.

Kaplan is the author of *Getting Started in Entrepreneurship*, published by John Wiley & Sons in January 2001. His previous book was *Smart Cards: The Global Information Passport*, and his articles have appeared in *Technology News* and *Crain's of New York Business*.

His professional seminar experience includes conducting courses on new product strategies for Fortune 500 companies, including MIT Enterprise Forum, Aetna Insurance Company, Panasonic Global Sales Group, and Johnson & Johnson. He was a judge for the Ernst & Young Entrepreneur of the Year award program in New York and has appeared on A&E Biography, CNN, and CNBC. He is a graduate of the University of Colorado and received his MBA from the City University of New York.

Dr. Anthony C. Warren was formerly the Farrell Professor of Entrepreneurship at the Smeal College of Business, Penn State University, named "the hottest school for entrepreneurship" by

Newsweek magazine and the recipient of the NASDAQ Center for Entrepreneurial Excellence Award in 2005. He led educational programs in entrepreneurship at the undergraduate, graduate, and executive levels. Under grants from the Kauffman Foundation, Dr. Warren created unique courses in entrepreneurship based on problem-based learning, which have been recognized by several national organizations as being at the forefront of teaching methods. These courses are being introduced into colleges and high schools across the country and overseas.

Prior to joining Penn State, Dr. Warren started and grew several companies and until recently was a venture partner in Adams Capital Management, a venture capital firm managing more than $720 million. He consults regularly with both small and large companies on subjects of innovation management. A regular speaker at national conferences, Dr. Warren is often quoted in the press regarding innovation and entrepreneurship. He has authored several patents and research papers on technical and business issues and has contributed to many books. He has a B.Sc. and Ph.D. from the University of Birmingham. He recently started a telehealth company for the treatment of chronic diseases.

Isabel C. Botero (Ph.D., Michigan State University) is an adjunct professor in the management department at Stetson University. She is also a principal at Fediuk Botero LLC. Her extensive published research interests include communication in and about family firms, influence processes in their organization, information sharing, and crisis management. She is the lead author of Chapter 14.

Jeremy Kagan is the founder and CEO of Pricing Engine, a web service that empowers users to benchmark, optimize, and expand their digital marketing campaigns. He is also an adjunct professor of marketing at Columbia Business School. He provided content on digital marketing methods in Chapter 4.

Jack McGourty (Ph.D.) is the director of Community and Global Entrepreneurship at the Columbia Business School and a faculty member teaching graduate courses in entrepreneurship, innovation, and technology management. He provided content on the canvas model techniques in Chapter 3.

Marion Poetz (Ph.D., Vienna University of Economics and Business) is an associate professor of innovation management in Copenhagen Business School's Department of Innovation and Organizational Economics. Her research revolves around innovation search and problem solving in a world of widely distributed knowledge. She has published in leading academic and practitioner journals. She is the lead author of Chapter 5.

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List of Cases, Profiles, and Company Examples

Profiles are entrepreneurs' stories, mini-cases are short, illustrative examples, and cases are full case studies for student analyses.

Chapter No	Name	Type	Roadmap Topics
1	Wayne McVicker	Profile	A Typical Entrepreneur
1	Neoforma	Case	Master-Case in Management
2	Becky Minard and Paal Gisholt	Profile	Finding a Point of Pain
2	Greif Packaging	Mini-case	Building a Service
2	Blyth Candles	Mini-case	Incremental Innovation
2	Netflix	Mini-case	Disruptive Innovation
2	Pizza-on-a-truck	Mini-case	Thinking Big
3	Alexander Osterwalder	Profile	Building and Using Business Models
3	TinyUpdates	Mini-case	Using the Canvas
3	ChemStation	Mini-case	Franchising in a Business Model
3	BreatheSimple 1	Mini-case	Smoke-Screen Idea Testing
4	HubSpot	Profile	Digital Marketing
4	BreatheSimple 2	Mini-case	Web-Enabled Market Research
4	Glue Isobar	Mini-case	Viral Digital Marketing
5	FashionStake/David Gulati	Profile	Using Communities
5	Flitto	Mini-case	Using Volunteering Crowds
5	Goldcorp	Mini-case	Crowd-Based Problem Solving
5	Hello.com	Mini-case	Crowdfunding
5	Bragi	Mini-case	International Crowdfunding
?	Threadless	Mini-case	Using Customers for Product Design
6	Alex Shkolnik	Profile	Business Planning
6	Surf Parks	Case	Writing a Business Plan
7	Ethan Wendle	Profile	Setting Up the Company
8	James Dyson	Profile	Bootstrapping
8	BenchPrep	Mini-case	Funding Stages
8	Injection Research	Mini-case	Contingent Litigation
8	Xobni	Mini-case	Micro-equity
8	Best Lighting Products	Mini-case	Factoring
8	Jason Cong	Profile	Staged Investments
8	Coretek	Case	Use of Grants/Dilution Protection
9	Paul Silvis	Profile	Building a Great Culture
9	Teacher/Student Interaction	Mini-case	Conflicts of Interest

Chapter No	Name	Type	Roadmap Topics
10	Craig Bandes	Profile	Customizing Presentations
10	Leafbusters	Mini-case	Teaser
10	Railway Technology	Mini-case	Presentations
11	Alan Trefler	Profile	Private to Public Ownership
11	AEC	Mini-Case	Boutique Investment Banking
12	Khanjan Mehta	Profile	A Social Entrepreneur
12	Fairtrade	Mini-case	Pure Social Enterprise
12	HeartMath Institute	Mini-case	Hybrid Social Enterprise
12	Sea Tow Services	Mini-case	Hybrid Social Enterprise
12	Propeller Health	Mini-case	Dual Mission Enterprise
12	eno energy	Mini-case	Cooperative Green Energy
12	REI	Mini-case	Retailer’s Cooperative
13	Ian Kibblewhite	Profile	Integrated IP Strategy
13	Ultrafast	Mini-case	Licensing
14	Richard Edelman	Profile	Family Business Entrepreneur
14	Motor Coils	Mini-case	Succession Planning
14	Sheetz	Mini-case	Professionalization
14	Wilkin & Sons	Mini-case	Reputational Asset

Brief Contents

Contents

Getting Started as an Entrepreneur

PART 1

"Getting Started as an Entrepreneur" includes seven chapters that establish the foundations of entrepreneurship from understanding the personal attributes and management challenges that entrepreneurs will confront to developing ideas, business opportunities, and setting up a company. Chapter 1 covers the personal attributes of entrepreneurs and the management skills needed within the context of a new business. This topic is right up front to assist you in understanding the makeup of a typical entrepreneur and how closely you fit the mold. It is important that you consider what you may be getting yourself into before starting on the road to identifying an opportunity. The latter part of this chapter describes the entrepreneurial process and the steps to becoming an entrepreneur. The scope of the business idea that you choose to follow should match your personal aspirations and lifestyle aims. Chapter 2 explains how ideas are developed into business opportunities in the early venture stage. Here, you will also learn why innovation is important and the techniques used to become creative in developing new business ideas. In today's complex world, it is no longer sufficient just to have an idea for a new product or service; to be successful, you have to wrap the idea inside a "way of doing business" that provides sustainable growth and profits. Chapter 3 is devoted entirely on showing you how to design such "business models." Your business, like every business, must have customers that choose to buy from you rather than a competitor. Chapter 4 shows how to apply digital marketing tools for research, analyze the market and potential customers, conduct a competitive analysis, create a marketing plan for the venture, and use the Internet to get to your customers. Chapter 5 introduces the broad and exciting concepts in crowd-sourcing resources, and in Chapter 6 how to structure a short business plan is learned. Finally, Chapter 7 explores the various forms that ventures may take and describes how to register your company officially.

1 The Entrepreneurial Process

"Good management is the art of making problems so interesting and their solutions so constructive that everyone wants to get to work and deal with them."

Paul Hawken, Environmentalist, Entrepreneur, Author

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.
- Learn the master-case story and context.
- 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

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. Chapter 5 is devoted entirely to how you can access resources in many ways through "crowd-sourcing." 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 Mcvicker[4]—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 healthcare 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 healthcare 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. (See the Appendix to this chapter for more on Wayne and Neoforma.) The Neoforma story is used as a master-case throughout this book. The case can be found on the book web site together with video clips of interviews with the key persons in the case.

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 *entreprendeur* 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 entreprendeurs 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.

> "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*

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 three "special topic" chapters on the book web site for students who wish to specialize in these areas;—Chapter 12, Social Entrepreneurship; Chapter 13, Technology Entrepreneurship; and Chapter 14, Family Businesses—Important and Different.

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. The reorientation from "technology push" to "market-pull" is hard to make; more on this in Chapter 13.

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.

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 IPO (initial public offering). 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 8.

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. Exercises at the end of this chapter and Chapter 8 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 break Chapter 8 into two distinct parts to deal with them.

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!

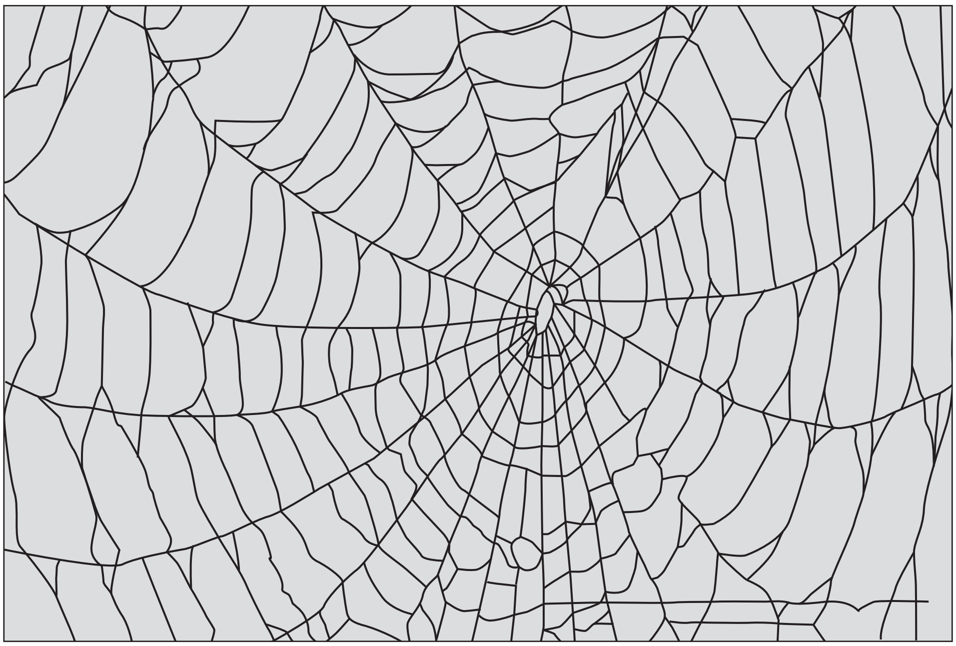

FIGURE 1-1

A Fragile Spider's Web