

PART

II

THE OPPORTUNITY

One often hears, especially from younger, newer entrepreneurs, the exhortation: “Go for it! You have nothing to lose now. So what if it doesn’t work out. You can do it again. Why wait?” While the spirit this reflects is commendable and there can be no substitute for doing, such itchiness can be a mistake unless it is focused on a solid opportunity.

Most entrepreneurs launching businesses, particularly the first time, run out of cash quicker than they bring in customers and profitable sales. While there are many reasons for this, the first is that they have not focused on the *right* opportunities. Unsuccessful entrepreneurs usually equate an idea with an opportunity; successful entrepreneurs know the difference!

Successful entrepreneurs know that it is important to “think big enough.” They understand that they aren’t simply creating a job for themselves and a few employees; they are building a business that can create value for themselves and their community.

While there are boundless opportunities for those with entrepreneurial zest, a single entrepreneur will likely be able to launch and build only a few good businesses—probably no more than three or four—during his or her energetic and productive years. (Fortunately, all you need to do is grow and harvest one quite profitable venture whose sales have exceeded several million dollars. The result will be a most satisfying professional life, as well as a financially rewarding one.)

How important is it, then, that you screen and choose an opportunity with great care? Very important! It is no accident that venture capital investors have consistently invested in no more than 1 or 2 percent of all the ventures they review.

As important as it is to find a good opportunity, even good opportunities have risks and problems. The perfect deal has yet to be seen. Identifying risks and problems before the launch while steps can be taken to eliminate them or reduce any negative effect early is another dimension of opportunity screening.

C · H · A · P · T · E · R

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THE ENTREPRENEURIAL PROCESS

I don't make movies to make money. I make money to make movies.

Walt Disney

RESULTS EXPECTED Upon completion of this chapter, you will be able to:

1. Articulate a definition of entrepreneurship and the entrepreneurial process—from lifestyle ventures to high-potential enterprises.
 2. Understand the practical issues and explore the complex map of requirements necessary to launch; including an appreciation that no one works alone—an array of stakeholders play a role.
 3. See how entrepreneurs and their financial backers get the odds for success in their favour by defying the pattern of disappointment and failure experienced by many.
 4. Explain the Timmons Model of the entrepreneurial process, how it can be applied to your entrepreneurial career aspirations and ideas for businesses, and how recent research confirms its validity.
- RESULTS EXPECTED**

DEMYSTIFYING ENTREPRENEURSHIP

Entrepreneurship is a way of thinking, reasoning, and acting that is opportunity obsessed, holistic in approach, and leadership balanced. Entrepreneurship results in the creation, enhancement, realization, and renewal of value, not just for owners, but for all participants and stakeholders. At the heart of the process is the creation and/or recognition of opportunities,¹ followed by the will and initiative to seize these opportunities. It requires a willingness to take risks—both personal and financial—but in a very calculated fashion in order to constantly shift the odds of success, balancing the risk with the potential reward. Typically, entrepreneurs devise ingenious strategies to marshal their limited resources. Take for example Tom Jablonski, who started ShoeGuru, the subject of this chapter’s case, a new venture formed to deliver stylish shoes combined with a slick Web site experience.

Today, entrepreneurship has evolved beyond the classic start-up notion to include companies and organizations of all types, in all stages. Thus, *entrepreneurship can occur—and fail to occur—in firms that are old and new, small and large; fast and slow growing; in the private, not-for-profit, and public sectors; in all geographic points; and in all stages of a nation’s development, regardless of politics.*

Entrepreneurial leaders inject imagination, motivation, commitment, passion, tenacity, integrity, teamwork, and vision into their companies. They face dilemmas and must make

decisions despite ambiguity and contradictions. **Very rarely is entrepreneurship a get-rich-quick proposition.** On the contrary, it is one of continuous renewal, as entrepreneurs are never satisfied with the nature of their opportunity. The result of this value creation process is that the total economic pie grows larger and society benefits.

CLASSIC ENTREPRENEURSHIP: THE START-UP

The classic expression of entrepreneurship is the raw start-up company, an innovative idea that develops into a high growth company. The best of these become entrepreneurial legends: Virgin Group, Netscape, Amazon.com, Sun Microsystems, Home Depot, Tim Hortons, Compaq Computer, Canadian Tire, and hundreds of others are now household names. Success, in addition to the strong leadership from the main entrepreneur, almost always involves building a team with complementary talents. The ability to work as a team and sense an opportunity where others see contradiction, chaos, and confusion are critical elements of success. Entrepreneurship also requires the skill and ingenuity to find and control resources, often owned by others, in order to pursue the opportunity. It means making sure the upstart venture does not run out of money when it needs it the most. Most highly successful entrepreneurs have held together a team and acquired financial backing in order to chase an opportunity others may not recognize.

ENTREPRENEURSHIP IN POST-BRONTOSAURUS CAPITALISM: BEYOND START-UPS

The upstart companies of yesterday and today have had a profound impact on the competitive structure of North American and global industries. Giant firms, such as IBM (knocked off by Apple, then Microsoft, and recently Lenovo acquired IBM's once strong PC division), Digital Equipment Corporation (another victim of Apple and acquired by Compaq Computer, which was in turn absorbed by HP), the music recording industry (hobbled by Napster and then legally by Apple's iTunes), or Eaton's and Kmart (entirely disappearing from Canada) once thought invincible, have been dismembered by the new wave of entrepreneurial ventures. The resulting downsizing during the 1980s returned in waves; economic downturns, rising fuel prices, and shifting consumer preferences were responsible for restructuring in the auto industry. While large companies, like Nortel Networks, shrink head count, new ventures add jobs. As autopsy after autopsy was performed on failing large companies, a fascinating pattern emerged, showing, at worst, a total disregard for the winning entrepreneurial approaches of their new rivals and, at best, a glacial pace in recognizing the impending demise and the changing course.

"People Don't Want to Be Managed. They Want to Be Led!"²

These giant firms can be characterized, during their highly vulnerable periods, as hierarchical in structure with many layers of reviews, approvals, and vetoes. Their tired executive blood conceived of leadership as *managing and administering* from the top down, in stark contrast to Ewing M. Kauffman's powerful insight, "People don't want to be managed. They want to be led!" These stagnating giants tended to reward people who accumulated the largest assets, budgets, number of plants, products, and head count, rather than rewarding those who created or found new business opportunities, took calculated risks, and occasionally made mistakes, all with bootstrap resources. While very cognizant of the importance of corporate culture and strategy, the corporate giants' pace was glacial: Research on these dinosaurs concludes that it typically **took six years for a large firm to change its strategy and 10 to 30 years to change its culture.** Meanwhile, the median time it took start-ups to accumulate the necessary capital was **one month, but averaged six months.**³

To make matters worse, these **corporate giants had many bureaucratic tendencies, particularly arrogance.** They shared a blind belief that if they followed the almost sacred best-management practices of the day, they could not help but prevail. Previously, these best-management practices did not include entrepreneurship, entrepreneurial leadership, and entrepreneurial reasoning. If anything, these were considered dirty words in the corporate world. Chief among these sacred cows was staying close to your customer. What may shock you is the following conclusion of a study of disruptive technologies:

One of the most consistent patterns in business is the failure of leading companies to stay at the top of their industries when technologies or markets change. ... But a more fundamental reason lies at the heart of the paradox: Leading companies succumb to one of the most popular, valuable management dogmas. They stay close to their customers.⁴

When they do attack, the [new] entrant companies find the established players to be easy and unprepared opponents because the opponents have been looking up markets themselves, discounting the threat from below.⁵

One gets further insight into just how vulnerable and fragile the larger, so-called well-managed companies can become, and why it is the newcomers who pose the greatest threats. This pattern also explains why there are tremendous opportunities for the coming e-generation even in markets that are currently dominated by large players.

The problem is that managers keep doing what has worked in the past: serving the rapidly growing needs of their current customers. The processes that successful, well-managed companies have developed to allocate resources among proposed investments are incapable of funnelling resources in programs that current customers explicitly don't want and whose profit margins seem unattractive.⁶

Coupled with the number of new innovations, firms, and industries have been created in the past 30 years, it is no wonder that brontosaurus capitalism has found its ice age.

Signs of Hope in a Corporate Ice Age

Fortunately, for many giant firms, the entrepreneurial revolution may spare them from their own ice age. One of the most exciting developments of the decade is the response of some large, established corporations to the revolution in entrepreneurial leadership. After decades of experiencing the demise of giant after giant, corporate leadership, in unprecedented numbers, is launching experiments and strategies to recapture entrepreneurial spirit and to instill the culture and practices we would characterize as entrepreneurial reasoning. The e-generation has too many attractive opportunities in truly entrepreneurial environments. They do not need to work for a brontosaurus that lacks spirit.

Increasingly, we see examples of **large companies adopting principles of entrepreneurship and entrepreneurial leadership in order to survive and to renew.** Researchers document how large firms are applying entrepreneurial thinking, in pioneering ways, to invent their futures, including companies such as GE, Corning, Motorola, PotashCorp of Saskatchewan, Bombardier, and EnCana.⁷ Most large brontosaurus firms could learn valuable lessons on how to apply entrepreneurial thinking from companies such as these.

Metaphors

Improvisational, quick, clever, resourceful, and inventive all describe good entrepreneurs. Likewise, innumerable metaphors from other parts of life can describe the complex world of the entrepreneur and the entrepreneurial process. From music it is jazz, with its uniquely impromptu flair. From sports many metaphors exist: LeBron James's agility, the broken-field running of Pinball Clemons, the wizardry on ice of Sidney Crosby, or the competitiveness of Silken Laumann. Even more fascinating are the unprecedented comebacks of athletic greats such as Mario Lemieux, Picabo Street, and Lance Armstrong.

Perhaps the game of golf, more than any other, replicates the complex and dynamic nature of managing risk and reward, including all the intricate mental challenges faced in entrepreneuring. No other sport, at one time, demands so much physically, is so complex,

intricate, and delicate, and is simultaneously so rewarding and punishing; and none tests one's will, patience, self-discipline, and self-control like golf. Entrepreneurs face these challenges and remunerations as well. If you think that the team concept isn't important in golf, remember the 2004 American Ryder Cup "dream team," which failed to work together and lost to the Europeans. And what about the relationship between the caddy and golfer?

An entrepreneur also faces challenges like a symphony conductor or a coach who must blend and balance a group of diverse people with different skills, talents, and personalities into a superb team. On many occasions it demands all the talents and agility of a juggler who must, under great stress, keep many balls in the air at once.

The complex decisions and numerous alternatives facing the entrepreneur also have many parallels with the game of chess. As in chess, the victory goes to the most creative player, who can imagine several alternate moves in advance and anticipate possible defences. This kind of mental agility is frequently demanded in entrepreneurial decision-making. Mike Chiasson and Chad Saunders both of the University of Calgary find that entrepreneurial actions are driven as well as constrained by mental processes. Recognizing and formulating entrepreneurial opportunity is a cyclical yin and yang where restrictions and possibilities must be reconciled.⁸

Regardless of the metaphor or analogy you choose for entrepreneurship, each is likely to describe a creative, even artistic, improvised act. The outcomes are often either highly rewarding successes or painfully visible misses. Always, urgency is on the doorstep.

ENTREPRENEURSHIP = PARADOXES

One of the most confounding aspects of the entrepreneurial process is its contradictions. Because of its highly dynamic, fluid, ambiguous, and chaotic character, the process's constant changes frequently pose paradoxes. A sampling of entrepreneurial paradoxes follows. Can you think of other paradoxes that you have observed or heard about?

- ✓ **An opportunity with no or very low potential can be an enormously big opportunity.** One of the most famous examples of this paradox is Apple. Founders Steve Jobs and Steve Wozniak approached their employer, Hewlett-Packard, with the idea for a desktop, personal computer and were told this was not an opportunity for HP. Hence, Jobs and Wozniak started their own company. Frequently, business plans rejected by some venture capitalists become legendary successes when backed by another investor. In addition to quite a few instances where some now famous and successful entrepreneurs had their ideas initially turned down, there are a growing number of cases where some entrepreneurs said 'no' to investment money—despite indications from many that it is getting harder to find venture capital in Canada. One such individual is Albert Lai. He turned down offers of funding and it turned out to be the right move—he later sold BubbleShare for \$3 million... and didn't have to share his winnings. In his blog Albert Lai writes:

Lack of entrepreneurial support systems for students (and recent grads): students are not given the a) role models & motivation, b) knowledge & encouragement, c) support systems & funding, d) education/network, to enable them to succeed. Many of the most innovative start-ups/products on the net that you use everyday today were started in dorm rooms of university students—especially in the B2C space (i.e., Netscape, Napster, Yahoo, Google, Facebook, etc.). Virtually none of them are from Canadian university dorm rooms. The above points can really be boiled down to two things a) lack of funding, b) lack of entrepreneurial culture/encouragement.

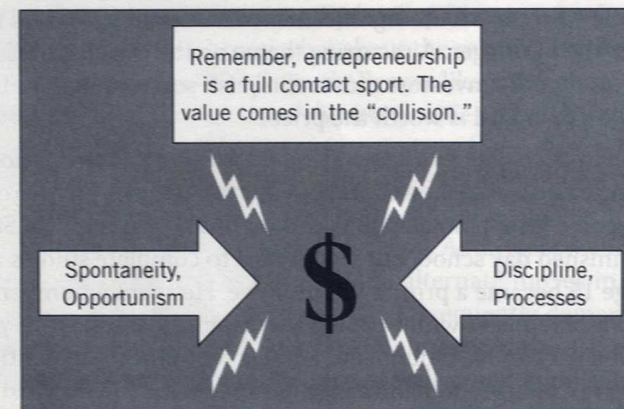
How do we solve this? We need to provide Canadian students with more exposure to "what's possible" and a real support system.

- ✓ **To make money you have to first lose money.** It is commonly said in the venture capital business that the lemons, or losers, ripen in two-and-a-half years, while the plums take seven or eight years. A start-up, venture-backed company typically loses money, often \$10 million or more, before sustaining profitability and going public, usually at least five to seven years later.

- ✓ **To create and build wealth one must relinquish wealth.** Among the most successful and growing companies, the founders aggressively dilute their ownership to create ownership throughout the company. By rewarding and sharing the wealth with the people who contribute significantly to its creation, owners motivate stakeholders to make the pie bigger. A recurring theme on the popular CBC television show, *Dragons' Den*, is that the investors must relinquish some equity but the value of bringing a Dragon on board is worth the price.
- ✓ **To succeed, one first has to experience failure.** It is a common pattern that the first venture fails; yet the entrepreneur learns and goes on to create a highly successful company. Joseph Smallwood grew up in abject poverty in St. John's, Newfoundland. He finished day school but was unable to complete studies at Bishop Field College and at age 15 became a printer's apprentice. He spent a number of years gaining experience as a reporter with various newspapers, including five years in New York City. He moved back to Newfoundland and his first venture in politics was a flop. He did go on to serve as Newfoundland's premier for nearly 25 years and brought the island into Confederation.⁹ A recent study finds those entrepreneurs who have previously failed increase their odds of success compared to those who are first time entrepreneurs. Of course those with a track record of success do even better!¹⁰
- ✓ **Entrepreneurship requires considerable thought, preparation, and planning, yet is basically an unplannable event.** The highly dynamic, changing character of technology, markets, and competition make it impossible to know all your competitors today, let alone five years from now. Yet great effort is invested in attempting to model and envision the future. The resulting business plan is inevitably obsolete when it comes off the printer. This is a creative process—like moulding clay.¹¹ You need to make a habit of planning and reacting as you constantly re-evaluate your options, blending the messages from your head and your gut, until this process becomes second nature.
- ✓ **For creativity and innovativeness to prosper, rigour and discipline must accompany the process.** For years, hundreds of thousands of patents for new products and technologies lay fallow in government and university research labs because there was no commercial discipline.
- ✓ **Entrepreneurship requires a bias toward action and a sense of urgency, but also demands patience and perseverance.** While his competitors were acquiring and expanding rapidly, one entrepreneur's management team became nearly outraged at his inaction. This entrepreneur reported he saved the company at least \$50 million to \$100 million during the prior year by just sitting tight. He learned this lesson from a case study in *New Venture Creation*.
- ✓ **The greater the organization, orderliness, discipline, and control, the less you will control your ultimate destiny.** Entrepreneurship requires great flexibility and nimbleness in strategy and tactics. One has to play with the knees bent. Overcontrol and an obsession with orderliness are impediments to the entrepreneurial approach. As the great racecar driver Mario Andretti said, "If I am in total control, I know I am going too slow!"
- ✓ **Adhering to management best practice, especially staying close to the customer that created industry leaders in the 1980s, became a seed of self-destruction and loss of leadership to upstart competitors.** We discussed earlier the study of "disruptive technologies."
- ✓ **To realize long-term equity value, you have to forgo the temptations of short-term profitability.** Building long-term equity requires large, continuous reinvestment in new people, products, services, and support systems, usually at the expense of immediate profits.

The world of entrepreneurship is not neat, tidy, linear, consistent, and predictable, no matter how much we might like it to be that way.¹² In fact, it is from the collisions inherent in these paradoxes that value is created as illustrated in Exhibit 2.1. These paradoxes illustrate just how contradictory and chaotic this world can be. To thrive in this environment, one needs to be very adept at coping with ambiguity, chaos, and uncertainty, and at building management skills that create predictability.

EXHIBIT 2.1 Entrepreneurship IS a Contact Sport



The Higher Potential Venture: Think Big Enough

One of the biggest mistakes aspiring entrepreneurs make is strategic. They think too small. Sensible as it may be to think in terms of a very small, simple business as being more affordable, more manageable, less demanding, and less risky, the opposite is true. The chances of survival and success are lower in these small, job-substitute businesses, and even if they do survive, they are less financially rewarding. As one founder of numerous businesses put it: Unless this business can pay you at least five times your present salary, the risk and wear and tear won't be worth it.

Consider one of the most successful venture capital investors ever, Arthur Rock. His criterion for searching for opportunities is very simple: *look for business concepts that will change the way people live or work.* His home-run investments are legendary, including Intel, Apple, Teledyne, and dozens of others. Clearly, his philosophy is to think big. Today an extraordinary variety of people, opportunities, and strategies characterize the millions of proprietorships, partnerships, and corporations in the country. Remember, high potential ventures become high impact firms that often make the world a better place!

Nearly 10 percent of the Canadian population is actively working on a new venture.¹³ More than 95 percent of start-ups have revenues of less than \$1 million annually. Statistics Canada reports about 150,000 new businesses enter the playing field annually and nearly as many exit each year. Harry Bowen of Queen's University and Dirk De Clercq of Brock University find that entrepreneurial effort toward high-growth activities is related to financial conditions and educational factors that vary from place to place as well as over time.¹⁴

Not only can nearly anyone start a business, but also a great many can succeed. While it certainly might help, a person does not have to be a genius to create a successful business. As Nolan Bushnell, founder of Atari, one of the first desktop computer games in the early 1980s, and Pizza Time Theater, said, "If you are not a millionaire or bankrupt by the time you are 30, you are not really trying!"¹⁵ It is an entrepreneur's preparedness for the entrepreneurial process that is important. Being an entrepreneur has moved from cult status in the 1980s to rock star infamy in the 1990s to become de rigueur at present. Amateur entrepreneurship is over. The professionals have arrived.

A stunning number of mega-entrepreneurs launched their ventures during their 20s. While the rigours of new ventures may favour the "young at start," age is not a barrier to entry. Most studies show that about 25 percent of founders were over 40 when they embarked on their entrepreneurial careers, half were in their 30s, and just over one-quarter did so by the time they were 25. The Global Entrepreneurship Monitor finds that 25 to 34-year-olds are most active in entrepreneurship and that entrepreneurial activity declines after the age of 35.¹⁶ However, numerous examples exist of founders who were over 60 at the time of launch, including one of the most famous seniors, Colonel Harland Sanders, who at 65 started franchising KFC with his first old-age pension cheque.

SMALLER CAN MEAN HIGHER FAILURE ODDS

Unfortunately, the record of survival is not good among all firms started. Most estimates place the failure rate for start-ups at 50 percent in the first few years. While government data, research, and business mortality statisticians may not agree on the precise failure and survival figures for new businesses, they do agree that failure is the rule, not the exception.

Complicating efforts to obtain precise figures is the fact that it is not easy to define and identify failures, and reliable statistics and databases are not available. One study reports after one year, 71 percent of new ventures are still in business, the number drops to 58 percent by year two and 49 percent by year three. At the five-year mark 37 percent are still in business and going into the tenth year only 23 percent of those original start-ups remain in business (see Exhibit 2.2).

Exit rates vary widely across industries, but so too do entry rates. For instance, **retail and services accounted for the majority of all failures.** Restaurants come and go like clockwork, everybody thinks they have a better idea or menu. Chances of success also differ for other factors.

The likelihood that start-ups will survive their initial year differs dramatically across provinces. Firms in their initial year of life exhibit a much higher success rate in Ontario (75 percent) than in the Atlantic Provinces (59 percent). Business start-ups in British Columbia (75 percent), Québec (74 percent), and Alberta (72 percent) are more likely to survive their first year than those in Saskatchewan or Manitoba (63 percent) (see Exhibit 2.3).

The following discussion provides a distillation of a number of failure-rate studies over many years. These studies illustrate that (1) failure rates are high, and (2) although the majority of the failures occur in the first two to five years, it may take considerably longer for some to fail.¹⁷

EXHIBIT 2.2 Start-up Survival Rates by Firm Size

Firm Size	Number of Years (Percent)								
	1	2	3	4	5	6	7	8	9
Small (1-4)	71	57	49	42	36	31	27	24	22
Medium (5-99)	74	61	53	47	42	38	34	31	29
Large (100+)	81	68	63	58	54	52	50	49	45
All	71	58	49	42	37	32	28	25	23

Source: Longitudinal Employment Analysis Program (LEAP), Small Business Research and Policy, Industry Canada. Start-ups tracked from 2003 to 2008. Statistics based on firm size at start-up: 1 to 4 employees 130,021 observations; 5 to 99 employees 18,255 observations; 100+ employees 184 observations.

EXHIBIT 2.3 Start-up Survival Rates by Firm Location

Region	Number of Years (Percent)								
	1	2	3	4	5	6	7	8	9
Atlantic Canada	58.9	43.6	36.0	30.7	26.8	23.8	21.3	19.3	17.1
Quebec	74.2	56.0	46.8	40.7	36.3	32.6	29.6	27.1	24.8
Ontario	74.7	57.8	49.0	42.8	38.2	34.4	31.2	28.5	25.6
Prairies	63.2	49.4	41.6	35.9	31.7	28.5	25.7	22.9	20.2
Alberta	72.3	56.8	48.8	42.9	38.2	34.6	31.5	28.6	25.7
British Columbia	74.7	57.7	48.7	42.1	37.0	32.9	29.6	26.7	24.0
Canada	71.3	54.8	46.1	40.1	35.5	31.9	28.9	26.3	23.7

Source: Small Business Research and Policy, Industry Canada, July 2008.

Finally, “failure” may not always be the most appropriate term. There are instances where an entrepreneur chooses to get out—either to close it or sell it off. Further, an idea may have run its course and no longer be viable, even after only one year—such as a product or service tied to an event like a music festival or a Winter Olympics. A better opportunity may come along and the entrepreneur may have to abandon the current venture for that more attractive one. Entrepreneurs that hop from one opportunity to another have been described as having a high churn rate. The serial entrepreneur is one who goes from venture to venture in succession, but there is also evidence of the portfolio entrepreneur, an individual who can’t concentrate his or her efforts on a single venture—perhaps even counting on some falling off along the way. Often data are unable to capture businesses that de-register or change name.

Failure rates across industries vary as well. **The real estate industry, with a 37-percent rate of start-up failure, is the lowest.** The technology sector has a high rate of failure at 54 percent. The software and services segment of the technology industry has an even higher failure rate; 55 percent of start-ups tracked closed their doors. Unfortunately, the record of survival is not good among all firms started.

To make matters worse, most people think the failure rates are actually much higher. Since actions often are governed by perceptions rather than facts, this perception of failure, in addition to the dismal record, can be a serious obstacle to aspiring entrepreneurs.

Still other studies have shown significant differences in survival rates among industry categories: retail trade, construction, and small service businesses accounted for 70 percent of all failures and bankruptcies. One study calculates a risk factor or index for start-ups by industry, which sends a clear warning signal to the would-be entrepreneur.¹⁸ “The fishing is better in some streams versus others,” is another favourite saying of the authors. Further, the vast majority of these failed companies had fewer than 100 employees. Through observation and practical experience one would not be surprised by such reports. The implications for would-be entrepreneurs are important: Knowing the difference between a good idea and a real opportunity is vital. This will be addressed in detail in Chapter 3. Monica Diochon of St. Francis Xavier, Teresa Menzies of Brock University, and Yvon Gasse of the Université Laval point out that opportunity identification is not the same as opportunity pursuit. Factors that may help in identifying opportunities, such as education and experience, may even hamper pursuing opportunities.¹⁹

A certain level of failure is part of the “creative destruction” described by Joseph Schumpeter in his writings. It is part of the dynamics of innovation and economic renewal, a process that requires both births and deaths. More important, it is also part of the learning process inherent in an entrepreneurial apprenticeship. Businesses fail, but entrepreneurs survive and learn.

The daunting evidence of failure poses two important questions for aspiring entrepreneurs. First, are there any exceptions to this general rule of failure, or are we faced with a punishing game of entrepreneurial roulette? Second, if there is an exception, how does one get the odds for success in one’s favour?

Getting the Odds in Your Favour

Fortunately, there is a decided pattern of exceptions to the overall rate of failure among the vast majority of small, marginal firms created each year. Most smaller enterprises that cease operation simply do not meet our notion of entrepreneurship. They do not create, enhance, or pursue opportunities that realize value. They tend to be job substitutes in many instances. Undercapitalized, undermanaged, and often poorly located, they soon fail.

Threshold Concept

Who are the survivors? The odds for survival and a higher level of success change dramatically if the venture reaches a critical mass of at least 10 to 20 people with \$2 million to \$3 million in revenues and is currently pursuing opportunities with growth potential. Survival rates for new firms increase steadily as the firm size increases. The survival rates at

the three-year mark jump from approximately 49 percent for firms having up to five employees to approximately 63 percent for firms with over 100 employees.

Empirical evidence supports the *liability of newness* and *liability of smallness* arguments and suggests that **being new and small make survival difficult.** The authors of one study inferred, “Perceived satisfaction, cooperation, and trust between the customer and the organization [are] important for the continuation of the relationship. High levels of satisfaction, cooperation, and trust represent a stock of goodwill and positive beliefs which are critical assets that influence the commitment of the two parties to the relationship.”²⁰ The authors of this study noted, “Smaller organizations are found to be more responsive, while larger organizations are found to provide greater depth of service. ... The entrepreneurial task is to find a way to either direct the arena of competition away from the areas where you are at a competitive disadvantage, or find some creative way to develop the required competency.”²¹

Although any estimates based on sales per employee vary considerably from industry to industry, this minimum translates roughly to a threshold of \$50,000 to \$100,000 of sales per employee annually. But highly successful firms can generate much higher sales per employee.

Promise of Growth

The definition of entrepreneurship implies the promise of expansion and the building of long-term value and durable cash flow streams as well. It is perhaps not surprising that time frames and growth aspirations are idiosyncratic. Dev Dutta of the University of New Hampshire and Stewart Thornhill of the University of Western Ontario find that entrepreneurs vary in their cognitive styles. This outlook combined with their assessment of the competitive environment influences the growth intentions for their enterprise.²²

However, as will be discussed later, it takes time for enterprises to become established and grow. Historically, two of every five small firms founded survive four years but few achieve growth during those first few years. Odds of survival increase substantially for those enterprises that grow, and the earlier in the life of the business that growth occurs, the higher the chance of survival.²³ The 2008 INC. 500 exemplify this, with a median three-year growth rate of 334 percent.²⁴ Profit’s Hot 50 for 2008 achieved average two-year revenue growth of 756 percent, but 26 percent of them were not yet profitable in their most recent fiscal year.²⁵ Of Canada’s hottest 50 home-grown enterprises, 54 percent are headed by CEOs that have started ventures in the past.²⁶ The 2008 list of enterprises includes a wide range of products and services offered: model train manufacturer (Rapido Trains), organic food ingredient distributor (N2 Ingredients), oilfield construction (CerPro Energy Services), designer doggy wear (FouFou Dog), Web systems integrator (Spheric Technologies), custom ‘skins’ for electronics (MyTego.com), cosmetics (Bleu Lavande), and online auction management (Auctionwire).

Some of the true excitement of entrepreneurship lies in conceiving, launching, and building firms such as these.

Venture Capital Backing

Another notable pattern of exception to the failure rule is found for businesses that attract start-up financing from successful private venture capital companies. As Exhibit 2.4 shows venture-backed firms account for a very small fraction of the population each year.

Venture capital is not essential to a start-up, nor is it a guarantee of success. Of the companies making the 2001 INC. 500, only 18 percent raised venture capital and only 3 percent had venture funding at start-up.²⁷ Consider, for instance, that even in the dot-com heyday of 2000 only 1,300 Canadian enterprises received venture capital. However, companies with venture capital support fare better overall. Perhaps as few as 1 percent of the venture-backed companies declare bankruptcy or become defunct.²⁸

These compelling data have led some to conclude a threshold core of 10 to 15 percent of new companies will become the winners in terms of size, job creation, profitability, innovation, and potential for harvesting (and thereby realize a capital gain).

EXHIBIT 2.4 Canadian Venture Capital Activity

Year	Amount invested	Number of deals	Average deal
1998	1.5 billion	850	\$1.8 million
1999	2.75 billion	900	3.1 million
2000	5.9 billion	1300	4.5 million
2001	3.7 billion	925	4 million
2002	2.75 billion	790	3.5 million
2003	1.7 billion	680	2.5 million
2004	1.85 billion	600	3 million
2005	1.82 billion	630	2.9 million
2006	1.7 billion	408	4.2 million
2007	2.1 billion	412	5.1 million
2008	1.3 billion	371	3.5 million

Source: Courtesy of CVCA—Canada's Venture Capital and Private Equity Association and Thomson Reuters.

Private Investors Join Venture Capitalists

Entrepreneurs that have cashed out, harvesting their enterprises, by the tens of thousands have become "angels" as private investors in the next generation of entrepreneurs. Many of the more successful entrepreneurs have created their own investment pools and are competing directly with venture capitalists—such as Skypoint Capital, Garage Technology Ventures, Golden Opportunities Fund, TriWest Capital, AVAC, or Ventures West—for deals. Their operating experiences and successful track records provide a compelling case for adding value to an upstart company. Take, for example, Purple Angel, a Canadian group of former high-tech executives who came together in 2001 to give back—to support technology start-ups by investing resources: time, money, and effort. Some of their chosen projects have required business acumen (e.g., help with market identification or making an introduction to a key contact); others have needed technological expertise. While Purple Angel's mission explicitly mentions the goal of fun, generating wealth is a stated objective too.

Private investors and entrepreneurs have very similar selection criteria to the venture capitalists: They are in search of the high potential, higher growth ventures. Unlike the venture capitalists, however, private investors are not constrained by having to invest so much money in a relatively short period that they must invest it in minimum chunks of \$3 million to \$5 million or more. Angel investors, therefore, are prime sources for less capital-intensive start-ups and early-stage businesses.

This overall search for higher potential ventures has become more evident in recent years. The new e-generation appears to be learning the lessons of these survivors, venture capitalists, private investors, and founders of higher potential firms. Hundreds of thousands of students now have been exposed to these concepts over the years, and their strategies for identifying potential businesses are mindful of and disciplined about the ingredients for success. Unlike 20 or more years ago, it is now nearly impossible not to hear and read about these principles whether on television, in books, on the Internet, or in a multitude of seminars, courses, and programs for would-be entrepreneurs of all types.

Find Financial Backers and Associates Who Add Value

One of the most distinguishing disciplines of these higher potential ventures is how the founders identify financial partners and key team members. They insist on backers and partners who do more than bring just money, friendship, commitment, and motivation to the venture. They surround themselves with backers who can add value to the venture through

their experience, know-how, networks, and wisdom. Key associates are selected because they are smarter and better at what they do than the founder; and they raise the overall average of the entire company. This theme will be examined in detail in later chapters.

Option: The Lifestyle Venture

For many aspiring entrepreneurs, issues of family roots and location take precedence. Accessibility to a preferred way of life, whether it is access to skiing, hiking, music, surfing, canoeing, a rural setting, the mountains, can be more important than how large a business one has or the size of one's net worth. Others vastly prefer to be with and work alongside their family or spouse. They want to live in a non-urban area that they consider very attractive or even pursue a noble cause. Maria Panínguakí Kjærulff (www.mariagreenland.com) is a full-time artist that, for now, calls Nuuk, Greenland home. After graduating from Nova Scotia College of Art and Design with a Bachelor of Fine Arts, including a semester at Cooper Union School of Art in New York City, she chose her hometown. Though she has spent time in Minnesota and Denmark, she returned to comfortable surroundings, family, and friends. Despite the relative isolation of Greenland—a large island with low population, primarily within the Arctic Circle—Maria's art is exhibited in Denmark, Canada, Korea, Iceland, Finland, Sweden, and Norway.

Yet, couples who give up successful careers in Toronto to buy a bed-and-breakfast in cottage country to avoid the rat race generally last only six to seven years. They discover the joys of self-employment, including seven-day, 70- to 90-hour workweeks, chefs and day help that do not show up, roofs that leak when least expected, and the occasional guests from hell. The grass is always greener, so they say.

Methods of financing often separate ventures. Jean-Etienne de Bettignies of Queen's University finds that equity-type contracts are prevalent for high-growth ventures whereas debt-type contracts are typical of lifestyle ventures.²⁹

THE TIMMONS MODEL: WHERE THEORY AND PRACTICE COLLIDE IN THE REAL WORLD

How can aspiring entrepreneurs—and the investors and associates who join the venture—get the odds of success on their side? What do these talented and successful high potential entrepreneurs, their venture capitalists, and their private backers do differently? What accounts for their exceptional record? Are there general lessons and principles underlying their successes that can benefit aspiring entrepreneurs, investors, and those who would join a venture? If so, can these lessons be learned?

These are the central questions of our lifetime work. We have been immersed as students, researchers, teachers, and practitioners of the *entrepreneurial process*. As founding shareholders and investors of several high potential ventures (some of which are now public), advisors to ventures, and mentors to entrepreneurs—including many former students, we have each applied, tested, refined, and tempered academic theory as fire tempers iron into steel: in the fire of practice. Chances are that your instructor for this course has considerable background in entrepreneurship, perhaps advising government on policy matters or local/regional economic development agencies. Much of the wisdom we have gained, whether from activities such as judging and coaching business plan and elevator pitch competitions or a seat on a board of directors, comes from you—the student.

Intellectual and Practical Collisions with the Real World

Throughout this period of evolution and revolution, *New Venture Creation* has adhered to one core principle: In every quest for greater knowledge of the entrepreneurial process and more effective learning, there must be intellectual and practical collisions between

academic theory and the real world of practice. The standard academic notion of something being all right in practice but not in theory is unacceptable. This integrated, holistic balance is at the heart of what we know about the entrepreneurial process and getting the odds in your favour.

Value Creation: The Driving Forces

A core, fundamental entrepreneurial process accounts for the substantially greater success pattern among higher potential ventures. Despite the great variety of businesses, entrepreneurs, geographies, and technologies, central themes or driving forces dominate this highly dynamic entrepreneurial process.

- It is *opportunity* driven.
- It is driven by a *lead entrepreneur* and an *entrepreneurial team*.
- It is *resource parsimonious* and *creative*.
- It depends on the *fit* and *balance* among these.
- It is *integrated* and *holistic*.
- It is *sustainable*.

These are the controllable components of the entrepreneurial process that can be assessed, influenced, and altered. Founders and investors focus on these forces during their careful due-diligence process to analyze the risks and determine what changes can be made to improve a venture's chances of success.

First, we will elaborate on each of these forces to provide a blueprint and a definition of what each means. Then using the early years of Mitel as an example, we will illustrate how the holistic, balance, and fit concepts pertain to a start-up.

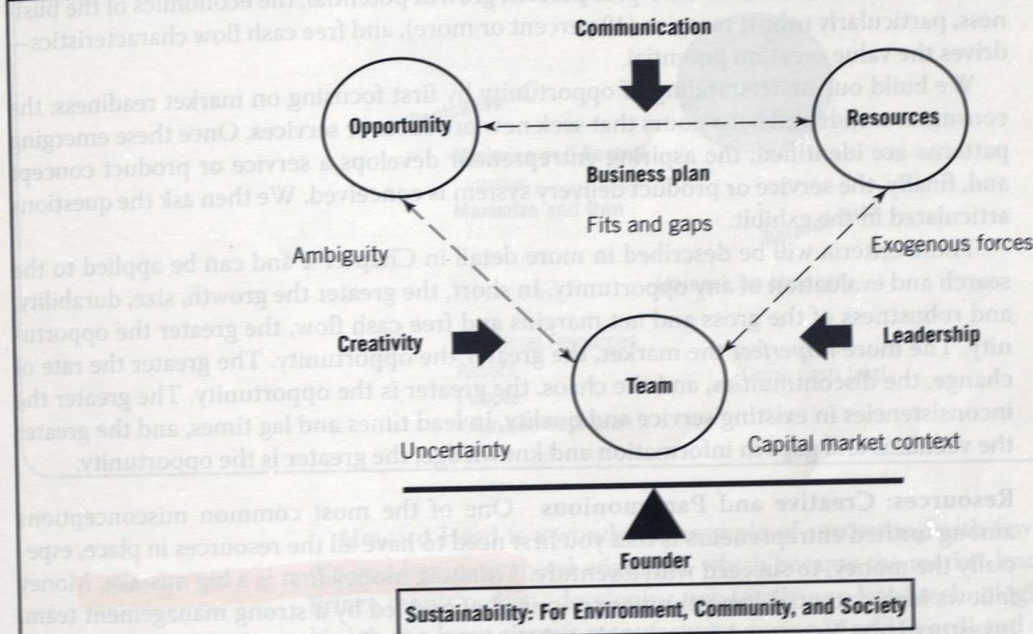
Change the Odds: Fix It, Shape It, Mould It, Make It

The driving forces underlying successful new venture creation are illustrated in Exhibit 2.5. The process starts with opportunity, not money, strategy, networks, team, or the business plan. Most genuine opportunities are much bigger than either the talent and capacity of the team or the initial resources available to the team. The role of the lead entrepreneur and the team is to juggle all these key elements in a changing environment. Think of a juggler bouncing up and down on a trampoline that is moving on a conveyor belt at unpredictable speeds and directions, while trying to keep objects of various shapes, weights, and sizes all in the air. That is the dynamic nature of an early-stage start-up. The business plan provides the language and code for communicating the quality of the three driving forces of the Timmons Model and of their fit and balance.

In the entrepreneurial process depicted in the Timmons Model, the shape, size, and depth of the opportunity establishes the required shape, size, and depth of both the resources and the team. We have found that many people are a bit uncomfortable viewing the opportunity and resources somewhat precariously balanced by the team. It is especially disconcerting to some because we show the three key elements of the entrepreneurial process as circles, and thus the balance appears tenuous. These reactions are justified, accurate, and realistic. The entrepreneurial process is dynamic. Those who recognize the risks better manage the process and garner higher returns.

The lead entrepreneur's job is simple enough. He or she must carry the deal by taking charge of the success equation. In this dynamic context, ambiguity and risk are actually your friends. Central to the homework, creative problem solving and strategizing, and due diligence that lies ahead is analyzing the fits and gaps that exist in the venture. What is wrong with this opportunity? What is missing? What good news and favourable events can happen, as well as the adverse? What has to happen to make it attractive and a fit for me? What market, technology, competitive, management, and financial risks can be reduced or eliminated? What can be changed to make this happen? Who can change it? What are the

EXHIBIT 2.5 The Timmons Model of the Entrepreneurial Process



least resources necessary to grow the business the farthest? Is this the right team? By implication, if you can determine these answers and make the necessary changes by figuring out how to fill the gaps and improve the fit and attract key players who can add such value, then the odds for success rise significantly. In essence, the entrepreneur's role is to manage and redefine the risk-reward equation—all with an eye towards sustainability. Since part of the entrepreneur's legacy is to create positive impact without harming the environment, the community, or society, the concept of sustainability appears as the underlying foundation in the model.

The Opportunity At the heart of the process is the opportunity. Successful entrepreneurs and investors know that a good idea is not necessarily a good opportunity. For every 100 ideas presented to investors in the form of a business plan or proposal, usually fewer than four get funded. More than 80 percent of those rejections occur in the first few hours; another 10 to 15 percent are rejected after investors have read the business plan carefully. Less than 10 percent attract enough interest to merit a more thorough review; that due diligence can take several weeks or months. These are very slim odds. Countless hours and days have been wasted by would-be entrepreneurs chasing ideas that are going nowhere. An important skill for an entrepreneur or an investor is to be able to quickly evaluate whether serious potential exists, and to decide how much time and effort to invest. Many give the aspiring entrepreneur the advice to visit a bank to ask for a loan even if you do not need the money. The rigour of the assessment is worthwhile and often the banker delivers medicine that others cannot see or friends will not share.

One senior partner at a prominent venture capital fund asserted, "There's never been a better time than now to start a company. In the past, entrepreneurs started businesses. Today they invent new business models. That's a big difference, and it creates huge opportunities."³⁰ Even after a big stock market crash, when financing often dries up, those words still ring true. In fact, of those enterprises that started during the toughest times and survived, most go on to thrive.

Another venture capitalist stated, "After the irrational exuberance of the late 90s, it is again a great time to start a business. Venture capital is plentiful, valuations make sense and venture capitalists are anxious for high potential ventures."³¹

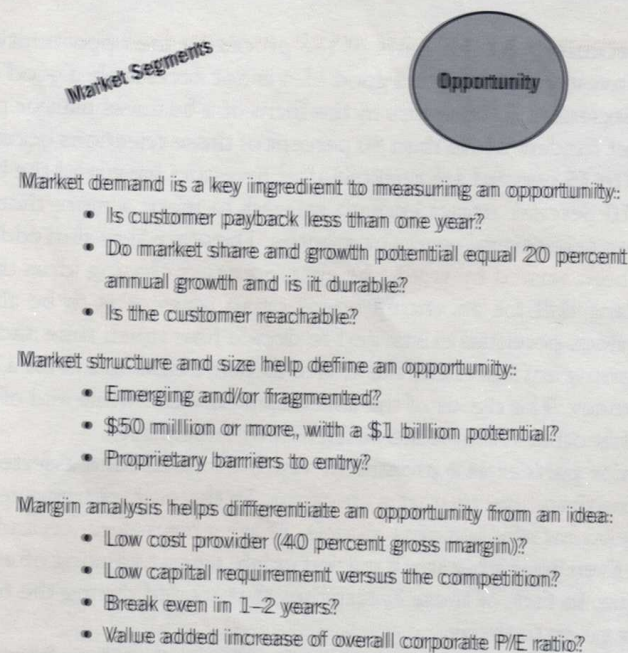
Exhibit 2.6 summarizes the most important characteristics of good opportunities. Underlying market demand—because of the value-added properties of the product or service, the market's size and 20-plus percent growth potential, the economics of the business, particularly robust margins (40 percent or more), and free cash flow characteristics—drives the value creation potential.

We build our understanding of opportunity by first focusing on market readiness: the consumer trends and behaviours that seek new products or services. Once these emerging patterns are identified, the aspiring entrepreneur develops a service or product concept and, finally, the service or product delivery system is conceived. We then ask the questions articulated in the exhibit.

These criteria will be described in more detail in Chapter 4 and can be applied to the search and evaluation of any opportunity. In short, the greater the growth, size, durability, and robustness of the gross and net margins and free cash flow, the greater the opportunity. The more *imperfect* the market, the greater the opportunity. The greater the rate of change, the discontinuities, and the chaos, the greater is the opportunity. The greater the inconsistencies in existing service and quality, in lead times and lag times, and the greater the vacuums and gaps in information and knowledge, the greater is the opportunity.

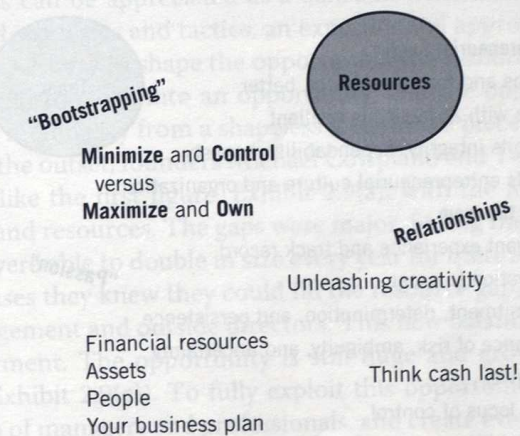
Resources: Creative and Parsimonious One of the most common misconceptions among untried entrepreneurs is that you first need to have all the resources in place, especially the money, to succeed with a venture. **Thinking money first is a big mistake.** Money follows high potential opportunities conceived of and led by a strong management team. Investors have bemoaned for years that there is too much money chasing too few deals. Some insist that there is a shortage of quality entrepreneurs and opportunities, not money. Successful entrepreneurs devise ingeniously creative and stingy strategies to marshal and gain control of resources (Exhibit 2.7). Surprising as it may sound, investors and successful entrepreneurs often say one of the worst things that can happen to an entrepreneur is to have *too much money too early*. This flies contrary to the most common advice from entrepreneurs: Get enough capital; then get some more.³² These seemingly clashing perspectives will be reconciled in due course.

EXHIBIT 2.6 The Entrepreneurial Process Is Opportunity Driven*



*Durability of an opportunity is a widely misunderstood concept. In entrepreneurship, durability exists when the investor gets his or her money back plus a market or better return on investment.

EXHIBIT 2.7 Understand and Marshal Resources, Don't Be Driven by Them



Howard Head is a wonderful example of succeeding with few resources. He developed the first laminate, metal-edged ski, which became the market leader, and then the oversize Prince tennis racket—developing two totally unrelated technologies is a rare feat. Head left his job at a large aircraft manufacturer during World War II and worked in his garage on a shoestring budget to create the modern ski. It took more than 40 iterations before he developed a ski that worked and could be marketed. He insisted that one of the biggest reasons he finally succeeded is that he had so little money. He argued that if he had complete financing he would have blown it all long before he evolved the ski into something that weighed half as much as solid wood skis and had better performance. Within a few years the Head Ski company was making the majority of skis in use. The company went on to diversify into tennis and other racquet sports and manufactured an aluminium honeycomb tennis racquet. Howard Head sold his venture and retired. Head played more tennis in retirement with the aid of a tennis ball machine (built by Prince Manufacturing). Howard Head became the majority shareholder and chairman of the board of Prince. While he worked to improve the ball machine, his own game of tennis never got better. He went on to patent the oversize racquet and develop graphite composites—changing the game of tennis forever.³³

Bootstrapping is a way of life in entrepreneurial companies and can create a significant competitive advantage. Doing more with less is a powerful competitive weapon. The necessary approach is to minimize and control the resources, not necessarily own them. Whether it is assets for the business, key people, the business plan, or start-up and growth capital, many successful entrepreneurs *think cash last*. Such strategies encourage a discipline of leanness, where everyone knows that every dollar counts, and the principle "conserve your equity" becomes a way of maximizing shareholder value.

The Entrepreneurial Team There is little dispute today that the entrepreneurial team is a key ingredient in the higher potential venture. Investors are captivated "by the creative brilliance of a company's head entrepreneur. . . and bet on the superb track records of the management team working as a group."³⁴ French-born Georges Doriot's dictum was: I prefer a grade A entrepreneur and team with a grade B idea, over a grade B team with a grade A idea. "In the world today, there's plenty of technology, plenty of entrepreneurs, plenty of money, plenty of venture capital. What's in short supply is great teams. Your biggest challenge will be building a great team."³⁵

"If you can find good people, they can always change the product. Nearly every mistake I've made has been I picked the wrong people, not the wrong idea."³⁶ Finally, as we noted earlier, ventures with more than 20 employees and \$2 million to \$3 million in sales are much more likely to survive and prosper than smaller ventures. In the vast majority of cases, it is very difficult to grow beyond this without a team of two or more key contributors.

Clearly, a new venture requires a lead entrepreneur that has personal characteristics described in Exhibit 2.8. But the high potential venture also requires interpersonal skills to foster communications and, therefore, team building.

EXHIBIT 2.8 An Entrepreneurial Team Is a Critical Ingredient for Success

An entrepreneurial leader

- Learns and teaches—faster, better
- Deals with adversity, is resilient
- Exhibits integrity, dependability, honesty
- Builds entrepreneurial culture and organization

Quality of the team

- Relevant experience and track record
- Motivation to excel
- Commitment, determination, and persistence
- Tolerance of risk, ambiguity, and uncertainty
- Creativity
- Team locus of control
- Adaptability
- Opportunity obsession
- Leadership and courage
- Communication

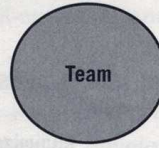


Exhibit 2.8 summarizes the important aspects of the team. These teams invariably are formed and led by a very capable entrepreneurial leader whose track record exhibits both accomplishments and several qualities that the team must possess. A pacesetter and culture creator, the lead entrepreneur is central to the team as both a player and a coach. The ability and skill in attracting other key management members and then building the team is one of the most valued capabilities investors look for. The founder who becomes the leader does so by building heroes in the team. A leader adapts a philosophy that rewards success and supports honest failure, shares the wealth with those who help create it, and sets high standards for both performance and conduct. We will examine in detail the entrepreneurial leader and the new venture team in Chapters 5 and 6.

Importance of Fit and Balance Rounding out the model of the three driving forces is the concept of fit and balance between and among these forces. Note that the team is positioned at the bottom of the triangle in the Timmons Model (Exhibit 2.5). Imagine the founder, the entrepreneurial leader of the venture, standing on a large ball, balancing the triangle over her head. This imagery is helpful in appreciating the constant balancing act since opportunity, team, and resources rarely match. When envisioning a company's future, the entrepreneur asks: What pitfalls will I encounter to get to the next boundary of success? Will my current team be large enough, or will we be over our heads if the company grows 30 percent over the next two years? Are my resources sufficient (or too abundant)? Vivid examples of the failure to maintain a balance are everywhere, such as when large companies throw too many resources at a weak, poorly defined opportunity. For example, Lucent Technologies' misplaced assumption and slowness to react to bandwidth demand resulted in an almost 90-percent reduction in market capitalization.

Exhibit 2.9 shows how this balancing act evolved for Mitel from inception through the initial public offering to British Telecom's purchase and later sell-off. While the drawings oversimplify these incredibly complex events, they help us to think conceptually—an important entrepreneurial talent—about the company building process, including the strategic and managerial implications of striving to achieve balance and the inevitable fragility of the process.

A telephony tone receiver was Mitel's first product to hit the market. Following Michael Cowpland's and Terry Matthews' success with the tone receiver, the founders saw the potential of microprocessors to revolutionize telephone equipment. The opportunities were huge in this rapidly growing field and they quickly expanded into semiconductors. Though short on significant capital or other resources, the team had big ideas. Such a

mismatch of ideas, resources, and talent could quickly topple out of the founder's control and fall into the hands of someone who could turn it into a real opportunity. Visually, the process can be appreciated as a constant balancing act, requiring continual assessment, revised strategies and tactics, an experimental approach. By addressing the types of questions necessary to shape the opportunity, the resources, and the team, the founder begins to mould the idea into an opportunity, and the opportunity into a business, just as you would mould clay from a shapeless form into a piece of artwork.

At the outset, founders Michael Cowpland and Terry Matthews would have seen something like the first figure, Exhibit 2.9(a), with the huge opportunity far outweighing the team and resources. The gaps were major. Seeing the size and potential of the opportunity they were able to double in size every year for quite a few years. With great faith and many promises they knew they could fill the resource gaps and build the team, both with inside management and outside directors. This new balance in Exhibit 2.9(b) creates a justifiable investment. The opportunity is still huge and growing, and competitors are inevitable (see Exhibit 2.9(c)). To fully exploit this opportunity, attract a large and highly talented group of managers and professionals, and create even greater financial strength than competitors, an influx of cash is often necessary. British Telecom purchased a controlling 51 percent of Mitel in 1985 and Cowpland and Matthews were out. Strategic investors can greatly enhance the balance of the driving forces. Strategic investors, or partners, are defined as those who can fill gaps left by other members of the team. They create balance where imbalance exists. The role of the strategic investor differs according to the needs of a venture. In 1990 British Telecom started looking for a buyer for their 'investment.' In 1992 Schroeders Ventures stepped in and bought out British Telecom. In 2001 Mitel was split in two. The PBX division and the company name were sold back to Terry Matthews; the semiconductor division was given the name Zarlink.

Mitel emerged (see Exhibit 2.9(d)) larger and stronger in people and resources but faced new challenges. Even the best and brightest of new ventures tend to erode over three or more decades into slow-moving, reactive firms. Could Mitel sustain and reinvent its entrepreneurial roots and organization as the opportunity continued to mushroom and competition for markets, people, and technology were greater than ever? Would it become blindsided and eclipsed by a new disruptive technology? It hoped that its merger with Inter-Tel and partnership with Sun Microsystems would take it in the right direction.

EXHIBIT 2.9(a) Mitel—Journey through the Entrepreneurial Process: At Start-up, a Huge Imbalance

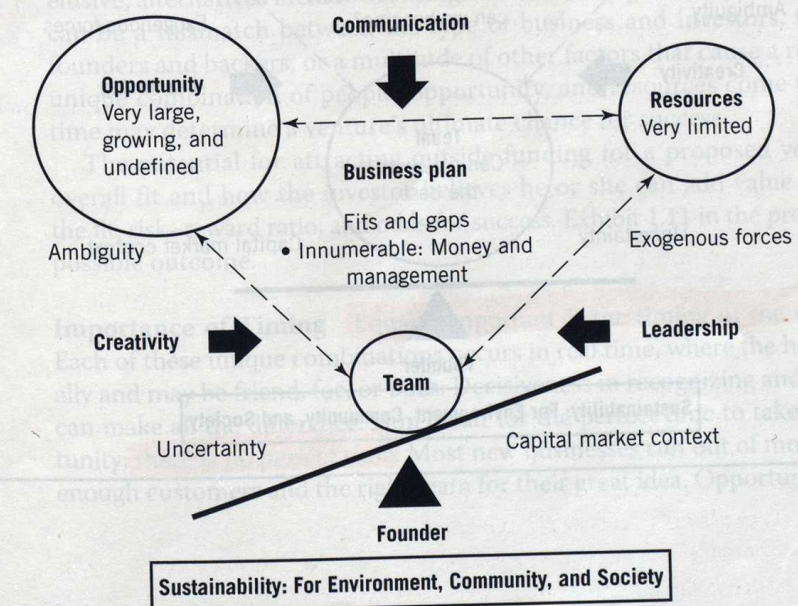


EXHIBIT 2.9(b) Mitel—Journey through the Entrepreneurial Process: At IPO, toward a New Balance

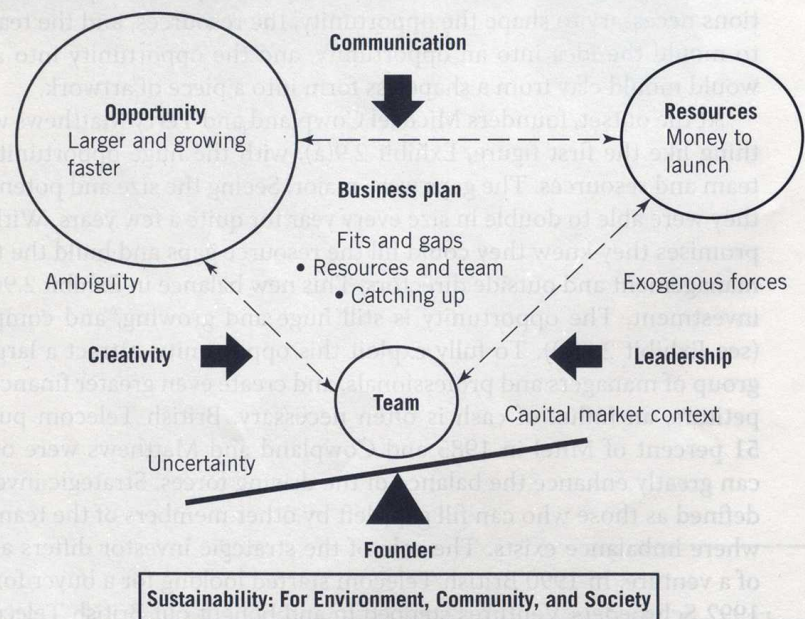


EXHIBIT 2.9(c) Mitel—Journey through the Entrepreneurial Process: British Telecom Steps In (and Then Out), a New Balance

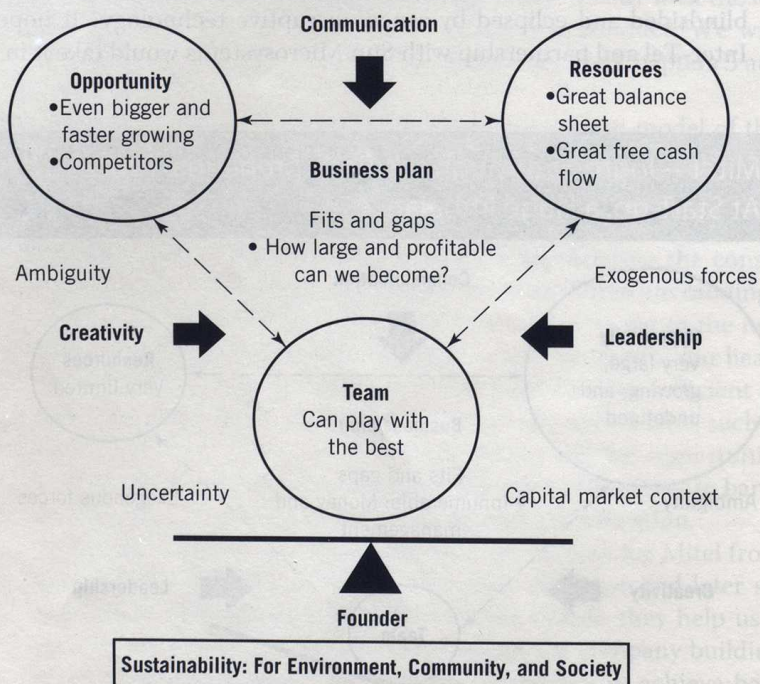
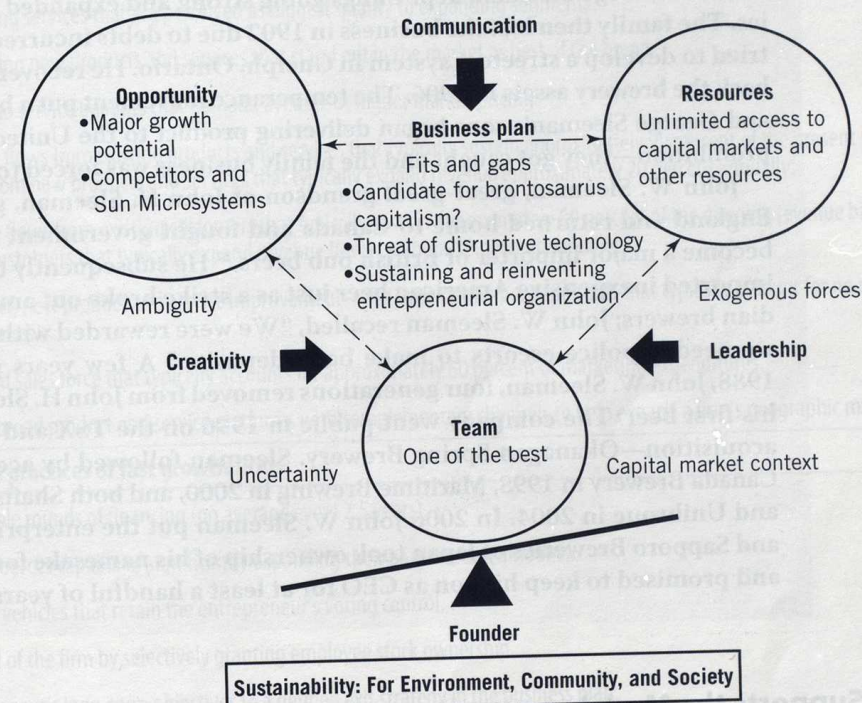


EXHIBIT 2.9(d) Mitel—Journey through the Entrepreneurial Process: Merger with Inter-Tel, a New Imbalance



This iterative entrepreneurial process is based on both logic and trial and error. It is both intuitive and consciously planned. It is a process not unlike what the Wright brothers originally engaged in while creating the first self-propelled airplane. They conducted more than 1,000 glider flights before succeeding. These trial-and-error experiments led to the new knowledge, skills, and insights needed to actually fly. Entrepreneurs have similar learning curves.

The fit issue can be appreciated in terms of a question: This is a fabulous opportunity, but for whom? Some of the most successful investments ever were turned down by numerous investors before the founders received financial backing. And even if investors remain elusive, alternatives include licensing and franchising to fuel growth. Time and again, there can be a mismatch between the type of business and investors, the chemistry between founders and backers, or a multitude of other factors that cause a rejection. Thus, how the unique combination of people, opportunity, and resources come together at a particular time may determine a venture's ultimate chance for success.

The potential for attracting outside funding for a proposed venture depends on this overall fit and how the investor believes he or she can add value to this fit and improve the fit, risk-reward ratio, and odds for success. Exhibit 1.11 in the previous chapter shows the possible outcome.

Importance of Timing Equally important is the timing of the entrepreneurial process. Each of these unique combinations occurs in real time, where the hourglass drains continually and may be friend, foe, or both. Decisiveness in recognizing and seizing the opportunity can make all the difference. Don't wait for the perfect time to take advantage of an opportunity; **there is no perfect time**. Most new businesses run out of money before they can find enough customers and the right team for their great idea. Opportunity is a moving target.

Beer: It Must Be in the Sleeman Family Blood

John H. Sleeman had been brewing beer in Canada since immigrating in 1834. His son, George Sleeman, kept things going strong and expanded to two breweries. The family then lost the business in 1902 due to debts incurred when George tried to develop a streetcar system in Guelph, Ontario. He recovered and bought back the brewery assets in 1906. The temperance movement put a hamper on sales and George Sleeman's sons began delivering product to the United States during prohibition—they got caught and the family business was forced to close in 1933.

John W. Sleeman, great-great grandson of John H. Sleeman, got married in England and returned home to Canada and fought government regulations to become a major importer of British pub beers.³⁷ He subsequently took a risk and imported inexpensive American beer just as a strike broke out among the Canadian brewers; John W. Sleeman recalled, "We were rewarded with so much cash we needed police escorts to make bank deposits." A few years passed and in 1988, John W. Sleeman, four generations removed from John H. Sleeman brewed his first beer. The company went public in 1996 on the TSX and made its first acquisition—Okanagan Spring Brewery. Sleeman followed by acquiring Upper Canada Brewery in 1998, Maritime Brewing in 2000, and both Shaftsbury Brewing and Unibroue in 2004. In 2006 John W. Sleeman put the enterprise up for sale and Sapporo Breweries of Japan took ownership of his namesake for \$400 million and promised to keep him on as CEO for at least a handful of years.

Recent Research Supports the Model

The Timmons Model evolved from Jeffrey Timmons' doctoral dissertation research at the Harvard Business School, about new and growing ventures. Over nearly four decades, the model has evolved and been enhanced by ongoing research, case development, teaching, and experience in high potential ventures and venture capital funds. The fundamental components of the model have not changed, but their richness and relationships of each to the whole have been steadily enhanced as they have become better understood. Numerous other researchers have examined a wide range of topics in entrepreneurship and new venture creation. The bottom line is that the model, in its simple elegance and dynamic richness, harnesses what you need to know about the entrepreneurial process in order to get the odds in your favour. As each of the chapters and accompanying cases, exercises, and issues expand on the process, addressing individual dimensions, a detailed framework with explicit criteria will emerge. If you engage this material fully, you cannot help but improve your chances of success.

A research effort focused on 906 high growth companies provides important benchmarks of the practices in a diverse group of industries.³⁸

Most significantly, these results reconfirm the importance of the model and its principles: the team, the market opportunity, the resource strategies, most of the individual criteria, the concept of fit and balance, and the holistic approach to entrepreneurship.

Exhibit 2.10 summarizes the 26 leading practices identified in four key areas: marketing, finance, management, and planning.

EXHIBIT 2.10 Leading Practices

Leading marketing practices of fast growth firms

- Deliver products and services that are perceived as highest quality to expanding segments.
- Cultivate pacesetter new products and services that stand out in the market as best of the breed.
- Deliver product and service benefits that demand average or higher market pricing.
- Generate revenue flows from existing products and services that typically sustain approximately 90 percent of the present revenue base, while achieving flows from new products and services that typically expand revenue approximately 20 percent annually.
- Generate revenue flows from existing customers that typically sustain approximately 80 percent of the ongoing revenue base, while achieving flows from new customers that typically expand revenue flows by about 30 percent annually.
- Create high impact, new product and service improvements with development expenditures that typically account for no more than approximately 6 percent of revenues.
- Utilize a high yield sales force that typically accounts for approximately 60 percent of marketing expenditures.
- Rapidly develop broad product and service platforms with complementary channels to help expand a firm's geographic marketing area.

Leading financial practices of fast growth firms

- Anticipate multiple rounds of financing (on average every 2.5 years).
- Secure funding sources capable of significantly expanding their participation amounts.
- Utilize financing vehicles that retain the entrepreneur's voting control.
- Maintain control of the firm by selectively granting employee stock ownership.
- Link the entrepreneur's long-term objectives to a defined exit strategy in the business plan.

Leading management practices of fast growth firms

- Use a collaborative decision-making style with the top management team.
- Accelerate organizational development by assembling a balanced top management team with or without prior experience of working together.
- Develop a top management team of three to six individuals with the capacity to become the entrepreneur's entrepreneurs. Align the number of management levels with the number of individuals in top management.
- Establish entrepreneurial competency first in the functional areas of finance, marketing, and operations. Assemble a balanced board of directors comprised of both internal and external directors.
- Repeatedly calibrate strategies with regular board of directors meetings.
- Involve the board of directors heavily at strategic inflection points.

Leading planning practices of fast growth firms

- Prepare detailed written monthly plans for each of the next 12 to 24 months and annual plans for three or more years.
- Establish functional planning and control systems that tie planned achievements to actual performance and adjust management compensation accordingly.
- Periodically share with employees the planned versus actual performance data directly linked to the business plan.
- Link job performance standards that have been jointly set by management and employees to the business plan.
- Prospectively model the firm based on benchmarks that exceed industry norms, competitors, and the industry leader.

Chapter Summary

1. We began to demystify entrepreneurship by examining its classic start-up definition and a broader, holistic way of thinking, reasoning, and acting that is opportunity obsessed and leadership balanced.
2. Entrepreneurship has many metaphors and poses many paradoxes.
3. Getting the odds in your favour is the entrepreneur's perpetual challenge.
4. Thinking big enough can improve the odds significantly. Higher potential ventures are sought by successful entrepreneurs, venture capitalists, and private investors.
5. The Timmons Model is at the heart of spotting and building the higher potential venture and understanding its three driving forces: the team, opportunity, and resources. The concept of fit and balance is crucial.
6. Research on entrepreneurs and their fast-growth ventures adds validity to the model.

Study Questions

1. Can you define what is meant by classic entrepreneurship and the high potential venture? Why and how are threshold concepts, cover your equity, bootstrapping of resources, fit, and balance important?
2. "People don't want to be managed, they want to be led." Explain what this means and its importance and implications for developing your own style and leadership philosophy.
3. What are the most important determinants of success and failure in new businesses? Who has the best and worst chances for success, and why?
4. What are the most important things you can do to get the odds in your favour?
5. What criteria and characteristics do high growth entrepreneurs, venture capitalists, and private investors seek in evaluating business opportunities? How can these make a difference?
6. Define and explain the Timmons Model. Apply it and graphically depict, as in the Mitel example, the first five years or so of a new company with which you are familiar.
7. What are the most important skills, values, talents, abilities, and mind-sets one needs to cultivate as an entrepreneur?

Mind Stretchers *Have you considered?*

1. Who can be an entrepreneur? When?
2. More than 80 percent of entrepreneurs learn the critical skills they need after age 21. What does this mean for you?
3. In your lifetime, the odds are that leading firms today such as Sony, Research In Motion, Apple, Air Canada, McDonald's, and the Gap will be knocked off by upstarts. How can this happen? Why does it present an opportunity, and for whom?
4. What do you need to be doing now, and in the next 12 months, to get the odds in your favour?
5. List 20 ideas and then pick out the best two that might be an opportunity. How can these become opportunities? Who can make them opportunities?
6. How many different ways can a new venture go off the tracks?

EXERCISE Visit with an Entrepreneur and Create a Lifelong Learning Log

Through an interview with entrepreneurs who have, within the past 5 to 10 years, started firms with significant growth and are profitable, you can gain insight into an entrepreneur's reasons, strategies, approaches, and motivations for starting and owning a business. Gathering information through interviewing is a valuable skill to practise. You can learn a great deal in a short time through interviewing if you prepare thoughtfully and thoroughly.

The Visit with an Entrepreneur Exercise has helped students interview successful entrepreneurs. While there is no right way to structure an interview, the format in this exercise has been tested successfully on many occasions. A breakfast, lunch, or dinner meeting is often an excellent vehicle.

Select two entrepreneurs and businesses about which you would like to learn. This could be someone you see as an example or role model to which you aspire, or which you know the least about but are eager to learn. Interview at least two entrepreneurs with differing experiences, such as a high potential (e.g., \$5 million revenue plus) and a lifestyle business (usually much smaller, but not necessarily).

Create a Lifelong Learning Log

Create a computer file or acquire a notebook or binder in which you record your goals, triumphs and disappointments, and lessons learned. This can be done as key events happen or on some other frequent basis. You might make entries during times of crisis and at year's end to sum up what you accomplished and your new goals. The record of personal insights, observations, and lessons learned can provide valuable anchors during times of difficult decisions as well as interesting reading—for you at least.

A Visit with an Entrepreneur

Step 1 Contact the person you have selected and make an appointment.

Be sure to explain why you want the appointment and to give a realistic estimate of how much time you will need.

Step 2 Identify specific questions you would like to have answered and the general areas about which you would like information. (See The Interview in STEP 3.)

Using a combination of open-end questions, such as general questions about how the entrepreneur got started, what happened next, and so forth, and closed-end questions, such as specific questions about what his or her goals were, if he or she had to find partners, and so forth, will help keep the interview focused and yet allow for unexpected comments and insights.

Step 3 Conduct the interview.

Recording this interview on audiotape can be helpful and is recommended unless you or the person being interviewed objects. Remember, too, that you most likely will learn more if you are an interested listener.

The Interview

Questions for Gathering Information

- Would you tell me about yourself before you started your first venture?

Who else did you know while you were growing up who had started or owned a business, and how did they influence you? Anyone later, after you were 21 years old?

Were your parents, relatives, or close friends entrepreneurial? How so?

Did you have role models?

What was your education/military experience? In hindsight, was it helpful? In what specific ways?

Did you have a business or self-employment during your youth?

In particular, did you have any sales or marketing experience? How important was it, or a lack of it, to starting your company?

When, under what circumstances, and from whom did you become interested in entrepreneurship and learn some of the critical lessons?

- Describe how you decided to create a job by starting your venture instead of taking a job with someone else.

How did you spot the opportunity? How did it surface?

What were your goals? What were your lifestyle needs or other personal requirements? How did you fit these together?

How did you evaluate the opportunity in terms of the critical elements for success? The competition? The market? Did you have specific criteria you wanted to meet?

Did you find or have partners? What kind of planning did you do? What kind of financing did you have?

Did you have a start-up business plan of any kind? Please tell me about it.

How much time did it take from conception to the first day of business? How many hours a day did you spend working on it?

How much capital did it take? How long did it take to reach a positive cash flow and break-even sales volume? If you did not have enough money at the time, what were some ways in which you bootstrapped the venture (bartering, borrowing, and the like)? Tell me about the pressures and crises during that early survival period.

What outside help did you get? Did you have experienced advisors? lawyers? accountants? tax experts? patent experts? How did you develop these networks and how long did it take?

How did any outside advisors make a difference in your company?

What was your family situation at the time?

What did you perceive to be the strengths of your venture? Weaknesses?

What was your most triumphant moment? Your worst moment?

Did you want to have partners or do it solo? Why?

• Once you got going:

What were the most difficult gaps to fill and problems to solve as you began to grow rapidly?

When you looked for key people as partners, advisors, or managers, were there any personal attributes or attitudes you were particularly seeking because you knew they would fit with you and were important to success? How did you find them?

Are there any attributes among partners and advisors that you would definitely try to avoid?

Have things become more predictable? Or less?

Do you spend more time, the same amount of time, or less time with your business now than in the early years?

Do you feel more managerial and less entrepreneurial now?

In terms of the future, do you plan to harvest? To maintain? To expand?

In your ideal world, how many days a year would you want to work? Please explain.

Do you plan ever to retire? Would you explain?

Have your goals changed? Have you met them?

Has your family situation changed?

What do you learn from both success and failure?

What were/are the most demanding conflicts or trade-offs you face (e.g., the business versus personal hobbies or a relationship, children, etc.)?

Describe a time you ran out of cash, what pressures this created for you, the business, your family, and what you did about it. What lessons were learned?

Can you describe a venture that did not work out for you and how this prepared you for your next venture?

Questions for Concluding

- What do you consider your most valuable asset, the thing that enabled you to make it?
- If you had it to do over again, would you do it again, in the same way?
- As you look back, what do you believe are the most critical concepts, skills, attitudes, and know-how you needed to get your company started and grown to where it is today? What will be needed for the next five years? To what extent can any of these be learned?
- Some people say there is a lot of stress being an entrepreneur. What have you experienced? How would you say it compares with other "hot seat" jobs, such as the head of a big company, or a partner in a large law or accounting firm?
- What things do you find personally rewarding and satisfying as an entrepreneur? What have been the rewards, risks, and trade-offs?
- Who should try to be an entrepreneur? And who should not?
- What advice would you give an aspiring entrepreneur? Could you suggest the three most important lessons you have learned? How can I learn them while minimizing the tuition?
- Would you suggest any other entrepreneur I should talk to?
- Are there any other questions you wished I had asked, from which you think I could learn valuable lessons?

Step 4 Evaluate what you have learned.

Summarize the most important observations and insights you have gathered from these interviews. Contrast especially what patterns, differences, and similarities exist between lifestyle and high potential entrepreneurs. Who can be an entrepreneur? What surprised you the most? What was confirmed about entrepreneurship? What new insights emerged? What are the implications for you personally, your goals, career aspirations?

Step 5 Write a thank you note.

This is more than a courtesy; it will also help the entrepreneur remember you favourably should you want to follow up on the interview.

CASE SHOEGURU.CA

Preparation Questions

1. What items or options can ShoeGuru provide in the proposal to attract the distributor?
2. How can ShoeGuru convince the distributor that it has the ability to be an effective partner?
3. Does ShoeGuru and its model provide any sustainable competitive advantage that would be hard to recreate by competitors? Does ShoeGuru have any competitive disadvantages with its model?

Introduction

It was a regular afternoon at the college. Tom Jablonski set up his PowerPoint presentation quietly in a computer lab. Tom had a new business proposal for his company and wanted to gain some insight from professors at the college before pursuing it. He found that the growth of his company was slowing and was essentially limited by his current situation. Business could not continue this way and something needed to change. A solution Tom thought up was that rather than having his company, ShoeGuru, responsible for shipping to customers, he would ask the distributor to take care of shipping for him. This would allow Tom to focus on the global market and pursue the desired growth opportunities for his company. He felt that this proposal would be advantageous for both parties; ShoeGuru could increase its revenue due to the removal of inventory constraints and his distributor would benefit by selling more shoes. Was there enough trust for Tom to convince his distributor to accept this proposal? Could Tom, a college student, really offer that much benefit to a large distributor?

Tom and ShoeGuru

Tom was in his second year of commerce at an Edmonton college. Tom was also an avid entrepreneur, and current owner and operator of ShoeGuru.ca. He entered the world of online sales with visions of opportunities. He found a distributor in the United States that had fashionable English sporting shoes and decided to start up his company, ShoeGuru, selling these shoes online. He had never actually met in person with his current distributor. His distributor was unaware of his age and the fact that he was still a student in college. All contact between the two parties had been made over the phone and the Internet. Tom viewed this as an advantage because it gave him the opportunity to establish himself as a serious businessperson and to be taken seriously—rather than as just a student.

Tom started ShoeGuru during his first year at the college. With a bit of financial support from his dad and some Web site design help from his friends, he opened a business selling shoes targeting men on the Internet. Tom was not your average student at the college; while other students focused on studying and living the college life, Tom devoted his time to an entrepreneurial aspiration to make money. Most students chose to finish their education before pursuing such endeavours, but not Tom. He is greatly enticed by the many different opportunities that exist in the world of business and feels it would be a waste not to get a head start. A close friend

of Tom's is involved in the online car import business. Tom actively observed many of his friend's successes and saw a clear opportunity that existed in the area of online shopping.

ShoeGuru and the Online Market

ShoeGuru was a self-managed online company specializing in the sale of fashionable men's footwear. Since launching his Web site ShoeGuru.ca, in July 2007, Tom had already been nominated in the category of "top 20 e-commerce Web site designs" by www.tutorialblog.org. With the help of a local Web designer Tom was able to develop an interactive Web site where the shoes featured were positioned and displayed in different environments rather than the common white, one dimensional background. Online shoppers could not only see the shoe, but could flip it around and look at it from different angles and views giving them a better idea of the styles and specific features of each individual shoe. Tom's success had been built on ShoeGuru's customer service, quality of products, free shipping within Canada, and low competitive pricing worldwide.

It has been predicted by many that sales in online shopping would more than double in the next five years. Tom recollected reading a global Internet survey that concluded that online consumers spend 15 percent of their total shopping dollars on the online market, and that this number would jump to 36 percent in the next three years. People were becoming more amenable to purchasing products and services online. In addition, the Internet market's growth had been attributed to increased security measures. Payment methods such as PayPal had added very secure means for online payments. This payment system was readily available for use by many different online vendors. ShoeGuru was one of the many Web sites that chose to use PayPal for secure payment transactions. As the online shopping market grew, so had methods of online marketing and advertising. In recent years online advertising had developed rapidly, helping to target consumers with interests in certain products. With essentially free methods of storage and data transferring, online companies found fewer constraints to enter the market.

Some of the major companies that existed on the Internet took full advantage of the online market. By eliminating the physical store from the shopping equation they were able to offer lower prices. The main concept held by them was that if they could offer products for cheaper prices on the Internet, people would be more attracted to buy online. The customers they were trying to attract were the people who wanted to save money. These store Web sites often consisted of a crowded

This case was written by Gordon Lucyk and Daniel Mireault (both of Grant MacEwan University) for purposes of classroom discussion.

layout. They were "busy," containing many smaller images that they hoped would catch the average Internet user's eyes. Most Web sites had a relatively standard design and Tom believed that there was not one shoe site that really stood out from the rest. This standard design divided the site into a men's section, women's section, and sometimes a children's section. Most of these companies had large inventories and tried to position themselves in Google's search engines to receive high amounts of traffic. Tom thought that one of the main customers these companies were not supplying was the person who sought the shopping experience; going to the store, holding the shoe and seeing how it may look on them. Could this type of shopper be attracted to online shopping? One of the biggest fears with buying clothing and accessories online was that they wouldn't fit. The aforementioned survey also suggested that another reason consumers worry most about online shopping was high shipping costs. Could there be a supplier in the market that could overcome these worries and convince more shoppers into buying wearable merchandise? Tom felt there was and wanted to develop his business around these ideas. ShoeGuru made it very clear on their Web site that customers should feel free to contact Tom about any concerns relating to fit or other specific details.

SHOEGURU.CA WEB SITE

We here at ShoeGuru believe that shoes should be both comfortable and fashionable. That is why we shop the world for the most modern and conventional fashions to make your feet both look and feel good. Unlike other stores we offer a variety of services to help our customers find what they're looking for through more interactive methods. With our Fashion Weekly section, customers can see and get a feel for the products before they buy, through photos, reviews and much more.

ShoeGuru thrives on customer satisfaction and if you have any questions concerns or even want some advice, please feel free to contact our shoe experts. We stand behind every item we sell and inspect everything to make sure that it is of the highest quality. We are very confident that we can cater to your fashion footwear needs and hope to do business with you very soon.

Was online shopping really that different from shopping at the mall? Tom believed that most malls had two common types of stores; the discount store where you go to save money, and the store where you go to find the latest trends. The stores where you go to save money were usually larger, dull, and had lots of products. The customer service you received at a store like this was usually minimal. The trendy stores offered an upscale atmosphere, mannequins, and tried to offer a better customer experience. The customer service was usually much greater at these stores and sometimes the sales associates would even offer an opinion on how the products look. One of the main focuses of ShoeGuru's Web site was to recreate the same atmosphere that you got from going to a trendy store into an online format.

In Tom's opinion, ShoeGuru offered a superior Web layout than its competitors. They not only wanted to sell shoes, they also wanted to offer a shopping experience. They followed the concept of what a customer would experience in going to the mall. Tom felt that the trendier the store looked, the more likely you were to check it out. Currently ShoeGuru did minimal advertising, as their Web layout alone attracted enough

potential buyers. ShoeGuru hoped to use advertising such as AdWords by Google in the future. This would offer the potential for millions of online consumers to be directed to their Web site whenever searches relating to shoes were placed on Google. It would allow them to narrow in on their target market and select search terms they wanted to be associated with, such as "men's shoes" or "fashionable footwear." ShoeGuru was currently being published in a book on "1,000 best Web designs of the year," and had a feature article in an issue of the online magazine ImportOnly. Tom was striving to take the Internet shopping experience to the next level by treating customers as individuals with specific needs. He wanted to develop real-life advertising that provided the shopper with the ability to get an accurate perspective of the product. He wanted to attract more than just the customer who thinks prices are cheaper on the Internet. He wanted to attract the customer looking for the latest trends.

In pursuing these fashionable markets Tom also saw great potential in the global market. A main benefit from being an online company was that the seller was essentially connected to the world market. ShoeGuru had staff that spoke three languages fluently, and many of ShoeGuru's sales were currently to customers in European countries. The fashionable men's footwear sector showed potential for strong European market growth. Tom thought that with proper research on the global market, expansion could truly be remarkable for a company that possessed the ability to supply it. ShoeGuru hoped to gain the ability to access these markets as well as local markets more effectively and efficiently.

ShoeGuru and Basement Inventory

ShoeGuru's business idea of where it wanted to be was pretty much established; the uncertainty lay in how it would get there. Tom currently found himself operating his business from his basement. The shoe inventory in his basement was something he was tired of being surrounded by. Inventory was also a huge limiting factor for Tom right now. Tom currently had to carefully select what he was going to order from the distributor to make sure it sold well. If the shoes he selected did not have a fast turnover rate, inventory accumulation became excessive, and his working capital became a concern. This prevented him from ordering new products and staying up to date with current trends.

As inventory has accumulated, Tom has reduced his selection of items and has removed product descriptions from his Web site, leaving blank spaces. These spaces have in part developed as a result of Tom's struggle with inventory. The benefits gained by having his basement full of shoes are no longer worth it for him. Tom is tired of being constrained by the lack of new inventory. Many growth opportunities exist in markets all over the world if he could just overcome the problems of inventory.

Tom felt the need to change his supply model in order to move forward. He has considered many different alternatives in expanding his company in order to make it more profitable. One idea considered was finding inventory space in which he could store the shoes. He could rent or buy a large space and keep all his shipments of shoes in it until he shipped them to the customer. This idea would work but the costs of implementing it would be quite high. Organizing and maintaining the warehouse, as well as tracking shoe inventory would provide a new level of complexity, as well as a new level of cost. Another idea considered was to find a warehouse on the U.S. side of the bor-

der that could simplify the process. Instead of shipping the shoes from the U.S. into Canada, Tom could have the shoes shipped to a central location. Shipping across the border results in an extra expense; if Tom could reduce the amount of times his shoes had to cross borders he would be lowering his costs. The central location that would warehouse the shoes would result in an extra employee and also the costs of having a warehouse. Tom would have lowered expenses by eliminating double shipping, while increasing warehousing costs. This solution, like the previous ideas contemplated by Tom, was not all that attractive after he performed some analysis.

The next idea Tom came up with was to create a "drop-shipping" strategy in which the distributor took care of all the shipping. ShoeGuru simply would take the orders and relay them to the distributor to ship. This made a lot of sense because it allowed ShoeGuru to focus on the aspects of the business they were best at. They could focus on establishing their Web site, increasing their ad campaigns, and concentrate on taking care of their customers. By doing these three things Tom could establish a solid base and create the company he wanted ShoeGuru to be.

The first benefit Tom would gain would be to avoid the hassles of shipping. Every time Tom shipped a pair of shoes he had to receive the package from the distributor, open the package, check the package, re-seal the package, and then ship the package to the customer. By avoiding double shipping he could put more effort into other areas and simplify his business process. Double shipping held huge disadvantages for Tom. Crossing up to three borders every time a customer purchased a pair of shoes was becoming expensive. Another benefit was that Tom could offer his customers a larger selection of products. He could do this without having to store a single pair of shoes in his basement. This thought alone made him very happy. Tom then began to realize the opportunities that existed in cost savings. He began to calculate that the price of shoes could be decreased by \$30 to \$40 per pair, which is a savings of nearly 20 to 30 percent for the consumer. The cost savings were huge. This gave ShoeGuru great leverage in setting their prices online. Tom believed the opportunities were endless; he could even add a section onto the Web site for women's shoes if he wanted. The selection of shoes Tom could offer would increase greatly, giving shoppers a variety of styles to choose from. Tom would also be able to stay up to date with all the current trends. The opportunities Tom would gain from a drop-shipping proposal would be tremendously advantageous.

The First Phone Call

Tom thought over his ideas about the drop-shipping possibility. He came to the conclusion that it was a great idea and he should pursue it. That same day he made a phone call to his distributor. He had become familiar with most of the people in the office of the distributor and thought that introducing the idea to them would be a good place to start. He called and talked to one of the representatives from the distributor. He explained the business idea to them and stated how much it could increase sales. The response they gave was neutral and the main concern they conveyed regarded return policy. The distributor stated that their biggest fear was having to deal with potential returns and phone calls from customers.

In the past, ShoeGuru had a very low rate of returns from their customers. In fact there was only one incident to date; Tom mixed up two pairs of shoes prior to mailing them. The

incident actually had nothing to do with the customer being unsatisfied with the product. ShoeGuru currently offered a return policy in which they accepted shoes as long as the customer paid for return shipping. Tom felt this return policy was important in order to adhere to their customer-oriented service policy.

SHOEGURU.CA WEB SITE

Returns and Exchanges

Unworn merchandise may be returned for store credit or exchange. Merchandise must be returned within 30 days of purchase, in original packaging and in the same condition that it was received in. Customer is responsible for all shipping costs.

With this in mind, Tom felt confident he could take care of any returns that might occur. The proposed idea of the distributor shipping the shoes to customers still seemed good.

The Proposal

Tom now had to decide what he was going to do next. He decided that he should prepare a proposal that he would formally submit to the distributor. Tom started to prepare his proposal and was overcome by the many different questions that began to emerge. What items should the proposal include? How am I going to submit the proposal? When should I finish the proposal by?

The questions continued piling up. There were many different directions Tom could go with his proposal. He could offer the distributor a little more money to ship the shoes. The distributor would gain by selling more shoes and making more money. Was this enough though? Even if the distributor agreed would Tom be able to trust them to ship the shoes to his customers? Tom then thought he could create a shipping contract that was inversely related to volume. If Tom sold a small quantity of shoes from his Web site the distributor would collect a larger percentage of profit from Tom. If Tom sold large quantities of shoes the percentage collected would gradually go down. This would signal to the distributor that Tom was confident in his ability to sell large quantities of shoes and persuade the distributor to do business with him. Tom began to consider their relationship and realized both parties would have to work together to make the proposal a success. In exploring all this new information he decided to create a PowerPoint presentation and turn to a valuable resource he had for guidance; his instructors. Tom scheduled a meeting with instructors from the school's Negotiation, Supply Chain, Finance, and Accounting courses to deliver his primary pitch.

The October 10 Meeting

Tom set up his PowerPoint presentation quietly in a computer lab. Tom hoped to gain some valid insight, as the instructors possessed a great deal of experience and knowledge.

Tom presented his presentation to the instructors and explained his situation as in-depth as he could. He made sure everyone in the meeting had a clear understanding of his business process and continued by asking for some feedback. The first response he got was that the proposal seemed very good for ShoeGuru but lacked any incentive for a large distributor. Another response focused on the Internet side of things; was Tom aware of the threats that could result from having a Canadian Internet domain (www.ShoeGuru.ca)? If ShoeGuru

was to expand into a larger Internet retailer, customers may expect a dot-com domain (www.ShoeGuru.com). If ShoeGuru did not have rights to this domain anybody could operate the domain. Anything from ladies fashion reports to foot-fetish pornography could come up with the click of a button. This dot-com domain could be important in the long run. Tom would have to look into purchasing the domain, which could be very costly. An example of the ShoeGuru.ca Web site has been included in Exhibit 1.

The next instructor asked how Tom was going to present his proposal. Would he present it in person or was email good enough? Also, when was his deadline? Tom was not sure if he really had a deadline.

The next idea that came up was the concept of trust. Could Tom trust the distributor to represent the ShoeGuru name? The ShoeGuru Web site contained a 5–10 day shipping policy that Tom felt was important in satisfying customers. Would the distributor adhere to some of the main values of ShoeGuru, and if not was it still worthwhile to implement the drop-shipping policy? As complications continued to surface he realized there was still a lot to prepare for. The answers were certainly not coming as easily as he would have liked.

After the meeting he realized that he needed to review some fundamental issues. He questioned the relationship he had with the large distributor. Was the large distributor going to take him

seriously and take full responsibility for ShoeGuru's shipping? Could Tom maybe find another distributor that would be a better fit for him? Many distributors existed and maybe Tom was being unwise in only considering the first one he did business with.

Tom eventually concluded that business is about taking risks and decided to continue with his current distributor. Tom had many other things to review before making his next move on his proposed business solution, which was to call the main manager of the distributor and gain some more insight on the form his proposal should take.

The Second Phone Call and the Deadline

Tom sat at his kitchen table preparing what he was going to say in his next phone call. He reluctantly dialed the number of the distributor. The main manager of the distributor answered the phone. He and the manager began to talk about the proposal. The distributor said a written proposal would be fine as long as it included all the necessary details. A relative deadline was established, giving Tom a couple weeks to prepare. He was still left with a limited idea of what to include in the proposal.

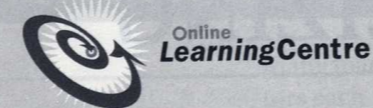
Three days later Tom's cellphone rang; it was the manager from the distributor. The manager said he was going on a vacation and needed the proposal by the end of the week. This gave Tom less than three days to complete and submit the proposal. He struggled to balance some studying for a midterm he had

the next day and began to compile a rough draft. After his class he went to get some last minute advice from a professor at the college. The professor gave Tom some guidelines to portray his proposal as mutually beneficial. He suggested a win-win approach would have to be present in order to be successful. In the previous meeting he mentioned that Tom made it sound like the distributor was doing him a favour. Tom needed to move away from that perception so that both parties would feel they were deriving benefit from the relationship.

Tom sat down and began to look at the advantages and disadvantages for ShoeGuru and his distributor. How could he construct this proposal to portray the mutual benefits each party would receive? ShoeGuru had a great chance to establish itself successfully in the online market. Tom didn't want to miss out on this opportunity. He was not sure if all the pieces were fitting together though. There were many things he might have been overlooking. He had never done anything

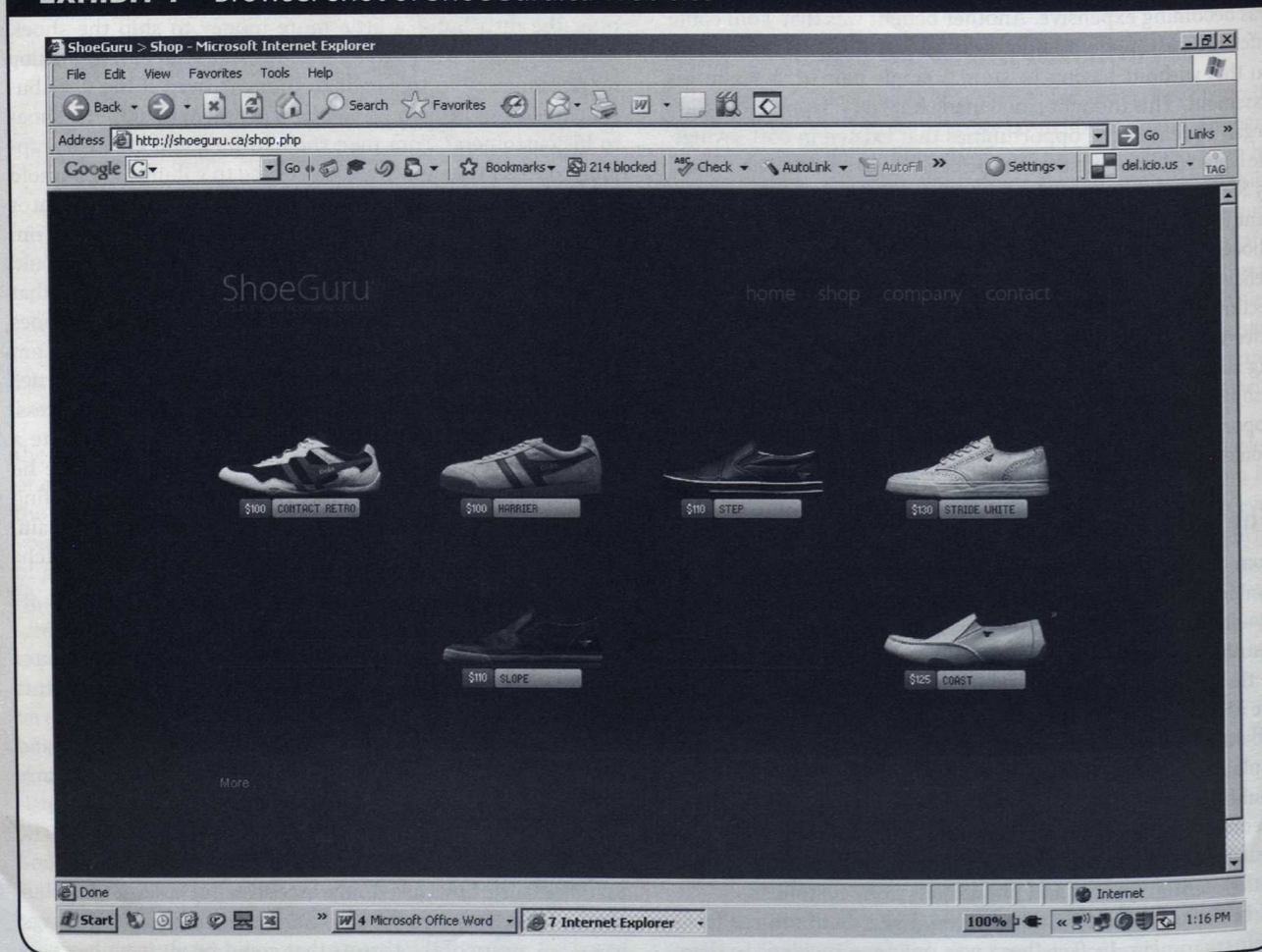
like this before and was worried that he was rushing in too quickly. At the same time he was worried that he would miss his opportunity. Tom began typing his proposal.

What conditions did Tom need to include in making the proposal a success? Tom was not sure if he should emphasize the benefits to the distributor and just mention the benefits of ShoeGuru, or if he should emphasize all the benefits of the proposal. How was Tom going to achieve this win-win mentality? What was the distributor expecting from him? As Tom began to write his proposal he began to feel like an average college student. The reality was Tom actually was a college student. What could the large distributor really gain from doing business with a college student? The world of business was a large sea of competition and Tom felt like a small fish with a good idea.



Find more great exercises and additional study tools on the Online Learning Centre at www.mcgrawhill.ca/olc/timmons

EXHIBIT 1 Browser shot of ShoeGuru.ca Web site



Source: Courtesy of ShoeGuru, www.shoeguru.ca.