

THE OPPORTUNITY: CREATING, SHAPING, RECOGNIZING, SEIZING

You miss 100 percent of the shots you don't take.

Wayne Gretzky

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

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| <p>RESULTS EXPECTED</p> | <ol style="list-style-type: none"> 1. Appreciate the importance of thinking big enough. 2. Assess opportunity via a zoom lens on the criteria used by successful entrepreneurs, angels, and venture capital investors in evaluating potential ventures. 3. Describe how the most successful ventures track a "circle of ecstasy" and match investors' appetites in "the food chain" for ventures. | <ol style="list-style-type: none"> 4. Differentiate between an idea and an opportunity. 5. Explain the role of ideas, pattern recognition, and the creative process in entrepreneurship. 6. Identify sources of information for finding and screening venture opportunities. | <p>RESULTS EXPECTED</p> |
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THINK BIG ENOUGH

Since its inception, *New Venture Creation* has attempted to inspire aspiring entrepreneurs to "think big enough." Time and again the authors have observed the classic small business owner who, almost like a dairy farmer, is enslaved by and wedded to the business. Extremely long hours of 70, 80, or even 100 hours a week, and rare vacations, are often the rule rather than the exception. And these hardworking owners rarely build equity, other than in the real estate they may own for the business. One of the big differences between the growth- and equity-minded entrepreneur and the traditional small business owners is

that the entrepreneur thinks *bigger*. Patricia Cloherty puts it this way: "It is critical to think big enough. If you want to start and build a company, you are going to end up exhausted. So you might as well think about creating a BIG company. At least you will end up exhausted and *rich*, not just exhausted!"

Her theme of thinking bigger is embedded throughout this book. How can you engage in a "think big" process that takes you on a journey treading the fine line between high ambitions and being totally out of your mind? How do you know whether the idea you are chasing is a worthy endeavour or a waste of time and energy? You can never know which side of the line you are on—and can stay on—until you try and until you undertake the journey. This is not to say that being big is all that matters. A small business owner may judge their effort to be a success even if the business does not pass a certain size threshold. There are examples of firms that remained small by staying within their objectives and remaining true to their strengths, resources, and capabilities or were limited by the scope of the opportunity. Further, a lifestyle or hobby enterprise may satisfy the proprietor for many years despite low margins or revenues. But for those of you wanting more, the content in this book should provide a solid basis for reaching those goals!

OPPORTUNITY THROUGH A ZOOM LENS

Many many proposals to launch new companies are turned down by venture capital investors each year. The opportunity recognition process is complex, subtle, and situational (at the time, in the market space, in relation to the investor's other alternatives, etc.). If the brightest, most knowledgeable, and most sophisticated investors in the world miss good opportunities and occasionally hop on board with the losers, we can conclude that the journey from idea to high potential opportunity is illusive, contradictory, and perilous. Think of this journey as a race through varied terrain and weather conditions. At times, the journey consists of full sunshine and straight, smooth highways, as well as twisting, turning, narrow one-lane passages that can lead to breathtaking views. Along the way you also will unexpectedly encounter fog, hail storms, white-out conditions, and freezing rain. All too often you seem to run out of gas and obstacles and hold-ups come when you least expect them. This is the entrepreneur's journey. As Aydin Mirzaee put it, "You have to make every decision right every step of the way." One wrong move and you're done. If too much equity is doled out too quickly, later round investors won't hop on board.

Transforming Caterpillars into Butterflies

This chapter is dedicated to making that journey friendlier by focusing a zoom lens on the opportunity. It shares the road maps and benchmarks used by successful (and unsuccessful) entrepreneurs, venture capitalists, angels, and other private equity investors in their quest to transform the often amorphous, fuzzy idea into a spectacularly prosperous venture. These criteria comprise the core of their due diligence to ascertain the viability and profit potential of the proposed business, and therefore, the balance of risk and reward. It will examine the role of ideas and pattern recognition in the creative process of entrepreneurship.

You will come to see the criteria used to identify higher potential ventures as jumping-off points at this rarefied end of the opportunity continuum, rather than mere endpoints. One to 10 out of 100 entrepreneurs create ventures that separate themselves from the pack. Scrutinized through our lens, these ventures reveal a highly dynamic, constantly moulding, shaping, and changing work of art, rather than a product of a formula or a meeting of certain items on a checklist. This highly organic and situational character of the entrepreneurial process underscores the criticality of determining *fit* and balancing *risk and reward*. As the authors have argued for decades: The business plan is obsolete as soon as it comes off the printer! It is in this shaping process that the best entrepreneurial leaders and investors add the greatest value to the enterprise and creatively transform an idea into a venture.

New Venture Realities

It is useful to put the realities faced by countless entrepreneurs into perspective. Consider the following fundamental realities as normal as you seek to convert your amorphous idea into a successfully realized outcome:

New Ventures: Fundamental Realities

- ✓ Most new ventures are works in process and not works of art. What you start out to do is not what you end up doing.
- ✓ Most business plans are obsolete at the printer.
- ✓ Onset Venture Partners¹ found that 91 percent of portfolio companies that followed their business plans failed!
- ✓ Speed, adroitness of reflex, and adaptability are crucial. Keep your knees bent!
- ✓ The key to succeeding is failing quickly and recouping quickly, and keeping the tuition low.
- ✓ Success is highly situational, depending on time, space, context, and stakeholders.
- ✓ The best entrepreneurs specialize in making “new mistakes” only.
- ✓ Starting a company is a lot harder than it looks, or you think it will be; but you can last a lot longer and do more than you think if you do not try to do it solo, and you don't give up prematurely.

These realities are intended to convey the highly transient, at times chaotic, nature of this beast, and the dynamic context within which most new ventures evolve. Such realities present so much room for the unexpected and the contradictory that it places a premium on thinking bold enough and doing everything you can to make sure your idea becomes an opportunity. Therefore, how can the aspiring entrepreneur think about this complex, even daunting challenge?

The Circle of Ecstasy and the Food Chain for Ventures

What most small businesses do not know, but what is a way of life in the world of high potential ventures, is what we will call the “circle of venture capital ecstasy” (Exhibit 3.1) and “the food chain for entrepreneurial ventures” (Exhibit 3.2). These concepts enable the

EXHIBIT 3.1 Circle of Venture Capital Ecstasy

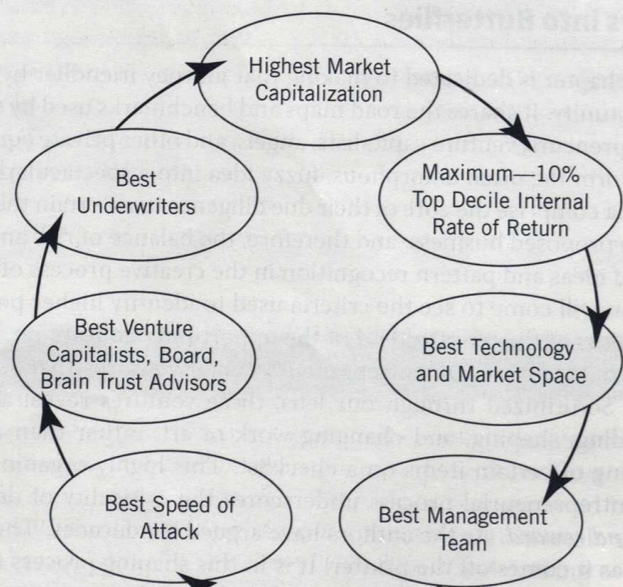


EXHIBIT 3.2 The Capital Markets Food Chain for Entrepreneurial Ventures

Stage of Venture	R&D	Seed	Launch	High Growth
Company Enterprise Value at Stage	Less than \$1 million	\$1–\$5 million	>\$1–\$50 million-plus	More than \$100 million
Sources	Founders High net worth individuals FFF* SR&ED,	FFF* Angel funds Seed funds SR&ED**	Venture capital series A, B, C... [†] Strategic partners Very high net worth individuals Private equity	IPOs Strategic acquirers Private equity
Amount of Capital Invested	Up to \$200,000	\$10,000–\$500,000	\$500,000–\$20 million	\$10–\$50 million-plus
% Company Owned at IPO	10–25%	5–15%	40–60% by prior investors	15–25% by public
Share Price and Number [‡]	\$.01–\$.50 1–5 million	\$.50–\$1.00 1–3 million	\$1.00–\$8.00+/- 5–10 million	\$12–\$18+ 3–5 million

* Friends, Families, and Fools

[†] Venture Capital Series A, B, C... (Average Size of Round)

Round	A	@ \$5.1 million—start-up
	B	@ \$8.1 million—product development
	C+	@ \$11.3 million—shipping product

Valuations vary markedly by industry (e.g., 2x)

Valuations vary by region and VC cycle

[‡] At Post-IPO

** Scientific Research and Experimental Development tax incentive program.

entrepreneur to visualize how the company building-investing-harvesting cycle works. Understanding this cycle and the appetites of different suppliers in the capital markets food chain enables you to answer the questions for *what* reason does this venture exist and for *whom*? Knowing the answers to these questions has profound implications for fundraising, team building, and growing and harvesting the company—or coming up short in any of these critical entrepreneurial tasks.

Exhibit 3.1 shows that the key to creating a company with the highest value (e.g., market capitalization) begins with identifying an opportunity in the “best technology and market space,” which creates the attraction for the “best management team.” Speed and agility to move quickly attracts the “best venture capitalists, board members, and other mentors and advisors” who can add value to the venture.

Exhibit 3.2 captures the food chain concept, which will be discussed again in greater detail in Chapter 9 “Financing the Venture.” Different players in the food chain have very different capacities and preferences for the kind of venture in which they want to invest. The vast majority of start-up entrepreneurs spend inordinate amounts of time chasing the wrong sources with the wrong venture. One goal in this chapter, and again in Chapter 9, is to provide a clear picture of what those criteria are and to grasp what “think big enough” means to the players in the food chain. This is a critical early step to avoid wasting time chasing venture capitalists, angels, and others when there is a misfit from the outset. As one CEO put it, “There are so many investors out there that you could spend the rest of your career meeting with them and still not get to all of them.” In fact, the problem is compounded when seeking angel or informal investors since there are a hundred times more of them than there are venture capitalists.

Why waste time thinking too small and on ventures for which there is no appetite in the financial marketplace? Knowing how capital suppliers and entrepreneurs think about the opportunity creation and recognition process, their search and evaluation strategies, and what they look for is a key frame of reference.

When Is an Idea an Opportunity?

The Essence: Four Anchors If an idea is not an opportunity, what is an opportunity? Superior business opportunities have the following four fundamental anchors:

1. They create or add significant value to a customer or end-user.
2. They do so by solving a significant problem, removing a serious pain-point, or meeting a significant want or need—for which someone is willing to pay a premium.
3. They have robust market, margin, and moneymaking characteristics that will allow the entrepreneur to estimate and communicate sustainable value to potential stakeholders.
4. They are a good fit with the founder(s) and management team at the time and marketplace—along with an attractive risk-reward balance.

For an opportunity to have these qualities, the “window of opportunity” is opening and will remain open long enough. Further, entry into a market with the right characteristics is feasible, and the management team is able to achieve it. The venture has or is able to gain a competitive advantage (i.e., to achieve leverage). Finally, the economics of the venture are rewarding and forgiving enough to allow for significant profit and growth potential.

To summarize: A superior opportunity has the qualities of being attractive, durable, and timely and is anchored in a product or service which creates or adds value for its buyer or end-user—usually by solving a very painful, serious problem.² The most successful entrepreneurs, venture capitalists, and private investors are opportunity-focused; that is, they start with what customers and the marketplace want, and do not lose sight of this.

The Real World

Opportunities are created, or built, using ideas and entrepreneurial creativity. Yet, while the image of a carpenter or mason at work is useful, in reality the process is more like the collision of particles in a nuclear reaction or like the spawning of hurricanes over the ocean. Ideas interact with real-world conditions and entrepreneurial creativity at a point in time. The product of this interaction is an opportunity around which a new venture can be created.

The business environment in which an entrepreneur launches his or her venture cannot be altered significantly. Despite assumptions often made concerning social and non-profit organizations, they also are subject to market forces and economic constraints. Consider, for instance, what would happen to donations if it were perceived that a non-profit organization was not reinvesting its surplus returns, but instead was paying management excessive salaries. Or what if a socially oriented organization concentrated all its efforts on the social mission, while neglecting revenues? Clearly, dealing with suppliers, production costs, labour, and distribution is critical to the health of these social corporations. Thus, social and non-profit organizations are just as concerned with positive cash flow and generating sufficient cash flows, even though they operate in a different type of market than for-profit organizations. For-profit businesses operate in a free enterprise system characterized by private ownership and profits.

Spawners and Drivers of Opportunities

In a free enterprise system, changing circumstances, chaos, confusion, inconsistencies, lags or leads, knowledge and information gaps, and a variety of other vacuums in an industry or market spawn opportunities.

Changes in the business environment and the ability to anticipate these changes are so critical in entrepreneurship that constant vigilance for changes is a valuable habit. An entrepreneur with credibility, creativity, and decisiveness can seize an opportunity while others study it.

Opportunities are situational. Some conditions under which opportunities are spawned are idiosyncratic, while at other times they are generalizable and can be applied to other industries, products, or services. In this way, cross-association can trigger in the entrepreneurial mind the crude recognition of existing or impending opportunities. It is often

assumed that a marketplace dominated by large, multi-billion-dollar players is impenetrable by smaller, entrepreneurial companies. You can't possibly compete with entrenched, resource-rich, established companies. The opposite can be true for several seasons. It can take three to five years or more for a large company to change its strategy and even longer to implement the new strategy, since it can take 10 years or more to change the culture enough to operate differently. For a new or small company, 10 or more years can be forever.³ It may even be easier for a large company to try something new by adopting a new name or spinning off a new division. General Motors created Saturn in 1985 to try something different and more recently distanced itself from Hummer. Air Canada Jazz is separate from Air Canada. In 2001 Air Canada launched Tango, the same year that Canada 3000 went bankrupt. In 2002 Air Canada launched Zip. Though Zip operated as a totally separate airline it was dissolved in 2004. Tango—short for “Tan and Go”—competed against the likes of Air Transat in the lucrative southern winter destination markets and like Zip the plug was pulled on Tango in 2004.

Some of the most exciting opportunities have come from fields the conventional wisdom said are the domain of big business: technological innovation. The performance of smaller firms in technological innovation is remarkable—95 percent of the radical innovations since World War II have come from new and small firms, not the giants. According to Tom Brzustowski, president of the Natural Sciences and Engineering Research Council from 1995 to 2005:

As far as innovations are concerned, with the exception of Nortel, I believe that all radical innovations in Canada have come from companies with fewer than 10,000 employees. Take Magna, though a large company by Canadian standards, its radical innovation—pressure forming—emerged from one of their small constituent companies.

Commercialization of radical innovations is not the same as being the source of the IP behind the innovation. The companies that produced the radical innovations may have acquired somebody else's intellectual property to do it.

In his book, *The Way Ahead*, Tom Brzustowski calls “for entrepreneurial managers in companies of all sizes in all sectors to be on the prowl for opportunities to add new value in what they do and make, and thus to produce innovations that will let them operate in a price-setting mode.”⁴

There can be exciting opportunities in ordinary businesses that might never get the attention of venture capital investors. The revolution in microcomputers, management information systems (MIS), and computer networking had a profound impact on a number of businesses that had changed little in decades. The used-auto-parts business had been stagnant for generations. Yet, the team at Pintendre Auto Inc., saw a new opportunity in this field by applying the latest computer and information technology to a traditional business that relied on crude, manual methods to track inventory and find parts for customers.⁵ In just three years, Pintendre Auto grew to \$16 million in sales. Today this Québec-based enterprise owns and operates over 100 facilities in the U.S. and Canada.

Technology and regulatory changes have profoundly altered and will continue to alter the way we conceive of opportunities. Cable television with its hundreds of channels came of age in the 1990s and brought with it new opportunities in the sale and distribution of goods from infomercials to shopping networks to pay-per-view. The Internet has created an even more diverse set of opportunities in sales and distribution, most notably Amazon.com, iTunes, Craigslist, Priceline, YouTube, and eBay.

Consider the following example that illustrates the phenomenon of vacuums in which opportunities are spawned:

Bulldog Fitness for Kids

Bulldog Interactive Fitness was opened by Holly Bond as a gym for youth in Dartmouth, Nova Scotia. This innovative kids-only fitness centre was developed to fill a market need. With so many overweight children, largely the result of a sedentary lifestyle (TV, computer, videogames), she asked why not combine gaming with exercise? “She went looking for a high-tech solution, but found no specialized equipment on the market... Bond sensed a gap and decided to capitalize on the opportunity.”⁶

The gym, targeted at getting the "Xbox generation" off the couch, opened in 2005 after nearly a year of hard work and research. Holly became a certified personal trainer and with her husband drew up a business plan and secured financing, all in secrecy. "We didn't even tell our best friends what we were doing," said Bond. "We were so afraid that someone else was going to do it first." Niche fitness chains like women-only Curves and Sisters Pace Fitness proved that demographic-specific gyms could access a market that others missed.

About a year and half into operations, Bond decided to franchise. "It was always our intention to franchise," says Bond, "but we thought we'd be doing that later, maybe in three or four years, once we had a few of our own open." With a steady stream of enquiries and \$200,000 from angel investors in Halifax the franchising began. The interactive equipment was a hit, exercise bikes provided input to PlayStation games on big wall mounted screens, rowing machines hooked up to display the user competing with others and escaping from sea monsters, Dance Dance Revolution, a rock climbing treadmill, Wii stations, and many others—including some old fashioned dodge-ball type activities—kept the business and business model thriving.⁷

With a handful of Canadian franchises and some U.S. ones in the works, Holly Bond expected the brand to explode. She publicly shared her ambitious goal of 400 franchises worldwide by 2011. She picked up a 2007 Export Achievement Award and admitted, "We're all exhausted, but it's an exciting exhausted." With her sights set on launching a DVD, writing a book, developing a line of kid-size workout equipment, and creating a TV show, she caught the attention of DHX Media Ltd., an independent producer and distributor of TV programming and interactive content. David Regan, executive VP at DHX Media said, "We've been tracking these guys for awhile as they've been refining their model and think they've come a long way from where they started out." DHX Media acquired Bulldog Interactive Fitness Inc. for \$625,000 and 99,333 shares in DHX (locked for one year). Bond stayed on at the helm and additional compensation was tied to meeting financial performance benchmarks. Holly indicated, "There is a huge amount of synergy between the two companies and this allows us to operate at an entirely new level."⁸ A Bulldog Interactive Fitness franchise started with a fee of \$34,900, capital costs of between \$250,000 and \$400,000, and royalty fees of 7 percent gross sales and 2 percent for national advertising.

Exhibit 3.3 summarizes the major types of discontinuities, asymmetries, and changes that can result in high potential opportunities. Creating such changes through technical innovation (PCs, wireless telecommunications, Internet servers, software), influencing and creating the new rules of the game (airlines, telecommunications, financial services and banking, medical products), and anticipating the various impacts of such changes is central to recognizing opportunities.

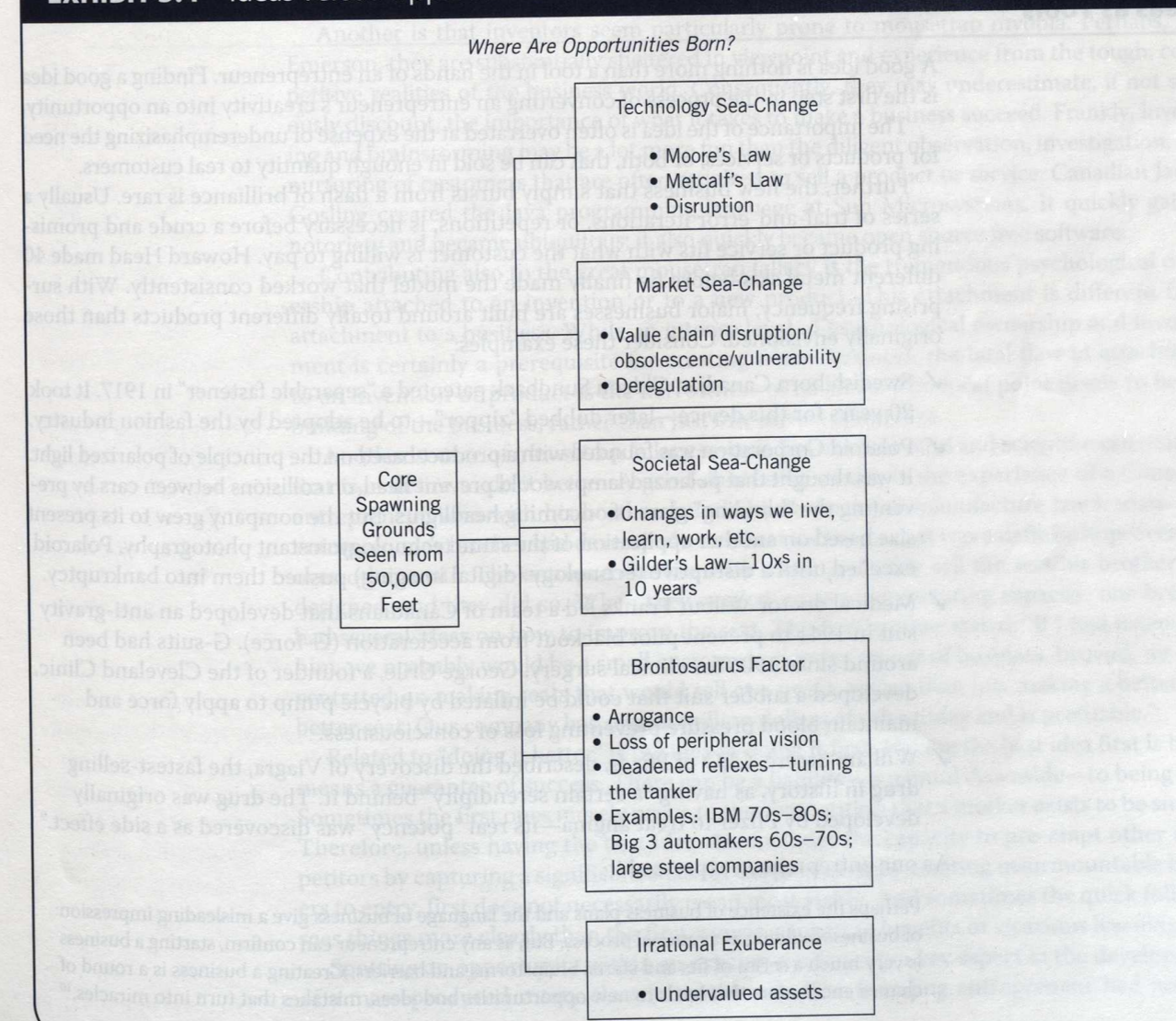
Search for Sea-Changes

A simple criterion for the highest potential ventures comes from Vancouver's Ventures West, "We target companies that are addressing worldwide markets which are large enough to allow the portfolio company to grow to a significant size." Garage Technology Ventures states: "We're looking to invest in entrepreneurial teams with big ideas and a need for seed capital to turn their ideas into great companies. We are willing to invest in unproved teams attacking unproved markets with unproved solutions." The best place to start in seeking to identify such ideas in a macro sense is to identify significant sea-changes that are occurring or will occur. Think of the profound impact that personal computing, biotechnology, and the Internet have had on the past generation. The great new ventures of the next generation will come about by the same process and will define these next great sea-changes. Exhibit 3.4 summarizes some categories for thinking about such changes. These include

EXHIBIT 3.3 Summary of Opportunity Spawners and Drivers

Root of Change/Chaos/Discontinuity	Opportunity Creation
Regulatory changes	Airlines, insurance, telecommunications, medical, pension fund management, financial services, banking, tax laws and securities regulations.
10-fold change in 10 years or less	Moore's Law—computer chips double productivity every 18 months: financial services, private equity, consulting, Internet, biotech, information age, publishing
Reconstruction of value chain and channels of distribution	Superstores—Loblaws, Wal-Mart; publishing; automobiles; Internet sales and distribution of all services
Proprietary or contractual advantage	Technological innovation: patent, licence, contract, franchise, copyrights, distributorship
Existing management/investors burned out/undermanaged	Turnaround, new capital structure, new breakeven, new free cash flow, new team, new strategy; owners' desires for liquidity, exit; telecom, waste management service, retail businesses
Entrepreneurial leadership	New vision and strategy, new team equals secret weapon; organization thinks, acts like owners
Market leaders are customer obsessed or customer blind	New, small customers are low priority or ignored: hard disk drives, paper, chemicals, mainframe computers, centralized data processing, desktop computers, corporate venturing, office superstores, automobiles, software, most services

EXHIBIT 3.4 Ideas versus Opportunities: Search for Sea-Changes



technology, market and societal shifts, and even opportunities spawned from the excesses produced by the Internet boom. Moore's Law (the computing power of a chip doubles every 18 months) has been a gigantic driver of much of our technological revolution over the past 30 years. Breakthroughs in gene mapping and cloning, biotechnology, and nanotechnology and changes brought about by the Internet will continue to create huge opportunities for the next generation. Beyond the macro view of sea-changes, how can one think about opportunities in a more practical, less abstract sense? What are some parameters of business/revenue models that increase the odds of thinking big enough and therefore appeal to the food chain? To go with this chapter is the online Sea-Change Exercise, which will challenge you to think creatively and expansively about how new technology discoveries will drive the next new industries. This pattern continues to this day.

Desirable Business/Revenue Model Metrics

We will emphasize time and again in *New Venture Creation* that *happiness is a positive cash flow!—but think cash last*. You don't have an entry strategy until you have said no to lots of ideas; ideas that just come to you aren't usually opportunities; and the numbers don't matter but the economics really do matter.

THE ROLE OF IDEAS

Ideas as Tools

A good idea is nothing more than a tool in the hands of an entrepreneur. Finding a good idea is the first step in the process of converting an entrepreneur's creativity into an opportunity.

The importance of the idea is often overrated at the expense of underemphasizing the need for products or services, or both, that can be sold in enough quantity to real customers.

Further, the new business that simply bursts from a flash of brilliance is rare. Usually a series of trial-and-error iterations, or repetitions, is necessary before a crude and promising product or service fits with what the customer is willing to pay. Howard Head made 40 different metal skis before he finally made the model that worked consistently. With surprising frequency, major businesses are built around totally different products than those originally envisioned. Consider these examples:

- ✓ Swedish born Canadian Gideon Sundback patented a "separable fastener" in 1917. It took 20 years for this device—later dubbed "zipper"—to be adopted by the fashion industry.
- ✓ Polaroid Corporation was founded with a product based on the principle of polarized light. It was thought that polarized lamps would prevent head-on collisions between cars by preventing the "blinding" glare of oncoming headlights. But the company grew to its present size based on another application of the same technology: instant photography. Polaroid excelled until a disruptive technology (digital imaging) pushed them into bankruptcy.
- ✓ Medical doctor Wilbur Franks led a team of Canadians that developed an anti-gravity suit in 1941 to prevent pilot blackout from acceleration (G-force). G-suits had been around since 1906 for clinical surgery. George Crile, a founder of the Cleveland Clinic, developed a rubber suit that could be inflated by bicycle pump to apply force and maintain blood pressure preventing loss of consciousness.
- ✓ William Steere, CEO of Pfizer, described the discovery of Viagra, the fastest-selling drug in history, as having "a certain serendipity" behind it. The drug was originally developed by Pfizer to treat angina—its real "potency" was discovered as a side effect.⁹

As one entrepreneur expressed it:

Perhaps the existence of business plans and the language of business give a misleading impression of business building as a rational process. But, as any entrepreneur can confirm, starting a business is very much a series of fits and starts, brainstorm and barriers. Creating a business is a round of chance encounters that leads to new opportunities and ideas, mistakes that turn into miracles.¹⁰

The Great Mousetrap Fallacy

Perhaps no one did a greater disservice to generations of would-be entrepreneurs than Ralph Waldo Emerson in his oft-quoted line: "If a man can make a better mousetrap than his neighbour, though he builds his house in the woods the world will make a beaten path to his door."

What can be called the great mousetrap fallacy was thus spawned. It is often assumed that success is possible if an entrepreneur can just come up with a new idea. In today's changing world, if the idea has anything to do with technology, success is certain—or so it would seem.

But the truth is that ideas are inert and, for all practical purposes, worthless. Ideas are infinite but resources simply are not. Further, the flow of ideas is phenomenal. Venture capital investors, for instance, during the investing boom of the late 1990s, received as many as 100 to 200 proposals and business plans each month. Only 1 to 3 percent of these actually received financing, however.

Yet the fallacy persists despite the lessons of practical experience noted long ago in the insightful reply to Emerson by Owen B. Winters: "The manufacturer who waits for the world to beat a path to his door is a great optimist. But the manufacturer who shows this 'mousetrap' to the world keeps the smoke coming out his chimney."

Contributors to the Fallacy

One cannot blame it all on Ralph Waldo Emerson. There are several reasons for the perpetuation of the fallacy. One is the portrayal in oversimplified accounts of the ease and genius with which such ventures as Xerox, Seagram's, and Polaroid made their founders wealthy. Unfortunately, these exceptions do not provide a useful rule to guide aspiring entrepreneurs.

Another is that inventors seem particularly prone to mousetrap myopia. Perhaps, like Emerson, they are substantially sheltered in viewpoint and experience from the tough, competitive realities of the business world. Consequently, they may underestimate, if not seriously discount, the importance of what it takes to make a business succeed. Frankly, inventing and brainstorming may be a lot more fun than the diligent observation, investigation, and nurturing of customers that are often required to sell a product or service. Canadian James Gosling created the Java programming language at Sun Microsystems. It quickly gained notoriety and became ubiquitous; it also quickly became open source free software.

Contributing also to the great mousetrap fallacy is the tremendous psychological ownership attached to an invention or to a new product. This attachment is different from attachment to a business. While an intense level of psychological ownership and involvement is certainly a prerequisite for creating a new business, the fatal flaw in attachment to an invention or product is the narrowness of its focus. The focal point needs to be the building of the business, rather than just one aspect of the idea.

Another source of mousetrap fallacy myopia lies in a technical and scientific orientation, that is, a desire to do it better. A good illustration of this is the experience of a Canadian entrepreneur who with his brother founded a company to manufacture truck seats. The entrepreneur's brother had developed a new seat for trucks that was a definite improvement over other seats. The entrepreneur knew he could profitably sell the seat his brother had designed, and they did so. When they needed more manufacturing capacity, one brother had several ideas on how to improve the seat. The first brother stated: "If I had listened to him, we probably would be a small custom shop today, or out of business. Instead, we concentrated on making seats that would sell at a profit, rather than just making a better and better seat. Our company has several million dollars of sales today and is profitable."

Related to "doing it better" is the idea of doing it first. Having the best idea first is by no means a guarantee of success. There can be a liability—a painful downside—to being first. Sometimes the first ones merely prove to the competition that a market exists to be snared. Therefore, unless having the best idea also includes the capacity to pre-empt other competitors by capturing a significant share of the market or by erecting insurmountable barriers to entry, first does not necessarily mean most viable. And sometimes the quick follower sees things more clearly than the first-mover, capturing benefits of vicarious learning.

Spotting an opportunity within an existing market was a key aspect in the development of a mass-produced rotary electric toothbrush. The founding entrepreneur had noted a

large pricing spread among retail products. At the low end were devices in the range of \$5. There was then a jump to the \$60 to \$80 range, and then another jump to products that were selling for well over \$100. His research showed that new battery technology, plus outsourcing and a new rotary design, could result in a disposable product that would fill the gaps, steal market share, and yield substantial profits. His \$1.75-million business turned into \$475 million when his company was sold to Procter & Gamble. This is an excellent example of a clear pricing pattern that can be applied elsewhere.

PATTERN RECOGNITION

The Experience Factor

One cannot build a successful business without ideas. In this regard, **experience is vital in looking at new venture ideas.**

Time after time, experienced entrepreneurs exhibit an ability to recognize quickly a pattern—and an opportunity—while it is still taking shape. Nobel laureate Herbert Simon wrote extensively about pattern recognition. He described the recognition of patterns as a creative process that is not simply logical, linear, and additive but intuitive and inductive as well. It involves, he said, the creative linking, or cross-association, of two or more in-depth “chunks” of experience, know-how, and contacts.¹¹ Simon contended that it takes 10 years or more for people to accumulate what he called the “50,000 chunks” of experience that enable them to be highly creative and recognize patterns—familiar circumstances that can be translated from one place to another.

Thus, the process of sorting through ideas and recognizing a pattern can also be compared to the process of fitting pieces into a three-dimensional jigsaw puzzle. It is impossible to assemble such a puzzle by looking at it as a whole unit. Rather, one needs to see the relationships between the pieces and be able to fit together some that are seemingly unrelated before the whole is visible.

Recognizing ideas that can become entrepreneurial opportunities stems from a capacity to see what others do not—that one plus one equals three. Consider the following examples of the common thread of pattern recognition and new business creation by linking knowledge in one field or marketplace with quite different technical, business, or market know-how:

- ✓ Jim Treiving quit the RCMP to open a franchise restaurant—Boston Pizza. The leap was made after Jim ate at the original restaurant in Edmonton; Jim recounts, “It was love at first bite.” Jim partnered with George Melville and over 10 years built up a chain of 16 franchised restaurants. They then turned the tables and took over the 44-restaurant chain for \$3.8 million to become the franchisor. They divested 15 of the restaurants keeping one as a corporate training restaurant.
- ✓ During travel throughout Europe, the eventual founders of Crate & Barrel frequently saw stylish and innovative products for the kitchen and home that were not yet available in North America. When they returned home, the founders created Crate & Barrel to offer these products for which market research had, in a sense, already been done. In Crate & Barrel, the knowledge of consumer buying habits in one geographical region, Europe, was transferred successfully to another, the U.S. and Canada.
- ✓ Laurence Lewin, worked in a variety of jobs before settling on the fashion industry in the mid-1970s. Lewin failed to complete medical school; joined the military where he lost his rifle; barely passed England’s lowest level accounting qualification; and then worked in the computer industry. He went to work for Suzy Shier in 1987 and in 1990 co-founded La Senza. A few years later Suzy Shier was cast off for cash to fuel growth of La Senza. Today Lewin heads an empire of 700 stores, about half of which are in Canada and the remainder in 40 other countries.

Enhancing Creative Thinking

The creative thinking described above is of great value in recognizing opportunities, as well as other aspects of entrepreneurship. The notion that creativity can be learned or enhanced holds important implications for entrepreneurs who need to unlock imaginative solutions. Most people can certainly spot creative flair. Children seem to have it, and many seem to lose it. Several studies suggest that creativity actually peaks around the first grade because a person’s life tends to become increasingly structured and defined by others and by institutions. Further, the development of intellectual discipline and rigour in thinking takes on greater importance in school than during the formative years, and most of our education beyond grade school stresses a logical, rational mode of orderly reasoning and thinking. Finally, social pressures may tend to be a taming influence on creativity.

Evidence suggests that one can enhance creative thinking in later years. The Eureka! Ranch (www.eurekaranch.com) was founded on the principle that creativity is inherent in most people and can be unleashed by freeing them from convention. Often, executives will be doused with water as they step out of their vehicles onto the ranch.

Approaches to Unleashing Creativity

Since the 1950s, much has been learned about the workings of the human brain. Today, there is general agreement that the two sides of the brain process information in different ways. The left side performs rational, logical functions, while the right side operates the intuitive and nonrational modes of thought. A person uses both sides, actually shifting from one mode to the other (see Exhibit 3.5). Approaching ideas creatively and maximizing the control of these modes of thought can be of value to the entrepreneur.

More recently, attention has focused on the creativity process. For instance, evidence is mounting that administrative tasks crowd out more contemplative but non-urgent tasks:

Entrepreneurs are creative people who follow passions and may toy with 101 ideas for a business before starting one. Then come the endless Things That Must be Done: raising capital, closing sales, hiring staff, securing suppliers. Activities that don’t have deadlines, such as inventing, designing, and concocting new products, can get pushed to the bottom of to-do lists. As more time-sensitive and urgent tasks accumulate at the top of those lists, the creative stuff simply falls off.¹²

To keep the creative visualization process alive, entrepreneurs need to carve out some time to think freely. A walk in the woods is often pointed to as a prime setting for the activity.

Team Creativity

Teams of people can generate creativity that may not exist in a single individual. The creativity of a team of people is impressive, and comparable or better creative solutions to problems evolving from the collective interaction of a small group of people have been observed.

A good example of the creativity generated by using more than one head is that of Spin Master. It was founded when three friends who had just graduated from the University of Western Ontario, armed with \$10,000 set out to build a business. Earth Buddy, a small, pantyhose-covered head filled with grass seeds that sprouted hair when watered was their first product. It was a huge hit—a Pet Rock-like phenomenon—providing the team a foundation to sprout their next idea. The venture boasts a willingness to take risks, creativity, playfulness, and constant scanning for great new innovative toys.

Students interested in exploring this further may want to do the Creative Squares exercise online after completing this chapter. To access the exercise and many other useful tools, visit the Online Learning Centre at www.mcgrawhill.ca/olc/timmons.

EXHIBIT 3.5 Comparison of Left-Mode and Right-Mode Brain Characteristics

L-Mode	R-Mode
Verbal: Using words to name, describe, and define.	Nonverbal: Awareness of things, but minimal connection with words.
Analytic: Figuring things out step-by-step and part-by-part.	Synthetic: Putting things together to form wholes.
Symbolic: Using a symbol to stand for something. For example, the sign + stands for the process of addition.	Concrete: Relating to things as they are at the present moment.
Abstract: Taking out a small bit of information and using it to represent the whole thing.	Analogic: Seeing likenesses between things; understanding metaphoric relationships!
Temporal: Keeping track of time, sequencing one thing after another, doing first things first, second things second, etc.	Nontemporal: Without a sense of time.
Rational: Drawing conclusions based on reason and facts.	Nonrational: Not requiring a basis of reason or facts; willingness to suspend judgment.
Digital: Using numbers as in counting.	Spatial: Seeing where things are in relation to other things, and how parts go together to form a whole.
Logical: Drawing conclusions based on logic; one thing following another in logical order—for example, a mathematical theorem or a well-stated argument.	Intuitive: Making leaps of insight, often based on incomplete patterns, hunches, feelings, or visual images.
Linear: Thinking in terms of linked ideas, one thought directly following another, often leading to a convergent conclusion.	Holistic: Seeing whole things all at once; perceiving the overall patterns and structures, often leading to divergent conclusions.

Source: "A Comparison of Left-Mode and Right-Mode Characteristics," from *Drawing on the Right Side of the Brain* by Betty Edwards (New York, NY: Putnam Books, 1999).

Big Opportunities with Little Capital

Within the dynamic free enterprise system, opportunities are apparent to a limited number of individuals—and not just to the individuals with financial resources. Ironically, successful entrepreneurs such as Howard Head attribute their success to the discipline of limited capital resources. Many entrepreneurs have learned the key to success is in the art of bootstrapping, which "in a start-up is like zero inventory in a just-in-time system: it reveals hidden problems and forces the company to solve them."¹³ And Canadians take pride in their conservative nature—often avoiding risks associated with becoming highly leveraged (see Chapter 11 "Obtaining Debt Capital")—growing through retained earnings. Consider the following:

- Approximately three-quarters of start-ups launch with \$50,000 or less; half begin with \$10,000 or less as seed capital. Further, the primary source of capital was, overwhelmingly, personal savings (77 percent), rather than outside investors with deep pockets.¹⁴
- In the 1930s, Josephine Esther Mentzer assisted her uncle by selling skin care balm and quickly created her own products with an initial investment of \$100. After convincing the department stores rather than the drugstores to carry her products, Estee Lauder was on its way to becoming a corporation with 2008 sales of US\$8 billion.¹⁵
- Putting their talents (cartooning and finance) together, Roy and Walt Disney moved to California and started their own film studio—with \$290 in 1923. By 2009, the Walt Disney Co. had a market capitalization exceeding \$50 billion.
- While working in real estate, Montréal immigrant Assaad Abdelnour's vision for CLIC Foods began. He later bought and operated a supermarket and the full concept took shape. CLIC (Canadian Lebanese Investment Corporation) became a pioneer in ethnic foods and today is a leader in the production and distribution of international food products with annual sales of nearly \$40 million. CLIC boasts 200 employees at six locations across Canada, derives 25 percent of revenues from exports, and in 2007 opened a facility in New Jersey.
- With \$100 Calgary-native Nicholas Graham, age 24, went to a local fabric store, picked out some fabrics, and made \$100 worth of ties. Having sold the ties to specialty shops, Graham was approached by Macy's to place his patterns on men's underwear. So Joe

Boxer Corporation was born and "six months into Joe Boxer's second year, sales had already topped \$1 million."¹⁶ Graham, CUO (Chief Underpants Officer) successfully harvested the business a few years later when annual sales reached US\$20 million.

Real Time

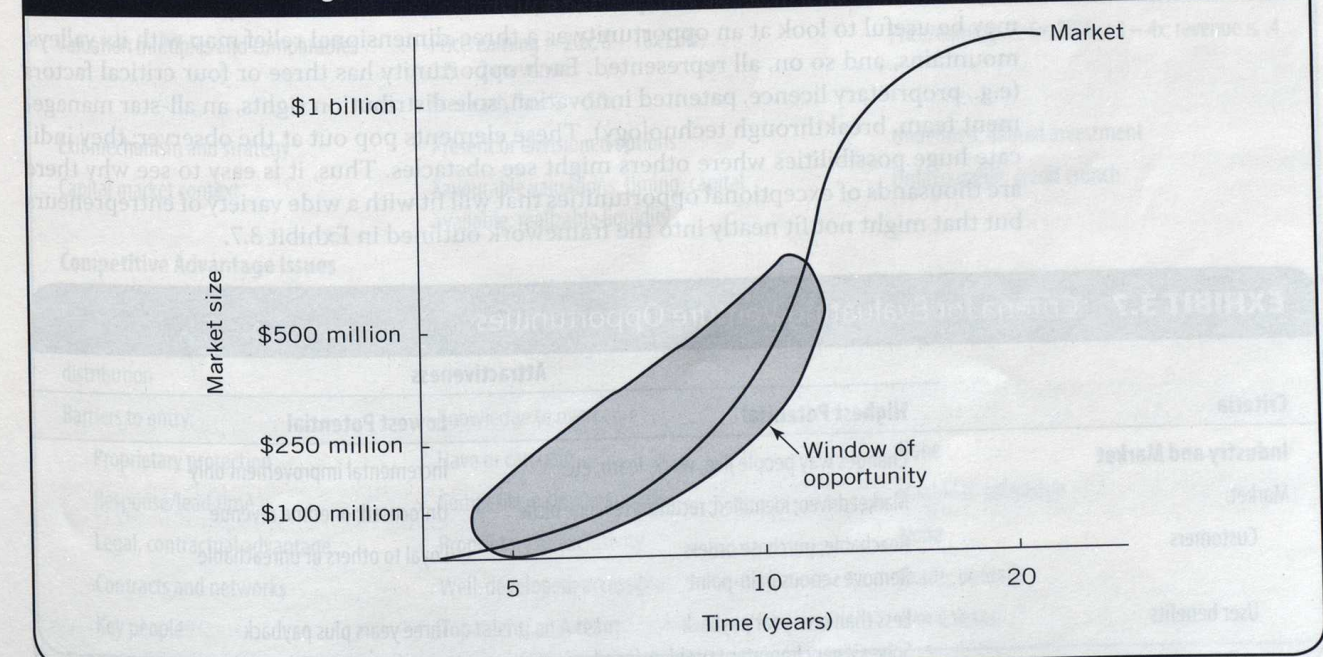
Opportunities exist or are created in real time and have what we call a window of opportunity. For an entrepreneur to seize an opportunity, the window must be open and remain open long enough to achieve market-required returns.

Exhibit 3.6 illustrates a window of opportunity for a generalized market. Markets grow at different rates over time and as a market quickly becomes larger, more and more opportunities are possible. As the market becomes established, conditions are not as favourable. Thus, at the point where a market starts to become sufficiently large and structured (e.g., at five years in Exhibit 3.6), the window opens; the window begins to close as the market matures (e.g., at 12 to 13 years in the exhibit).

The curve shown describes the rapid growth pattern typical of such new industries as microcomputers and software, cellphones, quick oil changes, and nanotechnology. For example, in the cellular phone industry, most major cities began service between 1984 and 1985. In 1996, U.S. and Canadian cellphone use was comparable, 13 in 100 U.S. residents and 9 in 100 Canadian residents had one, but by 2007, U.S. penetration reached 76 percent while Canada was at 60 percent.¹⁷ In other industries where growth is not so rapid, the slope of a curve would be less steep and the possibilities for opportunities fewer.

In considering the window of opportunity, the length of time the window will be open is important. It takes a considerable length of time to determine whether a new venture is a success or a failure. And, if it is to be a success, the benefits of that success need to be realized.

Evidence shows that for venture-capital-backed firms, the lemons (i.e., the losers) ripen in about two and a half years, while the pearls (i.e., the winners) take seven or eight years to mature. An extreme example of the length of time it can take for a pearl to be harvested is the experience of one Silicon Valley venture capital firm that invested in a new firm in 1966 and was finally able to realize a capital gain in early 1984. Another way to think of the process of creating and seizing an opportunity in real time is to think of it as a process of selecting objects (opportunities) from a conveyor belt moving through an open window,

EXHIBIT 3.6 Changes in the Placement of the Window of Opportunity

the window of opportunity. The speed of the conveyor belt changes, and the window through which it moves is constantly opening and closing. The continually opening and closing window and the constantly changing speed of the conveyor belt represent the volatile nature of the marketplace and the importance of timing. For an opportunity to be created and seized, it needs to be selected from the conveyor belt before the window closes.

The ability to recognize a potential opportunity when it appears and the sense of timing to seize that opportunity, as the window is opening, rather than slamming shut, are critical. That opportunities are a function of real time is illustrated in a statement made by Ken Olsen, then president and co-founder of Digital Equipment Corporation, in 1977, "There is no reason for any individual to have a computer in their home." Though taken out of context, Ken Olsen did take the fall in 1992 and within the decade the struggling company's assets were sold off.¹⁸ It is not easy for even the world's leading experts to predict just which innovative ideas and concepts for new business will evolve into the major industries of tomorrow. This is vividly illustrated by several quotations from famous innovators. In 1901, two years before the famous flight, Wilbert Wright said, "Man will not fly for 50 years." In 1910, Thomas Edison said, "The nickel-iron battery will put the gasoline buggy . . . out of existence in no time." Albert Einstein in 1932 made it clear, "[There] is not the slightest indication that nuclear energy will ever be obtainable. It would mean that the atom would have to be shattered at will." Thomas Watson, IBM Chairman in 1943 predicted, "I think there is a world market for maybe five computers." And in 1981 Bill Gates, Microsoft Chairman stated, "640K ought to be enough for anybody."

Clearly predicting opportunity is tricky business. Charles Duell, commissioner at the U.S. Office of Patents in 1899 stated, "Everything that can be invented has been invented." While today just about every appliance on the kitchen counter has a computer, some are foretelling that the desktop/home computer may fade as more "Net" devices and individuals tap into a CPU remotely. Sun Microsystems' business model and mantra has been: "The network is the computer." Presently, Edison's belief that a battery-powered vehicle would replace gasoline-powered ones is looking ever more likely.

Relation to the Framework of Analysis

Successful opportunities, once recognized, fit with the other forces of new venture creation. This iterative process of assessing and reassessing the fit among the central driving forces in the creation of a new venture were shown in Chapter 2. Of utmost importance is the fit of the lead entrepreneur and the management team with an opportunity. Good opportunities are both desirable to and attainable by those on the team using the resources that are available.

To understand how the entrepreneurial vision relates to the analytical framework, it may be useful to look at an opportunity as a three-dimensional relief map with its valleys, mountains, and so on, all represented. Each opportunity has three or four critical factors (e.g., proprietary licence, patented innovation, sole distribution rights, an all-star management team, breakthrough technology). These elements pop out at the observer; they indicate huge possibilities where others might see obstacles. Thus, it is easy to see why there are thousands of exceptional opportunities that will fit with a wide variety of entrepreneurs but that might not fit neatly into the framework outlined in Exhibit 3.7.

EXHIBIT 3.7 Criteria for Evaluating Venture Opportunities

Criteria	Attractiveness	
	Highest Potential	Lowest Potential
Industry and Market	Changes way people live, work, learn, etc.	Incremental improvement only
Market:	Market driven; identified; recurring revenue niche	Unfocused; onetime revenue
Customers	Reachable; purchase orders Remove serious pain-point	Loyal to others or unreachable
User benefits	Less than one-year payback Solves a very important problem/need	Three years plus payback

EXHIBIT 3.7 Criteria for Evaluating Venture Opportunities (continued)

Criteria	Attractiveness	
	Highest Potential	Lowest Potential
Value added	High; advance payments	Low; minimal impact on market
Product life	Durable	Perishable
Market structure	Imperfect, fragmented competition or emerging industry	Highly concentrated or mature or declining industry
Market size	\$100 million to \$1 billion sales potential	Unknown, less than \$20 million or multibillion sales
Growth rate	Growth at 30–50% or more	Contracting or less than 10%
Market capacity	At or near full capacity	Undercapacity
Market share attainable (Year 5)	20% or more; leader	Less than 5%
Cost structure	Low-cost provider; cost advantages	Declining cost
Economics		
Time to break even/positive cash flow	Under 1½–2 years	More than 4 years
ROI potential	25% or more; high value	Less than 15–20%; low value
Capital requirements	Low to moderate; fundable/bankable	Very high; unfundable or unbankable
Internal rate of return potential	25% or more per year	Less than 15% per year
Free cash flow characteristics:	Favourable; sustainable; 20–30% or more of sales	Less than 10% of sales
Sales growth	Moderate to high (15–20%)	Less than 10%
Asset intensity	Low/sales \$	High
Spontaneous working capital	Low, incremental requirements	High requirements
R&D/capital expenditures	Low requirements	High requirements
Gross margins	Exceeding 40% and durable	Under 20%
After-tax profits	High; greater than 10%; durable	Low
Time to break-even profit and loss	Less than two years; breakeven not creeping or leaping	Greater than four years; breakeven creeping or leaping up
Harvest Issues		
Value-added potential	High strategic value	Low strategic value
Valuation multiples and comparables	Price/earning = 20x; 8 – 10x EBIT; 1.5 – 2x revenue; Free cash flow 8 – 10x	Price/earnings ≤ 5x; EBIT ≤ 3 – 4x; revenue ≤ .4
Exit mechanism and strategy	Present or envisioned options	Undefined; illiquid investment
Capital market context	Favourable valuations, timing, capital available; realizable liquidity	Unfavourable; credit crunch
Competitive Advantage Issues		
Fixed and variable costs	Lowest; high operating leverage	Highest
Control over costs, prices, and distribution	Moderate to strong	Weak
Barriers to entry:	Knowledge to overcome	
Proprietary protection	Have or can gain	None
Response/lead time	Competition slow; napping	Unable to gain edge
Legal, contractual advantage	Proprietary or exclusivity	None
Contracts and networks	Well-developed; accessible	Crude; limited
Key people	Top talent; an A team	B or C team

(continued)

EXHIBIT 3.7 Criteria for Evaluating Venture Opportunities (continued)

Criteria	Attractiveness	
	Highest Potential	Lowest Potential
Management Team		
Entrepreneurial team	All-star combination; free agents	Weak or solo entrepreneur; not free agents
Industry and technical experience	Top of the field; super track record	Underdeveloped
Integrity	Highest standards	Questionable
Intellectual honesty	Know what they do not know	Do not want to know what they do not know
Fatal-Flaw Issue	Nonexistent	One or more
Personal Criteria		
Goals and fit	Getting what you want; but wanting what you get	Surprises; only making money
Upside/downside issues	Attainable success/limited risks	Linear; on same continuum
Opportunity costs	Acceptable cuts in salary, etc.	Comfortable with status quo
Desirability	Fits with lifestyle	Simply pursuing big money
Risk/reward tolerance	Calculated risk; low risk/reward ratio	Risk averse or gambler
Stress tolerance	Thrives under pressure	Cracks under pressure
Strategic Differentiation		
Degree of fit	High	Low
Team	Best in class; excellent free agents	B team; no free agents
Service management	Superior service concept	Perceived as unimportant
Timing	Rowing with the tide	Rowing against the tide
Technology	Groundbreaking; one of a kind	Many substitutes or competitors
Flexibility	Able to adapt; commit and decommit quickly	Slow; stubborn
Opportunity orientation	Always searching for opportunities	Operating in a vacuum; napping
Pricing	At or near leader	Undercut competitor; low prices
Distribution channels	Accessible; networks in place	Unknown; inaccessible
Room for error	Forgiving and resilient strategy	Unforgiving, rigid strategy

SCREENING OPPORTUNITIES**Opportunity Focus**

Opportunity focus is the most fruitful point of departure for screening opportunities. The screening process should not begin with strategy (which derives from the nature of the opportunity), nor with financial and spreadsheet analysis, nor with estimations of how much the company is worth and who will own what shares.

These starting points, and others, usually place the cart before the horse. Also, many entrepreneurs who start businesses—particularly those for whom the ventures are their first—run out of cash at a faster rate than they bring in customers and profitable sales. There are lots of reasons why this happens, but one thing is certain: These entrepreneurs have not focused on the right opportunity.

Over the years, those with experience in business and in specific market areas have developed rules to guide them in screening opportunities. For example, during the initial stages of the irrational exuberance about the dot-com phenomenon, number of “clicks” changed to attracting “eyeballs,” which changed to pages viewed. Many investors got caught up in false metrics. Those who survived the stock market crash of 2000–2001 understood

that dot-com survivors would be the ones who executed transactions. Number of customers, amount of the transaction, and repeat transactions became the recognized standards.¹⁹ And in the aftermath of the 2009 financial downturn the winners and losers were revealed. A stout recession provided threats to established enterprises and opportunities for new ventures. During such transformation periods the status quo is repeatedly proved to be no longer viable and business models are quickly evaluated and refined as consumers shift priorities dramatically.

Screening Criteria: The Characteristics of High Potential Ventures

Venture capitalists, savvy entrepreneurs, and investors also use this concept of boundaries in screening ventures. Exhibit 3.7 summarizes criteria used by venture capitalists to evaluate opportunities: opportunities, many of which tend to have a high-technology bias. As will be seen later, venture capital investors reject 60 to 70 percent of the new ventures presented to them very early in the review process, based on how the entrepreneurs satisfy these criteria.

However, these criteria are not the exclusive domain of venture capitalists. The criteria are based on good business sense that is used by successful entrepreneurs, angels, private investors, and venture capitalists. Consider the following examples of great small companies built without a dime of professional venture capital.

Herb and Rhoda Singer established Discount Car & Truck Rentals in 1980. Discount has grown from the first location in Hamilton, Ontario, to 300 locations, most of which are franchises. It has a few locations in Australia and has expansion plans for the United States. Discount included hybrids in its fleet in 2004, and in 2008 during a looming Toronto Transit Authority strike, offered discounts to stranded public transportation riders.

Wester's Garage, located in Tilley, Alberta (pop. 397), “in the heart of truck country, surrounded by oil fields and wide open space” provides custom performance tuning for trucks and cars. Owner, Lyndon Wester offers reprogramming of the computer chip that controls the engine. It all started in late 1998 with some simple electronics work, but by 2000 they had developed custom performance profiles for the Pontiac Fiero and GM diesel trucks. Their first big break was an order in July 2002 for converting UPS vans across North America. In 2003 Lyndon Wester secured a U.S. military contract for 50 Chevy Suburbans and two local contracts for oil service company fleet vehicles to modify GM trucks to improve fuel economy, limit speed, and alter powertrain parameters. These contracts secured the future for Wester's Garage. While maintaining customers in Alberta's oil fields they thrived with performance tuning for car and truck enthusiasts—even the occasional boat engine. As one online bulletin board posting noted, “Seems amazing that someone living 13 miles from nowhere is getting computers shipped to him from all over North America.”

In 1986 Pleasant Rowland founded the Pleasant Company as a mail order catalogue company selling the American Girls Collection of historical dolls. She had begun the company with the modest royalties she received from writing children's books and did not have enough capital to compete in stores with the likes of Mattel's Barbie.²⁰ By 1992 she had grown the company to US\$65 million in sales.²¹ Mattel acquired it in 1998 for US\$770 million, and under Rowland's continued management, the company had sales of US\$350 million in 2001.

Edgy musician Ashley MacIsaac offered half of his future revenues on eBay in the summer of 2008 with a minimum bid of \$1.5 million. Seeking a patron of the arts, MacIsaac said, “I see this as no different than what they did in Mozart's day.” David Bowie issued bonds in the late 1990s using future royalties as guarantee; Bowie collected tens of millions of dollars on the spot.²² In 2007, Madonna came to a similar arrangement with concert promoter Live Nation Inc. for over \$100 million. The point of departure here is opportunity and, implicitly, the customer, the marketplace, and the industry. Exhibit 3.7 shows how higher and lower potential opportunities can be placed along an attractiveness scale. The criteria provide some quantitative ways in which an entrepreneur can make judgments about industry and market issues, competitive advantage issues, economic and harvest issues, management team issues, and fatal flaw issues and whether these add up to a compelling opportunity. For example, dominant strength in any one of these criteria can readily translate into a winning entry, whereas a flaw in any one can be fatal.

Entrepreneurs contemplating opportunities that will yield attractive companies, not high potential ventures, can also benefit from paying attention to these criteria. These entrepreneurs will then be in a better position to decide how these criteria can be compromised. As outlined in Exhibit 3.7, business opportunities with the greatest potential will possess many of the following, or they will dominate in one or a few for which the competition cannot come close.

Industry and Market Issues

Market. Higher potential businesses can identify a market niche for a product or service that meets an important customer need and provides high value-added or value-created benefits to customers. This invariably means the product or service eliminates or drastically reduces a major pain-point for a customer or end-user, or solves a major problem/bottleneck for which the customer is willing to pay a premium. Customers are reachable and receptive to the product or service, with no brand or other loyalties. The potential payback to the user or customer of a given product or service through cost savings or other value-added or value-created properties is one year or less and is identifiable, repeatable, and verifiable. Further, the life of the product or service exists beyond the time needed to recover the investment, plus a profit. And so much the better if the company is able to expand beyond a single product. If benefits to customers can be calculated in dollar terms, then the market potential is far less difficult and risky to ascertain.

Lower potential opportunities are unfocused regarding customer need, and customers are unreachable and/or have brand or other loyalties to others. A payback to the user of more than three years and low value-added or value-created properties also makes an opportunity unattractive. Being unable to expand beyond a one-product company can make for a lower potential opportunity. The failure of one of the first portable computer companies, Osborne Computer, is a prime example of this. Adam Osborne's business plan called for sales of 10,000 of his Osborn 1 computer over the product's lifespan; sales peaked at 10,000 units per month. Despite market appeal, quality control fell during rushed production. Osborne's boasts of a second-generation model that was months away from release did not boost confidence. Customers poised to buy the current model held off and dealers cancelled orders for the Osborne 1. The young venture never recovered and his blunder came to be known as "Osborneing." Med-Eng CEO Richard L'Abbe recounts a similar—though non-fatal—scenario. It occurred several iterations into the product line. An update to their bomb disposal suit and helmet combo was introduced half-way through the usual cycle. The word got out and customers held-off buying. Med-Eng quickly took note and went back to their normal update cycle.

Market Structure. Market structure, such as evidenced by the number of sellers, size distribution of sellers, whether products are differentiated, conditions of entry and exit, number of buyers, cost conditions, and sensitivity of demand to changes in price, is significant.

A fragmented, imperfect market or emerging industry often contains vacuums and asymmetries that create unfilled market niches—for example, markets where resource ownership, cost advantages, and the like can be achieved. In addition, those where information or knowledge gaps exist and where competition is profitable, but not so strong as to be overwhelming, are attractive. An example of a market with an information gap is that experienced by an entrepreneur who encountered a large out-of-town company that wanted to dispose of a small, old downtown office building. This office building, because its book value was about \$200,000, was viewed by the financially oriented firm as a low-value asset, and the company wanted to dispose of it so the resulting cash could be put to work for a higher return. The buyer, who had done more homework than the out-of-town sellers, bought the building for \$200,000 and resold it in less than six months for more than \$8 million.

Industries that are highly concentrated, that are perfectly competitive, or that are mature or declining are typically unattractive. The capital requirements and costs to achieve distribution and marketing presence can be prohibitive, and price-cutting and other competitive strategies in highly concentrated markets can be a significant barrier to entry. (The most blatant example is organized crime and its life-threatening actions when territories

are invaded.) Revenge by normal competitors who are well positioned through product strategy, legal tactics, and the like, also can be punishing to the newcomer.

The unattractiveness of perfectly competitive industries is captured by the comment of prominent venture capitalist William Egan, who put it this way: "I want to be in a nonauction market."

Market Size. An attractive new venture sells to a market that is large and growing (i.e., one where capturing a small market share can represent significant and increasing sales volume). A minimum market size of more than \$100 million in sales is attractive. In the medical and life sciences today, this target boundary is more like \$500 million or \$1 billion. Such a market size means it is possible to achieve significant sales by capturing roughly 5 percent or less and thus not threatening competitors. For example, to achieve a sales level of \$1 million in a \$100-million market requires only 1 percent of the market. Thus, a recreational equipment manufacturer entered a \$60-million market that was expected to grow at 20 percent per year to over \$100 million by the third year. The founders were able to create a substantial, but smaller company without obtaining a major share of the market and possibly incurring the wrath of existing companies.

However, a market can be too large. A multi-billion-dollar market may be too mature and stable, and such a level of certainty can translate into competition from Fortune 500 firms and, if highly competitive, into lower margins and profitability. Further, an unknown market or one that is less than \$10 million in sales also is unattractive. To understand the disadvantages of a large, more mature market consider the entry of a firm into the micro-computer industry today versus the entry of Apple into that market in 1975.

Growth Rate. An attractive market is large and growing (i.e., one where capturing a good share of the increase is less threatening to competitors and where a small market share can represent significant and increasing sales volume). An annual growth rate of 30 to 50 percent creates niches for new entrants, and such a market is a thriving and expansive one, rather than a stable or contracting one, where competitors are scrambling for the same niches. Thus, for example, a \$100-million market growing at 50 percent per year has the potential to become a \$1-billion industry in a few years, and if a new venture can capture just 2 percent of sales in the first year, it can attain sales in the first year of \$1 million. If it just maintains its market share over the next few years, sales will grow significantly.

Market Capacity. Another signal of the existence of an opportunity in a market is a market at full capacity in a growth situation—in other words, a demand that the existing suppliers cannot meet. Timing is of vital concern in such a situation, which means the entrepreneur should be asking: Can a new entrant fill that demand before the other players can decide to and then actually increase capacity?

Market Share Attainable. The potential to be a leader in the market and capture at least a 20-percent share can create a very high value for a company that might otherwise be worth not much more than book value. For example, one such firm, with less than \$15 million in sales, became dominant in its small market niche with a 70-percent market share. The company was acquired for \$23 million in cash.

A firm that will be able to capture less than 5 percent of a market is unattractive in the eyes of most investors seeking a higher potential company.

Cost Structure. A firm that can become the low-cost provider is attractive, but a firm that continually faces declining cost conditions is less so. Attractive opportunities exist in industries where economies of scale are insignificant (or work to the advantage of the new venture). Attractive opportunities boast of low costs of learning by doing. Where costs per unit are high when small amounts of the product are sold, existing firms that have low promotion costs can face attractive market opportunities.

For instance, consider the operating leverage of Johnsonville Sausage. Its variable costs were 6 percent labour and 94 percent materials. What aggressive incentives could management put in place for the 6 percent to manage and to control the 94 percent? Imagine the disasters that would occur if the scenario were reversed!

A word of caution from Scott Kunkel and Charles Hofer, who observed:

Overall, industry structure ... had a much smaller impact on new venture performance than has previously been suggested in the literature. This finding could be the result of one of several possibilities:

1. Industry structure impacts the performance of established firms, but does NOT have a significant impact on new venture performance.
2. The most important industry structural variables influencing new ventures are different from those which impact established firms and thus research has yet to identify the industry structural variables that are most important in the new venture environment.
3. Industry structure does NOT have a significant DIRECT impact on firm performance, as expected. Instead, the impact of industry structure is strongly mitigated by other factors, including the strategy selected for entry.²³

Economics

Profits After Tax. High and durable gross margins usually translate into strong and durable after-tax profits. Attractive opportunities have potential for durable profits of at least 10 to 15 percent and often 20 percent or more. Those generating after-tax profits of less than 5 percent are quite fragile.

Time to Breakeven and Positive Cash Flow. As mentioned above, breakeven and positive cash flow for attractive companies are possible within two years. Once the time to breakeven and positive cash flow is greater than three years, the attractiveness of the opportunity diminishes accordingly.

Return on Investment Potential. An important corollary to forgiving economics is reward. Very attractive opportunities have the potential to yield a return on investment of 25 percent or more per year. During the 1980s, many venture capital funds achieved only single-digit returns on investment. High and durable gross margins and high and durable after-tax profits usually yield high earnings per share and high return on shareholders' equity, thus generating a satisfactory "harvest" price for a company. This is most likely true whether the company is sold through an initial public offering or privately, or whether it is acquired. Given the risk typically involved, a return on investment potential of less than 15 to 20 percent per year is unattractive.

Capital Requirements. Ventures that can be funded and have capital requirements that are low to moderate are attractive. Realistically, most higher-potential businesses need significant amounts of cash—several hundred thousand dollars and up—to get started. Businesses that can be started with little or no capital are rare, but they do exist. In today's venture capital market, the first round of financing is typically \$1 to \$2 million or more for a start-up.²⁴ Some higher potential ventures, such as those in the service sector or "cash sales" businesses, have lower capital requirements than do technology-intensive firms with large research and development expenditures.

If the venture needs too much money or cannot be funded, it is unattractive. An extreme example is a venture that a team of students proposed to repair satellites. The students believed that the required start-up capital was in the \$50 to \$200 million range. Projects of this magnitude are in the domain of the government and the very large multinational corporation, rather than that of the entrepreneur and the venture capitalist. Think Richard Branson of Virgin Galactic launching commercial space flights!

Internal Rate of Return Potential. Is the risk-reward relationship attractive enough? The response to this question can be quite personal, but the most attractive opportunities often have the promise of—and deliver on—a very substantial upside of 5 to 10 times the original investment in 5 to 10 years. Of course, the extraordinary successes can yield 50 to 100 times or more, but these are exceptions. A 25 percent or more annual compound rate of return is considered very healthy. In economically stable times, those investments considered basically risk free have yields of 3 to 8 percent.

Free Cash Flow Characteristics. Free cash flow is a way of understanding a number of crucial financial dimensions of any business: the robustness of its economics; its capital requirements, both working and fixed assets; its capacity to service external debt and equity claims; and its capacity to sustain growth.²⁵ We define unleveraged free cash flow (FCF) as earnings before interest but after taxes (EBIAT) plus amortization (A) and depreciation (D) less spontaneous working capital requirements (WC) less capital expenditures (CAPex), or $FCF = EBIAT + [A+D] - [+ \text{ or } - WC] - CAPex$. EBIAT is driven by sales, profitability, and asset intensity. Low-asset-intensive, high-margin businesses generate the highest profits and sustainable growth.²⁶ We will explore this in detail in Chapter 9 "Financing the Venture."

Gross Margins. The potential for high and durable gross margins (i.e., the unit selling price less all direct and variable costs) is important. Gross margins exceeding 40 to 50 percent provide a tremendous built-in cushion that allows for more error and more flexibility to learn from mistakes than do gross margins of 20 percent or less. High and durable gross margins, in turn, mean that a venture can reach breakeven earlier, preferably within the first two years. Thus, for example, if gross margins are just 20 percent, for every \$1 increase in fixed costs (e.g., insurance, salaries, rent, and utilities), sales need to increase \$5 just to stay even. If gross margins are 75 percent, however, a \$1 increase in fixed costs requires a sales increase of just \$1.33. One entrepreneur, who built the international division of an emerging software company to \$17 million in highly profitable sales in just five years (when he was 25 years old), offers an example of the cushion provided by high and durable gross margins. He stresses there is simply no substitute for outrageous gross margins by saying, "It allows you to make all kinds of mistakes that would kill a normal company. And we made them all. But our high gross margins covered all the learning tuition and still left a good profit."²⁷ Gross margins of less than 20 percent, particularly if they are fragile, are unattractive.

Time to Breakeven—Cash Flow and Profit and Loss (P&L). New businesses that can quickly achieve a positive cash flow and become self-sustaining are highly desirable. It is often the second year before this is possible, but the sooner the better. Obviously, simply having a longer window does not mean the business will be lousy. Two great companies illustrate that a higher potential business can have a longer window. Pilkington Brothers, an English firm that developed plate glass technology, ran huge losses for over two and a half years before it was regarded as a great company. Similarly, Federal Express went through an early period of enormous negative cash flows of \$1 million a month. More recently, auto giant General Motors managed \$3.6 billion in negative cash flow for the second quarter of 2008.

Harvest Issues

Value-Added Potential. New ventures that are based on strategic value in an industry, such as valuable technology, are attractive, while those with low or no strategic value are less attractive. For example, most observers contend that technology services capacity of compelling strategic value to HP was acquired when it purchased EDS for \$13.9 billion in 2008, whereas the merger with Compaq was less so. "In Compaq, HP grabbed more of what it already had;" with EDS, HP is getting something new.²⁸ Opportunities with extremely large capital commitments, whose value on exit can be severely eroded by unanticipated circumstances, are less attractive.

Thus, one characteristic of businesses that command a premium price is that they have high value-added strategic importance to their acquirer, such as distribution, customer base, geographic coverage, proprietary technology, contractual rights, and the like. Such companies might be valued at four, five, or even six times (or more) last year's sales, whereas perhaps 60 to 80 percent of companies might be purchased at .75 to 1.25 times sales.

Valuation Multiples and Comparables. Consistent with the above point, there is a large spread in the value the capital markets place on private and public companies. Part of your analysis is to identify some historical boundaries for valuations placed on companies in the market/industry/technology area you intend to pursue. The rules outlined in Exhibit 3.7 are variable and should be thought of as a boundary and a point of departure.

Exit Mechanism and Strategy. Businesses that are eventually sold—privately or to the public—or acquired, usually are started and grown with a harvest objective in mind. Attractive companies that realize capital gains from the sale of their businesses have, or envision, a harvest or exit mechanism. **Unattractive opportunities do not have an exit mechanism in mind.** Planning is critical because, as is often said, it is much harder to get out of a business than to get into it. Giving some serious thought to the options and likelihood that the company can eventually be harvested is an important initial and ongoing aspect of the entrepreneurial process.

Capital Market Context. The context in which the sale or acquisition of the company occurs is largely driven by the capital markets at that particular time. **Timing can be a critical component of the exit mechanism** because, as one study indicated, since World War II, the average bull market on Bay Street has lasted five and a half years, adding from 82 to 266 percent to the market's value and the average bull/bear cycle has been just over six years.²⁹ "Over the last half century, the average bear market has lasted 12 months. The shortest—four months between August and November 1987—included the Toronto market's biggest one-day crash. Bay Street stocks lost 22 percent of their value on Monday, October 19. But that bear market ushered in the longest bull market in the exchange's history. The bulls ran for almost 10½ years, resulting in an overall return of 247 per cent." For a keener appreciation of the critical difference the capital markets can make, one only has to recall such stock market events or even a bank credit crunch. Initial public offerings are especially vulnerable to the vicissitudes of the capital markets; here the timing is vital. Some of the most successful companies seem to have been launched when debt and equity capital were most available and relatively cheap.

Competitive Advantages Issues

Variable and Fixed Costs. An attractive opportunity has the potential for being the lowest-cost producer and for having the lowest marketing and distribution costs. For example, Bowmar was unable to remain competitive in the market for electronic calculators after the producers of large-scale integrated circuits, such as Hewlett-Packard, entered the business. **Being unable to achieve and sustain a position as a low-cost producer shortens the life expectancy of a new venture.**

Degree of Control. Attractive opportunities have **potential for moderate-to-strong degree of control over prices, costs, and channels of distribution.** Fragmented markets where there is no dominant competitor—no Rogers, Shaw, or Vidéotron—have this potential. These markets usually have a market leader with a 20-percent market share or less. For example, sole control of the source of supply of a critical component for a product or of channels of distribution can give a new venture market dominance even if other areas are weak.

Lack of control over such factors as product development and component prices can make an opportunity unattractive. For example, if a young enterprise's supplier is unable to produce inputs needed at low enough prices or high enough quantities that young enterprise is vulnerable. Maintaining control is a key factor in determining a venture's fate.

A market where a major competitor has a market share of 40 percent or more usually implies a market where power and influence over suppliers, customers, and pricing create a serious barrier and risk for a new firm. Such a firm will have few degrees of freedom. However, if a dominant competitor is at full capacity, is slow to innovate or to add capacity in a large and growing market, or routinely ignores or abuses the customer (Bell Canada is a frequent example), **there may be an entry opportunity.** However, entrepreneurs usually do not find such sleepy competition in dynamic, emerging industries dense with opportunity.

Entry Barriers. **Having a favourable window of opportunity is important.** Having or being able to gain proprietary protection, regulatory advantage, or other legal or contractual advantage, such as exclusive rights to a market or with a distributor, is attractive. Having or being able to gain an advantage in response/lead times is important because these can create barriers to entry or expansion by others. For example, advantages in response/lead times in technology, product innovation, market innovation, people, location, resources, or capacity make an opportunity attractive. Possession of well-developed, high-quality, accessible contacts that are the product of years of building a top-notch reputation and that cannot be acquired

quickly is also advantageous. Sometimes this competitive advantage may be so strong as to provide dominance in the marketplace, even though many of the other factors are weak or average. An example of how quickly the joys of start-up may fade if others cannot be kept out is the experience of firms in the hard disk industry that were unable to erect entry barriers into the market in the early to mid-1980s. During this period nearly 100 hard disk drive companies were launched and severe price competition led to a major industry shakeout.

If a firm cannot keep others out or if it faces already existing entry barriers, it is unattractive. An easily overlooked issue is a firm's capacity to gain distribution of its product. As simple as it may sound, even venture-capital-backed companies fall victim to this market issue. Air Florida apparently assembled all the right ingredients, including substantial financing, yet was unable to secure sufficient gate space for its airplanes. Even though it sold passenger seats, it had no place to pick the passengers up or drop them off!

Management Team Issues

Entrepreneurial Team. Attractive opportunities have existing teams that are strong and contain industry superstars. The team has proven profit and loss experience in the same technology, market, and service area, and members have complementary and compatible skills. An unattractive opportunity does not have such a team in place or has no team.

Industry and Technical Experience. A management track record of significant accomplishment in the industry, with the technology, and in the market area, with a proven profit and lots of achievements where the venture will compete is highly desirable. A top-notch management team can become the most important strategic competitive advantage in an industry. Imagine relocating the Chicago Bulls or the Phoenix Suns to Halifax, Nova Scotia. Do you think you would have a winning competitor in the National Basketball Association?

Integrity. **Trust and integrity are the oil and glue that make economic interdependence possible.** Having an unquestioned reputation in this regard is a major long-term advantage for entrepreneurs and should be sought in all personnel and backers. A shady past or record of questionable integrity is for B team players only.

Intellectual Honesty. There is a fundamental issue of whether the founders know what they do and do not know, as well as whether they know what to do about shortcomings or gaps in the team and the enterprise.

Fatal-Flaw Issues. Basically, attractive ventures have no fatal flaws; an opportunity is rendered **unattractive if it suffers from one or more fatal flaws.** Usually, these relate to one of the above criteria, and examples abound of markets that are too small, that have overpowering competition, where the cost of entry is too high, where an entrant is unable to produce at a competitive price, and so on. An example of a fatal-flaw entry barrier is experience. Linda Collier, former Canadian Woman Entrepreneur of the Year, president and CEO of Tri-ad International Freight Forwarding (i.e., air, sea, land) was doing "brisk business" and wanted to expand. She "hired a vice-president to assist with that task. Eight months later, he launched a rival company, taking five Tri-ad employees with him." Fortunately for Collier, the VP had a fatal flaw: inexperience. "This industry is easy to get into. To stay and grow in it is completely different." Within six months his business was bankrupt. This incident with her VP was the second of four tries her employees have made to come after her business. "I must make it look easy," Collier jokes. She has since put multiple measures in place to protect databases, customer profiles, service rates, and non-compete agreements to stymie staff from becoming competitors.³⁰

Personal Criteria

Goals and Fit. Is there a good match between the requirements of business and what the founders want out of it? The crux of this is contained in the adage: "Success is getting what you want. Happiness is wanting what you get."

Upside/Downside Issues. An attractive opportunity does not have excessive downside risk. The upside and the downside of pursuing an opportunity are not linear, nor are they on the same continuum. The upside is easy, and it has been said that success has a thousand sires. The downside is another matter; it has also been said that failure is an orphan. An entrepreneur needs to be able to absorb the financial downside in such a way that he or she can rebound without becoming indentured to debt obligations. If an entrepreneur's financial exposure in launching the venture is greater than his or her net worth—the resources he or she can reasonably draw upon, and his or her alternative disposable earnings stream if it does not work out—the deal may be too big. While today's bankruptcy laws are generous, the psychological burdens of living through such an ordeal are infinitely more painful than the financial consequences. An existing business needs to consider if a failure will be too demeaning to the firm's reputation and future credibility, aside from the obvious financial consequences.³¹

Opportunity Cost. In pursuing any venture opportunity, there are also opportunity costs. An entrepreneur who is skilled enough to grow a successful, multi-million-dollar venture has talents that are highly valued by medium- to large-size firms as well. While assessing benefits that may accrue in pursuing an opportunity, an entrepreneur needs to heed other alternatives, including potential "golden handcuffs," and account honestly for any cut in salary that may be involved in pursuing a certain opportunity.

Further, pursuing an opportunity can shape an entrepreneur in ways that are hard to imagine. An entrepreneur will probably have time to execute between two and four multi-million-dollar ventures between the ages of 25 and 50. Each of these experiences will position him or her, *for better or for worse*, for the next opportunity. Since an entrepreneur in the early years needs to gain relevant management experience and since building a venture (either one that works or one that does not) takes more time than is commonly believed, it is important to consider alternatives while assessing an opportunity.

Desirability. A good opportunity is not only attractive but also desirable (i.e., good opportunity fits). An intensely personal criterion would be the desire for a certain lifestyle. This desire may preclude pursuing certain opportunities that may be excellent for someone else. The founders of new start-ups are taking time to consider the location of their work. Basing that decision on a telephone area code, favourite mountain bike trail, or a host of other social, cultural, and demographic characteristics of a city or region. Richard Florida of the University of Toronto delivered a keynote address in Saint John, New Brunswick.³² Florida, drawing on his latest book *Who's Your City?* highlights that the creative economy is making the place where you live the most important decision of your life. Place is not only important, it's more important than ever. Place is becoming more relevant to our individual lives. Where to live is not an arbitrary choice.

Risk/Reward Tolerance. Successful entrepreneurs take calculated risks or avoid risks they do not need to take. This is not to suggest that all entrepreneurs are gamblers or have the same risk tolerance; some are quite conservative while others actually seem to get a kick out of the inherent danger and thrill in higher risk and higher stake games. The real issue is fit—recognizing that gamblers and overly risk-averse entrepreneurs are unlikely to sustain any long-term successes.

Stress Tolerance. Another important dimension of the fit concept is the stressful requirements of a fast-growth high-stakes venture. But having to keep up may not be the sole reason for stress. One investigation of the 62 serial entrepreneurs in the 2007 Profit 100 found that the initial start-up stage was the most stressful time.³³ Brik Eksten of Markham, Ontario-based Digital Rapids Corp., which helps TV and film producers place content on the Internet, notes that things get easier the more ventures you have under your belt: Eksten went from "only the worried survive" to "there will always be setbacks. Eventually, you become accustomed to a certain level of bombardment." A 2008 study published in the *Journal of Business Venturing* revealed that thinking and planning for the future may reduce the stress an entrepreneur faces.³⁴

Strategic Differentiation

Degree of Fit. To what extent is there a good fit among the driving forces (founders and team, opportunity, and resource requirements) and the timing given the external environment?

Team. There is no substitute for an absolutely top quality team. The execution of and the ability to adapt and to devise constantly new strategies is vital to survival and success. A team is nearly unstoppable if it can inculcate into the venture a philosophy and culture of superior learning, as well as teaching skills, an ethic of high standards, delivery of results, and constant improvement. Are they free agents—clear of employment, noncompete, proprietary rights, and trade secret agreements—who are able to pursue the opportunity?

Service Management. Research was conducted across a wide range of industries with several hundred companies to determine why customers stopped buying these companies' products. The results were surprising: 15 percent of the customers defected because of quality and 70 percent stopped using a product or service because of bad customer service. Having a "turbo-service" concept that can be delivered consistently can be a major competitive weapon against small and large competitors alike. Home Depot, in the home supply business, and Lexus, in the auto industry, have set an entirely new standard of service for their respective industries. Studies have also shown that service recovery is an important ingredient. When things do go wrong, what transpires to "recover" can be crucial: We're sorry your meal is late, how can we make it up to you? We apologize for overbooking, how can we make this right? A loyal customer is worth a lot. Customer relations can be managed and the best individuals and organizations have learned how to keep customers loyal.

Timing. From business to historic military battles to political campaigns, timing is often the one element that can make a significant difference. Time can be an enemy or a friend; being too early or too late can be fatal. The key is to row with the tide, not against it. Strategically, ignoring this principle is perilous.

Technology. A breakthrough, proprietary product is no guarantee of success, but it creates a formidable competitive advantage (see Exhibit 3.8).

Flexibility. Maintaining the capacity to commit and uncommit quickly, to adapt, and to abandon if necessary is a major strategic weapon, particularly when competing with larger organizations. Larger firms can typically take six years or more to change basic strategy and 10 to 20 years or more to change the culture.

Opportunity Orientation. To what extent is there a constant alertness to the marketplace? A continual search for opportunities? As one insightful entrepreneur put it, "Any opportunity that just comes in the door to us, we do not consider an opportunity. And we do not have a strategy until we are saying no to lots of opportunities."

Pricing. One common mistake of new companies, with high-value-added products or services in a growing market, is to underprice. A price slightly below to as much as 20 percent below competitors is rationalized as necessary to gain market entry. In a 30-percent gross margin business, a 10-percent price increase results in a 20 to 36-percent increase in gross margin and will lower the breakeven sales level for a company with \$900,000 in fixed costs to \$2.5 million from \$3 million. At the \$3-million sales level, the company would realize an extra \$180,000 in pre-tax profits.

Distribution Channels. Having access to the distribution channels is sometimes overlooked or taken for granted. New channels of distribution can leapfrog and demolish traditional channels;³⁵ for example, direct mail, home shopping networks, infomercials, the World Wide Web, and the coming revolution in interactive television in your own home.

Room for Error. How forgiving is the business and the financial strategy? How wrong can the team be in estimates of revenue costs, cash flow, timing, and capital requirements? How bad can things get, yet be able to survive? If some single-engine planes are more prone to accidents, by 10 or more times, which plane do you want to fly in? High leverage, lower gross margins, and lower operating margins are the signals in a small company of flights destined for fatality.

EXHIBIT 3.8 Canadian Inventions in the 20th Century

Hydrofoil boat	Alexander Bell and Casey Baldwin (1908)
Jolly Jumper	Olivia Pool (1910)
Variable pitch propeller	Wallace Turnbull (1918)
Ski-Doo	Armand Bombardier (1922)
Snowblower	Arthur Sicard (1925)
Quartz clock	Warren Marrison (1927)
Pablum	Alan Brown, Theodore Drake, and Frederick Tisdall (1930)
Plexiglass	William Chalmers (1931)
Scanning electron microscope	James Hillier and Albert Prebus (1939)
Paintroller	Norman Breakey (1940)
Walkie-talkie	Donald L. Hings (1942)
Garbage bag	Harry Wasylyk and Larry Hansen (1950)
Electric wheelchair	George Klein (1952)
Instant replay	CBC's Hockey Night in Canada (1955)
Alkaline battery	Lewis Urry (1959)
Wonderbra	Louise Poirier (1964)
IMAX	Grahame Ferguson, Roman Kroitor, and Robert Kerr (1968)
UV degradable plastics	James Guillet (1971)
Computerized Braille	Roland Galarneau (1972)
Digital film colourization	Wilson Markle and Brian Hunt (1983)
Abdominizer	Dennis Colonello (1984)
Newt suit	Phil Nuytten (1987)
CPR mannequin	Diane Croteau and Richard Brault (1989)
Infant stretcher	Wendy Murphy (1990)

GATHERING INFORMATION**Finding Ideas**

Finding a potential opportunity is most often a matter of being the right person, in the right place, at the right time. Certainly past experience and industry exposure can help, but one also has to be tuned in and astutely listening. Creativity again plays a role in sense-making and generating connections to make mental leaps. How can you increase your chances of being the next Anita Roddick of The Body Shop or Ablan Leon of Leon's Furniture? Numerous sources of information can help generate ideas.

Existing Businesses Purchasing an ongoing business is an excellent way to find a new business idea. Such a route to a new venture can save time and money and can reduce risk as well. Investment bankers and business brokers are knowledgeable about businesses for sale, as are trust officers. However, brokers do not advertise the very best private businesses for sale, and the real gems are usually bought by the individuals or firms closest to them, such as management, directors, customers, suppliers, or financial backers. Bankruptcy judges have a continual flow of ventures in serious trouble. Excellent opportunities may be buried beneath all the financial debris of a bankrupt firm.

Franchises Franchising is another way to enter an industry, by either starting a franchise operation or becoming a franchisee. This is a fertile area. The number of franchisors nationally stands at more than 400, according to the Canadian Franchise Association and franchisors account for well over \$100 billion in sales annually and approximately one-fifth of all retail sales. See Chapter 13 "Franchising" for a more complete discussion of franchises, including resource information.

Patents Patent brokers specialize in marketing patents that are owned by individual inventors, corporations, universities, or other research organizations to those seeking new commercially viable products. Some brokers specialize in international product licensing, and occasionally a patent broker will purchase an invention and then resell it. Although, over the years, a few unscrupulous brokers have tarnished the patent broker's image, acquisitions effected by reputable brokers have resulted in significant new products. For example, Bausch & Lomb acquired, through National Patent Development Corporation, the rights to hydron, a material used in contact lenses. Some patent brokers are:

- Inventarium, Montréal, Québec
- Furman & Kallio, Regina, Saskatchewan
- Battison Williams Dupuis, Winnipeg, Manitoba
- Mario Theriault & Co., Fredericton, New Brunswick
- Stewart McKelvey, Halifax, Nova Scotia and the rest of Atlantic Canada
- Adams Patent & Trademark Agency, Kanata, Ontario
- Semiconductor Insights, Kanata, Ontario
- Borden Ladner Gervais, nationwide, Canada
- Smart & Biggar/Fetherstonaugh, nationwide, Canada
- McCarthy Tétrault, nationwide, Canada

Product Licensing A good way to obtain exposure to many product ideas available from universities, corporations, and independent investors is to subscribe to information services such as the *American Bulletin of International Technology*, *Selected Business Ventures* (published by General Electric), *Technology Mart*, *Patent Licensing Gazette*, and the National Technical Information Service. In addition, corporations, not-for-profit research institutions, and universities are sources of ideas.

Corporations. Corporations engaged in R&D often develop inventions or services that they do not exploit commercially. These inventions either do not fit existing product lines or marketing programs or do not represent sufficiently large markets to be interesting to major corporations. A good number of such corporations license these kinds of inventions, either through patent brokers, product-licensing information services, or their own patent-marketing efforts. Directly contacting a corporation with a licensing program may prove fruitful. Among the major corporations known to have active internal patent-marketing efforts are the following:

- Mosaid³⁶
- Texas Instruments
- Nortel Networks
- Intel
- Dow Chemical
- Volkswagen
- Juniper Networks

Not-for-Profit Research Institutes. These non-profit organizations do R&D under contract to the government and private industry as well as some internally sponsored investigation of new products and processes that can be licensed to private corporations for further development, manufacturing, and marketing. One example of how this works is

Battelle Memorial Institute's participation in the development of xerography and the subsequent license of the technology to the Haloid Corporation, now Xerox Corporation. Canada's National Research Council (NRC) is composed of over 20 institutes with active licensing programs.

Universities. A number of universities are active in research in the physical sciences and seek to license inventions that result from this research either directly or through an associated research foundation that administers its patent program. Massachusetts Institute of Technology and the California Institute of Technology publish periodic reports containing abstracts of inventions they own that are available for licensing. In addition, since a number of very good ideas developed in universities never reach formal licensing outlets, another way to find these ideas is to become familiar with the work of researchers in your area of interest. Among the universities that have active licensing programs are:

- University of Alberta
- University of British Columbia
- University of Waterloo
- McMaster University
- Carleton University
- University of Montréal
- Memorial University of Newfoundland

Industry and Trade Contacts

Trade Shows and Association Meetings. Trade shows and association meetings in a number of industries can be an excellent way to examine the products of many potential competitors, meet distributors and sales representatives, learn of product and market trends, and identify potential products. The Canadian Photonics Consortium is a good example of an association that holds such seminars and meetings.

Customers. Contacting potential customers of a certain type of product can identify a need and where existing products might be deficient or inadequate. Discussions with doctors who head medical services at hospitals might lead to product ideas in the biomedical equipment business.

Distributors and Wholesalers. Contacting people who distribute a certain type of product can yield extensive information about the strengths and weaknesses of existing products and the kinds of product improvements and new products that are needed by customers.

Competitors. Examining products offered by companies competing in an industry can show whether an existing design is protected by patent and whether it can be improved or imitated.

Former Employers. A number of businesses are started with products or services, or both, based on technology and ideas developed by entrepreneurs while others employed them. In some cases, research laboratories were not interested in commercial exploitation of technology, or the previous employer was not interested in the ideas for new products, and the rights were given up or sold. In others, the ideas were developed under government contract and were in the public domain. In addition, some companies will help entrepreneurs set up companies in return for equity. Nortel Networks has done this repeatedly.

Professional Contact. Ideas can also be found by contacting such professionals as patent agents, accountants, commercial bankers, and venture capitalists who come into contact with those seeking to license patents or to start a business using patented products or processes.

Consulting. A method for obtaining ideas that has been successful for technically trained entrepreneurs is to provide consulting and one-of-a-kind engineering designs for people in fields of interest. For example, an entrepreneur wanting to establish a medical equipment company can do consulting or can design experimental equipment for medical researchers.

These kinds of activities often lead to prototypes that can be turned into products needed by a number of researchers. For example, this approach was used in establishing a company to produce psychological testing equipment that evolved from consulting done at a hospital. In another instance the design and manufacture of oceanographic instruments came out of what was developed from consulting done for an oceanographic institute.

Networking. Social networks can be a stimulant and source of new ideas, as well as a source of valuable contacts with people. Much of this requires personal initiative on an informal basis, but around the country, organized networks can facilitate and accelerate the process of making contacts and finding new business ideas. The Digital Moose Lounge is a network for Canadian expatriates living in Silicon Valley and greater San Francisco Bay area. TiE (The Indus Entrepreneurs) is another such organization; with its genesis in Silicon Valley it has grown to over 50 chapters in a dozen countries. Outside of Canada, most Canadian embassies and consulates organize Terry Fox Runs—a great chance to meet up with fellow Canadians.

Shaping Your Opportunity

You will need to invest in thorough research to shape your idea into an opportunity. *Data available about market characteristics, competitors, and so on, are frequently inversely related to the real potential of an opportunity;* that is, if market data are readily available and if the data clearly show significant potential, then a large number of competitors will enter the market and the opportunity will diminish.

The good news: Most data will be incomplete, inaccurate, and contradictory, and their meaning will be ambiguous. For entrepreneurs, gathering the necessary information and seeing possibilities and making linkages where others see only chaos are essential.

Jonathan Calof, director of the Canadian Institute of Competitive Intelligence, defined competitor intelligence as specific and timely information about a business adversary. Finding out about competitors' sales plans, key elements of their corporate strategies, the capacity of their plants and the technology used in them, who their principal suppliers and customers are, and what new products rivals have under development is difficult, but not impossible, even in emerging industries, when talking to intelligence sources.³⁷

Using published resources is one source of such information. Interviewing people and analyzing data are also critical. Leonard Fuld believes that because business transactions generate information, which flows into the public domain, one can locate intelligence sources by understanding the transaction and how intelligence behaves and flows.³⁸

This can be done legally and ethically. There are, of course, less-than-ethical (not to mention illegal) tactics, which include conducting phony job interviews, getting customers to put out phony bid requests, and lying, cheating, and stealing. Entrepreneurs need to be very careful to avoid such practices and are advised to consult legal counsel when in doubt.

The information sources provided on the next page are just a small start. Much creativity, work, and analysis will be involved to find intelligence and to extend the information obtained into useful form. For example, a competitor's income statement and balance sheet will rarely be handed out. Rather, this information must be derived from information in public filings or news articles or from credit reports, financial ratios, and interviews many of which are available on the Internet.³⁹

PUBLISHED SOURCES

The first step is a complete search of materials in libraries and on the Internet. You can find a huge amount of published information, databases, and other sources about industries, markets, competitors, and personnel. Some of this information will have been uncovered when you search for ideas. Listed below are additional sources that should help get you started.

Guides and Company Information

Valuable information is available in special issues and the Web sites of *Business 2.0*, *Canadian Business*, *INC.*, *Fast Company*, *Mercury News*, and *Fortune*.

Additional Sources of Intelligence

Everything entrepreneurs need to know will not be found in libraries because this information needs to be highly specific and current. This information is most likely available from people—industry experts, suppliers, and the like. Summarized below are some useful sources of intelligence.

Trade Associations Trade associations, especially the editors of their publications and information officers, are good sources of information. Trade shows and conferences are prime places to discover the latest activities of competitors.⁴⁰

Employees Employees who have left a competitor's company often can provide information about the competitor, especially if the employee departed on bad terms. Also, a firm can hire people away from a competitor. While consideration of ethics in this situation is very important, the number of experienced people in any industry is limited, and competitors must prove that a company hired a person intentionally to get specific trade secrets in order to challenge any hiring legally. Students who have worked for competitors are another source of information.

Consulting Firms Consulting firms frequently conduct industry studies and then make this information available. Frequently, in such fields as computers or software, competitors use the same design consultants, and these consultants can be sources of information.

Market Research Firms Firms doing market studies, such as those listed under published sources above, can be sources of intelligence.

Key Customers, Manufacturers, Suppliers, Distributors, and Buyers These groups are often a prime source of information.

Public Filings Federal, provincial, and local filings, such as with the Canadian Securities Administrators, Canadian Intellectual Property Office, or Access to Information Act, can reveal a surprising amount of information. There are companies that process inquiries of this type.

Reverse Engineering Reverse engineering can be used to determine costs of production and sometimes even manufacturing methods. An example of this practice is the experience of Advanced Energy Technology, which learned firsthand about such tactics. No sooner had it announced a new product, which was patented, when it received 50 orders, half of which were from competitors asking for only one or two of the items.

Networks The networks mentioned in Chapter 2 as sources of new venture ideas also can be sources of competitor intelligence.

Other Classified ads, buyers guides, labour unions, real estate agents, courts, local reporters, and so on, can all provide clues.⁴¹

INTERNET IMPACT: RESEARCH AND LEARNING

The Internet has become the resource for entrepreneurial research and opportunity exploration. The rapid growth of data sources, Web sites, sophisticated search engines, and consumer response forums allows for up-to-date investigations of business ideas, competitive environments, and value chain resources.

Google is currently the top search engine in the world. One of the reasons for Google's success is its increasingly deep and wide platform of tools. Google offers the means to view, for example, the text of patents and scholarly publications, archives of news stories, and blogs on hundreds of subjects.

As virtual communities of people who share a common interest or passion, blogs can be a tremendously valuable resource of insights and perspectives on potential opportunities. Proactive, low- or no-cost research can also be conducted with emailed questionnaires or by directing potential subjects to a basic Web site set up to collect responses. In addition, the Internet provides entrepreneurs and other proactive searchers with the extraordinary capability to tap wisdom and advice from experts on virtually anything—anywhere in the world.

SCREENING VENTURE OPPORTUNITIES

Time is the ultimate ally and enemy of the entrepreneur. The harsh reality is that you will not have enough time in a quarter, a year, or a decade to pursue all the ideas for businesses you and your team can think of. Perhaps the cruelest part of the paradox is that you have to find and make the time for the good ones. To complicate the paradox, you do not have a strategy until you are saying no to lots of opportunities! This demand is part of the both punishing and rewarding Darwinian aspect of entrepreneurship: Many will try, many will fail, some will succeed, and a few will excel. While the number of new enterprises launched in Canada can vary widely from year to year, only a small percentage of those will ever prove to be opportunities that achieve sales of \$1 million or more. Many live by the creed: "Go big or go home!" and feel being bold is critical to getting noticed. Studies show that those who are outspoken are rewarded more.

QuickScreen

If most sophisticated private equity investors and venture capitalists invest in only 2 to 3 out of 100 ideas, then one can see how important it is to focus on a few superior ideas. The ability to quickly and efficiently reject ideas is a very important entrepreneurial mind-set. To make the struggle more manageable, two methodologies are provided on the Online Learning Centre at www.mcgrawhill.ca/olc/timmons. The first, QuickScreen, should enable you to conduct a preliminary review and evaluation of an idea in an hour. Unless the idea has been, or you are confident it can be, moulded and shaped so that it has the four anchors, you will waste a lot of time on a lower potential idea.

Venture Opportunity Screening Exercises (VOSE)

The second methodology, the Venture Opportunity Screening Exercises, is also located on the Online Learning Centre at www.mcgrawhill.ca/olc/timmons. These exercises are designed to segment the screening of ideas into manageable pieces. The QuickScreen provides a broad overview of an idea's potential. In a team effort, each member of the team should complete the exercise separately and then meet as a team to merge the results. After each VOSE, you should revisit the QuickScreen and reevaluate your scoring.

Chapter Summary

1. Ideas are a dime a dozen. Perhaps 1 out of 100 becomes a truly great business, and 1 in 10 to 15 becomes a higher potential business. The complex transformation of an idea into a true opportunity is akin to a caterpillar becoming a butterfly.
2. High potential opportunities invariably solve an important problem, want, or need that someone is willing to pay for now. In renowned venture capitalist Arthur Rock's words: "I look for ideas that will change the way people live and work."
3. There are decided patterns in superior opportunities, and recognizing these patterns is an entrepreneurial skill aspiring entrepreneurs need to develop.
4. Rapid changes and disruptions in technology, regulation, information flows, and the like cause opportunity creation. The journey from idea to high potential opportunity requires navigating an undulating, constantly changing, three-dimensional relief map while inventing the vehicle and road map along the way.
5. Some of the best opportunities actually require some of the least amount of capital, especially via the Internet.
6. The best opportunities often don't start out that way. They are crafted, shaped, moulded, and reinvented in real time and market space. Fit with the entrepreneur and resources, the timing, and the balance of risk and reward govern the ultimate potential.
7. The highest potential ventures are found in high growth markets, with high gross margins, and robust free cash flow characteristics, because their underlying products or services add significantly greater value to the customer, compared with the next best alternatives.
8. Trial and error. Learning-by-doing alone is not enough for developing breakthrough ventures, which require experience, creativity, and conceptualizing.

Study Questions

1. What is the difference between an idea and a good opportunity?
2. Why is it said that ideas are a dime a dozen?
3. What role does experience play in the opportunity creation process, and where do most good opportunities come from? Why is trial-and-error learning not good enough?
4. List the sources of ideas that are most relevant to your personal interests, and conduct a search using the Internet.
5. What conditions and changes that may occur in society and the economy spawn and drive future opportunities? List as many as you can think of as you consider the next 10 years.
6. Evaluate your best idea against the summary criteria in Exhibit 3.7. What appears to be its potential? What has to happen to convert it into a high potential business?

Mind Stretchers *Have you considered?*

1. Steve Jobs and Steve Wozniak, co-founders of Apple, were kids when they built their first computers. Colonel Sanders was 65 years old when he started to expand Kentucky Fried Chicken. What is an opportunity for whom?
2. Most successful existing businesses are totally preoccupied with their most important, existing customers and therefore lack the peripheral opportunity vision to spot new products and services. Is this happening where you work? Is this an opportunity for you?
3. The most successful ventures have leadership and people as important competitive advantages. How does this change the way you think about opportunities?
4. Who can you work with during the next few years to learn a business and have the chance to spot new opportunities outside the weak peripheral vision of an established business?
5. Barriers to entry can create opportunities for those with the right knowledge and experience. Why is this so? Can you find some examples?

EXERCISE Idea Generation Guide

Before beginning the process of generating ideas for new ventures, it is useful to reflect on an old German proverb that says, "Every beginning is hard." If you allow yourself to think creatively, you will be surprised at the number of interesting ideas you can generate once you begin.

The Idea Generation Guide is an exercise in generating ideas. The aim is for you to generate as many interesting ideas

as possible. *While generating your ideas, do not evaluate them or worry about their implementation.* Discussion and exercises in the rest of the book will allow you to evaluate these ideas to see if they are opportunities and to consider your own personal entrepreneurial strategy.

And remember—in any creative endeavour there are no right answers.

Name: _____

Date: _____

Step 1

Generate a list of as many new venture ideas as possible.

As a consumer or paid user, think of the biggest, most frustrating, and painful task or situation you continually must take, and one which would be worth a lot to eliminate or minimize. These are often the seeds of real opportunities. Thinking about any unmet or poorly filled customer needs you know of that have resulted from regulatory changes, technological changes, knowledge and information gaps, lags, asymmetries, inconsistencies, and so forth, will help you generate such a list. Also, think about various products and services (and their substitutes) and the providers of these products or services. If you know of any weaknesses or vulnerabilities, you may discover new venture ideas.

Step 2

Expand your list if possible. Think about your personal interests, your desired lifestyle, your values, what you feel you are likely to do very well, and contributions you would like to make.

Step 3

Ask at least three people who know you well to look at your list, and revise your list to reflect any new ideas emerging from this exchange. See the discussion about getting feedback in Chapter 1.

Step 4

Jot down insights, observations, and conclusions that have emerged about your business ideas or your personal preferences. Which ones solve the greatest pain-point/aggravation/frustration for which you (and others you have spoken with) would pay a significant premium to eliminate?

CASE

WE BUILT IT, NOW WILL THEY COME? bOK SYSTEMS CORP.

Preparation Questions

1. If you were the CEO of bOK Systems which option or combination of options would you choose?
2. How would you go about implementing those choices?

The Problem

Aydin Mirzaee was about to graduate with a degree in Electrical and Computer Engineering and a minor in Entrepreneurship and Management. While in school, Aydin found it almost impossible to effectively use his cellphone. Cellphones were obviously very convenient as they were portable. Unfortunately, in Canada, cellphone use was not practical from a price perspective.

Aydin had a cellphone plan that included 100 daytime outgoing minutes. If he ever used more than his allotted minutes, his phone company would charge him approximately 35 cents a minute. This meant that an hour-long conversation would cost

over \$20. Long distance calls to cities within Canada or to the U.S. were equally expensive (e.g., calling another city such as Montreal, Toronto, or Calgary cost him about 35 cents a minute).

Having grown up in New York, Aydin found it very expensive to call his family and friends to keep in touch. Calling cards were an option, but they were definitely not hassle free. With calling cards, one had to dial a 1-800 number and then enter an access code. Every time the calling card ran out of funds, a trip to the convenience store was necessary to purchase another one. With a busy schedule, this was not convenient. As a student, having a \$100/month cellphone bill was not easy to justify. This was not just a problem for Aydin but one that was shared

This case was written by Aydin Y. Mirzaee and Prescott C. Ensign, for purposes of classroom discussion.

by many. A better alternative was needed. This realization was what led Aydin to start bOK Systems (www.bOKnow.com).

bOK Systems was Aydin's first major start-up and was proving to be a great learning experience. It was now October 2007, nearly 18 months after graduation, Aydin worked full-time for a large multinational telecommunications equipment manufacturer and was discovering that living the life of an entrepreneur had its glamour and fun times but it also had its share of challenges, stressful decisions, and sleepless nights.

The Solution

The structure of cellphone plans in Canada led Aydin to wonder if there was a way to transform all outgoing calls into incoming ones. If such a method could be discovered, then this would potentially give him the opportunity to make as many calls as he wanted to without using up his daytime minutes. The idea was simply this:

Instead of just calling someone directly, one could...

1. Compose a text message that contained the destination number.
2. Send this text message to the bOK number.
3. Receive an incoming call. Pick up and talk.

For example, assume that Amanda lives in Ottawa and would like to call her friend Jill in New York. Amanda creates a text message that contains nothing but Jill's phone number in New York, which is: 7185207734. She sends this text message to the bOK Ottawa number, which is: 6132552437. After about 5–10 seconds, both Amanda and Jill receive a local incoming call on their phones. When they pick up, they can start talking. In the process, Jill will not notice a difference in the way she receives the call. Amanda saves money and the friends can talk for as long as they want.

The advantage here was that one could initiate a call as an incoming one rather than an outgoing one and anyone with an unlimited incoming call plan, would not use up their minutes. The destination party would not notice a difference between a call initiated through bOK and one initiated through conventional means.

This all sounded very nice. However, there was a long way to go. Aydin spoke to his brother Amin at McGill about the idea and together they set forth the plan to complete the project. The process was long and arduous. Aydin and Amin decided

to bring two other engineers on board, an accomplished mathematician from Chicago also studying at McGill and a cousin in Toronto to help create the final product. After about three to four months of work, the first version of bOK was ready. The first version was really more a test than anything else.

The founders started using bOK on their own. They told a few friends but made sure to tell them not to spread the word. Almost overnight, about 150 people started using the system to make their phone calls. The traffic was too high for the platform in place at the time to handle. It was for this reason that the founders had to shut down the system and go back to the drawing board. Except, what they realized was that there was a lot of interest in the product that they had put together. This was very exciting and it was the beginning of their business endeavour. The founders realized that this could be turned into a very viable operation if a good business model were put together.

The business model originally conceived would allow users to call any location in North America or internationally for prices lower than what phone cards offered. bOK would be able to undercut phone card prices as they would be dealing directly with end consumers whereas phone card companies had to deal with many intermediaries before their product reached their target customers. This was a unique business model and everyone was quite excited about the possibilities.

Alternatives

The bOK founding team had to make a decision on what to do and it needed to act fast as things were changing rapidly around them. The truth was that bOK was late to market and this made things difficult. At the time, a few options came to mind:

1. Quit and try a new idea.
2. Tweak the idea to make bOK ahead of the game.
3. Obtain venture capital/angel funding.
4. Attempt to sell the product/firm.
5. Bring in a new CEO.
6. Quit all other engagements and focus on bOK full time.

The options were many and each required further analysis. Aydin wondered as CEO, which option he should choose? There may be no "right answer" in business, but some paths were better than others. And how would he go about implementing his decisions?

C · H · A · P · T · E · R

4

THE BUSINESS PLAN

Madame, enclosed please find the novel you commissioned. It is in two volumes. If I had had more time I could have written it in one.

Voltaire

RESULTS EXPECTED

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

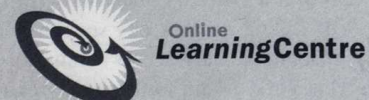
1. Utilize a business plan model proven and refined through years of use.
2. Determine what needs to be included in the plan, why, and for whom. Remember, the business plan (which is not the business!) is written for an intended audience.
3. Identify some of the pitfalls in the business plan preparation process and how to avoid these.
4. Appreciate what has to be done to develop and complete a business plan for your proposed venture.
5. See that a well-articulated business plan is an important part of the entrepreneurial process, not an end in itself.
6. Critically examine a business plan developed by a young entrepreneur to raise capital for Chide.it—a new crowdsourcing Internet venture.

RESULTS EXPECTED

DEVELOPING THE BUSINESS PLAN

The business plan itself is the culmination of a usually lengthy, arduous, creative, and iterative process that, as we explored in Chapter 3 and the accompanying exercises, can transform a raw idea into a magnificent opportunity. The plan will carefully articulate the merits, requirements, risks, and potential rewards of the opportunity and how it will be seized. It will demonstrate how the *Four Anchors* noted below (and in the online exercises for Chapter 3) reveal themselves to the founders and investors by converting all the research, careful thought, and creative problem solving from the online Venture Opportunity Screening Exercises into a thorough plan. The business plan for a high potential venture reveals the business's ability to:

- **Create** or add significant value to a customer or end-user.
- **Solve** a significant problem, or meet a significant want or need for which someone will pay a premium.



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