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Entre-preneur-ship

Entrepreneurship

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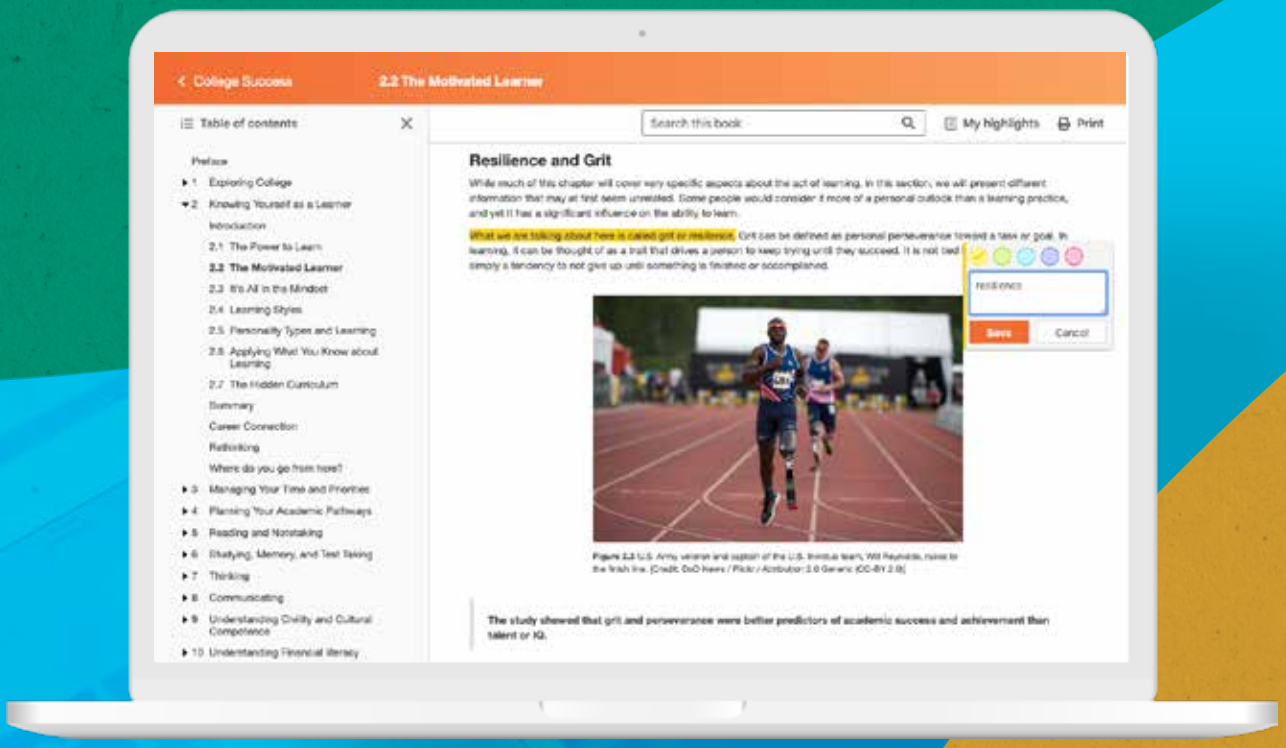

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Preface

Welcome to *Entrepreneurship*, an OpenStax resource. This textbook was written to increase student access to high-quality learning materials, maintaining highest standards of academic rigor at little to no cost.

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About *Entrepreneurship*

Entrepreneurship is designed to meet the course needs of a one-semester undergraduate course on the subject. This resource will cover the key principles of entrepreneurship alongside the concepts, strategies, and tools needed to succeed as a small business owner, franchisee, founder, or other entrepreneurial professional.

Coverage and scope

Our *Entrepreneurship* textbook aligns to the scope and sequence of most introductory entrepreneurship courses. We have endeavored to make the core theories and practical concepts engaging, relevant, and accessible to students. We sought to achieve this by relating concepts to everyday life, contemporary issues, and the real-world challenges that students may face as twenty-first century entrepreneurs.

Entrepreneurship course coverage and approach varies greatly by institution. Some programs focus on research or cases, others on simulation or competition, and many synthesize a variety of approaches. While OpenStax engaged a wide array of faculty reviewers, opinions differ based on the purpose, audience, and structure of the course. The material's open licensing enables you to customize the content and incorporate additional resources in order to fit your course goals.

Engaging Feature Boxes

Throughout *Entrepreneurship*, you will find features that engage students by taking selected topics a step further and challenge students to apply what they are learning. Each feature box contains either a link to a deeper exploration of the topic at hand or critical thinking questions that may be geared toward class discussion, student projects, or written essays. Our features include:

- **Work It Out.** This feature presents entrepreneurial opportunities or dilemmas for which students are asked to work out a solution.
- **Are You Ready?** Students are asked to reflect on their readiness for applying the chapter's concepts in these integrated exercises, partial plans, or scenarios of a plan or project.
- **What Can You Do?** This feature challenges students to take the role of a social entrepreneur and balance a host of interests, some conflicting, as they explore possible venture opportunities.
- **Entrepreneur in Action.** Chapter-relevant entrepreneurial endeavors are profiled so students can examine the real-life efforts of entrepreneurs.
- **Link to Learning** This feature provides online resources and videos that are pertinent to students' deeper exploration of the topics. Link to Learning boxes allow students to connect easily to some of the most important thought leaders and concepts in the field.

Module materials that reinforce key concepts

- **Learning Objectives.** Every module begins with a set of clear and concise learning objectives. These objectives are designed to help the instructor decide what content to include or assign, and to guide students on what they can expect to learn. After completing the module and end-of-module exercises, students should be able to demonstrate mastery of the learning objectives.
- **Summaries.** Section summaries distill the information in each module for both students and instructors down to key, concise points addressed in the section.
- **Key Terms.** Key terms are bold and are followed by a definition in context. Definitions of key terms are also listed in the glossary, which appears at the end of the module online and at the end of the chapter in print.
- **Assessments.** Review, discussion, and case questions accompany every chapter, providing opportunities for students to recall, discuss, and examine the concepts learned in each chapter.
- **Suggested Resources** Each chapter concludes with a collection of additional resource links to provide budding entrepreneurs with additional resources to support their entrepreneurial goals.

Answers to Questions in the Book

Answer to all Review Questions and Case Questions are provided in the Instructor Answer Guide via the Instructor Resources page. Due to the high variability of responses and the focus on critical thinking, answers to Work It Out, Are You Ready, and What Can You Do questions are not provided.

Additional resources

Student and instructor resources

We've compiled additional resources for both students and instructors, including Getting Started Guides Companion PowerPoints, an Instructor Solution Guide, and a Test Bank. Instructor resources require a verified instructor account, which you can apply for when you log in or create your account on openstax.org.

Instructor and student resources are typically available within a few months after the book's initial publication. Take advantage of these resources to supplement your OpenStax book.

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1 The Entrepreneurial Perspective

Figure 1.1 Phil Libin, former CEO of Evernote, discusses his product. Evernote is an app that allows users to create notes in a variety of formats and save and share them across platforms. (credit (a): modification of "Phil Libin and Loic Le Meur - LeWeb Day 1 - Dan Taylor/Heisenberg Media" by Heisenberg Media/Flickr, CC BY 2.0; credit (b): modification of "screenshot of the old Evernote iPhone app" by Jason Jones/Flickr, CC BY 2.0)

Chapter Outline

1.1 Entrepreneurship Today
1.2 Entrepreneurial Vision and Goals
1.3 The Entrepreneurial Mindset

Introduction

Phil Libin, cofounder and former CEO of Evernote, once said there are "lots of bad reasons to start a company. But there's only one good, legitimate reason . . . it's to change the world."[1] Evernote is an example of an entrepreneurial startup. Its goal is to make our lives more organized and increase our personal memory abilities by storing necessary and desired information on the Evernote app. Evernote is designed to capture information through note taking (including pictures, web pages, drawings, and even audio), track and organize this material, and then save and archive the information. Evernote Corporation describes itself as "not only an organization, rather it is a family of professionals who are creative, innovative and experienced in their respective fields."[2]

Around the globe, individuals, communities, and organizations advocate for and support the entrepreneurship movement. Many colleges and universities offer courses, degrees, and competitions for entrepreneurship teams. Communities provide support through services such as incubators that foster planning and startup activities. Organizations like UNESCO's Global Action Programme on Education for Sustainable Development holds a Youth Entrepreneurship Competition annually.[3] That is where student Chloe Huang, in 2017, submitted her idea for an algae energy pavilion to the Education for Sustainable Development competition. Huang recognized the problem of lakes suffering from oversaturation of algae and saw a solution in converting the algae into a biofuel, creating green energy while alleviating an environmental problem.[4]

1 Robin Wauters. "Evernote CEO Phil Libin: 'My Advice to Aspiring Entrepreneurs? Don't Do It.'" *The Next Web.* April 27, 2012. https://thenextweb.com/video/2012/04/27/evernote-ceo-phil-libin-my-advice-to-aspiring-entrepreneurs-dont-do-it-video/
2 "Evernote SuccessStory." *SuccessStory.* June 24, 2018. https://successstory.com/products/evernote

In the examples of both Libin and Huang, the entrepreneurial products focus on the use of technology and improving life, but they also represent two vastly different approaches to entrepreneurship. Libin's focus was on improving quality of life by allowing users to track and organize information in their business and personal lives, whereas Huang focused on a global environmental issue to sustainably improve water quality. Each idea solves a problem that many people might not even have noticed. Becoming aware of problems that need to be solved, then solving the problem to make our lives easier or better, is part of the entrepreneurial perspective.

1.1 Entrepreneurship Today

Learning Objectives

By the end of this section, you will be able to:

- Define entrepreneur and entrepreneurship
- Describe types of entrepreneurial careers and lifestyles
- Understand entrepreneurs as problem solvers
- Explain current factors driving the growth of entrepreneurship
- Compare differences in entrepreneurial opportunities around the globe

As we delve into the study of entrepreneurship, let's define what we mean by the word *entrepreneur*. An **entrepreneur** is someone who identifies and acts on an idea or problem that no one else has identified or acted on. This combination of recognizing an opportunity to bring something new to the world and acting on that opportunity is what distinguishes an entrepreneur from a small business owner. A small business owner is someone who owns or starts a business that already has an existing model, such as a restaurant, whereas an entrepreneur is someone who creates something new. This new creation can be a new process or product, a business that identifies a new or unique target market, or a combination of ideas that creates a new approach or method, for example.

In a broader sense, what people consider an *entrepreneur* can vary. Some scholars strictly differentiate between entrepreneurs and small business owners.[5] Others acknowledge that a small business owner may also be an entrepreneur—they are not mutually exclusive. Someone may start a venture that is not a completely new idea, but that introduces a product or service to a new region or market. Where does a franchise fall in this discussion? Again, there is not complete agreement, with some claiming that a franchisee and entrepreneur cannot be the same, and others arguing that a franchise is, indeed, an entrepreneurial venture. According to an article in *Forbes*, "In the for-profit world, an entrepreneur is someone who creates and runs a new business where one did not exist before. And, no, the McDonald's franchisee didn't create McDonald's. But he certainly created a McDonald's where there never was one before. Franchisees are entrepreneurs."[6] The point is that small business owners and franchisees can be considered entrepreneurs. For the purposes of this course, you will learn the key principles of entrepreneurship alongside the concepts, strategies, and tools needed to succeed as a small business owner or franchisee.

Entrepreneurs have many different talents and focus on a variety of different areas, taking advantage of many opportunities for entrepreneurial ventures. An **entrepreneurial venture** is the creation of any business, organization, project, or operation of interest that includes a level of risk in acting on an opportunity that has not previously been established. For some entrepreneurs, this could be a for-profit venture; for other entrepreneurs, this could be a venture focused on social needs and take the form of a nonprofit endeavor.

3 UNESCO. "Global Action Programme on Education for Sustainable Development." n.d. https://en.unesco.org/gap
4 Chloe Huang. "Algae Energy Pavilion." *Entrepreneurship Campus.* August 1, 2017. https://www.entrepreneurship-campus.org/ideas/14/7404/
5 Hamid Bouchikhi. "A Constructivist Framework for Understanding Entrepreneurship Performance." *Organization Studies.* July 1, 1993. doi.org/10.1177/017084069301400405; William D. Bygrave and Charles W. Hofer. "Theorizing about Entrepreneurship." *Entrepreneurship Theory and Practice* 16, no. 2 (1991): 13–22.; Michael A. Hitt, R. Duane Ireland, S. Michael Camp, and Donald L. Sexton. *Strategic Entrepreneurship: Creating a New Mindset.* (Hoboken, NJ: Wiley-Blackwell, 2002).; Jeffry A. Timmons. *New Venture Creation: Entrepreneurship for the 21st Century.* (Irwin Press, Burr Ridge, IL: Irwin Press, 1994).
6 Paul B. Brown. "Franchisees Are Entrepreneurs (Let the Debate Begin)." *Forbes.* September 19, 2012. https://www.forbes.com/sites/actiontrumpseverything/2012/09/19/franchisees-are-entrepreneurs-let-the-debate-begin/#55c9fb8f2bf3

Entrepreneurs might take a variety of approaches to their entrepreneurial venture, such as those shown in Table 1.1.

Types of Entrepreneurs

Type of Entrepreneur	Approach to Venture
Innovators	Find new approaches, methods, or products that add value through solving a problem in a unique manner
Creators	Make something new or see a problem that other people have not noticed
Market makers	Innovate or reinvent their market from a future perspective by asking what the market could evolve into
Expanders and scalers	Seek out opportunities to expand upon previously created methods, processes, or products

Table 1.1

In this course, you will explore these myriad avenues toward entrepreneurship.

ARE YOU READY?

How Do You Define Success?

What is your personal definition of success? How would you define success for your venture idea? Take time to consider these questions carefully.

- Write your answers to both questions as formal descriptions of your definition of success.
- After completing your definitions, meet with your family members or your personal support group (the important people whose support you need to achieve the defined success statement) to discuss your personal definition of success.
- After hearing their input, you might want to revise your personal success statements.

Follow through with this activity by talking to your startup team or other supporting people about your venture's success definition. This activity may help guide you in decision-making throughout your life journey and the journey of starting your venture. It will also be helpful when you and your startup team create a vision statement for your venture.

The Entrepreneurial Lifestyle and Career

People often have thought of entrepreneurs as corporate rebels, nonconformists, or activists. Being an entrepreneur has become synonymous with being an innovator, a change agent, or a risk taker. Regardless of job titles or descriptive characteristics, entrepreneurship has a universal appeal for how people think and engage with the world.

Choosing the path of entrepreneurship requires a willingness to take on calculated risks. The difference between risk and *calculated* risk is **due diligence**, or conducting the necessary research and investigation to make informed decisions that minimize risk. Not everyone is comfortable letting go of a steady paycheck, especially when we know that there is no long-term guarantee that the paycheck will continue into the future.

In one approach to minimizing personal financial risk, some startup entrepreneurs continue with their current employment while working on the side to develop their idea into a venture that eventually will generate an income. Until the venture requires near full-time work and generates income, maintaining an outside income works well for many entrepreneurial teams.

Consider the eyeglass startup Warby Parker (Figure 1.2). Dave Gilboa and Neil Blumenthal, lead entrepreneurs for Warby Parker, were still working their normal jobs when they approached an angel investor with their idea. The angel investor asked a few questions and wasn't impressed. This investor believed that Gilboa and Blumenthal should demonstrate their solid commitment to the venture by quitting their day jobs to dedicate more time and energy to Warby Parker. Instead of following that advice, Gilboa and Blumenthal kept their day jobs while they continued to work toward building their venture, and Warby Parker eventually became highly successful. There are many paths to becoming an entrepreneur, and many paths to creating a successful venture (see Entrepreneurial Journey and Pathways). It is important to identify the path that works best in your life—and for the venture—and that supports your goals and your unique situation and visions.

(a) (b)

Figure 1.2 (a) Co-founder and co-CEO Dave Gilboa helped push (b) Warby Parker to become a successful entrepreneurial venture. (credit (a): modification of "775208326EC00084_TechCrunch" by TechCrunch/Flickr, CC BY 2.0; credit (b): modification of "Warby Parker Aventura Mall" by Phillip Pessar/Flickr, CC BY 2.0)

Within the entrepreneurial world, the idea of a **lifestyle venture** has evolved to mean a business in which the founders' primary focus is the lifestyle they will attain through becoming entrepreneurs, rather than a primary interest in financial rewards through the selling of the business. Within the entrepreneurial world, harvesting is the typical exit strategy. The **harvest** is the point at which the investors and entrepreneurial team receive their return on creating and building the venture.

For a lifestyle venture, the entrepreneur is more likely to be a solo entrepreneur, someone who moves forward in starting a new venture without the support of a team or group of likeminded individuals who recognize the value or potential of an entrepreneurial idea that could potentially result in significant returns. A lifestyle venture is also more likely to be funded through family and friends, and more traditional methods such as a bank loan or a small business loan. This lifestyle includes greater freedom to decide areas of responsibilities, hours of contribution to the venture, and other decisions that support the desired lifestyle. An example of a startup lifestyle venture is The Wander Girls, a company that identified the unique concerns of women traveling alone.[7] The Wander Girls organizes trips and events for groups of women traveling in India. A team member organizes the trip, travels with the female tourists, and handles daily interactions and transactions.

Another example of a lifestyle venture is based on how an entrepreneur aligns values, interests, and passions to create a balance between enjoying life and earning enough money to support those passions. Roxanne Quimby had a passion for living off the grid, creating her own life in the woods of Maine, and not being restricted by the rules and regulations required when working as an employee. After becoming a parent, Quimby faced the challenges presented by her lifestyle choices and started making candles to earn enough money to support her family. Eventually, Quimby's lifestyle candle-making business expanded into the highly successful Burt's Bees Corporation, moving her lifestyle business into a career as the CEO of Burt's Bees

7 The Wander Girls. n.d. http://thewandergirls.com/

(Figure 1.3). After selling Burt's Bees to Clorox Co., Quimby continued her passion for the north woods of Maine by donating land and money to create a wildlife sanctuary and preserve that land from development.

Figure 1.3 The Burt's Bees product line grew from an idea for a lifestyle entrepreneurial venture into a major company. (credit: "Burt's Bees" by Carol Bleistine/Flickr, CC BY 4.0)

Quimby's latest endeavors include creating a pasta company, My Pasta Art, focused on increasing employment opportunities for people in northern Maine,[8] and building the tourist industry to encourage people to enjoy the region's beautiful habitat and scenery. Although she is highly successful from a financial perspective, money was never the motivation for her ventures. As you can see, there are many paths to finding your career in entrepreneurship, and multiple trigger points at which you might make the decision to become an entrepreneur.

WHAT CAN YOU DO?

How Can You Put Your Strengths to Work?

Create a list of ten strengths that you currently possess. If you need help creating your list, ask your friends or family what they believe you are good at doing. Think about what achievements you have accomplished, what compliments you have received, and what people say about you. The answers to these questions will help you identify your strengths.

- Create a list of ideas that build off your strengths or are related to your strengths.
- Then analyze this list to create another list of possible businesses that you could start that relate to your strengths.

The Entrepreneur as a Problem Solver

What are some challenges you face in your life? Have you ever actively thought about how you could solve those problems? Or have you actively identified exactly what the problem is from an analytical perspective? We often have a tendency to jump quickly from noticing a problem to selecting a solution, with little understanding of whether we have even correctly identified the problem. Identifying the problem—and testing the potential, novelty, and feasibility of your solution—is an important part of resolving the problem. Often, when we start to explore the problem, we find that it has multiple causes. Among them are:

- The need for something to be better, faster, or easier
- The effects of changes in world on your industry, product, or service
- Market trends based on geography, demographics, or the psychology of the customers

8 Mary Pols. "Making Pasta's the New Focus for Roxanne Quimby." *Portland Press Herald*. August 13, 2017.

You will learn more about identifying opportunities in Identifying Entrepreneurial Opportunity and Problem Solving and Need Recognition Techniques.

One characteristic of a savvy entrepreneur is recognizing the ability to identify a problem from an opportunity-identification perspective. We might identify feeling hungry as a problem, but an entrepreneur would identify the problem using an **opportunity-identifying perspective** by determining how the problem could be translated into an opportunity to create a new venture—perhaps combining the problem of feeling hungry between meals into a street kiosk or a vending machine with food choices or creating a new snack that is nutritious, satisfying, and portable. People need to eat, and they get hungry, but during a busy day with no open time or convenient food, people end up hungry. Rephrasing the problem, or need, from an opportunity viewpoint opens the search for a sustainable solution beyond the simple awareness of feeling hungry. We might solve this problem by opening a snack bar with offerings that contain essential vitamins and proteins, and is easy to transport with a long shelf life. Understanding the problem from the perspective of how to solve it for one person into how to solve it for multiple people rephrases the problem into an opportunity-identification perspective.

You might also have an interest in solving food-related problems on a larger scale. People trapped in a war-torn region may not be able to leave the safety of their shelters to find food, grow food, or barter for food, or they may not have the money to buy food. How could you reach your target market within a war-torn area? Red Cross emergency response vehicles traveled 2.5 million miles to deliver food, relief supplies, and support to communities affected by disasters during 2017.[9] That's the equivalent of driving around the globe 103 times. Could your idea of creating a snack bar fit into a partnership with the Red Cross?

Although this might seem like a simple problem with a simple solution, persevering from the recognition of a problem to finding a realistic solution, then moving that solution forward into a successful venture, requires an entrepreneurial mindset. Every day, people become entrepreneurs as they identify and solve problems, or face new challenges or frustrations, and resolve them in creating products or services to address these issues.

WHAT CAN YOU DO?

Recognizing Problems

In your daily life, what problems do you encounter? What would make your life easier? How would you finish this sentence: "If only _____ existed, my life would be better or easier"? To spur your creativity, you might research global problems to find an area that interests you, that sparks your passion for living a fulfilling life. When identifying a problem, consider process-related problems as well as service-related problems.

For more ideas like Chloe Huang's, visit the UNESCO Global Action Programme on Education for Sustainable Development (https://en.unesco.org/gap) and review other submissions that may activate your own creativity in thinking about how you want to contribute your skills and knowledge to improve our world.

- What problem have you identified?
- What can you do to resolve that problem?

9 American Red Cross. "2017 in Review: Red Cross Delivers More Food, Relief Items, and Shelter Stays Than Last 4 Years Combined." December 18, 2017. https://www.redcross.org/local/georgia/about-us/news-and-events/news/2017-in-Review-Red-Cross-Delivers-More-Food-Relief-Items-and-Shelter-Stays-than-Last-4-Years-Combined.html

Factors Driving the Growth of Entrepreneurship

Do you know anyone who has lost their job? Or who has been rejected or mistreated at work? Or had their income reduced, or benefits removed? Research shows that 47 percent of all US employment is at risk through artificial intelligence and other technologies, although there will also be new opportunities for jobs that currently don't exist.[10] These types of experiences and outlooks have provided the impetus for many people to start their own businesses. When we work for someone else, we are at the mercy of their decisions and actions, but we get paid and don't carry the full risk of their decisions. When we work for ourselves, we get to make the decisions (not that making decisions is easy). But when we have our own business, we have greater control—in exchange, we also carry the risk for all decisions we make. This control over decision-making is one reason that some people find the world of entrepreneurship attractive.

Another contributing factor to the desire to become an entrepreneur is the excitement and fun of creating something new. Many entrepreneurs are excited at the idea of moving the concept through to the materialization of the idea.

A third factor that supports the growth in entrepreneurship is the combination of retirement and longer life expectancies. Many people enjoy working. For them, retirement consists of too much open time and not enough activities or the type of engagement with the outside world that fulfilled their needs during their working lives. Retirement also presents unique financial considerations, depending on an individual's lifetime savings and planning. The combination of having available time and a desire for continued earnings encourages some older adults to explore their own entrepreneurial opportunities.

A fourth factor driving the growth of entrepreneurship is the expanding awareness and support of entrepreneurship as a viable career choice. In much of the twentieth century, families encouraged their children to find a stable career with a large corporation. During this era, there was a certain expectation of reciprocal loyalty between the employer and the employee based on some traditional employee-employer roles in that century. The general, informal agreement was that if employees came to work every day and fulfilled their responsibilities, they would have long-term employment with that corporation. But as competition increased and new business practices evolved, this unspoken guarantee no longer held true. The model of certainty of employment gradually disappeared. As people acquired a new perspective on their careers and income, they increasingly realized that we are all responsible for our own paths. Most studies suggest that people change their careers between three and seven times.[11] Note that this is not how often people change jobs, but how often they change their careers, moving from one industry to another, or moving from one type of work to a different type of work. The older model of stability through working hard for someone else has vanished. This awareness and acceptance have encouraged recent generations to consider creating their own futures through entrepreneurial ventures.

Just as individuals have become aware of the benefits of entrepreneurship, communities and organizations have also become aware of how entrepreneurial ventures add economic development and enhancements worth supporting, bolstering opportunities for those who decide on this path.

Entrepreneurship around the Globe

In the United States, entrepreneurial opportunities abound, relatively speaking. Between 1990 and 2014, the number of campus-based entrepreneurship education programs increased from 180 to over 2,000.[12] Comparing globally, the United States has the greatest number of entrepreneurial ventures, with Switzerland, Canada, Sweden, Denmark, and Australia following in order, according to Global Entrepreneurship Index, a global consulting firm (Figure 1.4).

10 Carl Benedikt Frey and Michael A. Osborne. "The Future of Employment: How Susceptible Are Jobs to Computerization?" *Technological Forecasting and Social Change* 114 (2013): 254–280. https://www.oxfordmartin.ox.ac.uk/downloads/academic/The_Future_of_Employment.pdf

11 Dawn Rosenberg McKay. "How Often Do People Change Careers?" *The Balance*. September 20, 2019. https://www.thebalancecareers.com/how-often-do-people-change-careers-3969407

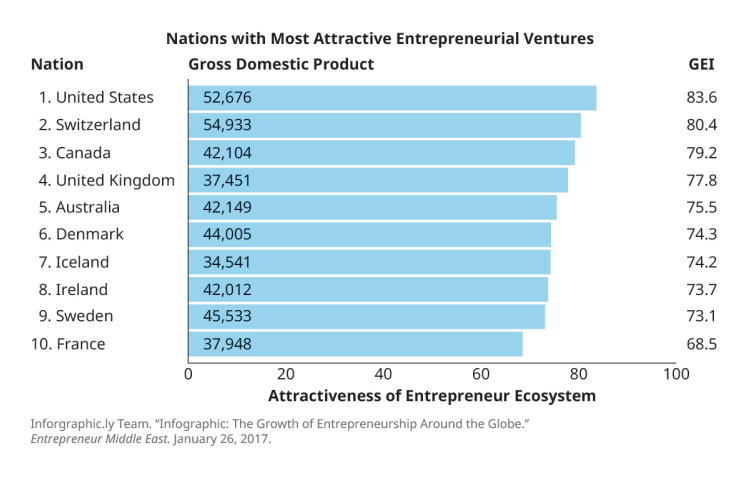

Figure 1.4 The number of entrepreneurial businesses, in millions, is shown for several countries. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Why is the United States leading with the greatest number of entrepreneurial ventures? What does it take to become an entrepreneur? In addition to having an entrepreneurial mindset (see The Entrepreneurial Mindset), entrepreneurs also need education and funding to support their new ventures.

You will learn more about funding in Entrepreneurial Finance and Accounting, but as an introduction, you should know there are three primary sources of outside funding: family and friends, angel investors, and venture capitalists. Some family members and friends are willing and able to invest money in helping the entrepreneurial team. An angel investor is someone who has available funds and an interest in supporting a new venture. They are often entrepreneurs who have successfully launched and harvested their own ventures, and who have an interest in helping other entrepreneurs in their startups, staying active in the entrepreneurial world, and a desire to receive a return on their investment in the venture. Angel investors often provide funding early in the life of a venture. As the venture grows, it typically requires more funding, at which time venture capitalists may invest in the venture. A venture capitalist (VC) is a group of people (or organizations) who pool resources to invest in entrepreneurial ventures, contributing larger sums of funds than are available through angel investors. In each funding round, investors receive an equity stake in the venture with expectations that at some point in the future, the venture will be sold, or harvested, at which time the investors will receive a return on their investment. Because they tend to be in larger groups, VCs typically have access to larger amounts of money and resources than individual angel investors. (You will also learn about other types of financing, such as bank loans and bootstrapping, in Entrepreneurial Finance and Accounting.)

In the United States, VCs contributed $72.3 billion in 2015 for 3,916 deals, or funding rounds. In China that same year, $49.2 billion were invested in 1,611 ventures.[13] European VC investment totaled $14.4 billion and 1,598 deals. Tracking these numbers over time shows steady increases in VC funding as entrepreneurial ventures have become more common (Figure 1.5).

12 Infographic.ly Team. "Infograpic: The Growth of Entrepreneurship around the Globe." *Entrepreneur Middle East*. January 26, 2017. https://www.entrepreneur.com/article/288286
13 Infographic.ly Team. "Infographic: The Growth of Entrepreneurship around the Globe." *Entrepreneur Middle East*. January 26, 2017. https://www.entrepreneur.com/article/288286

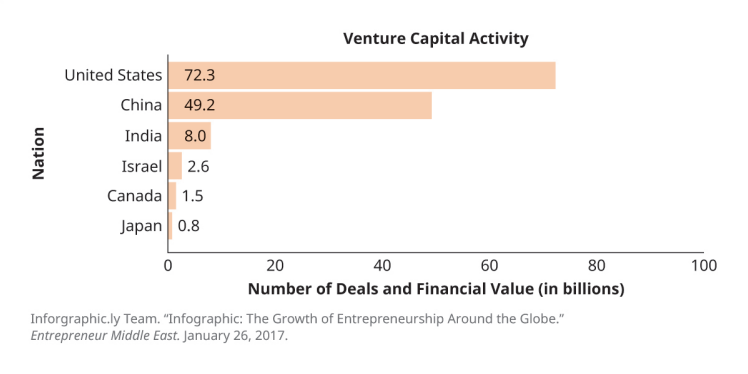

Figure 1.5 The total venture capitalist investment and number of deals for several countries are shown. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Other factors that can affect entrepreneurial opportunity include employment rates, government policies, and trade issues. For example, in the Middle Eastern kingdom of Saudi Arabia, a newer driver of entrepreneurship includes a high unemployment rate with a large percentage of the population in its prime earning years. In the past, employment was less of a concern because of dependency on state support from oil revenue. The population received monthly allotments to cover expenses from state-owned oil production. More recently, the population has become restless, with a desire to become productive and have greater control over their own resources. And the rulers recognize that oil production income is volatile and unsustainable. Today, with more future-oriented leaders, countries in the Middle East desire to encourage their citizens to consider starting their own businesses.[14] The example of entrepreneurship in the United States has spread around the globe, with other countries taking an interest in developing support systems to encourage their populations to become entrepreneurs.

As noted, the United States is a world leader in entrepreneurial innovation. Perhaps because the United States is, in large part, a nation of immigrants, with people arriving from all over the world, Americans have few prescribed traditions that encourage conformity. America's longstanding traditions and reputation for individualism, ingenuity, and self-reliance have reinforced this mindset. However, the governments of other nations have discouraged their citizens from independent or innovative thinking. Some cultures emphasize political, cultural, and economic unity, and place a strong value on not being noticed, blending in, and following prescribed habits and traditions. Countries like Japan, France, Russia, China, and others continue to reflect these norms. Other countries have complex bureaucracies that prevent quick responses and place barriers to entrepreneurial activities. Parts of worldwide economic structures (banking, investments, and technology) are not accessible or even explicitly exclude some nations and the poor. Systems like this discourage people from coming forward with entrepreneurial ideas because the culture and bureaucracy prevent people from finding access to information necessary for the successful advancement of an idea. In contrast, other countries are noticing the benefits of encouraging their populations to become more open-minded and creative through new ventures.

LINK TO LEARNING

Transparency International is an organization that tracks corruption, which can be an inhibitor to entrepreneurship. The Transparency International website (https://openstax.org/l/52TransparencyI) provides information to rank 180 countries in identifying the abuse of entrusted power for private gain.[15]

Key characteristics that encourage entrepreneurship include support for freedom to create and innovate. What

14 Infographic.ly Team. "Infographic: The Growth of Entrepreneurship around the Globe." *Entrepreneur Middle East*. January 26, 2017. https://www.entrepreneur.com/article/288286
15 Transparency International. n.d. www.transparency.org

conditions encourage creativity and innovation? Acceptance of failure is a key characteristic for success as an entrepreneur. Many of the great inventions in the United States resulted after dozens of failures, as when Thomas Edison eventually developed a working light bulb. Edison identified a problem: Once the sun set, working hours were restricted, as were daily activities such as reading a book or washing dishes. Edison, along with many other inventors, recognized the need for an artificial light source. Consider how complex this idea was and how many failures must have occurred before creating a product that emitted light.

Another condition that encourages entrepreneurial behavior is the ability and opportunity to connect with other people to discuss ideas, problems, challenges, and solutions. This connection with other people, in an open environment that supports the exchange of ideas, is essential for encouraging creativity and innovation.

With the advent of the Internet, people around the planet are becoming increasingly aware of geopolitical and environmental situations across the globe. As more people observe these changes and situations, more people exchange ideas. These discussions can generate new opportunities for people to discover methods for solving problems. Any one of us could be living in one country but identifying a problem in another country. Given our interests and backgrounds, we could actively choose to develop a solution for that problem. What we need, as a general approach, is an efficient and transparent way to form companies and enable constructive competition, along with continued free and fair trade.

These are just some of the areas that many nations and organizations consider as they seek to encourage a transition away from group-prescribed thinking toward uniquely individual entrepreneurial ideas. Each of us encounters life from a different perspective. Although we all might recognize the restrictions presented by the sun setting every night, only a few people might question why we couldn't change that situation by creating our own light. Similarly, someone in another country may observe our country (or vice versa) and ask why that country has a particular problem. Meanwhile, people living with that problem may have become so accustomed to it that they might not recognize the opportunity to seek solutions.

Increasing opportunities in entrepreneurial education are also driving growth. More colleges and universities are teaching entrepreneurial studies and opening entrepreneurial centers that encourage students from every discipline to become entrepreneurs.[16,17] As the employment and entrepreneurial landscape continue to evolve, some institutions have started offering courses to prepare students for work in the gig economy.[18] In fact, some of the best new entrepreneurial ideas come from groups of students in different majors who collaborate to create new, innovative business ideas that meet specific needs and challenges in today's world. In some cases, students from different universities around the globe are connecting to come up with business ideas to solve global problems, such as the lack of clean drinking water and the need for medical vaccination programs. Technology and global travel have made such partnerships more common and very productive.

The world of entrepreneurship opens doors for each of us to look beyond our own self-created barriers and explore opportunities around the world. Consider the creation of Starbucks, borne from the realization of how pleasant it can be to sit at a European café and drink excellent coffee. Awareness of an idea that is commonplace in one country, but new to a different country, presents the possibility of introducing that idea to another nation. In the Starbucks example, was there a problem that needed to be solved? Not necessarily, but the founder, Howard Schultz, had a desire to bring a specific quality-of-life element from one country to another, a business idea with an entrepreneurial aspect. One of the entrepreneurial aspects of creating Starbucks was the idea of mass expansion of coffee shops. Prior to Starbucks, the idea of creating a high-quality coffee drink hadn't been developed. Even more significant was the idea of expanding the business across the United States and then around the world.

16 National Survey of Entrepreneurship Education. n.d. www.nationalsurvey.org
17 "The Princeton Review & Entrepreneur Name the Top Undergraduate & Graduate Schools for Entrepreneurship Studies for 2020." Cision PR Network. November 12, 2019. https://www.prnewswire.com/news-releases/the-princeton-review--entrepreneur-name-the-top-undergraduate--graduate-schools-for-entrepreneurship-studies-for-2020-300955876.html
18 Diane Mulcahy. "Universities Should Be Preparing Students for the Gig Economy." *Harvard Business Review*. October 3, 2019. https://hbr.org/2019/10/universities-should-be-preparing-students-for-the-gig-economy

Given the growth of coffee shops throughout the United States, we might not think that this idea is innovative, but before Starbucks, coffee typically was served at a diner, and it was served out of habit, rather than as the main attraction. With Starbucks, people changed their ideas about coffee and their coffee-drinking habits. Although businesses like Dunkin' Donuts served coffee, their focus was on selling donuts, not coffee. As Starbucks grew through repositioning coffee as their main product, other companies like Dunkin' Donuts and McDonalds realized the missed opportunity in not reinventing the coffee market with multiple choices of high-quality coffee. In fact, Dunkin' Donuts has changed its name to just "Dunkin," removing the emphasis on doughnuts.[19]

Social and Environmental Issues and Opportunities

A **social entrepreneur** has an interest in solving a social, environmental, or economic problem. A social entrepreneur identifies a problem with a social or community focus, a concern for quality of life, or concern for our entire planet's health (you will learn more about social entrepreneurship in The Ethical and Social Responsibilities of Entrepreneurs). One such person is Angad Daryani, a young serial inventor. Daryani left school in the ninth grade to join the Media Lab at the Massachusetts Institute of Technology (MIT), where he worked on an industrial-scale air filter to clean pollutants and carcinogens out of our planet's air. Daryani's home country of India is the world's third largest emitter of carbon dioxide, according to Global Carbon Atlas, behind China and the United States (Figure 1.6).[20]

Figure 1.6 The Mumbai skyline is clouded by hazy pollution. (credit: modification of "Smog over Mumbai" by Christian Haugen/Flickr, CC BY 2.0)

WHAT CAN YOU DO?

Social Entrepreneurship

Consider a social issue that you might feel compelled to take on as a passion project. Some social issues include childhood hunger, access to clean water, access to education, or opioid abuse. Watch Johann Hari's Ted Talk on addiction (https://openstax.org/l/52HariTedTalk) to learn more.

- Do you have any ideas for creating an entrepreneurial venture around the idea of building quality relationships and communities?
- How would you balance a passion project with an entrepreneurial purpose?

Not only is Daryani interested in solutions for air pollution, but his product will also provide financial gains and

19 Kate Taylor. "Dunkin' Donuts Is Officially Dropping the 'Donuts' from Its Name Despite Earlier Backlash." *Business Insider*. September 25, 2018. https://www.businessinsider.com/dunkin-donuts-changes-name-no-donuts-2018-9
20 "Fossil Fuel Emissions." Global Carbon Atlas. 2017. http://www.globalcarbonatlas.org/en/CO2-emissions

add to his personal credibility as a **serial entrepreneur**, or someone who starts and harvests multiple entrepreneurial ventures. Darvani describes himself as an inventor and social entrepreneur, combining his interest in improving lives through a variety of entrepreneurial ventures including products like Sharkits (a do-it-yourself-kit company that teaches children how to build technology), the SharkBot 3D Printer (an attractive, low-cost, and reliable 3D printer), and several other projects that combine technology and human needs. As each of these products advances to commercialization, the products and technology are becoming more applicable for other uses as well. For more examples of projects that Darvani is working on, take a look at his website (http://www.angadmakes.com), which includes videos and articles, and highlights the international recognition he has received for his innovative work.

ENTREPRENEUR IN ACTION

Angad Daryani

Research Angad Daryani and his technology to remove air pollution (https://www.cnn.com/2018/03/28/health/angad-daryani-tomorrows-hero/index.html).

- What other products could this technology or methodology be used for, besides the originally intended application of improving air quality?
- What critical decisions would you anticipate that Angad will face in creating and commercializing his product?
- How would you define success for Angad or this air-cleaning company?

1.2 Entrepreneurial Vision and Goals

Learning Objectives

By the end of this section, you will be able to:

- Define an entrepreneurial vision
- Develop a vision statement

When you think of yourself as a successful entrepreneur, what types of images or feelings do you experience? Do you find yourself daydreaming about creating the next great solution to society's problems, or do you see yourself providing a solution for the next health or environmental crisis? Maybe you can imagine yourself creating something that equally balances art, function, and ingenuity.

This section is designed to help you develop your entrepreneurial vision. Vision is an important part of everyone's future, and this is especially true for entrepreneurs. Establishing your vision is the first of several steps toward making your venture a reality.

Many would-be entrepreneurs aspire to launch the next great business or organization that will change the world. Some know exactly what they want to create, whereas others figure it out as they go along. Although there is no secret to success, you do need to have some idea about what you envision for your entrepreneurial future. What do you see in your future? How do you want to contribute to the world?

Entrepreneurial Vision

Every successful entrepreneur that you encounter or read about likely started with an image or idea related to something he or she felt passionate about creating. This occurs even when the person has no idea how (or if) what they desire to accomplish or create will become a reality. An entrepreneur's vision is the start of a roadmap that will determine where he or she wants to go with their entrepreneurial efforts. Vision speaks to what the entrepreneur wants the business to look like in the future—perhaps five or ten years out. Unfortunately, many potential entrepreneurs have dreams and ideas but never develop a concrete vision. A

vision statement is the picture you have for what the venture will become in the future: what it will grow into. Be aware, though, that oftentimes, the identified vision at the start of the venture changes into something different. In later chapters, we discuss how this change requires open-mindedness and a willingness to adapt. The **mission statement** is a formal declaration about what the venture will do, what value it will provide to the end customer, and how it will accomplish this action. In describing your mission, carefully think about the value proposition that you provide. The **value proposition** is a summary statement that conveys the benefits your product, service, or unique business process/model provides to customers. This relates back to the perspective of problem solving. Not only do you need to solve the problem, but you also must provide value. We might solve a problem, but if the value proposition isn't relevant or seen as "real" by the customer, the venture will probably not be successful. Both concepts of a future vision and the mission of the venture should be formalized into statements.

In spite of your best efforts, you may have trouble putting your entrepreneurial vision on paper. This is normal, especially in the early stages of the process. You may want to start with an outline and fill in the details later. Or set aside a short time each day that you can spend on this task so you train your mind to think about the vision you are setting for yourself. If you experience a mental block, try changing your environment—go outside, try a different time of day, or go to a setting that has similarities to the business you are interested in creating. You might also consider talking with someone who has experience in the industry to give you suggestions. Or better yet, find a mentor in your chosen area of interest and keep this person apprised of your progress. Having someone to bounce ideas off is a great asset to have when imagining the possibilities of the future.

WORK IT OUT

Finding a Mentor

Mentorships can provide you with numerous benefits (Figure 1.7).

Figure 1.7 Finding a mentor can provide you with invaluable benefits. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Read the article at https://www.forbes.com/sites/goncalodevasconcelos/2017/11/02/my-best-advice-for-entrepreneurs-find-a-mentor-this-is-why-and-how/#2bec86b1d469 on the benefits of having a mentor, and click on the resources the author provides in the article.

Then read the article at https://www.inc.com/young-entrepreneur-council/4-types-of-mentors-every-young-entrepreneur-should-have.html, which discusses types of mentors. Notice that in this second article, the author focuses on sales, operations, business development, and entrepreneurial experience as the most significant areas that need expertise for startups.

Next, describe the areas that you would want help from a mentor for learning and developing your business idea. Then, list a few possible avenues where you could find a mentor who fits your needs. Considering the information in these articles, how would this information help you develop your statements and describe your value proposition?

An **entrepreneurial vision** considers what you want your venture to become, what this venture will look like, what the driving forces are, and what values and culture should surround it. Each individual entrepreneur has a unique picture of what the venture will become. For example, Kevin F. Adler wanted to help homeless people. He created Miracle Messages, a volunteer-based nonprofit organization with a goal of helping homeless people reconnect with loved ones. The vision for this organization includes building a vast network of volunteers and partnerships to stop homelessness and bring people together. This vision is about creating community, helping each other, and strengthening communities. The business model encourages homeless people to create short Miracle Messages through video, audio, or text, with messages then uploaded to social media and other methods to find that person's loved one.

WHAT CAN YOU DO?

Globalizing Miracle Messages

Go to the website www.miraclemessages.org to learn about the vision and mission of Miracle Messages. Their slogan, "Everyone is someone's somebody," conveys their culture of care and concern for all human life. As you read about this organization, consider what this organization could become in the future, with an extensive network that supports connecting volunteers to homeless people, then to loved ones, and to other organizations that support the physical relocations and resources to address the original reasons why the person became homeless. How can this organization become a global business? Consider families dislocated through wars, famine, and other disasters who want to find their loved ones. The infrastructure developed with Miracle Messages could be replicated for other populations besides homeless people in the United States. Depending on the founder's vision, Miracle Messages could continue to focus on homelessness in the United States, or the vision could expand into other geographic areas and needs.

In an entrepreneurial venture, when the vision has a shorter timeline, such as five years, it could focus on a local problem or situation, and over time evolve into a vision that is broader and includes more diverse markets or populations. Your vision should inspire the people involved in your startup to support your venture. Use your imagination to create this picture of your venture with a focus on the future of the venture. Even though entrepreneurs use their imaginations and creativity in developing this picture, they also need to understand the venture's industry, the competition, and trends that are evolving or might evolve in the future. This information helps guide the vision for the venture and define how it is uniquely different from any other business. Ideally, the vision should be insightful, bold, inspirational, and believable, and it should be developed into a formal vision statement.

The vision statement should also be clearly stated and discussed with the startup team. Although you might

not have a startup team, a mentor, or a support group developed yet, to create an entrepreneurial venture, you will need support. Your support network understands that working without pay is often the normal situation at the beginning, with the potential for financial rewards coming when the venture is harvested or sold. For some entrepreneurs, knowing the vision includes the sale of the venture to another group or corporation is difficult to accept. However, that is the point at which the venture can grow to become ever more viable. Alternatively, if your vision is to be a small business owner, such as owning a franchise, then you are buying into a business plan package that has already fine-tuned the processes and decisions to support your success as the owner/manager of that business. A small business owner starts or buys into a business idea that already exists, whereas an entrepreneur is someone who seeks to create something new through either new products, services, methodologies, or combinations of ideas that create a new venture or organization.

The lead entrepreneur should share the vision statement with employees and investors, as these groups are formalized, communicating what this vision means personally and to the success of the venture. You might also need to revisit this vision as your venture grows, making changes based on your decisions and knowledge about your industry, products, and customers' needs. Even if your vision statement changes based on new information and decisions, creating an initial vision statement is a valuable step and will help guide your decisions.

ARE YOU READY?

A Personal Vision Statement

What do you want your life to look like ten to twenty years from now? Consider these questions:

- Where are you living?
- What are you doing for a living?
- What does your home look like?
- Who lives in your home?
- What are you doing with your life?

You could describe a typical workday and weekend day in your life as part of answering these questions. Create a vision statement that describes the answers to these questions.

Creative Approaches to Developing Your Vision

There are many definitions of and ways to express creativity (you will learn more about creativity in Creativity, Innovation, and Invention). Artists typically show their creative side in their art, musicians show their creativity through music, and writers express their creativity in writing. Others express technical creativity through cell phone innovations or new car technology. It is up to you to determine how you will express your creativity in your venture and in your professional life. In most cases, when people follow their passions, their creativity flows from that passion.

One approach to discovering your vision for your future is to begin with the end in mind. What picture of your desired future do you have in mind? How could this vision fit with the ideas you have of creating a successful venture? Notice that these questions are about both your personal future and the vision for your venture's future. These two pictures should coexist. The vision for your personal future should allow for the necessary resources to support the venture's future, just as the venture's future will provide for your personal future. We will discuss work-life balance later in the chapter to help you identify what creates success as you describe your vision.

Another approach to developing your vision is to use a creative thinking process. This type of thinking allows people to come up with ideas that they might not have had without adopting a creative mindset. The creative

thinking process (covered in more depth in Creativity, Innovation, and Invention) has four steps: preparation, incubation, illumination, and verification (Figure 1.8).

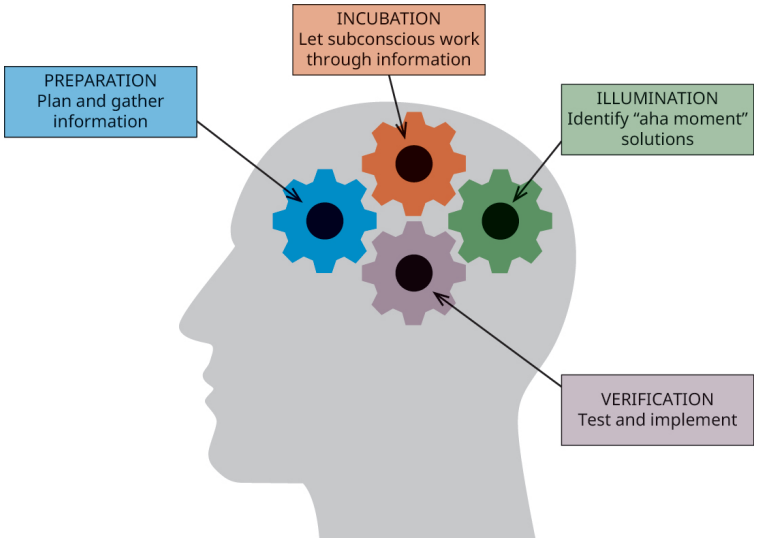

Figure 1.8 These are the four steps of the creative thinking process. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

In the preparation stage, gather information and collect ideas. As part of the process of tapping into creative ideas, you can apply **divergent thinking** by generating as many ideas as possible, even when those ideas do not seem logical. Create a list of conflicting ideas, or ideas that are diverse and disparate. *Preparation* is the first step of the creative thinking process. The next action is to walk away from thinking about the activity: *incubation*. We are programming our minds to realize that the work done in preparation is an important topic for consideration. When we walk away from consciously thinking about the activity or problem, we allow our unconscious minds to continue to think about the activity, even though our conscious minds are busy doing other things. This incubation period is essential for advancing creativity. In the incubation stage, you might go for a walk, take a nap, or just continue with your daily activities. At some point, you may have a sudden inspiration or *illumination*—an *aha!* moment—that clearly addresses the activity or problem you want to solve. In this step, the answer often pops into our conscious minds, and we recognize how to proceed. The last step is *verification*, crafting our vision statement or message, or responding to the exercise in creative thinking. You can apply this creative thinking process to many different business situations. Once we further develop and crystallize our ideas (the Business Model Canvas discussed in Launch for Growth to Success is a good tool for this activity), we provide an opening for a creative and viable solution as we continue to think about the issue.

Design thinking, brainstorming, and mind mapping are tools that you will learn about later in the course. Although these tools may be familiar, there are specific methodologies that can optimize their success in entrepreneurial situations. Brainstorming requires that participants generate ideas around the desired topic without judgment. You can do this alone or with others, but including other people provides a greater variety of ideas, as one person's ideas might trigger another idea from someone else. Be sure to write down your thoughts so that you can return to them later. Brainstorming is different from divergent thinking, which does not require ideas to be associated with the identified topic. For example, in brainstorming on the topic of helping the homeless population, we might come up with ideas such as finding community food and housing, or providing free medical care. Using divergent thinking, we would arrive at more diverse ideas, such as filming homeless people then uploading the videos to a social media website to connect family members with the homeless person. These tools could incorporate divergent thinking in the idea-generation step, but typically, unless people are taught how to use divergent thinking, the ideas generated are more structured and constrained, and more logical. As much as we want to encourage divergent ideas, we also want to discourage any judgment around our ideas. Once we start judging our ideas, we restrict our creativity and end up with less than ideal solutions. Approach this process with some playfulness and relaxation.

Mind mapping is another popular technique for creative thinking. Here, you create an illustration on paper or a chalk board. Write down the words that come to mind then link those words together with lines in a diagram that shows how each word relates to the others. The idea is that one word can lead to another. You can discover associations that might not have been evident before you created the mind map.

You can conduct research on entrepreneurial ideas by creating surveys and asking people questions about their experiences related to your idea. For example, let's say you are considering creating a new non-messy health food that can be eaten while commuting to work. You could ask people about their experiences eating while commuting to work or ask questions about nutritional concerns or diets. Or you could find secondary data on when people eat, eating while commuting, popular diets, or other related topics. Or you could find case studies that focus on a few in-depth similar areas of interest or perform your own case studies by selecting a few peers to track their eating habits. Or you could create a prototype of your product and ask people to tell you about their experience using your product. You will learn more about research strategies in Identifying Entrepreneurial Opportunity, Problem Solving and Need Recognition Techniques, and Entrepreneurial Marketing and Sales.

ARE YOU READY?

Creativity through a Change in Routine

Practice your creativity skills by changing your routine. Because our brains block out many routine activities, such as our commute to work, or other repetitious habits, we often fail to notice our surroundings. Pick one day this week to experience the world through a new perspective. Change your routine in as many ways as possible. As you change your routine, pay attention to how you are experiencing the day.

- What was the experience like?
- Did you notice being more alert to your surroundings?

Consider how you can use this experience to learn how to identify new opportunities and to interact with people, situations, and objects to identify problems in a way that could be translated into an entrepreneurial venture.

Achieving Balance

Entrepreneurship comes with many challenges because the entrepreneur must wear many hats. This is especially true if the entrepreneur is the only employee in the business. But regardless of the business model, all entrepreneurs must be able to achieve balance in their lives between their dedication to growing their entrepreneurial venture and their personal life. Developing a vision that includes different areas of your professional and personal life can help make this type of balance achievable.

How do you define balance in your life? What areas do you consider when you think about a balanced life? Having enough money to support your lifestyle might be one goal. Other areas might include physical activities or hobbies, social interactions and entertainment, satisfaction with how you earn money, your family and personal relationships, and other interests and values. Some entrepreneurs start lifestyle ventures to achieve this balance. But how do we achieve balance when our goal is to be a career entrepreneur?

A **career entrepreneur** is someone who takes on the daily management as the owner of the venture, accepting, and perhaps enjoying, the daily risks and rewards of managing and building the venture such as Roxanne Quimby. For Roxanne Quimby, growing Burt's Bees involved making difficult decisions, such as relocating from Maine to California to meet the growth needs of the company. Even though Roxanne wanted to provide employment opportunities to people in northern Maine, she knew that her business needed the right infrastructure for success, and that infrastructure wasn't available in Maine. If you choose to become a career entrepreneur, your focus may be primarily on advancing your entrepreneurial idea into a successful

venture, like Roxanne did with Burt's Bees; this can come at the expense of personal life goals.

Many career entrepreneurs need support from family and friends who accept that the lead entrepreneur's attention and energy are required for the success of the venture, and many lifestyle entrepreneurs will find challenges in meeting the needs of the venture while maintaining work-life balance. Discussions with family, close connections, and the entrepreneurial team should occur in the early idea-formulation stage to gauge the support of the people whose interests might be compromised by the entrepreneur's dedication to advancing the venture.

Clearly defining your idea of success for your life, and for your venture, is an important step in achieving balance. What are your priorities? What can you do to balance the success of your new venture, the success of your own life, and the success of your family? Considering that balancing all the roles that we have in life is a frustration point for many people, can you find an opportunity to create an entrepreneurial venture?

WORK IT OUT

Exploring What Success Means to You

What is your own definition of success? It's helpful for your entrepreneurial ventures for you to explore and define what success means for you personally and professionally.

- This short Ted Talk explores what makes a person successful: https://www.ted.com/talks/richard_st_john_s_8_secrets_of_success?referrer=playlist-short_talks_to_watch_during_yo. Knowing how you personally define success is a worthwhile activity to help achieve balance.
- Consider these eight secrets to success as you think about work-life balance: https://www.ted.com/talks/nigel_marsh_how_to_make_work_life_balance_work
- Here is another Ted Talk that offers perspective on our lives and what we consider as success: https://www.ted.com/talks/alain_de_botton_a_kinder_gentler_philosophy_of_success

After reviewing these resources, think about how you would define success, and how you can use that knowledge to plan for a satisfying work-life balance.

As you explore what success means for your venture and how your definition aligns with balance between your personal life and dedication to your venture, you should consider some of the unique challenges entrepreneurs can face. For example, there might be a learning curve in unfamiliar areas of business, such as accounting or finance. Or you might face a dilemma about whether to expand a product line, or whether or where to open a new location. Entrepreneurs often mention the physical requirements of starting up a business. Physical demands can include the sheer stamina needed to clean a new space, move in, and set up shop. Depending on your business, you also might need to adjust to being on call twenty-four/seven. Here again, developing a vision of where you want to be in the future can help you plan for the challenges you will face in the early stages of your business.

Entrepreneurship can be especially draining if you are not prepared for the tasks at hand—as can be the case with any professional or personal role. Therefore, self-care and emotional awareness can play a key role in maintaining your emotional health as an entrepreneur. Taking time for yourself is very important. This could involve creating a time management calendar. Tracking how you spend your time can keep you on schedule with tasks and prevent you from expending too much on any one area of the business or your personal life in detriment to the other. Taking time away from the business is emotionally healthy and can provide important perspective that can help you make better decisions. "Leaving work at the office" is a successful strategy that many business people use to separate their personal and professional lives. If this is not possible—for example, if you work from home—setting aside family or personal time can allow for work-life balance.

Having trusted advisors and mentors for your business and personal life can also promote emotional health.

When you face a decision or challenge that you have difficulty with, it is important to have someone to talk to who knows you and knows your situation. Some entrepreneurs may find themselves in their first experience of leading others, with total responsibility for the outcomes as owner of the business. Every business person should have a personal leadership improvement plan. This plan can take the form of academic classes or professional coaching, but sometimes, it will be a personal commitment to improvement. You should identify your preferred leadership styles, as well as leadership strengths and weaknesses. It might be useful to look back on your own work experiences to identify which leadership traits you admired and which ones you didn't. As with any other business skill set, you can learn and improve these strengths in yourself. You also can hire people with complementary skills to handle the areas that you feel unsure about.

Being aware of your own strengths and weaknesses, as well as of your preferences and dislikes, will help you achieve and maintain balance in your life. Having counselors, mentors, advisors, checklists, and timelines can keep you on track and prevent any one area of your business or personal life from taking over or being neglected.

The Importance of Goals

Entrepreneurial vision imagines a future, whereas goals focus on a desired outcome. Although vision is key to creating the future that you want for yourself and your business, goals are important to help you realize the steps needed to make that vision a reality.

Read through your definitions of success and your vision statement. Now create a list of possible actions that will help you achieve success and accomplish your vision. Review your list and categorize the words and actions in terms of relevance and time frames.

SMART goals are well-structured and defined goals that are specific, measurable, achievable, relevant, and timely (Figure 1.9).

- Specific: Your goals should be precise rather than overly broad.
- Measurable: You should be able to test in some **quantifiable manner** whether a goal has been met, meaning that there needs to be some method to determine if the goal has been met or not.
- Achievable: The goal must be attainable; it cannot be so lofty that it cannot be accomplished. On the other hand, the goal should not be so easy that it can be accomplished quickly or with little effort.
- Relevant: The goal should be well suited for what you want to accomplish; this means that the goal should be relevant to the outcome needed.
- Timely: Each goal needs to have a defined deadline, the time when the goal must be accomplished. What time frame do you have for completing your goals? How does this timeline fit into your overall plan?

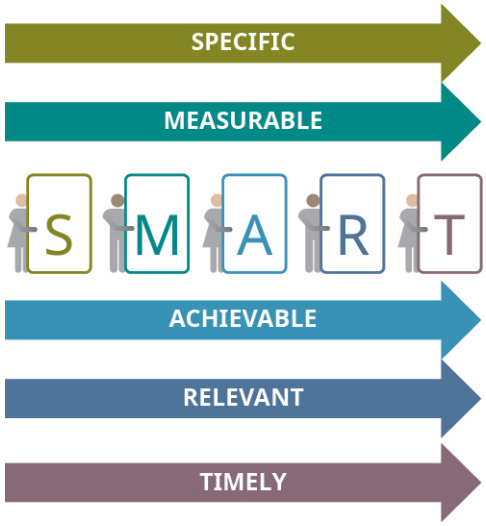

Figure 1.9 Creating SMART goals can help you realize your vision. (attribution: Copyright Rice University, OpenStax, under CC BY NC-

SA 4.0 license)

For example, if your personal definition of success and your vision for your future include financial independence—with, say, a vacation home in the mountains—what goals can you define today that will lead to this outcome? You would include financial goals tracked either monthly or yearly to save a set amount of money based on your projection of how much money it will take to own these two vacation homes. You would also set goals about finding the right locations. This process is also necessary to support the success of your business venture. Setting goals is a powerful approach that leads us to the future we want for our lives.

ENTREPRENEUR IN ACTION

Roomify's Goals

Research Roomify at https://www.inc.com/profile/roomify and www.roomify.com. If you were one of the cofounders of this company, what goals would you create for this business? Should you harvest the company? Expand into other related products? Repackaging products for ease of purchasing is an excellent idea that can be translated into other areas. Can you think of a new idea based on repackaging products that is focused on the benefits of saving people time and the hassle of decision-making? Create a list of at least ten ideas based on the idea of saving people time and adding convenience to their lives. Which ideas most appeal to you?

Here is a fictional example of an entrepreneur's goals, which we can test against the SMART criteria to see if they are feasible. Soraya runs a small tutoring business in Dallas, Texas. Her target market is high school students. Soraya is currently the only employee in her sole proprietorship, but she hopes to hire more employees soon. She is excited about her business, and so far, she has done well in the four years that she has been operating it. On the advice of a friend in business school, Soraya has defined three business goals for the next year. They are:

1. Increase sales by 50 percent.
2. Open a new location.
3. Hire two employees.

In reviewing these goals using the SMART criteria, it is evident that goals one and three are *specific* because they are quantitative, but goal two is not. All three goals can be *measured*. With Soraya as the only employee, it is unlikely that she can achieve goals one and two, but goal three is *achievable*. And hiring more staff would increase the likelihood of achieving additional goals. All three goals are *relevant* to growing the business. And each goal could use more detail in terms of being *timely*. That is, in order to increase sales by 50 percent in the upcoming year, Soraya should have additional monthly or quarterly sales goals to meet her annual goal. Likewise, the opening of a new location requires more time-bound details, such as leasing or purchasing the location, and determining the business model for this location. Finally, hiring additional employees should have a time component as well, such as a timeline for recruiting, interviewing, selection, hiring, and training. Therefore, Soraya's goals are appropriate for her small tutoring business, but they need refining so that they meet the SMART criteria. Soraya is more likely to achieve SMART goals, and they are more likely to lead to desired business outcomes.

1.3 The Entrepreneurial Mindset

Learning Objectives

By the end of this section, you will be able to:

- Explain what it means to have an entrepreneurial mindset
- Describe what is meant by entrepreneurial spirit or passion

Entrepreneurship takes many forms (see Table 1.1), but entrepreneurs share a major trait in common: An entrepreneur is someone who identifies an opportunity and chooses to act on that opportunity. Most business ventures are innovative variations of an existing idea that has spread across communities, regions, and countries, such as starting a restaurant or opening a retail store. These business ventures are, in some ways, a lower-risk approach but nonetheless are entrepreneurial in some way. For example, Warby Parker, a profitable startup founded by four graduate students at Wharton, disrupted a major incumbent (Luxottica) by providing a more convenient (online initially), affordable, and stylish product line for a large segment of consumers. In this sense, their innovation is about creating something new, unique, or different from the mainstream. Yet they attracted an existing, and in some ways mature, sector of an established industry. In a different way, McDonalds, which is 90 percent owned by franchisees, introduced an "all day breakfast" menu in 2017 that was hugely successful; it also targeted a larger segment (in part younger consumers) and brought back consumers who had chosen other options. In summary, many entrepreneurs start a new venture by solving a problem that is significant, offering some value that other people would appreciate if the product or service were available to them. Other entrepreneurs, in contrast, start a venture by offering a "better mousetrap" in terms of a product, service, or both. In any case, it is vital that the entrepreneur understand the market and target segment well, articulate a key unmet need ("pain point"), and develop and deliver a solution that is both viable and feasible. In that aspect, many entrepreneurs mitigate risks before they launch the venture.

Being aware of your surroundings and the encounters in your life can reveal multiple opportunities for entrepreneurship. In our daily lives, we constantly find areas where improvements could be made. For example, you might ask, "What if we didn't have to commute to work?" "What if we didn't have to own a vehicle but still had access to one?" "What if we could relax while driving to work instead of being stressed out by traffic?" These types of questions inspired entrepreneurial ventures such as ride-sharing services like Uber, the self-driving vehicle industry,[21] and short-term bicycle access in the free bike-sharing program in Pella, Iowa (Figure 1.10).[22]

Figure 1.10 A bike-sharing program in Pella, Iowa, allows users to access bikes at a variety of locations. (credit: "Corral of VeoRide Dockless Bike Share" by "paul.wasneski"/Flickr, Public Domain)

These ideas resulted from having an **entrepreneurial mindset**, an awareness and focus on identifying an opportunity through solving a problem, and a willingness to move forward to advance that idea. The entrepreneurial mindset is the lens through which the entrepreneur views the world, where everything is considered in light of the entrepreneurial business. The business is always a consideration when the entrepreneur makes a decision. In most cases, the action that the entrepreneur takes is for the benefit of the business, but sometimes, it helps the entrepreneur get ready to adopt the appropriate mindset. The mindset

21 Matthew DeBord. "Waymo Could Be Worth as Much as $75 Billion—Here's a Brief History of the Google Car Project." *Business Insider*. September 9, 2018. https://www.businessinsider.com/google-car-project-history-2018-8
22 Ethan Goetz. "Bike Share Program Launched Monday." *The Chronicle*. July 2, 2018. https://www.pellachronicle.com/gallery/bike-share-program-launched-monday/article_950cebac-7e49-11e8-97a0-8fd615410188.html

becomes a way of life for the entrepreneur. Entrepreneurs often are predisposed to action to achieve their goals and objectives. They are forward thinking, always planning ahead, and they are engaged in “what if” analyses. They frequently ask themselves, “What if we did this?” “What if a competitor did that?”—and consider what the business implications would be.

Most people follow habits and traditions without being aware of their surroundings or noticing the opportunities to become entrepreneurs. Because anyone can change their perspective from following established patterns to noticing the opportunities around them, anyone can become an entrepreneur. There is no restriction on age, gender, race, country of origin, or personal income. To become an entrepreneur, you need to recognize that an opportunity exists and be willing to act on it. Note, however, that the execution of the entrepreneurial mindset varies in different parts of the world. For example, in many Asian cultures, group decision-making is more common and valued as a character trait. In these regions, an entrepreneur would likely ask the advice of family members or other business associates before taking action. In contrast, individualism is highly valued in the United States and so many US entrepreneurs will decide to implement a plan for the business without consulting others.

Entrepreneurial Spirit and Passion

An entrepreneurial spirit allows entrepreneurs to carry a manner of thinking with them each day that allows them to overcome obstacles and to meet challenges with a can-do attitude. What does it mean to have an entrepreneurial spirit? For the purposes of this discussion, it could mean being passionate, purposeful, positive, bold, curious, or persistent.

The founders of Airbnb have a passion for supporting individual rights to rent out unused space. Why should the established model of hotels prevail? Why shouldn’t an individual homeowner have the freedom to rent out unused space and leverage that space into an income? Airbnb has succeeded in creating more flexible and affordable options in the space of the rapidly growing "sharing" economy. At the same time, some states and municipalities have raised issues about the regulations monitoring ventures like this. While entrepreneurial spirit is partly about fighting for individual rights and freedoms, there should be a balance between economic freedom and consumer protection. The entrepreneurial spirit involves a passion for presenting an idea that is worthwhile and valuable, and a willingness to think beyond established patterns and processes, while still keeping in mind local laws and regulations, in the quest to change those established patterns, or at least to offer alternatives to those established patterns.

Passion is a critical component of the entrepreneurial process. Without it, an entrepreneur can lose the drive to run the business. Passion can keep an entrepreneur going when the outside world sends negative messages or less-than-positive feedback. For example, if you are truly passionate about starting an animal shelter because of your love of animals, you will find a way to make it happen. Your internal drive to help animals in need will spur you on to do whatever it takes to make the shelter become a reality. The same is true of other types of startups and owners with similar passions. However, passion needs to be informed by the entrepreneur’s vision and mission—passion of the sake of passion is not enough. A clear mission statement—which details why the business exists and the entrepreneur’s objectives for achieving that mission—will guide an entrepreneur’s passion and keep the business on track. Passion, vision, and mission can reinforce each other and keep the entrepreneur on the right track with next steps for the business.

Some ideas might seem small or insignificant, but in the field of entrepreneurship, it’s important to recognize that for every new startup, someone else may recognize a spin-off idea that expands upon the original idea. The opportunities for identifying new possibilities are endless. Review your work in creating spinoff ideas for Angad Darvani’s projects, or Kevin F. Adler’s Miracle Messages venture. Or consider possible spin-off ideas around the technology used in agriculture. Creating spin-off ideas fits well with our discussion of divergent thinking and brainstorming. Through these processes, we can discover new uses for existing technology, just as Ring did by using video technology to add security by allowing customers to see who is at the door without opening it.

An Entrepreneurial Mindset in Your Discipline or Field

Within your industry of interest or area of study, what are the challenges that create frustration? How can these be turned into opportunities? Earlier in this chapter, we discussed Evernote, a company that focuses on expanding our memories by storing and organizing information. Let's look at some other examples of entrepreneurial endeavors in specific industries to help you plan your own venture in your own industry.

In the agriculture industry, insects, weeds, weather conditions, and the challenges of harvesting crops are all ripe for entrepreneurial activities. The move toward organic produce has also affected this industry. From an entrepreneurial perspective, what products could you invent to support both organic farming and the problems of insects that damage or destroy crops? The old method was to use chemical sprays to kill the insects, but today, the growing demand for organic foods and increased awareness of the impact of chemical sprays on our environment are changing this scenario. One new idea to solve this problem combines a vacuum cleaner with an agriculture product.

LINK TO LEARNING

Watch this video on the creation of a crop vacuum that sucks up insects and bugs (https://openstax.org/l/52BugVacuum) to learn more.

A bug vacuum is an example of how using divergent thinking contributed to the solution of removing bugs from crops without using chemicals. In the group activity of creating divergent ideas, this idea may not have been received well. However, in the incubation stage, the idea must have come forward as a viable solution. Entrepreneurs frequently face the challenge of pressure to conform to established habits and patterns within industries.

Often, the entrepreneurial mindset includes futuristic ideas that shake up the normal, conventional processes that are grounded in experience over time. Tried-and-tested processes and products that have a proven history of success can be a formidable obstacle to new ideas. A new idea may even appear as impossible or outlandish, perhaps even an embarrassment to the steady and predictable practices established within an industry. This can create a dilemma: Do we try something new and unproven that lacks documented research? Sometimes, we must disregard our past successes and research to be open to new possibilities for success and failure. An entrepreneurial mindset includes creativity, problem-solving skills, and a propensity to innovation.[23] Open-mindedness is one characteristic that supports creativity, problem solving, and innovation. Taking the time to explore new ideas, dream, reflect, and view situations from a new perspective contribute to the entrepreneurial mindset. Some innovations can lead to disruptions within the industry, or even create a new industry.

The innovator's dilemma was presented by Clayton Christensen to explain **disruptive technology**, which are technologies that, once introduced, displace established patterns, processes, and systems previously accepted as normal or accepted. One example of a disruptive technology is Airbnb, a company that threatens the established hotel industry by connecting personal resources to people who desire those resources. If you have a spare bedroom that you aren't using, why not sell that space to someone who wants and needs the space?

23 Emma Fleck. "Needed: Entrepreneurial Mindset." *Central Penn Business Journal*, *34*(12), 10. http://pageturnpro2.com.s3-website-us-east-1.amazonaws.com/Publications/201803/15/83956/PDF/131668002208352000_CPBJ033018WEB.pdf

Airbnb has become a significant threat to the established hotel industry's business model of building large hotels and renting rooms within those hotels to their customers. Airbnb has reconfigured that model, and since its 2008 launch, 150 million travelers have taken advantage of 3 million Airbnb listings in more than 191 countries. Airbnb has raised more than $3 billion (plus a $1 billion credit line) and is considering selling stocks to support significant expansion. The value of Airbnb is approximately $30 billion. Compare this market value to Hilton's market capitalization of $19 billion and Marriott's of $35 billion. If you were the CEO of Hilton or Marriott, would you be worried? The hotel industry recognized Airbnb as a threat, and in 2016, began a campaign to create legislation to rein in Airbnb's growth and popularity. From the hotel industry's perspective, Airbnb is not playing by the same rules. This is the definition of disruptive technology, the focus on creating a new idea or process that negates or challenges established process or products.[24]

Sometimes disruptive technologies result from *not* listening to customers. Customers don't always know what they want. Customer groups might need to be redefined by the entrepreneurial team on the basis of better models, knowing when to invest in developing lower-performance products that promise lower margins while still satisfying the need, and knowing when to pursue small markets at the expense of larger or established markets. Basically, disruptive technologies occur through identifying new and valuable processes and products.

The founders of Airbnb recognized that some people have unused resources, bedrooms, that other people need. We can apply this idea to other unused resources such as vehicles and motor homes. We see this model reproduced in short-term car rental and bike-sharing programs.

24 Katie Benner. "Inside the Hotel Industry's Plan to Combat Airbnb." *New York Times*. April 16, 2017. https://www.nytimes.com/2017/04/16/technology/inside-the-hotel-industrys-plan-to-combat-airbnb.html

Key Terms

career entrepreneur someone who takes on the daily management as the owner of the venture, accepting, and perhaps enjoying, the daily risks and rewards of managing and building the venture
disruptive technology technology that once introduced, displaces established patterns, processes, and systems previously accepted as normal or accepted methods
divergent thinking process of generating as many ideas as possible, even when those ideas do not seem logical; the list of ideas can be conflicting, diverse, and disparate
due diligence conducting the necessary research and investigation to make informed decisions that minimize risk
entrepreneur someone who identifies an idea that no one else has acted on or identified; small business ownership and franchising are also entrepreneurial options
entrepreneurial mindset awareness and focus on identifying an opportunity through solving a problem, and a willingness to move forward to advance that idea
entrepreneurial venture any business, organization, project, or operation of interest that includes a level of risk in acting on an opportunity that has not previously been established
entrepreneurial vision idea of what an entrepreneur wants a venture to become, what it will look like, what the driving forces are, and what values and culture should surround it
harvest point at which the venture is sold, at which time the investors receive a return on their investment
lifestyle venture business whose founders' primary focus is the lifestyle they will attain through becoming entrepreneurs, rather than a primary interest in financial rewards
mission statement statement of an organization's reason for being that defines its primary long-term goal, explains what the venture will do, what value it will provide to the end customer, and how it will accomplish that action
opportunity-identifying perspective method for identifying a problem and determining how it could be translated into an opportunity to create a new venture
quantifiable manner method to determine if a goal has been met or not
serial entrepreneur entrepreneur who becomes involved in starting multiple entrepreneurial ventures
SMART goals well-structured and defined goals that are specific, measurable, achievable, relevant, and timely
social entrepreneur entrepreneur who has an interest in solving a social, environmental, or economic problem
value proposition summary describing the benefits (value) customers can expect from a particular product or service
vision statement picture of what the venture will become in the future or what the venture will grow into

Summary

1.1 Entrepreneurship Today

An entrepreneur is someone who takes on an entrepreneurial venture to create something new that solves a problem; small business ownership and franchising are also entrepreneurial options. The venture could be for profit or not for profit, depending on the problem it intends to solve. Entrepreneurs can remain in a full-time job while pursuing their ideas on the side, in order to mitigate risk. On the opposite end of the spectrum, entrepreneurs can take on lifestyle ventures and become serial entrepreneurs. There are many factors driving the growth of entrepreneurship, including employment instability, motivation to create something new, financial factors and free time associated with retirement, and the greater acceptance of entrepreneurship as a career choice. The cultures of nations around the world affect the ability for entrepreneurs to start a venture, making the United States a leader in entrepreneurial innovation. Entrepreneurs often find inspiration in social, environmental, and economic issues.

1.2 Entrepreneurial Vision and Goals

Establishing an entrepreneurial vision helps you describe what you want your venture to become in the future. For most entrepreneurial ventures, the vision also includes the harvesting or selling of the venture. There are creative ways, such as brainstorming and divergent thinking, as well as investigative ways to define an entrepreneurial vision. Once you have established your vision, it is important to write goals to help you realize the steps toward making your vision a reality.

1.3 The Entrepreneurial Mindset

Identifying new possibilities, solving problems, and improving the quality of life on our planet are all important aspects of entrepreneurship. The entrepreneurial mindset allows an entrepreneur to view the world as full of possibilities. Entrepreneurial passion and spirit help entrepreneurs overcome obstacles to achieve their goals. Disruptive technologies involve using existing technology in new ways and can provide new opportunities as well as new challenges. Entrepreneurship is transforming some industries and potentially creating others, though many entrepreneurs create value by starting small businesses, buying franchises, or introducing new services in mature industries. The key thing to remember is that anyone can be an entrepreneur and that new technologies are making the cost of starting a new business less costly, but still risky at some level.

Review Questions

1. What factors contribute to a growing interest in entrepreneurship?
   A. unemployment levels
   B. low job turnover rates
   C. increasing levels of creativity
   D. decreasing rates of discrimination

2. Angel investors contribute to the entrepreneurial world by _____.
   A. outpacing venture capitalists in access to startup funds
   B. directly investing in entrepreneurial startups
   C. holding seminars to teach people how to become an entrepreneur
   D. forming groups of other investors to supply greater quantities of investment funds to entrepreneurs.

3. An entrepreneur is someone who _____.
   A. creates a small business based on other existing businesses
   B. creates a home-based business that sells products available through other retailers
   C. creates a business around the idea of solving a problem
   D. is highly creative

4. Roxanne Quimby of Burt's Bees is an example of an entrepreneur primarily for which of the following reasons?
   A. She saw available resources and recognized the resources could be used to create a business.
   B. She acted on her passions.
   C. She solved a significant societal problem.
   D. She had the time and energy to dedicate to starting business.

5. In the early stages of developing an entrepreneurial venture, the entrepreneur might seek funding from which group?
   A. venture capitalists
   B. the local bank
   C. friends and family
   D. shark tank

6. The acronym SMART for goal setting stands for _____.
   A. short-term, measurable, accurate, relevant, and timely
   B. specific, measurable, achievable, relevant, and timely
   C. specific, measurable, achievable, realistic, and time oriented
   D. specific, measurable, achievable, results, and time oriented

7. A vision statement does not include _____.
   A. a picture of the future described in words
   B. concepts and ideas that inspire and focus people's actions toward a united outcome
   C. both creative and exploratory process in creating the vision
   D. the scope of the venture

8. Which one of the following is not a quantifiable result?
   A. 5 percent annual growth in sales
   B. increase market share by 2 percent
   C. decrease collection of accounts receivable by $5,000.00
   D. increase creativity throughout the venture

9. Which of the following is not a creativity building technique or tool?
   A. conducting a case study
   B. brainstorming activities
   C. mind map creation
   D. brain writing

10. Disruptive technologies include all but which of the following?
    A. new methods or approaches that make established methods obsolete
    B. self-booking of air travel
    C. restaurant food delivery services
    D. a change from ownership of resources to the ability to have access to resources

11. The entrepreneurial mindset includes _____.
    A. a willingness to develop ideas that are not always initially popular
    B. a willingness to wait for an idea to become popular before moving forward with that idea
    C. an ability to focus on past successes
    D. a belief in following tradition and established patterns

Discussion Questions

1. Why is the United States a leader in entrepreneurship?
2. What commonalities do the top five countries have that put them in the lead for entrepreneurial ventures?
3. One of Roxanne Quimby's motivations in starting businesses included helping employ people in her community. How does or doesn't this motivation fit in the definition of an entrepreneur as someone who identifies a problem and solves that problem?
4. What are the similarities and differences between the business ventures of Wander Girls and Roxanne Quimby?
5. Why is knowing your vision for the future important?
6. Why should we create goals using the SMART method?

7. What is the value in using divergent thinking when trying to solve a problem?
8. How would you explain the concept of an entrepreneurial vision to your college roommate who is a history major?
9. What is the primary difference between divergent thinking and brainstorming?
10. Identify five disruptive technologies and the industries that these technologies impact.
11. In thinking about the future, and your own experiences, what opportunities are there for disruptive technologies in one or two familiar industries?
12. What is the difference between an entrepreneurial mindset and entrepreneurial spirit?
13. Describe your own level of entrepreneurial spirit.

Case Questions

1. What suggestions could you make to Angad Daryani on other products that would fit his focus on improving the lives of people?
2. On Angad Daryani's website, he says he believes "that the path humanity follows, need to be pivoted for the better." What other needs or problems do humans have? Create a list of twenty needs that would fit Angad Daryani's belief statement.
3. Research Miracle Messages. Identify Miracle Messages vision statement, mission statement, and value statements. Do not copy their statements, but rather create your own statements based on what you would create if you were the lead entrepreneur for this organization.
4. Identify five other organizations that have services or products that you would want to partner with if you were the lead entrepreneur of Miracle Messages. What value does each of these five organizations provide to Miracle Messages' vision, mission, and value? What services or products are not supported either through Miracle Messages or the five organizations you addressed? What new for-profit or nonprofit could be created as a spinoff idea from your research on Miracle Messages?
5. Review the website http://www.coastaltractor.com/ to learn more of about Coastal Tractor. What spinoff ideas could you identify using this same technology or concept as the bug vacuum?
6. In reviewing Coastal Tractor's website, what evidence of an entrepreneurial mindset is present within this company's website?
7. Do you think Coastal Tractor is using a disruptive technology? Why or why not?

Suggested Resources

1.1 Entrepreneurship Today

https://www.entrepreneurship-campus.org

https://youtu.be/zV2vi8FilLM

1.2 Entrepreneurial Vision and Goals

The following links might provide you with more ideas about creating a vision statement.

https://website-designs.com/business/the-importance-of-a-vision-statement-for-entrepreneurs/

https://www.businessnewsdaily.com/3882-vision-statement.html

Check out this website's ideas for developing your vision: https://www.executestrategy.net/blog/write-good-vision-statement

Eleven Free Goal Setting Software & Tools You Can Use: http://www.goal-setting-college.com/goal-setting-software/11-goal-setting-software-tools-you-can-use-for-free/

YouTube: Achieve More by Setting Smart Goals: https://www.youtube.com/watch?v=yA53yhiOe04

Twenty-four Essential Mind Mapping and Brainstorming Tools: http://mashable.com/2013/09/25/mind-mapping-tools/#jP47h7Q818qM

Read more about the challenges of work-life balance and what brings satisfaction to entrepreneurs in this article: https://www.wsj.com/articles/why-some-entrepreneurs-feel-fulfilledbut-others-dont-1432610236

Learn about applying a SWOT analysis (strengths, weaknesses, obstacles, threats) to your personal life: https://www.forbes.com/sites/lisaquast/2013/04/15/how-to-conduct-a-personal-s-w-o-t-analysis/

1.3 The Entrepreneurial Mindset

M. M. Baluku, J. F. Kikooma, and K. Otto, "Positive mindset and entrepreneurial outcomes: The magical contributions of psychological resources and autonomy." *Journal of Small Business & Entrepreneurship* 30, no. 6 (2018): 473–498.

E. Fleck, "Needed: Entrepreneurial mindset." *Central Penn Business Journal* 34, no. 12 (2018): 10.

M. Israr and M. Saleem, "Entrepreneurial intentions among university students in Italy." *Journal of Global Entrepreneurship Research* 8, no. 1 (2018): 1.

https://www.christenseninstitute.org/results/?_sft_topics=disruptive-innovation

2

The Entrepreneurial Journey and Pathways

Figure 2.1 College graduates face numerous choices and challenges when deciding which pathway will lead to career satisfaction and success. (credit: modification of "commencement graduation ceremony" by "Goodfreephotos_com"/Pixabay, CC0)

Chapter Outline

2.1 Overview of the Entrepreneurial Journey
2.2 The Process of Becoming an Entrepreneur
2.3 Entrepreneurial Pathways
2.4 Frameworks to Inform Your Entrepreneurial Path

Introduction

What do you plan to do with your life after graduating from school? This is one of the most common—and admittedly most terrifying—questions that students are asked on a regular basis. There are literally thousands of career choices and just as many pathways or options to reach them. How do you decide which career pathway is best for you? You might select a new career based on your major, a favorite high school subject, the advice of a family member or friend, or an inspirational summer or internship experience.

What if none of those options reflect the future that you see for yourself? It may mean that you are destined to create your own career path by becoming an entrepreneur. Regardless of the career pathway that you follow, your entrepreneurial journey begins with a single step.

2.1 Overview of the Entrepreneurial Journey

Learning Objectives

By the end of this section, you will be able to:

- Explain the entrepreneurial journey to explore and discover entrepreneurship as a career choice
- Identify the steps, decisions, and actions involved in the entrepreneurial journey
- Recognize the rewards and risks of the steps in the entrepreneurial journey

Self-Employment as an Entrepreneurial Journey

When the economy and the job market are strong, the entrepreneur has a safety net that decreases the risks in creating a new **venture**, a startup company or organization that conducts business or is created to satisfy a need, and allows for a quick recovery if the venture is not successful. There are more new startups when there are high levels of confidence in both the venture's success and the entrepreneur's confidence in finding employment if the venture fails. People over 40 years of age account for most new startup activity, in part because of the continuing trend in which a business may choose not to hire an employee but instead hire an **independent contractor**, a person who provides work similar to an employee without being part of the payroll for the contracting business, and who is responsible for paying their own taxes and providing their own benefits. With previous knowledge and expertise, this group of entrepreneurs recognizes opportunities created by this move away from hiring full-time employees to more outsourcing to independent contractors. One contributor is the gig economy, which involves using temporary and often transitional positions hired on a case-by-case basis, rather than keeping a full staff of hired employees. Advantages for the employer include a decrease in cost of benefits and loyalties to specific employees. Advantages for the hired worker or independent contractor (sometimes called a freelancer) include no long-term commitment and flexibility in accepting contracts. From an entrepreneurial perspective, the creation of websites that support the gig economy offers opportunities for independent ventures. Many people today are becoming small entrepreneurs. This process goes by a variety of names, such as the sharing economy, the gig economy, the peer economy, or the collaborative economy. Maybe it means driving for a company such as Lyft, Uber, or GrubHub, or perhaps offering services through TaskRabbit, UpWork, or LivePerson. The projected numbers of independent contractors and on-demand workers are stated as 42 percent for small businesses by the year 2020, a growth of 8 percent from current figures.[1] And a projection of greater than 50 percent of the workforce will be independent contractors by 2027 if this trend continues at the current pace.[2] In the "Freelancing in America: 2019" report, the sixth annual study by UpWork and Freelancers Union, 57 million United States citizens are estimated to freelance, with income approaching 5 percent of US gross domestic product (GDP) at nearly $1 trillion and earning a median rate of $28.00 an hour, representing an hourly income greater than 70 percent of workers in the overall US economy.[3] One report found that 94 percent of net job growth from 2005 to 2015 was in alternative work categories, with 60 percent due to independent contractors and contract company workers.[4]

According to the US Bureau of Labor Statistics, the number of self-employed Americans is growing, with 9.6 million self-employed people at the end of 2016. That number is expected to grow to 10.3 million by 2026.[5] A more recent study by FreshBooks' second annual "Self-Employment" report predicts that 27 million US employees will leave traditional work in favor of self-employment by 2020, tripling the current population of full-time self-employed professionals to 42 million. The main driver for this change in the workforce is a greater desire for control over one's career with the ability to have greater control over working hours and acceptance of work.[6,7] Of course, self-employment is a broad category that includes small-business owners as well as entrepreneurial startups and freelance gig employees. Since 2016, there has been a downward slide in the number of employees working for self-employed businesses, which results from a variety of factors, including difficulties in finding qualified employees, qualified employees having more employment options, such as employment through the gig economy, outsourcing activities, and technology actions that decrease the need for employees, with entrepreneurial activity remaining steady.[8]

1 David Pridham. "Entrepreneurs: Here's Good News for 2018." *Forbes*. 2018. https://www.forbes.com/sites/davidpridham/2018/01/10/entrepreneurs-heres-good-news-for-2018/#660f5ebd6659
2 UpWork and Freelancers Union. "Freelancers Predicted to Become the U.S. Workforce Majority within a Decade, with Nearly 50% of Millennial Workers Already Freelancing, annual 'Freelancing in America' Study Finds." *UpWork*. October 17, 2017. https://www.upwork.com/press/2017/10/17/freelancing-in-america-2017/
3 UpWork. "Sixth Annual 'Freelancing in America' Study Finds That More People Than Ever See Freelancing as a Long-Term Career Path." *UpWork*. October 3, 2019. https://www.upwork.com/press/2019/10/03/freelancing-in-america-2019/
4 David Pridham. "Entrepreneurs: Here's Good News for 2018." *Forbes*. 2018. https://www.forbes.com/sites/davidpridham/2018/01/10/entrepreneurs-heres-good-news-for-2018/#660f5ebd6659; Lawrence F. Katz and Alan B. Krueger. "The Rise and Nature of Alternative Work Arrangements in the United States, 1995–2015." 2016. https://scholar.harvard.edu/files/katz_krueger_cws_final_nov2018.pdf.

Entrepreneurship around the World

In a 2017 *Business Insider* article, "America Needs Immigrant Entrepreneurs," David Jolley writes that immigrants constitute 15 percent of the US workforce and 25 percent of the country's workforce of entrepreneurs.[9] Forty percent of startups include at least one immigrant. Jolley's article cites a study that identified immigrants as twice as likely to start a business as people born in the United States. In 2016, 40.2 percent of Fortune 500 companies were founded by at least one immigrant or a child of immigrant parents. Dinah Brin, writing for *Forbes*, stated in a 2018 article that immigrants form 25 percent of new US businesses and that new immigrant-owned firms generated 4 to 5 million jobs.[10]

These statistics and other findings have prompted countries such as Canada to revise their immigration policies to attract more entrepreneurial-minded immigrants. A World Bank report from May 2018 ranked the United States 53rd out of 190 countries for ease in starting a business, with higher scores representing greater ease.[11] The same report ranks the United States eighth for ease of doing business. The difference in these rankings indicates that once a business is established, factors such as regulations, permits, access to credit, and infrastructure support the business owner's ability to continue the business, but actually starting the business is more challenging. For any given country, ease in starting a business and the country's interest in supporting entrepreneurial activity are crucial in both attracting entrepreneurial people and supporting their ability to open a business. Imposing restrictive regulations and processes on new ventures significantly decreases the number of new ventures.

According to a 2018/2019 report, the highest rate of entrepreneurial activity worldwide in 2018 was in Angola at 41 percent.[12] Angola's low-income economy meant fewer employment opportunities, creating pressures to find other ways to earn an income. Guatemala and Chile reported 28 percent and 25 percent of entrepreneurial activity, respectively, with medium- and high-income economies. These percentages are quite high, considering that these economies offer employment opportunities in existing companies. In terms of innovation, India at 47 percent, and Luxembourg and Chile at 48 percent each, take the lead in offering new products and services not previously available. This entrepreneurial activity reflects the ease of starting a business. The Netherlands, Poland, and Sweden were reported as the easiest countries in which to start a new business, in part because many people in those countries view entrepreneurship as an attractive lifestyle. As you can see, both economic opportunities and a country's specific support for entrepreneurial behavior contribute to the number of people who enter entrepreneurial activities.

From a gender perspective, there are currently over 11 million woman-owned businesses in the United States. This number includes both small business owners and entrepreneurs. Thirty years ago, there were only 4 million woman-owned businesses.[13] The number of woman-owned businesses has increased 45 percent between 2007 and 2016, five times faster than the national average, with 78 percent of new women-owned businesses started by women of color.

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5 Elka Torpey and Brian Roberts. "Small-Business Options: Occupational Outlook for Self-Employed Workers." *US Bureau of Labor Statistics*. May 2018. https://www.bls.gov/careeroutlook/2018/article/self-employment.htm

6 Carly Moulton and Dave Cosgrave. "Second Annual Self-Employment Report." *FreshBooks*. 2017. https://www.freshbooks.com/wp-content/uploads/2018/04/2018selfemploymentreport.pdf

7 OECD Data. "Self-employment Rate." *OECD.org*. n.d. https://data.oecd.org/emp/self-employment-rate.htm.

8 Arnobio Molrelix. "The Biggest Reason the U.S. Needs Small Businesses to Thrive Has Nothing to Do with Taxes or the Economy." *Inc.*, Dec. 20, 2018. https://www.inc.com/arnobio-morelix/inc-entrepreneurship-index-2018-q3.html

9 David Jolley. "America Needs Immigrant Entrepreneurs." *Business Insider*. September 5, 2017. https://www.businessinsider.com/america-needs-immigrant-entrepreneurs-2017-9

10 Dinah Wisenberg Brin. "Immigrants Form 25% of New U.S. Businesses, Driving Entrepreneurship in 'Gateway' States." *Forbes*. July 31, 2018. https://www.forbes.com/sites/dinahwisenberg/2018/07/31/immigrant-entrepreneurs-form-25-of-new-u-s-business-researchers/#10ee8099713b

11 "Ease of Doing Business Rankings." *Doing Business*. May 2019. http://www.doingbusiness.org/en/rankings

12 Niels Bosma and Donna Kelley. "Global Entrepreneurship Monitor 2018/2019 Global Report." *GEM Consortium*. January 21, 2019. https://www.gemconsortium.org/report/50213

13 Gary Stockton. "Statistics and Obstacles Facing Women Entrepreneurs." *Experian*. January 29, 2018. http://www.experian.com/blogs/small-business-matters/2018/01/29/statistics-and-obstacles-facing-women-entrepreneurs/

Starting Your Entrepreneurial Journey

How do you fit into this entrepreneurial journey? This chapter will help you to explore and discover your potential for entrepreneurship as a career choice. Think of this exploration and discovery experience as a way to map out a strategy to reach your goals or dreams. Let's imagine that your dream vacation is a hiking trip to Glacier National Park in the US state of Montana. Just as hikers have different levels of experience, so do entrepreneurs. Just as your plan for a wilderness hike would involve many stages, your entrepreneurial journey involves multiple levels of self-discovery, exploration, experiences, and accomplishments on your way to success. For our purposes, the term **entrepreneurial venture** means any type of new business, organization, project, or operation of interest that includes a level of risk in acting on an opportunity that has not previously been established. For each story of entrepreneurial success that is shared—such as that of Facebook or Airbnb—there are even more lesser-known entrepreneurial success stories such as Zipline, a company that delivers medical supplies in Rwanda and Ghana by drone. These entrepreneurs faced the same dilemmas in pursuing their passion, or opportunities, which led them to their entrepreneurial destiny. They courageously stepped out of their comfort zones to explore the possibilities that lie ahead. What is the difference between entrepreneurs and you? The main difference is taking that first step. Many people have ideas that fit into the definition of an entrepreneurial idea but never take that first step. Just as the Chinese philosopher Lao Tzu suggests, every journey begins with a single step.

ARE YOU READY?

Taking the First Step

Go to Fire Nation's website on taking the first step (https://openstax.org/l/52TakeFirstStep) to learn more. Changing your mindset (your perception of yourself and your life situation) and encountering trigger events (significant external situations) can nudge you into taking the first step toward being an entrepreneur.

- Is there a venture you've always thought you should start but never did?
- Think about what factors are stopping you. Consider your mindset and how you might change your mindset so that your venture could become a reality.
- What are some possible trigger events that could make the difference between starting your venture and waiting to start your venture?

Opening your future to the possibility of starting your own venture brings new and exciting experiences (Figure 2.2). Every entrepreneur moves through several steps in considering the entrepreneurial journey. Once you understand this journey, the steps will help you define your path toward creating and starting your new venture. Each step of this process offers another level of understanding that prepares you for long-term success. How will you achieve this success? By taking one step at a time, exploring and learning, considering new ideas and expectations, and applying these experiences to achieve your personal outcome. Think of the entrepreneurial journey as a guide to knowing what is in store for you as you start your new venture.

Figure 2.2 For some, preparing for an entrepreneurial journey may seem like going on a river-rafting adventure that combines beautiful scenery with some exciting, but perhaps frightening, challenges. (credit: "Hands Up" by Jeramey Jannene/Flickr, CC BY 2.0)

One benefit of outlining a step-by-step process is the opportunity to explore different paths or behaviors that may lead to an entrepreneurial venture. Think again of your dream visit to Glacier National Park. How would you get there? What equipment would you need? What kinds of experiences would you expect to have? Think of the Glacier National Park journey as your entrepreneurial journey, a metaphor intended to help you as you create your career as an entrepreneur.

What makes someone ready or willing to choose entrepreneurship over becoming an employee of an established business or a small business owner? It takes confidence, courage, determination, resilience, and some know-how to select entrepreneurship as a career as well as the recognition of the opportunity. An entrepreneur is defined as someone who not only recognizes an opportunity but who also is willing to act on that opportunity. Both actions are required. We might identify an opportunity, but many people do not act on the idea. Confidence, courage, and willingness are necessary to take that first step, as well as remembering the following:

- You are unique. Even if two similar people attempted to launch identical ventures, the results would likely not be the same. This is because each one of us has different ideas, approaches, available resources, and comfort levels, all of which influence the venture's development and eventual success.
- Although there are no hard and fast rules or theories of the best way to launch into entrepreneurship, we can gain wisdom from the lessons learned by experienced entrepreneurs.
- Selecting an entrepreneurial career requires honesty, reflection, and a tendency to be action oriented. You will need to recognize your own strengths, limitations, and commitment as part of that honesty. Reflection is required for self-growth—seeking improvements in your own skills, interactions, and decision making—and commitment is required to maintain consistency in your willingness to make the new venture a top priority in your life. You will also need to understand that you cannot accomplish everything by yourself, and you may need to ask for help. It helps to be curious, open, and able to take calculated risks and to be resourceful and resilient when faced with challenges or obstacles.

ARE YOU READY?

Entrepreneurial Potential Self-Assessment

Take this quick Entrepreneurial Potential Self-Assessment (https://openstax.org/l/52EntSelfAssess) to assess your potential to become an entrepreneur. After completing this self-assessment, what new information did

you learn about yourself? Do you think your answers will change as you acquire more life experiences and education? Why or why not?

ARE YOU READY?

Optimizing Interest Areas

What are three areas that interest you? These could be hobbies, work activities, or entertainment activities. How would someone else describe your skills and interests, or what you are known for? Answering these questions provides insights into your strengths and interests. Next, what is one area that you are passionate about? What strengths could you bring to this passion to build your own business?

Keep an open mind in looking for an opportunity that fits your strengths and interests. If you decide to explore entrepreneurship, what would be your first step? What are your initial thoughts about being an entrepreneur? What would you review or search to find more information on your idea or area of interest? With whom would you first question or discuss this idea? Why?

The Entrepreneurial Journey as a Trip

The **entrepreneurial journey** is your exploration to discover if entrepreneurship is right for you. Every entrepreneurial journey is unique; no two individuals will experience it in the same way. Along the way, you will find opportunities and risks coupled with challenges and rewards. It's useful to think about the entrepreneurial journey as an exciting trip or other adventure. Most of the preparations and steps involved with planning a trip are like those for starting a venture. Just as you would plan and prepare for a trip—starting with inspiration and leading up to finally traveling on the trip—you might follow similar steps to launch a venture. And just as you would prepare for any challenges that you might encounter on a trip—bad weather, lost luggage, or detours—so you should consider potential obstacles or barriers along your entrepreneurial journey (Figure 2.3). Think of these difficulties as opportunities to learn more about the entrepreneurial process—and about yourself and how you manage challenges.

Figure 2.3 The entrepreneurial journey might also include potential obstacles and barriers that travelers on this path must overcome. (credit: "Flickr - The U.S. Army - Camp Taji obstacle course" by The U.S. Army/Wikimedia Commons, Public Domain)

Developing a venture can be an exciting and active experience. It is also a lot of hard work, which can be equally rewarding and enjoyable. Here we present the entrepreneurial journey as seven specific steps, or experiences, which you will encounter along the road to becoming an entrepreneur. You'll find more

information about the entrepreneurial journey in other chapters in this book.

- Step 1: Inspiration – What is your motivation for becoming an entrepreneur?
- Step 2: Preparation – Do you have what it takes to be an entrepreneur?
- Step 3: Assessment – What is the idea you plan to offer through your venture?
- Step 4: Exploring Resources – What resources and characteristics do you need to make this venture work?
- Step 5: Business Plan – What type of business structure and business model will your venture have?
- Step 6: Navigation – In what direction will you take your venture? Where will you go for guidance?
- Step 7: Launch – When and how will you launch your venture?

As you work through each step of the entrepreneurial journey you should prepare for significant aspects of this experience. You will meet with rewards and challenges, the consequences that result from the decisions made at various points along your journey. To visualize the steps of the entrepreneurial journey, imagine your possible hiking trip to Glacier National Park (Table 2.1). Just as hikers have different levels of experience, so do entrepreneurs. Compare the following aspects of preparing for a hike with aspects of your entrepreneurial journey.

Hiking and Entrepreneurial Journey Metaphor

Type of Hiker	Mountain Hiking Skill Level	Entrepreneurial Journey Equivalent
Walker	• Basic or limited hiking experience	• New or limited entrepreneurial exposure • Never started a venture
Climber	• Moderate hiking experience • Special skills for adventure, difficult terrain	• Some entrepreneurial knowledge or experience • Exposure to entrepreneurship (family or friend in business)
Mountaineer	• Experienced hiker with technical skills for climbing hills and mountains	• Experienced entrepreneur • Attempted or launched a venture (solo or with partner)

Table 2.1

Step 1: Inspiration

When you think of being an entrepreneur, what is the inspiration for your venture? Just as you might have an inspiration for a hiking trip to Glacier National Park, you will have an inspiration behind the decision to become an entrepreneur. When you're planning a trip to a new and exciting place, one thing you might do is to imagine what you will experience along the journey and on arriving at your destination (Figure 2.4). This portion of the entrepreneurial journey includes imagining yourself as an entrepreneur or as part of an entrepreneurial team. For this stage, you need a creative, open, and innovative state of mind, also known as an entrepreneurial mindset, which is discussed in more detail in The Entrepreneurial Mindset and Creativity, Innovation, and Invention. Dream *big* about your potential future and opportunities (Figure 2.5).

Figure 2.4 The journey to entrepreneurship is as important as reaching your destination. (credit: "raise challenge landscape mountain" by "mohamed_hassan"/Pixabay, CC0)

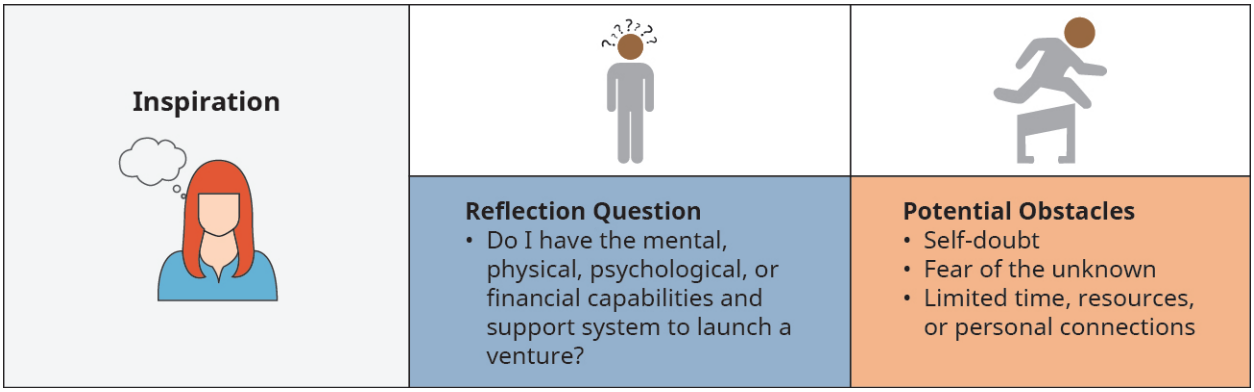


Figure 2.5 When inspired to start an entrepreneurial venture, one questions whether they can do it and identifies obstacles that might present challenges. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 2: Preparation

Just as when you are preparing for a trip, you need a plan (Figure 2.6) to move forward on your entrepreneurial journey. Before your dream hiking trip, you might gather information about Glacier National Park from a trusted source, such as a good friend with travel experience, or you might conduct online research. Your friend's feedback could be just the motivation you need to try this experience yourself. Or you might use your research to determine if the trip is possible. You will need to look at maps, either online or on paper. Either way, you might also consider travel and accommodation options, such as booking a flight and finding a place to stay. You might want to create benchmarks to align your journey with your available resources, such as the amount of time and the amount of money you have to spend on the trip. **Benchmarking** is a method of tracking target expectations with actionable results by comparing one's own company's performance with an industry average, a leader within the industry, or a market segment. Benchmarking can help design the trip to meet incremental goals and timelines. From both a travel plan and an entrepreneurial perspective, although benchmarking is used as a control mechanism, we know that situations can arise that require an alteration in the plan, causing the benchmarked items to also need adjustments.

Figure 2.6 It is important to plan out your entrepreneurial journey, as you would plan out a trip. (credit: "#conservationlands15 Social Media Takeover, August 15th, Santa Rosa and San Jacinto National Monument in California" by Bureau of Land Management/Flickr, CC BY 2.0)

LINK TO LEARNING

Which type of benchmarking will help you the most in beginning your entrepreneurial journey? Visit the American Society for Quality's resource page on benchmarking (https://openstax.org/l/52ASQbenchmark) for help.

To plan for an entrepreneurial journey, you should first conduct some preliminary research regarding your venture idea. Your research must be honest and objective if it is to give you a clear picture of the venture. Next, you might organize and prioritize your research and thoughts. For instance, you might see an idea like yours online or on television, and feel disappointed that someone stole your great idea or beat you to the punch. This is a common occurrence in entrepreneurship, but it should not discourage you. Instead, use that knowledge and energy to find an overlooked or different aspect of your original idea. The difference might even be the focus on a different **target market**, a specific group of consumers for whom you envision developing a product or service. Further, it is critical to maintain a fluid focus upon expanding the scope of a product or service to uniquely differentiate provisions of benefits apart from existing benefits or those offered by competitors. A focus on a different target market is exactly how the Jitterbug smartphone was created, because it targeted senior citizens. The Jitterbug smartphone offers a larger screen, larger buttons, and simpler features that make it easier for older people to make quick calls or send texts.

Preparation also includes opening space in your life to the time and energy commitment needed to support your new venture. Are the important people in your life willing to support the interest and passion you will need to dedicate the time, energy, and other resources to this new venture? Review the questions shown in (Figure 2.7) to consider your answers to these questions. Preparation through research and other activities is discussed in more detail in Identifying Entrepreneurial Opportunity.

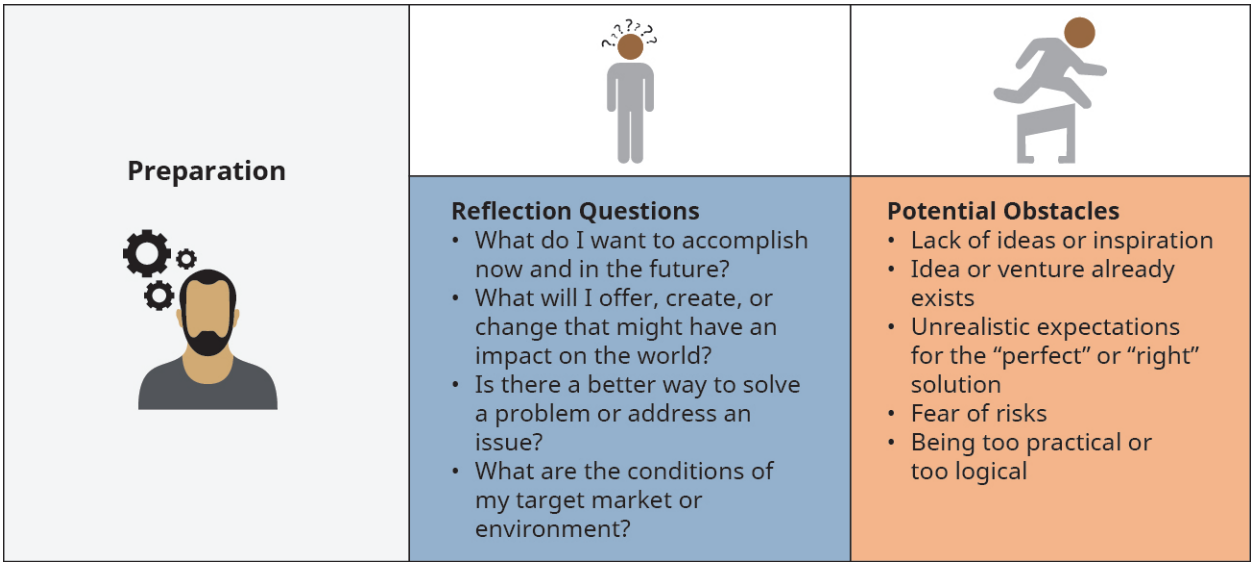


Figure 2.7 In preparing for your venture, you need to ask what you want to accomplish, what you want to offer, and who you want to target. You also need to consider what potential obstacles might present challenges. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 3: Assessment

Now that you have decided where to go for your trip and have gathered information to prepare for it, the next action is to create and set your schedule. This action is simple but critical, because it involves connecting and coordinating information and resources that fit your lifestyle and needs. For example, you might schedule an early-morning Uber or Lyft to the airport and electronic delivery of your plane tickets to your smartphone. For the entrepreneurial journey, this phase might also include recognizing appropriate relationships and gathering needed resources. For many entrepreneurs, the opportunity to receive guidance from trusted advisors or mentors may provide valuable insights on how to manage the process. This step allows for reflection on your idea and intentions. After you've done your researching and gathering knowledge about your idea through the preparation step, is the idea still viable? Is the idea still interesting to you? With a better understanding of the industry, your idea, and your own interests that you gained in Step 2, is this idea something that you still want to explore? This step is discussed more fully in Problem Solving and Need Recognition Techniques with deeper coverage on the topic of opportunity recognition (Figure 2.8).

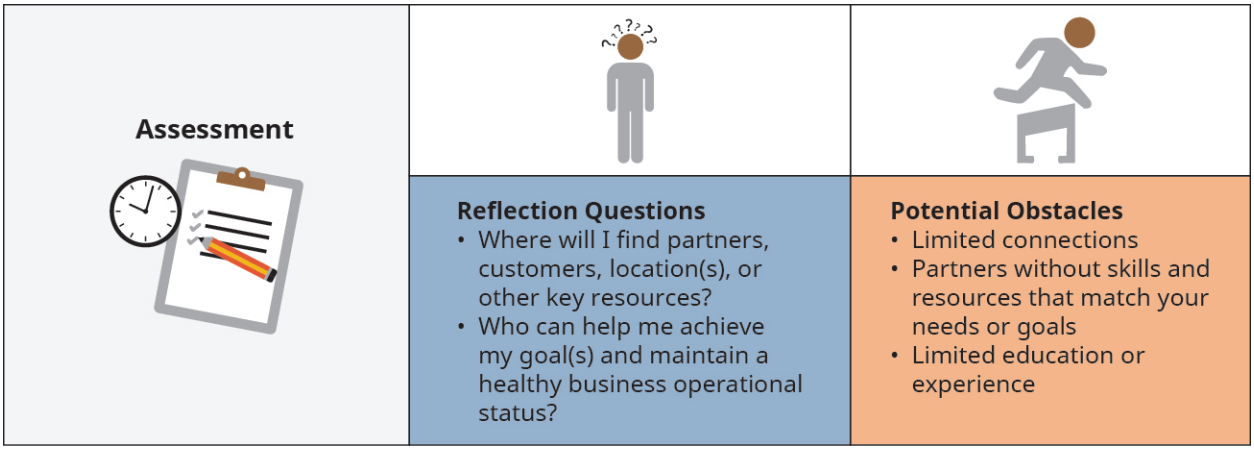


Figure 2.8 Assessing relationships and resources allows for reflection on your idea and intentions. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 4: Exploring Resources

Regardless of where you might travel, you could not complete your trip without adequate resources such as available financing. There are many ways you might fund a hiking trip: savings, loan, pay-as-you-go,

sponsorship (family or friends), or any combination of these options, to name a few. No matter how you finance your trip, it might help to have a balance of available credit and cash on hand to support your day-to-day expenses and any extracurricular activities or even unforeseen emergencies. As discussed in Entrepreneurial Finance and Accounting, the US Small Business Administration (SBA) provides funding opportunities.

This scenario is mirrored in the entrepreneurial journey. Just as you wouldn't begin a trip without adequate resources, including access to cash, you wouldn't begin your entrepreneurial journey without the necessary resources, including cash. The options between funding a trip and funding a new venture are similar, but they have different names. For example, on a trip, you might use the cash you have on hand, from savings or a personal loan. For an entrepreneurial journey, you might address **cash management**—management of cash inflows and outflows to support cash needs of the venture—to include **bootstrapping**, a funding strategy that seeks to optimize use of personal funds and other creative strategies (such as bartering) to minimize cash outflows. (See Entrepreneurial Finance and Accounting for more information on bootstrapping.) Bootstrapping includes ideas like leasing instead of purchasing, borrowing resources, or trading unneeded resources for needed ones. Another example of cash management includes a business model that offers subscriptions rather than a payment received for an item purchased. Subscriptions provide the entrepreneur with cash up front, with the buyer receiving benefits throughout the year. Consider the example of Amazon. Amazon offers Prime with a yearly subscription service, as well as Subscribe & Save, Amazon Instant Video, Amazon Mom, and Amazon Web Services, all based on a subscription business model.

According to Entrepreneur.com, other potential subscription-based models include services or products geared to older consumers, with 8,000 people turning sixty-five every day. A similar idea offers services to college students. Both ideas would offer family members a subscription that sends monthly gifts or products to either the elderly person or college student. We also see this model offered to pet owners who pay a monthly subscription to receive treats and toys for the family dog. Looking back at Amazon, we see the company offering the ease of repeat purchases for frequently used products such as vitamins and air filters.

ENTREPRENEUR IN ACTION

Prospurly

Prospurly is a subscription-based company that uses Cratejoy's subscription platform to sell small-batch artisanal products for bath, body, and home, marketing a natural lifestyle focused on the happiness of living a simple and appreciated life. Conduct your own research on Prospurly and other subscription-based businesses. Read the article, "How I Built a Subscription Business That's Made over 50k in 6 Months," on Cratejoy (https://openstax.org/l/52CratejoyProsp) for more information about this company and Prospurly's move from ideation to profitability.

Other ideas for finding funding include applying for grant funding. The importance of cash and cash management requires in-depth coverage, which is presented in Entrepreneurial Finance and Accounting and Business Structure Options: Legal, Tax, and Risk Issues.

The idea of exploring resources includes many other options besides how to fund a new venture. In a trial run, you would offer your product or service for sale within a limited market on a test basis to evaluate what additional resources are needed to support the success of the venture (Figure 2.9). Examples of places where a trial run fits well, depending on your product, include farmers markets, in-home sales, or through friends and family. The idea is to track the feedback you receive about your product or service. How do people react to the price, the quality of the product, the packaging? You can experiment by selecting one variable to adjust—changing the price, the packaging, the sales pitch, the presentation, or the quantity—to track reactions and make improvements based on this feedback. You may then decide to adjust other variables to

gather more information, as well as considering what other resources are needed for the success of the new venture. Financing and ideas to preserve your financial stability are discussed more fully in Entrepreneurial Finance and Accounting.

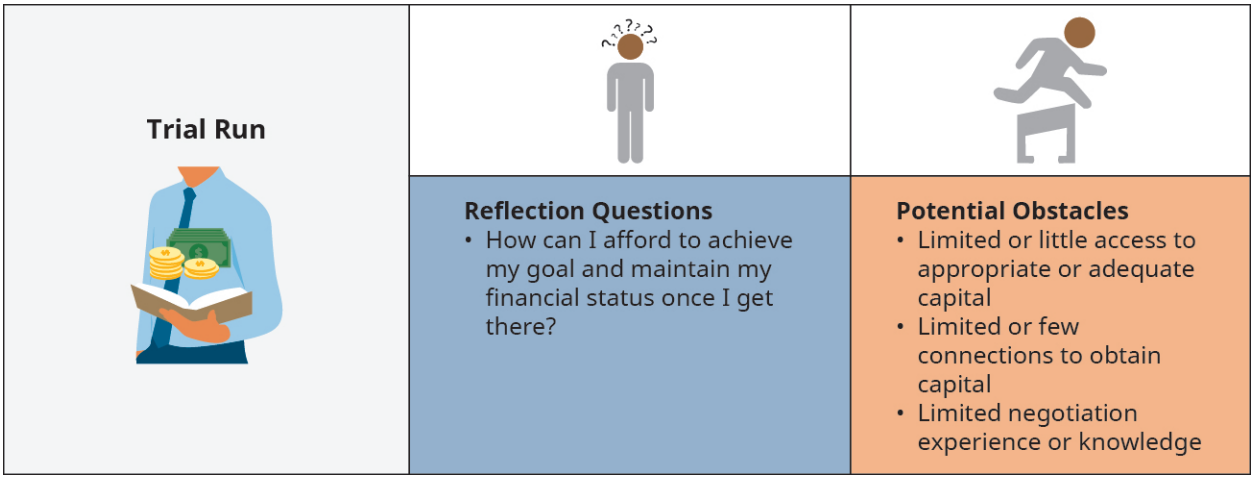


Figure 2.9 During a trial run, you can use a limited market to test your product or service. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 5: Business Plan

The ability to travel and visit new locations is a privilege and a great opportunity to gain exposure to new experiences and opportunities. In addition to the work involved in preparing for a trip, the act and process of traveling involves constant decision making to achieve your desired goals and outcomes. For instance, should you travel to one location in Glacier National Park and explore that area in depth? Or should you attempt to visit as many areas of the park as possible with your given resources and abilities?

The challenge at this step of your entrepreneurial journey is to remain focused on managing your resources to meet your goals and outcomes as you write your business plan for your new venture. You will need to focus on the skills, experience, and resources necessary for your venture, and the management and decision making required to ensure success and adjust your plan based on changes and new information. Just as you might find a location in Glacier National Park where you want to stay for a couple of nights, a deviation from your original business plan (discussed in Business Model and Plan) will also require adjustments and changes based on new information and insights.

Be honest with yourself by running a reality check about your ability to manage a venture, especially from a personal-capacity perspective. For example, if you start a business, will it be a part-time or full-time venture? Will you start while in school? Or will you wait until after graduation? The timing of opening the venture can be the difference between success and failure. Consider the difference between hiking in Glacier National Park in the middle of winter, when the daytime temperature is thirteen degrees below zero, and hiking in the middle of summer, when the daytime temperature is seventy-nine degrees. The timing of your visit to the park is an important part of your enjoyment and success in reaching your destination. In planning for your trip, you would pay attention to your departure time to ensure enjoyment and success in your adventure. Similarly, as part of your business plan, you would also research the best time to open your venture.

Finally, during your travels, getting lost, overwhelmed, or sidetracked is always possible. If you get lost when traveling, you might refer to social navigation apps such as Google Maps, Waze, or HERE WeGo, to find turn-by-turn directions and information. Or you might refer to a weblink, a printed map, or a local expert or guide familiar with the area. The business plan is your map. You should identify decision points and **milestones**, significant key accomplishments, in your plan. Milestones could include points such as hitting your **breakeven point**, the point at which income from operations results in exactly enough revenue to cover costs. If the financial projections in your business plan are unattainable, what is your next move within the plan? If you

don't reach the milestones identified in your business plan, what alternative choices can you make to redirect your venture? The business plan, in its first draft, should inform you whether your venture has a chance at success. If there are negative areas, what can you change? Building this plan before starting the business provides you with knowledge and insights about your idea. Make any necessary changes to the plan to strengthen the possibility of success. Then when you open the venture, track whether the reality of the venture aligns with your business plan's projections and expectations. The business plan functions as both a road map to help you see where you are going next in building your venture and as a checklist to track whether you are on course or need to make adjustments. When entrepreneurs get off track, they can check out self-help websites, speak with a business coach or counselor, or contact local agencies or organizations, including those affiliated with the federal SBA. Organizations that offer free (or low-cost) small business counseling, mentoring, and training, include:

- SCORE (Service Corps of Retired Executives): https://www.score.org/
- Small Business Development Center (SBDC): https://www.sba.gov/offices/headquarters/osbdc/resources
- Women's Business Center (WBC): https://www.sba.gov/local-assistance/find/?type=Women%27s%20Business%20Center&pageNumber=1
- US Export Assistance Center: https://www.export.gov/welcome
- Veterans Business Outreach Center (VBOC): https://veteransoutreachcenter.org/
- Other organizations include locally organized support such as pop-up entrepreneurial schools like PopUp Business School (https://www.popupbusinessschool.co.uk/) and https://www.pbs.org/newshour/show/this-free-program-trains-people-how-to-start-a-business-but-without-debt

These and other resources will be discussed in more depth in Building Networks and Foundations. Look at the review questions and the discussion questions at the end of this section to prepare for creating your business plan. Business plans (Figure 2.10) are discussed more fully in Business Model and Plan.

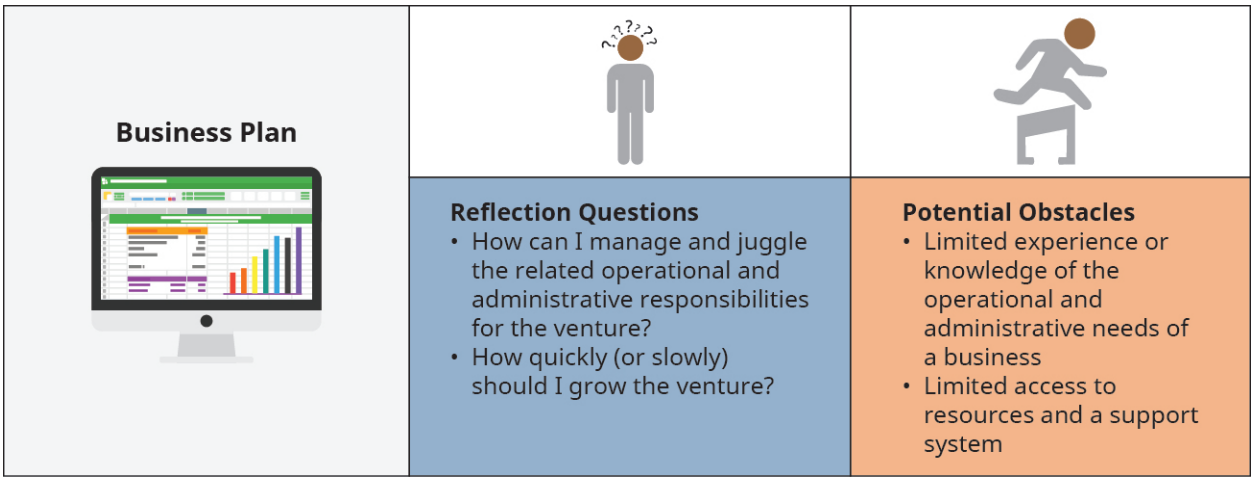


Figure 2.10 Writing a business plan before launching a venture can give you important insights into your idea and can help you modify your business before launch to give it a better chance of success. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 6: Navigation

Once you've completed your trip, reflect on the experiences you had. No matter how well you feel you have planned, there is no way you can prepare for all of the potential challenges, changes, and obstacles that may occur: missed or changed flights, poor weather, an unexpected illness, a trail or road closed for repairs, or sudden good fortune. What parts of the trip went well? If you ran into a problem, how did you handle it? Was the problem something you could have anticipated and planned for? Or was it unexpected? What did you learn from the experience? If you were planning a trip to another national park, what would you do differently in your planning stage? Just as seasoned travelers adjust to their circumstances and learn from their experiences, so should you, as an entrepreneur, learn to adjust by meeting and managing challenges head on.

After completing your business plan, you will probably need to adjust your plan (Figure 2.11). You might decide that you will not have enough resources to survive the time until your venture reaches the breakeven point, or you might determine that the location you selected is no longer available. There are multiple variables that require further exploration and research.

By nurturing an entrepreneurial mindset, you will be better prepared when opportunities, challenges, or obstacles surface. Although you won't be able to predict or plan for every potential scenario along the entrepreneurial journey, an entrepreneurial mindset helps you to be resourceful when opportunities, challenges, or disappointments occur. By unpacking, or by taking an inventory of your available resources, you can also get a better picture of what you may need to unload, retain, or discard, or even if a new direction is the best course of action. On your entrepreneurial journey, evaluating the experience or situation is a perfect opportunity for you to determine how realistic, overambitious, or shortsighted your dreams and goals for your venture may be. This chapter will explore your vision for your future and your venture. Does your vision include a level of flexibility when you discover new information that supports exploring a new area?

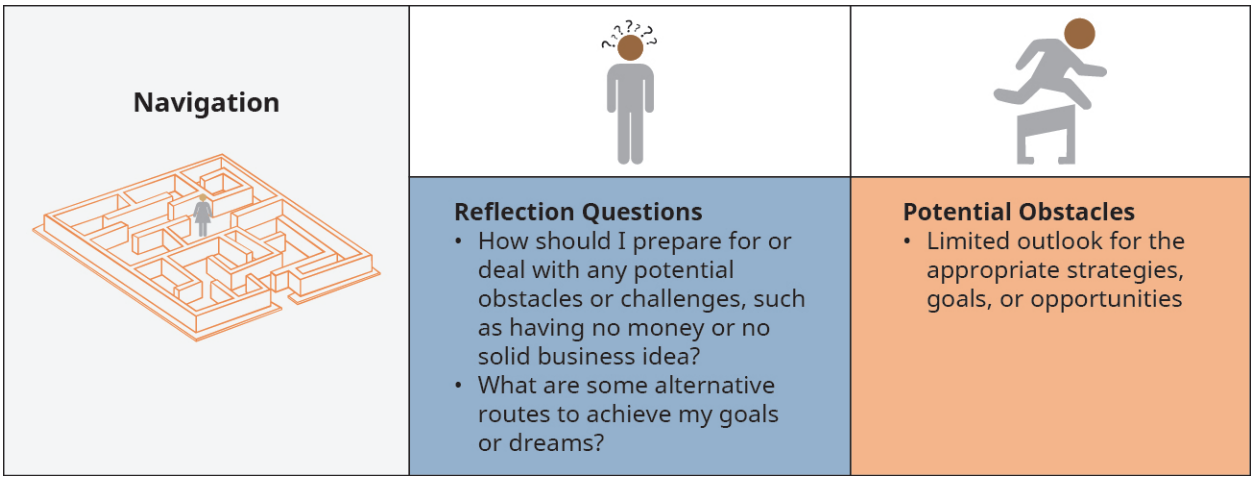


Figure 2.11 Navigation involves being prepared for and making changes when faced with obstacles. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 7: Launch

The actual launch is the exciting event when you open your business. By this point, you have made improvements to your product through feedback received in your trial run; you've identified the value or benefits provided by your product; you've identified your target market; and you've identified the location of your launch, whether it is a geographical location or an Internet location.

Inc. magazine provides an analysis of the best locations to launch a new venture, with Austin, Texas, taking the lead (see "Surge Cities: These Are the 50 Best Places in America for Starting a Business," in Suggested Resources). Consider your target market and the resources necessary to support your venture when choosing the location for your launch. Advice from within the entrepreneurial world suggests that sometimes the launch should take place "under the radar," meaning in a location where you can make mistakes, fine-tune your business model and offerings, and even become successful without competitors noticing that you have created a disruption within the industry. (You will learn more about this in Launch for Growth to Success).

Even as you are launching your venture, many variables will require your attention, just as we covered in Step 7. Navigating through these variables as your venture grows requires constant attention as new potential opportunities arise.

ENTREPRENEUR IN ACTION

Sixto Cancel and Think of Us

Sixto Cancel successfully faced the harsh challenges of aging out of the foster-care system without adult support or guidance. He imagined a better foster-care system for young people then cofounded the firm Think of Us. Think of Us is a platform that helps young people in foster care build their own personalized digital advisory board of supportive adults who act as a virtual life-coaching group. The adults guide the young people through the foster-care system and ensure that they are able to become independent when they leave the system at age eighteen. For more information about this venture, visit www.thinkof-us.org.

2.2 The Process of Becoming an Entrepreneur

Learning Objectives

By the end of this section, you will be able to:

- Describe the evolution of entrepreneurship through American historical periods
- Understand the nine stages of the entrepreneurial life cycle

Scholars of business and entrepreneurship have long debated how people become entrepreneurs. Are entrepreneurs born or made? That is, are some people born with the natural skills, talent, and temperament to pursue entrepreneurship? Or can you develop entrepreneurship skills through training, education, and experience? These questions reflect the classic debates known as "nature versus nurture" or "born versus made," which attempt to explain the determinants of a person's personality and character.

This debate has been around for centuries. In classical Greece, Plato supported the nature argument, whereas Aristotle believed in the nurture perspective. During the eighteenth-century Enlightenment period, Immanuel Kant (1724–1824; supported the supremacy of human reason) and John Locke (1632–1704; opposed authoritarianism) argued their views. Kant firmly believed that obedience was the expected and desired behavior, whereas Locke believed in allowing some degree of freedom and creativity. The focus of the aspects of this argument changed when late-nineteenth-century psychologists sought to understand how individuals obtain knowledge, and as modern psychologists concentrated on additional factors such as intelligence, personality, and mental illness.

Scott Shane, a professor of entrepreneurial studies at Case Western Reserve University, codirected a study using identical twins and fraternal twins as the research subjects. Shane determined that entrepreneurs are about 40 percent born and 60 percent made, meaning that nature—that is, an individual's DNA—is responsible for 40 percent of entrepreneurial behaviors, whereas nurture is responsible for about 60 percent of entrepreneurial behaviors.[14] Although "nature versus nurture" and "born versus made" are parallel arguments, researchers and experienced entrepreneurs suggest a combined viewpoint. You can unite your natural talents and abilities with training and development to achieve a well-rounded entrepreneurial experience and outcome. Once you determine that entrepreneurship is in your future, the next action is to establish a process to follow, such as identifying useful reading materials, attending classes or workshops, finding a mentor, or learning by doing through simulations or firsthand experiences. Firsthand experiences occur throughout our days and lives as we gain relevant experiences and as we develop a mindset to seek out opportunity-recognition behaviors. Completing coursework, such as reading this textbook, and reviewing the suggested resources provided within this textbook are actions that can support your knowledge and awareness of entrepreneurship as a valid option for your future.

14 I. Mount, "Nature vs. Nurture," *Fortune Small Business* 19, no. 10 (2009): 25.

ARE YOU READY?

Entrepreneurial Personality Test

Review Bill Wagner's article "What's Your Entrepreneurial Personality Type?" in *Entrepreneur* at this link: https://www.entrepreneur.com/article/84134. Then, go to The Entrepreneur Next Door at http://www.theentrepreneurnextdoor.com/ to take the Entrepreneurial Personality Test to find your personality type.

- Think about your results. Are you a generalist or a specialist?
- Once you know this information, what other entrepreneurial personality types do you fit into?
- How can you use this information in your pursuits as an entrepreneur?
- What does this information tell you about selecting members of your startup team?

Historical Perspective

The evolution of entrepreneurship in the United States has spanned centuries. Entrepreneurs have responded to and innovated within the political and economic conditions of their times. The United States' economic and industrial spirit has inspired generations of entrepreneurial Americans. Understanding this history might help you appreciate the importance of entrepreneurship as you consider your own entrepreneurial journey.

During the late 1700s, the Pembina Band of Chippewa lived along the Red River of the North, which flows through North Dakota and Minnesota, and into Canada. European explorers established trading posts in this region and bargained with the Pembina and others for pemmican, a buffalo or fish jerky created by tribes for survival during harsh winters when food was scarce. The Pembina pemmican was exported internationally through trading with French, Canadian, British, and other explorers.[15] The Pembina solved a problem of food scarcity, then leveraged the product to trade for other products they needed that were available through the trading posts.

In the late 1880s, Madam C. J. Walker, an African American hair-care entrepreneur, developed and marketed her products across the United States (Figure 2.12), hiring sales agents and founding the Madam C. J. Walker Hair Culturists Union of America and the National Negro Cosmetics Manufacturers Association in 1917.[16] She started her company with a philosophy of "hair culture," which quickly became popular and eventually led to steady employment for African American women. Another African American, Charles Drew, established the national blood bank in the late 1930s, just before World War II gave rise to the need for quick access to blood.[17] He researched transfusion medicine and saw a need that he wanted to fulfill. Drew applied the ideas from his doctoral thesis to create the blood bank and continued to innovate, developing mobile blood donation stations.

15 "Summary of North Dakota History – Fur Trade." State Historical Society of North Dakota, Red River Fur Traders. n.d. https://www.history.nd.gov/ndhistory/furtrade.html
16 "Madam C. J. Walker's 'Wonderful Hair Grower.'" *National Museum of African American History and Culture,* Smithsonian Institution. https://nmaahc.si.edu/blog-post/madam-cj-walker%E2%80%99s-%E2%80%9Cwonderful-hair-grower
17 "The Color of Blood." *National Museum of African American History and Culture*, Smithsonian Institution. https://nmaahc.si.edu/blog-post/color-blood

Figure 2.12 Madam C. J. Walker developed her own hair care line, which is still sold today. (credit: Collection of the Smithsonian National Museum of African American History and Culture, Gift from Dawn Simon Spears and Alvin Spears, Sr.)

Colonial and Early America: 1607–1776

The earliest concept of an "entrepreneur" can be traced to this era, from the French *entreprendre*, which translates as "to do something" or "to undertake."[18] Jean-Baptiste Say (1767–1832), a French philosopher, economist, and businessman, supported lifting restraints to encourage business growth, a highly liberal view in the late 1700s. "The entrepreneur shifts economic resources out of an area of lower and into an area of higher productivity and greater yield," is a concept attributed to Say, as is the word *entrepreneur*.[19]

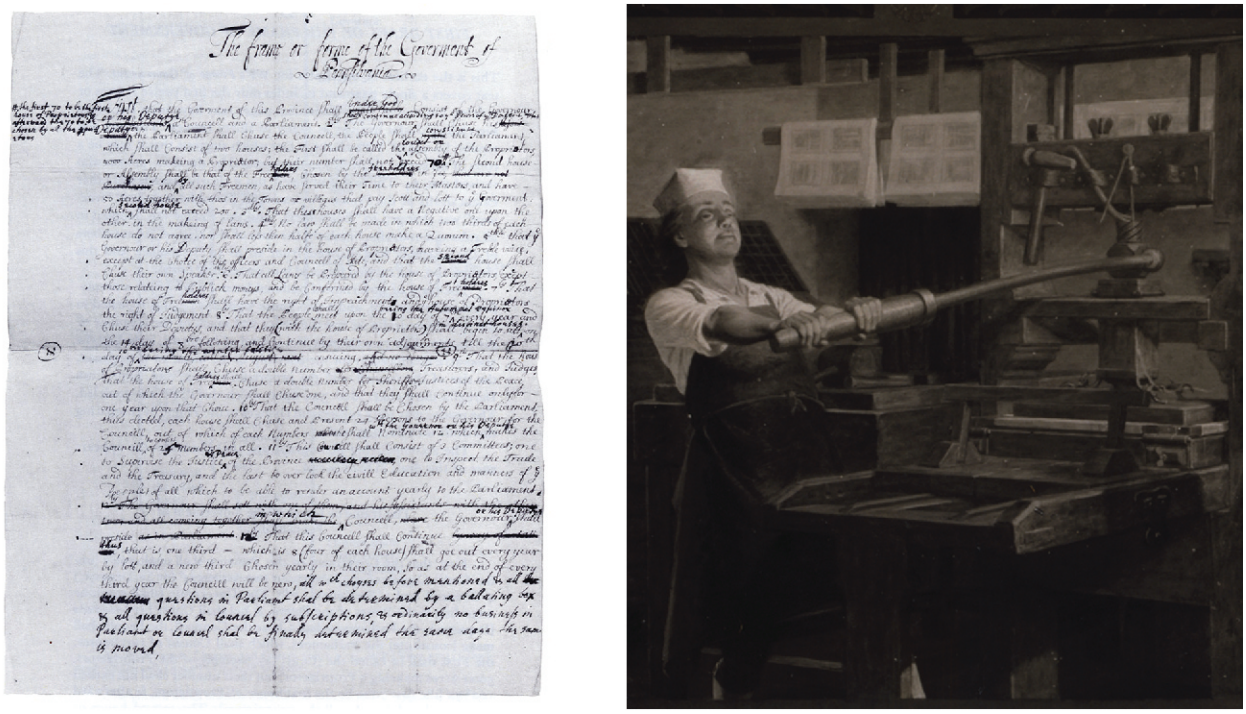
Entrepreneurial-minded persons included merchants, landowners, manufacturers in textile-related trades, shipbuilders, explorers, merchants, and world market traders.[20] The first immigrants to the British colonies took advantage of several key inventions developed before this era, such as printing, double-entry bookkeeping, and improvements in ship design and navigational instruments. The first North American patent was granted in 1641 by the Massachusetts General Court to Samuel Winslow for a new process for making salt. The entrepreneurial spirit of the early colonists helped shape an economic landscape that lasted for generations. Some notable pioneering inventors and entrepreneurs are shown in Table 2.2 and (Figure 2.13).

18 Russell S. Sobel. "Entrepreneurship." *Library of Economics and Liberty*. 2008. http://www.econlib.org/library/Enc/Entrepreneurship.html
19 Tim Hindle. "Entrepreneurship." *The Economist*. April 27, 2009. Adapted from Tim Hindle, *The Economist Guide to Management Ideas and Gurus*, Profile Books.
20 J. McAllister. "Colonial America, 1607–1776." *Economic History Review*. 42, no. 2 (1989): 245–59. https://www.jstor.org/stable/2596204?seq=1#page_scan_tab_contents

Notable Early US Inventors and Entrepreneurs

Inventor or Entrepreneur	Contribution(s)	Significance
Pierre-Esprit Radisson (1640–1710), French explorer	Founded Hudson's Bay trading company	Offered bartering of furs for textiles and guns
William Penn (1644–1718), colonist	Founded Commonwealth of Pennsylvania as a sanctuary for Quakers	Early social entrepreneur
Sybilla Masters (1676–1720), inventor	Invented method to clean and refine corn grown by early settlers	Patent for a process for cleaning and milling corn (1715)
Thomas Hancock (1703–1764), merchant	Founded trading house that furnished multiple goods	Sought alternative funding sources to finance business interests
Benjamin Franklin (1706–1790), inventor, publisher, statesman	Established printing franchises and an infrastructure for his apprentices to launch in other colonies	Epitome of an inventor and serial entrepreneur

Table 2.2



(a) **(b)**

Figure 2.13 (a) William Penn founded the Commonwealth of Pennsylvania as a sanctuary for persecuted Quakers. This colony could be considered an early form of social entrepreneurship. Shown is his first draft of *The Frame of Government in Pennsylvania*. (b) As one of the country's founders, Benjamin Franklin contributed to the Declaration of Independence. His accomplishments as a printer, writer, postmaster, diplomat, and scientist (he contributed to the understanding of electricity) epitomize serial entrepreneurship. In

this painting by Charles Mills, a young Ben Franklin is seen operating a printing press. (credit (a): modification of "William Penn - The First Draft of the Frame of Government - c1681" by University of Pennsylvania/Wikimedia Commons, Public Domain; credit (b): modification of "Franklin the printer" by Library of Congress/Wikimedia Commons, Public Domain)

As entrepreneurship flourished in the American colonies, the economic structure also began to emerge. The prevailing view of economics was associated with the stockpiling of gold and silver. Colonists perceived imports as a reduction of metal wealth—gold and silver money—and felt that exports channeled these metals back to the colonies. To categorize the economic mindset of the time, the Scottish philosopher and economist Adam Smith (1723–1790) wrote *An Inquiry into the Nature and Causes of the Wealth of Nations* (1776). This influential treatise outlined the concepts of free trade and economic expansion through **capitalism**, a system in which individuals, people, and companies have the freedom to make decisions and own property as well as benefit from their own efforts, with government playing a secondary role in oversight. This book confirmed Smith as the "father of economics" and modern free trade. Among the most significant concepts that Smith proposed were the "invisible hand" theory of supply and demand in the marketplace; the use of the GDP to measure a country's level of production and commerce; and the self-interest concept, whereby individuals inadvertently help others as they pursue their own goals.[21] The ability to gain personally from entrepreneurial activities is a key factor in supporting entrepreneurial behavior. Smith's concepts continue to influence modern economics and entrepreneurial activity.

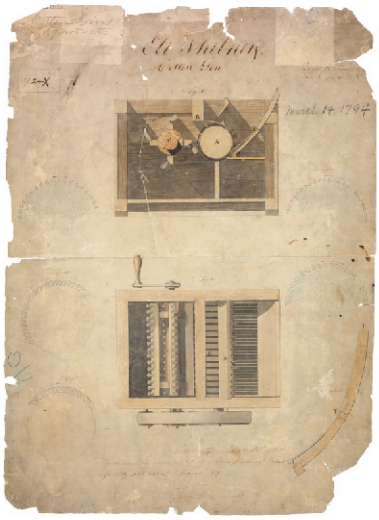
The First Industrial Revolution: 1776–1865

As the colonies expanded, so did opportunities and interest in property ownership, manufacturing, inventions, and innovations. An **innovation** is any new idea, process, or product, or a change to an existing product or process. The understanding and acceptance of innovation developed around 1730, when the economist Richard Cantillon identified the first academic meaning and characteristics of "entrepreneurship" as the "willingness to bear the personal financial risk of a business venture."[22] The First Industrial Revolution was notable for the explosion of inventive activities by the "great inventors," who pursued entrepreneurial opportunities to meet market needs, demands, and economic incentives.[23]

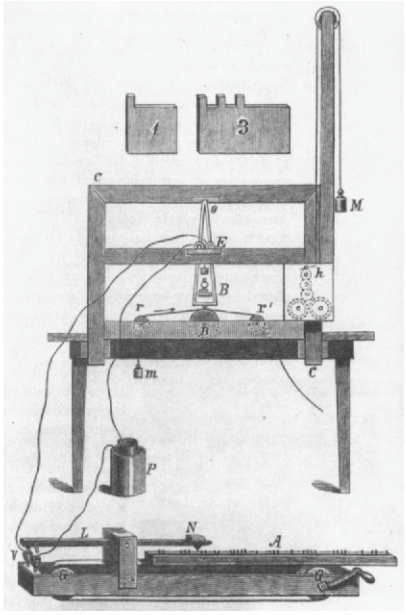
An important thing to keep in mind is that dates of inventions don't necessarily reflect specific launch dates. Development of these inventions may have been ongoing for years or decades before they were considered market-viable products.

A plethora of inventors and their inventions transformed several industries and economic classes across the growing nation. During this era, the country benefited from inventions that created, expanded, or revolutionized industry and increased wealth and expansion. These revolutionary inventors included Eli Whitney (cotton gin, 1794), Elias Howe (sewing machine, 1845), and Samuel Morse (telegraph, 1830s–1840s) (Figure 2.14). Many other people contributed to these and other inventions.

21 "About Adam Smith." *Adam Smith Institute*. n.d. https://www.adamsmith.org/about-adam-smith/
22 Russel S. Sobel. "Entrepreneurship." *The Library of Economics and Liberty*. n.d. http://www.econlib.org/library/Enc/Entrepreneurship.html
23 B. Zorina Khan and Kenneth L. Sokoloff. "'Schemes of Practical Utility': Entrepreneurship and Innovation among 'Great Inventors' in the United States, 1790–1865." *Journal of Economic History*. 53, no. 2 (289–307) doi: 10.1017/S0022050700012924



(a)



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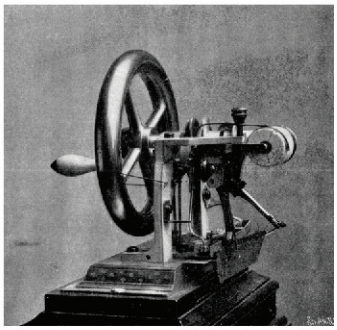


(c)

Figure 2.14 Inventions abounded during the First Industrial Revolution. (a) A US patent was granted to Eli Whitney in 1794 for the cotton gin. (b) This sketch shows Samuel Morse's telegraph. (c) Elias Howe invented the sewing machine. (credit (a): modification of "Patent for Cotton Gin (1794)" by "Gamaliel"/Wikimedia Commons, Public Domain; credit (b): modification of "Morse telegraph" by Unknown/Wikimedia Commons, Public Domain; credit (c): modification of "Elias Howe Sewing Machine 1846" by Unknown/Wikimedia Commons, Public Domain)

Although he was not an inventor but an industrialist, Andrew Carnegie provides an interesting example. A manufacturer who focused on the value of innovations and how to implement them, Carnegie adopted newly developed techniques to improve steel production. He also was among the first to implement **vertical integration**, the strategy of gaining control over suppliers of raw materials and distributors of finished products to expand or control the relevant supply chain. He developed a reliable network of suppliers and distributors to support his steel factories. Carnegie also was one of the first magnates to practice philanthropy. He gave away much of his immense fortune to support community and public library systems, concert halls, museums, and scientific research.[24]

These entrepreneurial pioneers, and many others like them, sought ways to earn a return on investment on an invention and to protect themselves legally through the patent process. A **patent** is a legal grant of protection for an inventor over the rights, usage, and commercialization of an invention for a set time period.[25] An early US patent was issued in 1790 to Samuel Hopkins for his process of making potash as a fertilizer ingredient.[26]

24 Susan Stamberg. "How Andrew Carnegie Turned His Fortune into a Library Legacy." *Morning Edition*. August 1, 2013. https://www.npr.org/2013/08/01/207272849/how-andrew-carnegie-turned-his-fortune-into-a-library-legacy
25 Shontavia Johnson. "With Patents or Without, Black Inventors Reshaped American History." *Smithsonian*. February 16, 2017. https://www.smithsonianmag.com/innovation/with-patents-or-without-black-inventors-reshaped-american-industry-180962201/
26 U.S. Patent and Trademark Office. "First U.S. Patent Issued Today in 1790." USPTO Press Release #01-33. July 31, 2001. https://www.uspto.gov/about-us/news-updates/first-us-patent-issued-today-1790

The innovations of women, African Americans (enslaved or free persons), and other marginalized groups were crucial during this era. As we saw earlier, Sybilla Masters invented a method for grinding corn. She received a patent from the English king in 1715. But because women were not allowed to file for patents or even to own property at that time, the patent was filed in her husband's name.[27] Although the invention of the cotton gin is attributed to Eli Whitney, as we have seen, it may have been based on a design by enslaved African Americans. Social and legal discrimination could limit or conceal the identities of actual inventors, especially if they were women or slaves.[28] Most patent applicants and awardees were White men. One exception was Mary Dixon Kies, who in 1809 became the first woman awarded a patent for her process of weaving straw with silk or thread. This was a key innovation for the hat industry, due to an embargo on European goods.[29] Likewise, many enslaved people were extremely innovative, but laws and prejudice prevented them from filing independently for patents. Because enslaved people had no rights, many sought patent submissions under their owners' names but received no recognition or compensation for their efforts.[30] It was not until 1820 that an African American, Thomas Jennings, was granted a patent for a process called "dry scouring" for cleaning fabric.[31] As the successes and failures of inventors and innovations expanded, so did the consumer demand for better-performing products and services. This led to the Second Industrial Revolution.

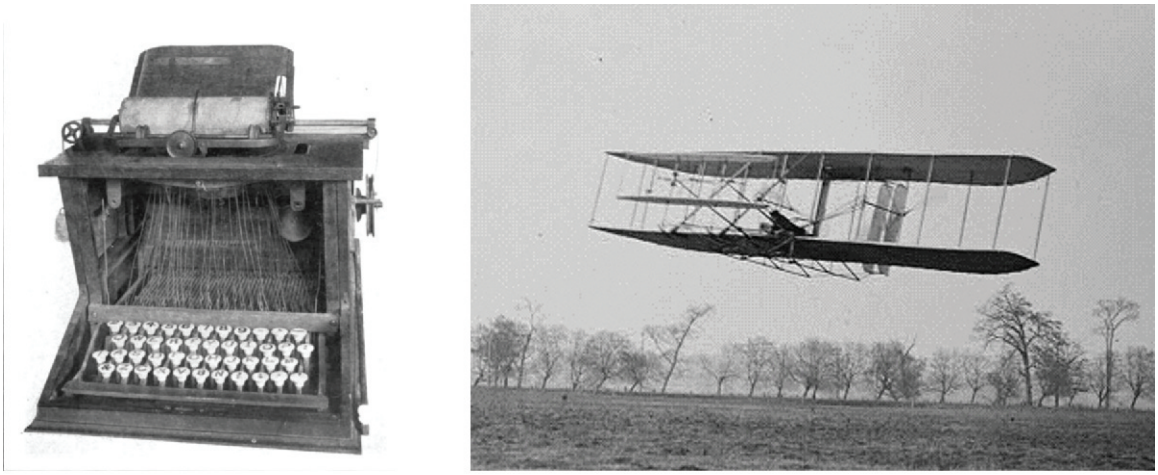
The Second Industrial Revolution: 1865–1920

Although the First Industrial Revolution had a broad scope and a transformative impact, the Second Industrial Revolution helped shape consumer demand for the latest inventions and innovations developed by small and large businesses. The breakthroughs of this era brought applicable innovations in many fields, from chemistry to engineering to medicine.[32]

The nineteenth-century economists Jean-Baptiste Say and John Stuart Mill (1806–1873) refined and popularized Cantillion's definition of an entrepreneur to capture the spirit of their era. Their definition of "entrepreneur" describes someone who creates value by effectively managing resources for better productivity, and someone who is a financial risk taker.[33]

After the US Civil War and into the 1870s, many industries flourished with improvements in production organization (petroleum refinery storage, mass production) and technological systems (electricity and the telephone). Additional inventions included improvements in steel production, chemical dyes, transportation (diesel and gasoline engines, the airplane), assembly-line production, agriculture and food-processing improvements (refrigeration), textiles, and the typewriter (Figure 2.15).[34] As entrepreneurial activity, economic prosperity, and productivity demands increased, entrepreneurs and their inventions were highly regarded and sought after, contributing to the belief that the United States was a land of opportunity.

27 "Sybilla Righton Masters." *New Jersey Women's History.* http://www.njwomenshistory.org/discover/biographies/sybilla-righton-masters/
28 Shontavia Johnson. "With Patents or Without, Black Inventors Reshaped American History." *Smithsonian*. February 16, 2017. https://www.smithsonianmag.com/innovation/with-patents-or-without-black-inventors-reshaped-american-industry-180962201/
29 US Patent and Trademark Office. "USPTO Recognizes Inventive Women during Women's History Month." USPTO Press Release #02-16. March 1, 2002. https://www.uspto.gov/about-us/news-updates/uspto-recognizes-inventive-women-during-womens-history-month
30 Shontavia Johnson. "With Patents or Without, Black Inventors Reshaped American History." *Smithsonian*. February 16, 2017. https://www.smithsonianmag.com/innovation/with-patents-or-without-black-inventors-reshaped-american-industry-180962201/
31 Alex Camarota. "National Inventors Hall of Fame Inducts Next Class of Innovators." *Inventors Eye*. US Patent and Trademark Office. May 2015. https://www.uspto.gov/inventors/independent/eye/201506/index.jsp
32 Joel Mokyr. "The Second Industrial Revolution, 1870–1914." *Semantic Scholar*. 1998. https://pdfs.semanticscholar.org/769c/a06c2ea1ab122e0e2a37099be00e3c11dd52.pdf
33 Russell S. Sobel. "Entrepreneurship." *The Library of Economics and Liberty*. n.d. http://www.econlib.org/library/Enc/Entrepreneurship.html
34 Russell S. Sobel. "Entrepreneurship." *The Library of Economics and Liberty*. n.d. http://www.econlib.org/library/Enc/Entrepreneurship.html



(a) (b)

Figure 2.15 (a) The first commercially successful typewriter was produced by Christopher Latham Sholes and Carlos S. Glidden; this is their 1873 prototype model. (b) The Wright brothers are among the best-known pioneers of early flight. In this photo, Orville flies over their air field in 1904. (credit (a): modification of "Sholes typewriter" by George Iles/Wikimedia Commons, Public Domain; credit (b): modification of "1904WrightFlyer" by "DonFB"/Wikimedia Commons, Public Domain)

Interwar and Postwar America: 1920–1975

When World War I began, the US economy was in a recession, with Europeans purchasing US materials for the war. When the United States entered World War I in 1917, an economic boom ensued. Unemployment declined from 7.9 percent in 1914 to 1.4 percent in 1918 as the United States produced goods and equipment necessary to support the war efforts of the nation and its allies.[35] From an entrepreneurial perspective, World War I contributed to military-related advancements, communication equipment, and improvements in production processes. The American economic landscape began to shift during this era from small independent companies to big corporations. The smaller businesses in the previous era either dissolved or were absorbed by larger corporations. As the stock market crash of October 1929 and the Great Depression of the 1930s struck worldwide, innovation slowed. Consumer confidence waned as economic confidence and production declined, and unemployment rose.

LINK TO LEARNING

Visit the History site on the Great Depression (https://openstax.org/l/52HistGrtDepres) or PBS's American Experience article on the Great Depression (https://openstax.org/l/52PBSGrtDepres) to understand the background and circumstances that led to the stock market crash of 1929, the Great Depression, and how the United States rebounded during this period.

After World War II ended in 1945, American society shifted from reliance on the traditional entrepreneur as a resource to reliance on large organizations that offered stability and job security. Corporations continued to buy up small firms to standardize innovative, large-scale mass production of goods, services, and jobs. The idea of being an entrepreneur gave way to the idea of the "corporate man" with job security and health benefits offered by big employers. Although entrepreneurship did not totally vanish, its growth slowed tremendously compared with previous years and shifted to **corporate entrepreneurship**, whereby large corporations funded the development of new ideas, opportunities, or ventures through formal research and development processes that focused on the corporations' own strategies and goals. Figure 2.16 lists some of the corporations that emerged during this period.

35 Carlos Lozada. "The Economics of World War I." *National Bureau of Economics Digest.* January 2005. https://www.nber.org/digest/jan05/w10580.html

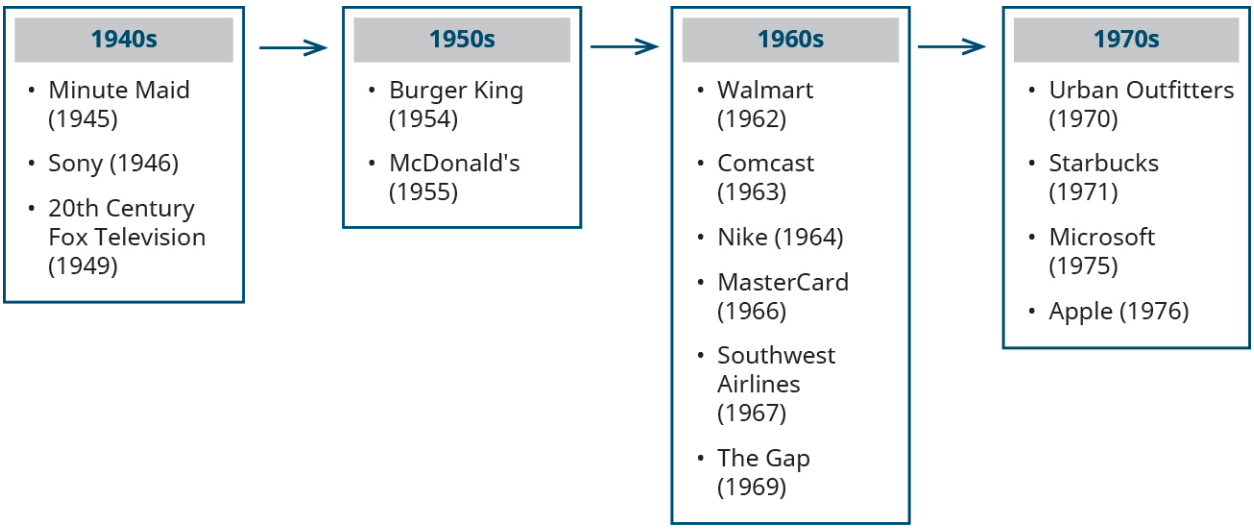


Figure 2.16 Many important corporations developed in the decades after World War I. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

As economic views and confidence in how the United States might regain economic prosperity shifted, so did the scholarly meaning of entrepreneurship. One scholar and economist, Joseph Schumpeter (1883–1950), introduced theories and terminology that continue to influence modern entrepreneurial concepts and practices. He originated two critical phrases: **entrepreneurial spirit**, which is associated with those individuals who are productive self-starters and make things happen, and **creative destruction**, which he defined as the "process of industrial mutation that incessantly revolutionizes the economic structure from within, incessantly destroying the old one, incessantly creating a new one."[36] Schumpeter's theory that innovation would destroy established corporations to create new ones was not a popularly held or shared view at the time. The thought leaders of this era had different approaches to addressing the rise of corporations as part of the entrepreneurial fabric of the United States. Schumpeter theorized that corporations were better positioned than individuals to support the kinds of research and development that would result in innovations and have economic impact.[37] To complement this view, he also proposed the concept that corporate support of entrepreneurs' visions would result in a sustainable "capitalistic financial system" to support and expand on the free-market system espoused by Adam Smith.[38] In contrast, the sociologist and journalist William Whyte (1917–1999) argued that entrepreneurial culture had changed because "American business life had abandoned the old virtues of self-reliance and entrepreneurship in favor of a bureaucratic 'social ethic' of loyalty, security and 'belongingness.'"[39]

Finally, it is critical to note that the growth of corporations and opportunities expanded beyond the borders of the United States. Corporations faced novel global experiences that supported Schumpeter's creative destruction theory, as other countries presented new dynamics to address. The annually created Global Entrepreneurship Monitor (GEM) report is a scholarly examination that examines how a group of nineteen countries benefited from venture-capital investments and the factors affecting those investments for entrepreneurial activity. This study addressed the question of entrepreneurial opportunities, entrepreneurial capacity, and entrepreneurial motivation as parts of the engagement within all industries and the direct correlation between venture-capital investment and high-growth startups.[40] The GEM report is created annually with timely and relevant information related to entrepreneurship and is available at this website: https://www.gemconsortium.org/. This cultural shift in the American entrepreneurial spirit generated new interest in the training and education of workers, ushering in the knowledge economy.

36 "Joseph Schumpeter." *New World Encyclopedia*. http://www.newworldencyclopedia.org/entry/Joseph_Schumpeter
37 "Joseph Schumpeter." *New World Encyclopedia*. http://www.newworldencyclopedia.org/entry/Joseph_Schumpeter
38 "Joseph Schumpeter." *New World Encyclopedia*. http://www.newworldencyclopedia.org/entry/Joseph_Schumpeter
39 William Whyte. *The Organization Man*. New York: Simon and Schuster, 1956.
40 William D. Bygrave, Pamela Lopez-Garcia, and Paul D. Reynolds. "The Global Entrepreneurship Monitor (GEM) Model for Economic Growth: A Study of Venture Capital in 19 Nations." 2001. https://www.researchgate.net/publication/

The Knowledge Economy: 1975 to Today

In the mid-1970s, the promises of corporate life began to lose their appeal to entrepreneurial-minded individuals. One change was established corporations' shift in focus on innovations from research and development departments to internal entrepreneurial activities by **intrapreneurs**. An intrapreneur is an employee who acts as an entrepreneur within an organization, rather than going solo. Intrapreneurs contribute entrepreneurial ideas, products, and services, using corporate work time and resources, but on a much less formal basis than past corporate contributions to innovation. Quickly evolving advances in technology have touched every industry, and people with tech know-how have become champions. Firms dominating the technological landscape include Apple, Microsoft, 3M, Alphabet (the parent company of Google), IBM, and Oracle. In today's David-versus-Goliath culture, these companies once were small startups, but now they command seemingly endless resources. New opportunities have arisen in the world of technology for those willing and able to compete with these giants. All companies, large and small, are interested in a more informed and educated workforce with specialized or advanced degrees in entrepreneurship and business administration. The new entrepreneurs are prepared to develop and lead firms that can become startup superstars. Viewed through our current lens, companies like Apple, Microsoft, Google, and others have become the new Goliaths, but in their startup days, these companies were the disruptors that fought to create new industries or reshape previously established ones.

The Entrepreneurial Process

Your approach to the **entrepreneurial process**, or the set of decisions and actions that you might follow (as in Figure 2.17) as a guide to developing or adjusting your venture, is fluid, not static. This is because your personal interests, background, experiences, resources, and connections are unique to you—but those areas may change over time. For instance, you and a friend might take an art class together for fun and both discover a hidden talent and eye for creating handcrafted jewelry that everyone loves. One day over lunch, you share some of your frustrations with your friend about an interest in potentially selling your unique creations to a local art gallery. Despite your research, you have few clues about where to start or how to get your art shown in a gallery. During your conversation, you are surprised to learn that your friend has already sold several pieces by following a mentor's advice. Through several referrals, she figured out that her best option was to create a presence on Etsy, an artisan-focused website for **e-commerce**, electronic transactions, particularly over the Internet, for the exchange of goods and services. Even though you both started at the same place with similar goals, your results differed because you followed different entrepreneurial pathways. In this case, your friend decided to enter the entrepreneurial process at a different stage than you did. This type of scenario occurs every day and clarifies why ventures differ: The decisions of the entrepreneur or the entrepreneurial team are the heart and success of the venture. *Why* the entrepreneur is the most crucial resource for a venture will be discussed in more detail in later chapters.

242407165_THE_GLOBAL_ENTREPRENEURSHIP_MONITOR_GEM_MODEL_FOR_ECONOMIC_GROWTH_A_STUDY_OF_VENTURE_CAPITAL_IN_19_NATIONS

Figure 2.17 Your entrepreneurial process may involve changing directions many times. (credit: modification of "this way or that" by Robert Couse-Baker/Flickr, CC BY 2.0)

If you decide to take the leap into entrepreneurship, you should follow a certain process before you launch your venture. What is that process? As we discussed previously in the steps of the entrepreneurial journey, you need to think through your goals, prepare and follow an action plan, make sound decisions and adjustments along the way, and persevere through challenges and crises to ensure a successful journey. If that sounds like you have some work to do, you are correct. However, if you follow or recognize the stages in the journey and keep track of the related elements, it could be the most satisfying work of your career. Many people find the entrepreneurial journey fulfilling, in part because they get to define their own paths. The plan to graduate, then find a career working hard to help a company or organization reach its goals, are even more satisfying when you can work for yourself to create your own path and purpose in the world.

Before you create your path, a key action in the entrepreneurial process is developing your entrepreneurial mindset. Recall that an entrepreneurial mindset is about being open, self-reflective, and honest about what you are willing to do and capable of doing to achieve success. For instance, are you comfortable with making sacrifices like spending an evening doing research instead of hanging out with friends or family?

The Entrepreneurial Process: Venture Life Cycle and Product Life Cycle

In general, the entrepreneurial process includes several key stages or some variation of these stages. Keep in mind that these stages do not always follow a sequential pattern, as circumstances and opportunities change. One popular method of understanding and connecting to this entrepreneurial process is to think of your new venture as similar to the human life cycle, the major stages that humans pass through in their life development, and the different growth processes in between.

As we can see in Figure 2.18 and Figure 2.19, the startup stage is similar to the birth of an infant. During the startup stage, or the birth of the idea, the venture requires resources to support the startup as the entrepreneur develops the idea, creates the prototype, and builds the infrastructure to support production. During the startup stage, cash supports building the venture. Meanwhile, the startup is seldom ready to generate sales. Planning for this situation, knowing that cash is needed but not replenished through sales, is an important consideration.

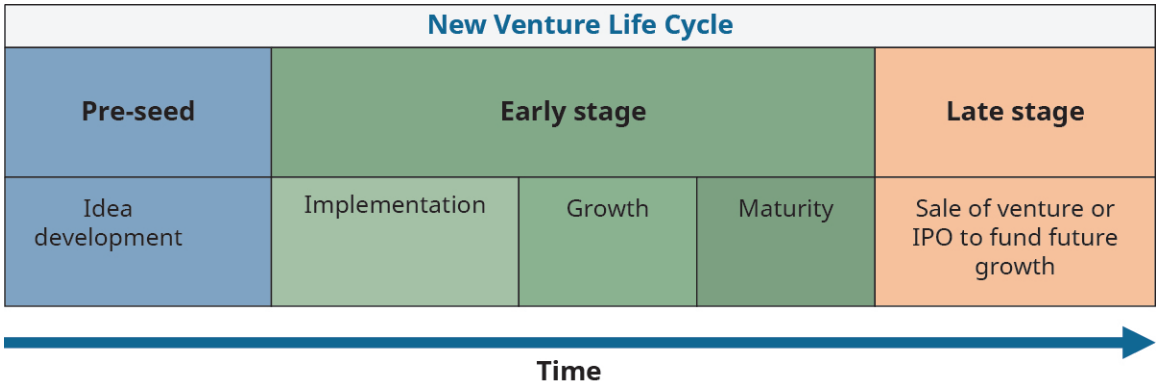


Figure 2.18 This image displays the phases that a new venture moves through as the idea is developed then created as a prototype. The prototype is then perfected in preparation for stage 4, when sales are generated. Stage 4 leads to the start of the growth stage, shown in Figure 2.19. Growth occurs through an increase in sales of the product. At this point, in the product life cycle, adding features or enhancements to the product will encourage increasing sales. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

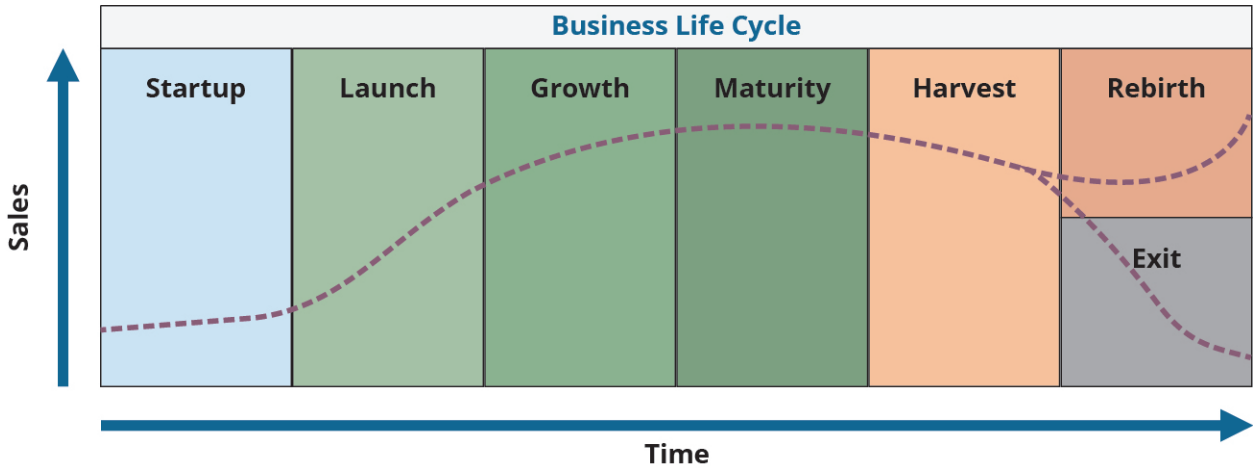


Figure 2.19 This image demonstrates the phases a business moves through from origination through the death of the business. The purple dashed line represents sales, or success of the business's products. We see the most sales dollars in the growth and maturity phases. At this point, the owner or entrepreneurial team must make decisions for the rebirth of the business, at which time the business returns to the growth phase. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Just as a child grows rapidly in their early years, often a business venture experiences quick growth as the product or service becomes commercialized and experiences strong demand, reflected through increasing sales and stronger knowledge and access to the target market. Again, this stage requires resources to support growth. The difference between this stage and the startup stage is cash is generated through sales activity. In some entrepreneurial ventures, however, the growth stage is about building the venture, rather than generating sales. For ventures like YouTube, the growth stage entails increasing the inventory of videos as well as an increase in people accessing the videos.

Just as humans achieve maturity during their life cycle, the business might reach a point where growth slows and perhaps moves into a decline stage. In our human experience, we can take actions to improve or lengthen the maturity stage of our lives through better life choices, such as nutritious eating habits and exercise, to increase longevity and delay decline. We can also extend the maturity of the business and even move into a rebirth and a new growth phase through insightful decisions, such as adding new features to the product or service, or offering the product or service to a new target market. The goal in our lives, and in this analogy, is continued growth and success. Products can be altered or enhanced to extend the product's life cycle, which also extends the life cycle of the venture.

Examples of avoiding the decline and death of a business fit well into the concept of product life cycle and are prevalent in technology-related products such as the television, the personal computer, and the cell phone. For

example, black-and-white televisions underwent a growth stage after World War II. Color televisions were introduced in the 1950s. As technology improved, television manufacturers have repeatedly moved through the life cycle and avoided declines in sales with new features and adaptations with options such as plasma, LED, and smart technology. An example of a product that started and then quickly declined into the death stage of the business is the eight-track player, a music player available between the mid-1960s to the early 1980s. The eight-track player replaced the reel-to-reel tape recorder as a more accessible product for installation in moving vehicles, from cars to Lear jets, to offer individual music purchased by the vehicle owner for listening while traveling. Even as the eight-track player was becoming popular, moving from the introductory stage into the growth stage of the product life cycle, the compact cassette was being developed. In the early 1980s, the compact cassette format replaced the eight-track player, abruptly ending the product life cycle of the eight-track player.

Some products lend themselves more easily than others to managing the life cycle. The goal is to manage the product for continuous growth, whereas other products, such as the eight-track player, are based on technology that quickly becomes obsolete when a better option becomes available. Other examples of products with short life cycles are categorized as fads, like the hula hoop and pet rocks—fads from the past that were reintroduced to a new generation of consumers and that moved quickly through the product life cycle into the last stage—the death of the product with sales either nonexistent or so few that the product becomes a novelty item.

The life cycles of the venture and of the product are two different concepts but are closely related. The venture will need different resources during each stage of the cycle to support the growth and success of the venture. Knowing what stage of the life cycle the product is in assists in decision making. For example, a decrease in sales triggers the need to enhance the product's value to extend and continue strong levels of growth. From the venture's perspective, managing the product life cycle also supports the continued success of the venture.

A successful venture avoids decline or death with the potential to prepare for either the sale of the venture or a public offering of stock, known as an initial public offering (IPO), which gives the company access to significant funds for future growth. Two entrepreneurial IPOs in May 2019 were Zoom and Uber. Zoom is a company that offers video conferencing, web conferencing, webinars, and cross-platform access. Uber is a ride-sharing company. Both entrepreneurial ventures used IPOs to support their future plans for growth.

Think about some of the friends you've known since childhood compared with those you've met in recent years. Suppose you plan to work on a project together and want to figure out who should handle which parts of the work. You might learn some information about a newer friend's past experiences through conversations, observations, or other collaborations. Even so, it would not be possible—or necessary—to learn everything about their childhood and how they learned a specific set of skills or acquired certain connections. You would just start your interaction and work with your friend from the current time. The same is the case for a venture. You might start a venture from the idea-generation stage or from infancy as part of the pre-launch stage. Or you might join the process after someone else has already completed the early stages of the business—for example, by purchasing an existing business or entering into a partnership. You might not have been around when the business was launched, but you can continue with the development of the business from the present moment. Just as each stage of human experience involves different concerns and milestones, the same holds true for your venture. The venture is your responsibility to manage during each stage of the development process.

Figure 2.20 provides an overview of each stage and the associated decisions that you might consider or encounter for the entrepreneurial process.

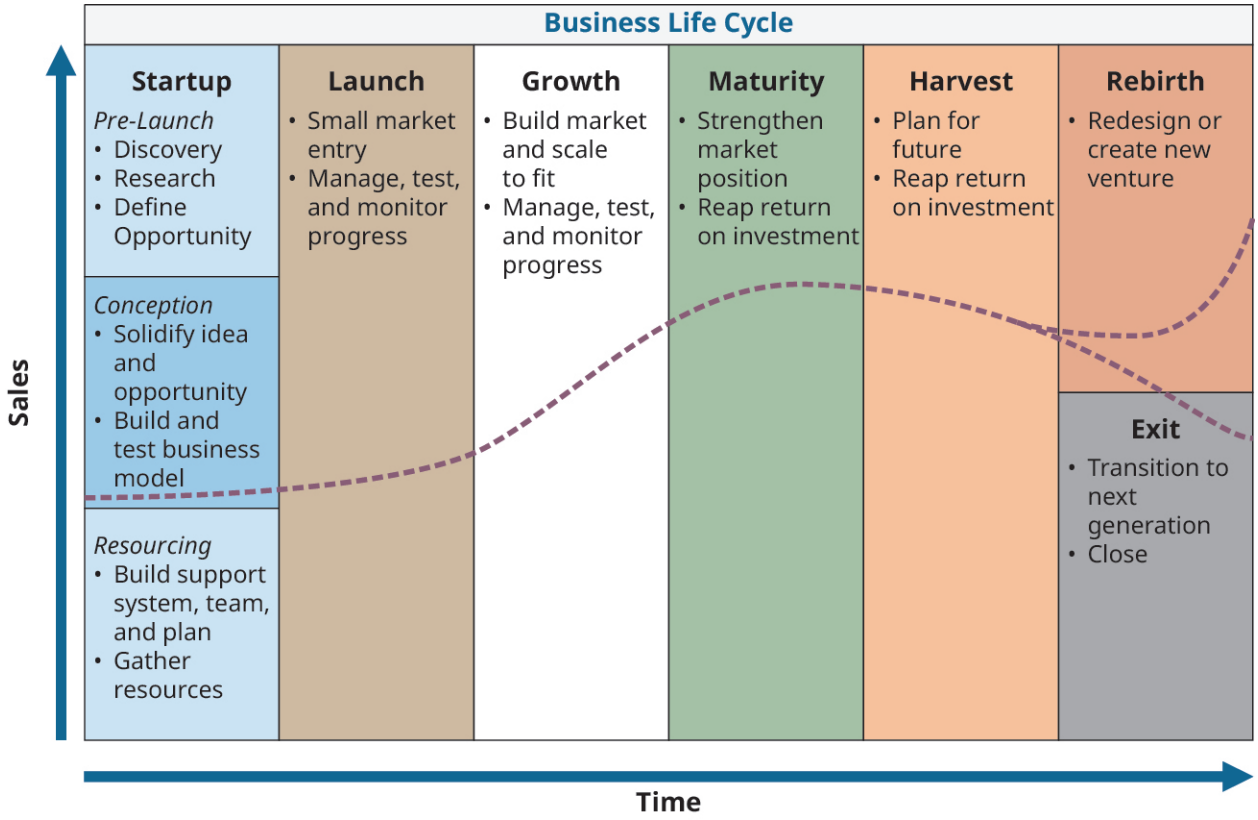


Figure 2.20 The life cycle of a venture roughly parallels the life cycle of a person through different stages that span pre-birth through infancy, youth, maturity, retirement, and then an end or a restart. However, unlike in the human life cycle, the venture stages do not have to be static or sequential. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Stage 1: Startup

In stage 1, startup activities are related to your perceptions about a potential idea, how you develop your idea, and how you might recognize appropriate opportunities. At this stage, the crucial activity is defining the opportunity to develop your concept into a realizable business venture with a strong potential for success. In this stage, you work on developing the idea more thoroughly to determine whether it fits your current and future circumstances and goals. You will also work through exercises to distinguish ideas from viable opportunities. Each of these actions is addressed in greater detail in future chapters. The goal of this section is to introduce concepts for a greater understanding of these stages. Key actions or exercises in this stage include:

- Idea development
- Opportunity recognition
- Identification of a market opportunity
- Research and **due diligence**, or conducting the necessary research and investigation to make informed decisions that minimize risk, such as ensuring you are not duplicating an idea that already exists

Stage 2: Development

Now that you have confidence in your idea, it is time to develop a structure to determine what type of venture will work best for the idea. In Stage 2, you might select a business model (discussed further in Business Model and Plan) and pull together a team (discussed in Building Networks and Foundations) to make your dream venture a reality. The **business model** identifies how a business will build revenue, deliver value, and receive compensation for that value. Some examples of business models include monthly subscriptions, pre-sale orders, kiosk sales, and other choices. Entrepreneurial decisions in the development stage include many options to consider, including bootstrapping, starting out with limited funds, receiving venture funding from

external sources, licensing to receive royalties on a per-item basis, purchasing another business, inheriting a business, franchising either through the purchase of a franchise or building your company with the goal of eventually creating your own franchise, creating a virtual web-based company, using mobile apps that support your business or connect with other businesses, founding a social venture to support a cause, consulting, or freelancing. Choosing among these options or creating your own unique approach to supporting the success of your business will change your results and success level.

Key activities in this stage include:

- Formulation or refinement of your concept
- Design of business model, plan, goals, launch team, and operational structure
- Creation of prototype product to fit market (sample or model for customer feedback)
- Further research and due diligence, as needed

Stage 3: Resourcing

Using knowledge you gained in the first two stages, in the resource stage, you will evaluate the necessary resources to support your new venture. Resources include financial support; support and selection of a manufacturing location or facility (if you are producing a physical product); personnel talents, knowledge, and skills; possible political and community support; and family support, because the new venture will require time commitments that will cut into time with your family. Fundamentals of Resource Planning discusses obtaining resources in more detail.

The key activities in this stage include:

- Gathering pertinent resources, such human and financial capital, investors, facilities, equipment, and transportation
- Establishing connections, networks, and logistics
- Further research and due diligence, as needed

Stage 4: Market Entry

Market entry—the launch of your venture—is often undertaken in a soft launch, or soft open, within a limited market to minimize exposure to unforeseen challenges. As an entrepreneur, you are presenting your new venture to a specific market to see how well it is received and supported. You might make last-minute adjustments at this stage, but the crucial part is to see how the market reacts to your venture. This is an excellent time to scrutinize all aspects of your business for solutions to unexpected problems and improvements in efficiencies, and to track customer reactions to your venture.

One of your most important responsibilities at this point is managing your **cash flow**, or the money coming into and going out of a business, as cash is essential for the success of the venture. In the early stages of the venture, you will need large amounts of cash to fund the operational activities, because your sales are not yet guaranteed. Production costs, payroll, supplies, inventory, lease payments, and marketing: All of these expenditures involve cash outflows from your venture as part of the startup costs. A successful business needs available cash as well as customers for its products and services, or it will not survive. Key activities at this stage include:

- Assessing management structure and needs, adjusting as necessary
- Managing cash flow
- Launching the entity
- Monitoring progress
- Further research and due diligence, as needed

Stage 5: Growth

The growth stage includes making decisions that support the future growth of your venture. In the growth

stage, your decisions reflect the scalability of your venture. There is a big difference between a small-scale venture and a venture that must handle significant levels of sales. At this point, your organizational structure needs an update. You might need new functional levels, such as a finance department, or a human resources department, or perhaps an assistant manager. Other considerations include the size of your facilities. Is the current size, or capacity, appropriate for the growth of the venture? Other questions relate to the appropriateness of your suppliers or inventory providers. Are quality and delivery time meeting your needs? Is the payment system appropriate for your venture? In this stage, you should also monitor the growth of your venture and make appropriate adjustments. For instance, if your venture is not growing as expected, then you might go back to your business plan and see what adjustments you can make. Key actions in this stage include:

- Managing the venture
- Making key adjustments, as needed
- Further research and due diligence, as needed

Stage 6: Maturity

In the maturity stage, your venture has moved into the maintenance phase of the business life cycle. Entrepreneurs monitor how a venture is growing and developing according to the business plan, and its projections and expectations. Is your venture growing faster or slower than you expected? What milestones has it reached? What changes are needed to continue the success of the venture? How can you address those changes? Are you still able to maintain or meet the needs of the venture?

Depending on your situation, you still will need to take action to support the venture. Even if the venture is operating efficiently and in a predictable manner, external changes could compel you to change your venture, for example, by making improvements to the product or service, finding new target markets, adopting new technologies, or bundling features or offerings to add value to the product.

One of the key points to understand at this stage is that ventures can, and often do, fail. Entrepreneurship is about taking calculated risks to achieve a reward. Sometimes your venture may not turn out how you planned. Keeping an open mind and learning from experience presents new opportunities for either changes to the existing venture or even a new venture. Consider these examples of early entrepreneurial failures by people who later went on to achieve great success:

- Bill Gates's early Traf-O-Data company failed because the product did not work
- Walt Disney was told he lacked creativity and was fired from a newspaper job
- Steve Jobs was once fired by his own company, Apple
- Milton Hershey started three candy companies before he founded the successful Hersey Company

Key actions of this stage include:

- Strengthening market position
- Awareness and willingness to change
- Reaping return on investment (ROI)

Stage 7: Harvest

At some point, your company may outgrow your dreams, ambitions, or interests. At this stage, you are harvesting or collecting the most return on your investment while planning how to retire or make a transition away from this venture. Many entrepreneurs enjoy the excitement of starting and building a venture but are less interested in the routine aspects of managing a company. In the field of entrepreneurship, the entrepreneurial team creates a venture with the goal of harvesting that venture. Harvesting is the stage when all your hard work and ingenuity are rewarded through a sizable return on the invested money, time, and talents of the startup team, including any investors. During this stage, the entrepreneurial team looks for the best buyer for the venture to achieve both a return on investment and a match for the continued success of

the venture. Key actions in this stage include:

- Identifying what the entrepreneurial team, and investors, want out of the venture, their ROI
- Planning for your future: What's next on your entrepreneurial journey?

Stage 8: Exit

The exit stage is the point at which your venture either has fulfilled its purpose as a harvested success that is passed along to the next generation of business owners or has not met your needs and goals. These two situations give rise to vastly different scenarios. In the harvesting of the venture, you might receive a sizable cash payment, or a combination of cash payment and a minority share of stock in the venture's buyout. In an exit that reflects the closing of the venture, your option is most likely liquidation of assets, which you would sell to pay off any remaining creditors and investors. In both harvesting and liquidation, the challenge for you as an entrepreneur can be to accept the emotional withdrawal from a venture that has consumed your thoughts, time, and energy. The time has come for you to step out of the picture and allow the venture to be cared for by a new "parent" or to close the venture completely. Key actions in this stage include:

- Exit strategy and plan
- Transition to the next generation of owners

Stage 9: Rebirth

For some entrepreneurs, the excitement of creating a new venture supersedes the financial gain from harvesting a successful venture. The thrill of transforming an idea into a realizable opportunity and then creating a thriving venture is difficult to find elsewhere. In the rebirth phase, the entrepreneur decides to seek out another new venture to begin the process all over again. As an experienced entrepreneur, you can create a new type of venture or develop a new spin-off of your original venture idea. At this point, you have become a **serial entrepreneur**, an entrepreneur who becomes involved in starting multiple entrepreneurial ventures. Key actions in this stage include:

- Redesigning or creating a new venture
- Bringing in a new entrepreneurial team or the team from the previous venture

LINK TO LEARNING

"Drop into" Man Crates to learn about this entrepreneurial venture. Who is their clientele? Does this company sell an experience, a product, or both? What life cycle stage is this business in now? Applying your assessment of the company's life cycle stage, pretend that you are the CEO of the company. What recommendations do you have for the company's continued success and growth?

Visit the Man Crates site (https://openstax.org/l/52ManCrates) to learn more.

2.3 Entrepreneurial Pathways

Learning Objectives

By the end of this section, you will be able to:

- Understand how venture opportunities present different pathways to entrepreneurship
- Describe methods for finding your personal path to entrepreneurship

When you think of which career pathway (as in Figure 2.21) to follow, you might not think of being an entrepreneur in the same way that you would think of being a nurse, an attorney, or an engineer—but you should. Entrepreneurship offers you the chance to express your creativity and business acumen and to control your destiny. Conversely, if you were to earn an engineering degree, your employment options could involve

working for an engineering company. Your job would be relatively secure and structured, with a paycheck and some perks. Or you could leverage your engineering degree into an entrepreneurial venture.

The entrepreneurial journey includes multiple experiences and decisions that will help you reach your entrepreneurial goals. For example, some individuals inherit a family business. If your choice career proves not so ideal or available as planned, entrepreneurship may be an attractive option. However, a growing number of people intentionally choose business ownership as a vehicle for fulfilling their career goals and interests. If you reach this crossroads in selecting your ideal vocation, how do you successfully navigate the entrepreneurial pathway as a career option? Your entrepreneurial journey might travel several paths, each presenting obstacles, twists, and turns before you reach your destination. Many of today's entrepreneurs have followed different pathways—sometimes conventional, sometimes not—that have led to the creation of various business structures matched to each entrepreneur's spirit. These businesses include established or adapted business models that met a need, solved a problem, or developed a social solution.

Regardless of the type of entrepreneurial venture you may choose, many pathways can take you to your goal. Venture types differ in their missions and visions. Their purposes range from earning income (for profit) to meeting a community need through tax-exempt status (nonprofit) to solving a social or environmental problem (social enterprise) to combinations of these types (hybrid). Business Structure Options: Legal, Tax, and Risk Issues examines each type in depth.

Figure 2.21 There are many different pathways you can take on your entrepreneurial journey. (credit: "Explorer" by Sakeeb Sabakka/Flickr, CC BY 2.0)

For many established businesses, the pathway is not always as clear as the entrepreneurial process suggests. This is because entrepreneurs are opportunists, leaders, and initiators: They take calculated risks to create or adapt something to solve a problem or create a response for potential financial gain or intrinsic value. The reality is that these situations or opportunities do not always occur in a logical sequence or order. Instead, entrepreneurial-focused individuals might encounter opportunities, offers, or options that spark a new venture.

Opportunities and Options

If you are ready to launch a venture, you will find numerous situational opportunities to pursue your interests. A **situational opportunity** is one that becomes available, depending on factors such as where you work, your family obligations, your idea or invention, your unique creative expression, or a recent career search or job change. The evolution of entrepreneurship, your own receptiveness to entrepreneurial thinking, and many existing and emerging platforms make this possible.

As you plan your venture, you should consider opportunities in these areas:

- On the Job. Some workplaces offer intrapreneurial opportunities, or ventures created within the company, for entrepreneurial-minded individuals. The firm 3M, for example, has historically nurtured employee creativity and promoted innovative opportunities for employees. This environment inspired an employee project that resulted in the invention of Post-it notes. Even if a company does not support venture creation, there is also the possibility of taking the entrepreneurial idea out of the company to create your own venture.
- Family Obligations. You might work in a family-owned business or take over after family members retire or transfer ownership to other family members.
- Franchises. You might purchase an existing **franchise**, a license granted to an entrepreneur to operate under the franchise's name.
- Web-Based Venture. You might launch a product venture through Etsy, Shopify, or another e-commerce web site.
- Work for Hire, or Independent Contractor. You might launch a consulting business or work as an independent contractor to gain clients, experience, and income on a flexible schedule.
- Unemployment. Being underemployed or unemployed might make entrepreneurship a pathway to economic freedom.
- Purchase. You might purchase an existing business from a retiree, your current company, or a family that owns a business. As a business owner's life situations change, due to aging or new interests, the business becomes available for new ownership. Working for a company can offer the option of buying out the current owner to become the new owner. Purchasing an existing company provides historical financial data and decisions that support future successes. If you are employed by the company, you have the opportunity of learning details about how the business is managed, an advantage that could support your success in purchasing and managing the company.
- Frustration. You might encounter a currently existing product or situation that needs improvement or a solution, and decide to tackle the situation yourself.
- Serendipity. This is a situation in which various pieces come together to support the creation of a new company or product. The Entrepreneur in Action: Gordon Moore and Fairchild Semiconductor box describes how Gordon Moore (creator of Moore's Law on the exponential growth of a single silicon chip doubling every year) was working for Shockley Semiconductor in 1956. At that time, he had little-to-no knowledge of semiconductors. However, he quickly learned about semiconductors by applying his PhD in chemistry and physics from Caltech to the semiconductor industry. After one year of employment, Moore and seven other employees left to form Fairchild Semiconductor, financed by Sherman Fairchild. During his eleven-year employment with Fairchild Semiconductor, Moore published a paper describing what we now know as Moore's Law. His next move was based on recognizing the importance of the microprocessor in transforming the computer and related industries. After frustrations with Fairchild's lack of support for this new direction, Moore, along with a colleague from Fairchild Semiconductor, Robert Noyce, formed Intel, the second largest semiconductor chip manufacturing company in the world.

ENTREPRENEUR IN ACTION

Gordon Moore and Fairchild Semiconductor

Sometimes the path to entrepreneurship doesn't occur as you might plan or think. Consider the story of Gordon Moore, a cofounder of Fairchild Semiconductor: "Like many other scientists and engineers who have ended up founding companies, I didn't leave Caltech as an entrepreneur. I had no training in business; after my sophomore year in college, I didn't take any courses outside of chemistry, math, and physics. My career as an entrepreneur happened quite by accident. There is such a thing as a natural-born entrepreneur....But the accidental entrepreneur like me has to fall into the opportunity or be pushed into it. Most of what I learned as an entrepreneur was by trial and error, but I think a lot of this really could have been learned more efficiently."[41]

The combination of diversity in educational background and skills, the serendipity of being in the right place at the right time, and facing frustrations with the current situation can combine into recognizing an entrepreneurial opportunity. For Gordon Moore, learning about semiconductors, and creating the company Intel, was the furthest idea of what he pictured for his future. The serendipity of his experiences, knowledge, and intelligence combined to support the creation of Intel. Gordon Moore is reported to have a net worth as of October 2019 of $10.6 billion.

One core concern of entrepreneurship is how you will fund your venture and where you will find the necessary resources. Although some businesses require significant startup funding, it might surprise you to learn that many ventures have been launched by entrepreneurs who used their own capital, labor, connections, or other resources to start—an approach known as bootstrapping. Some savvy bootstrapping strategies include launching a venture part-time while maintaining a full-time job, using personal savings, bartering for services and materials, and securing pre-orders. Some entrepreneurs seek financial support for their venture through funding from angel investors, venture capitalists, or traditional loans or debt. The advantages and disadvantages of these approaches are covered in Entrepreneurial Finance and Accounting, along with an in-depth discussion of bootstrapping.

Finding Your Entrepreneurial Path

The process and pathways to entrepreneurship can be overwhelming. With so many choices and decisions involved, entrepreneurial choices can seem intimidating, and the route you follow may sometimes produce some anxiety. Before you get consumed with the technical aspects of launching a venture, it is important to start with the most important foundation: finding your personal path to entrepreneurship.

Your Personal Path through Self-Reflection

Your decision to launch a venture should not be taken lightly. Entrepreneurship requires a lot of energy, decision-making skills, tenacity, resourcefulness, and flexibility. As you consider entrepreneurship as a career, you should complete some self-reflection to figure out how, why, and when entrepreneurship may be the right professional path for you. For example, if your personality is introverted—that is, you often find it most energizing to be alone—you might consider a venture that capitalizes on that scenario. (Recall your entrepreneurial self-assessment Are You Ready?: Entrepreneurial Potential Self-Assessment.) It might be helpful to study or meet other entrepreneurs with a venture you find interesting.

41 Gordon E. Moore. "The Accidental Entrepreneur." *Engineering & Science*. Summer 1994. http://calteches.library.caltech.edu/3777/1/Moore.pdf

WORK IT OUT

Startup Ideas

Visit Medium.com to check out this "Top 10 Business Ideas for Startups" article (https://openstax.org/l/52TenBusIdeas) and then review the startup ideas for introverted personality types (https://openstax.org/l/52IntrovertBus) at Small Business Trends.[42],[43] Review the lists of ideas. Next create a list of five or more of your own startup ideas. Often, we gain new insights by reading through other ideas. Your idea might be a spin-off of an original ideas. Or the information you gain could trigger a brand-new idea.

Your Personal Path through Research and Experiments

A key step to finding your personal pathway to entrepreneurship is to conduct research and try out roles related to your desired venture. Researching the potential industry or entrepreneurial options available to you will provide some level of comfort and validate your decisions about what you might do next. One concrete way to do this is to "shadow" a professional in your desired field. This means arranging to be an observer during a standard workday to see firsthand what is involved in running that type of business. You may also be able to secure some experience by serving as an apprentice, intern, or lab assistant, or as an independent contractor or freelancer, an individual who contracts to offer professional services or tasks for a negotiated fee. Informational interviews—whether informal chats with new or established business owners at a trade show or networking event, or a formal question session—can also provide insight.

Your Personal Path through a Soft Launch

One sure pathway to entrepreneurship is to jump in with both feet and experience the process by launching a venture. Although this may seem like a big leap or you may feel you are not ready, remember that entrepreneurship is an experiential discipline that can be understood fully only through hands-on experiences. Launching a venture for a limited time frame or audience to gain experience, insights, and feedback about the target market or consumer—a process known as a **soft launch** (or soft open)—will provide valuable feedback on how to meet the consumer's needs or improve on your product to ensure success. You might explore a soft launch by creating a sketch or sample of what you plan to offer and asking friends and potential customers what they think, or by creating a website or app prototype to share with a limited number of people to see if it works as planned (sometimes called a beta test) and get feedback.

2.4 Frameworks to Inform Your Entrepreneurial Path

Learning Objectives

By the end of this section, you will be able to:

- Identify common frameworks used to shape an entrepreneurial venture
- Compare how some frameworks better fit certain venture types
- Define an action plan and identify tools available for creating an action plan
- Describe some common types of entrepreneurs

In designing a venture that is sustainable or capable of being self-funded, it is helpful to use specific tools to manage information. One such tool is a **framework**—a structure or outlined process that can be used to accomplish entrepreneurial goals through problem solving, idea generation and validation, and brainstorming.

42 Vikas Agarwal. "Top 10 Business Ideas for Startups," *Medium*. August 25, 2016. https://medium.com/search?q=top%2010%20business%20ideas%20for%20startups

43 Annie Pilon. "50 Business Ideas for Introverts." *Small Business Trends*. October 4, 2016. https://smallbiztrends.com/2016/09/business-ideas-for-introverts.html.

Selecting a Framework

You can choose any of several popular frameworks to help with the design and integration of your business experience and entrepreneurial thinking. The most widely used frameworks that have been developed as integrative tools to support entrepreneurial thinking include:

- Business Model Canvas (BMC) offers a simple, one-page tool used to design an innovative business model that can be presented to key stakeholders (Figure 2.22). The business model canvas is discussed more fully in Business Model and Plan.

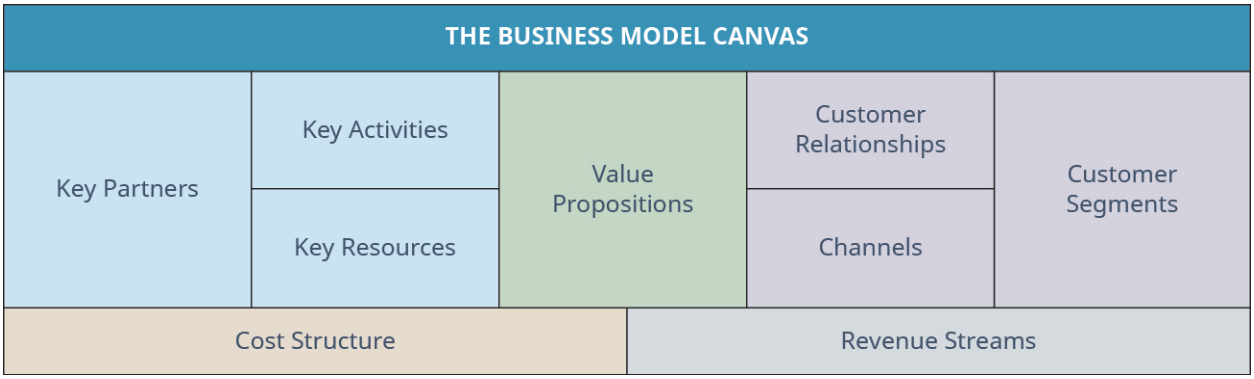


Figure 2.22 Here is an example of a Business Model Canvas with a framework to identify key components of the venture. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

- Lean Strategy Canvas is a spinoff of the BMC that introduces a potential customer feedback loop for continuous product or idea improvement to meet the market's needs (Figure 2.23). The lean strategy canvas is discussed more fully in Launch for Growth to Success.

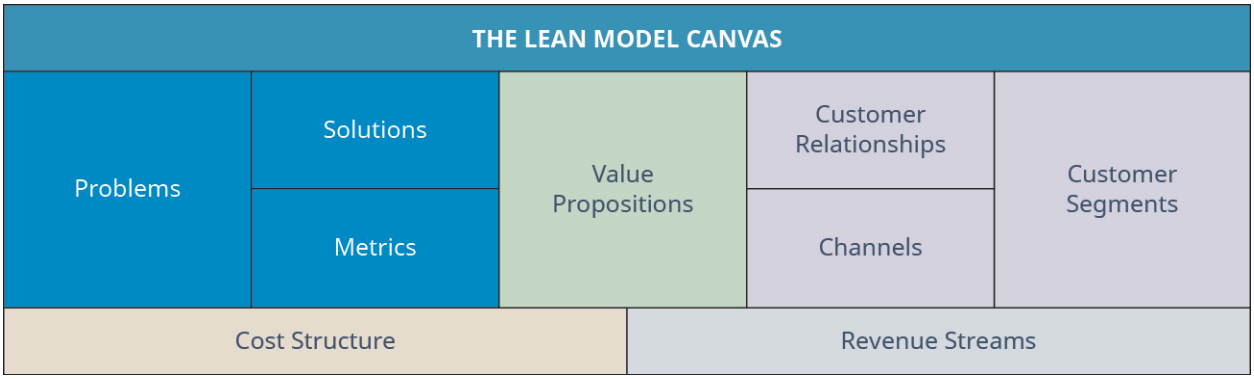


Figure 2.23 Here is an example of Lean Strategy Canvas, a framework to assist in developing the business model, and competitive advantage and related areas aligning the product and market for the venture. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

- Design Thinking Process supports a systematic, logical approach for addressing and solving problems with multiple solutions (Figure 2.24). Design thinking was first applied in relation to STEM fields—science, technology, engineering, and mathematics. Due to the success of this process, design thinking has become popular in many other areas.

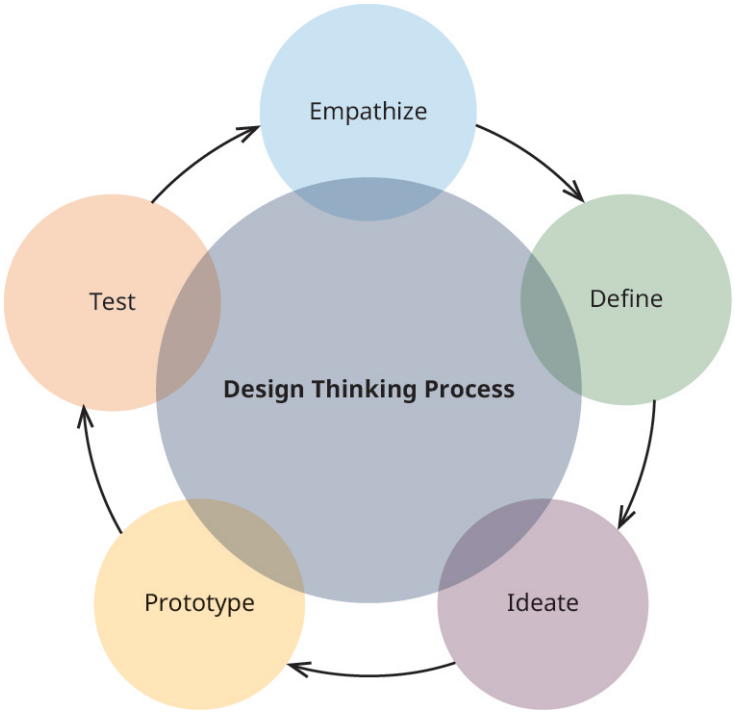


Figure 2.24 The design thinking process is a systematic approach for solving problems. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Design thinking approaches problem solving or the creation of a new venture from the perspective of the customer. For example, Amazon provides easy-to-open packages after observing the challenges customers had in opening the delivered products. Design thinking is covered in greater detail in Problem Solving and Need Recognition Techniques with applications to starting an entrepreneurial venture, product design, and improvements to existing products.

- Four Lenses Strategic Framework is used for the development of social enterprises; assesses four strategic areas (stakeholder engagement, resource mobilization, knowledge development, and culture management) to address a social problem and provide sustainable social impact (Figure 2.25).

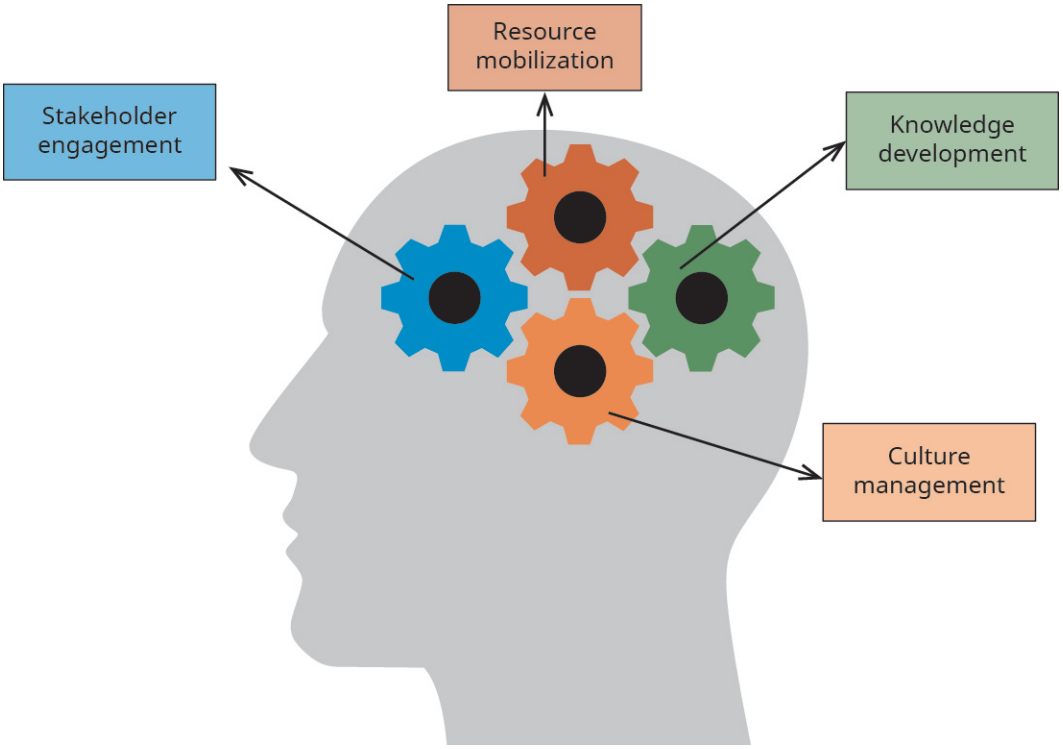


Figure 2.25 The Four Lenses Strategic Framework involves stakeholder engagement, culture management, resource mobilization/application, and knowledge development, and can provide synergies and insights in building compatible and aligned actions. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The typical application of each framework is shown in Table 2.3. The process of selecting the most appropriate framework for your entrepreneurial interests might help you understand how to develop your idea. We recommend that you try all four frameworks before selecting one. Even though each framework is identified for a general class of venture, each one provides a different perspective for developing your venture.

Frameworks

Framework	Description	Typical Use
Business Model Canvas	A one-page tool that maps out nine basic building blocks that are necessary for a successful business model	Helps prepare a sustainable business model
Lean Startup	Outlines a quick feedback loop through customer input	Used for fast-paced industries and quick idea validation
Design Thinking Process	Outlines a systematic, results-oriented process to address and solve problems	Used for the development of STEM fields with expansion into entrepreneurial ventures, products, and processes; applicable to all areas
Four Lenses Strategic Framework	A practitioner-driven model that considers four perspectives to support and develop a client-focused ecosystem	Used for the development of social ventures

Table 2.3

Applying the Framework through an Action Plan

At some point during your venture development process, it becomes critical to capture your thoughts and intentions in a meaningful and productive way. Creating a customized **action plan**—an organized, step-by-step outline or guide that pulls together the ideas, thoughts, and key steps necessary to help set the stage for entrepreneurial success—at an early stage will make the entrepreneurial process much smoother and potentially more successful in the long run. Applying an appropriate framework will provide you with a visible, tangible, strong foundation for your future venture. In completing the framework, you should identify gaps as well as ideas for further development, then add both to your action plan. Just as you can choose from several types of frameworks, you can apply any of a variety of action plans. This section introduces some widely used action-planning tools but is not exhaustive. These selected action plans are presented as a way to jumpstart your thinking for the venture creation process.

Action Plans

You may have heard stories about potential entrepreneurs who hesitated to start a venture, largely out of fear of creating a business plan. Historically, business plan creation has required significant amounts of time, resources, and research. Although business plans are still enormously valuable (and are discussed in depth in Business Model and Plan), some useful business-plan-like tools have emerged: These are essentially variations on the development, content, and structure of a traditional business plan or one of its components. One other concern about business plans is how entrepreneurs use them once they are completed. In many cases, when the venture is launched, the entrepreneurial team discovers that the business plan does not reflect the realities that the team faces. A wide range of variables can often negate the value of the business plan. The true benefit of completing the business plan is that it forces the entrepreneurial team to think through their decisions as reflected in the plan. Even if the venture and the business plan change, the process of creating the business plan encourages critical thinking and improved decisions. In real time, you will need to make changes to your business plan and your venture. Throughout the venture's life span, you should continue your background research and projections to adapt the business plan.

Unlike with the business plan, the purpose of an action plan is to pull together the ideas, thoughts, and actions necessary to help you set the stage for entrepreneurial success. Consider what kind of action plan you need to prepare a holiday meal. We have a vision of the end result—friends and family gathered together to share a delicious, festive meal. We will need to select the right location for the holiday meal, identify the guests to invite, and create a financial budget for the related costs of the holiday meal. Then we would need to create our action plan—similar to a business plan—to identify what actions are necessary to support the event. In our action plan, we would include inviting guests to the event, drawing up a menu and a grocery list, designing a timeline to ensure that all the dishes of the holiday meal are completed in the correct sequence: We want all the food to be ready at the right time. Our action plan would also include the clean-up process and any after-dinner activities that we want at our event. As you can see, both the business plan and the action plan are necessary for success.

Once you select a framework and an action plan, you have the basic tools and information you need to outline the path of your venture. The framework offers a big picture of what you want to create and the resources required for that goal, whereas the action plan provides you with concrete actions for starting along your entrepreneurial path and, later, for supporting the business plan.

Action plans can also result from using the tools listed in Table 2.4. These tools can help you visualize the process necessary to reach your end goal by clarifying the necessary actions. They are also tangible guidelines for innovating, exploring, and creating solutions to entrepreneurial problems or opportunities. You might also use your action plan to get "unstuck" during any challenging phase of the entrepreneurial process. One word of caution regarding these tools: You need to use them to get results. So be sure you are realistic about your interests, abilities, and availability when you create your plans. For example, wireframing is a technique for webpage design used early in the development process in which content, layout, and functionality are

identified prior to the actual creation of the webpage. Coincidentally, this is another application of design thinking through the focus on the end user's interaction with the website. As you can see from this example, searching for popular tools used within specific industries will provide you with support in building your framework. Table 2.4 provides a few examples of action planning tools that are used to delve into the specific topic.

Action Plan Support Tools

Tool	Description	Use
Vision or Dream Board	A visual tool to present the ideal situation that you are working towards achieving	Wireframing
Storyboard	A scene-by-scene visual of the activity process from start to finish	Downloading method (IDEO)
Mind map	A visual tool that assists with categorizing brainstorming types of ideas	Brainstorming
Hypothesis	A proposition or statement as a basis for further testing or investigating	Interviewing
Logic Map	Visual representation of relationships between various components or variables	Questionnaires

Table 2.4

The action plan support tools presented in Table 2.4 are a sample list of representative tools that are useful in motivating, inspiring, identifying, and clarifying needed actions. This list is not exhaustive; if you have something that works for you, then use it. Several apps are also available to help you capture ideas to create action plans, as shown in the Suggested Resources. The idea is to find and use a visual or tangible tool that inspires you to get focused, organized, and committed to taking the actions necessary to turn your entrepreneurial dream into a reality. Let's say you know that you want to start a venture that helps people recover after some type of disaster. You could use one of these action plan support tools, such as a mind map, to help you brainstorm possible needs resulting from a disaster in a city (Figure 2.26). You can categorize the ideas to help people and animals, or to repair the city's infrastructure. After completing the mind map, you would then consider which areas fit your interests, passions, and skills. From this point, you could identify the type of venture you want to create and the necessary actions to move forward with your idea. Using these types of tools assists in identifying actions that need to be addressed in your action plan.

Figure 2.26 From this mind map of disasters that occur and actions to take, we could focus on one action area that matches our interests, passions and skills. After selecting an area of interest, we could create another mind map focused on our area of interest to identify solution sets. Next, we could apply one of the frameworks listed in Table 2.3. From there we could create an action plan of actions needed to become more informed about the idea or solutions. As you can see, an action plan fits into multiple areas. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Types of Entrepreneurs

Recall from The Entrepreneurial Perspective that for some people, the entrepreneurial pathway is clear cut and logical. For example, a career in a biomedical lab may involve research and clinical trials that lead to patent applications for a product to sell in the marketplace, leading to a new venture. Others experience the entrepreneurial pathway through nontraditional methods, as when an unexpected opportunity arises. As the global marketplace continues to evolve, new entrepreneurial opportunities will open for individuals who are open to opportunities that build on creativity and innovation.

Traditional entrepreneurs were perceived as individuals who did not fit in a typical organizational structure or as people who had the brains, creativity, imagination, and money to launch out on their own. However, this perception is changing with increasing support to reduce barriers to enable access to entrepreneurship for all demographic groups. According to a 2018 Capitol Hill discussion on women, minorities, and entrepreneurship, the current entrepreneurial demographics show that only 12 percent of US innovators are women and that US-born minorities accounted for 8 percent, with African Americans making up only one-half of 1 percent of this group.[44] According to a National Academies of Sciences report, as cited in the same Capitol Hill discussion, women- and minority-owned small businesses received less than 16 percent of all Small Business Innovation Research (SBIT) program awards. Even though women account for 51 percent of the US population and own 29 percent of businesses, they received only 6 percent of SBIT awards.

Also cited at the Capitol Hill briefing, a 2015 report by the US Department of Commerce showed that women-owned small businesses have a 21 percent lower rate of winning federal contracts. One result from this Capitol Hill briefing was the passage of the Promoting Women in Entrepreneurship Act to require the National Science Foundation to encourage entrepreneurial programs to recruit and support women in commercial activities

44 Information Technology & Innovation Foundation. "Promoting diversity in entrepreneurship." 2018. https://itif.org/events/2018/03/07/promoting-diversity-entrepreneurship

rather than purely laboratory-based activities. Some of the challenges identified in this discussion for groups other than the traditional entrepreneurs described include life choices such as childbearing, access to funding, and lack of support and follow-through to support women and minorities in their interests related to potential entrepreneurial activities.

Other findings drawn from the Census Bureau data and reported by the Kauffman Foundation found that over 70 percent of Asian, Hispanic, and African American entrepreneurs relied on personal and family savings as their main source of startup capital. Women also face challenges in funding, receiving just 2.2 percent of venture capital funding in 2018.[45] A bill called the Support Startup Businesses Act, reintroduced in the US Senate in 2019, would address these challenges by increasing overall funding to help startups, creating more flexibility in funding, and expanding services for startups.[46] The panelists ended the Capitol Hill discussion by noting that "bro culture" has proliferated at the expense of women- and minority-based entrepreneurial ideas. Cultural barriers, including historical disenfranchisement of women, minorities, and immigrants, arise from biases, with one speaker noting that investors ask more difficult and probing questions of male entrepreneurs but pose more skeptical questions to women.

Today, opportunities have expanded for businesses and organizations that respond to current challenges, which may include trying to improve a negative situation or finding a need in a positive situation, with an increasing awareness of the benefits provided through entrepreneurial activities. As more global, cultural, and economic issues and opportunities arise, more individuals will explore entrepreneurship as a response to these challenges. For example, noting the challenges that women and minorities face in starting a new venture, Alan Donegan and his team train people on how to turn their entrepreneurial visions into a reality through his PopUp Business School. The point is that opportunities should be available to everyone, as long as we keep an open mind when considering how change contributes to new venture creation.

WHAT CAN YOU DO?

Barriers to Funding

Given this list of cultural factors and economic factors, what can you do to assist in solving the challenges related to biases? Consider how Alan Donegan's responded to the need to educate people on how to start their own business. He created a company to address this need. You may also consider reading statistical information such as census data and news reports to identify unique target markets and potential needs that could result in a new venture.

The Kauffman Foundation reports these issues, summarized in Table 2.5.

Potential Barriers to Entrepreneurial Funding[47]

Table 2.5

45 Emma Hinchliffe. "Funding for Female Founders Stalled at 2.2% of VC Dollars in 2018. *Fortune*. January 28, 2019. https://fortune.com/2019/01/28/funding-female-founders-2018/

46 Jason Rittenberg. "Startup Act Reintroduced Innovation Support." *State Science & Technology Institute (SSTI)*. January 31, 2019. https://ssti.org/blog/startup-act-reintroduced-would-expand-federal-innovation-support

47 Ewing Marion Kauffman Foundation. *Access to Capital for Entrepreneurs: Removing Barriers*. April 2019. https://www.kauffman.org/-/media/kauffman_org/entrepreneurship-landing-page/capital-access/capitalreport_042519.pdf

Potential Barrier	Challenges
Geographical barriers	Close to 80 percent of about $21.1 billion in venture-capital funding in the first quarter of 2018 was disbursed in five regional clusters—San Francisco (North Bay Area), Silicon Valley (South Bay Area), New England, New York City metro, and LA/ Orange County—with slightly more than 44 percent in the North and South Bay Areas.
Gender bias	Women are substantially less likely to start businesses than men. In 1996, the rate of new entrepreneurs for women was 260 per 100,000 people, compared to 380 per 100,000 for men. In 2017, the rate of new entrepreneurs for women was 270 per 100,000, compared to 400 per 100,000 for men. This reflects new entrepreneurs, regardless of incorporation or employer status.
Racial and ethnic bias	The landscape of entrepreneurship in the United States is marked by significant differences across racial and ethnic groups. Minority-owned firms are found to face significant barriers to capital. For example, minority-owned firms are disproportionately denied when they need and apply for additional credit. One study compared sources of finance and found that new businesses owned by Black people start with almost three times less in terms of overall capital than new businesses owned by White people, and that this gap does not close as firms mature.
Lack of initial wealth	Low-income individuals without initial (pre-existing) wealth also face significant barriers to capital. Research on liquidity constraints showed that the top ninety-fifth percentile of wealthy individuals in the United States is more likely to start businesses than other income groups, and that personal and household wealth are important drivers of entry. Research at the neighborhood level found that in New York City, the richer third of neighborhoods had more than twice the rate of self-employment than the poorest third. A higher household net worth of a founder is linked to larger amounts of external funding received, even after accounting for human capital, venture characteristics, and demand for funds.
Shift in the banking industry	Large banks have become larger, while there are fewer small and medium-size banks. Larger banks survived the Great Recession with balance sheets restored, while small banks—the ones more likely to lend to entrepreneurs—were limited by both economic conditions and new regulatory barriers
Information asymmetry	The persistence of information asymmetry in capital markets between the supply of capital (investors) and the demand for capital (entrepreneurs) gives rise to barriers faced by entrepreneurs. Entrepreneurs face a larger challenge than established businesses in accessing capital because established businesses can leverage their longer track records and existing relationships.

Table 2.5

- What challenges do you face in these areas?
- What steps might you take to help mediate those challenges?

As the traditional view of entrepreneurship evolves, different types of entrepreneurship are emerging and are worth noting as you contemplate your entrepreneurial journey. The types presented here are among the most common today, each with its own unique opportunities and challenges.

- College Entrepreneur: As the cost of higher education continues to rise, more college students are seeking ways to reduce reliance on tuition loans by launching a venture. The college entrepreneur might launch an enterprise while attending or after graduating from college. Entrepreneurship courses might require a student to create and launch a venture as part of the curriculum, and this can turn into an actual earnings opportunity.
- Corporate Intrapreneur: If you work for a progressive company that seeks innovative solutions for growth and opportunities, you can become an intrapreneur by organizing the necessary resources to pursue a venture of organizational interest.
- Franchise Entrepreneur: Since a franchise grants a license to an entrepreneur to trade under the franchise's name, a franchise entrepreneur gains a head start in an industry by launching the franchise.
- Immigrant Entrepreneur: With increasing global unrest, more immigrants are traveling to new countries. In the United States, ethnic communities of immigrants welcome their compatriots and assist them in becoming independent through entrepreneurship. These communities pool together the necessary resources to support the new immigrant until the business is self-sustaining.
- Internet Entrepreneur: As access to technology and its related platforms increases, so do opportunities for Internet-based businesses. Internet entrepreneurs utilize social media platforms, smartphones and tablets, applications (apps), and any other form of accessible technology as their product or venture. The critical structure for these ventures is the inclusion of an e-commerce or online payment processing capability.
- Woman or Minority Entrepreneur: Women have a unique perspective and potential to capitalize on new or already existing niches in many entrepreneurial fields. Many cultural groups, such as Haitians, Cubans, or Jamaicans, also have unique marketplace skills and demands.
- Part-time Entrepreneur: In response to economic downturns, underemployment, and unemployment, more individuals are supplementing income through part-time activities, casually referred to as "side hustles." These individuals may launch businesses through multilevel marketing firms, such as Avon, Mary Kay, Stella & Dot, and others. This category may also include self-employed freelancers. Examples include writers, graphic designers, artists, web developers, and massage therapists.
- Social Entrepreneur: Some entrepreneurs are driven to offer innovative solutions to existing and emerging social problems, such as poverty, hunger, human trafficking, and environmental degradation. Most social enterprises are structured as nonprofit entities. However, increased interest in for-profit entities that marry business and social goals has given rise to a subcategory has emerged known as a B-corp (see Business Structures Options: Legal, Tax, and Risk Issues), or benefits corporation. The B-corp designation is a voluntary certification that is managed by the nonprofit group B Lab to ensure that corporations adhere to specific guidelines, rules, and accountability.

Key Terms

action plan organized, step-by-step outline or guide that pulls together the ideas, thoughts, and key steps necessary to help set the stage for entrepreneurial success

benchmarking comparing one's own company's performance with an industry average, a leader within the industry, or a market segment

bootstrapping funding strategy that seeks to optimize use of personal funds and other creative strategies (such as bartering) to minimize cash outflows

breakeven point level of operations that results in exactly enough revenue to cover costs

business model plan for how venture will be funded; how the venture creates value for its stakeholders, including customers; how the venture's offerings are made and distributed to the end users; and the how income will be generated through this process

capitalism system in which individuals, people, and companies have the freedom to make decisions and own property as well as benefit from their own efforts, with government playing a secondary role in oversight

cash flow money collected by the business through revenue and funding versus money disbursed by the business through expenses

cash management management of cash inflows and outflows to support cash needs of the venture

corporate entrepreneurship development of new ideas, opportunities, or ventures through formal research and development processes that focused on the corporation's strategy and goals

creative destruction theory developed by Joseph Schumpeter stating that entrepreneurial innovation is the disruptive force that creates and sustains economic growth, though in the process, it destroys established companies and disrupts employment

due diligence conducting the necessary research and investigation to make informed decisions that minimize risk

e-commerce electronic transactions, particularly over the Internet, for the exchange of goods and services

entrepreneurial journey your exploration to discover if entrepreneurship is right for you

entrepreneurial process set of decisions or actions that can be outlined and followed as a guide to developing or adjusting a venture

entrepreneurial spirit describes a quality of those individuals who are productive self-starters focused on making changes happen

entrepreneurial venture any business, organization, project, or operation of interest that includes a level of risk in acting on an opportunity that has not previously been established

framework structure or outlined process that can be used to accomplish entrepreneurial goals through problem solving, idea generation and validation, and brainstorming

franchising form of licensing that allows the business (franchisor) to share its business model to expand through various distributors (franchisees) for a fee

independent contractor (also, freelancer) people or businesses that provide work similar to an employee without being part of the payroll for the contracting business, and who pay their own taxes and pay for their own benefits

innovation new idea, process, or product, or a change to an existing product or process

intrapreneur employee who acts as an entrepreneur within an organization, rather than going solo

milestone significant decision point or significant accomplishment

patent legal grant of protection for an inventor over the rights, usage, and commercialization of an invention for a set time period

serial entrepreneur entrepreneur who becomes involved in starting multiple entrepreneurial ventures

situational opportunity one that becomes available, depending on factors such as where you work, your family obligations, your idea or invention, your unique creative expression, or a recent career search or job change

soft launch (also, soft open) launching a venture for a limited time frame or audience to gain experience, insights, and feedback about the target market or consumer

target market specific group of consumers for which a company seeks to provide a good or service
venture startup company or organization that conducts business or is created to satisfy a need
vertical integration strategy of gaining control over suppliers of raw materials and distributors of finished products to expand or control the relevant supply chain

Summary

2.1 Overview of the Entrepreneurial Journey

As you prepare for your journey into entrepreneurship, it is critical to consider the multiple aspects associated with preparing for, experiencing, and completing a journey unique to you. The key is an honest and introspective assessment of how you can make a journey that brings your desired outcomes and results. The seven steps outlined in this section will provide you with a perspective of what you might encounter on your entrepreneurial venture.

2.2 The Process of Becoming an Entrepreneur

The entrepreneurial process provides a flexible guideline for launching a venture with an individualized approach. This process should be a fluid, not static, exercise that adjusts to market needs and demands until you achieve an appropriate fit to reap the rewards of your investment. The material in this section will be covered in greater depth as you progress through the rest of the chapters. For now, gaining a perspective on the entire process provides you with a background understanding of what an entrepreneurial venture involves, from ideation through creating the venture to harvesting the venture with the potential to begin the process all over again with a new idea.

2.3 Entrepreneurial Pathways

Your pathway to entrepreneurship might arise out of necessity, opportunity, or a combination of situations. Being open to the idea of becoming an entrepreneur provides you with the potential to identify a unique opportunity that fits your interests and goals. Entrepreneurs learn to recognize when an opportunity presents itself and how and when it fits with their goals and dreams.

2.4 Frameworks to Inform Your Entrepreneurial Path

You can connect your background, training, and discipline with your entrepreneurial pathway by using frameworks that capture your developmental activities. To achieve your goals, you need some type of plan that outlines the steps you need to take to reach them. Just as there are many types of ventures, there are many versions and types of plans and tools that can assist you in developing the plan that best fits you. As more global issues and opportunities continue to arise, many different types of entrepreneurs have emerged, offering innovative solutions. The diversity of entrepreneurial types provides unique niches for opportunities that might not fit the mainstream or traditional route to entrepreneurial success.

Review Questions

1. Why is interest in entrepreneurship growing among those entering or re-entering the workforce?
2. What is an entrepreneurial mindset?
3. What does the phrase “entrepreneurial venture” refer to?
4. What does the process of “cash management” entail for a business?
5. Why is the entrepreneurial process considered a fluid process rather than a rigid step-by-step guide?
6. What does the term “creative destruction” mean?
7. What is the difference between a corporate entrepreneur and an intrapreneur?

8. What are situational opportunities?
9. What does an entrepreneurial journey entail?
10. Under which circumstances might a person choose to bootstrap a venture?
11. What is an independent contractor?
12. What does the term "framework" mean in terms entrepreneurship?
13. What is an action plan? How is it different from a framework?
14. Why are action plans useful in the development or improvement of a venture?
15. What are the characteristics associated with traditional entrepreneurship?
16. What are some biases that minorities and women face in acquiring funding?

Discussion Questions

1. What does it mean to have an entrepreneurial mindset?
2. Discuss the basis for defining a target market. How does a focus on a target market assist with the development or adjustment of an idea?
3. Explain the importance of being self-reflective and honest before, during, and after starting an entrepreneurial journey.
4. Using the information on the steps for an entrepreneurial journey, give your own example with connections to this section's main concepts.
5. Consider the potential questions that you might ask yourself before you launch a venture. Discuss two or three questions that resonate with you and your personal experiences. Why or how do these questions influence you more than others?
6. Think about yourself within the context of the "nature or nurture," "born or made" argument. How do you feel these perspectives combine in your own potential as an entrepreneur?
7. What are the similarities and differences between the life cycle stages of a person and a venture? How can these two concepts assist you in creating a successful venture?
8. Consider the historical information on entrepreneurship and innovation. How does our current economy, which is based on technology and knowledge, support entrepreneurial activity?
9. Consider the multiple pathways to entrepreneurship. How might your own current situation reflect a potential pathway to entrepreneurship?
10. Is there a difference between a soft launch and a soft open? Why are two different terms used?
11. What are the benefits of a soft launch? What are the negatives of a soft launch?
12. Outline your background and training, and then discuss the importance of connecting your background and training with a potential entrepreneurial pathway.
13. How does creating an action plan help you become a successful entrepreneur?
14. What is the connection between an action plan and a framework? How are they different?
15. Why are more individuals pursuing nontraditional entrepreneurship opportunities?
16. What is the difference between an immigrant entrepreneur and a minority entrepreneur? What are the similarities?

Case Questions

1. Review the story of Sixto Cancel and his journey to developing the social venture Think of Us.
   A. Consider Sixto's entrepreneurial journey and the development of Think of Us. What types of challenges or obstacles do you think he had to overcome to complete his journey?
   B. Discuss some of the advantages and disadvantages related to Sixto Cancel's background and his experiences in developing an organization and board.
   C. Consider how Sixto Cancel developed his organization. Discuss how he followed or skipped any steps of an entrepreneurial journey.
2. Explore the websites of Cratejoy and Prospurly, which are discussed in Entrepreneurship in Action: Prospurly. How did these venture founders follow the entrepreneurial journey?
3. After researching Man Crates, explain how Man Crates has followed the model in Figure 2.20?
4. What additional ideas can you think of for starting your own business, using Man Crates as a source of inspiration?
5. Go back to the Work It Out: Startup Ideas Feature Box. Select either an idea that you've created or an idea listed on either of the websites. Where could you go to gain more information about this idea? This might mean finding a business where you could shadow someone, or perhaps an internship, or research conducted in some other manner.
6. Return to the Work It Out: Startup Ideas Feature Box and revisit the links to business ideas, using the same idea that you identified in question 1. What are five other businesses that could be spinoff ideas from your one new idea?
7. Refer to the case questions in Entrepreneurial Pathways. Select one of the framework tools discussed in this section and apply that framework to your idea.
8. Why did you select this framework over another framework?
9. By applying the framework to your idea, what new information did you learn and what information is lacking, or needs further development?

Suggested Resources

2.1 Overview of the Entrepreneurial Journey

View the YouTube video "The Jitterbug Smart phone" at https://www.youtube.com/watch?v=tRGAL42gWco to see an example of a product endorsement that geared to a specific target market.

Visit the SBA website to learn more about the local organizations that might assist you to launch or manage a venture: https://www.sba.gov/tools/local-assistance

Caron Beesley. "8 Things You Can Do to Be Taken Seriously as a Young Entrepreneur": https://kitsapscore.org/2017/08/26/8-things-you-can-do-to-be-taken-seriously-as-a-young-entrepreneur/

"Surge Cities: These Are the 50 Best Places in America for Starting a Business": https://www.inc.com/surge-cities/best-places-start-business.html

"How I Built a Subscription Business That's Made over 50k in 6 Months": https://www.cratejoy.com/sell/blog/case-study-50k-6-months-subscription-business-2/

National Association of Women Business Owners: https://www.nawbo.org/resources/women-business-owner-statistics

Are you ready to start your entrepreneurial venture? Visit the SBA site and take the Small Business Readiness

Assessment: https://eweb1.sba.gov/cams/training/business_primer/assessment.htm

2.2 The Process of Becoming an Entrepreneur

Are entrepreneurs BORN or MADE? (Lord Sugard #AND Robert Greene): https://www.youtube.com/watch?v=HNHUbrVcpRA

Learn about how Man Crates was created: https://www.mancrates.com

For more information about the Pembina tribe and entrepreneurial behavior: https://www.ndstudies.gov/gr4/frontier-era-north-dakota/part-2-fur-trade-red-river/section-2-red-river-fur-traders

For more information about Dr. Charles Drew: https://nmaahc.si.edu/blog-post/color-blood

For more information about the creation of the cotton gin: https://www.history.com/topics/inventions/cotton-gin-and-eli-whitney

For more information on how to start a business: https://www.pbs.org/newshour/show/this-free-program-trains-people-how-to-start-a-business-but-without-debt

For more information on Global Entrepreneurship: https://www.gemconsortium.org/

Take the Myers Briggs test to discover your personality type: https://www.idrlabs.com/test.php

2.3 Entrepreneurial Pathways

50 Business Ideas for Introverted Entrepreneurs: https://smallbiztrends.com/2016/09/business-ideas-for-introverts.html

2.4 Frameworks to Inform Your Entrepreneurial Path

YouTube Video: Business Model Canvas Explained: https://www.youtube.com/watch?v=QoAOzMTLP5s

The Four Lenses Strategy Framework website: www.4lenses.org

Evernote, a cross-platform app that allows you to create, update, and synch notes: https://evernote.com/about

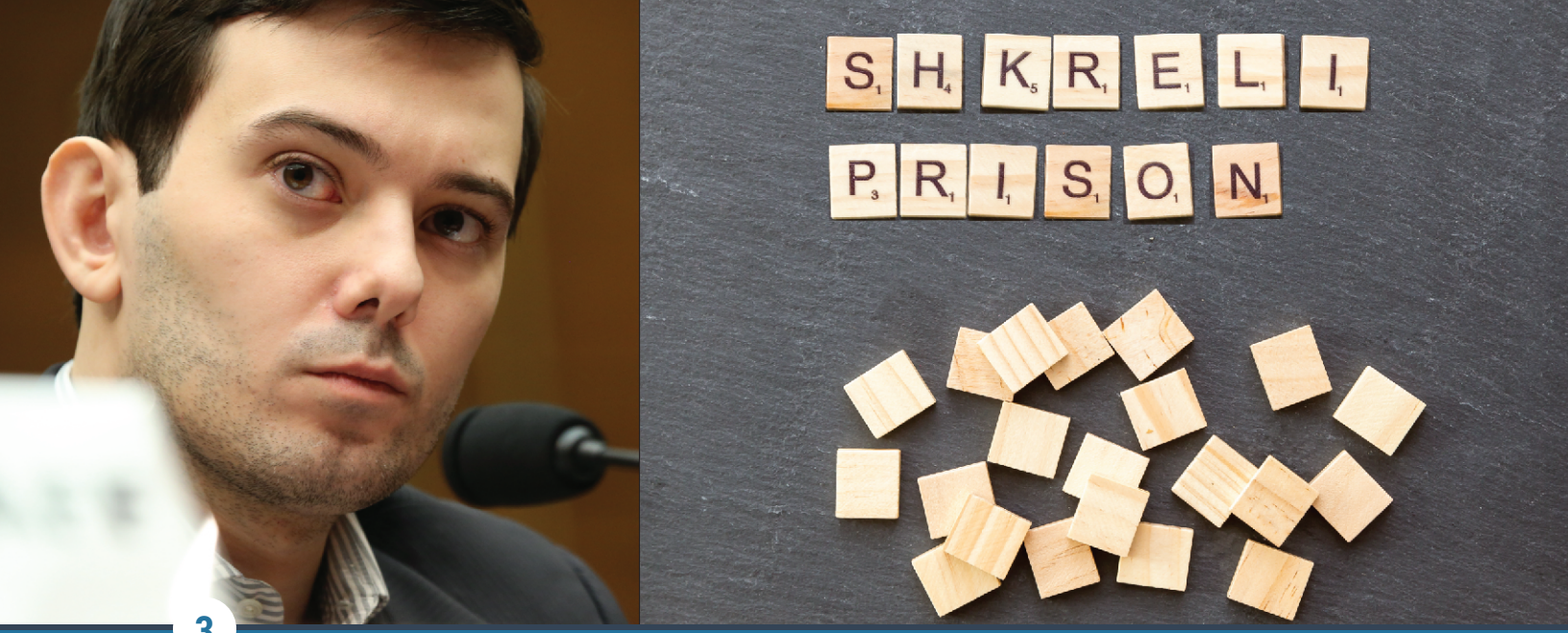
YouTube Video: We have a dream, B-corp overview and mission: https://www.youtube.com/watch?time_continue=3&v=V-VFZUFJwt4

Business Model Canvas Strategyzer: https://www.strategyzer.com/canvas

For more information on the diversity of entrepreneurs in the United States: https://www.entrepreneur.com/article/286574

For more information on entrepreneurship and resource providers supporting entrepreneurship: https://www.kauffman.org/eship-summit-2017/overview#1g

For a list of resources available to support entrepreneurship: https://www.kauffman.org/what-we-do/entrepreneurship/research/data-resources



3

The Ethical and Social Responsibilities of Entrepreneurs

Figure 3.1 Photo of Martin Shkreli (left). Scrabble tiles spelling SHKRELI PRISON (right). (credit (left): modification of "Martin Shkreli 2016" by House Committee on Oversight and Government Reform/Wikimedia Commons, Public Domain; credit (right): modification of "Martin Shkreli sentenced to seven years in prison for defrauding investors" by Marco Verch/Flickr, CC BY 2.0)

Chapter Outline

3.1 Ethical and Legal Issues in Entrepreneurship
3.2 Corporate Social Responsibility and Social Entrepreneurship
3.3 Developing a Workplace Culture of Ethical Excellence and Accountability

Introduction

Martin Shkreli, an aspiring pharmaceutical entrepreneur and former hedge fund manager, made headlines in 2015 when he capitalized on a profitable and controversial business opportunity. As the founder and CEO of Turing Pharmaceuticals, Shkreli obtained the expired patent for a lifesaving drug used to combat HIV. He raised the US market price overnight from $13.50 to $750 per pill—a 5,000 percent increase. When criticism by the medical community, the public, and politicians led to demands for a return to the original pricing, Shkreli defended his decision as a smart business practice that contributed to his firm's bottom line. Eventually, he agreed to reverse the price but later reneged on his promise, offering instead to provide discounted pricing to hospitals.

The damage to Shkreli's reputation, however, was already complete. The BBC described him as the "most-hated" CEO in America due to his business decisions, obnoxious behavior, and negative social media rants.[1] Infectious disease specialists and patient advocates rejected Shkreli's argument that his "price adjustment strategy" was helpful for patients since those being treated would need the drug long after being released from the hospital. Although the pricing strategy was not illegal, Shkreli was eventually investigated and found guilty of securities fraud that involved falsely raising money from hedge fund investors and stealing money from his drug company to repay investors.[2]

1 Zoe Thomas and Tim Swift. "Who Is Martin Shrkeli—'The Most Hated Man in America'?" *BBC News*. August 4, 2017. http://www.bbc.com/news/world-us-canada-34331761
2 Dan Mangan. "'Pharma Bro' Martin Shkreli Found Guilty of 3 of 8 Charges, Including Securities Fraud." *CNBC*. August 4, 2017. https://www.cnbc.com/2017/08/04/pharma-bro-martin-shkreli-convicted-in-federal-fraud-case.html

3.1 Ethical and Legal Issues in Entrepreneurship

Learning Objectives

By the end of this section, you will be able to:

- Develop the ability to identify ethical and legal issues
- Develop an approach to resolve ethical/legal dilemmas once identified

What does it mean to be both ethical and socially responsible as an entrepreneur? When Martin Shkreli decided to increase the price overnight of a lifesaving HIV drug from $13.50 to $750 per pill, the public immediately characterized his actions as unethical. However, he viewed his position as responsible behavior that served the best interests of his company and his shareholders. Although Shkreli's decision to raise prices was within legal limits, his actions were critically judged in the court of public opinion.

As an entrepreneur, should Shkreli's concerns be with ensuring the sustainability of his business or with providing patients with a more affordable (less profitable) lifesaving drug? This fundamental question raises a number of related questions about the ethics of the situation. Was the decision to raise the price of the HIV drug by 5,000 percent in the best interest of the business? Was Shkreli aware of all aspects (ethical, legal, financial, reputational, and political) of the decision he made? To critically examine the decisions of an individual such as Shkreli, one needs an enhanced awareness of the multitude of stakeholders to be considered, as opposed to only shareholders.

Stakeholders

A comprehensive view of business and entrepreneurial ethics requires an understanding of the difference between shareholders, a small group who are the owners (or stockholders), and stakeholders, a large group that includes all those people and organizations with a vested interest in the business. Serving the needs of the shareholders, as perhaps Shkreli thought he was doing, is based on a limited view of organizational purpose. This view, known as the "shareholder primacy" doctrine, stems from a famous Michigan Supreme Court case involving the Ford Motor Company and two shareholders named the Dodge brothers (who would go on to form the Dodge Motor Company).[3] This case established a precedent that lasted for decades, built on the premise that the only thing that should matter to a CEO and their company is shareholder profits. However, this concept has gradually been replaced by a more progressive viewpoint, mandating the consideration of all stakeholders when making key business decisions that have potentially far-reaching consequences. As an example of this new awareness, the Business Roundtable, a group of CEOs from the biggest and most successful companies in the US, recently released a new statement addressing business ethics. The CEOs prefaced this statement saying, "Together with partners in the public, private and non-profit sectors, Business Roundtable CEOs are committed to driving solutions that make a meaningful difference for workers, families, communities and businesses of all sizes."[4]

WORK IT OUT

Business Roundtable Official Statement on the Purpose of a Corporation[5]

Read the following statement on the purpose of a corporation from *Business Roundtable:*

> "Americans deserve an economy that allows each person to succeed through hard work and creativity and to lead a life of meaning and dignity. We believe the free-market system is the best means of generating good jobs, a strong and sustainable economy, innovation, a healthy

3 Dodge v. Ford Motor Company, 204 Mich. 459, 170 N.W. 668 (1919).
4 "Leadership in Action." *Business Roundtable*. https://www.businessroundtable.org/
5 "Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans.'" *Business Roundtable*. August 19, 2019. https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans

environment and economic opportunity for all.

Businesses play a vital role in the economy by creating jobs, fostering innovation and providing essential goods and services. Businesses make and sell consumer products; manufacture equipment and vehicles; support the national defense; grow and produce food; provide healthcare; generate and deliver energy; and offer financial, communications and other services that underpin economic growth.

While each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders. We commit to:

- Delivering value to our customers. We will further the tradition of American companies leading the way in meeting or exceeding customer expectations.
- Investing in our employees. This starts with compensating them fairly and providing important benefits. It also includes supporting them through training and education that help develop new skills for a rapidly changing world. We foster diversity and inclusion, dignity and respect.
- Dealing fairly and ethically with our suppliers. We are dedicated to serving as good partners to the other companies, large and small, that help us meet our missions.
- Supporting the communities in which we work. We respect the people in our communities and protect the environment by embracing sustainable practices across our businesses.
- Generating long-term value for shareholders, who provide the capital that allows companies to invest, grow and innovate. We are committed to transparency and effective engagement with shareholders.

Each of our stakeholders is essential. We commit to deliver value to all of them, for the future success of our companies, our communities and our country."

- Question: Does it appear that Shkreli, in the preceding pharmaceutical example, considered all the stakeholders as the Business Roundtable Statement recommends, or did he follow the older shareholder primacy doctrine approach?

The aim of this chapter is twofold: first, to assist entrepreneurs in understanding the significance of ethics and the role that entrepreneurs play in developing an ethical and responsible organization. This includes the ability to recognize and identify both ethical dilemmas and legal issues that might arise. Second, we want to enable entrepreneurs to develop a moral compass that allows them to lead their business organization in a manner consistent with ethical and legal principles. An example of an ethical business organization is one that follows the Statement of Purpose by the *Business Roundtable*. This means creating a business environment in which each member of the organization is encouraged, enabled, and supported to develop the ethical capabilities to habitually and systematically differentiate between right or wrong. This also means that the organization, as a total system, provides consistent, meaningful, and timely consequences for unethical behavior and irresponsible actions.

LINK TO LEARNING

Read this article from *Forbes* to see a list of companies recently deemed the most ethical (https://openstax.org/l/52MostEthical) in the world.

Being an Ethical Entrepreneur

Whenever you think about the behavior you expect of yourself, in both your professional and personal life, you are engaging in a philosophical dialogue with yourself to establish the standards of behavior you choose to

uphold—that is, your **ethics**. You may decide you should always tell the truth to family, friends, customers, clients, and stakeholders, and if that is not possible, you should have very good reasons why you cannot. You may also choose never to defraud or mislead your business partners. You may decide, as well, that while you are pursuing profit in your business, you will not require that all the money earned comes your way. Instead, there might be sufficient profits to distribute a portion of them to other stakeholders in addition to yourself—for example, those who are important because they have helped you or are affected one way or another by your business. This group of stakeholders might include employees (profit sharing), shareholders (dividends), the local community (time), and social causes or charities (donations).

Being successful as an entrepreneur may therefore consist of much more than simply making money and growing a venture. Success may also mean treating employees, customers, and the community at large with honesty and respect. Success may come from the sense of pride felt when engaging in honest transactions—not just because the law demands it, but because we demand it of ourselves. Success may lie in knowing the profit we make does not come from shortchanging others. Thus, **business ethics** guides the conduct by which entrepreneurs and their companies abide by the law and respect the rights of their stakeholders, particularly their customers, clients, employees, and the surrounding community and environment.

LINK TO LEARNING

Read the Ten Principles of the United Nations Global Compact (https://openstax.org/l/52TenPrinciples) that urges corporations to develop a "principled approach to doing business." The principles cover human rights, labor, the environment, and corruption.

Nearly all systems of moral, ethical, spiritual, and/or religious beliefs stress the building blocks of engaging others with respect, empathy, and honesty. These foundational beliefs, in turn, prepare us for the codes of ethical behavior that serve as ideal guides for business. Still, we need not subscribe to any particular faith to hold that ethical behavior in business is necessary. Just by virtue of being human, we all share obligations to one another, and principal among these is the requirement that we treat others with fairness and dignity, including in our commercial transactions.

For this reason, we use the words *ethics* and *morals* interchangeably in our discussion. We hold that "an ethical person" conveys the same sense as "a moral person." Ethical conduct by entrepreneurs/business owners is not only the right way to behave, but it also burnishes our own professional reputation as business leaders of integrity.

Integrity—that is, unity between what we say and what we do—is a highly valued trait. But it is more than just consistency of character. Acting with **integrity** means we adhere strongly to a system of ethical values. Such values often serve as the foundation for the creation of ethical codes, or codes of conduct. A code of ethics acts to guide conduct and may be derived from a variety of sources. It could be a personal, internal code of conduct, or an official code adopted by a business organization. Or it could be an external code based on one's profession (e.g., CPAs, attorneys, CFPs, and others have professional codes of ethics), or a more broadly applicable external code such as that of the Business Roundtable or Business for Social Responsibility. Being a professional of integrity means consistently striving to be the best person and professional that you can be in all your interactions with others. Integrity in business brings many advantages, not the least of which is that it is a critical factor in allowing businesses and society to function properly. It is also a fundamental basis for developing and maintaining trust, which is vital to all contractual and informal commitments between businesses and all their key stakeholders.

Successful entrepreneurs and the companies they represent will take pride in their enterprise if they engage in business with transparency, intentionality, and integrity. To treat customers, clients, employees, and all those

affected by a venture with dignity and respect is ethical. In addition, ethical business practices serve the long-term interests of businesses because customers, clients, employees, and society at large will be much more willing to patronize a business and work hard on the business's behalf if that business is perceived as caring about the community it serves. And what type of firm has long-term customers and employees? One whose track record gives evidence of honest business practices.

Research on the performance of the World's Most Ethical Companies (WMEC) indicates a positive association between ethical conduct and successful long-term financial performance. These businesses often outperform their market expectations, both in periods of market growth and decline. The WMEC list of companies shows an average annual excess return of more than 8 percent higher than expected profitability. This may be due to a variety of reasons, including what researchers term a positive effect on business culture, stakeholders, and reputation.[6] In other words, being ethical beneficially influences employees, investors, and customers.

ARE YOU READY?

Which Corporate Culture Do You Value?

Imagine that upon graduation, you have the good fortune to face two entrepreneurial opportunities. The first is with a startup known to value a hard-nosed, no-nonsense business culture in which keeping long hours and working intensely are highly valued. At the end of each year, the company plans to donate to numerous social and environmental causes. The second entrepreneurial opportunity is with a nonprofit recognized for a very different culture based on its compassionate approach to employee work-life balance. It also offers the chance to pursue your own professional interests or volunteerism during a portion of every workday. The earnings plan with the first opportunity pays 20 percent more per year.

- Which of these opportunities would you pursue and why?
- In what ways might company contributions to a cause carry more power to impact the cause? In what ways might individual contributions be more powerful? Think of examples for each scenario.
- How important an attribute is income, and at what point would a higher income override for you the nonmonetary benefits of the lower-compensated opportunity?

Many people confuse ethical and legal compliance. However, these concepts are not interchangeable and call for different standards of behavior. The law is needed to establish and maintain a functioning society. Without it, our society would be in chaos. Compliance with legal standards is mandatory. If we violate these standards, we are subject to punishment as established by the law. Therefore, compliance generally refers to the extent to which a company conducts its business operations in accordance with applicable regulations, statutes, and laws. Yet this represents only a baseline minimum. Ethical observance builds on this baseline and reveals the principles of an individual business leader or a specific organization. Ethical acts are generally considered voluntary and personal—often based on our individual perception of what is right and wrong.

Some professions, such as medicine and the law, have traditional and established codes of ethics. The Hippocratic Oath, for example, is embraced by most professionals in healthcare today as an appropriate standard always owed to patients by physicians, nurses, and others in the field. This obligation traces its lineage to ancient Greece and the physician Hippocrates. Businesses are different in not having a mutually shared standard of ethics. This is changing, however, as evidenced by the array of codes of conduct and mission statements many companies have adopted over the past century. These beliefs have many points in common, and their shared content may eventually produce a code universally claimed by business practitioners. What central point might constitute such a code? Essentially, a commitment to treat with honesty and integrity customers, clients, employees, and others affiliated with a business.

6 Nelson Areal and Ana Carvalho. "The World's Most Ethical Companies: Does the Fame Translate into Gain?" Presented to the European Financial Management Association (EMFA). n.d. https://efmaefm.org/0efmameetings/efma%20annual%20meetings/2012-Barcelona/papers/EFMA2012_0401_fullpaper.pdf

The law is typically indebted to tradition and precedent, and compelling reasons are needed to support any change. Ethical reasoning often is more topical and reflects the changes in consciousness that individuals and society undergo. Often, ethical thought precedes and sets the stage for changes in the law.

Behaving ethically requires that we meet the mandatory standards of the law, but that is not enough. For example, an action may be legal that we personally consider unacceptable (consider how many viewed Shkreli's legal price hike). Entrepreneurs today need to focus not only on complying with the letter of the law but also on going above and beyond that basic mandatory requirement to consider their stakeholders and do what is right.

WORK IT OUT

The Equifax Data Breach

In 2017, from mid-May to July, hackers gained unauthorized access to servers used by Equifax, a major credit reporting agency, and accessed the personal information of nearly one-half of the US population.[7] Equifax executives sold off nearly $2 million of company stock they owned after finding out about the hack in late July, weeks before it was publicly announced on September 7, 2017, in potential violation of insider trading rules. The company's shares fell nearly 14 percent after the announcement, but few expect Equifax managers to be held liable for their mistakes, face any regulatory discipline, or pay any penalties for profiting from their actions. To make amends to customers and clients in the aftermath of the hack, the company offered free credit monitoring and identity-theft protection. On September 15, 2017, the company's chief information officer and chief of security retired. On September 26, 2017, the CEO resigned, days before he was to testify before Congress about the breach. Numerous government investigations and hundreds of private lawsuits have been filed as a result of the hack. Equifax will pay at least $650 million, with the possibility of more, to resolve most claims stemming from the data breach. The settlement covers 147 million consumers, just under one-half of the population of the United States.[8]

- Which elements of this case might involve issues of legal compliance? Which elements illustrate acting legally but not ethically? What would acting ethically and with personal integrity in this situation look like?

To return to the case of Martin Shkreli, let's examine it through some foundational theoretical lenses, based on ethical theories. Normative theories of ethics are primarily concerned with establishing standards or criteria that delineate what is considered ethical behavior. Common examples of normative ethical theories are utilitarianism, duty-based ethics (also known as Kantian ethics and/or deontology), and virtue ethics. These ethical theories, discussed in the following paragraph, provide a systematic means of examining and evaluating business conduct.

From an ethical theory perspective, Kantian or duty-based ethics emphasizes the underlying intent or reason behind a decision and whether that decision is good or bad. For example, if the decision to raise the price of a lifesaving drug by 5,000 percent is moral and if it is intended to add value, then an individual is obligated to raise the price. *Utilitarian ethics* focuses on the usefulness or utility of the decision. If the decision to raise the price adds value and usefulness for shareholders, then that decision should be made. The *Protestant work ethic* looks at the decision from the viewpoint of capitalism, free markets, and a sense of duty to ensure maximum return on investment. If the decision deals with a change that is financially sound and beneficial, if there are an adequate number of customers that need and value the HIV product and are willing to pay that

7 Tyler Durden. "Massive Data Breach at Equifax: As Many As 143 Million Social Security Numbers Hacked." *Zero Hedge*. September 7, 2017. http://www.zerohedge.com/news/2017-09-07/massive-data-breach-equifax-many-143-million-social-security-numbers-hacked

8 Stacy Cowley. "Equifax to Pay at Least $650 Million in Largest-Ever Data Breach Settlement." *New York Times*. July 22, 2019. https://www.nytimes.com/2019/07/22/business/equifax-settlement.html

price, then that decision should be made. Proponents of *virtue ethics* claim that ethics consists of a series of innate but latent virtues that an individual needs to develop over time. These virtues consist of trust and derivatives of trust such as truthfulness. In this perspective, if the price hike is fair and equitable, if it is responsible to behave in this way, and if it does not cause harm to the society, then the price should be raised.

While it remains with the courts to determine the underlying intent, legal implications, and consequences of Shkreli's decision, evidence from this and other case studies shows that some corporate leaders have not developed ethical capabilities, or they have not internalized a moral compass that enables them to differentiate between right and wrong.

Developing a Moral Compass

A moral compass is a state of mind where an individual has developed the needed capabilities to differentiate between right and wrong, or between just and unjust in challenging circumstances. When individuals are able to act in an ethical manner systematically, habitually, and without struggling to decide how to act or what to do in difficult situations, they have internalized that moral compass. It can be said that these individuals possess a good character, are able to earn trust, and have qualities that are deemed necessary for leadership.

To develop and internalize a moral compass, an entrepreneur and the members of the organization need to continually exercise and develop their ethical "muscles." These ethics-based muscles include qualities such as trust, truthfulness, respect, responsibility, commitment, care, love, and justice. However, as you will learn, an entrepreneur needs to first provide the organizational framework and foundation in which individuals and business units regularly exercise these qualities. This framework and foundation include that everyone receive the right training, be given the opportunity to identify and close gaps in their behavior, receive recognition and incentives that reinforce good ethical behavior, and receive consistent, timely, and substantial consequences when they fail to act responsibly. These and other actions begin to help individuals develop and internalize an ethical compass.

LINK TO LEARNING

A white-collar criminal convicted of fraud, this interview with Mark Faris (https://openstax.org/l/52MarkFaris) shows his admission that greed, arrogance, and ambition were motivating factors in his actions. He also discusses the human ability to rationalize our behavior to justify it to ourselves. Note his proposed solutions: practicing ethical leadership and developing awareness at an individual level via corporate training.

Legal Issues in Entrepreneurship

Unlike working in a large corporate environment with an established structure, entrepreneurs often create and operate a new business venture by their own rules. The pressure to create a new venture, within constraints and limitations, inspires entrepreneurs to find innovative ways to meet potential market demands. At the same time, the challenge to meet these expectations can create temptations and ethical pressures as entrepreneurs make a variety of decisions. Common areas rife with potential legal issues include contracts, torts, employment, intellectual property, conflicts of interest, full disclosure/truthfulness in product or service claims and performance, and antitrust/competition law (Figure 3.2).

Figure 3.2 There are many legal issues facing entrepreneurs, including intellectual property, contracts, antitrust laws, fraud, employment, and torts. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Intellectual Property: Patents, Copyrights, and Trademarks

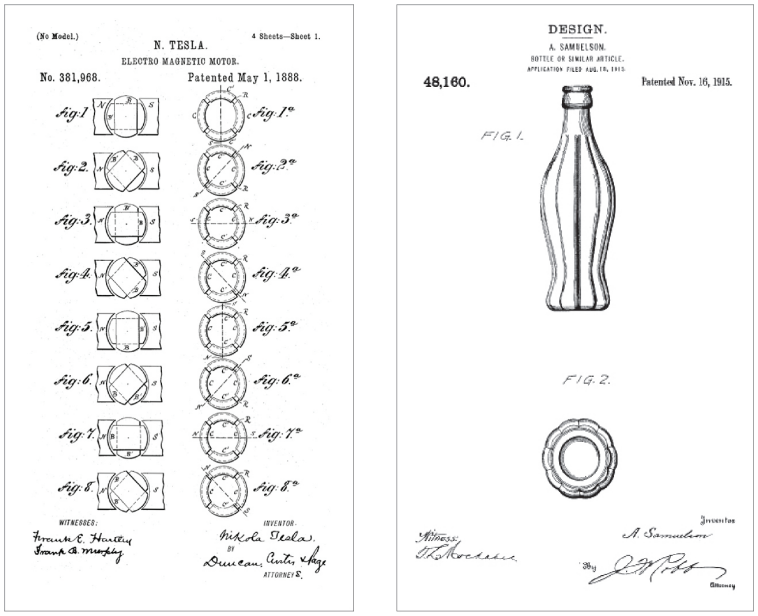
There are multiple reasons why an entrepreneur should be aware of intellectual property rights under the law. For example, if a new startup business comes up with a unique invention, it is important to protect that intellectual property. Without such protection, any competitor can legally, even if not ethically, copy the invention, put their own name or company brand on it, and sell it as if it were their own. That would severely curtail the entrepreneur's ability to make money off a product that they invented. Intellectual property (IP) rights are created by federal law and protect small businesses from problems such as this. IP law also helps establish brand awareness and secure secondary revenue streams.

Intellectual property (IP) is the output or result of the creative work of one or more individuals to turn a unique idea into a practical and value-added product/service; this manifestation of original ideas is legally protected. IP applies to anything that is the exclusive right of a firm, will help differentiate that organization, and will contribute to a sustained competitive advantage. This creative work can result in a product idea, a new invention, an innovative pivot, or an improvement in an existing product or service. IP can take the form of a patent, a copyright, a trademark, or a variation thereof called a trademark secret.

To develop a sustained competitive advantage, an entrepreneur is responsible to protect, provide the needed safeguards, and continually grow a firm's IP. These responsibilities include understanding, differentiating between, and dealing with the different types and technical aspects of a firm's IP. It also means that the entrepreneur should be concerned with the nontechnical aspect of IP, which is to develop a culture of creativity that enables the organization to deliver a continuous stream of new IP.

From a technical aspect, there are two different types of patents: utility and design patents (Figure 3.3). A **utility patent** protects a brand-new product idea or invention under US law for a period of twenty years (see the discussion on patents in Entrepreneurial Journey and Pathways. A few examples of utility patents would be Nikola Tesla's electric magnetic motor, dynamo-electric machine, electrical transmission of power, and his system of electrical distribution patents. A **design patent** protects the ornamental aspects of a product idea.

Examples include the design of a new font, a soft drink bottle, or the design features of Apple's iPhone. In the US, design patents are typically protected for a period of fourteen years.



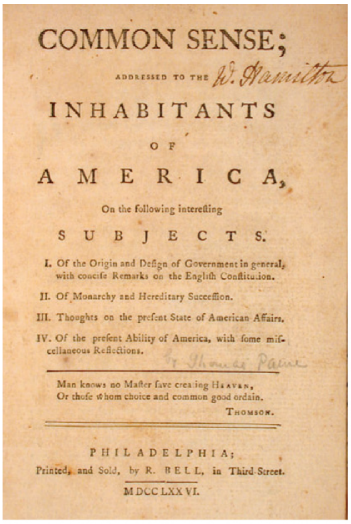
(a) (b)

Figure 3.3 (a) This drawing of Nikola Tesla's alternating-current motor was granted U.S. Patent 381968 and represents a utility patent. (b) The design of the Coca-Cola soft drink bottle was granted a design patent. (credit (a): modification of modification of "US Patent US381968A" by Nikola Tesla/Google Patents, Public Domain; credit (b): modification of "Coke bottle patent" by Unknown/ Wikimedia Commons, Public Domain)

Copyrights and trademarks are also protected IP (Figure 3.4). A **copyright** grants the creator of a work the exclusive right to reproduction of the work for a specified period of time (usually the life of the author plus seventy years). A **trademark** is a registration that provides the owner the ability to use a name, symbol, jingle, or character in conjunction with a specific product or service, and prevents others from using those same symbols to sell their products. A trademark can be protected for an unlimited number of ten-year renewable terms as long as it is still in use. Finally, there is a special category of IP known as a **trade secret**. This concept refers to proprietary information, processes, or other internal knowledge that contribute to an organization's competitive advantage in a market. However, unlike patents, copyrights, and trademarks, a trade secret is not included as a protected category under federal IP law. A trade secret is dependent on being kept a secret by the business that owns it and is enforced through contract law.

Entrepreneurs should pay especially close attention to the legal implications of how patent law can affect a business. Patent laws are strictly enforced and are intended to protect inventions. This protection is afforded because a continuous stream of innovations can be a major source of revenue for a firm as well as a vehicle for developing a sustained competitive advantage. A legal patent gives an exclusive right to its patent holder or proprietor to use the invention in any shape or form they deem necessary. It also gives the patent holder the exclusive right to block or withhold access to others, or to sell the right to use the patent. This period of protection ranges from fourteen to twenty years, and is essentially a government-granted monopoly, after which, protection usually expires and competition is opened up to anyone (e.g., generic drugs).

Regardless of its type, a firm has the exclusive rights to the ownership of its IP. To protect those rights, it is important that a firm meticulously and immediately document each IP, the process and timeline by which each IP was developed, the resources used to develop the IP, the details of who owns and has access to the IP, and how others can obtain and use the IP.


COMMON SENSE;

ADDRESSED TO THE INHABITANTS OF AMERICA,

On the following interesting SUBJECTS.

I. Of the Origin and Design of Government in general, with concise Remarks on the English Constitution.

II. Of Monarchy and Hereditary Succession.

III. Thoughts on the present State of American Affairs.

IV. Of the present Ability of America, with some miscellaneous Reflections.

Man knows no Master save creating HEAVEN,
Or those whom choice and common good ordain.
THOMSON.

PHILADELPHIA;
Printed, and Sold, by R. BELL, in Third-Street.
MDCCLXXVI.

(a) (b)

Figure 3.4 (a) Published texts and artwork are granted a copyright, which will expire over time (usually a long period), as is the case with Thomas Paine's seminal work *Common Sense*. (b) McDonald's iconic golden arches are a trademarked symbol, which usually do not expire unless abandoned. (credit (a): modification of "Commonsense" by Niki K/Wikimedia Commons, Public Domain; credit (b): modification of work by "JeepersMedia"/Flickr, CC BY 2.0)

An entrepreneur should consider these questions when growing and protecting a firm's IP.

- Is IP law relevant to my business, and if so, how can it help me?
- How do we identify what IP to protect?
- What are the steps we need to take to get protection?

Less formally, the development of a culture of creativity and innovation is one of the most important responsibilities of an entrepreneur. This responsibility will enable the entrepreneur to develop a sustained competitive advantage. This means you should not be satisfied with an occasional spark of creativity from a designated individual, department, or functional area within your organization (such as research and development). You need to nurture an environment in which every member of your organization is able to be creative, add value, and be engaged in the continuous improvement of the firm. One example of this dynamic is the culture of continuous improvement at Toyota (Kaizen) (see Launch for Growth to Success). In this culture, every member of the organization is expected to be creative and continually improve the processes they are engaged with on a daily basis.

The story of Nikola Tesla—a Serbian-American inventor, engineer, and physicist—offers a cautionary tale for why entrepreneurs need to be attuned to both the technical aspects of a venture's IP and its culture of creativity. Having filed 300 patents, Tesla is considered by many to be one of the fathers of modern electricity. After immigrating to the United States, Tesla was employed by the Continental Edison Company and began to develop AC technology. However, Edison preferred DC technology and was not supportive of Tesla's ideas. Tesla had to quit, teaming up with Westinghouse to open the Tesla Electric Light company, bringing his valuable creativity and ideas with him to his new venture.[9] Eventually, Tesla's AC became the American standard, not Edison's DC.

Contracts and Torts

Every entrepreneur enters into contracts, usually on a regular basis, and thus should have an understanding of basic contract concepts. Likewise, most businesses are likely to have some involvement with tort law: that area of law that protects the rights of people not to be harmed physically, financially, or in any other way, such as a breach of privacy. Some areas of the business world involve a combination of tort law and contract law, such as litigation involving the wrongful termination of an employee.

9 Nikola Tesla. *My Inventions: The Autobiography of Nikola Tesla*. (Austin: Hart Brothers, 1982).

Contracts can be formal or informal agreements. Ideally, you should use written contracts whenever you enter into a substantial transaction with another party. Oral agreements are enforceable in most situations; however, proving their terms can be difficult. If you are in the midst of a startup, chances are you are moving quickly. Perhaps you don't have the time, or the money, to hire a lawyer to prepare a formal written contract. In that event, you should at least follow-up with all parties via traditional mail or email to document the key terms of your agreement. That way, if a dispute arises, you'll have documentation to fall back on.

Torts are a potential area of risk for entrepreneurs. Financial liability often results from the assumption of and exposure to risk; therefore, this is an important issue for entrepreneurs to manage. This is especially true for the concept of vicarious liability, which is the area of the law that imposes responsibility upon one person for the failure of another, with whom the person has a special relationship (e.g., employer and employee) to exercise reasonable care. Most employers understand they run a risk that their employees may commit a tort, and that they are responsible when employees cause harm to others (customers or coworkers) while on duty, working on company property, and using company equipment. However, many employers are not aware that employers can actually be liable for harm caused by an employee if that employee caused harm within the scope of their job duties. For example, if an employer asks an employee to drop something off at FedEx or UPS after work hours, and that employee negligently causes an auto accident, even if the employee is driving their personal vehicle and not a company car, the employer could be liable for damages. It is an all-too-common situation that could have serious liability consequences for an entrepreneurial business if adequate insurance is not procured.

Antitrust

Antitrust laws (or competition laws) were developed to ensure that one competitor does not abuse its position and power in the market to exclude or limit competitor access to the market. A few examples of antitrust laws are the Sherman Act, the Clayton Act, the Federal Trade Commission Act, and the Bayh-Dole Act. These acts were created to encourage competition and provide options for consumers. In effect, these laws make it illegal for a competitor to make agreements that would limit competition in the market.

The antitrust concept is important to the entrepreneur's ability of entrepreneurs to form new startup businesses that are able to compete with larger, more established corporations (which may try to discourage competition). Table 3.1 summarizes the contributions of these acts to supporting antitrust efforts. It is important to note that any deviation from these laws may result in long and costly legal problems.

Antitrust Acts

Antitrust Act	Protection
Sherman Act (1890)	Prohibits attempts to monopolize
Clayton Act (1914)	Prohibits price fixing, related practices
Federal Trade Commission Act (1914)	Prohibits unfair business practices
Bayh-Dole Act (1980)	Encourages development of inventions

Table 3.1

An example of illegal competition would be the competition and patent war between Intel Corporation and American Micro Devices (AMD). In 2009, AMD filed a suit against Intel claiming that the company had used "leveraging dominance" to exclude AMD from effectively competing in the marketplace through exclusionary pricing, discounts, and similar practices. This claim was later settled by the two firms and resulted in Intel

paying AMD $1.25 billion in damages.

Conflict of Interest

A **conflict of interest** occurs when an individual (or company) has interests in multiple areas (financial investments, work obligations, personal relationships), and the interests may conflict with each other. Employees, for example, have an interest in producing expected work for their employer. A conscious or deliberate attempt to avoid, ignore, or marginalize that which is rightfully due an employer by addressing other interests would be a conflict of interest. This could be as simple as using company time or resources to work on a personal project that has not been sanctioned and will not add value to the company. It could also mean using the tangible and intellectual resources of a company on something that will benefit your private interests instead of your employer's. This action is unethical since you are not giving the employer what they are due, which are your time, talents, and services in exchange for agreed-upon compensation. Consider the example of Mike Arrington, a Silicon Valley lawyer and entrepreneur who created a blog called TechCrunch. Arrington became the go-to source for tech enthusiasts and investors. His coverage of Silicon Valley-based startup companies could help ensure the successful launch of a new business or product. However, he was criticized for routinely covering stories about the companies he invested in and consulted for. Although he provided full disclosures of his interests, rival critics challenged his conflicts of interest. How could he simultaneously be both an investor and an independent journalist blogging about the very companies in which he had a financial interest? He was in a classic conflict of interest position.[10] Similar cases involving business reporters and potential conflicts of interest include *The Wall Street Journal*, *Business Week*, *Time* magazine, and the *L.A. Herald Examiner*.

Another situation in which potential conflicts arise is in the area of professional services, which attracts many young potential business owners. Perhaps you want to start your own CPA accounting firm, or CFP financial advisory firm, or IT consulting firm. A professional must be very cautious about conflicts of interest, especially in areas in which you owe a fiduciary duty to your clients. This requires a very high duty of conduct and full disclosure, one that prohibits being involved in both sides of a transaction. For example, as an IT consultant, do you recommend to a client that they buy a software product, when unknown to them, you own stock in that company? Or as a financial advisor, are you getting commissions on both ends of a transaction?

Fraud: Truthfulness and Full Disclosure

Ethical entrepreneurs consistently strive to apply ethics-based concepts in practice, including truthfulness and full disclosure. These two concepts are not only part of an ethical approach to doing business but are also underlying requirements of several areas of law including fraud. A business that makes/sells a product or service has responsibility for fully disclosing the truth about its products/services.

The underlying facts, reality, and evidence behind something are the **truthfulness** of a matter. An individual who is being truthful is exercising the capability of being factual about a subject matter, dealing with reality, and aware of evidence. Truthful individuals earn a level of credibility and reliability over time because what they say and what they do are in alignment. A corollary of truthfulness is fairness, which means to be impartial, unbiased, and in compliance with rules and standards of right and wrong behavior. **Fairness** deals with doing what is right, just, and equitable. From the standpoint of application, the quality of being truthful forms the foundation for fairness.

Disclosure describes sharing the needed facts and details about a subject in a transparent and truthful way. This information should be adequate, timely, and relevant to allow the recipient to understand the purpose and intent behind a product/service and to make a good decision about the value of that product/service. Any deliberate attempt to hide, change, or bend the truth is an unethical and irresponsible action subject to criminal investigation.

10 Ira Basen. "Why Transparency Is Not Enough: The Case of Mr. Mike." *Center for Journalism Ethics*. University of Wisconsin–Madison. June 21, 2011. https://ethics.journalism.wisc.edu/2011/06/21/why-transparency-is-not-enough-the-case-of-mr-mike/

One example of a firm that has repeatedly run into several serious, embarrassing, and costly legal issues is Eli Lilly. In one instance, this company admitted in court that they had illegally marketed Zyprexa, which was primarily intended and approved by the US Food and Drug Administration office (FDA) to treat depression, to be used for off-label (not cleared by FDA to market and advertise) ailments such as sleep disorders, Alzheimer's disease, and dementia. As a result, in 2009, Eli Lilly was fined $1.4 billion by the office of criminal investigation of the US Department of Justice.[11]

3.2 Corporate Social Responsibility and Social Entrepreneurship

Learning Objectives

By the end of this section, you will be able to:

- Define and describe corporate social responsibility (CSR) and social entrepreneurship
- Identify types of social entrepreneurship ventures, and the key values accompanying them

To understand the role of a socially responsible entrepreneur, it is important to first look at the major tenets of corporate social responsibility (CSR) and the underlying reason why this concept was conceived. Few directives in business can override the core mission of maximizing shareholder wealth, and today, that particularly means increasing quarterly profits. Such an intense focus on one variable over a short time (i.e., a short-term perspective) leads to a short-sighted view of what constitutes business success.

Measuring true profitability, however, requires taking a long-term perspective. We cannot accurately measure success within a quarter of a year; a longer time is often required for a product or service to find its market and gain traction against competitors, or for the effects of a new business policy to be felt. Satisfying consumers' demands, going green, being socially responsible, and acting above and beyond the basic requirements all take time and money. However, the extra cost and effort will result in profits in the long run. If we measure success from this longer perspective, we are more likely to understand the positive effect ethical behavior has on all who are associated with a business.

Corporate Social Responsibility (CSR)

If you truly appreciate the positions of your various stakeholders, you will be well on your way to understanding the concept of **corporate social responsibility** (CSR). CSR is the practice by which a business views itself within a broader context: as a member of society with certain implicit social obligations and environmental considerations and issues. As previously stated, there is a distinct difference between legal compliance and ethical responsibility, and the law does not fully address all ethical dilemmas that businesses face. CSR ensures that a company is engaging in sound ethical practices and policies in accordance with the company's culture and mission, above and beyond any mandatory legal standards. A business that practices CSR cannot have maximizing shareholder wealth as its sole purpose, because this goal would necessarily infringe on the rights of other stakeholders in the broader society. For instance, a mining company that disregards its CSR may infringe on the right of its local community to clean air and water if it pursues only profit. In contrast, CSR places all stakeholders within a broader contextual framework.

An additional perspective of CSR is that ethical business leaders opt to do *good* at the same time that they do *well*. This is a simplistic summation, but it speaks to how CSR plays out within any corporate setting. The idea is that a corporation is entitled to make money, but it should not only make money. It should also be a good civic neighbor and commit itself to the general prospering of society as a whole. It ought to make the communities of which it is part better at the same time that it pursues legitimate profit goals. These ends are not mutually exclusive, and it is possible—indeed, praiseworthy—to strive for both. When a company approaches business in this fashion, it is engaging in a commitment to CSR.

11 Food and Drug Administration. Office of Criminal Investigations of the US Department of Justice. www.usdoj.gov/usao/pae

An interesting example of an entrepreneurial company that is committed to CSR is the New Belgium Brewing Company (NBBC), maker of Fat Tire Beer, among other brands. The NBBC is 100 percent employee owned, which makes this company different from the more traditional corporation in which investors own the company rather than the employees. This type of company with employee ownership means that the workers benefit directly from the profits generated by their efforts for the company, a sort of democratized capitalism. The NBBC is focused on sustainability. It has a brewery in Fort Collins, CO, where the brewery produces almost 20 percent of its own electricity—a large percentage for a commercial factory—through solar panels and wastewater. It makes a corporate commitment to contribute to causes related to sustainability, for example, to bicycle-related organizations supplying people with green personal transportation options. According to the company's director of CSR, the NBBC considers social and environmental well-being to be a high priority of the company.[12]

From a historical perspective, the development of CSR has been somewhat like a rollercoaster ride, characterized by low points with extreme ethical failures (see Table 3.2) followed by high points in which corporate conduct improved, largely as a result of statutory laws and/or agency regulations enacted in response to failures. After such scandals, we also saw a number of voluntary ethics-based ideas begin to find their way into the corporate world, such as CSR and corporate citizenship. While these concepts have provided strategies and tools to strengthen the ethical foundations of businesses, scandals do continue, and new approaches to address them emerge. Ethical failures such as the Michael Milken/Drexel Burnham Lambert scandal, the Enron collapse, and many others, including the recent 2008/2009 mortgage industry/derivatives scandal, led Congress to enact new laws. Examples of statues enacted by the federal government in response to ethical failures include laws such as the Sarbanes-Oxley Act, the Insider Trading and Securities Fraud Enforcement Act, and the Dodd-Frank Act.

In addition to the enactment of statutory reforms, various government agencies have also promulgated new regulations in an attempt to prevent companies from engaging in unethical, illegal, and otherwise damaging activities. Examples of agencies that have created new regulations in response to ethical failures in the business sector include the Securities and Exchange Commission (SEC), the Public Company Accounting Oversight Board (PCAOB), the Consumer Financial Protection Bureau (CFPB), and the Financial Industry Regulatory Authority (FINRA).

The concept of doing what's right ethically, following the law, and giving back to society are closely related concepts (see Table 3.2).

Corporate Social Responsibility, Ethics, and Law

Area of Responsibility	Desired Outcome	Compliance
Legal	Comply with laws/regulations	Required by government
Financial	Profits	Required by shareholders
Ethical	Act fairly/avoid doing harm	Expected by stakeholders
Social/philanthropic	Be a good "corporate citizen"	Desired by society

Table 3.2 Notice which duties, or responsibilities, are mandatory versus discretionary.

Examples of organizations that have experienced ethical lapses causing serious and costly multi-billion-dollar

12 Clodagh O'Brien. "16 Brands Doing Corporate Social Responsibility Successfully." *Digital Marketing Institute*. 2019. https://digitalmarketinginstitute.com/en-us/blog/corporate-16-brands-doing-corporate-social-responsibility-successfully

problems can be seen in Table 3.3. Each has had a profound and far-reaching impact on the lives of individuals, on the communities and society in which they operate, and/or on the global environment. These problems—which have resulted in loss of lives, loss of jobs, property damage, depletion of life savings, and environmental devastation—resulted from issues of quality and ethics.

Examples of Multi-Billion Dollar Corporate Responsibility Problems

Organization	Area of Failure
Chevron Corporation	Amazonian toxic waste disposal disaster
Volkswagen Group	Diesel emissions scandal
Takata Corporation	Defective airbag problems
General Motors	Defective ignition switch problem
Wells Fargo Financial Services	Unethical banking practices
BP P.L.C. (British Petroleum)	Gulf of Mexico oil spill disaster
ENRON Corporation	Illegal accounting practices
Union Carbide India	Bhopal chemical disaster
Pfizer, Elli Lilly	Fraudulent marketing practices
US Corps of Engineers	Hurricane surge protection disaster
Toyota Motor Corporation	Uncontrollable vehicle acceleration
Nike Corporation	Breach of code-of-conduct/labor laws
Intel Corporation	European union antitrust case
Phar-Mor, Inc.	Largest accounting fraud
Bernard L. Madoff Investment Securities, LLC	Madoff Ponzi scheme

Table 3.3

One vulnerability in the corrective measures discussed to address the scandals listed in Table 3.3 is that they do not necessarily prevent the repeat of ethical deviations because they are primarily compliance and fear based. In some instances, instead of preventing unethical activity, the system has enabled unethical leadership to take minimum actions and merely pay fines rather than correct their actions or change their approach.

WORK IT OUT

General Motors' Failure to Consider Stakeholders

General Motors (GM) has struggled with its brands and its image. Over the years, it has jettisoned some of its once-popular brands, including Oldsmobile and Pontiac, sold many others, and climbed back from a 2009 bankruptcy and reorganization. The automaker was hiding an even bigger problem, however: The ignition switch in many of its cars was prone to malfunction, causing injury and even death. The faulty switches caused 124 deaths and 273 injuries, and GM was finally brought to federal court. In 2014, the company reached a settlement for $900 million and recalled 2.6 million cars.

The case exemplifies the tension between the concept that "the only goal of business is to profit, so the only obligation that the business person has is to maximize profit for the owner or the stockholders" on one hand, and the ethical obligations a company owes to its other stakeholders on the other.[13] GM's failure to consider its stakeholders and consumers when choosing not to report the potential for malfunction of the ignition switches led to an ethical breakdown in its operations and cost the company and its customers dearly. In addition, by treating customers as only a means toward an end, the company turned its back on a generation of loyal buyers.

- What virtues and values shared by its long-time customers did GM betray by failing to disclose an inherent danger built into its cars?
- How do you think that betrayal affected the company's brand and the way car buyers felt about the firm? How might it have affected its shareholders' views of GM?

In recent years, many organizations have embraced CSR, in which the company's expected actions include not only producing a reliable product, charging a fair price with fair profit margins, and paying a fair wage to employees, but also caring for the environment and acting on other social concerns. Many corporations work on prosocial endeavors and share that information with their customers and the communities in which they do business. CSR, when conducted in good faith, is beneficial to corporations and their stakeholders. This is especially true for stakeholders that have typically been given low priority and little voice, such as the natural environment and community members who live near corporate sites and manufacturing facilities. CSR in its ideal form focuses managers on demonstrating the social good of their new products and endeavors. It can be framed as a response to the backlash that corporations face for a long track record of harming the environment and communities in their efforts to be more efficient and profitable.

The trend to adopt CSR may represent an opportunity for greater engagement and involvement by groups mostly ignored until now by the wave of corporate economic growth reshaping the industrialized world.

Social Entrepreneurship

Social entrepreneurship describes ventures launched by entrepreneurs who are first and foremost advocates or champions for a social cause. However, they are able to leverage that cause as a platform to develop and maintain an economically viable organization. These individuals are primarily driven and motivated by a higher vision or grander purpose. This new breed of entrepreneur leverages the power of their position, their standing in the community, and the potential synergy and wealth-creation power of an enterprise as a vehicle or platform to advance their social goals and personal agenda. These social causes often include a solution for a costly and chronic social problem or pain, a social wrong or injustice that must be corrected, or a global issue that has been either overlooked or marginalized by society or organizations.

While the primary goal and end-state for a socially responsible entrepreneur is to generate wealth, the

13 Chelsea Bateman. "General Motors: A Recall Nightmare (2014)." *Business Ethics Case Analyses*. November 23, 2015. http://businessethicscases.blogspot.com/2015/11/general-motors-recall-nightmare-2014_23.html

dominant goal for a social entrepreneur is to serve a specific cause as they generate wealth to support that cause. This means a social entrepreneur works to advance society instead of accumulating greater wealth for the shareholder. Social entrepreneurs often share qualities such as a selfless attitude, a sense of obligation and responsibility towards someone or something, a strong commitment to make a change, and a resilience to withstand failure.

There are numerous examples of companies that have embraced the concept of CSR. In fact, some entrepreneurs have created startups based primarily on the idea of giving back, many of whose ventures have become well-known. The list includes, to name a few, TOMS Shoes (discussed in a feature box in this chapter), Bombas Socks, and Warby Parker Eyewear. Each of these companies follows a CSR approach and donates one product for each one purchased, (shoes, socks, glasses). Some companies go the extra mile and become officially certified as B-corporations, which is a CSR-type of designation. (See Business Structure Options: Legal, Tax, and Risk Issues for more discussion of B-corps).

Environmental Entrepreneurship

Similar to social entrepreneurship, **environmental entrepreneurship** advocates for a meaningful and beneficial social cause that is also economically viable. This environmental focus deals with such initiatives that preserve our ecosystem such as clean and renewable energy, waste management, programs to counteract climate change, improved water supplies, protection of biodiversity, and reduction of environmental degradation and deforestation.[14] These initiatives are financially sound from a business standpoint and, at the same time, don't pollute, waste, destroy, and leave a negative environmental footprint.

There are multiple ways in which an entrepreneur can demonstrate a commitment to environmental awareness. One way is to own a company that directly helps clean up the environment, such as Ocean Cleanup, the nonprofit started by a twenty-five-year-old entrepreneur to clean up the Great Pacific Garbage Patch. Another option is to own a traditional private sector company that pledges to operate in an environmentally responsible way, such as Patagonia, committed to responsible sourcing and other initiatives. A third option is to become part of an advocacy organization, an example of which is E2. E2 is "a national, nonpartisan group of business leaders, investors and others who advocate for smart policies that are good for the economy and good for the environment."[15] This group strives to influence policies at the state, regional, and federal levels dealing with energy, climate, oceans, water, transportation, and smart growth. These policies are primarily intended to improve air, water, public health, as well as job creation in these areas. One example of an initiative that has resulted from this group deals with passing the nation's first automobile emissions standards.

In recent decades, corporations have responded to stakeholder concerns about the environment and sustainability. In 1999, Dow Jones began publishing an annual list of companies for which sustainability was important. Sustainability, in this context, is the practice of preserving resources and operating in a way that is ecologically responsible in the long term.[16] The Dow Jones Sustainability Indices "serve as benchmarks for investors who integrate sustainability considerations into their portfolios."[17],[18] There is a growing awareness that human actions can, and do, harm the environment. Destruction of the environment can ultimately lead to reduction of resources, declining business opportunities, and lowered quality of life.

Enlightened entrepreneurs realize that profit is only one positive effect of business operations. Operating a successful business creates opportunities for entrepreneurs to give back to society in responsible ways. In addition to safeguarding the environment, other ethical contributions that entrepreneurs can consider include

14 Thaddeus McEwan. "Ecopreneurship as a Solution to Environmental Problems: Implications for College Level Entrepreneurship Education." *International Journal of Academic Research in Business and Social Sciences* 5, no. 3 (2013): 5. http://hrmars.com/admin/pics/1822.pdf
15 E2. www.e2.org
16 Victoria Knowles. "What's the Difference Between CSR and Sustainability?" *2degrees*. March 25, 2014.
17 "Dow Jones Sustainability Indices." *RobecoSAM*. https://www.robecosam.com/csa/indices/djsi-index-family.html
18 "Results Announced for 2017 Dow Jones Sustainability Indices Review." *Cision: PRNewswire*. September 7, 2017. https://www.prnewswire.com/news-releases/results-announced-for-2017-dow-jones-sustainability-indices-review-300515107.html

establishing schools and health clinics in impoverished neighborhoods and endowing worthwhile philanthropies in the communities in which companies have a presence.

During the last few decades, there has been an explosion of studies on how business activities affect our planet. In one study, Tony Juniper points out that population growth, with its accompanying demand for natural resources and the impact of environmental disasters, has had a profound and lasting impact on the planet. Juniper states that we have increased our consumption of natural resources tenfold, increased grain production fourfold, increased freshwater usage fivefold, increased fish capture fourfold, doubled our consumption of earth's renewable production, and increased the concentrations of greenhouse gases in the atmosphere.[19]

In prior sections, we briefly discussed the devastating environmental impact of oil companies such as Texaco and Chevron. When you drill for oil in one of the most biodiverse corners of the world, the Ecuadorian rainforest of the Amazon, and dump 18.5 billion gallons of oil byproducts and waste into the Amazon's rainforest and streams, you are definitely leaving a negative footprint on our planet. If you meticulously study the local wildlife, vegetation, and other natural characteristic of a region before clearing a region to conduct your business (e.g., harvest the trees for lumber, plants for medication, or drill for oil) and then restore the region to its original natural form when done, you are neutralizing your footprint on the planet. However, it you enhance and strengthen the region, open up schools, provide jobs, educate the local population to preserve and strengthen their natural resources, and take other actions to improve the region, you are in fact leaving a positive footprint on the planet. Entrepreneurs should learn the impact made by all aspects of their company, weigh the choices, and consider adopting a policy that does no harm and possibly leaves a positive footprint on the planet.

LINK TO LEARNING

Elon Musk, founder of the electric car manufacturer Tesla and other companies, recently spoke at a global conference held at the Panthéon-Sorbonne University in Paris. Watch this video of Musk explaining the effects of carbon dioxide emissions on climate change (https://openstax.org/l/52MuskEmissions) in clear and simple terms.

Sustainability

Sustainability deals with actions and a way of life that considers the continuity of future generations. It is deeply rooted in doing what is moral/ethical. For example, it is unjust to take actions that benefit the current generation at the detriment of future generations. What this means is that a sustainable entrepreneur is also driven by and is an advocate for a socially responsible approach to owing and running a business, leveraging the economic potential of renewable and readily available resources to add value to the world in which it operates. However, sustainability means more than just environmental awareness. A simple definition of **sustainability** is the ability to be maintained at a certain rate or level. This means not only the environment, but also natural resources, human resources, product supply chains, and multiple related concepts. Thus, as an entrepreneur aware of issues related to sustainability, one would want to consider a wide range of issues. Examples might include the responsible use of electricity or water, or participating in supplier diversity/responsible sourcing programs, or funding worker wellness initiatives. The idea of sustainability, at its root, is to think long term as opposed to short term.

Given the prominence of the sustainable environment movement worldwide, no well-managed business today should be conducted without an awareness of the tenuous balance between the health of the environment and corporate profits. It is quite simply good business practice for executives to be aware that their enterprise's long-term sustainability, and indeed its profitability, depend greatly on their safeguarding the

19 Tony Juniper. *What's Really Happening to Our Planet?: The Facts Simply Explained*. (London: DK/Penguin Random House, 2016).

natural environment. Ignoring this interrelationship between business and the environment not only elicits public condemnation and the attention of lawmakers who listen to their constituents, but it also risks destroying the viability of the companies themselves. Virtually all businesses depend on natural resources in one way or another.

Responsible Entrepreneurs and Social Entrepreneurship Opportunities

The ability to establish a new venture is an exciting opportunity and privilege. To intentionally plan and establish a new venture in a responsible manner promotes the continuation of a better world. Development of a new venture that supports an awareness and sensitivity to immediate and long-term impacts reflects upon the entrepreneur's personal and organizational values and goals.

Some entrepreneurs start businesses with a community project in mind. A community project venture leverages the available power, synergy, talents, capabilities, and resources of the community to add value and change the world in a positive way. This approach uses the creativity, viewpoints, and feelings of community members to innovate and add value to the local area. An example is that of an entrepreneur who started a company with the idea of giving back to the community.

ENTREPRENEUR IN ACTION

The Story of the TOMS Shoes Entrepreneur in His Own Words by Blake Mycoskie

Read Blake Mycoskie's own telling of how he founded TOMS Shoes:

> "In 2006 I took some time off from work to travel to Argentina. I was twenty-nine years old and running my fourth entrepreneurial startup: an online driver's education program for teens. Argentina was one of the countries my sister, Paige, and I had sprinted through in 2002 while we were competing on the CBS reality program The Amazing Race.
>
> I met a woman volunteering on a shoe drive who explained that many kids lacked shoes, even in relatively well-developed countries like Argentina, an absence that didn't just complicate every aspect of their lives—including essentials like attending school and getting water from the local well—but also exposed them to a wide range of diseases. Her organization collected shoes from donors and gave them to kids in need. Their complete dependence on donations meant that they had little control over their supply of shoes.
>
> My first thought was to start my own shoe-based charity, but instead of soliciting shoe donations, I would ask friends and family to donate money to buy the right type of shoes for these children on a regular basis. I have a large family and lots of friends, but it wasn't hard to see that my personal contacts could dry up sooner or later. And then what? These kids needed more than occasional shoe donations from strangers.
>
> Then I began to look for solutions in the world I already knew: business and entrepreneurship. An idea hit me: Why not create a for-profit business to help provide shoes for these children? Why not come up with a solution that guaranteed a constant flow of shoes, not just whenever kind people were able to make a donation?
>
> And for every pair I sell, I'm going to give a pair of new shoes to a child in need. There will be no percentages and no formulas. It was a simple concept: Sell a pair of shoes today, give a pair of shoes tomorrow.
>
> Something about the idea felt so right, even though I had no experience, or even connections, in the shoe business. I did have one thing that came to me almost immediately: a name for my new company. I called it TOMS. I'd been playing around with the phrase "Shoes for a Better Tomorrow,"

> which eventually became "Tomorrow's Shoes," then TOMS. (Now you know why my name is Blake but my shoes are TOMS. It's not about a person. It's about a promise—a better tomorrow.)
>
> I got a break with an article about my new startup, TOMS, in the *LA Times*, it was a headline story. By the end of that day, we'd received 2,200 orders. That was the good news. The bad news was that we had only about 160 pairs of shoes left sitting in my apartment. On the website we had promised everyone four-day delivery. What could we do?
>
> Craigslist to the rescue. I quickly posted an ad for interns and soon I had selected three excellent candidates, who began working with me immediately. We ended up selling 10,000 pairs of shoes that first summer—all out of my Venice apartment."
>
> Blake Mycoskie. "How I Did It: The TOMS Story." *Entrepreneur*. 2011. https://www.entrepreneur.com/article/220350
>
> (This excerpt from *Entrepreneur* magazine was written by Blake Mycoskie in his own words.)

There are multiple types of business entities that function with a social purpose in mind. *Nonprofit* organization entrepreneurs (as well as those starting for-profit companies such as the TOMS story) have the potential to look beyond their own financial gains. These organizations typically partner with federal, state, or local government organizations, public and private institutions, foundations, or individuals with financial means and community standing to serve the greater public. One example of a nonprofit initiative is the National Kidney Foundation of Arizona.[20] This organization seeks solutions for kidney and urinary diseases through education, prevention, and treatment.

A *cooperative venture* leverages the talents, finances, and intellectual resources of the members of an organization to operate and deliver value to the members of the organization. One difference between a cooperative and a nonprofit corporation is how money flows back into the community. In a nonprofit organization, the managers cannot distribute profits to members or investors; the remaining money stays in the nonprofit. In contrast, a cooperative generally can distribute profits to members based on member participation/temporary ownership. One example of a cooperative would be the Unity One Credit Union, which is a member-owned, not-for-profit cooperative, working for its members' benefit.

Two other types of entities that are essentially the same are known as *social enterprises* or *social purpose businesses*. These entities are primarily driven by a meaningful social cause. Social entrepreneurs are able to meet their strategic organizational goals and objectives by delivering a value-added product/service that closes a gap, addresses a problem or pain, or corrects a social injustice. A social enterprise is typically designed to be financially self-sufficient. One example of a social entrepreneur and a social enterprise is the Grameen Bank founded by Muhammed Yunus, a Nobel Peace Prize laureate who defined the term micro-lending and micro-finance. Grameen Bank thrives on giving small loans to those individuals who have very little to no collateral and wish to start a business to support their family.[21]

A social purpose business is often referred to as a B- or benefit Corporation (also discussed in Business Structure Options: Legal, Tax, and Risk Issues). The process of becoming a certified B-corporation is a formal process that involves compliance with various standards and an audit of this compliance (managed by the B-Corp organization).[22] The essence of these new B-corporations is that "they recognize the imperative to do no harm and create positive impact throughout the value chain."[23] According to the B-Corp organization, these certified businesses are legally required to consider the impact of their decisions on their workers, customers, suppliers, community, and the environment. As of 2019, there are approximately 3,000 certified B-corps in 65 countries, covering 150 different industries.[24]

20 National Kidney Foundation of Arizona. www.azkidney.org
21 Muhammad Yunus. *Banker to the Poor: Micro-Lending and the Battle against World Poverty.* New York: PublicAffairs, 2008.

One example of a certified B- (or benefit) corporation is Kickstarter, the crowdfunding website. Kickstarter is one of the world's largest funding communities for creative projects—everything from films, games, restaurants, and music to art, design, and technology—and offers entrepreneurs a way to raise funds when they cannot borrow from a bank.

A *hybrid venture* uses a combined business strategy to enable the organization to deliver profitable and socially valued products and services. The hybrid business model attracts different investors and capitalizes on a variety of investment opportunities, while supporting a mission centered on a socially meaningful cause and grander purpose. One example is Embrace Innovations, a manufacturer of incubators for infants born prematurely, originally established as a nonprofit entity. Embrace, an example of a relationship between academic and business, was started as part of a special course at Stanford University. The Stanford Design for Extreme Affordability Program consists of a course for student teams seeking further support (the Social Entrepreneurship Lab and the Design Lab). This project was launched in 2007, the company was formed in 2008, and the first version of the product launched in 2011. The product is currently being distributed to clinics in India, where dozens of babies have already benefited. Partnerships have been formed with several multinational organizations to distribute the product.[25]

LINK TO LEARNING

Female entrepreneur Stacey Edgar started Global Girlfriend (https://openstax.org/l/52GlobalGirl) on a very small budget and a larger social cause. Through hard work by a team of people, she built a business organization founded on the premise of wanting to have a social impact. The company eventually supported up to 100 different women-led organizations in over thirty countries. Her goal was for the company not only to touch the lives of end customers, but also change the supply chain of retail apparel distribution. It is an example of a successful entrepreneurial startup spreading the message of women's empowerment.

When launching a social enterprise, you need to consider both the technical aspects of launching an enterprise as well as the underlying cause or purpose that has driven you to launch a social enterprise. As you develop your business model, marketing strategy, and other elements to support your venture, it is crucial to ensure your grander purpose remains the foundation of your business planning and decisions.

Identifying Your Values and Mission

The values we choose to honor are the essence of ourselves, and we carry them with us wherever we live, work, and play. As we noted, the entrepreneurial path you choose should reflect your values, whether you create a for-profit or nonprofit organization. It also is possible that you might establish a for-profit company and volunteer extensively on your own or on behalf of your firm in the nonprofit sector. Whatever your entrepreneurial path, it remains important not to let your well-considered values be diminished by others who do not prize loyalty or industriousness, for instance. Entrepreneurship is not a contest in which the person who finishes with the biggest portfolio or fastest jet skis wins anything other than an empty prize. It is far better to treat others with integrity and respect, and be surrounded by the true emblems of a successful career—family, friends, and colleagues who will attest to the dignity with which you have worked. In the final analysis, if you achieve a life of honor, then you have succeeded.

How do you keep personal values like integrity, fairness, and respect close at hand? The best way is by writing them down, prioritizing them, and fashioning them into a personal mission statement. Most companies have

22 Certified B-Corporations. https://bcorporation.net/
23 Network for Business Innovation and Sustainability. "B Corporations, Benefit Corporations, and Social Purpose Corporations: Launching a New Era of Impact-Driven Companies." October 2012. http://nbis.org/wp-content/uploads/2012/10/ImpactDrivenCompanies_NBIS_Whitepaper_Oct2012.pdf
24 Certified B-Corporations. https://bcorporation.net/
25 Design for Extreme Affordability. "Embrace." https://extreme.stanford.edu/projects/embrace/

mission statements, and people can have them, too. Yours will guide you on your path, clear away distractions on the road, and help you correct any missteps. It should be flexible, too, to account for changes in yourself and your goals. Your mission statement is not a global positioning system so much as a compass that guides you toward discovering who you are and what drives you (Figure 3.5).

Figure 3.5 Entrepreneurs should develop a personal mission statement to avoid straying from the path they have set for themselves. A personal mission statement can serve as an ethical/moral compass, guiding an individual through their professional and personal life. (credit: modification of "Adventure Compass Hand Macro" by "Pexels"/Pixabay, CC0)

Let us write your mission statement. Because it will reflect your values, start by identifying a handful of values that matter most to you. You can do this by answering the questions in Table 3.4; you may also find it beneficial to keep a journal and update your answers to these questions regularly. Additionally, the US Department of Labor has a free online self-assessment called the Interest Profiler. The Interest Profiler can help you find out what your interests are and how they relate to the world of work. The Interest Profiler can help you focus on avenues of interest that you might want to explore as an entrepreneur.

LINK TO LEARNING

Click on the O*Net Profiler link (https://openstax.org/l/52ONetProfiler) and take the self-assessment. It's quick, fun, and easy.

Identifying Your Values

1. Of all the values that matter to you (e.g., honesty, integrity, loyalty, fairness, honor, hope), list the five most important.
2. Next, write down where you believe you learned each value (e.g., family, school, sports team, belief community, work).
3. Write a real or potential challenge you may face in living each value. Be as specific as possible.
4. Commit to an action in support of each value. Again, be specific.

Table 3.4

Now you can incorporate these values into your business mission statement, which can take the form of a narrative or action. There are many formats you can follow, but the basic idea is to unite your values with the goals you have set for your life and career. You can, for instance, link the benefit you want to create, the market or audience for which you want to create it, and the outcome you hope to achieve.[26] Keep your statement brief. Richard Branson, founder of the Virgin Group, wants "to have fun in [my] journey through life and learn from [my] mistakes." Denise Morrison, CEO of Campbell Soup, aims "to serve as a leader, live a balanced life, and apply ethical principles to make a significant difference."[27] Your own statement can be as simple as, for instance, "to listen to and inspire others," or "to have a positive influence on everyone I meet."

LINK TO LEARNING

Read this blog, "The Ultimate Guide to Writing Your Own Mission Statement," by Andy Andrews (https://openstax.org/l/52BlogAndrews) for more information about creating a personal mission statement.

Watch the TEDx talk "How to Know Your Life Purpose in Five Minutes" about the self and identifying values (https://openstax.org/l/52TEDpurpose) to learn more.

Putting Your Values and Mission Statement to the Test

There may be no better place to put your personal values and mission to the test than in an entrepreneurial role. Startups cannot be run on concepts alone. More than almost any other kind of venture, they demand practical solutions and efficient methods. Entrepreneurs usually begin by identifying a product or service that is hard to come by in a particular market or that might be abundantly available but is overpriced or unreliable. The overall guiding force that inspires the startup then is the execution of the company's mission, which dictates much of the primary direction for the firm, including the identification of underserved customers, the geographic site for operations, and the partners, suppliers, employees, and financing that help the company get off the ground and then expand. In a brand-new organization, though, where does that mission come from?

The founder or founders of a firm develop the company's mission directly from their own personal beliefs, values, and experience; this is particularly true for nonprofits. Sometimes the inspiration is as simple as the recognition of an unmet need, such as the rising global demand for food. Bertha Jimenez, an immigrant from Ecuador who was studying engineering at New York University, could not help but be concerned that while craft breweries were riding a wave of popularity in her adopted city, they were also throwing away a lot of barley grain that still had nutritional value but that no one could figure out how to reuse it. After a few attempts, Jimenez and two friends, also immigrants, finally hit on the idea of making flour out of this barley grain, and thus was born the Queens, New York–based startup Rise Products, whose website proclaims that "Upcycling is the future of food."

Rise Products supplies local bakers and pasta makers with its protein- and fiber-packed "super" barley flour for use in products from pizza dough to brownies. It has also sent product samples on request to Kellogg, Whole Foods, and Nestlé, as well as to a top chef in Italy. Jimenez and her fellow cofounders say, "In the long term, we can bring this to countries like ours. We want to look at technologies that won't be prohibitive for other people to have."[28]

If we were to diagram the relationship between founders' values and the entrepreneurial mission, it would look something like this:

26 Jessica Stillman. "Here Are the Personal Mission Statements of Musk, Branson, and Oprah (Plus 7 Questions to Write Your Own)." *Inc.*, May 29, 2018. https://www.inc.com/jessica-stillman/how-to-write-your-own-personal-mission-statement-7-questions.html
27 Drew Hendricks. "Personal Mission Statement of 13 CEOs and Lessons You Need to Learn." *Forbes.* November 10, 2014.
28 Larissa Zimberoff. "From Brewery to Bakery: A Flour That Fights Waste." *New York Times.* June 25, 2018. https://www.nytimes.com/2018/06/25/dining/brewery-grain-flour-recycling.html; Rise Products. http://www.riseproducts.co/

personal values → personal mission statement → entrepreneurial mission statement

Just as a personal mission statement can change over time, so can the company mission be adapted to fit changing circumstances, industry developments, and client needs. TOMS Shoes, profiled earlier, is an example of a business that has expanded its mission to also offer eyeglasses and improved access to clean water to people in developing countries, in addition to its original mission of shoes for the needy. It calls itself the "One for One" company, promoting founder Blake Mycoskie's promise that "With every product you purchase, TOMS will help a person in need."[29]

The point is, if you have clarified your personal values and mission statement, there is almost no limit to the number of ways you can apply them to your business goals and decisions to "do good and do well" in your entrepreneurial career. The purpose of business is relationships, and the quality of relationships depends on our acceptance of self and concern for others. These are developed through the virtues of humility on one hand and courage on the other. The demanding but essential task of life is to practice both. In that way—perhaps *only* in that way—can we be truly human and successful business professionals.

3.3 Developing a Workplace Culture of Ethical Excellence and Accountability

Learning Objectives

By the end of this section, you will be able to:

- Describe workplace challenges in an entrepreneurial culture
- Distinguish between reactive and proactive approaches to managing ethics
- Describe the foundations and framework of an organizational culture of ethical excellence
- Define the components of an ethical workplace

Successful entrepreneurs understand that the workplace of 2020 is quite different from that of 2000, just twenty years ago. As the heading to this section suggests, progressive entrepreneurs want to create a workplace culture of ethical excellence. However, doing that means understanding a changing workforce, both in terms of demographics and values. Millennials, born between 1983 and 1995, now outnumber baby boomers in the workforce, and by 2025, will compose three-quarters of all workers on a global basis.[30] Entrepreneurs and managers who are in a position to hire and supervise millennial workers must adjust to the differing expectations and demands of a mid-twenty-first century workplace. This is especially true with regard to CSR/ethics. What matters most to millennials, according to a recent *New York Times* article, is that work aligns with their values.[31]

Approximately 60 percent of millennial workers would agree to work for 15 percent less money just for the chance to work for a company whose business values parallel their personal values.[32] It turns out that millennials don't just want a job, they want a job that matters—one in which they can do rewarding work that achieves a worthwhile outcome. In other words, they want the work they do to mean something. Furthermore, according to an article in the *Texas Bar Journal* by career coach and consultant Martha Newman, millennial workers place a high value on workplace policies that promote open communication, collaboration, and participation in short- and long-term decision making with their employer.[33] Newman also says that millennials expect a degree of work-life balance; career isn't all that matters in their life.

What this means for entrepreneurs who manage employees is that they must adjust. For example, an owner can create a workplace in which there is a culture ensuring that people matter as much as money, where there is work-life balance with things like flexible scheduling, and where good work is recognized and rewarded.

29 TOMS. https://www.toms.com/
30 Deloitte Reports. 2019. https://www2.deloitte.com/global/en/pages/about-deloitte/articles/millennialsurvey.html
31 Elizabeth Olsen. "Graying Firms Wrestle with Making Room for Younger Lawyers." *New York Times.* November 4, 2015. https://www.nytimes.com/2015/11/05/business/dealbook/graying-firms-wrestle-with-making-room-for-younger-lawyers.html
32 Elizabeth Olsen. "Graying Firms Wrestle with Making Room for Younger Lawyers." *New York Times.* November 4, 2015. https://www.nytimes.com/2015/11/05/business/dealbook/graying-firms-wrestle-with-making-room-for-younger-lawyers.html
33 M. Newman, "Decoding Millennial Lawyers," *Texas Bar Journal* 82, no. 8 (2019): 639.

There's an adage that says, "People don't quit their job, they quit their bosses." If you don't want a very high turnover rate among your workforce, be the kind of boss that millennials want to work for and with.

Entrepreneurial Culture

A fairly common characteristic of successful startups is charismatic, driven founders with competitive mentalities. After all, it takes a thick skin and powerful ego to get through the inevitable disappointments that confront a startup leader. Often, however, companies discover that a different leadership ethos is necessary as they grow. Could entrepreneurs still succeed if they also embraced a humanistic leadership style at the outset, or would this invariably undermine the already low initial odds of success? It is a difficult problem with which many firms wrestle. Dedicated employees may be put off by demanding leaders who are harsh, giving little back to loyal workers even after achieving success. New employees may decide the working climate is less congenial than they anticipated and simply leave.

One question an ethical entrepreneur should ask is this: Do my employees feel like they can speak freely? In reality, at many companies, according to SHRM (Society for Human Resource Management), human resources departments often find it difficult to get employees to complete employee workplace climate (satisfaction) surveys.[34] Workers often believe that if management really wants to find out who said what, they easily could, although the surveys are supposed to be anonymous. The difference between ethical and unethical entrepreneurial management is whether they want to find out. Whether it involves small, mid-size, or large companies, management should encourage employees to speak out, whether as an anonymous whistleblower or in person to their supervisor. Absence of this type of encouragement often allows unethical business practices to flourish, such as was seen in the Wells Fargo case example.

LINK TO LEARNING

Although no single set of traits identifies the ideal startup leader, a demanding, driven nature is a fairly common characteristic. Consider these brief profiles of entrepreneurs: first, a profile on Walt Disney (https://openstax.org/l/52WaltDisney) and then video showing a contrasting view from Kerrie Laird (https://openstax.org/l/52KerrieLaird) at Vodafone.

After watching the videos, consider this thought experiment: Suppose the cult of the charismatic—but dogmatic—entrepreneurial leader such as Walt Disney or Steve Jobs were replaced by one steeped in a commitment to employee empowerment that Kerrie Laird claims for Vodafone? Could this change the culture at startups? If it could, do you believe that change would be for the better or worse?

These observations identify what may be unique to entrepreneurial culture. This is a combination of personality and management style often identified with those business leaders who strike out on their own, bring a startup to life, and shape its initial business practices and culture on the job. If the enterprise is successful, the principles and philosophy of the founder become enshrined in the lore of the company, so that long after their departure, succeeding leaders find themselves beholden to the management philosophy exemplified from the early days of the firm.[35] As *you* seek the right leadership style to implement in your entrepreneurial plans, begin by asking precisely what kind of leader you would prefer to work for if you were not the boss. The answer you provide may very well be the best model to follow as you develop your own leadership personality.

The first employees of a startup realize what is at stake as the company tiptoes into new entrepreneurial

34 Dana Wilkie. "Employee Engagement Surveys: Why Do Workers Distrust Them?" Society for Human Resource Management. January 5, 2018. https://www.shrm.org/resourcesandtools/hr-topics/employee-relations/pages/employee-engagement-surveys.aspx

35 Steven Byars. Personal statement. Dr. Byars worked for many years in the 1980s in human resources at the Walt Disney Company at its corporate site in Burbank, California. A popular training course offered in-house to employees new to professional or managerial roles was "Disney Way," in which the leadership culture of the company was traced back to its founding in 1926 and how that culture had remained greatly intact over the intervening years.

waters. The founder may be the boss, but their associates sense a collaborative spirit that directly joins them to the founder as well as to each other. There can be a genuine camaraderie among those who have been with the firm since day one or shortly thereafter. Founding members of an entrepreneurial business are also often willing to undergo the strains and rigors attached to a startup in return for an ownership stake in the company that allows them to profit handsomely from its later growth and success.

Newer staff, however, may not share this mindset. They may simply be seeking a secure position with a growing business rather than a chance to get in on the ground floor of a risky startup. They will not necessarily have the tolerance for the demanding hours, chaos, and abrasive personalities that can characterize the early days of an enterprise. Can entrepreneurial founders shape a company's culture so that it can accommodate talented employees who are looking for a corporate culture that supports some work-life balance?

Consider also the ethical practices of an entrepreneur and the ethical expectations of employees. Suppose that one of the distinguishing features woven into the fabric of the startup is the respect extended to customers or clients. An entrepreneur typically promises always to hold customers in the highest regard, never lie to them, and serve them well. Furthermore, suppose this entrepreneur successfully instills this same ethos among all employees from the outset. Respect for customers is intended to become a distinguishing feature of the business; even if it causes monetary loss to the company, this entrepreneur will neither cheat a client nor misrepresent the company's services. Finally, presume that this ethos is embedded into the culture of the company while it is still in startup mode.

Now suppose the company becomes successful. This may signal the hardest time of all for the entrepreneur. Growth often accompanies success, and growth means, among other things, more employees. Not all these new hires will be as committed to the same degree of responsibility for customers. They will not necessarily set out to cheat clients, but they might lack the founder's enthusiasm for the most honorable treatment of customers. How can an entrepreneur ensure that the initial commitment carries over to the second generation of leadership? He or she cannot simply order it to happen—human nature usually does not respond so easily. So entrepreneurs must do their best to ensure that their version of customer service, one that prioritizes respect for clients, is passed along to new employees. It may be ingrained in the longest-serving employees, but it must be nurtured to the point where it has the same significance for the newest hires.

As a leader, you need to plan and follow-up to ensure your organization follows the values and ethical principles you uphold. This planning process goes beyond taking a few simple actions such as hiring the right people, providing consequences, or setting expectations. It goes beyond communicating a few niceties and encouraging sound bites such as establishing trust and working with uncompromising integrity. It needs more than the application of a few popular concepts and slogans such as CSR, conscious capitalism, or servant leadership. It also needs more than the effective communication of a few success criteria and expectations.

There are effective techniques that can support the infusion of ethical principle into the daily work life of employees. Sometimes known as **anchoring strategies**, ethical values can become part of the business culture through the implementation of employee training, and reward/recognition programs. The Society for Human Resource Management (SHRM) website has a toolkit for entrepreneurs and managers that provides useful ideas on infusion and anchoring strategies.

LINK TO LEARNING

View the toolkit for understanding and developing organizational culture (https://openstax.org/l/52OrgCulToolkit) to learn more.

While the use of popular management approaches can be successful, they can be inadequate to stop unethical behavior. Instead, you need a plan to nurture and develop a culture where ethical qualities and capabilities such as truthfulness, justice, responsibility, and compassion are developed and internalized as a moral

compass. It also demands that these qualities and capabilities are infused into the fabric of organization, adhered to habitually, and are integrated into the organization's daily operations.

Proactive versus Reactive Approaches

Creation of an ethical workplace environment has both reactive and proactive components. The reactive side enables an entrepreneur to identify and address reckless behavior, irresponsible actions, and ethical deviations as they occur. However, there may be times that a reactive approach, which can be heavy-handed, may not be the best approach for addressing ethical deviations.

In contrast, a proactive approach to developing an ethical workplace strives to prevent reckless behavior, irresponsible actions, and ethical deviations by establishing and nurturing a culture of ethics, responsibility, and compliance. It also demands that you establish a workplace environment of ethics where every member of the organization is able to proactively develop, internalize, and apply a moral compass. This approach serves to operationalize popular—but often silent or nebulous—concepts such as truthfulness, fairness, trust, integrity, commitment, innovation, and excellence, leading to a sustained competitive advantage.

Developing the Foundation and Framework of an Ethically Responsible Organization

An entrepreneur must build a foundation for developing an organization grounded in ethics and responsibility. Foundational building blocks enable an entrepreneur to systematically add the greatest value to society, and to do so responsibly. Additionally, for entrepreneurs modifying their businesses or taking over new ventures, building a foundation of ethical conduct should neither disrupt normal business operations nor add significant overhead, since the main concepts are infused into the fabric of the organization.

To develop an organization's foundation for ethics and a framework for management, an entrepreneur needs to incorporate three essential ethical qualities—trust, fairness, and excellence—into the organization's core values (see Figure 3.6). Additional ethical qualities, dependent on the enterprise's specific goals, might include responsibility, commitment, compassion, and so on. The entrepreneur should infuse these qualities into all aspects of organizational governance and daily operations, and track these values to ensure they are being integrated into planning, and are met and enforced by all business units.[36],[37],[38] The application and implementation of these three core qualities will begin to shape the framework and establish a foundation of ethics and responsibility.

Figure 3.6 illustrates and approach to building a foundation for ethics-based behaviors, principles, and effective collaboration.

36 Mehran Ferdowsian. "Total Business Excellence—A New Management Model for Operationalizing Excellence," *International Journal of Quality & Reliability Management* 33, no. 7 (2016): 942–984. https://doi.org/10.1108/IJQRM-08-2014-0109
37 Thomas A. Hemphill and Waheeda Lillevik. "The Global Economic Ethics Manifesto: Implementing a Moral Values Foundation in the Multinational Enterprise." *Journal of Business Ethics* 101, no. 2 (2011): 213–230. doi: 10.1007/s10551-010-0718-4.
38 Hans Küng. "The Global Economic Crisis Requires a Global Ethic: The Manifesto for a Global Ethics." Symposium on the Global Economic Ethics, United Nations Headquarters, New York, NY. October 6, 2009. https://www.bbvaopenmind.com/en/articles/the-global-economic-crisis-requires-a-global-ethic/

Figure 3.6 Ethical entrepreneurs/managers have these foundational qualities. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Second, the organization should consider what ethical principles it wants to prioritize. Examples of ethical principles might include:

- Service and advancement of society
- Collaborative excellence
- Gender equity
- Elimination of prejudices

Once the framework and foundation for an ethical and high-performing organization has been established, other qualities and principles can easily be integrated as needed to further strengthen this framework, differentiate the organization, and develop a sustained competitive advantage. It also enables leadership to align other aspects of organizational governance with ethics and responsibility. For example, if leadership wants to leverage the power of diversity to develop a sustained competitive advantage, they would adopt the principles of equality of sexes, the elimination of prejudices, and the principle of oneness of humanity. If leadership wants to develop and use teamwork and collaboration as a strategic competitive advantage, they would integrate the behaviors and principles for collaborative excellence and working cohesively as one.

The framework and foundation of ethics and responsibility will enable the entrepreneur to consistently manage the needed qualities and principles for success in all aspects of daily operations. These aspects include research and development, engineering, manufacturing, sales, marketing, planning, decision-making, problem solving, conflict management, and other aspects of organizational governance. To demonstrate what this means in practice, the leadership of each of functional area could serve as role models, raise awareness, and encourage individuals to internalize a line of ethical reasoning, asking questions such as, "Is my decision right or wrong (good or bad)?" "Am I dealing with factual information or is conjecture?" "What is the consequence of my action?" "Is my decision fair and equitable?" "Did I give the individual what they are due?" "Would I want to be treated this way?" "Will this action help me achieve the best results for the collective?" This mindset, line of reasoning, and congruence between individual and organizational ethics is often lacking, which leads to ethical deviations.[39,40,41,42,43,44] Establishing the foundation outlined here enables each member of the organization to exercise sound moral judgment, develop ethical capabilities, and internalize a moral compass. It also allows employees to be aligned with the company's grander purpose, vision, mission, and values that then translates into actions.

39 Mehran Ferdowsian. "Total Business Excellence—A New Management Model for Operationalizing Excellence." *International Journal of Quality & Reliability Management* 33, no. 7 (2016): 942–984. https://doi.org/10.1108/IJQRM-08-2014-0109
40 Shannon Bowen. "Organizational Factors Encouraging Ethical Decision-Making: An Exploration into the Case of an Exemplar." *Journal of Business Ethics* 52, no. 4 (2004): 311–324.
41 Muel Kaptein. "Developing and Testing a Measure for the Ethical Culture of Organizations: The Corporate Ethical Virtues Model."

Develop a Grander Purpose

Once the entrepreneur has designed and configured the organization to develop a sustained competitive advantage in a responsible manner, they need to develop a higher vision or a grander purpose for the organization. This grander purpose is not the same as a mission or vision (although they may overlap). It is not financially motivated, it is not product/service centric, and it is not shareholder driven. Instead, the grander purpose defines and highlights the reasoning for a firm's long-term existence and success; it provides guidance and direction during decision-making, problem solving, and conflict resolution; it provides the motivation for individuals to achieve excellence and the sense of urgency for social change; and it enables individuals to be part of a larger cause. For example, the integration of the right grander purpose into the operations of an organization could have prevented the manufacturing of toys made with lead-based paint or the poisoning of the Flint, Michigan, water supply. The grander purpose provides a mechanism to help individuals calibrate their day-to-day activities against a more meaningful and stable target.[45]

Develop a Culture of Collaborative Excellence

The establishment of a framework and foundation for ethical behavior opens up the organization for effective and meaningful teamwork and collaboration. Many existing approaches to collaboration, while demonstrating successes and benefits, also are sometimes inadequate in addressing complex group interactions dealing with mistrust, competition, politics, and ideological differences. A successful culture of collaboration should convince individuals to find the best ideas, leverage diversity, grow new solutions, gain wholehearted support, develop champions of change, nurture a safe environment, and encourage people to express all ideas.

An effective process for encouraging collaboration takes time to build; however, it's worth it because it will provide the inspiration and motivation needed to accomplish tasks and exceed expectations. The organization should also have consequences in place for ineffective collaboration, which may be evidenced in gossip, backstabbing, self-centered behavior, and biases or prejudices. Such consequences could include probation plans and one-on-one meetings that work to determine the root cause and identify steps forward.

Creativity is also key for a team to think differently. There must be freedom in the workplace for creativity to blossom. When developing a culture of creativity, entrepreneurs should consider these issue and challenges:

- How can we create a culture of creativity and innovation?
- How can we encourage the members of the organization to collaborate and leverage each other's creativity?
- How can we reward and recognize people for their creativity?

Human Resources Development

A human resources development plan enables a company to continually grow its intellectual resources, enables individuals to develop ethical capabilities, strengthens individual creativity and organizational innovation, provides a steady stream of capable human resources for its leadership pipelines, and enables the firm to leverage and harvest those human resources to advance society in a responsible manner. This is achieved by providing a new employee assessment process where every member of the organization is given the needed opportunities and is expected to collaborate with their superior(s) to own and manage their lifelong development plan (LDP). At a minimum, an LDP should:

Journal of Organizational Behavior 29 (2008): 923–947. Muel Kaptein. "The Ethics of Organizations: A Longitudinal Study of the US Working Population." *Journal of Business Ethics* 92, no. 4 (2009): 601–618. Muel Kaptein and F. Bons. "The Business Codes of the Fortune Global 200—What the Largest Companies in the Work Say and Do." Findings of a whitepaper from a study conducted by KPMG in conjunction with the RSM Erasmus University. 2014.

42 B. Elango, Karen Paul, and Shishir K. Paudel. "Organizational Ethics, Individual Ethics, and Ethical Intentions in International Decision-Making." *Journal of Business Ethics* 97, no. 4 (2010): 543–561.

43 Ding-Yu Jiang, Yi-Chen Lin, and Lin-Chin Lin. "Business Moral Values of Supervisors and Subordinates and Their Effect on Employee Effectiveness." *Journal of Business Ethics* 100, no. 2 (2010): 239–252.

44 Robert J. Sternberg. "Ethics from Thought to Action." *Educational Leadership* 68, no. 6 (2011): 34–39.

45 Mehran Ferdowsian. "Total Business Excellence—A New Management Model for Operationalizing Excellence." *International Journal of Quality & Reliability Management* 33, no. 7 (2016): 942–984. https://doi.org/10.1108/IJQRM-08-2014-0109

- Include short-term and long-term career goals and objectives
- Help identify, continually develop, and leverage individual strengths
- Enable individuals to identify and measurably close gaps in deliverables, behavior, and professional improvement
- Clarify major deliverables and success indicators

In sum, an LDP becomes the primary instrument to assist individuals to achieve excellence by raising performance, closing gaps in assessment, and aligning the individual with the grander purpose, vision, mission, goals, needs, and objectives.

WORK IT OUT

Growing Collaboration and Creativity

Entrepreneurs are entrusted with the growth and development of their people. This growth and development should not be stopped, delayed, or marginalized in any shape or form. Instead, an entrepreneur needs to learn how to use the available resources to systematically train, develop, and deliver a steady stream of responsible individuals who are able to grow within the company as well as grow the company. List three strategies an entrepreneur could use to achieve the following major objectives:

1. Develop the best, the brightest, and most creative and motivated people who have a strong sense of right and wrong
2. Develop individuals who have a strong sense of ownership, responsibility, and commitment to achieve and sustain a competitive edge
3. Leverage these intellectual forces and the synergy within the organization to generate the greatest value and wealth for all stakeholders.

Develop Ethical and Responsible Leadership/Management

Significant research shows that the culture of the organization is mostly shaped by its leadership values—by how leaders develop the bonds of trust, by how they motivate their people, by their responsible decisions and actions, and by how they empower, delegate, and monitor tasks. A recent *Harvard Business Review* article, by a group of professors and entrepreneurs, synthesized the research of experts including Edgar Schein, Shalom Schwartz, Geert Hofstede, and other leading scholars on this topic.[46] The article indicates that the attributes of a business's leaders define that organization's culture. A business's culture is essentially defined as the social order within an organization that helps shape attitudes and behaviors—delineating what type of behavior is encouraged and/or discouraged.

While it is possible for a company to hire individuals who possess these attributes, the organization should have a plan in place to systematically train and develop responsible leaders. At minimum, this should include the development and management of a leadership pipeline, the nurturing of ethical and intellectual capabilities, and rewards and consequences that enable a leader to develop and internalize a moral compass.

WHAT CAN YOU DO?

Entrepreneurs Must Not Just Talk the Talk but Walk the Walk

As both a leader and an entrepreneur, you need to have a good understanding of ethics and responsibility, and be able to apply the major tenets of concepts such as CSR. To build and maintain trust, it is important

46 Boris Groysberg, Jeremiah Lee, Jesse Price, and J. Yo-Jud Cheng. "The Leader's Guide to Corporate Culture." January/February 2018. *Harvard Business Review*. https://hbr.org/2018/01/the-culture-factor

that these concepts not start and end with mere empty words and gestures. Rather, entrepreneurs need to exemplify and model these concepts, and apply them through meaningful, consistent, and timely actions. In sum, an entrepreneur needs to live the values they wish to see in others. They need to become the embodiments of trust, respect, responsibility, commitment, and other key qualities. These core values need to be infused into the fabric of the organization.

Entrepreneurs have been placed in a position of power and responsibility. They need to use their position, power, social standing, and the synergy of the vast financial and intellectual resources at their disposal to move and shake the world in a meaningful way. For example, imagine for a moment using the resources of companies such as Apple, Google, Microsoft, Amazon, and Facebook, whose combined worth is estimated to be close to $2.2 trillion, to address complex and difficult global issues dealing with education, poverty, hunger, and other chronic problems.

Develop Internal/External Organizational Alignment and Cohesion

Key to ethical organizational success is the alignment and cohesion between individuals, groups, and the enterprise as a whole. This alignment starts with the development of a grander purpose that enables the entrepreneur and the organization to serve, add value, and advance the society in which it operates. It ensures individuals and units within the company understand the grander purpose, mission, vision, and the goals and objectives of the company, and it provides each member or the organization the opportunity to serve and fit into that grander purpose, mission, and vision. It is further strengthened by asking individuals to achieve excellence in their own right instead of competing with each other. It sets clear expectations about how people are to treat and deal with each other to deliver results. It deals with the alignment of corporate values with the espoused values, and the alignment between what leadership says and does. When combined, these and other alignments can enable individuals and groups to stay on track and reach the company's goals efficiently.

ENTREPRENEUR IN ACTION

Unilever "Enhancing Livelihoods" through Project Shakti

According to management guru Peter Drucker, whose ideas significantly contributed to the foundations of thought about the workings of the modern business corporation, workers "need to know the organization's mission and to believe in it." How do organizations ensure this commitment? By satisfying workers' values.[47] A program undertaken by Unilever, the Dutch-British multinational company co-headquartered in Rotterdam and London, illustrates the kind of values-oriented corporate endeavor Drucker describes. Project Shakti is a Unilever CSR initiative in India that links CSR with financial opportunities for local women.[48] It is considered a leading example of micro-entrepreneurship, and it expands the concept of sustainability to include not only environmental issues but also economic opportunities and financial networking in underdeveloped areas.

The goal, according to Unilever, is to give rural Shakti women the ability to earn money for themselves and their families as micro-entrepreneurs. Unilever's subsidiary in India, Hindustan Lever, has started training programs for thousands of women in small towns and villages across India to help them understand how to run their own small sole proprietorships as distributors of the company's products. With support from a team of rural sales managers, women who had been unable to support themselves are now becoming empowered by learning how a supply chain works, what products Hindustan Lever produces, and how to distribute them. The sales managers also act in a consulting capacity to help with business basics, money

47 Rick Wartzman. "What Peter Drucker Knew About 2020." *The Harvard Business Review*. October 16, 2014. https://hbr.org/2014/10/what-peter-drucker-knew-about-2020
48 Unilever. https://www.unilever.com/sustainable-living/values-and-values/

management, negotiations, and related skills that help the women run their businesses effectively.

Project Shakti has enlisted more than 100,000 rural participants, which includes about 75,000 women. The project has changed their lives in ways that are profound, and not only because of the income earned. The women now have increased self-esteem based on a sense of empowerment, and they finally feel they have a place in Indian society. According to the Unilever Sustainable Living Plan, Project Shakti is one of the best and most sustainable ways the company can address women's social concerns. It allows Unilever to conduct business in a socially responsible manner, helping women help themselves while extending the reach of its products.

- Do you believe Unilever sponsors the Shakti program to help women, boost its own profits, or both? Explain your answer.
- How is this program an example of both corporate and personal sustainability?

Develop a Culture of Creativity and Innovation

The next building block is developing a culture of creativity and innovation. This means going beyond a spark of creativity from select individuals or business units, and instead nurturing a culture where every member of the organization is continually creative and the organization is innovative. This also means providing the means and opportunities for individuals to be engaged, creative, and contributing members on a full-time basis. What makes this possible results from the prior building blocks. Innovation requires good leadership and management; a meaningful and effective process for teamwork and collaboration; a culture of learning and improvement; a consistent and measurable process to encourage, recognize, compensate, and track innovation; and company-wide focus on the training and development of the sense of creativity.[49]

Develop a Culture of Delivering Responsible Results

Measurable results compose the final building block of a framework for ethics and responsibility. This involves developing systems and indicators that will demonstrate how your business is achieving ethical standards and progressively improving as it adds value to society. While the details of which indicators to select is left up to the discretion of the entrepreneur, this building block defines success in terms of ten dimensions of business excellence, shown in Figure 3.7.

49 Mehran Ferdowsian. "Total Business Excellence—A New Management Model for Operationalizing Excellence." *International Journal of Quality & Reliability Management* 33, no. 7 (2016): 942–984. https://doi.org/10.1108/IJQRM-08-2014-0109

Figure 3.7 Delivering responsible results involves multiple considerations. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Figure 3.7 serves as an easy-to-understand guide for entrepreneurs seeking to create a culture of excellence. Focusing on these ten dimensions can help a business achieve excellence, from which a company may derive multiple benefits. Examples of reasons why a company strives to achieve excellence include strengthening alignment between company values and those of stakeholders, balancing goals versus measures of success, clarifying strategic focus versus operational concerns, selecting areas within the company wherein improvement is needed, and shifting from a preoccupation with daily activities and processes to focus on outcomes. Companies seek excellence with regard to internal and external outcomes, both of which are important. Thus, whether examining internal aspects such as finance and operations, or external aspects such as product quality and customer service, each of these ten areas is an ingredient of company excellence.

Creating an Ethical and Responsible Workplace Environment

A safe, healthy, and productive workplace is an environment in which an individual has a high level of trust and confidence that if they give their best, they will see a number of results and be afforded a number of things in exchange for their hard work. This concept resembles an employer-employee contract. This contract includes the following employee expectations:

1. They are treated with the respect, dignity, and courtesy they deserve as a human being.
2. They are given the needed support, equal opportunities, and resources to excel.
3. They are given what they deserve and what they are due in a fair and equitable way.
4. They are provided a safe, secure, and prejudice-free work environment.
5. They are not pushed, pressured, or expected to behave irresponsibly.

This type of workplace environment enables individuals to continually grow and develop to their full potential and then leverage that potential to add value to their own lives, careers, and society. This type of environment is one in which individuals are not afraid to speak their mind; they feel safe to discuss problems and concerns, and feel free to question and reject that which is wrong.

Prejudice

Prejudice is often thought of as a negative attitude and/or feeling toward an individual based solely on one's membership in a particular group. Prejudice is common against people who are members of unfamiliar cultural groups. In employment, it can be the root cause of unfair discrimination.[50] One factor essential to the development of a safe and healthy work environment is that it strives to be a place free of prejudice. This is an environment where everyone is treated with the respect and dignity they deserve and are afforded equal opportunities for growth, development, and advancement both within and outside of the organization. For example, it is important to look at the merit or value of the work done by an individual and the manner by which those results have been delivered. It is unethical to treat people differently based on their race, gender, age, nationality, and other differentiating factors. To develop trust and respect, everyone needs to be afforded the same opportunities.

Competition and Collaboration

Effectively managing a workforce includes a systematic approach to appraisal of employee performance. A manager/entrepreneur must decide how to do this within their company. A forced ranking system is one in which scoring employee performance is competitive and can pit employees against each other instead of fostering a collaborative work environment. Some employers have switched to a system that does not require forced rankings and attempts to downplay the competitive nature of assessment, focusing instead on individual continuous improvement. There is a legitimate difference of opinion on this issue. According to a *Wall Street Journal* article by the accounting and consulting firm Deloitte,[51] executives are split on whether it is an effective practice. Jack Welch, former CEO at General Electric, was a proponent of it, whereas others see it as counterproductive. Companies that have discontinued the process include Microsoft and GE.

In an environment of collaborative excellence, individuals are encouraged to express their ideas and viewpoints in an unfettered and respectful way, where the merit of each idea is weighed against the merit of other ideas. In this environment, individuals are not reprimanded for being creative, taking calculated and reasonable risks, or challenging management or leadership.

WORK IT OUT

Anonymous Whistleblower Hotlines

Most large companies now have anonymous hotlines that employees may call to report ethical violations. What are some other concrete and actionable ways you can develop a safe environment where every member of your organization is able to question authority, point out a wrong, and stop an unethical decision/action?

One example of a problem that can arise in an overly competitive environment or culture created by an organization would be the faulty ignition switch scandal at GM. According to Valdes-Depena, and Yellin,[52] GM knew about this problem in 2001. However, it took the company over twelve years, more than 100 deaths, and 30 million vehicles being recalled to finally admit that there was a problem. In 2014, GM admitted that a faculty ignition switch may result in the engine of a vehicle being shut down while in drive, resulting in accidents, severe injuries, or death.[53] If GM had developed an effective environment of collaboration, individuals from leadership, management, sales, marketing, engineering, manufacturing, and human resources, as well as major stakeholders, might have collaborated and prevented the ignition switch problem.

50 Paul C. Holinger. "Understanding Bias, Prejudice, and Violence." *Psychology Today*. June 6, 2017. https://www.psychologytoday.com/us/blog/great-kids-great-parents/201706/understanding-bias-prejudice-and-violence
51 Deloitte CIO Journal. "It's Official: Forced Ranking Is Dead." *Wall Street Journal*. 2014. https://deloitte.wsj.com/cio/2014/06/10/its-official-forced-ranking-is-dead/
52 Peter Valdes-Dapena and Tal Yellin. "GM: Steps to a Recall Nightmare." *CNN Money*. March 19, 2014. http://money.cnn.com/

Diversity

Entrepreneurs need to appreciate, respect, and learn to effectively leverage the unique and diverse qualities that each individual brings to the table. These qualities can be used to innovate, make better decisions, solve complex problems/conflicts, move an organization cohesively in a single direction, or rapidly change direction when needed. If used correctly, these differences enable an entrepreneur to develop a sustained competitive advantage by looking at the different thoughts, ideas, and viewpoints to make better and more informed decisions.

Diversity, in terms of a legal concept, deals with innate characteristics such as an individual's sex, color, race, national origin, religion, and age. It might also include educational background, cultural background, socioeconomic background, and potentially even political affiliations. However, diversity in terms of an ethical concept rather than purely a legal one also deals with a number of not-so-obvious characteristics such as the diversity of behavior, thought-process, comprehension, attitudes, temperaments, and learning styles. Combined, these differences can be beneficial to a business organization and result in high-level performance by the workforce as a whole.

Diversity may be an actual legal requirement depending upon what type of business an entrepreneur enters. For example, if you plan on doing any government contracting work, whether local, state, or federal, the chances are that your business will have to meet a diversity standard. Many private companies also have diversity clauses in the supply chain contracts related to supplier diversity initiatives.

WORK IT OUT

Building Diversity

For each of the following, identify two examples of a concrete action or activity an entrepreneur could implement to achieve the stated goal.

1. Introduce the concept of diversity and highlight the significance, the value, and the benefits of a diverse work environment.
2. Set clear expectations for individuals to value diversity, the concept of unity in diversity, and show how others can leverage the power of diversity to innovate.
3. Exemplify, role model, and live good ethical behavior that strengthens diversity such as the elimination of prejudice of all kinds and expect others to do the same around you.
4. Ensure that you design the hiring process, including job descriptions, recruiting, interview questions, and other related steps, with diversity in mind.
5. Provide training to educate people on the concept of prejudice, the different forms of prejudices, and the negative aspects of prejudices.
6. Provide opportunities for building ethical capacities such as becoming truthful, trustworthiness, and a just individual.
7. Provide consistent, meaningful, substantial, and timely consequences for prejudicial behavior in organizations.

infographic/pf/autos/gm-recall-timeline/

53 Arthur W. Page Society. "General Motors' Corporate Culture Crisis: An Assessment of the Ignition Switch Recall." 2015 Case Study Completion. January 16, 2016. https://page.org/attachments/1edd5184509636aabbdc07ef0c3546e0facf5c0c/store/00f8d9b37cec4d725c881b7235467635aeab21b4d2333398c819839d426b/General-Motors-Case-Study-2015.pdf

Gender Equality

As an entrepreneur, you need to recognize the significance, value, and impact of the principle of equality of men and women on developing a sustained competitive advantage. Then you need to incorporate this principle into the fabric of your organization. Aside from being the right thing to do, one reason why this principle is so important is that close to one-half of the planet is female (and has traditionally been marginalized in the business world).[54,55] If you overlook this fact, you will also be potentially overlooking one-half of the talent that can help you excel and develop a sustained competitive advantage. In turn, this will result in a loss of trust and confidence. A second and more important reason would be that any deviation from this principle goes against the whole concept of ethics and responsibility. Moreover, this principle will help your organization attract the best and brightest employees.

The principle of gender equality does not deny differences between men and women. This principle primarily asks that we give each member of society fair and equal opportunities for growth, development, and advancement. It also recognizes that women have been historically marginalized or excluded from the business world. This claim holds true today and is applicable to even to the most advanced countries in the world (e.g., the discrepancy of pay between women and men in Western societies). Therefore, women need to be afforded the same opportunities for education, rewards, recognitions, and promotions as men.

Trust and Ethical Accountability

Finally, the development of safe environments also deals with an environment where individuals are able to develop unbreakable bonds of trust, where they don't feel they have to constantly watch their backs, where individuals are free to point out misconduct without being reprimanded, and where individuals feel they will be given what they are due or deserve. This dimension of the development of a safe work environment deals with making sure individuals feel they are being treated in a fair and equitable manner and that their need for the development of an ethical and moral work environment is being met.

WORK IT OUT

Sherron Watkins and Enron

Enron is one of the most infamous examples of corporate fraud in US history. The scandal that destroyed the company resulted in approximately $60 billion in lost shareholder value. Sherron Watkins, an officer of the company, discovered the fraud and first went to her boss and mentor, founder and chairperson Ken Lay, to report the suspected accounting and financial irregularities. She was ignored more than once and eventually went to the press with her story. Because she did not go directly to the SEC, Watkins received no whistleblower protection. (The Sarbanes-Oxley Act was not passed until after the Enron scandal. In fact, it was Watkins's circumstance and Enron's misdeeds that helped convince Congress to pass the law.[56])

Now a respected national speaker on the topic of ethics and employees' responsibility, Watkins talks about how an employee should handle such situations. "When you're faced with something that really matters, if you're silent, you're starting on the wrong path…go against the crowd if need be," she said in a speech to the National Character and Leadership Symposium (a seminar to instill leadership and moral qualities in young men and women).

Watkins talks openly about the risk of being an honest employee, something employees should consider when evaluating what they owe their company, the public, and themselves. "I will never have a job in corporate America again. The minute you speak truth to power and you're not heard, your career is never

54 R. A. Fisher. *The Genetical Theory of Natural Selection*. (Clarendon, Oxford, 1930).
55 W. D. Hamilton, "Extraordinary Sex Ratios," *Science* 156 (1967): 477–488.
56 Shaheen Pasha. "Enron's Whistle Blower Details Sinking Ship." *CNN Money*. March 16, 2006. http://money.cnn.com/2006/03/15/news/newsmakers/enron/

the same again."

Enron's corporate leaders dealt with the looming crisis by a combination of blaming others and leaving their employees to fend for themselves. According to Watkins, "Within two weeks of me finding this fraud, [Enron president] Jeff Skilling quit. We did feel like we were on a battleship, and things were not going well, and the captain had just taken a helicopter home. The fall of 2001 was just the bleakest time in my life, because everything I thought was secure was no longer secure."

- Did Watkins owe an ethical duty to Enron, to its shareholders, or to the investing public to go public with her suspicions? Explain your answer.
- How big a price is it fair to ask a whistleblowing employee to pay?

Ideally, it is best that entrepreneurs exemplify good ethical behavior, expect their people to do the same, and help the members of the organization develop a moral compass. However, it is equally as important that business owners take action and put in place the right checks and balances that verify that the organization's people are complying with its policies and principles of ethical behavior.

Organizations should set up systems that monitor compliance. In addition, you should develop a leadership pipeline that ensures that individuals would be placed in the pipelines only if they exhibit good ethical behavior, working with each business unit manager to ensure this is happening. Individual assessments should clearly assess ethical behavior and provide rewards, recognitions, and promotions for good ethical behavior, and consequences and training/solutions for actions that do not meet company standards. You should provide meaningful, substantial, and timely consequences for lack of acceptable behavior, such as removing an executive from a leadership pipeline when it has been established that they will not govern responsibly.

Importantly, members of the organization should not be intimidated to blindly follow or accept the existing monitoring system without question. An entrepreneur needs to cultivate an environment where they expect, support, and encourage every member of their organization to be inquisitive, be creative, question authority, and search for the underlying truth in all matters. It must be noted that questioning authority does not mean anything goes; it simply means that employees are expected to think on their own. Accountability should be encouraged; it is both an ethical and legal issue.

An example of a system of accountability that is appropriate for entrepreneurs is one proposed by an article in the *Harvard Business Review*.[57] A sound approach to accountability requires a multistep process that includes establishing expectations, ensuring employees have the capability to do it, measurement of results, feedback, and consequences for unethical behavior. In addition to an ethical approach, remember that there are federal laws mandating accountability. The most well-known of these is the Sarbanes-Oxley Act,[58] discussed elsewhere in this chapter, and other chapters in this text. Also called the Corporate and Auditing Accountability, Responsibility, and Transparency Act, the Sarbanes-Oxley Act requires publicly traded companies to have an internal system of control that emphasizes transparency and accountability.

If You Make a Mistake

If you or your organization makes a mistake or misstep, you must decide how to address it. In general, you are faced with the choice of paying now or paying a hundredfold later. A closer look at the largest, most expensive, and most devastating corporate failures of our times shows that these failures have resulted in the loss of life, property, and/or monumental environmental disasters. For the most part, these corporate failures have been caused by one or more ethical deviations on behalf of leadership. To combat these problems, entrepreneurs

57 Peter Bregman. "The Right Way to Hold People Accountable." *Harvard Business Review*. January 11, 2016. https://hbr.org/2016/01/the-right-way-to-hold-people-accountable
58 Pub.L. 107–204. https://legcounsel.house.gov/Comps/Sarbanes-oxley%20Act%20Of%202002.pdf

need to start by first being responsible, accepting their failures, and admitting when they have made mistakes. This admittance needs to be genuine, transparent, prompt, truthful, and authentic if they wish stakeholders to accept and believe their remorse. Once that first step is taken, they need to take immediate steps to proactively address the problems they have caused. Many leaders or entrepreneurs have learned the hard way that they need to be open and transparent with their stakeholders at the outset. Failure to rapidly admit mistakes can and has resulted in paying a very steep price when exposed. The actions that an entrepreneur needs to take include:

1. Admitting their mistakes, failures, and shortcomings to all stakeholders
2. Effectively communicating the nature of the problem to major stakeholders
3. Informing the stakeholders of the impact, side effect, and causes of the problem
4. Taking necessary and immediate steps to address the issue and stop the bleeding
5. Conducting a thorough and unbiased root-cause analysis to identify the underlying cause
6. Addressing any people and systemic gaps that caused the problem in the first place
7. Putting in place measures that will prevent the repeat of the same mistakes

To summarize, the best approach is that you admit your mistakes and shortcomings, pay the price, fix and uproot the problem, and systematically prevent the repeat of the same mistakes. A few examples of corporate mistakes and shortcomings that were quickly addressed before turning into severe problems would be the Tylenol poisoning and the customer accounts stolen at Target. A few examples of a problem that were not handled correctly and resulted in multi-billion-dollar problems are GM's faulty ignition switch problem, Volkswagen's emission control fraud, and Wells Fargo's account fraud.

ENTREPRENEUR IN ACTION

Taking the Ethical High Road

To go beyond a glowing commitment report, a shining website, or a few meaningless words in a code-of-conduct on corporate responsibility, an entrepreneur needs to follow the rule of law, the spirit of the law, and do the right thing at all times and under all circumstances. To achieve this, entrepreneurs need to develop and internalize a moral compass that prevents them from doing the wrong and unethical thing despite the consequences.

One classic example of doing the right thing which has been studied as a case study in business schools is attributed to Johnson & Johnson (J&J). In 1982, J&J found out that someone had tampered with and laced their Tylenol capsules with potassium cyanide.[59] To address this problem, safeguard their brand name, and prevent negative press, J&J removed all of their Tylenol products from the shelves.

59 Dan Fletcher. "A Brief History of the Tylenol Poisoning." *Time*. February 9, 2009. http://content.time.com/time/nation/article/0,8599,1878063,00.html

Key Terms

anchoring strategies in the ethical context, the process of making ethics a foundation (anchor) of your business so that decision makers act keeping in mind key ethical considerations
antitrust laws prevent companies from abusing position or power in the market through exclusion or limitation of competitor access to the market
business ethics conduct by which companies and their agents abide by the law and respect the rights of their stakeholders, particularly their customers, clients, employees, and the surrounding community and environment
conflict of interest when an individual or organization has interests in multiple areas that come into conflict with each other
copyright grants the creator of a work the exclusive right to reproduce the work, typically for a specified period of time
corporate social responsibility (CSR) practice in which a business views itself within a broader context, as a member of society with certain implicit social obligations and responsibility for its own effects on environmental and social well-being
design patent protects product design
disclosure sharing the needed facts and details about a subject in a transparent and truthful way
diversity inclusion of many types of employees, regardless of differences (race, religion, gender, disability, LGTBQ, socioeconomic, cultural)
environmental entrepreneurship entrepreneurial ventures focused on identifying an environmental problem and creating a product or process to solve that problem
ethics standards of behavior to which we hold ourselves in our personal and professional lives
fairness impartial, unbiased compliance with rules and standards of what is right, just, and equitable
integrity adherence to a code of moral values implying trustworthiness and incorruptibility because there is unity between what we say and what we do
intellectual property legally protected result of creative work to turn a unique idea into a product or service
prejudice way of thinking about or treating employees in a manner that favors or hinders one person or group over another, usually in a way considered to be unfair
social entrepreneurship entrepreneurial ventures focused on identifying a societal problem and creating a product or process to solve that problem
sustainability practice of preserving resources and operating in a way that is ecologically responsible in the long term
trade secret proprietary information, processes, or other internal knowledge that contribute to an organization's competitive edge in a market
trademark registration that provides the owner the ability to use a name, symbol, jingle, or character in conjunction with a specific product or service, and prevents others from using those same symbols to sell their products
truthfulness underlying facts, reality, and evidence on a matter
utility patent protects product ideas

Summary

3.1 Ethical and Legal Issues in Entrepreneurship

The first section of this chapter explores the relationship between entrepreneurship, ethics, social responsibility, and the law. At times, ethical conduct and legal conduct may seem intertwined; in other circumstances, they are quite different. This section discusses how ethical considerations can provide a moral compass for entrepreneurs seeking to find a balance between making money and doing the right thing. Keep in mind, however, that unlike legal mandates, following ethical business practices is more often a voluntary matter for business owners and operators. On the other hand, laws are important to follow, or you and your

business might well be held legally liable (civilly or criminally). Sometimes, making a mistake is only an ethical lapse; other times, the mistake also constitutes a violation of the law (e.g., the Equifax case discussed).

3.2 Corporate Social Responsibility and Social Entrepreneurship

This section explored examples of entrepreneurship in which social responsibility plays a key role in the organization. Causes such as sustainability/environmental awareness are often important to an entrepreneur and their workforce. Most startup businesses want to make money, and in fact, as this section demonstrates, it's quite possible to make money and carry out a social responsibility goal simultaneously. Some social entrepreneurship companies go the extra mile and become certified B-corporations, as opposed to C-corps or S-corps, which are tax distinctions. If an entrepreneur elects to become a B-corporation, it means that it has satisfied an outside organization's audit, proving that they truly act in a socially responsible manner.

3.3 Developing a Workplace Culture of Ethical Excellence and Accountability

This section of the chapter covers the area of employment. We explored how entrepreneurs can make their company one for which people want to work: where being ethical is a highly regarded trait. This type of approach to employment includes both ethical and legal considerations, such as no discrimination, fair pay, encouraging/rewarding ethical behavior, and creating an atmosphere of collegial teamwork. This approach to creating a socially responsible workplace requires a long-term commitment to being an ethical employer, which is not always easy. For example, it may mean, even though you are the boss or owner, admitting you made a mistake, accepting responsibility for it, and correcting it. You do not want to be the type of boss who can never say I got that wrong, and I'll do better next time.

Review Questions

1. Full and truthful disclosure _____.
   a. is often required under tort law
   b. is a matter of ethics, not a legal requirement
   c. is a risky business practice because it helps the competition
   d. is a strictly personal choice

2. Common IP law-mandated periods of protection are _____.
   a. copyrights are protected for twenty years
   b. patents are protected for fifty years
   c. trademarks are protected for renewable ten-year periods
   d. trade secrets are protected for fifteen years

3. Acting ethically includes acting with which of the following?
   a. integrity
   b. disclosure
   c. transparency
   d. All of these options are correct.

4. Antitrust law:
   a. may help small entrepreneurs by ensuring big companies do not have monopolies
   b. may hurt small entrepreneur by requiring them to disclose trade secrets
   c. only applies to businesses with over 500 employees
   d. None of these options are correct.

5. Patents _____.

a. are similar to trade secrets under IP law
b. allow a temporary monopoly for an invention
c. are protected under IP law for a period of ninety-nine years
d. None of these options are correct.

6. An example of a company(s) that have been fined millions of dollars for legal/ethical violations includes _____.
a. Enron
b. TOMS
c. British Petroleum
d. a and c

7. The B-corporation moniker _____.
a. requires government certification
b. requires no certification
c. can only be used after an audit and certification by the B-corp organization
d. is a social media concept used primarily for marketing purposes

8. What differentiates a social entrepreneurial enterprise from a traditional entrepreneur?
a. commitment to reduce pollution
b. pledge to undertake sustainable supply chain sourcing
c. effort to recycle water, waste, and other byproducts
d. All of these options are correct.

9. Core qualities for building a foundation of ethics-based behaviors include _____.
a. trust
b. fairness
c. excellence
d. All of these options are correct.

10. Millennial workers _____.
a. often do not place salary as their first priority
b. want work-life balance
c. usually expect their employer to have an ethical value system
d. All of these options are correct.

11. A diverse workforce _____.
a. is always optional
b. is usually required for government contracting
c. is always required under Title VII
d. is never required

Discussion Questions

1. How can ethics-based concepts such as truthfulness and fairness be integrated into the fabric of the organization?

2. How can we nurture an environment where each member of the organization develops and internalizes a moral compass?

3. Evaluate how an entrepreneurial business startup might benefit from the enforcement of antitrust laws

against a large competitor.

4. Discuss ways in which intellectual property, such as trademarks, can add value to a small business. How would you protect your ability to monetize intellectual property?
5. In this section of the chapter, there is an example of a customer data breach via computer hacking. Discuss the biggest risks of storing customer or company information online. What are some of the steps you would take to prevent a data breach?
6. Can a social enterprise work on a social issue and at the same time be profitable?
7. How will you ensure that your organization learns to develop and deliver products and services that reduces your carbon footprint?
8. Referring to Table 3.3 listing cases of corporate fraud, which company example do you think is one of the worst examples of unethical conduct? Is this because it involved the most money stolen, the most people cheated, or the most devious methods?
9. If an entrepreneur values sustainability and environmental awareness, does that mean the bottom line will suffer? Alternatively, is there a way to protect the environment and still make a profit?
10. You have learned about B-corporations. If you started a new business, would you commit to the rather stringent audit process necessary to become a B-corporation? Why or why not?
11. How can an entrepreneur maximize the benefits of a diverse workforce to develop a competitive advantage?
12. How can you combat the negative impact of biases and prejudices in your organization?
13. What would you do, as an entrepreneur, to make your employees feel you value their input and that they are free to speak honestly?
14. Explain why diversity is something that should matter to an owner. What would you do to try to achieve it?
15. Some small entrepreneurs do not have the budget for a full-fledged human resources department; however, that makes compliance with employment laws challenging. What steps would you take to comply with federal and state employment law if you do not have a full-time attorney or human resources specialist on staff?

Case Questions

1. In 2017, it became apparent that Wells Fargo had created over 2 million falsified customer accounts without the customers' consent, approval, or knowledge. John Stumpf, Wells Fargo CEO, who resigned amid this scandal, denied any leadership involvement and wrongdoing. He blamed his employees and fired over 5,300 employees over this scandal. Research this case and answer the following questions.
   A. What organizational and company-culture factors convinced employees to create false accounts?
   B. Why did the employees not question leadership?

2. In 2017, the US Environmental Protection Agency found that Volkswagen had installed a "defeat device"—software in the vehicle that detects that an emissions test is in progress, controls the engine, reduces emissions, and enables the vehicle to pass the test for US emissions standards. Martin Winterkorn, CEO of Volkswagen, denied any wrongdoing, was later forced to resign, and admitted they had cheated. Research this case and answer the following questions.
   A. What organizational and cultural factors convinced Volkswagen employees to cheat?
   B. Why did the workforce not question leadership?

3. If you were to create a top-ten list of the world's greatest corruption scandals, the problems of Petrobras (*Petróleo Brasileiro*) in Brazil surely would make the list. The majority state-owned petroleum conglomerate was a party to a multibillion-dollar scandal in which company executives received bribes and kickbacks from contractors in exchange for lucrative construction and drilling contracts. The contractors paid Petrobras executives upward of 5 percent of the contract amount, which was funneled back into slush funds. The slush funds, in turn, paid for the election campaigns of certain members of the ruling political party, *Partido dos Trabalhadores*, or the Workers Party, as well as for luxury items like race cars, jewelry, Rolex watches, yachts, wine, and art.[60] The original investigation into these practices was known as Operation Car Wash (*Lava Jato*) and began in 2014 at a gas station and car wash in Brasília, where money was being laundered. It has since expanded to include scrutiny of senators, government officials, and the former president of the republic, Luiz Inácio Lula da Silva. The probe also contributed to the impeachment and removal of Lula's successor, Dilma Rousseff. Lula and Rousseff are members of the Workers Party. The case is complex, revealing Chinese suppliers, Swiss bank accounts where money was hidden from Brazilian authorities, and wire transfers that went through New York City and caught the eye of the US Department of Justice. In early 2017, the Brazilian Supreme Court justice in charge of the investigation and prosecution was mysteriously killed in a plane crash. It is hard to imagine a more tragic example of systemic breakdown and individual vice. The loss of trust in government and the economy still affects ordinary Brazilians. Meanwhile, the investigation continues.
   A. Is this Brazilian company scandal unique to that culture?

4. In the fall of 2016, Samsung Electronics experienced a massive public relations disaster when its Galaxy Note 7 smartphones started exploding due to faulty batteries and casings. Initially, the company denied there were any technical problems. Then, when it became obvious the exploding phones posed a safety and health threat (they were banned from airplanes), Samsung accused its suppliers of creating the problem. In reality, the rush to beat Apple's iPhone 7 release date was the most likely reason corners were cut in production. Samsung finally owned up to the problem, recalled more than two million phones worldwide, and replaced them with new, improved Galaxy Note 7s. The company's response and its replacement of the phones went a long way toward defusing the disaster and even boosting the company's share price. Samsung focused on the customer (i.e., customer safety and satisfaction) with the motive of doing the ethically responsible thing.
   A. Although some might argue the company could have done far more and much more quickly, perhaps it still acted reasonably. What do you think?

5. Sometimes engaged employees go above and beyond in the interest of customer service, even if they have no "customers" to speak of. Kathy Fryman is one such employee. Fryman was a custodian for three decades at a 100-year-old school in the Augusta (KY) Independent School District. She was not just taking care of the school building, she was also taking care of the people inside.[61] Fryman fixed doors that would not close, phones that would not ring, and alarms that did not sound when they should. She kept track of keys and swept up dirty floors before parents' night. That was all part of the job of custodian, but she did much more. Fryman would often ask the nurse how an ill student was doing. She would check with a teacher about a kid who was going through tough times at home. If a teacher mentioned needing something, the next day it would show up on the teacher's desk. A student who needed something for class would suddenly find it in their backpack. Speaking of Fryman, district superintendent Lisa McCrane said, "She just has a unique way of making others feel nurtured, comforted, and cared for." According to Fryman, "...I need to be doing something for somebody." Fryman's customers were not there to buy a product on which she would make a commission. Her customers were students and teachers, parents and taxpayers. Yet she provided the kind of service that all employers would be proud of, the kind that makes a difference to people every day.

60 Jonathan Watts. "The Long Read Operation Car Wash: Is This the Biggest Corruption Scandal in History?" *The Guardian*. June 1, 2017.

A. Is there a way for a manager to find, develop, and encourage the next Fryman, or is the desire to "do something good for somebody" an inherent trait in some employees that is missing in others?
B. Employees who display Fryman's zeal often do so for their own internal rewards. Others may simply want to be recognized and appreciated for their effort. If you were the superintendent in her district, how would you recognize Fryman? Could she, for example, be invited to speak to new hires about opportunities to render exceptional service?

6. Please view the video ABC Nightline-IDEO Shopping Cart (https://openstax.org/l/52IDEOShopCart) on YouTube. This video demonstrates how an entrepreneurial mindset combined along with a collaborative process can be used to deliver the most innovative products.
   A. After watching the IDEO YouTube video, list the different factors that has enabled IDEO to become an industry example for corporate innovation.
   B. What top principles and behaviors that has contributed to the development of a culture of collaborative excellence?

Suggested Resources

3.1 Ethical and Legal Issues in Entrepreneurship

SBREFA Small Business Resource Center. This is a great site for help with understanding legal requirements and regulatory compliance.

https://www.dol.gov/agencies/oasam/business-operations-center/osdbu/compliance-assistance

US Department of Labor, Office of the Assistant Secretary for Administration & Management.

3.2 Corporate Social Responsibility and Social Entrepreneurship

List of Social Enterprise Business Models or Frameworks: http://www.thesedge.org/socent-spotlights/22-awesome-social-enterprise-business-ideas

TedTalk video: Carol Sanford at TEDxBerkeley 2014. "The Responsible Entrepreneur: Four Game Changing Archetypes": https://www.youtube.com/watch?v=Dqza5Uo1cFE

Global Entrepreneurship Monitor (GEM): www.gemconsortium.org

Social Enterprise and Entrepreneurship (SEE) the Change: https://seethechange.ca

3.3 Developing a Workplace Culture of Ethical Excellence and Accountability

Society for Human Resource Management: https://www.shrm.org

61 Brenna Kelly. "Augusta Schools Custodian Kathy Fryman Takes Care of Building and the People Inside; Gets Fred Award." *Northern Kentucky Tribune*. September 23, 2017. http://www.nkytribune.com/2017/09/augusta-schools-custodian-kathy-fryman-takes-care-of-building-and-the-people-inside-gets-fred-award/

4

Creativity, Innovation, and Invention

Figure 4.1 Creativity comes in many forms. It can be messy, but creativity is an essential element of innovation and inventiveness, both of which can drive entrepreneurship. (credit: modification of "On creativity" by Linus Bohman/Flickr, CC BY 2.0)

Chapter Outline

4.1 Tools for Creativity and Innovation
4.2 Creativity, Innovation, and Invention: How They Differ
4.3 Developing Ideas, Innovations, and Inventions

Introduction

We enter the world as curious beings. However, as we grow up, we are told to color inside the lines and that real animals can't talk—direction that can squelch creativity. Many successful entrepreneurs work to unlearn some of those messages in order to tap into creative thinking. What do you do when you are given a task that requires you to be creative? Do you get out your art supplies and start drawing? Do you pull out your phone or get on your computer and head straight for a search engine? Steve Jobs, the Apple founder and well-known innovator, had a preference when it came to creative contemplation, and it had nothing to do with art supplies or smartphones. Jobs did some of his best creative thinking when he went on a walk, or a walking chat.

Why did Jobs prefer walking as a way to develop new ideas? A Stanford University study found that walking improves creative thinking.[1] When you launch an entrepreneurial journey and set out to innovate and create, or when you hit a sticking point that requires a creative solution, it may be time to take a walk. Better yet, if you can find a friend, walk and talk. It might energize your creativity and lead to innovation and, possibly, to invention.

1 Marily Oppezzo and Daniel Schwartz. "Give Your Ideas Some Legs: The Positive Effect of Walking on Creative Thinking." *Journal of Experimental Psychology: Learning, Memory, and Cognition* 40, no. 4 (2014): 1142–1152.

4.1 Tools for Creativity and Innovation

Learning Objectives

By the end of this section, you will be able to:

- Describe popular, well-supported, creative problem-solving methods
- Understand which innovation or problem-solving methods apply best in different settings
- Know where to look for emerging innovation practices, research, and tools

Creativity, innovation, and invention are key concepts for your entrepreneurial journey. Fostering creativity and innovation will add essential tools to your entrepreneurial toolkit. In this chapter, first you'll learn about a few practical tools that can assist you in your efforts to create and innovate. Then, we'll define and distinguish creativity, innovation, and invention, and note the differences between pioneering and incremental innovation. Finally, we'll cover models and processes for developing creativity, innovation, and inventiveness. The science, study, and practice of creativity and design thinking are constantly evolving. Staying on top of well-documented, successful approaches can give you a competitive advantage and may remind you that entrepreneurship can be fun, exciting, and refreshing, as long as you keep your creative spirit alive and in constant motion.

Creative Problem-Solving Methods

Creative thinking can take various forms (Figure 4.2). This section focuses on a few creative thinking exercises that have proven useful for entrepreneurs. After discussing ideation practices that you can try, we conclude with a discussion of an in-depth innovation exercise that can help you develop a habit of turning creative ideas into innovative products and services. In this section, outcomes are vital.

Figure 4.2 When your process hits a sticking point, a walk—or a walk and talk—can help boost your creativity in thinking through solutions. (credit: "beard business city colleague" by "rawpixel"/Pixabay, CC0)

Three ideation practices are discussed here. Several others are offered in links at the end of this section. The first ideation practice comes from Stanford's Design School.[2] The objective is to generate as many ideas as possible and start to develop some of those ideas. This practice is the quintessential design thinking practice, or human-centric design thinking exercise, and it consists of five parts: accessing and expressing empathy, defining the problem, ideating solutions (brainstorming), prototyping, and testing (Figure 4.3). **Empathy** is the human ability to feel what other humans are feeling, which in the context of creativity, innovation, and invention is essential to beginning a process of human-centric design. Practicing empathy enables us to relate to people and see the problem through the eyes and feelings of those who experience it. By expressing empathy, you can begin to understand many facets of a problem and start to think about all of the forces you will need to bring to bear on it. From empathy comes the ability to proceed to the second step, defining the problem. Defining the problem must be based on honest, rational, *and* emotional observation for human-centric design to work. Third in the process is brainstorming solutions. The other two ideation exercises or practices in this section delve more deeply into brainstorming (also discussed in Problem Solving and Need Recognition Techniques), what it means, and how you can brainstorm creatively beyond the basic whiteboard scribbling in almost every organization. Designing for other people means building a prototype—the fourth step—and to test it. Once you apply this process to developing a product or service, you need to return to the empathetic mindset to examine whether you have reached a viable solution and, thus, an opportunity.

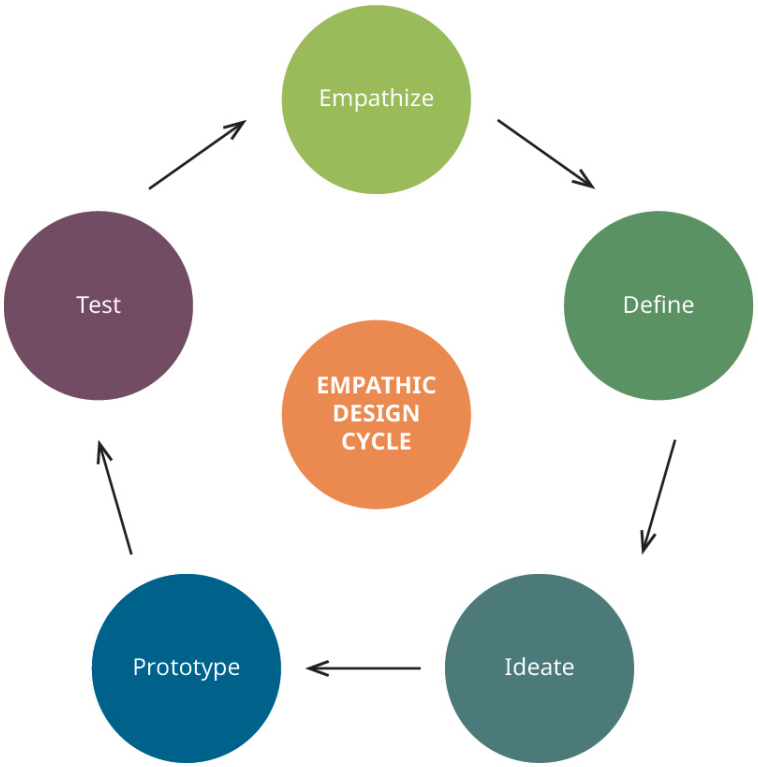


Figure 4.3 The empathetic design cycle is human-centric. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

LINK TO LEARNING

Watch this video on human-centered design (https://openstax.org/l/52HumnCntDesign) for more information, including an explanation of the phases involved.

2 Stanford d.school. https://dschool.stanford.edu/

To delve more deeply into ideation as a practice, we introduce here the Six Thinking Hats method (Figure 4.4).[3] There are different versions of this ideation game, but all of them are quite useful for encouraging thought by limiting the mindset of those involved in the game. Being encouraged to embody one mode of thinking frees you from considering other aspects of a problem that can limit creativity when you are looking for a solution. The six hats are:

- White Hat: acts as information gatherer by conducting research and bringing quantitative analysis to the discussion; sticks to the facts
- Red Hat: brings raw emotion to the mix and offers sensibilities without having to justify them
- Black Hat: employs logic and caution; warns participants about institutional limitations; also known as the "devil's advocate"
- Yellow Hat: brings the "logical positive" of optimism to the group; encourages solving small and large problems
- Green Hat: thinks creatively; introduces change and provokes other members when needed; new ideas are the purview of the Green Hat
- Blue Hat: maintains the broader structure of the discussion and may set the terms by which progress will be judged; makes sure the other hats play by the rules, or stay in their respective lanes, so to speak

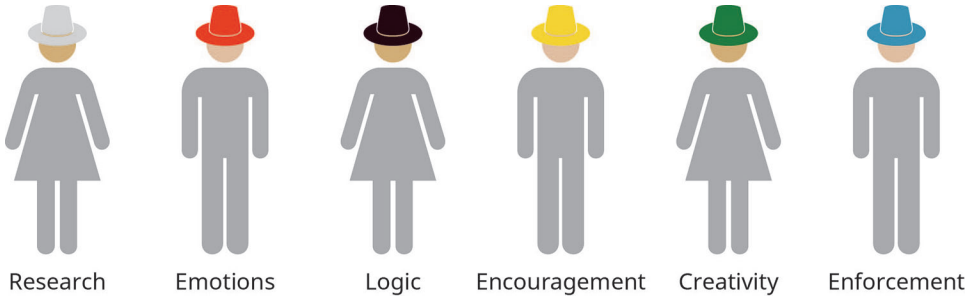


Figure 4.4 The Six Thinking Hats exercise is designed to have each participant focus on a particular approach to the problem or discussion. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

You can apply the Six Thinking Hats exercise to force structure on a discussion where, without it, several members of the group might try to wear several hats each. This game is not always easy to implement. If members cannot follow the rules, the process breaks down. When it works best, the Blue Hat maintains control and keeps the practice moving quickly. What you and your group should experience is a peculiar freedom arising from the imposition of limitations. By being responsible for only one mode of thinking, each participant can fully advocate for that point of view and can think deeply about that particular aspect of the solution. Thus, the group can be deeply creative, deeply logical, deeply optimistic, and deeply critical. This practice is meant to move entire groups past surface-level solutions. If you practice this exercise well, the challenges of implementing it are well worth the effort. It gives you the opportunity to vet ideas thoroughly while keeping many personality clashes at bay. If the participants stay in character, they can be accused only of acting in the best interests of their hat.

Your instructor may have your group members try different hats in different ideation exercises so you all can more fully develop each mindset.[4] This exercise forces you out of your most comfortable modes of thinking. You and your classmates can recognize in each other skills that you may not have realized you possess.

3 "10 Creative Techniques for You and Your Team." *MiroBlog.* n.d. https://miro.com/blog/creative-techniques/
4 "Six Thinking Hats." *The de Bono Group.* n.d. http://www.debonogroup.com/six_thinking_hats.php

The third ideation practice is quite simple. If stagnant thinking has begun to dominate an ongoing discussion, it can be helpful to inject an ideation framework. This is the "statement starters" method.[5] Ask, "How might we _____?" or "What if we _____?" in order to open up new possibilities when you seem to have reached the limits of creativity. This method is more than simply asking "Why not?" because it seeks to uncover *how* a problem might be solved. For entrepreneurs, the simplest form of framing a problem in the form of a question can be eye opening. It assumes open possibilities, invites participation, and demands focus. Statement starters assume that, at least, there *might* be a solution to every problem. Ideation is about starting down new paths. This mode of thought applies to social problems as well as consumer pain points (discussed later). Creating a list of statement starters can help entrepreneurs examine different possibilities by simply adopting different points of view when asking questions. For example, the question, "How might we keep rivers clean?" is similar to the question, "How might we prevent animal waste runoff from entering our city's waterways?" but the implications of each question are different for different stakeholders. Recall that stakeholders are individuals who have a vital interest in the business or organization. Statement starters almost always lead to a discussion of stakeholders and how they might be involved in finding solutions, offering support, and perhaps one day purchasing or contributing to dynamic, disruptive inventions or changes in social practice.

LINK TO LEARNING

Are you curious about ways to improve your ability to think creatively? Consider trying out some of the creative thinking exercises (https://openstax.org/l/52CreateThinkEx) provided at this site.

Matching Innovation Methods to Circumstances

Searching for innovation methods will often reveal many of the same, or similar, creativity exercises as we've just discussed. To go beyond ideation exercises, we will conclude with a foundation of thinking that can help when you are tackling all sorts of innovation problems. Simply put, **open innovation** involves searching for and finding solutions outside of the organizational structure. Open innovation is somewhat difficult to pin down. The educator and author Henry Chesbrough was one of the first to define it: "Open innovation is 'the use of purposive inflows and outflows of knowledge to accelerate internal innovation, and expand the markets for external use of innovation, respectively.'"[6] In other words, firms built on a structure of open innovation look beyond their own research and development capabilities to solve problems. This outlook can guide all sorts of product and service development processes. Open innovation models also allow innovations to be shared widely so that they can seed other innovations outside the original firm or institution.

Open innovation takes an optimistic view of sharing information and ideas across a society connected by instantaneous communication networks. It is also a shift from the classic research and development model. In a sense, you allow others to solve problems in your business, startup, or social entrepreneurship project. In this reciprocal world, you are open to the reality that information is difficult to keep under wraps. You may seek patents for your intellectual property, particularly in fixed product or service practice form, but you should expect, or even encourage, the widespread circulation of key elements of your solutions. This makes sense: If, as an entrepreneur or an innovative corporation, you are going to look beyond your own ideation, research, and development capabilities for solutions, you must expect that others will look to your solutions for ideas to borrow.

The open innovation model is far easier to describe in idealistic terms than it is to put into practice without ethical consequences. Unfortunately, industrial and corporate espionage, theft of intellectual property, and lawsuits are commonplace. Nevertheless, inspiration in innovation can come from myriad sources when

5 Michelle Ferrier. "Ideation." *Media Innovation and Entrepreneurship*. n.d. https://press.rebus.community/media-innovation-and-entrepreneurship/chapter/ideation-2/
6 Henry Chesbrough. "Everything You Need to Know about Open Innovation." *Forbes*. March 21, 2011. https://www.forbes.com/sites/henrychesbrough/2011/03/21/everything-you-need-to-know-about-open-innovation/#1861dd5275f4

constant streams of information are available to anyone with a high-speed data connection. Open innovation is a simple but essential framework for future innovation and for managing, even possibly guiding, disruption in an industry as discussed previously (i.e., disruptive innovation). Table 4.1 provides some examples of companies using disruptive technology.

Examples of Disruptive Technology

Company	Disruptive technology
Amazon	Speed based delivery Multiple delivery processes from drones to strategically located fulfillment centers Disruptive technology including processing the customer order before the customer has even finished the purchase, so that the product is already moving toward delivery
Uber and Lyft	Ride sharing versus taxi driving Apps and Beacon and Amp-color coded alert communication system disrupted the taxi system
Bitcoin	Digital currency not connected to a specific country or monetary standard Value based on market forces
Toyota E-Palette	Remote controlled driverless electric shuttle that brings the service to the customer rather than the customer going to the service

Table 4.1

Another element of the open innovation model is the connection between academic research and practical solutions. Reciprocal influence between academia, which often moves slowly, and leading corporate and entrepreneurial forces, which often focus too narrowly on short-term gains, could offer the balance this rapidly changing world needs. If you can manage to plug into the exchange of ideas between longstanding institutions and disruptive technological innovators, you may be positioned to effect positive change on society and to develop products that are received as useful and elegant, wildly new and creative, and essential to the human experience at the same time.

Staying on Top of Emerging Practices

Consider searching for ideation and innovation practice links using a web browser and comparing those results to what you can find in the academic literature via Google Scholar or other academic databases. To adopt a truly open innovation mindset, it is essential to leave yourself open to all sorts of influences, even if it demands time and much cognitive energy. The financial, social, and personal rewards may be great.

4.2 Creativity, Innovation, and Invention: How They Differ

Learning Objectives

By the end of this section, you will be able to:

- Distinguish between creativity, innovation, and invention
- Explain the difference between pioneering and incremental innovation, and which processes are best suited to each

One of the key requirements for entrepreneurial success is your ability to develop and offer something unique to the marketplace. Over time, entrepreneurship has become associated with **creativity**, the ability to develop

something original, particularly an idea or a representation of an idea. Innovation requires creativity, but innovation is more specifically the application of creativity. Innovation is the manifestation of creativity into a usable product or service. In the entrepreneurial context, **innovation** is any new idea, process, or product, or a change to an existing product or process that adds value to that existing product or service.

How is an invention different from an innovation? All inventions contain innovations, but not every innovation rises to the level of a unique invention. For our purposes, an **invention** is a truly novel product, service, or process. It will be based on previous ideas and products, but it is such a leap that it is not considered an addition to or a variant of an existing product but something unique. Table 4.2 highlights the differences between these three concepts.

Creativity, Innovation, and Invention

Concept	Description
Creativity	ability to develop something original, particularly an idea or a representation of an idea, with an element of aesthetic flair
Innovation	change that adds value to an existing product or service
Invention	truly novel product, service, or process that, though based on ideas and products that have come before, represents a leap, a creation truly novel and different

Table 4.2

One way we can consider these three concepts is to relate them to design thinking. **Design thinking** is a method to focus the design and development decisions of a product on the needs of the customer, typically involving an empathy-driven process to define complex problems and create solutions that address those problems. Complexity is key to design thinking. Straightforward problems that can be solved with enough money and force do not require much design thinking. Creative design thinking and planning are about finding new solutions for problems with several tricky variables in play. Designing products for human beings, who are complex and sometimes unpredictable, requires design thinking.

Airbnb has become a widely used service all over the world. That has not always been the case, however. In 2009, the company was near failure. The founders were struggling to find a reason for the lack of interest in their properties until they realized that their listings needed professional, high-quality photographs rather than simple cell-phone photos. Using a design thinking approach, the founders traveled to the properties with a rented camera to take some new photographs. As a result of this experiment, weekly revenue doubled. This approach could not be sustainable in the long term, but it generated the outcome the founders needed to better understand the problem. This creative approach to solving a complex problem proved to be a major turning point for the company.[7]

People who are adept at design thinking are creative, innovative, and inventive as they strive to tackle different types of problems. Consider Divya Nag, a millennial biotech and medical device innovation leader, who launched a business after she discovered a creative way to prolong the life of human cells in Petri dishes. Nag's stem-cell research background and her entrepreneurial experience with her medical investment firm made her a popular choice when Apple hired her to run two programs dedicated to developing health-related apps, a position she reached before turning twenty-four years old.[8]

7 "How Design Thinking Transformed Airbnb from Failing Startup to Billion Dollar Business." *First Round Review*. n.d. https://firstround.com/review/How-design-thinking-transformed-Airbnb-from-failing-startup-to-billion-dollar-business/
8 "Divya Nag, 26." *Fortune*. n.d. http://fortune.com/40-under-40/2017/divya-nag-27/

Creativity, innovation, inventiveness, and entrepreneurship can be tightly linked. It is possible for one person to model all these traits to some degree. Additionally, you can develop your creativity skills, sense of innovation, and inventiveness in a variety of ways. In this section, we'll discuss each of the key terms and how they relate to the entrepreneurial spirit.

Creativity

Entrepreneurial creativity and artistic creativity are not so different. You can find inspiration in your favorite books, songs, and paintings, and you also can take inspiration from existing products and services. You can find creative inspiration in nature, in conversations with other creative minds, and through formal ideation exercises, for example, brainstorming. **Ideation** is the purposeful process of opening up your mind to new trains of thought that branch out in all directions from a stated purpose or problem. **Brainstorming**, the generation of ideas in an environment free of judgment or dissension with the goal of creating solutions, is just one of dozens of methods for coming up with new ideas.[9]

You can benefit from setting aside time for ideation. Reserving time to let your mind roam freely as you think about an issue or problem from multiple directions is a necessary component of the process. Ideation takes time and a deliberate effort to move beyond your habitual thought patterns. If you consciously set aside time for creativity, you will broaden your mental horizons and allow yourself to change and grow.[10]

Entrepreneurs work with two types of thinking. **Linear thinking**—sometimes called vertical thinking—involves a logical, step-by-step process. In contrast, creative thinking is more often **lateral thinking**, free and open thinking in which established patterns of logical thought are purposefully ignored or even challenged. You can ignore logic; anything becomes possible. Linear thinking is crucial in turning your idea into a business. Lateral thinking will allow you to use your creativity to solve problems that arise. Figure 4.5 summarizes linear and lateral thinking.

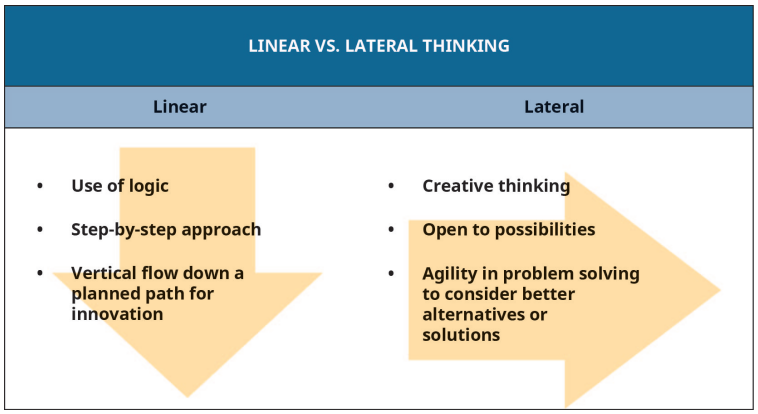


Figure 4.5 Entrepreneurs can be most effective if they use both linear and lateral thinking. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

9 Rikke Dam and Teo Siang. "Introduction to the Essential Ideation Techniques Which Are the Heart of Design Thinking." *Interaction Design Foundation*. April 2019. https://www.interaction-design.org/literature/article/introduction-to-the-essential-ideation-techniques-which-are-the-heart-of-design-thinking

10 Dawn Kelly and Terry L. Amburgey. "Organizational Inertia and Momentum: A Dynamic Model of Strategic Change." *Academy of Management Journal* 34, no. 3 (1991): 591–612.

It is certainly possible for you to be an entrepreneur and focus on linear thinking. Many viable business ventures flow logically and directly from existing products and services. However, for various reasons, creativity and lateral thinking are emphasized in many contemporary contexts in the study of entrepreneurship. Some reasons for this are increased global competition, the speed of technological change, and the complexity of trade and communication systems.[11] These factors help explain not just why creativity is emphasized in entrepreneurial circles but also why creativity should be emphasized. Product developers of the twenty-first century are expected to do more than simply push products and innovations a step further down a planned path. Newer generations of entrepreneurs are expected to be path breakers in new products, services, and processes.

Examples of creativity are all around us. They come in the forms of fine art and writing, or in graffiti and viral videos, or in new products, services, ideas, and processes. In practice, creativity is incredibly broad. It is all around us whenever or wherever people strive to solve a problem, large or small, practical or impractical.

Innovation

We previously defined innovation as a change that adds value to an existing product or service. According to the management thinker and author Peter Drucker, the key point about innovation is that it is a response to both changes within markets and changes from outside markets. For Drucker, classical entrepreneurship psychology highlights the purposeful nature of innovation.[12] Business firms and other organizations can plan to innovate by applying either lateral or linear thinking methods, or both. In other words, not all innovation is purely creative. If a firm wishes to innovate a current product, what will likely matter more to that firm is the success of the innovation rather than the level of creativity involved. Drucker summarized the sources of innovation into seven categories, as outlined in Table 4.3. Firms and individuals can innovate by seeking out and developing changes within markets or by focusing on and cultivating creativity. Firms and individuals should be on the lookout for opportunities to innovate.[13]

Drucker's Seven Sources of Innovation[14]

Source	Description
The unexpected	Looking for new opportunities in the market; unexpected product performance; unexpected new products as examples
The incongruity	Discrepancies between what you think should be and what is reality
Process need	Weaknesses in the organization, product, or service
Changes in industry/market	New regulations; new technologies
Demographics	Understanding needs and wants of target markets
Changes in perceptions	Changes in perceptions of life events and values
New knowledge	New technologies; advancements in thinking; new research

Table 4.3

11 Ian Fillis and Ruth Rentschler. "The Role of Creativity in Entrepreneurship." *Journal of Enterprising Culture* 18, no. 1 (2010): 49–81.
12 P. F. Drucker. *Innovation and Entrepreneurship: Practices and Principles.* New York: Harper & Row Publishers, 1986.
13 P. F. Drucker. *Innovation and Entrepreneurship: Practices and Principles.* (New York: Harper & Row Publishers, 1986), 35.
14 P. F. Drucker. *Innovation and Entrepreneurship: Practices and Principles.* New York: Harper & Row Publishers, 1986.

One innovation that demonstrates several of Drucker's sources is the use of cashier kiosks in fast-food restaurants. McDonald's was one of the first to launch these self-serve kiosks. Historically, the company has focused on operational efficiencies (doing more/better with less). In response to changes in the market, changes in demographics, and process need, McDonald's incorporated self-serve cashier stations into their stores. These kiosks address the need of younger generations to interact more with technology and gives customers faster service in most cases.[15]

Another leading expert on innovation, Tony Ulwick, focuses on understanding how the customer will judge or evaluate the quality and value of the product. The product development process should be based on the metrics that customers use to judge products, so that innovation can address those metrics and develop the best product for meeting customers' needs when it hits the market. This process is very similar to Drucker's contention that innovation comes as a response to changes within and outside of the market. Ulwick insists that focusing on the customer should begin early in the development process.[16]

Disruptive innovation is a process that significantly affects the market by making a product or service more affordable and/or accessible, so that it will be available to a much larger audience. Clay Christensen of Harvard University coined this term in the 1990s to emphasize the process nature of innovation. For Christensen, the innovative component is not the actual product or service, but the process that makes that product more available to a larger population of users. He has since published a good deal on the topic of disruptive innovation, focusing on small players in a market. Christensen theorizes that a disruptive innovation from a smaller company can threaten an existing larger business by offering the market new and improved solutions. The smaller company causes the disruption when it captures some of the market share from the larger organization.[17],[18] One example of a disruptive innovation is Uber and its impact on the taxicab industry. Uber's innovative service, which targets customers who might otherwise take a cab, has shaped the industry as whole by offering an alternative that some deem superior to the typical cab ride.

One key to innovation within a given market space is to look for pain points, particularly in existing products that fail to work as well as users expect them to. A **pain point** is a problem that people have with a product or service that might be addressed by creating a modified version that solves the problem more efficiently.[19] For example, you might be interested in whether a local retail store carries a specific item without actually going there to check. Most retailers now have a feature on their websites that allows you to determine whether the product (and often how many units) is available at a specific store. This eliminates the need to go to the location only to find that they are out of your favorite product. Once a pain point is identified in a firm's own product or in a competitor's product, the firm can bring creativity to bear in finding and testing solutions that sidestep or eliminate the pain, making the innovation marketable. This is one example of an **incremental innovation**, an innovation that modifies an existing product or service.[20]

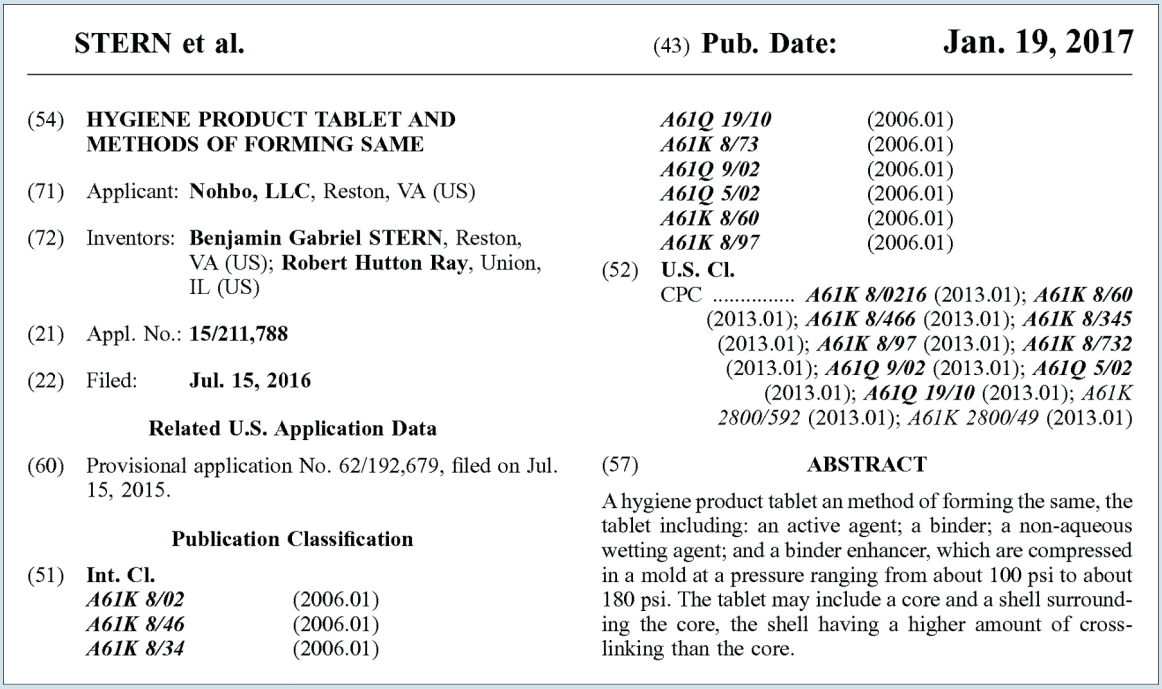
In contrast, a **pioneering innovation** is one based on a new technology, a new advancement in the field, and/or an advancement in a related field that leads to the development of a new product.[21] Firms offering similar products and services can undertake pioneering innovations, but pioneering the new product requires opening up new market space and taking major risks.

15 Blake Morgan. "5 Fresh Examples of Customer Service Innovation." *Forbes*. July 17, 2017. https://www.forbes.com/sites/blakemorgan/2017/07/17/5-fresh-examples-of-customer-experience-innovation/#3ae5a46e5c18
16 Tony Ulwick. "Reinventing Innovation for 25 Years." *Strategyn*. n.d. https://strategyn.com/tony-ulwick/
17 Chris Larson. "Disruptive Innovation Theory: What It Is & 4 Key Concepts." *Harvard Business School*. November 15, 2016. https://online.hbs.edu/blog/post/4-keys-to-understanding-clayton-christensens-theory-of-disruptive-innovation
18 Rosamond Hutt. "What Is Disruptive Innovation?" *World Economic Forum*. June 25, 2016. https://www.weforum.org/agenda/2016/06/what-is-disruptive-innovation/
19 Lloyd Waldo. "What's a Pain Point? A Guide for Startups." *StartupYard Seed Accelerator*. December 1, 2016. https://startupyard.com/whats-pain-point/
20 Abdul Ali, Manohar U. Kalwani, and Dan Kovenock. "Selecting Product Development Projects: Pioneering versus Incremental Innovation Strategies." *Management Science* 39, no. 3 (1993): 255–274.
21 Abdul Ali. "Pioneering versus Incremental Innovation: Review and Research Propositions." *Journal of Product Innovation Management* 11, no. 1 (1994): 46–61.

ENTREPRENEUR IN ACTION

Pioneering Innovation in the Personal Care Industry

In his ninth-grade biology class, Benjamin Stern came up with an idea to change the personal care industry. He envisioned personal cleaning products (soap, shampoo, etc.) that would contain no harsh chemicals or sulfates, and would also produce no plastic waste from empty bottles. He developed Nohbo Drops, single-use personal cleansing products with water-soluble packaging. Stern was able to borrow money from family and friends, and use some of his college fund to hire a chemist to develop the product. He then appeared on *Shark Tank* with his innovation in 2016 and secured the backing of investor Mark Cuban. Stern assembled a research team to perfect the product and obtained a patent (Figure 4.6). The products are now available via the company website.



STERN et al. (43) **Pub. Date: Jan. 19, 2017**

(54) **HYGIENE PRODUCT TABLET AND METHODS OF FORMING SAME**

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(57) **ABSTRACT**

A hygiene product tablet an method of forming the same, the tablet including: an active agent; a binder; a non-aqueous wetting agent; and a binder enhancer, which are compressed in a mold at a pressure ranging from about 100 psi to about 180 psi. The tablet may include a core and a shell surrounding the core, the shell having a higher amount of cross-linking than the core.

Figure 4.6 This is part of the patent application for Nohbo drops. (credit: modification of "US Patent US20170014313A1" by Nohbo LLC/Google Patents, Public Domain)

Is a pioneering innovation an invention? A firm makes a pioneering innovation when it creates a product or service arising from what it has done before. Pokémon GO is a great example of pioneering innovation. Nintendo was struggling to keep pace with other gaming-related companies. The company, in keeping with its core business of video games, came up with a new direction for the gaming industry. Pokémon GO is known worldwide and is one of the most successful mobile games launched.[22] It takes creativity to explore a new direction, but not every pioneering innovation creates a distinctly new product or capability for consumers and clients.

Entrepreneurs in the process of developing an innovation usually examine the current products and services their firm offers, investigate new technologies and techniques being introduced in the marketplace or in related marketplaces, watch research and development in universities and in other companies, and pursue new developments that are likely to fit one of two conditions: an innovation that likely fits an existing market better than other products or services being offered; or an innovation that fits a market that so far has been underserved.

22 JV Chamary. "Why 'Pokémon GO' Is the World's Most Important Game." *Forbes*. February 10, 2018. https://www.forbes.com/sites/jvchamary/2018/02/10/pokemon-go-science-health-benefits/#2b6f07fd3ab0

An example of an incremental innovation is the trash receptacle you find at fast-food restaurants. For many years, trash cans in fast-food locations were placed in boxes behind swinging doors. The trash cans did one job well: They hid the garbage from sight. But they created other problems: Often, the swinging doors would get ketchup and other waste on them, surely a pain point. Newer trash receptacles in fast-food restaurants have open fronts or open tops that enable people to dispose of their trash more neatly. The downside for restaurants is that users can see and possibly smell the food waste, but if the restaurants change the trash bags frequently, as is a good practice anyway, this innovation works relatively well. You might not think twice about this everyday example of an innovation when you eat at a fast-food restaurant, but even small improvements can matter a lot, particularly if the market they serve is vast.

Invention

An invention is a leap in capability beyond innovation. Some inventions combine several innovations into something new. Invention certainly requires creativity, but it goes beyond coming up with new ideas, combinations of thought, or variations on a theme. Inventors build. Developing something users and customers view as an invention could be important to some entrepreneurs, because when a new product or service is viewed as unique, it can create new markets. True inventiveness is often recognized in the marketplace, and it can help build a valuable reputation and help establish market position if the company can build a future-oriented corporate narrative around the invention.[23]

Besides establishing a new market position, a true invention can have a social and cultural impact. At the social level, a new invention can influence the ways institutions work. For example, the invention of desktop computing put accounting and word processing into the hands of nearly every office worker. The ripple effects spread to the school systems that educate and train the corporate workforce. Not long after the spread of desktop computing, workers were expected to draft reports, run financial projections, and make appealing presentations. Specializations or aspects of specialized jobs—such as typist, bookkeeper, corporate copywriter—became necessary for almost everyone headed for corporate work. Colleges and eventually high schools saw software training as essential for students of almost all skill levels. These additional capabilities added profitability and efficiencies, but they also have increased job requirements for the average professional.

Some of the most successful inventions contain a mix of familiarity and innovation that is difficult to achieve. With this mix, the rate of adoption can be accelerated because of the familiarity with the concept or certain aspects of the product or service. As an example, the “videophone” was a concept that began to be explored as early as the late 1800s. AT&T began extensive work on videophones during the 1920s. However, the invention was not adopted because of a lack of familiarity with the idea of seeing someone on a screen and communicating back and forth. Other factors included societal norms, size of the machine, and cost. It wasn’t until the early 2000s that the invention started to take hold in the marketplace.[24] The concept of a black box is that activities are performed in a somewhat mysterious and ambiguous manner, with a serendipitous set of actions connecting that result in a surprisingly beneficial manner. An example is Febreeze, a chemical combination that binds molecules to eliminate odors. From a black box perspective, the chemical engineers did not intend to create this product, but as they were working on creating another product, someone noticed that the product they were working on removed odors, thus inadvertently creating a successful new product marketed as Febreeze.

23 Morten Thanning Vendelø. “Narrating Corporate Reputation: Becoming Legitimate through Storytelling.” *International Studies of Management & Organization* 28, no. 3 (1998): 120–137.
24 Thomas J. Fitzgerald. “For the Deaf: Communication without the Wait.” *The New York Times.* December 18, 2003. https://www.nytimes.com/2003/12/18/technology/for-the-deaf-communication-without-the-wait.html

WHAT CAN YOU DO?

Did Henry Ford Invent the Assembly Line?

Very few products or procedures are actually brand-new ideas. Most new products are alterations or new applications of existing products, with some type of twist in design, function, portability, or use. Henry Ford is usually credited with inventing the moving assembly line Figure 4.7**(a)** in 1913. However, some 800 years before Henry Ford, wooden ships were mass produced in the northern Italian city of Venice in a system that anticipated the modern assembly line.

Various components (ropes, sails, and so on) were prefabricated in different parts of the Venetian Arsenal, a huge, complex construction site along one of Venice's canals. The parts were then delivered to specific assembly points Figure 4.7**(b)**. After each stage of construction, the ships were floated down the canal to the next assembly area, where the next sets of workers and parts were waiting. Moving the ships down the waterway and assembling them in stages increased speed and efficiency to the point that long before the Industrial Revolution, the Arsenal could produce one fully functional and completely equipped ship *per day*. The system was so successful that it was used from the thirteenth century to about 1800.

Henry Ford did not invent anything new—he only applied the 800-year-old process of building wooden ships by hand along a moving waterway to making metal cars by hand on a moving conveyor (Figure 4.7).

(a) **(b)**

Figure 4.7 (a) Workers assemble car parts on an early Ford factory assembly line. (b) The Venetian Arsenal was an early "assembly line" where workers could build a complete ship in a single day. (credit (a): modification of "Ford assembly line – 1913" by "Hohum"/Wikimedia Commons, Public Domain; credit (b): modification of "venice-arsenal-italy" by "irenetriches1"/Pixabay, CC0)

Opportunities to bring new products and processes to market are in front of us every day. The key is having the ability to recognize them and implement them. Likewise, the people you need to help you be successful may be right in front of you on a regular basis. The key is having the ability to recognize who they are and making connections to them. Just as those ships and cars moved down an assembly line until they were ready to be put into service, start thinking about moving down the "who I know" line so that you will eventually have a successful business in place.

The process of invention is difficult to codify because not all inventions or inventors follow the same path. Often the path can take multiple directions, involve many people besides the inventor, and encompass many restarts. Inventors and their teams develop their own processes along with their own products, and the field in which an inventor works will greatly influence the modes and pace of invention. Elon Musk is famous for founding four different billion-dollar companies. The development processes for PayPal, Solar City, SpaceX, and Tesla differed widely; however, Musk does outline a six-step decision-making process (Figure 4.8):

1. Ask a question.
2. Gather as much evidence as possible about it.
3. Develop axioms based on the evidence and try to assign a probability of truth to each one.
4. Draw a conclusion in order to determine: Are these axioms correct, are they relevant, do they necessarily lead to this conclusion, and with what probability?
5. Attempt to disprove the conclusion. Seek refutation from others to further help break your conclusion.
6. If nobody can invalidate your conclusion, then you're *probably* right, but you're not *certainly* right.

In other words, the constant underlying Musk's decision process is the scientific method.[25] The **scientific method**, most often associated with the natural sciences, outlines the process of discovering an answer to a question or a problem. "The scientific method is a logical organization of steps that scientists use to make deductions about the world around us."[26] The steps in the scientific method line up quite nicely with Musk's decision-making process. Applying the scientific method to invention and innovation makes sense. The scientific method involves becoming aware of a problem, collecting data about it by observing and experimenting, and coming up with suggestions on how to solve it.

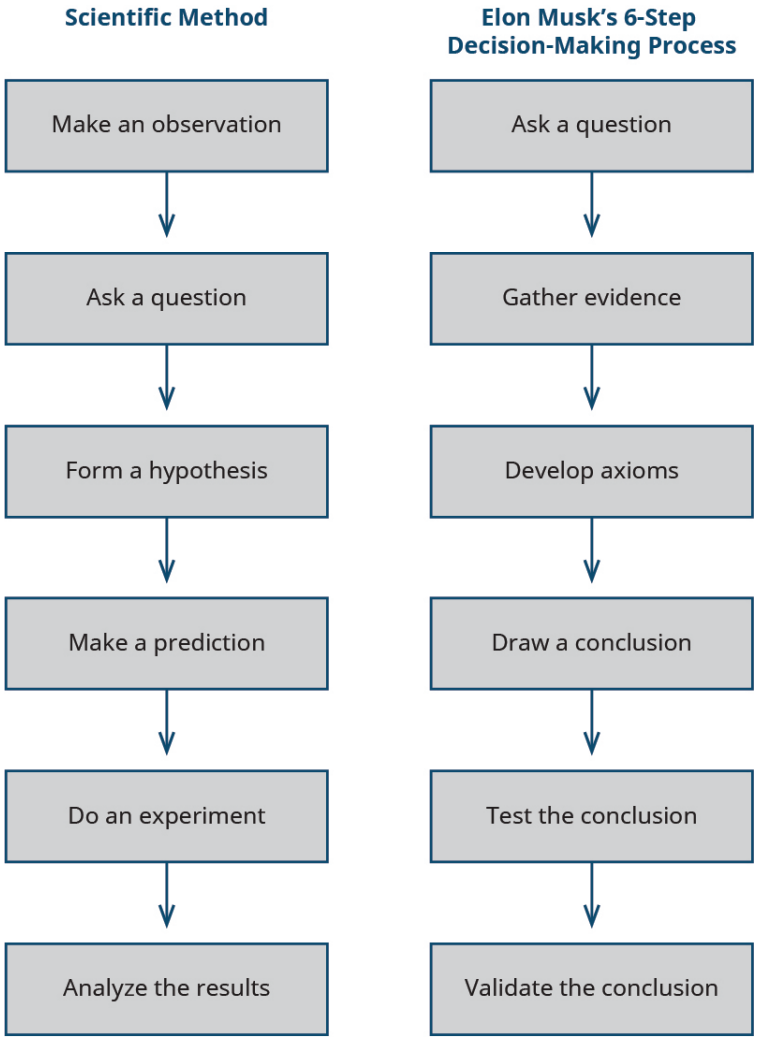


Figure 4.8 Elon Musk's six-step decision making process follows a sequence of steps similar to the scientific method. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

25 Abby Jackson. "Elon Musk Uses This 6-Step Process to Make Decisions." *Business Insider*. November 16, 2017. https://www.inc.com/business-insider/how-elon-musk-makes-decisions-rolling-stone.html
26 Joan Whetzel. "Formula for Using the Scientific Method." *Owlcation*. February 11, 2017. https://owlcation.com/academia/FormulaForUsingScientificMethod

Economists argue that processes of invention can be explained by economic forces. But this hasn't always been the case. Prior to 1940, economic theory focused very little on inventions. After World War II, much of the global economy in the developed world needed to be rebuilt. New technologies were developing rapidly, and research and development investment increased. Inventors and economists alike became aware of consumer demand and realized that demand can influence which inventions take off at a given time.[27] However, inventors are always up against an adoption curve.[28]

The Rogers Adoption Curve was popularized through the research and publications of the author and scientist Everett Rogers.[29] He first used it to describe how agricultural innovations diffused (or failed to) in a society. It was later applied to all inventions and innovations. This curve illustrates diffusion of an innovation and when certain people will adopt it. First is the question of who adopts inventions and innovations in society: The main groups are innovators, early adopters, early and late-majority adopters, and "laggards" (Rogers's own term).[30] The innovators are the ones willing to take a risk on a new product, the consumers who want to try it first. The early adopters are consumers who will adopt new inventions with little to no information. Majority adopters will adopt products after being accepted by the majority. And finally, laggards are often not willing to readily adopt change and are the hardest to convince to try a new invention.[31]

Rogers's second way of looking at the concept is from the point of view of the invention itself. A given population partially or completely adopts an invention or rejects it. If an invention is targeted at the wrong population or the wrong population segment, this can dramatically inhibit its chances of being adopted widely. The most critical point of adoption often occurs at the end of the early adoption phase, before the early majority steps in and truly confirms (or not) the diffusion of an invention. This is called the **diffusion chasm** (though this process is usually called the *diffusion of innovations*, for our purposes, it applies quite well to new inventions as we define them here).

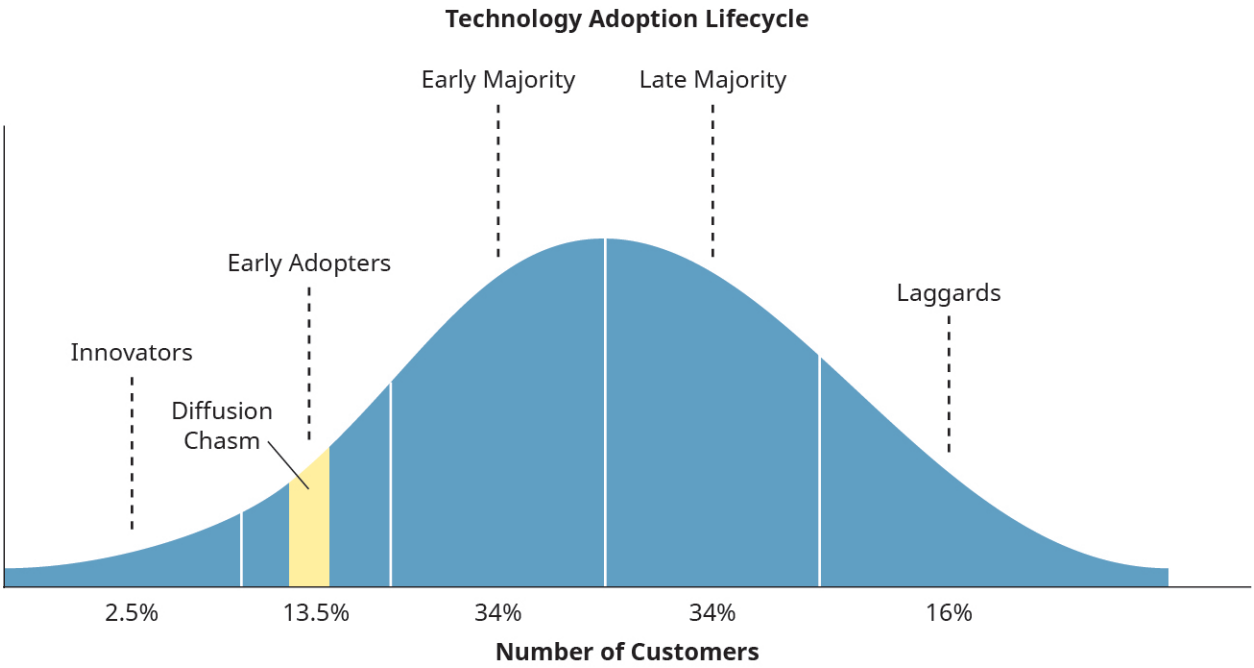


Figure 4.9 The diffusion curve shows the adoption lifecycle according to the research of Everett Rogers. The diffusion chasm occurs during early adoption. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

27 N. Rosenberg. "Science, Invention and Economic Growth." *The Economic Journal* 84, no. 333 (1974): 90–108.
28 Everett M. Rogers. *Diffusion of Innovations*, 5th ed. New York: Simon and Schuster, 2010.
29 John-Pierre Maeli. "The Rogers Adoption Curve & How You Spread New Ideas Throughout Culture." *The Political Informer*. May 6, 2016. https://medium.com/the-political-informer/the-rogers-adoption-curve-how-you-spread-new-ideas-throughout-culture-d848462fcd24
30 Everett M. Rogers. *Diffusion of Innovations*, 5th ed. New York: Simon and Schuster, 2010.
31 Wayne W. LaMorte. "Diffusion of Innovation Theory." September 9, 2019. http://sphweb.bumc.bu.edu/otlt/MPH-Modules/SB/BehavioralChangeTheories/BehavioralChangeTheories4.html

The diffusion curve depicts a social process in which the value of an invention is perceived (or not) to be worth the cost (Figure 4.9). Early adopters generally pay more than those who wait, but if the invention gives them a perceived practical, social, or cultural advantage, members of the population, the popularity of the invention itself, and marketing can all drive the invention over the diffusion chasm. Once the early majority adopts an innovation (in very large numbers), we can expect the rest of the majority to adopt it. By the time the late majority and the laggards adopt an innovation, the novelty has worn off, but the practical benefits of the innovation can still be felt.

Inventors are constantly trying to cross the diffusion chasm, often with many products at a time. Crossing the diffusion chasm is a nearly constant concern for business-focused or outcomes-focused inventors. Inventors put many of their resources into an invention during the innovation and early adoption stages. Inventions may not turn a profit for investors or the inventors themselves until they are well into the early majority stage of adoption. Some inventors are pleased to work toward general discovery, but most in today's social and cultural context are working to develop products and services for markets.

One shortcoming of the diffusion of innovations model is that it treats inventions and innovations as though they are finished and complete, though many are not. Not all inventions are finished products ready for market. Iterative development is more common, particularly in fields with high levels of complexity and in service-oriented ventures. In the **iterative development** process, inventors and innovators continuously engage with potential customers in order to develop their products and their consumer bases at the same time. This model of business learning, also known as the science of customer development, is essential.[32] Business learning involves testing product-market fit and making changes to an innovation or invention many times over until either investment funding runs out or the product succeeds. Perhaps the most accurate way to summarize this process is to note that many inventions are hit-or-miss prospects that get only a few chances to cross the diffusion chasm. When innovators follow the build-measure-learn model (discussed in detail in Launch for Growth to Success), they try to work their way across the diffusion chasm rather than making a leap of faith.

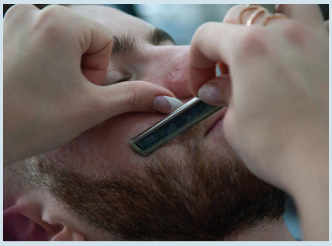
WORK IT OUT

Razors

The safety razor was an innovation over the straight razor. Safety razor blades are small enough to fit inside a capsule, and the location and type of handle was altered to suit the new orientation of handle to blade (Figure 4.10). Most contemporary razors are themselves innovations on the safety razor, whether they have two, three, four, or more blades. The method of changing razor blades has evolved with each innovation on the safety razor, but the designs are functionally similar.

The electric razor is a related invention. It still uses blades to shave hair off the face or body, but the blades are hidden beneath a foil or foils. Hairs poke through the foils when the razor is pressed against the skin, and blades moving in various directions cut the hairs. Although electric razors use blades as do mechanical razors, the new design and the added technology qualified the electric razor as an invention that offered something new in the shaving industry when Jacob Schick won the patent for a shaving machine in 1930.[33] Still other innovations in the shaving genre include gender-specific razors, beard trimmers, and, more recently, online clubs such as Dollar Shave Club and Harry's Shave Club.

32 Eric Ries. *The Lean Startup: How Today's Entrepreneurs Use Continuous Innovation to Create Radically Successful Businesses.* Largo, Maryland: Crown Books, 2011.
33 "Jacob Schick Invents the Electric Razor." *Connecticut History*. May 13, 2017. https://connecticuthistory.org/jacob-schick-invents-the-electric-razor/


(a)

(b)

(c)

Figure 4.10 (a) The straight razor is still in use, but there are newer innovations that are more popular. (b) The safety razor is an innovation over the straight razor. (c) The electric razor is an innovation related to the safety razor. (credit (a): modification of "barber-beard-razor-shaving" by "jackmac34"/Pixabay, CC0; credit (b): modification of "Safety Razor vs Cartridge Razor" by "Tools of Men"/Creative Commons, CC BY 2.0; credit (c): modification of "Philips 8290 shaver unboxing" by "renaissancechambara"/Creative Commons, CC BY 2.0)

Think about the conceptual difference between innovation and invention. Is the safety razor a pioneering innovation or an incremental one? What makes the electric razor an invention, as we define it here? What makes it stand out as a leap from previous types of razors? Do you think the electric razor is a "sure thing"? Why or why not? Consider the availability of electricity at the time the first electric razors were being made. Why do you think the electric razor made it over the diffusion chasm between early adopters and early majority adopters? Do you think the electric razor was invented iteratively with small changes to the same product in response to customer preferences? Or did it develop in a series of black box inventions, with each one either diffusing or not?

4.3 Developing Ideas, Innovations, and Inventions

Learning Objectives

By the end of this section, you will be able to:

- Describe and apply the five stages of creativity
- Discuss innovation as a system for problem solving and much more
- Outline the sequence of steps in developing an invention

The previous section defined creativity, innovation, and invention, and provided examples. You might think of creativity as raw; innovation as transforming creativity into a functional purpose, often meant to eradicate a pain point or to fulfill a need; and invention as a creation that leaves a lasting impact. In this section, you will learn about processes designed to help you apply knowledge from the previous section.

The Creative Process: The Five Stages of Creativity

Raw creativity and an affinity for lateral thinking may be innate, but creative people must refine these skills in order to become masters in their respective fields. They practice in order to apply their skills readily and consistently, and to integrate them with other thought processes and emotions. Anyone can improve in creative efforts with practice. For our purposes, practice is a model for applied creativity that is derived from an entrepreneurial approach (Figure 4.11).[34] It requires:

1. Preparation
2. Incubation
3. Insight
4. Evaluation
5. Elaboration

34 Aleza D'Agostino. "5 Stages of the Creative Process with James Taylor." *CreativeLive*. December 28, 2015. https://www.creativelive.com/blog/5-stages-of-the-creative-process-with-james-taylor/

Figure 4.11 These are the five stages of creativity, according to Graham Wallas in *The Art of Thought*.[35] (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Preparation

Preparation involves investigating a chosen field of interest, opening your mind, and becoming immersed in materials, mindset, and meaning. If you have ever tried to produce something creative without first absorbing relevant information and observing skilled practitioners at work, then you understand how difficult it is. This base of knowledge and experience mixed with an ability to integrate new thoughts and practices can help you sift through the ideas quicker. However, relying too heavily on prior knowledge can restrict the creative process. When you immerse yourself in a creative practice, you make use of the products or the materials of others' creativity. For example, a video-game designer plays different types of video games on different consoles, computers, and online in networks. They may play alone, with friends in collaboration, or in competition. Consuming the products in a field gives you a sense of what is possible and indicates boundaries that you may attempt to push with your own creative work. Preparation broadens your mind and lets you study the products, practice, and culture in a field. It is also a time for goal setting. Whether your chosen field is directly related to art and design, such as publishing, or involves human-centric design, which includes all sorts of software and product design efforts, you need a period of open-minded reception to ideas. Repetitive practice is also part of the preparation stage, so that you can understand the current field of production and become aware of best practices, whether or not you are currently capable of matching them. During the preparation stage, you can begin to see how other creative people put meaning into their products, and you can establish benchmarks against which to measure your own creative work.

Incubation

Incubation refers to giving yourself, and your subconscious mind in particular, time to incorporate what you learned and practiced in the preparation stage. Incubation involves the absence of practice. It may look to an outsider as though you are at rest, but your mind is at work. A change of environment is key to incubating ideas.[36] A new environment allows you to receive stimuli other than those directly associated with the creative problem you are working on. It could be as simple as taking a walk or going to a new coffee shop to allow your mind to wander and take in the information you gathered in the previous stage. Mozart stated, "When I am, as it were, completely myself, entirely alone, and of good cheer—say, traveling in a carriage, or walking after a good meal, or during the night when I cannot sleep; it is on such occasions that my ideas flow best and most abundantly."[37] Incubation allows your mind to integrate your creative problem with your stored memories and with other thoughts or emotions you might have. This simply is not possible to do when you are consciously fixated on the creative problem and related tasks and practice.

Incubation can take a short or a long time, and you can perform other activities while allowing this process to take place. One theory about incubation is that it takes language out of the thought process. If you are not working to apply words to your creative problems and interests, you can free your mind to make associations that go deeper, so to speak, than language.[38] Patiently waiting for incubation to work is quite difficult. Many creative and innovative people develop hobbies involving physical activity to keep their minds busy while they allow ideas to incubate.

35 Eugene Sadler-Smith. "Wallas' Four-Stage Model of the Creative Process: More Than Meets the Eye?" *Creativity Research Journal* 27, no. 4 (2015): 342–352.
36 Eugene Sadler-Smith. "Wallas' Four-Stage Model of the Creative Process: More Than Meets the Eye?" *Creativity Research Journal* 27, no. 4 (2015): 342–352.
37 Neal Zaslaw, "Mozart As a Working Stiff," in James M. Morris, ed., *On Mozart* (Cambridge: Cambridge University Press, 1994), 109.
38 Steven M. Smith, Thomas B. Ward, and Ronald A. Finke, eds., *The Creative Cognition Approach*. Cambridge, MA: MIT Press, 1995.

Insight

Insight or "illumination" is a term for the "aha!" moment—when the solution to a creative problem suddenly becomes readily accessible to your conscious mind. The "aha!" moment has been observed in literature, in history, and in cognitive studies of creativity.[39] Insights may come all at once or in increments. They are not easily understood because, by their very nature, they are difficult to isolate in research and experimental settings. For the creative entrepreneur, however, insights are a delight. An insight is the fleeting time when your preparation, practice, and period of incubation coalesce into a stroke of genius. Whether the illumination is the solution to a seemingly impossible problem or the creation of a particularly clever melody or turn of phrase, creative people often consider it a highlight in their lives. For an entrepreneur, an insight holds the promise of success and the potential to help massive numbers of people overcome a pain point or problem. Not every insight will have a global impact, but coming up with a solution that your subconscious mind has been working on for some time is a real joy.

Evaluation

Evaluation is the purposeful examination of ideas. You will want to compare your insights with the products and ideas you encountered during preparation. You also will want to compare your ideas and product prototypes to the goals you set out for yourself during the preparation phase. Creative professionals will often invite others to critique their work at this stage. Because evaluation is specific to the expectations, best practices, and existing product leaders in each field, evaluation can take on many forms. You are looking for assurance that your standards for evaluation are appropriate. Judge yourself fairly, even as you apply strict criteria and the well-developed sense of taste you acquired during the preparation phase. For example, you might choose to interview a few customers in your target demographics for your product or service. The primary objective is to understand the customer perspective and the extent to which your idea aligns with their position.

Elaboration

The last stage in the creative process is *elaboration*, that is, actual production. Elaboration can involve the release of a **minimum viable product (MVP)**. This version of your invention may not be polished or complete, but it should function well enough that you can begin to market it while still elaborating on it in an iterative development process. Elaboration also can involve the development and launch of a prototype, the release of a software beta, or the production of some piece of artistic work for sale. Many consumer-product companies, such as Johnson & Johnson or Procter & Gamble, will establish a small test market to garner feedback and evaluations of new products from actual customers. These insights can give the company valuable information that can help make the product or service as successful as possible.

At this stage what matters most in the entrepreneurial creative process is that the work becomes available to the public so that they have a chance to adopt it.

LINK TO LEARNING

Test marketing can reveal much information about the potential users of a product. Visit the Drive Research site on test markets (https://openstax.org/l/52TestMarkets) for more information.

39 Eugene Sadler-Smith. "Wallas' Four-Stage Model of the Creative Process: More Than Meets the Eye?" *Creativity Research Journal* 27, no. 4 (2015): 342–352.

Innovation as More than Problem Solving

Innovative entrepreneurs are essentially problem solvers, but this level of innovation—identifying a pain point and working to overcome it—is only one in a series of innovative steps. In the influential business publication *Forbes*, the entrepreneur Larry Myler notes that problem solving is inherently reactive.[40] That is, you have to wait for a problem to happen in order to recognize the need to solve the problem. Solving problems is an important part of the practice of innovation, but to elevate the practice and the field, innovators should anticipate problems and strive to prevent them. In many cases, they create systems for continuous improvement, which Myler notes may involve "breaking" previous systems that seem to function perfectly well. Striving for continuous improvement helps innovators stay ahead of market changes. Thus, they have products ready for emerging markets, rather than developing projects that chase change, which can occur constantly in some tech-driven fields. One issue with building a system for constant improvement is that you are in essence creating problems in order to solve them, which goes against established culture in many firms. Innovators look for organizations that can handle purposeful innovation, or they attempt to start them. Some innovators even have the goal of innovating far ahead into the future, beyond current capacities. In order to do this, Myler suggests bringing people of disparate experiential backgrounds with different expertise together. These relationships are not guarantees of successful innovation, but such groups can generate ideas independent of institutional inertia. Thus, innovators are problem solvers but also can work with forms of problem creation and problem imagination. They tackle problems that have yet to exist in order to solve them ahead of time.

Let's examine one multilevel approach to innovation (Figure 4.12). The base is problem solving. The next level up in the pyramid, so to speak, is prevention. The next level is working toward continuous improvement, and at the top of such efforts is creating the capacity to direct the future of your industry or multiple industries so that you can weather disruption in your career or even to create it.

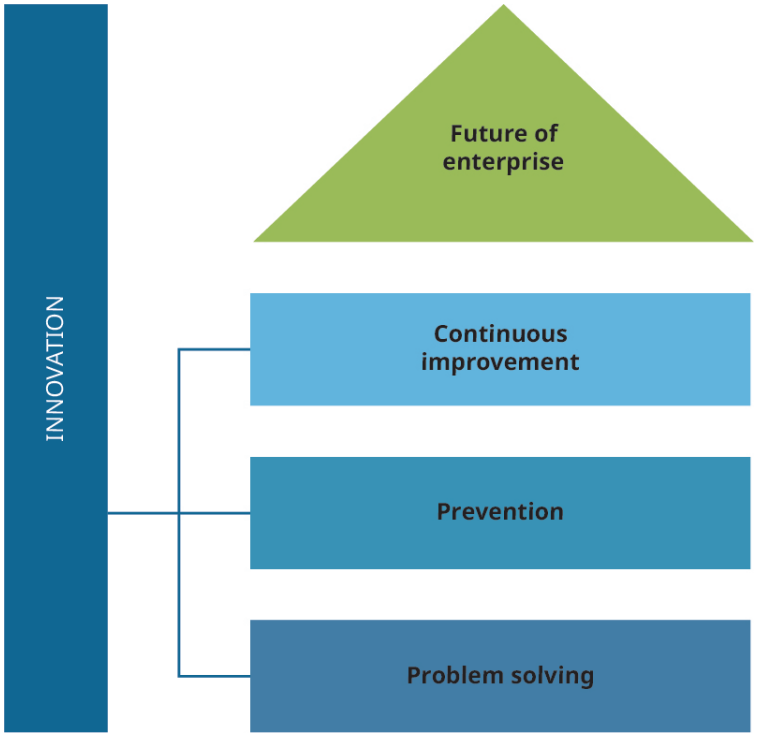


Figure 4.12 The innovation pyramid is one multileveled approach to innovation. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

40 Larry Myler. "Innovation Is Problem Solving . . . And a Whole Lot More." *Forbes.* June 13, 2014. https://www.forbes.com/sites/larrymyler/2014/06/13/innovation-is-problem-solving-and-a-whole-lot-more/#3f11abe533b9

Even if you are not interested in shaping the future of whole industry sectors, developing future-focused innovation practices still is a good idea. It will help you prepare for disruption. The pace of technological change is such that workers at all levels need to be prepared to innovate. Innovation leaders, such as the marketing guru Guy Kawasaki, have built on psychological principles to suggest new ways to approach innovation. According to Kawasaki, innovative products include five key qualities: deep, indulgent, complete, elegant, and emotive—DICEE (Figure 4.13).[41] You can strive to infuse individual innovations with these qualities in practical ways.

Figure 4.13 Innovative products are deep, indulgent, complete, elegant, and emotive. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Deep

Deep products are based on the logic of innovation that we've just established and anticipate users' needs before they have them. These types of innovations often have masterful designs that are intuitive for new users while still being capable of completing complex tasks. Adobe is an innovative corporation working in several fields, such as software, marketing, and artificial intelligence. Adobe often creates software applications with basic functions that are easily accessible to new users but that also enable experienced users to innovate on their own.[42] Creating a platform for innovation is a hallmark of deep, forward-thinking innovation.

Indulgent

Innovations with lasting power engage users in ways that make them feel special for having purchased the product or for having found the service. *Indulgence* refers to a depth of quality that does not come from being the fastest solution to a problem. Indulgence may even sound like a negative trait. In humans, it certainly can be, but for someone using an innovative product, feeling indulgent can relate to a richness of experience with the **user interface** (UI). The UI of a product, particularly a software product, is what the user sees and interacts with. A feeling of indulgence imbues your product with a sense of value and durability that reassures users and encourages them to use your product confidently.

Complete

Kawasaki's vision of a *complete* product includes the services wrapped around it and underlying it such that users understand the product well enough to be comfortable using it. Information about how it works and how it is meant to work is readily available. Thus, product innovation must include marketing and other communication efforts. For Kawasaki, this builds the "total user experience."[43] If you truly have solved a problem in the marketplace, users will understand what that problem is and how your product and related services deliver.

Elegant

Elegance also is part of a product's UI. It refers to intuitive design that immediately makes sense to consumers. Elegance conveys more information with fewer words. Elegant design is not afraid of negative space or of the occasional pause. Elegant innovations solve problems without creating new ones. For Kawasaki, elegance is

41 Guy Kawasaki. "Guy's Golden Touch." *Guy Kawasaki*. January 3, 2006. https://guykawasaki.com/guys_golden_tou/
42 Adobe Communications Team. "Adobe Named One of Fast Company's 'Most Innovative Companies' for AI." *Adobe Blog*. February 20, 2018. https://theblog.adobe.com/adobe-named-one-fast-companys-innovative-companies-ai/
43 Guy Kawasaki. "Guy's Golden Touch." *Guy Kawasaki*. January 3, 2006. https://guykawasaki.com/guys_golden_tou/

the difference between a pragmatic, good innovation and something great.

Emotive

Emotive innovations evoke the intended emotion and demand to be admired and shared. In other words, truly great innovations create fandoms, not just consumer bases. You can't force people to love your product, but you can give them experiences that create a sense of excitement and anticipation of what you might come up with next.

Developing an Invention

The general process of inventing involves systematic and practical steps that might include linear and nonlinear thinking. You might think that only people with innate artistic skills are creative and that only geniuses become innovators and inventors, but much of creativity is driven by being immersed in a practice. You can build and foster your own creativity. Your idea of an inventor might be someone like Johannes Gutenberg, who developed the printing press. The spread of printing ultimately redrew the map of Europe and resulted in the foundation of new centers of learning. Gutenberg's supposed spark actually was more of a slow burn. He was creative and innovative—one of history's most famous inventors—but his printing press, like all other inventions, was a synthesis of existing technologies. Gutenberg's most important innovation was his use of moveable, interchangeable metal type instead of entire hand-carved wooden blocks of text (Figure 4.14). Perfecting his printing process took decades and left him all but broke.[44] The notion of the inventor's single stroke of genius is mostly myth. The people that history remembers usually worked very hard to develop their creativity, to become familiar with the processes and tools that were ripe for innovation in their time, and ultimately to make something so unique that society recognizes it as an invention.

(a) (b)

Figure 4.14 Gutenberg's invention of movable type was an important innovation in printing. (credit (a): modification of "Printer in 1568-ce" by "Parhamr"/Wikimedia Commons, Public Domain; credit (b): modification of "Metal movable type" by Willi Heidelbach/Wikimedia Commons, CC BY 2.5)

The old adage claims that "necessity is the mother of invention," but an innovator needs experience in a field, creative effort, and knowledge to be a successful inventor. Entrepreneurship means taking your efforts and knowledge, and finding a market where your invention can first survive, then thrive.

One model for developing an invention is the first five steps of a plan adapted from Sourcify.com, which specializes in connecting product developers with manufacturers.[45] This process is succinct and includes suggestions for building a team along the way (Figure 4.15).

44 John Man. *The Gutenberg Revolution*. New York: Random House, 2010.

Figure 4.15 These are the five steps for developing an invention, according to Sourcify. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 1: Educate Yourself

Before your inventive product can do battle with other inventions, you will need to educate yourself. To prepare yourself to weather the competition, you need to learn as much as you can about the current investing climate, current product development opportunities, and current leadership approaches. Even if you are not deeply interested in leadership dogma, it helps to know what the current trends are in leadership and product development. To succeed as an inventor in a vast marketplace, you need to understand the rules, written and unwritten, of the industry and competitive landscape. The product development process can be quite involved. The process can vary by industry and by availability of resources.

Part of educating yourself is also gaining an understanding of your own strengths and weaknesses, and how those relate to your leadership style. A leadership style inventory can help you better understand your approach to leading others. This is just one example of many that exist to give you a starting point. As the inventor of your product or service, you will manage/lead others as you attempt to make your idea a reality. Also, the environment can constantly change. For this reason, it is important to understand the basic tenets of leadership and management in a dynamic work atmosphere. Many sources will give you insights into the challenges of management.

LINK TO LEARNING

A leadership style inventory (https://openstax.org/l/52LeadStyleQuiz) can help you understand your leadership style and how to adapt your own style to other situations and people.

Another key step in educating yourself is to find out which kinds of contributors you are going to need to build a successful entrepreneurial team. Building a team is essential to making your invention a reality. Even those who invent alone—and they are quite rare—must have a development team, a manufacturing and/or service team, a marketing team, and other members with specific skill sets such as coders, graphic designers, test marketers, and more.

Step 2: Stay Organized

Most tip sheets for inventors suggest that you find a method for organizing your creativity so that you don't spend time trying to remember previous ideas, plans, and decisions. You must organize information related to your business idea, your business plan, and your potential teammates in the process.

45 Natalie Peters. "9 Key Steps to Bring Your Invention to Life." *Sourcify*. December 11, 2017. https://www.sourcify.com/bring-your-invention-to-life/

Contact management software has been popular for decades. Nowadays, you can investigate many other productivity and team-chat tools. Research ways to organize information about the people you plan to work with and hope to work for. The team-chat program Slack (www.slack.com) enables you to create specific topics for team members to discuss and collaborate on. Slack offers several features to help keep employees connected. Insightly (www.insightly.com) is a customer relationship management tool to stay better connected to your customers. Ryver and Glip incorporate task management. Flock and Microsoft Teams offer a host of features, with Microsoft leveraging its corporate position to bring about deployment in more than 200,000 organizations. Select the tool set that works best for you and consider paying for the software that offers the precise team communication functionality and utility you need.[46]

Step 3: Conduct Market Research

Market research is an obvious must, but many entrepreneurs fail to go as deeply as they should in researching their competition. You must be aware of current and future competitors so that you are prepared to compete in the marketplace when you are actually ready. Being the best on paper now won't be much use when you enter the marketplace with an MVP in six to eight months in competition with competitors' new products and updates.

What should you consider with regard to team development when you're looking at the competition? Within the legal limits of any noncompete clauses, you should be shopping the competition for potential team members. The best leaders are always seeking talented people. If you sense that someone would be a good fit for your team, that they have not only the skill set but also the temperament that would help put your invention in the market, do not be afraid to reach out to them. How you reach out is something you must research for each industry. In some industries, you will have to be highly secretive. Part of market research is understanding the market well enough to understand the soft skills you need to find contributors who are already working in the industry or in an adjacent one

Step 4: Conduct Patent Research

If you expect to apply for a patent, take the time to read up on policies and procedures. Officials in the US Patent Office, or in similar bureaus in other countries, decide whether an invention is worthy of receiving a patent. A patentable invention must meet the criteria of being novel, useful, and nonobvious; it must be proven to be workable.[47] Those three standards—novel, useful, and nonobvious—are subjective. So is the concept of invention, but conceptualizing invention this way sets a high bar for entrepreneurs who truly wish to make a social impact. Developing an invention that is patentable also creates a barrier against competition, which can make the difference between business success and failure. There are two types of patents. *Utility* patents last twenty years, and *design* patents usually last fourteen years. If a patent is granted, the inventor has a window of time in which to secure further funding, work to produce the product, and try to gain mass-market adoption.[48] After all is said and done, you can apply your creativity to social innovations, product innovations, or service innovations. If you can combine enough innovations, add your unique creativity, and create something that survives the diffusion chasm, you can truly invent something new.

46 Aleksey Chepalov. "9 Slack Competitors in 2019: What Team Chat Tools Are Leading the Way?" *Chanty*. March 18, 2019. https://www.chanty.com/blog/slack-competitors/

47 "Patent Subject Matter Eligibility." United States Patent and Trademark Office (USPTO). n.d. https://www.uspto.gov/web/offices/pac/mpep/s2106.html

48 "How Long Does Patent, Trademark, or Copyright Protection Last?" Intellectual Property Rights Information and Assistance. July 7, 2016. https://www.stopfakes.gov/article?id=How-Long-Does-Patent-Trademark-or-Copyright-Protection-Last

The patent basics page of the US Patent and Trademark Office's website is roughly forty pages long.[49] The utility patent process includes a thirteen-step flow chart[50] that outlines the process. The patent office encourages you to use a registered patent attorney or agent. If you are skilled and diligent enough to secure a patent, you should expect to pay fees and file paperwork to maintain it for years after it is granted. We've already discussed the keys to securing a patent, but to reiterate, here is how an invention is defined in US patent law: "In the language of the statute, any person who 'invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof, may obtain a patent,' subject to the conditions and requirements of the law."[51]

When building a team to make your invention a reality, finding a patent lawyer or agent is key. Even those who have advocated for hiring patent attorneys in the past now suggest that hiring a patent agent might work. What's the difference? Patent attorneys often bill by the hour, but they offer a full suite of legal advice. As the author Stephen Key indicates, patent agents are narrowly focused on helping you get and defend your patent.[52] The other limitation that Key mentions is that patent agents may write a patent application in such a way that you are less prepared to protect your invention against future legal challenges. Key quotes Gene Quinn, a leading attorney on intellectual property and patent law: "By the time you realize that you are sitting on a million-dollar invention it will be too late to do anything about it....Patent agents as a general rule tend to be very good at describing what it is that you as an inventor show up with." What they tend to be much less good at is describing what your invention could be. They also frequently will use terms that are more concrete and limiting than would a patent attorney. Attorneys are taught the art of being hyper-specific, which is necessary at times, but also the art of being anything but specific."[53] Patents cannot be vague, but they can be written with just the right amount of specificity to protect against similar products that may arise and threaten your market share.

Step 5: Develop a Prototype

Developing a prototype can be the most fun or the most tedious part of inventing. Much of your attitude toward developing a prototype depends on available resources, technology, and expertise. In this text, we reference the concept of the lean startup from time to time. In the lean startup model, the prototype is most often an MVP. As we saw earlier, an MVP is a version of your invention that may not be polished or complete in terms of how you envisioned it, but it functions well enough and looks good enough that you can begin to market it with reasonable hopes that it will be adopted. For other inventions, you may need to build a more advanced prototype. This requires serious investment capital, but the payoff is that users will interact with a version of the product that looks and functions more like what you had in mind during your ideation phase. As an inventor, you are responsible for establishing quality control minimums for your product. You may have to compromise on your vision, but you should not compromise on basic functionality or basic levels of quality in materials.

49 "General Information Concerning Patents." *United States Patent and Trademark Office*. October 2015. https://www.uspto.gov/patents-getting-started/general-information-concerning-patents
50 "Process for Obtaining a Utility Patent." *United States Patent and Trademark Office*. n.d. https://www.uspto.gov/patents-getting-started/patent-basics/types-patent-applications/utility-patent/process-obtaining
51 "What Can Be Patented" in "General Information Concerning Patents." *United States Patent and Trademark Office*. October 2015. https://www.uspto.gov/patents-getting-started/general-information-concerning-patents#heading-4
52 Stephen Key. "Should You Hire a Patent Agent Instead of a Patent Attorney?" *Inc.* October 26, 2016. https://www.inc.com/stephen-key/should-you-hire-a-patent-agent-instead-of-a-patent-attorney.html
53 "Gene Quinn." *IP Watchdog*. n.d. https://www.ipwatchdog.com/people/gene-quinn-3/

You have many options at the prototype development stage. You can build the prototype yourself or with a small team. You can partner with design/invention firms that specialize in helping inventors create, but you must be very careful and involve your legal representation when working with such firms to be sure that you maintain the patents and other rights to your invention. Many inventors have partnered with such firms only to see their intellectual property stolen. Another option is to get funding for your invention on Kickstarter or some other crowdfunding site, but again you must beware that establishing such a campaign puts your idea in the public sphere. "Copycatters are monitoring crowdfunding platforms like Kickstarter and watching for trendy products to go viral," according to Amedeo Ferraro, an intellectual property attorney.[54] Competing companies, particularly in foreign markets, actively scout Kickstarter and similar platforms for new ideas that they can manufacture and bring to market before your crowdfunding project has run its course. Perhaps most chilling is this comment regarding legal protections that do not function, even when inventors take precautions to protect their intellectual property when working with some Chinese firms: "But even with these protections, there's no guarantee that you can stop someone from copycatting your product. [One U.S. intellectual property lawyer] said that the problem lies not in China's courts but enforcing rulings. Winning a case against one factory is relatively easy. But suing every factory and winning is expensive and time consuming."[55] For this reason, some inventors prefer to start small and local, if possible. It can be better for them to start with a trusted team striving for a small profit and a good market position than to see the market flooded with copycat products.

54 Jennifer Schlesinger, Andrea Day, Bianca Fortis, Eunice Yoon, and Lilian Wu. "How One Entrepreneur's American Dream Turned into a Copycat Nightmare." *CNBC*. April 30, 2019. https://www.cnbc.com/2019/04/30/how-one-entrepreneurs-american-dream-turned-into-a-copycat-nightmare.html

55 Josh Horwitz. "Your Brilliant Kickstarter Idea Could Be on Sale in China before You've Even Finished Funding It." *Quartz*. October 17, 2016. https://qz.com/771727/chinas-factories-in-shenzhen-can-copy-products-at-breakneck-speed-and-its-time-for-the-rest-of-the-world-to-get-over-it/

Key Terms

brainstorming generation of ideas in an environment free of judgment or dissension with the goal of creating solutions
creativity development of original ideas
design thinking method to focus the design and development decisions of a product on the needs of the customer, typically involving an empathy-driven process to define complex problems and create solutions that address those problems
diffusion chasm most critical point of adoption, which often occurs at the end of the early adoption phase, before the early majority steps in and truly confirms (or not) the diffusion of an invention
disruptive innovation process that significantly impacts the market by making a product or service more affordable and/or accessible often by smaller companies in an industry
empathy human ability to feel what other humans are feeling, which in the context of creativity, innovation, and invention is essential to beginning a process of human-centric design
ideation purposeful process of opening up one's mind to new trains of thought that branch out in many directions from a stated purpose or problem
incremental innovation innovation that modifies an existing product or service
innovation new idea, process, or product, or a change to an existing product or process
invention truly novel product, service, or process that, though based on ideas and products that have come before, represents a leap, a creation truly novel and different
iterative development process in which inventors and innovators continuously engage with potential customers in order to develop their products and their consumer bases at the same time
lateral thinking free and open thinking in which established patterns of logical thought are purposefully ignored or even challenged
linear thinking logical, step-by-step process
minimum viable product (MVP) early version or prototype of a product that may not be polished or complete but that functions well enough that you can begin to market it or test it with potential users
open innovation searching for and finding solutions outside of the organizational structure
pain point problem that people have with a product or service that might be addressed by creating a modified version that solves the problem
pioneering innovation one based on a new technology, a new advancement in the field, and/or an advancement in a related field that leads to the development of a new product
scientific method most often associated with the natural sciences, outlines the process to discover an answer to a question or a problem
user interface what the user sees and interacts with

Summary

4.1 Tools for Creativity and Innovation

There are many practical approaches to being creative and developing innovations. Many programs and models encourage creative thinking. Some of the best encourage entrepreneurs to think like the stakeholders they hope their products and services will help. Human-centered design begins with empathizing with the people experiencing a problem or pain point. It continues through steps meant to clearly define problems and examine solutions through careful testing. Returning to empathy is essential in the human-centric design protocol. The Six Thinking Hats method of ideation can open up deep avenues of creative thought directed at solving problems by *limiting* the roles individuals in a group play. This reinforces the idea that creative thinking is a practice, that it can be guided, and that sometimes a combination of open thinking and rule following is ideal for collaborative creativity. The statement starter method of creative thinking frames every problem as though there must be a solution. This type of open thinking is an effective way to begin a creative journey that can lead to innovation and invention of products or services for social benefit.

4.2 Creativity, Innovation, and Invention: How They Differ

Creativity is defined as the ability to develop something original, particularly an idea or an artistic representation of an idea. Innovation occurs when an individual or a firm applies something new to an existing product or service that adds value. Innovation can be planned or spontaneous, incremental or pioneering. Some pioneering innovations rise to the level of being unique inventions—truly novel products, services, or processes that, though based on ideas and products that have come before, represent a leap.

The diffusion curve is related to iterative innovations versus black box innovations. Innovators and inventors conduct the iterative innovation process by engaging with potential consumers on a near-continuous basis in order to develop the product and the consumer base at the same time, thus bridging the diffusion chasm. Black box innovations either jump the chasm or not, depending on the social perceptions through which they are perceived by potential users, the quality of the product itself, and marketing strategies.

4.3 Developing Ideas, Innovations, and Inventions

Whether an entrepreneur has innate creativity or not, practice can help improve creative efforts. One practice model includes preparation, incubation, insight, evaluation, and elaboration. Entrepreneurs can use their creativity to solve problems and innovate. However, innovators strive to anticipate and prevent problems, rather than react to them. The innovation pyramid begins with problem solving at the base, moving up to prevention, then continuous improvement, and finally directing the future of an industry. Innovative products are DICEE: They are deep, indulgent, complete, elegant, and emotive.

Building and fostering your own creativity often involves linear and nonlinear thinking. Models are available that help develop inventions, such as Sourcify.com's five steps: Educate yourself, stay organized, conduct market research, conduct patent research, and develop a prototype. This model has guidelines for working with teams as well. These models allow you to apply your knowledge of creativity, innovation, and invention in an entrepreneurial context. Seek inspiration from inventors who have come before and learn from the modes of thought and models of practice that guide inventors today.

Review Questions

1. The question "How might we find a way to make use of DVDs and other physical media as users adopt streaming services for films and television over time?" is an example of which form of ideation?
   A. statement starter
   B. open innovation
   C. design thinking
   D. brainstorming

2. The creative process that begins with empathy is known as _____.
   A. Stanford's model of human-centric design
   B. build-measure-learn
   C. open innovation
   D. disruptive innovation

3. In the Six Hats exercise, new ideas are the purview of the _____.
   A. Black Hat
   B. Blue Hat
   C. Green Hat
   D. Red Hat

4. _____ is thinking strategically, often to create human-centered products.
   A. Creativity

B. Innovation
C. Invention
D. Design thinking

5. An innovation that is *not* developed in tandem with consumers but that is introduced in a society or in a targeted market as completed and "finished" is often referred to as a "_____."
A. design thinking
B. iterative development
C. black box
D. corporate narrative

6. If linear thinking is the idea that progress follows or should follow a set of established, logical steps, _____ is free and open thinking where established patterns of logical thought are purposefully ignored or even challenged.
A. design thinking
B. iterative development
C. corporate narrative
D. lateral thinking

7. The model for building _____ also includes steps for team building, suggesting that the most complex developments require more than the lone mad scientist in a lab, despite what is often depicted in popular culture.
A. creativity in an individual
B. innovations
C. inventions

8. Problem solving is part of but not the entire model for building innovations. True or False?
A. true
B. false

9. DICEE is a model for _____ that focuses on going beyond problem solving to get at the underlying qualities of what makes certain new products "sticky" in ways that make people true fans.
A. creativity in practice
B. innovative products
C. inventions
D. building creative teams

Discussion Questions

1. Open innovation can be criticized for being vague and encouraging corporations to attempt to commit corporate espionage to look for solutions to problems shared by multiple firms in the same field. Is open innovation all it is cracked up to be? Is it truly new? Does it encourage intellectual property theft?

2. At what point is a product truly inventive? Can you think of products that some people think are inventions but that other people consider mere variations of previous products?

3. What is the value of creative efforts that are not meant for sale and that are never turned into products for the marketplace?

4. Critics of contemporary society suggest that there is something akin to a "technology cult" around the world. Some people treat innovation and inventiveness as cure-alls even as social conditions such as poverty, environmental degradation, and hunger persist. Can innovation cure all of society's ills? If so,

what is standing in the way? Why hasn't the modern era solved basic human needs and human rights problems with technology?

5. Can you think of a product you or someone you know adopted early only to watch it fall into the diffusion chasm between early adopters and early majority adopters? What was that product, and why do you think it failed to make it across that gap?
6. What makes a model for creativity necessary? Isn't creativity the opposite or the absence of structure?
7. Why does the model for innovation stress that it does not end with problem solving?
8. Why does the section on invention focus so much on building a team? Aren't most inventors and truly creative people famous for working solo?

Case Questions

1. Open innovation means more than searching online for others who are attempting to solve the same problems you are and trying to take inspiration from other corporations and other entrepreneurs. It also involves forming partnerships, supporting new ventures, investing in business accelerators, and acquiring firms that innovate in ways that are valuable to your firm or to your entrepreneurial effort (assuming you can raise the capital to acquire a firm while you develop your invention).[56] Think of an example of a firm (other than Samsung, the example from Merit Morikawa's article, and Apple, the "easy" answer) that has engaged in all of these practices. What seems to drive these different modes of open innovation? When are they most appropriate? When are they not appropriate ethically?
2. Read this article to prepare for answering this question: https://www.brookings.edu/blog/brookings-now/2018/05/23/artificial-intelligence-will-disrupt-the-future-of-work-are-we-ready/. (Brennan Hoban. "Artificial Intelligence Will Disrupt the Future of Work. Are We Ready?" Brookings. May 23, 2018.)
Many signs point to growing automation across a variety of industries in the coming decades. In many cases, disruptive technologies will force people to innovate. Based on the DICEE innovation model, explain how humans will be needed on the design side of innovation to create human-centric products. In what ways can you create a career that is "disruption-proof"?

Suggested Resources

4.1 Tools for Creativity and Innovation

The World's 25 Best Design Schools: https://www.businessinsider.com/the-worlds-25-best-design-schools-2012-11

Open Innovation Community: http://openinnovation.net/

The Seven All-Time Greatest Ideation Techniques: http://www.innovationmanagement.se/2013/05/30/the-7-all-time-greatest-ideation-techniques/

Ideation Method: Mash-Up: https://www.ideou.com/pages/ideation-method-mash-up

LUMA Institute's LUMA System of Innovation: https://www.youtube.com/watch?v=qDyElJ0xe2o

Ideation Method: Top Five: http://www.designkit.org/methods/15

4.3 Developing Ideas, Innovations, and Inventions

Additional information about product development: https://www.smartsheet.com/all-about-new-product-development-process

A summary of various leadership styles and traits that are essential for a changing business environment:

56 Merit Morikawa. "16 Examples of Open Innovation: What Can We Learn From Them?" *Viima.* November 20, 2016. https://www.viima.com/blog/16-examples-of-open-innovation-what-can-we-learn-from-them

https://www.christinespeaks.com/management/demonstrate-dynamic-leadership

5

Identifying Entrepreneurial Opportunity

Figure 5.1 Chris Johnson, CEO and founder of California-based company Rapid Brands, invented the Rapid Ramen Cooker and has since grown his offerings to a line of successful products. (credit: photo provided by Rapid Brands Inc.)

Chapter Outline

5.1 Entrepreneurial Opportunity
5.2 Researching Potential Business Opportunities
5.3 Competitive Analysis

Introduction

Like many college students, Chris Johnson ate a lot of ramen noodles, and like many college students, cooking meant microwaving something in his dorm room. At the time, ramen noodle companies did not print microwave instructions on the package, and there was a lack of microwave cookware in which to prepare the popular college food fare.

Many entrepreneurial ideas aim to solve small everyday problems. In his quest to find a better way to prepare ramen noodles, Chris Johnson invented the Rapid Ramen Cooker.

Johnson is now the CEO of Rapid Brands. He founded his company in 2013 with the Rapid Ramen Cooker. Johnson pitched his idea on the TV show *Shark Tank*. Although he negotiated with investor Mark Cuban for an ownership stake in the company, Johnson wound up not taking the deal. Instead, he made a deal with Walmart to position the Ramen cooker on the retailer's shelves. Rapid Brands sold more than 4 million Rapid Ramen Cookers in its first two years at Walmart and other retailers. Johnson has since introduced several new products, including cookers for eggs, hot dogs, and brownies.[1]

Finding an entrepreneurial opportunity and persisting until your business becomes successful is not easy and involves risk. But whether you start a new venture because you came up with an idea to solve an everyday problem, or whether you are deliberately searching for an opportunity because you want to start your own business, doing the research beforehand will help mitigate risk and determine the venture's likelihood of success.

1 Mark Anderson. "Local 'Shark Tank' Winner Cooks up a Major Expansion." *Sacramento Business Journal*. April 4, 2016. https://www.bizjournals.com/sacramento/news/2016/04/04/local-shark-tank-winner-cooks-up-a-major-expansion.html

5.1 Entrepreneurial Opportunity

Learning Objectives

By the end of this section, you will be able to:

- Define entrepreneurial opportunity
- Discuss Joseph Schumpeter's theories of opportunity
- Identify key drivers of opportunity

Aspiring entrepreneurs can come up with ideas all day long, but not every idea is necessarily a good idea. For an idea to be worth pursuing, we must first determine whether the idea translates into an *entrepreneurial opportunity*. **Entrepreneurial opportunity** is the point at which identifiable consumer demand meets the feasibility of satisfying the requested product or service. In the field of entrepreneurship, specific criteria need to be met to move from an idea into an opportunity. It begins with developing the right mindset—a mindset where the aspiring entrepreneur sharpens their senses to consumer needs and wants, and conducts research to determine whether the idea can become a successful new venture.

In some cases, opportunities are found through a deliberate search, especially when developing new technologies. In other instances, opportunities emerge serendipitously, through chance. But in most cases, an entrepreneurial opportunity comes about from recognizing a problem and making a deliberate attempt to solve that problem. The problem may be difficult and complex, such as landing a person on Mars, or it may be a much less complicated problem such as making a less expensive and more comfortable mattress, as companies like Casper and Purple did.

Theories of Opportunity

In the twentieth century, economist Joseph Schumpeter, as shown in Figure 5.2, stated that entrepreneurs create value "by exploiting a new invention or, more generally, an untried technological possibility for producing a new commodity or producing an old one in a new way, by opening up a new source of supply of materials or a new outlet for products, by reorganizing an industry" or similar means.[2]

Figure 5.2 Schumpeter believed that entrepreneurs create value in an economy. (credit: Joseph Alois Schumpeter, ca. 1910: HUGB

2 Joseph Schumpeter. *Capitalism, Socialism, and Democracy*, 3rd ed. (New York: Harper Torchbooks, Harper and Row Publishers, 1950), 132–134.

S276.90 p (2), olvwork369436. Harvard University Archives)

According to Schumpeter, entrepreneurial innovation is the disruptive force that creates and sustains economic growth, though in the process, it can also destroy established companies, reshape industries, and disrupt employment. He termed this force **creative destruction**. Schumpeter described business processes, including the concept of downsizing, as designed to increase company efficiency. The dynamics of businesses advances the economy and improves our lifestyle, but the changes (sometimes through technology) can make other industries or products obsolete. For instance, Schumpeter provided the example of the railroad changing the way companies could ship agricultural products quickly across the country by rail and using ice "cold cars," while at the same time, destroying the old way of life for many ranchers who wrangled cattle from one location to their intended commercial destination.

Today, we might think of the displacement of taxi drivers by ride-sharing services such as Uber and Lyft as a modern-day example of this concept. To own and operate a New York City cab, for instance, one must buy what is called a taxi medallion, which is basically the right to own and operate a cab. Drivers take out loans to buy these medallions, which cost hundreds of thousands of dollars. But now, ride-sharing services have eaten in to the taxi industry, all but destroying the value of the medallions, and the ability of taxi drivers to make the same money they were before the popular services existed. This change has left many taxi drivers in financial ruin.[3] Schumpeter argued that this cyclic destruction and creation was natural in a capitalist system, and that the entrepreneur was a prime mover of economic growth. To him, the goal was to progress, and progression starts with finding new ideas. He identified these methods for finding new business opportunities:

1. Develop a new market for an existing product.
2. Find a new supply of resources that would enable the entrepreneur to produce the product for less money.
3. Use existing technology to produce an old product in a new way.
4. Use an existing technology to produce a new product.
5. Finally, use new technology to produce a new product.

We can understand theories of opportunity as related to supply or demand, or as approaches to innovations in the use of technology. The first situation is a demand opportunity, whereas the remaining situations are supply situations. The final three incorporate technological innovations. *Supply* and *demand* are economic terms relating to the production of goods.

Supply is the amount of a product or service produced. **Demand** is the consumer or user desire for the outputs, the products, or services produced. We can use the ideas from Schumpeter to identify new opportunities. Our focus is on identifying where the current or future supply and the current or future demand are not being met or are not aligned, or where technological innovation can solve a problem.

More recent research has expanded on the concept of technological entrepreneurial opportunities, identifying several areas: creating new technology, utilizing technology that has not yet been exploited, identifying and adapting technology to satisfy the needs of a new market, or applying technology to create a new venture.[4]

Regardless of which of Schumpeter's paths entrepreneurs pursue, before investing time and money, the business landscape requires a thorough investigation to see whether there is an entrepreneurial opportunity. Remember, entrepreneurial opportunity is *the point at which identifiable consumer demand meets the feasibility of satisfying the requested product or service*. "Feasibility" in this definition includes identifying a sizable target market interested in the product or service that has sufficient profitability for the venture's financial success.

3 Winnie Hu. "Taxi Medallions, Once a Safe Investment, Now Drag Owners Into Debt." *The New York Times.* September 10, 2017. https://www.nytimes.com/2017/09/10/nyregion/new-york-taxi-medallions-uber.html

4 Jamalia Behrooz, Reza MohammadKazemi, Jahangir Yadollahi Farsi, and Ali Mobini Dehkordi. "Theories of Opportunity Creation and Effective Entrepreneurial Actions in Opportunity Creation Context." *Decision Science Letters* 7, no. 4 (2018): 443–454.

ENTREPRENEUR IN ACTION

Chester Carlson

Chester Carlson, a physicist, inventor, and patent attorney, spent ten years searching for a company to develop and manufacture a new photographic machine for office use to make copies faster and for less money. Carlson went on to found the XEROX Corporation, the company that made the first photocopy machines. Can you imagine a school or office today without a photocopy machine? The companies that Carlson approached with his invention missed the opportunity to invest. For Carlson, it was the beginning of a technology product development company that has been granted more than 50,000 patents worldwide.

Today, Xerox continues to innovate. Visit the innovation section of its website (https://www.xerox.com/en-us/innovation) and consider how one of the inventions it's developing now could spur creative destruction in an industry, according to Schumpeter's theory.

Identifying Opportunity

A good place to begin your entrepreneurial quest is to read as much as you can, especially with new technology developments, even outside the field you work in. Remember that as technologies start to emerge, we often do not yet understand their commercial potential. For example, microwave technology was first applied in radars to track military submarines. But, thanks to a curious man named Percy Spencer and the accidental melting of a peanut bar in his pocket one day while tinkering with the technology, the microwave was born. It would take a few decades for it to be produced at a price the mass market could afford.[5]

Think of drones, too. When they were invented, the multiple uses for this technology were not yet identified. Now, drone technology is being used by real estate firms, package delivery services, agriculture, underwater search and scientific research, security, surveillance, and more. Being tuned in to new experiences and information can lead to identifying opportunities. Entrepreneur Fred Smith found a system to solve the problem of overnight package delivery in founding Federal Express.[6] As a college student, he wrote a paper for an economics class where he discussed his business idea. He earned only a C on his paper, by the way. He received his bachelor's degree in 1966 and went on to found Federal Express a few years later, which, in 2019, generated almost $70 billion in revenue.[7] Prior to starting Federal Express, Smith was in the US Marine Corps serving in Vietnam where he observed the military's logistics systems.[8] This is where he honed his interest in shipping products while in the military. Many entrepreneurs start their business after working for someone else and seeing a better way to operate that business, and then start their own competing business.

Note that entrepreneurs need to be careful about starting competing businesses. See Telling Your Entrepreneurial Story and Pitching the Idea and Business Structure Options: Legal, Tax, and Risk Issues for information on noncompete clauses and agreements. Indeed, some entrepreneurs, like Smith, conduct research as an idea percolates, paying attention to new experiences and information to further advance their idea into an entrepreneurial opportunity. However, they must ensure that the existing product, service, or business process is not covered by any active and protected intellectual property (patent, trademark, copyright, or trade secret), as discussed in Creativity, Innovation, and Invention and Fundamentals of Resource Planning.

5 Matt Blitz. "The Amazing True Story of How the Microwave Was Invented by Accident." *Popular Mechanics*. February 24, 2016. https://www.popularmechanics.com/technology/gadgets/a19567/how-the-microwave-was-invented-by-accident/
6 "Success Story – Fred Smith | Federal Express." *Daily10Minutes*. n.d. http://www.dailytenminutes.com/2017/09/success-story-fred-smith-federal-express.html
7 "FedEx Corp. Reports Fourth Quarter and Full-Year Earnings." *Federal Express*. June 25, 2019. http://investors.fedex.com/news-and-events/investor-news/news-release-details/2019/FedEx-Corp-Reports-Fourth-Quarter-and-Full-Year-Earnings/default.aspx
8 Vance H. Trimble. *Inventing FedEx: The Cruel Ordeal* (2012). Vance Trimble. *Overnight Success: Federal Express and Frederick Smith, Its Renegade Creator* (1993).

Identifying consumer needs may be as simple as listening to customer comments such as "I wish my virtual orders could be delivered more quickly." or "I can never seem to find a comfortable pillow that helps me sleep better." You can also observe customer behavior to gather new ideas. If you are already in business, customer feedback can be a simple form of market research.

When purchasing an existing business or franchise, the process is a bit different. The first step will usually be searching for a business that suits your experience, personal preferences, and interests. You will still want to conduct research to understand the industry, the local market, and the business itself. Then, you will begin to examine all available company financial data. If purchasing a franchise, you may want to contact other franchise owners and discuss their experience in working with the franchisor.

ENTREPRENEUR IN ACTION

How Spanx Founder Developed Resilience and Persistence[9]

Another entrepreneur, Sara Blakely (Figure 5.3), admits that for the seven years she spent selling fax machines in the 1990s, many times, she became so frightened of approaching sales prospects that she would burst into tears and then have to drive around the block to collect herself before she could complete the next sales call.

(a) **(b)**

Figure 5.3 (a) Spanx, a new product that was created to solve an everyday problem, was invented by (b) Entrepreneur Sara Blakely (far right). (credit (a): "Spanx" by Mike Mozart/Flickr, CC BY 2.0; credit (b): "Ed Bastian and Sara Blakely at the Fast Company Innovation Festival" by Nan Palmero/Flickr, CC B 2.0)

One day in 1998, she was putting on pants and looked in the mirror and did not like how she looked. So, Blakely came up with the idea to wear a pair of control-top pantyhose underneath—but she cut the feet out. Blakely liked the look and comfort of the footless hose and decided to patent her own body-shaping footless version. Just a few years later, Blakely founded her company, Spanx, Incorporated, which since has gone on to launch more than 200 styles of body-shaping garments. This is another case of an entrepreneurial company born out of a simple way to solve an everyday problem.

Blakely is also a master of resilience, which is a quality of many successful entrepreneurs. When she was sixteen years old, right around the time her parents separated, she witnessed a good friend get hit and killed by a car. Her father gave her a set of motivational tapes to listen to: *How to Be a No-Limit Person* by Wayne Dyer. She found the tapes so helpful that she memorized all of them and still gives copies of the tapes as gifts.

As a child, her father encouraged his children to respect the valuable lessons we can learn through failure.

9 Teri Evans. "Sara Blakely on Resilience." *Entrepreneur*. March 21, 2011. https://www.entrepreneur.com/article/219367

Obviously, it helped Blakely at a young age develop persistence and determination. That persistence and determination helped her develop a business idea into a billion-dollar enterprise.

- Was Blakely's idea a demand or a supply idea?
- What industry information would Blakely need as she was researching this idea?

When researching supply and demand, you should also consider political factors. For example, changes in tax laws can inform decisions. One example is a tax credit that encourages alternative energy use, such as electric or hybrid vehicles. For 2019, the IRS tax credit is between $2,500 and $7,500 per new electric vehicle, with a concurrent phase-out of the plug-in electric vehicle tax credit. Changes in the tax code can therefore influence buyer behavior or the demand for vehicles. Another example is the Residential Energy Efficient Property Credit of up to $4,000 for solar electronic appliances such as solar water heaters and solar panels and for small wind turbines, through the end of 2021.[10] Tax incentives do not usually last more than a few years (the tax subsidy for corn farmers to produce ethanol, an ingredient in automotive fuels, is a notable exception due to heavy lobbying by the farming industry), so it is important that entrepreneurs do not rely on these incentives as a permanent "pillar" of their value proposition and business model.

Let's say you have an interest in machinery and art. Taking these two areas of interest, and knowing about this tax credit, you recognize that you have the talents to create artistic backyard wind turbines to create energy for a homeowner. Of course, you will still need to determine whether this is merely an idea, or if the conditions are in place to move forward in translating this idea into an entrepreneurial opportunity.

Drivers of Opportunity

Some recent drivers for change in the entrepreneurial space include new funding options, technological advancements, globalization, and industry-specific economics.

- Increased access to capital through social media sources like crowdsourcing (see the chapter on Problem Solving and Need Recognition Techniques for a more detailed discussion of crowdsourcing) is having a significant impact on entrepreneurship in that it enables underserved people and communities—such as women, veterans, African Americans, and Native Americans, who otherwise might not be able to start and own a business—to become entrepreneurs.
- Technological advancements continue to provide new opportunities, ranging from drones to artificial intelligence, advancements in medical care, and access to learning about new technology. For example, drone technology is being used to map and photograph real estate, deliver products to customers, and provide aerial security and many other services. Cell phones have spawned many new business opportunities for a wide range of cell phone accessories and related products, ranging from cell phone cases to apps that help make our cell phones faster for business and personal use.
- Increased globalization drives entrepreneurship by allowing importing and exporting to flourish. Globalization also helps spread ideas for new products and services to a world market instead of a local or regional market. Combined with the Internet and computer technology, even small businesses can compete and sell their products around the globe.
- Economic factors could include a strong economy that fuels other businesses. For example, growth in the housing market fuels growth for many housing-related products and services, ranging from interior decorating to landscaping as well as furniture, appliances, and moving services.

David Pridham, CEO of the patent advisory board and transaction firm Dominion Harbor Group in Dallas, cites six reasons that current conditions are excellent for startups:

1. Venture capital investment, which you will learn more about in Entrepreneurial Finance and Accounting,

10 "Tax Credits for Energy Efficient Home Improvements." *EFile.com*. January 24, 2019. https://www.efile.com/tax-credit/energy-credit/

has surged to the highest level ever, totaling $148 billion in 2018.
2. The concern over patent protection is improving with better trade protection of intellectual property rights.
3. Artificial intelligence could be a tremendous opportunity based on a McKinsey report projection, estimating artificial intelligence to become a $13 trillion industry by 2025.
4. The explosive growth in freelance workers has been a boon to startups and small businesses.
5. Another hot sector is technology-driven advancements such as self-driving vehicles.
6. Intellectual property now accounts for 38.2 percent of our total Gross Domestic Product (GDP) in the United States. That totals $6 trillion per year, more than any other nation's GDP except for China.[11]

In addition, Silicon Valley Bank (SVB) Financial Group surveyed new startup businesses in 2017 and found that 95 percent indicated they believe that business conditions will be the same or better. In addition, 83 percent plan to increase their workforce, and 24 percent found fundraising not to be a challenge.[12] These numbers represent the highest levels of optimism among entrepreneurs over the most recent five-year period.

Some other economic indicators favor entrepreneurship. According to the 2019 Goldman Sachs Economic Outlook, consumer confidence is up, business confidence is up, interest rates remain reasonable and steady, more people are working, and wages are higher.[13] When the economy is strong, there are generally more opportunities available and more potential customers with money to purchase your products and services; but of course, there are no guarantees.

LINK TO LEARNING

There are debates about so-called kill zones—markets that the tech giants like Facebook and Amazon control through aggressive anticompetitive tactics. Some argue that these zones have frightened off investors and stifled competition. But others maintain that investment in young tech startups is as strong as ever and that the creative effects of big tech companies outweigh their destructive forces.

Read this article on how tech giants make it difficult for startups (https://openstax.org/l/52TechGiant1) from *The Economist* and then this blog post refuting the idea that tech giants kill startups (https://openstax.org/l/52TechGiant2) from The American Enterprise Institute and see what you think about the issue.

5.2 Researching Potential Business Opportunities

Learning Objectives

By the end of this section, you will be able to:

- Describe opportunity screening
- Identify common sources of research data
- Explain how to research and verify business opportunities
- Identify industry and consumer sources of opportunities

In order to discover how reasonable your business idea is, you need to research many aspects of the concept. **Opportunity screening** is the process by which entrepreneurs evaluate innovative product ideas, strategies, and marketing trends. Focusing on the viability of financial resources, the skills of the entrepreneurial team, and the competition, this screening helps determine the potential for success in pursuing the idea and can help refine planning.

11 David Pridham. "Entrepreneurs: Here's Good News for 2018." *Forbes*. January 10, 2018. https://www.forbes.com/sites/davidpridham/2018/01/10/entrepreneurs-heres-good-news-for-2018/#18f02aef6659
12 Silicon Valley Bank. *2019 Startup Outlook Report*. 2019. https://www.svb.com/startup-outlook-report-2019
13 Goldman Sachs. *2019 Outlook: The Home Stretch*. US Economics Analyst. November 18, 2018. https://www.goldmansachs.com/insights/pages/outlook-2019/us-outlook/report.pdf

Common Sources of Research Data

As you embark on researching whether your idea is viable, a good place to start is with the sources recommended by the US Small Business Administration. These include US Census data (https://www.census.gov/academy), which provides insight into the population in your market area, such as the metropolitan statistical area data, as well as statistics on the economy and trade. For most entrepreneurs, research will also include asking potential customers, specifically your target customers, questions about products they like and don't like, how a product or service could be improved, how the customer buying experience could be improved, and even where customers might go to purchase products and services instead of your business.

Small business marketers can use several no-cost or low-cost methods, including surveys, questionnaires, focus groups, and in-depth interviews. Of course, you do not need to be an expert in these areas. Business assistance is available to you from the Small Business Administration, the Service Corps of Retired Executives (SCORE), and your local Small Business Development Center. You may also have a local college or university business department that provides assistance to local area businesses.

LINK TO LEARNING

The Small Business Administration website (https://openstax.org/l/52SBA2) and SCORE website (https://openstax.org/l/52SCORE2) are rich resources of information for entrepreneurs.

You will likely begin with **secondary research**—that is, data that are already available through some published source. There may be articles, research reports, or reliable Internet sources where you can research information about your industry, products, and customers. If you have the funds, you can also purchase research reports from firms that specialize in gathering research on certain topics or products. Secondary research has the advantage of being quickly available. However, secondary research often is not specific enough to provide all the details you need to know about your idea. For example, secondary research (this is research that has been developed from primary sources that is almost as useful as primary, direct research) might report how often consumers purchase shampoo, where they purchase shampoo, and what brands of shampoo they purchase. But if you want to understand the details of how people shampoo—for example, whether they shampoo then repeat, use a separate conditioner, or use a combination shampoo/conditioner product—then you would want to conduct primary research. Primary research is needed when secondary research does not address the questions you want to explore while investigating your business idea.

Primary research gathers data that do not yet exist. The information is specific to the business, product, or consumer. It takes time and money to obtain primary data. Some of the methods used to gather primary research data include developing a survey questionnaire, using secret shoppers, or using focus groups. Survey questionnaires can be simple, such as a customer comment card included on a receipt, or extensive, including dozens of detailed questions. Secret shoppers can be used by hiring a shopping service or using friends, family members, and even your customers. One local small business owner gave a friend gift certificates that could be used at his ice cream business in exchange for the friend reporting back on product quality, service, and other key issues.

Researching and Verifying the Entrepreneurial Opportunity

Whether you start your own business, buy an existing business, or purchase a franchise, researching the industry, your target market, and examining the economic and funding options are all part of performing due diligence. Due diligence is the process of taking reasonable steps to verify that your decisions are based on well-researched and accurate information. It means thoroughly researching potential pursuits, asking detailed questions, and verifying information.

Different industries have different meanings for due diligence. For example, in the legal industry, due diligence involves understanding the terms of a transaction and contract. In business finance, due diligence refers to raising capital or the work involved in merger and acquisition transactions. In the entrepreneurship field, research is necessary to verify whether the idea is really an opportunity, considering the entire process of starting the venture and funding the venture.

One of the more common questions entrepreneurs must ask is whether *now* is a good time to start a business. This question of timing is addressed in the investigation to determine whether the idea is merely interesting or fits the criteria of being an entrepreneurial opportunity.

An idea can move to a recognized opportunity when the following criteria are met. Figure 5.4 shows these three factors:

- Significant market demand
- Significant market structure and size
- Significant margins and resources to support the venture's success

Significant market demand means that the idea has value by providing a solution to a problem that the target market is willing to purchase. This value can result from a new product or service that fills an unmet need, a lower price, improved benefits, or greater financial or emotional value. This value can also result from capitalizing on "nonconsumption." For example, in the 1980s, the Disney Corporation realized that it was losing an opportunity to entice visitors to come to their theme parks from 9 p.m. to 9 a.m. when they were closed. So the company started having "school nights" when schools and students could use the parks at a discount.

Significant market structure and size involve growth potential and drivers of demand for the product or service. Barriers to entry are manageable, meaning that entering the industry or creating a new industry is not exceptionally difficult. If the industry already exists, there must be room within the industry for your venture to gain market share by providing a value that creates a competitive advantage.

Significant margins and resources involve the potential for achieving profit margins at a high-enough level that the work of starting the venture (including the entrepreneur's time and energy) is worth the risks involved. If the operating costs are too high and the profit margin is too low, it is important to analyze whether the idea is truly feasible. Significant margins also include the capital requirements—how much money is needed to start the venture—as well as the technical requirements, the complexity of the distribution system, and similar resources.

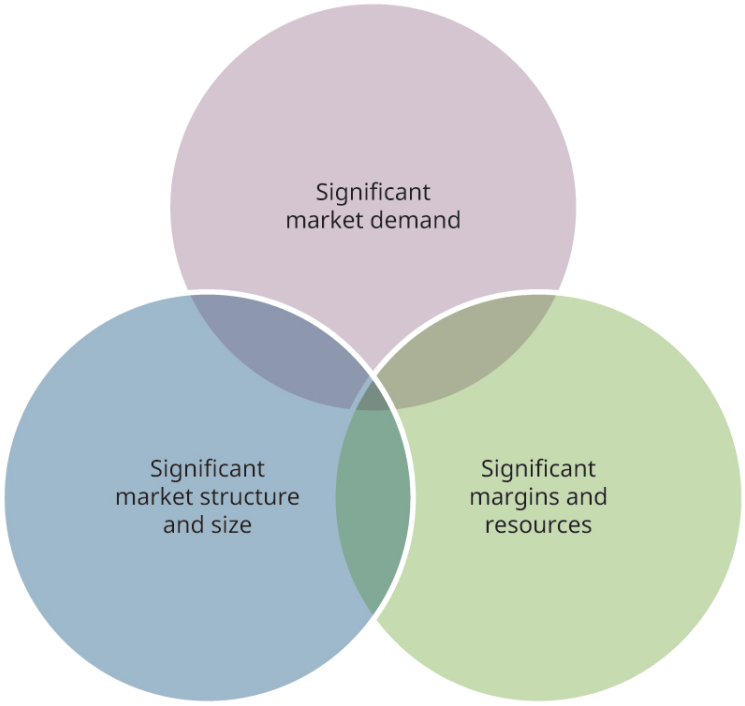


Figure 5.4 When these criteria are met, an idea is recognized as an opportunity. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Determining whether an idea has significant market demand, significant market structure and size, and significant margins and resources to support the venture's success represents the most basic concerns when screening a business idea as an entrepreneurial opportunity.

Keep in mind that these three criteria are based partially on creating a for-profit venture. If your entrepreneurial venture is focused on solving a societal problem, you want to know that the identified problem is realistic and that there is a need for solving it. In a for-profit venture, significant market structure and margins relate to the expectation that the venture will have significant sales with significant profit margins to sustain and grow. There are also examples of profitable entrepreneurial ventures, like YouTube, that did not have any sales, but there was still an expectation that harvesting or selling YouTube would result in a significant profit for the entrepreneurial team. You can read more about Google's purchase of YouTube at https://www.theringer.com/2016/10/10/16042354/google-youtube-acquisition-10-years-tech-deals-69fdbe1c8a06.

After confirming that a business idea is an entrepreneurial opportunity, the entrepreneur should ask more detailed questions in the next phase of screening the business. Here are some examples:

- Would other people value your product or service?
- Does your product or service solve a significant problem?
- Is the market for the product definable/specific?
- Does the market have unique needs or expectations that align with your entrepreneurial opportunity?
- Is the timing right to start the venture?
- Are there infrastructure or supporting resources that need to be commercialized or created prior to your launch of the venture?
- What resources are needed to start the venture?
- What is the competitive advantage your venture offers within the industry and is this competitive advantage sustainable?
- What is the timeline between starting the venture and the first sale?
- How long before the venture becomes profitable and do you have the resources to support this timeline?

A good starting point in your opportunity screening research is to begin learning about the demographics of the market you are targeting (your target market). **Demographics** are statistical factors of a population, such as race, age, and gender.

The government collects census data demographics,[14] which can provide a snapshot of the population in your city or town. Census data include the total population, a breakdown of the population by age, gender, race, and income, and some other useful data.

LINK TO LEARNING

The US Census website (https://openstax.org/l/52USCensus) and your local chamber of commerce (https://openstax.org/l/52ChamberComm) can help you learn more about the demographics of your target market or region.

For example, if you were considering opening a new ice cream store with unique flavors preferred by children, census data could tell you the number of children living in the area, the ratio of boys to girls, their ages, and the general income levels of the families in town. The census data would help you determine the size of the market and potential target market, local market growth, income levels, and key demographics that might fit the potential customer profile. Of course, there is other information you might want to collect, such as the percentage of the population that had lactose intolerance. If you found that a significant portion of your market was lactose intolerant, this could be your identified opportunity: You could create a lactose-free ice cream store or expand with a variety of lactose-free flavors. The census data also help identify where to locate your entrepreneurial venture. For example, if your lactose-free ice cream was expensive because of the necessary ingredients, you would not want to open your store in a low-income area.

There is a vast amount of data and information available through the Internet that can support your success in making informed decisions as you explore the feasibility of opening a successful venture. Or you can purchase more detailed consumer data through providers such as Claritas Research, which gathers information on demographics, consumer lifestyles, attitudes, and behaviors (https://claritas360.claritas.com/mybestsegments/?ID=70). For many small business startups that cannot afford sophisticated research data, the entrepreneur will probably have to rely on census data along with information that the local economic development council is able to provide.

WORK IT OUT

T-Shirt Startup

Create your own t-shirt line to target your classmates.

- What would be the theme?
- How much would you charge?
- Where would you sell the shirts?
- What are the expected sales of the business?
- What are the resources needed to get started?

After analyzing demographic data, the entrepreneur can then develop and conduct some basic research, which could range from observing customers to shopping at potential competitors. Entrepreneurs can also uncover business opportunities by asking questions of, and listening to, their customers, if they are working within the industry or looking for new entrepreneurial opportunities with a similar target market. Sometimes

14 United States Census Bureau. https://www.census.gov/

an easy and inexpensive customer survey can uncover problems and opportunities. Entrepreneurs can also gather information using their social media accounts and customer sales records.

For example, imagine a men's clothing store in Denver that maintained a detailed customer database that they used primarily to order the colors and sizes their customers were most likely to purchase. A marketing consultant begins researching customer data and finds a number of former customers who had not shopped at the store for a year or more. The consultant uncovers some lapses in service that had cost the store thousands of dollars in sales. Store management, working with the information from the consultant, develops a direct marketing campaign that helps bring back former customers and adds new customers, resulting in a substantial sales increase.

The lesson here is that research is important at all stages of the business—before you start your business and consistently thereafter. Markets change as new people move in or out of an area, styles and preferences change over time, and new technology can radically impact what customers want to buy. We all know of businesses like Blockbuster or Xerox that ignored evolving technology, to the detriment of their success. Constantly tracking changes in the external environment and competitive arena is an ongoing activity that supports the continued success of the venture.

A popular tool for market analysis is a product from Claritas Research called Potential Rating Index for Zip Markets (PRIZM), which characterizes census data according to certain lifestyle traits, even down to the neighborhood level. As an example, let's see how PRIZM can help us better understand the consumer market of a small town in Massachusetts. Oxford, Massachusetts (zip code 01540), has a population of 11,653, with slightly more half being female; a median income of $70,444; and a median age of 42.3 years. PRIZM data give us a better understanding of consumers than census data do in Oxford by examining the five dominant lifestyle segments from within PRIZM's sixty-six segments. The PRIZM segments are based on socioeconomic rank determined by characteristics such as income, education, occupation, and home value. A thorough analysis of available data could suggest the most likely products and sources consumers in this zip code market would likely purchase.

Entrepreneurs might also obtain data from economic development agencies, the local chamber of commerce, the state small business development center, or industry associations. Of course, lots of data can be found with a good search on your computer. Your university reference librarian can tell you what resources they have available and which resources would best fit your research question(s) and area of focus for your idea.

ENTREPRENEUR IN ACTION

Elon Musk's SpaceX

There have been many instances in which products have been promised but fail in their implementation. Space travel—think Elon Musk's venture SpaceX (Figure 5.5)—is an example of a bold concept that is still in the feasibility phase. Is it even possible to send humans to Mars? This is an extreme but interesting example for considering product feasibility.

Another application of the SpaceX technology is to develop satellite-based Internet access that can provide service to billions of people who do not already have Internet service.[15] However, the project will require new satellite networks, and it may take twenty years to fully develop.

- What short-term and long-term considerations are necessary in the project?
- As the concept will take twenty years of satellite development, how can technological changes be incorporated into the development of the idea?
- Given the description of an entrepreneurial opportunity, does this idea fit that definition?

15 Aaron Pressman. "Elon Musk's SpaceX May Fuel $1 Trillion Space Business Boom." *Fortune*. October 12, 2017. http://fortune.com/2017/10/12/elon-musk-spacex-morgan-stanley/

Figure 5.5 SpaceX operations are centered in these headquarters. (credit: "Iridium-4 Mission (25557986177)" by Official SpaceX Photos/Wikimedia Commons, CC0 1.0)

What should you do if your idea does not fit these criteria—significant market demand, market structure and size, and margins and resources—and your passion to develop the idea into an opportunity and new venture is still strong? This is also part of the entrepreneurial process. You, as the lead entrepreneur, are charged with the task of identifying the obstacles to turning your idea into an opportunity and what actions are necessary to overcome these. This could mean adjusting the idea, adding new features, or even removing some features. Adding new features should focus on increasing the value or benefit offered by the product or service, or creating a tighter alignment with the needs of the target market. Removing features could decrease the production costs or even the complexity in using the product.

As part of your research to verify whether your idea is truly an entrepreneurial opportunity, researching your state's laws and regulations is essential. Conduct an Internet search for your state's business regulations applicable to your business. You will need to comply with these laws, as well as purchase any licenses and permits necessary for your business. You should also check with your local or county government for additional local regulations, including zoning and signage laws. Remember that laws vary by state, so what is legal in one state may not be legal in another, or there might be stricter regulations. For emerging industries, the regulations and laws can fluctuate as industries evolve. This is especially true for emerging industries such as the sale and distribution of medical marijuana.

ARE YOU READY?

Getting a License or Permit to Start a Business

When starting a business, be sure that you have all the required licenses and permits, keeping in mind that you may need licenses from federal, state, county, and local government agencies. You can start with the SBA website at https://www.sba.gov/business-guide/launch-your-business/apply-licenses-permits#section-header-0. Another helpful resource is Fundera, an online financial resource that provides information about obtaining business licenses in all fifty states and links to essential government organizations for each state: https://www.fundera.com/blog/business-license. And try nav.com as well: https://www.nav.com/blog/266-business-licensing-by-state-5008/.

States regulate a larger number of business activities than the federal government. Business activities that are regulated locally include auctions, construction, dry cleaning, farming, plumbing, restaurants, retail, and vending.

- Select a business in a regulated industry and research what would be needed to start the venture in a specific locale.

Many estimates indicate that half of all new businesses will no longer exist within the first five years, but good research can help you avoid your business becoming a statistic.[16] On the surface, this fact can be daunting. However, there are many reasons why a business no longer exists that can reflect a positive outcome, such as the sale of a business or a merger with another business. Another example is when an entrepreneur intentionally starts a venture knowing that there is a short-term timeline for success, with the expectation that new technology will replace the gap that the venture originally filled. Most entrepreneurs are not big risk-takers but understand that there are no guarantees in starting a new business venture. Instead, entrepreneurs tend to take calculated business risks based on the best research they can gather. At some point, however, the entrepreneur recognizes that despite all the good research they have gathered, they still need to take a leap of faith when starting their new venture.

WHAT CAN YOU DO?

Why Small Businesses Fail

Why do half or more of new small businesses no longer exist after the first five years? In many cases, it is failure of the business. The Small Business Institute at Thomas College in Maine has cited factors in Table 5.1 as the most common reasons for small business failures. Many business development agencies have compiled similar lists.

Ten Reasons for Small Business Failure

Reason	Description
Low sales	Entrepreneurs may have overestimated sales, assuming they could take sales away from established competitors.
Lack of experience	Running a business is hard, and a new business can be especially challenging, as it is difficult to prepare adequately for the unexpected.
Insufficient capital	When calculating how much money you will need to start your new business venture, be sure to account for the time it will take before your business breaks even and be sure also to allow for some contingency funds for when the unexpected happens.
Poor location	For some types of businesses, location is critical. Of course, location may be less important for a home-based business and not at all important for an Internet business.
Poor inventory management	Too much inventory results in the business becoming cash-strapped and unable to buy advertising or other important goods and services.

Table 5.1 Understanding some of the factors that lead to business failure can help you be aware of those as you research your idea and opportunity.

16 US Small Business Administration Office of Advocacy. *Frequently Asked Questions about Small Business.* August 2018. https://www.sba.gov/sites/default/files/advocacy/Frequently-Asked-Questions-Small-Business-2018.pdf

Reason	Description
Overinvestment in fixed assets	Especially when starting a business, it is usually less expensive to lease or purchase used equipment, thereby saving cash for meeting operational expenses.
Poor credit arrangement management	Start your venture small and limit the amount of money you need to borrow. Work with your banker from the beginning by sharing your business plan and vision for the business with the banker and, most important, show that you are proactive in planning for when you will need to borrow money.
Personal use of business funds	The owner should pay him/herself a minimal salary and not dip into business funds. If the business has done well, the owner will earn additional funds at the end of the year.
Unexpected growth	Surprisingly, some businesses fail because the business owner cannot manage growth. Growing a new venture, especially if the growth is at a higher rate than expected, can create surprising challenges. For example, if creating a product, you need to consider the capacity of the factory where you are producing the product. If you are at 100 percent capacity and your orders increase, you will need to think about what actions can support this increase in demand. If you cannot meet the demand, you will have unhappy customers and negative publicity that will reflect negatively on your leadership and managerial skills. Your lack of planning for this surge in sales may open opportunities for someone else to start a competing business.
Competition	Many small business owners underestimate their competition. Remember, if there is money to be made, there will be competition! Larger competitors can beat you every day of the week on price, so find another way to challenge competitors.

Table 5.1 Understanding some of the factors that lead to business failure can help you be aware of those as you research your idea and opportunity.

- Given the preceding reasons for small business failure, what can be done to head off such failure?
- Why is it necessary to assemble a team of professional advisors to address financial, personnel, legal, accounting, and other business issues?
- Why is it vital to identify suppliers and personnel to be able to provide a product or service?
- What factors are important when considering whether a product should be manufactured internally or outsourced to a third party?

Let us analyze, as an example, opportunity recognition displayed by a company called Sweet Beginnings. Eddie Griffin, Kevin Greenwood, and Tiffany Chen were all residents of Chicago who were seeking jobs and a fresh start on life after serving time in prison. They wanted a chance to rebuild their lives and the ability to support themselves financially. Unfortunately, the odds were against them in their North Lawndale community: There was a 40 percent unemployment rate, 57 percent of residents had criminal histories, the average annual income was only $25,000, and the area was known for drugs, sex workers, and gangs. Statistically, they were destined to return to the criminal justice system.

But fate intervened in the form of Brenda Palms Barber, who knew all of these statistics. Palms Barber was the Executive Director of the North Lawndale Employment Network (LEN). When employers refused to hire Griffin, Greenwood, and Chen, whom she had coached, she researched what it would take to open various businesses,

including a temp agency, a landscaping company, and a delivery service, with the intent to offer employment to LEN clients. A recommendation from a board member's connection led her to consider, of all things, raising bees. It was not until she learned that the ins and outs of the apiary profession are passed on by word of mouth that she felt it was ideal for her clients who often faced learning challenges due to limited academic experience.

In 2005, Palms Barber founded Sweet Beginnings, a social enterprise that employs former inmates and teaches them job skills by running an apiary business directly in the heart of North Lawndale. The Sweet Beginnings brand, Bee Love (shown in Figure 5.6), sells honey and honey-infused skincare products in airports, hotels, and supermarkets, including Whole Foods. Palms Barber recognized that the skills her potential employees learned in the streets were transferrable to running and managing the business.[17,18,19]

Figure 5.6 Bee Love products are part of a social entrepreneurship venture. Founder Palms Barber researched the opportunity carefully and has found success. (credit: "Bee Love" by Alisha McCarthy/Flickr, CC BY 4.0)

Palms Barber also realized that a product gap existed between customer needs and products offered. She identified the niche market of customers who wanted all-natural skin care products and liked the idea of purchasing them from a social enterprise. Bee Love positioned itself for success as an appealing, high-end natural product to environmentally conscious consumers willing to pay a premium for it.

Palms Barber recognized an opportunity when she identified the societal problem of employment for people who had experienced incarceration. In seeking solutions to this problem, she encountered roadblocks from employers' resistance to hiring ex-prison inmates. She then researched other possible solutions including business startups. The idea of raising bees at first seemed an unusual solution to the problem of employment for her unique clients. In her due diligence, she identified a gap between customer preferences for all-natural skin care products and currently available offerings. Combining these ideas resulted in the opening of Bee Love. The fits between the clientele of ex-inmates, apiary, and skin care products supported the opening of this unique venture. Exploring the gaps was part of the process of finding the right solution and realizing that the idea of starting a business to support ex-inmates was an actual opportunity worth developing into a new venture.

Industry Sources of Opportunity

Your research process should include learning everything you can about the industry you plan to enter. This will help you to identify opportunities. An excellent source for industry information is the business reference section of your college library. Industry averages are available in reference books and can also be found at Dun & Bradstreet/Hoovers (http://www.hoovers.com/industry-analysis.html). The industry analysis contains important information including a brief description of the industry and its characteristics, the competitive

17 "Sweet Beginnings." *North Lawndale Employment Network.* n.d. https://www.nlen.org/sweetbeginnings
18 BeeLove. www.beelovebuzz.com
19 Leigh Buchanan. "Finding Jobs for Ex-Offenders." *Inc.* May 2011. https://www.inc.com/magazine/20110501/social-entrepreneurs-finding-jobs-for-ex-offenders.html

landscape, along with products, operations, and technology.

Industry sources reveal knowledge about a specific industry from the perspective of identifying unmet needs or areas for improvement within that industry. For example, Airbnb reshaped the hotel industry by connecting travelers with property owners, so that the travelers could rent the property when the owner was not using it. As Airbnb has grown, the company has made improvements to their offerings in meeting the needs of the traveler's demand based on property location and in categorizing the supply (the homeowner's property) for increased efficiency, meeting the needs of both the property owner and the traveler. Researching specific industries from supply and demand perspectives, and noticing unused supplies, as we saw in the Airbnb example, also applies to other industries, such as a sandwich shop. What happens to the unsold bread at the end of the day when there is an excess supply? For Stacy Madison and her pita sandwich food cart, unsold bread presented an opportunity to create pita chips by turning an oversupply into sliced and seasoned pita chips.[20]

Almost every industry is worth investigating from the perspective of identifying unused resources or extra resources that could be restructured for what are known as a *shared economy* or a *gig economy*. A **shared economy** considers that there are times when an asset in not in use. This down time when the asset is not in use provides an opening for someone else to use that asset, like Airbnb. Other companies, like Uber, Lyft, DoorDash, and Postmates, support the gig economy in aligning a person's choices for when they want to work with the flow of the work demand. A **gig economy** is an open or fluid market system with temporary positions made up of independent short-term workers. In these examples, we can see the alignment of supply and demand. The entrepreneurial opportunity happens in providing a platform to assist in connecting the supply and demand.

The tech sector, for example, is continually adapting to change. Items such as 3D printers and mobile devices are making the technology landscape expand. As new products come to market, the need for applications and increased efficiency abound. Several other industries are experiencing growth, including health care and nutrition. According to Global Market Insights (2019), the clinical nutrition market will exceed $87,530.7 million dollars by 2025.[21] This same source reported that this industry was valued at over $10,562.7 million in 2018, a significant increase over the previous seven years. Drivers in this industry include sedentary lifestyles and related health issues, such as obesity. The result of these societal changes is an increase in clinical nutrition products and home healthcare services. According to business management author, professor, and corporate consultant, Peter Drucker, entrepreneurs excel at finding and developing potential business opportunities created by social, technological, and cultural changes.

Consumer Sources of Opportunity

Consumer sources of opportunities relate to changes in our society, such as new habits or behaviors brought about by exposure to new information. For example, most people feel the pressure related to having less free or unrestricted time. Figure 5.7 tracks the average number of hours worked by country per worker per year.

20 "Stacy's Pita Chips: Stacy Madison." *How I Built This with Guy Raz*. National Public Radio (NPR). May 27, 2019. https://www.npr.org/2019/05/24/726755480/stacys-pita-chips-stacy-madison

21 Global Market Insights. "The Clinical Nutrition Market to Surpass $87,530.7 Million by 2025: Global Market Insights, Inc." *Cision PR Newswire*. March 5, 2019. https://www.prnewswire.com/news-releases/the-clinical-nutrition-market-to-surpass-87-530-7-million-by-2025-global-market-insights-inc-300806622.html

AVERAGE ANNUAL HOURS WORKED	
Country	**Annual Hours**
Mexico	2,246
South Korea	2,113
Greece	2,042
Chile	1,988
Russia	1,978
Turkey	1,832
United States	1,779
Italy	1,725
Japan	1,719
Canada	1,691
Spain	1,676
United Kingdom	1,674
Australia	1,665
France	1,482
Germany	1,371

Source: Niall McCarthy. "Who Works the Most Hours Every Year?" *Forbes*. January 8, 2018. Based on information from Statista and data from The Organization for Economic Co-Operation and Development (OECD).

Figure 5.7 This graph compares average annual hours worked by country. It does not distinguish between full-time and part-time employment. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The International Labour Organization and Bureau of Labor Statistics report that most people in the United States work more than forty hours per week, work significantly more hours per year than workers in many other countries, and are vastly more productive than they were half a century ago.[22]

Another consideration is tracking where our time is spent during commuting. The average commute time in major cities in the United States is twenty-six minutes, ranging from thirty-eight minutes in New York City to the shortest commute time of twenty minutes in Buffalo, New York.[23] When we add in commute times, work hours, and other required activities like sleeping and eating, we find that people struggle to find time for relaxation and personal activities. This large trend leads to recognizing that our working population in the United States and other countries would value novel approaches to completing tasks and making life simpler. For instance, several businesses have looked at making life easier and saving the consumer time, such as Amazon's One-Click-Checkout, grocery delivery, and product recommendations. Other examples include mobile businesses like pet grooming that come to your home, or diaper delivery services that pick up used diapers, wash and dry them, and return clean diapers to your home. Understanding consumer needs and problems opens the possibility of creating a business that addresses those needs or problems.

22 G.E. Miller. "The US Is the Most Overworked Developed Nation in the World." *20SomethingFinance*. January 2, 2018. https://20somethingfinance.com/american-hours-worked-productivity-vacation/
23 Jeff Desjardins. "Visualizing the Average Commute Time in US States and Cities." *Visual Capitalist*. April 1, 2018. https://www.visualcapitalist.com/average-commute-u-s-states-cities/

Another consumer trend is the demand for affordable housing. One solution involves offering more affordable "tiny homes" that make home ownership more accessible (Figure 5.8).[24] As one entrepreneurial opportunity materializes into a new product, spin-off ideas may also arise. The tiny home concept attracted the attention of groups that assist homeless veterans. The Veterans Community Project in Kansas City, has developed a community of forty-nine tiny homes for homeless veterans and the project is so successful that more than 500 cities around the country are building tiny home housing projects for veterans there.[25]

Figure 5.8 These tiny homes cost as little as $10,000 to build and come complete with one or two bedrooms, a small kitchen, and bath. (credit: photo provided by Veterans Community Project)

ENTREPRENEUR IN ACTION

Vestergaard

Vestergaard has a mission to prevent diseases, especially for vulnerable populations around the world, and to contribute to a healthier and more sustainable planet through good actions.

LifeStraw is a product that Vestergaard launched in 2005, making water safe to drink in areas where clean water is not readily available and redefining beliefs around safe drinking water. LifeStraw uses a combination of a hollow fiber membrane, a filtration process, and in some products, a second filtration process to remove chemicals like chlorine, lead, and pesticides.

- Apply the concepts of supply and demand in describing LifeStraw from the perspective of an entrepreneurial opportunity.
- What are three drivers that support the creation of LifeStraw?

5.3 Competitive Analysis

Learning Objectives

By the end of this section, you will be able to:

- Understand the elements of a competitive analysis
- Describe tools you can use to refine and focus your planning (three circles, SWOT, PEST)
- Recognize social media's role in saving time and money on research
- Understand how a business model helps determine the feasibility of an opportunity

Conducting a competitive analysis helps you focus your idea and identify your unique selling proposition and

24 Linda Federico-O'Murchu. "Tiny Houses: A Big Idea to End Homelessness." *NBC News*. February 26, 2014. https://www.nbcnews.com/business/real-estate/tiny-houses-big-idea-end-homelessness-n39316
25 Lauren Stewart. "Community Is Building Tiny Homes for Homeless Veterans in 500 Different Cities." *Do You Remember?* 2018. https://doyouremember.com/87151/community-builds-tiny-homes-for-homeless-veterans

competitive advantage.

Competitive Analysis

A competitive analysis should provide the entrepreneur with information about how competitors market their business and ways to penetrate the market by entry through product or service gaps in areas that your competitors do not serve or do not serve well. More importantly, competitive analysis helps the entrepreneur develop a competitive edge that will help create a sustainable revenue stream. For example, a big company like Walmart primarily competes on price. Small companies typically cannot compete on price, since the internal efficiencies and volume sales available to large corporations like Walmart are not available to small companies, but they may be able to compete successfully against Walmart on some other important variable such as better service, better-quality products, or unique buying experiences.

When preparing the competitive analysis, be sure to identify your competitors by product line or service segment. For an entrepreneur, this activity can be difficult when the industry does not yet exist. In the case of Bee Love, Palms Barber didn't have direct competitors, but she did have related competitors of traditional skin care products. Her unique idea of all-natural, honey-based skin care products created a new market. The competitive analysis might need to focus on substitute products rather than direct competitors. There are two main tools used in analysis of competitors: a competitive analysis grid and the "three circles" approach.

Competitive Analysis Grid

The competitive analysis grid should identify your competitors and include an assessment of the key characteristics of the competitive landscape in your industry, including competitive strengths and weaknesses and key success factors.

Table 5.2 provides an example of what a competitive analysis might look like for a bicycle shop in a tourist locale.

Competitive Analysis Grid for Sid's Cycle Shop in Branson, Missouri

Key Characteristics	Sid's Cycle	City Cycle	SpokeMasters	Target
Strengths	Product knowledge, Repair service	Repair service	High quality, Top brands	Price, hours (open seven days per week and online)
Weaknesses	Limited selection	Poor customer service	Pricing, no entry-level products	Low-end quality, no repair facilities
Product Quality Level	Low-middle	Middle-high	High-end	Entry-level
Price Point	Middle	Middle-high	High price	Lowest price

Table 5.2 This competitive analysis grid captures some of the main aspects of competitors within a given market.

Key Characteristics	Sid's Cycle	City Cycle	SpokeMasters	Target
Location of the business	Suburban strip-mall on busy highway	Outskirts of town on route 280	Downtown side street	Branson Mall
Promotion	Weekly ad in local newspaper, some radio and Internet/ social media	Advertising in local paper during season, Internet/ social media	Sponsors major bike race in area, Internet, social media	Advertises online and in Sunday newspaper (seasonally), Internet)

Table 5.2 This competitive analysis grid captures some of the main aspects of competitors within a given market.

As you complete an analysis for your venture's competitors, identify what contributes to the competitor's success. In other words, why do people purchase from the company? Some possible reasons include no nearby competitors, lower prices than competitors, a wider variety of products, offering services not offered elsewhere, or branding and marketing that appeals to the target market. Your analysis should inform you of a combination of key success factors within the industry (what it takes to be successful in the industry) and of what your competitors are not offering that is valued by your target market.

Another frequently used tool is a **SWOT analysis** (strengths, weaknesses, opportunities, and threats), which focuses on analyzing your venture's potential and builds on the knowledge gained from the competitive analysis grid and the three circles. You will need to identify the strengths your venture will need to support the competitive advantage identified through the competitive analysis tools. The weaknesses can be identified based on your current and foreseeable expectations. For a new venture, the opportunities and threats sections are based on current factors in the external environment that come from your research. In this context, opportunities are facts, changes, or situations within the external environment that could be favorably leveraged for the venture's success.

WORK IT OUT

Using SWOT Analysis to Evaluate Entrepreneurial Opportunity

Figure 5.9 A SWOT analysis can be used to identify the strengths, weaknesses, opportunities, and threats of a potential

entrepreneurial opportunity. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

One way to evaluate a business idea is to prepare a SWOT analysis (Figure 5.9). Note that strengths and weaknesses are internal to the entrepreneur, while opportunities and threats are external factors. Strengths are capabilities and advantages of the entrepreneur, including education, experience, and personal or professional contacts. Weaknesses are disadvantages of the entrepreneur, which could include lack of knowledge or experience. Opportunities are positive events that the entrepreneur can develop to their benefit. This could include development of new technologies, changes in consumer tastes and preferences, market growth, and new laws and regulations. Threats can be anything that could potentially harm the business or prevent the business from becoming successful such as competition, negative changes in economic conditions, and new laws or regulations.

- If you were starting a new business venture, what strengths would you be able to leverage to help your business be successful?
- Provide some examples of personal or professional weaknesses an entrepreneur might face when starting a new business.
- Discuss three occurring events such as new laws and regulations, changes in consumer tastes and preferences, or developing new technologies that could provide business opportunity for a new business venture.

Another tool that can be used to analyze opportunities and threats section is called PEST analysis (political, economic, societal, technology). In this analysis, we identify issues in each of these categories. Figure 5.10 shows an example of the topics that could be placed in a PEST analysis. The chapter on Fundamentals of Resource Planning discusses this tool as it relates to resource procurement.

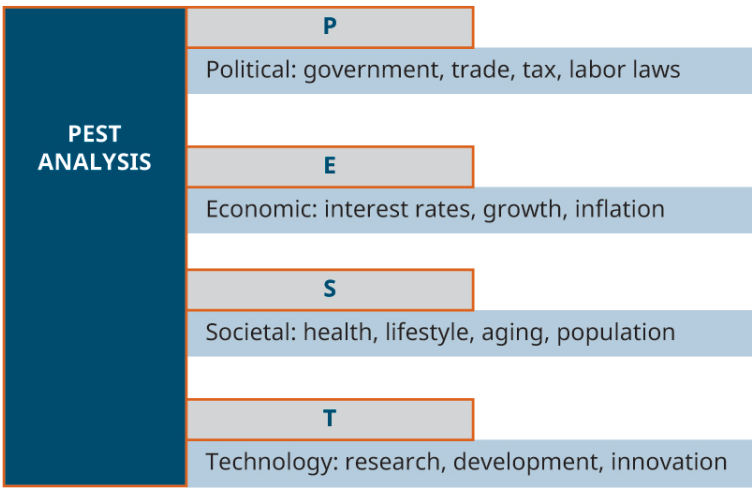


Figure 5.10 A PEST analysis can help identify opportunities and threats that can be used in a SWOT analysis. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Each of these categories should be completed with relevant facts related to your entrepreneurial opportunity. After completing this analysis, you then determine if these facts, or factors, would be placed in the opportunity section or the threat section of the SWOT.

Three Circles Tool

Another tool that can be used in competitive analysis is the three circles tool (Figure 5.11). The goal is to identify competitors' strengths and competitive advantages with any overlaps among competitors. Then, you would identify values or features not offered by competitors. This gap in value or offered services helps to identify your **unique selling proposition** and thereby your competitive advantage.

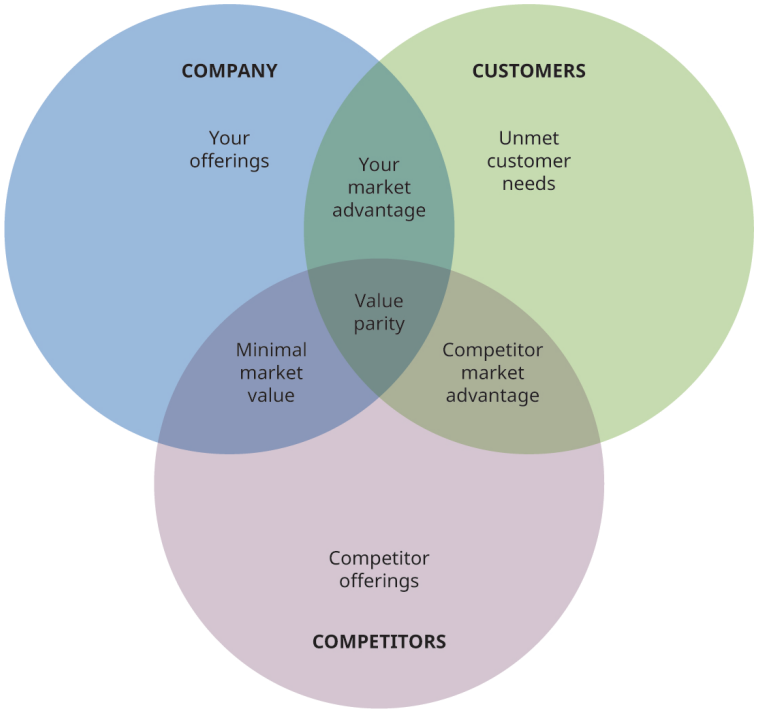


Figure 5.11 The three circles competitive analysis helps to identify where there is overlap and where there may be a gap in the market that a new venture could fill. The overlaps identify points of parity, the areas where competitors offer the same value with the important identification of the areas of unmet customer needs and how unique your competitive advantage is within the industry. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The unique selling proposition is important to the marketing plan and is often used as a slogan. It should also align with the value communicated by the product or company brand. These concepts are different from your venture's competitive advantage; the **competitive advantage** describes your venture's unique benefit, which supports growth of the venture, whereas the unique selling proposition describes the product or service itself, rather than the venture. Although these concepts are different, there should be alignment between the concepts.

For example, Amazon has a competitive advantage in its virtual presence, knowledge of the market, knowledge and application of technology, and knowledge of the industry. Through these competitive advantages, Amazon offers unique combinations of benefits to their customers, such as one-click checkout and algorithm-based recommendations using data mining to track an individual customer's preferences. Amazon's unique selling proposition becomes making the purchase as easy and as accurate as possible, whereas their competitive advantage lies in their ability to foresee future advances and act on those predictions, even to the point of shaping the industry.

The competitive advantage results from the analysis of the strengths and unique aspects of a venture, an analysis of the industry, including competitor's advantages, customer needs, and what the venture provides within this competitive landscape. The unique selling proposition should support the competitive advantage, just as the competitive advantage needs to support the unique selling proposition.

Social Media's Role in Research

For almost all new business ventures, two key issues related to research are time and money. Large-scale research projects can take months or longer, and cost a significant amount of money. Social media can offer some opportunities to overcome these concerns. Ray Nelson, writing for *Social Media Today*, reports several ways that social media can provide speedy, low-cost market research: tracking trends in real-time, helping the entrepreneur "learn the language" of their potential customers, discovering unnoticed trends by engaging consumers, and performing market research using a very cost-efficient means.[26] If the entrepreneur can perform social media research on their own, the cost will primarily be in terms of time. But the time it will take to conduct research through social media platforms such as Facebook or Twitter is usually well spent. This research should include learning the unique selling proposition of competitors, understanding their competitive advantage, and identifying what the customer values, which can be rather difficult. For example, before Amazon recognized that people are busy, were we aware that we wanted faster check-out processes for making purchases? Or were we aware that we wanted the package delivered to our home to be easier to unwrap? And yet, if we asked Amazon shoppers what they value in shopping at Amazon, we will receive answers that support an easier and faster process.

Another technique would be to read through customer reviews on Amazon (or another company related to your entrepreneurial venture) to find out what customers like and don't like about existing products and brands. You can also develop your own surveys on an app like SurveyMonkey and send them to customers and prospective customers. This usually works when sent to persons who have a strong interest in the product or issue rather than randomly sending out surveys.

Business Models and Feasibility

Part of the analysis in determining if your idea is an actual entrepreneurial opportunity is identifying a feasible business model. A **business model** is a plan for how the venture will be funded; how the venture creates value for its stakeholders, including customers; how the venture's offerings are made and distributed to the end users; and how income will be generated through this process. Basically, a business model describes how a venture will create a profit by describing each of these actions. The business model at this stage is composed of four components: the offering, customers, infrastructure, and financial viability (Figure 5.12). A fuller version of the business model is covered in Business Model and Plan.

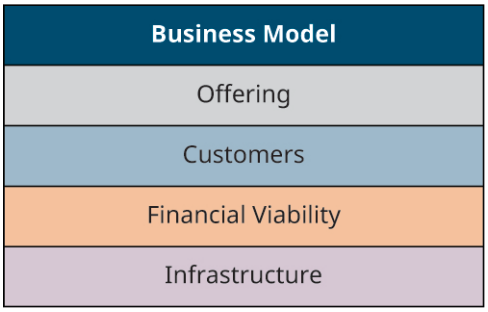


Figure 5.12 A business model has four components: the offering, customers, infrastructure, and financial viability. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The **offering** refers to the product or service you will be selling, the value proposition, and how you will reach and communicate with your target customers. The customer value proposition includes a detailed description of the products and services you will offer to customers, and what benefits (value) the customer will derive from using your product or service. The customer benefit could be the ability to do something more easily, more quickly, or at a lower cost than customers could before. The benefit could also solve a problem no one else has solved.

26 Ray Nelson. "How to Use Social Media for Market Research." *Social Media Today*. March 19, 2013. https://www.socialmediatoday.com/content/how-use-social-media-market-research

ARE YOU READY?

Writing a Customer Value Proposition

It is helpful to write out your customer value proposition. Then you have a draft to review and tweak as your ideas develop. Here is a general structure you can follow:[27]

- Start with a headline-style statement that describes how your offering benefits the customer.
- Provide a few sentences or a brief paragraph that explains the offering in more detail. Be sure to make clear what the offering is, who the customer is, and why you are offering it.
- Consider including a bulleted list or checklist highlighting 3–5 features of the product or benefits the customer will receive.
- If possible, add a graphic that engages interest or reinforces the idea.

Customers are the people you will be serving, including potential customers from one or more market segments, or subsections of the market categorized by similar interests or needs. Products seldom appeal to everyone, so the entrepreneur needs to determine, through high-level segmentation and targeting analysis, which segments of the market would make the most sense for the business, and the market environment and dynamics. Some products might appeal to market segments based on age or income, whereas other products might appeal to customers based on their lifestyle. A sign of a potential market opportunity is when a certain market is experiencing rapid growth. This could be a city with a fast-growing population, or it could be a style or consumer trend that is really taking off. The chapter on Entrepreneurial Marketing and Sales goes into more detail about these topics.

Infrastructure refers to all the resources the entrepreneur will need to launch and sustain the business venture. These include people, products, facilities, technology, suppliers, partners, and finances, all of which the entrepreneur must have to fulfill the customer value proposition.

Financial viability relates to the long-term financial sustainability of an organization to fulfill its mission. This goes back to our definition of an entrepreneurial opportunity. Knowing that the venture solves a sizable and significant problem that the target market is willing to purchase is a key piece in determining financial viability. This category also addresses how the venture will create profits.

For example, would a subscription-based business model fit the target market and venture's success? Currently, we see a significant growth in startups offering subscription services. What are the benefits to this sales method? For the venture, this model increases upfront cash to support the growth of the venture, especially when customers pay a year in advance for products that will be delivered over the subsequent twelve months. Receiving the payment prior to completing the sales provides the venture with operating cash to support current and future growth. The benefit to the customer in this situation is fewer transactions. The customer knows that the payment covers the next twelve months' worth of benefits (the received product or service) with no further purchases until the subscription runs out.

Another choice involves deciding whether to have a physical location, a virtual location, or both. Financial viability means exploring the benefits and drawbacks of various methods in creating your business model.

27 Modified from Lindsay Kolowich. "How to Write a Great Value Proposition [Infographic]." HubSpot/Marketing. June 5, 2018. https://blog.hubspot.com/marketing/write-value-proposition

WORK IT OUT

Researching Target Markets with Census Data

Practice conducting research by going to www.census.gov and two other sources to identify a specific target market for a product that interests you. Include the target market's:

- Disposable income. You might ask whether the target market has sufficient disposable income to purchase this product.
- Demographics
- Psychographics (the combination of buying personality behaviors and demographics)
- How you as the entrepreneur could reach this target market.

When you have a business idea that you have been researching and find that there is a large enough market that has a need that your idea meets, that this target market has the willingness and ability to satisfy the need through purchasing the provided solution, that you have access to the necessary resources to build an infrastructure for your business, that you have the right mix of products and services with a sound value proposition, and that you can secure funding, you have a real opportunity. This chapter has introduced you to all of these concepts. Further chapters delve into them in more depth.

Key Terms

business model plan for how venture will be funded; how the venture creates value for its stakeholders, including customers; how the venture's offerings are made and distributed to the end users; and the how income will be generated through this process

competitive advantage describes your venture's unique benefits that poise it for growth

creative destruction theory developed by Joseph Schumpeter stating that entrepreneurial innovation is the disruptive force that creates and sustains economic growth, though in the process, it destroys established companies and disrupts employment

customers people the business will be serving, including potential customers from one or more market segments

demand need or desire for the outputs, the product or services

demographics statistical factors of a population or group, such as information about age, gender, income, race, or ethnicity

entrepreneurial opportunity point at which identifiable consumer demand meets the feasibility of satisfying the requested product or service and meets the following conditions: significant market demand, significant market structure and size, significant margins, and resources to support the venture's success

financial viability long-term financial sustainability of an organization to fulfill its mission

gig economy market system in which independent contractors fill a variety of positions

infrastructure all resources the entrepreneur will need in order to launch and sustain a business venture

offering actual product or service, its value proposition, and how you will reach and communicate with your target customers

opportunity screening process used to evaluate innovative product ideas, strategies, and marketing trends, focusing on financial resources, skills of the entrepreneurial team, and competition

primary research research that involves gathering new data

secondary research research that uses existing data

shared economy economy in which some assets are not in use, which may present an entrepreneurial opportunity

supply amount of a product or service produced

SWOT analysis strategic analytical tool used to help a potential venture or existing company identify its strengths, weaknesses, opportunities, and threats related to business competition

unique selling proposition marketer's rationale as to why a product or service is different/better than the competitor's products

Summary

5.1 Entrepreneurial Opportunity

Entrepreneurial opportunity exists when consumer demand meets the feasibility of bringing the product or service to market. Joseph Schumpeter, an early scholar of entrepreneurship, identified creative destruction—when innovation is disruptive and creates potential entrepreneurial opportunities. Schumpeter's focus on economics led him to categorize potential opportunities based on supply, demand, or changes in how technology is used.

Burgeoning entrepreneurs should be engaged with industries of interest to remain informed and aware of opportunities to research. Additionally, they should be attentive to drivers of opportunity, such as emerging funding options, technological advancements, and economic factors.

5.2 Researching Potential Business Opportunities

Researching the viability of your entrepreneurial idea will help you determine whether the venture is currently worth pursuing. Use primary and secondary research to determine whether there is adequate demand, market structure and size, and the needed margins and resources to launch and sustain the enterprise.

Entrepreneurs researching options should also be aware of industry and consumer sources of opportunities.

5.3 Competitive Analysis

A competitive analysis helps determine the viability of your idea by considering how feasible it is within a specific competitive landscape. Tools such as a competitive analysis grid, a SWOT analysis, a PEST analysis, and the three circles approach can help you further examine issues and refine your plans.

Review Questions

1. What is entrepreneurial opportunity?
2. What are five methods through which an entrepreneur can create new economic opportunities, according to Joseph Schumpeter?
3. What are some factors that might indicate it is a good time to start a business?
4. When should an entrepreneur explore opportunities?
5. What should a potential entrepreneur research before starting a business?
6. What kind of information is available in census data and how might that data be useful?
7. Compare and contrast supply-based opportunities and demand-based opportunities.
8. How can using a PEST analysis contribute to discovering new patterns of trends for recognizing entrepreneurial opportunities?
9. What is a SWOT analysis and how is it useful?
10. What is a unique selling proposition?
11. What is a business model?

Discussion Questions

1. Explain the difference between an idea and an entrepreneurial opportunity. Why is it important to recognize if your idea is truly an entrepreneurial opportunity or only an idea?
2. Is now a good time to start a business? Why or why not?
3. If you were thinking about starting a clothing store for teens and young women in your hometown, what census information do you think would be useful to you?
4. What new patterns or behaviors have you noticed within your society or the country's society?
5. What unused resources are present in your own life that could be translated into a shared economy idea for a new venture?
6. What spin-off ideas can you think of that support a gig economy? For example, what services or products might gig employees value or gig employers value?
7. What are some of the reasons for business failures? If you were starting a business, what are some actions you could take to increase your potential for success?
8. Many entrepreneurs like Chris Johnson, who invented the ramen noodle cooker and Palms Barber had ordinary problems they were trying to solve. What are some examples of ordinary problems you could solve if you could invent a product?
9. How do social enterprises like Bee Love help the community? What problem was Palms Barber trying to solve? What problems did the company end up solving?

Case Questions

1. Mandy Tillman was a high school student who lived in a rural area of Oklahoma. Mandy was only fourteen years old but wanted to make some extra money for her family's trip to the Grand Canyon the following summer. While shopping with her parents, she noticed there was only one place in town to buy flats with flowers and vegetables for spring planting, and there was not much of a selection. Mandy made a note of the various types of plants and flowers the store sold and how much they sold for.
   When Mandy got home from shopping with her parents, she went online to see how much the seeds and equipment would cost. Her parents liked the idea of Mandy earning some money of her own to spend on vacation and made a large area in the basement available for her to start her plants.
   A. What else should Mandy know about this business before getting started?
   B. What else do you think Mandy needs to start this business?
   C. Do you see any potential problems with this business idea?
   D. What are some ways Mandy can sell her plants?
   E. Is this a business idea or an entrepreneurial opportunity?

2. Research the eyeglass company Warby Parker.
   A. What is Warby Parker's business model?
   B. What is the value proposition offered by Warby Parker?
   C. Describe Warby Parker's target market? What resources did you use to identify their target market?
   D. If Warby Parker did not exist and you decided that you wanted to open a direct to consumer eyeglass company, what would be the top five factors you would research to determine if your idea was truly an entrepreneurial opportunity?

3. Travis and Katelyn loved backpacking and had hiked the Appalachian Trail twice. Although they had been backpacking for several years, each time they went out on the trail, they learned something new. Almost every backpacker they met was quick to offer a good tip on the best clothing or equipment for the trail. Travis and Katelyn decided to start a backpacker's blog and sell advertising space to manufacturers and retailers of backpacking gear.
   A. If you were launching a company to help back packers trek through the wilderness, what products would you provide and what would be their unique selling propositions?
   B. What benefit would you build into your website that would attract backpackers to your website? Consider how you would distinguish your website from competitor websites.
   C. Using PEST around your knowledge of backpacking and interest in starting a business related to backpacking, identify one fact for each of the PEST categories that could be useful in identifying new information or patterns to support this business.
   D. How would you change your business model based on your answers to the previous question?

Suggested Resources

5.2 Researching Potential Business Opportunities

American Fact Finder (market research): http://factfinder2.census.gov/main.html

FedStats (statistics from more than 100 federal agencies): https://www.usa.gov/statistics

FindLaw Small Business Center (business forms): https://smallbusiness.findlaw.com/

National Federation of Independent Business: https://www.nfib.com/business-resources

The Small Business National Center: https://sites.google.com/a/uca.edu/sbanc/home

The U.S. Small Business Administration (SBA): www.sba.gov

Top Franchises of 2019: https://www.entrepreneur.com/franchise500/2019

U.S. patent and Trademark Office: https://www.uspto.gov/

General Business Statistics: https://www.census.gov/eos/www/naics/, http://www.census.gov/library/publications/2011/compendia/statab/131ed.html

Consumer Statistics: https://www.federalreserve.gov/releases/G19/, https://www.cpsc.gov/Research--Statistics

Demographics: https://factfinder.census.gov/faces/nav/jsf/pages/index.xhtml, http://www.bls.gov/bls/demographics.htm

Economic Indicators: https://www.bls.gov/cpi/, bea.gov

Employment Statistics: https://stats.bls.gov/bls/employment.htm

Income Statistics: https://www.bls.gov/cps/earnings.htm, https://www.bls.gov/data/#employment

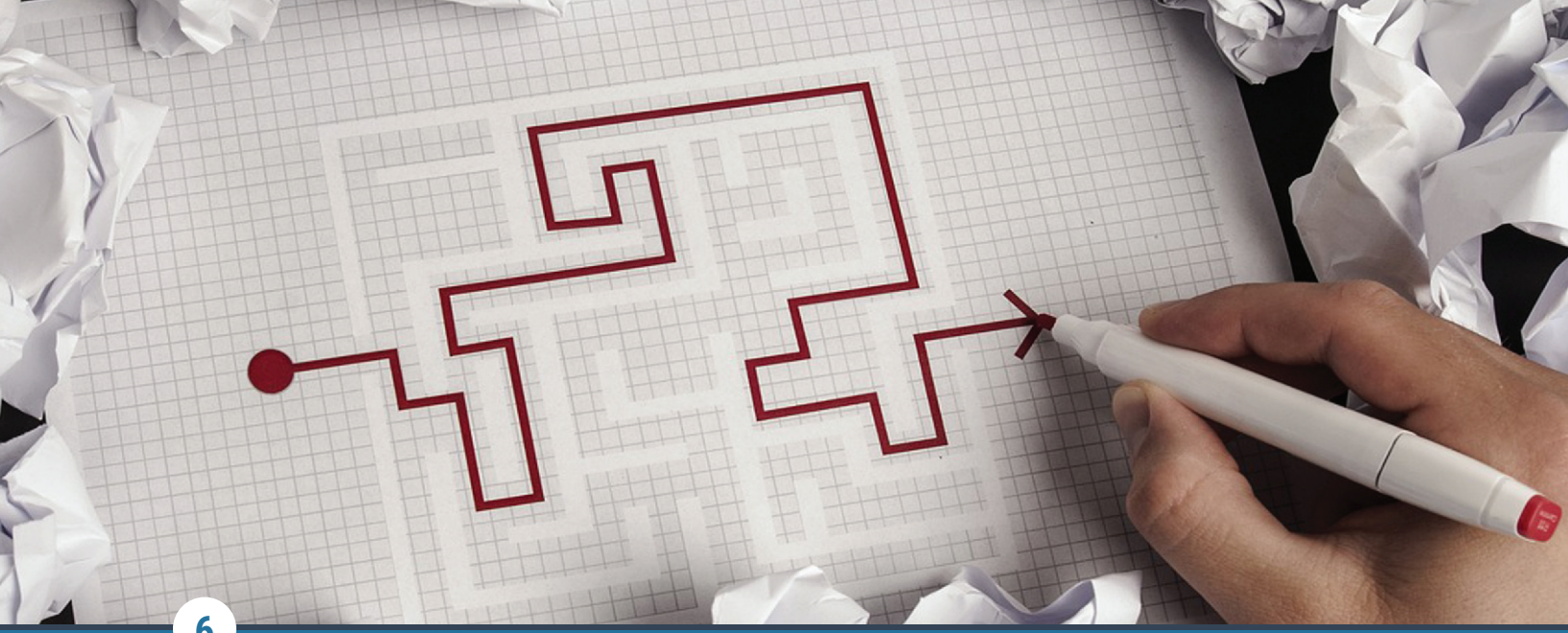
Money and Interest Rates: https://www.federalreserve.gov/releases/h15/, https://www.federalreserve.gov/data.htm

Production and Sales Statistics: https://www.bea.gov/data/consumer-spending/main,

Trade Statistics: https://www.bea.gov/data/economic-accounts/international#bop, https://usatrade.census.gov/

Statistics of specific Industries: https://www.census.gov/eos/www/naics/, https://www.census.gov/programs-surveys/susb.html

https://www.sba.gov/business-guide/plan-your-business/market-research-competitive-analysis#section-header-5



6

Problem Solving and Need Recognition Techniques

Figure 6.1 Sometimes, navigating from the recognition of an opportunity to overcoming problems in the development of that opportunity can feel like winding through a maze. (credit: modification of "human hand company paper solutions" by "Eluj"/Pixabay, CC0)

Chapter Outline

6.1 Problem Solving to Find Entrepreneurial Solutions
6.2 Creative Problem-Solving Process
6.3 Design Thinking
6.4 Lean Processes

Introduction

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Marah Lidey and Naomi Hirabayashi met when they worked together at DoSomething.org, a youth-oriented global nonprofit organization. They considered each other aspirational peers—accessible friends they looked up to and leaned on. While working together, they got the idea to turn the support they gave each other into a product idea: an inspirational platform that would send users a motivational text message each day. In 2015, Hirabayashi and Lidey began to focus on turning their idea into a reality. They conducted a test with seventy individuals before publicly releasing Shine in beta in October 2015. They formally left DoSomething.Org in April 2016 and their startup venture, Shine, was born.

The problem Shine tackles is that "self-help is broken" and its value proposition addresses in part what is known as "the confidence gap," often cited as a barrier that holds women back when it comes to advancing in their careers, raising money, investing, and planning retirement. Shine has four pillars it is built to address: mental health, confidence, daily happiness, and productivity. As of 2018, the Shine community had two million users from 189 countries. What began as a motivational text message service has since evolved to include an app and additional services such as Shine Talks and audio challenges.

Hirabayashi and Lidey recognized a need—or an *entrepreneurial opportunity*. You learned about identifying opportunities in the chapter on Identifying Entrepreneurial Opportunity. This chapter will explore what

happens next—the problem solving and need recognition techniques that entrepreneurs employ to carry the idea forward, and to solve issues that arise as the enterprise advances. Problem solving is essential to the genesis of entrepreneurship. At the same time, problem-solving techniques can be used in management and in an individual's everyday personal life.

6.1 Problem Solving to Find Entrepreneurial Solutions

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Learning Objectives

By the end of this section, you will be able to:

- Define problem solving in the context of entrepreneurship
- Describe and compare the adaptive model and the innovative model of problem solving
- Identify the skills entrepreneurs need for effective problem solving
- Identify types of problem solvers

As you've learned, entrepreneurs often visualize an opportunity gap, a gap between what exists and what could exist, as Hirabayashi and Lidey did with Shine. **Entrepreneurial problem solving** is the process of using innovation and creative solutions to close that gap by resolving societal, business, or technological problems. Sometimes, personal problems can lead to entrepreneurial opportunities if validated in the market. The entrepreneur visualizes the prospect of filling the gap with an innovative solution that might entail the revision of a product or the creation of an entirely new product. In any case, the entrepreneur approaches the problem-solving process in various ways. This chapter is more about problem solving as it pertains to the entrepreneur's thought process and approach rather than on problem solving in the sense of opportunity recognition and filling those gaps with new products.

For example, as we read in Identifying Entrepreneurial Opportunity, Sara Blakely (as shown in Figure 6.2) saw a need for body contouring and smoothing undergarments one day in the late 1990s when she was getting dressed for a party and couldn't find what she needed to give her a silhouette she'd be pleased with in a pair of slacks. She saw a problem: a market need. But her *problem-solving efforts* are what drove her to turn her solution (Spanx undergarments) into a viable product. Those efforts came from her self-admitted can-do attitude: "It's really important to be resourceful and scrappy—a glass half-full mindset."[1] Her efforts at creating a new undergarment met resistance with hosiery executives, most of whom were male and out of touch with their female consumers. The hosiery owner who decided to help Blakely initially passed on the idea until running it by his daughters and realizing she was on to something. That something became Spanx, and today, Blakely is a successful entrepreneur.[2]

1 Helen Lock. "'I Put My Butt on the Line': How Spanx Took Over the World." *The Guardian.* July 11, 2016. https://www.theguardian.com/small-business-network/2016/jul/11/put-butt-on-the-line-how-spanx-world
2 Gary Keller. "Business Success Series, Part 1: Sara Blakely-Spanx." *The One Thing.* n.d. https://www.the1thing.com/blog/the-one-thing/business-success-series-part-1-sara-blakely-spanx/

Figure 6.2 Sara Blakely (right) participates in a discussion at the 2018 Fast Company Innovation Festival. (credit: "Ed Bastian and Sara Blakely at the Fast Company Innovation Festival" by "Nan Palmero"/Flickr, CC BY 2.0)

Before getting into the heart of this chapter, we need to make a distinction: *Decision making is different from problem solving*. A decision is needed to continue or smooth a process affecting the operation of a firm. It can be intuitive or might require research and a long period of consideration. Problem solving, however, is more direct. It entails the solution of some problem where a gap exists between a current state and a desired state. Entrepreneurs are problem solvers who offer solutions using creativity or innovative ventures that exploit opportunities. This chapter focuses on different approaches to problem solving and need recognition that help potential entrepreneurs come up with ideas and refine those ideas.

Two Problem Solving Models: Adaptive and Innovative

There are two prominent established problem-solving models: *adaptive* and *innovative*. A renowned British psychologist, Michael Kirton, developed the Kirton Adaption-Innovation (KAI) Inventory to measure an individual's style of problem solving.[3] Problem-solving preferences are dependent on the personality characteristics of originality, conformity, and efficiency, according to Kirton. The KAI inventory identifies an individual's problem-solving approach by measuring agreement with statements that align with characteristics, such as the ability to produce many novel ideas, to follow rules and get along in groups, and to systematically orient daily behavior. The results categorize an individual as an innovator or an adaptor. Innovators are highly original, do not like to conform, and value efficiency less than adaptors.

The first and more conservative approach an entrepreneur may use to solve problems is the adaptive model. The **adaptive model** seeks solutions for problems in ways that are tested and known to be effective. An adaptive model accepts the problem definition and is concerned with resolving problems rather than finding them. This approach seeks greater efficiency while aiming at continuity and stability. The second and more creative approach is the **innovative model** of entrepreneurial problem solving, which uses techniques that are unknown to the market and that bring advantage to an organization. An innovative problem-solving style challenges the problem definition, discovers problems and avenues for their solutions, and questions existing assumptions—in a nutshell, it does things differently. It uses outside-the-box thinking and searches for novel solutions. Novelty is a shared trait of creative entrepreneurship, and it's why entrepreneurs gravitate toward this method of problem solving. According to Dr. Shaun M. Powell, a senior lecturer at the University of Wollongong, Australia: "Creative entrepreneurs are notable for a distinctive management style that is based on intuition, informality and rapid decision making, whereas the more conventional thinking styles are not in accord with the unique attributes of creative entrepreneurs."[4] This way of problem solving doesn't alter an existing product. It is the creation of something entirely new.

3 "Characteristics of Adaptors and Innovators." *Kirton KAI Inventory Tool.* n.d. http://pubs.acs.org/subscribe/archive/ci/31/i11/html/11hipple_box3.ci.html

For example, healthcare facilities have long been known as a source of methicillin-resistant *Staphylococcus aureus* (MRSA), a deadly infection that can have long-term effects on patients. Vital Vio, led by Colleen Costello, has developed white light technology that effectively disinfects healthcare facilities by targeting a molecule specific to bacteria. The light, safe to humans, can burn constantly to kill regenerative bacteria. An adaptive problem-solving model would seek to minimize harm of MRSA within a hospital—to respond to it—whereas the Vital Vio is an entirely new technique that seeks to eliminate it. Adaptive solutions to MRSA include established processes and protocols for prevention, such as having doctors, nurses, and other healthcare providers clean their hands with soap and water, or an alcohol-based hand rub before and after patient care, testing patients to see if they have MRSA on their skin, cleaning hospital rooms and medical equipment, and washing and drying clothes and bed linens in the warmest recommended temperatures.[5]

LINK TO LEARNING

Visit *Inc. Magazine* for support and advice for up-and-coming startups (https://openstax.org/l/52AdviceStartup) to learn more. Examples of how "Dorm Room" entrepreneurs spot and pursue opportunities are shared along with tips and advice for making your startup a success.

Problem-Solving Skills

While identifying problems is a necessary part of the origin of the entrepreneurial process, managing problems is an entirely different aspect once a venture is off the ground and running. An entrepreneur does not have the luxury of avoiding problems and is often responsible for all problem solving in a startup or other form of business. There are certain skills that entrepreneurs possess that make them particularly good problem solvers. Let's examine each skill (shown in Figure 6.3) .

Figure 6.3 These are a few of the skills that entrepreneurs possess that aid in solving problems. (attribution: Copyright Rice

4 Shaun Powell. "The Management and Consumption of Organisational Creativity." *Journal of Consumer Marketing* 25, no. 3 (2008): 158–166.

5 N.C Healthcare-Associated Infections Prevention Program. *Healthcare-Associated Infections in North Carolina: 2014 Annual Report, Healthcare Consumer Version.* April 2015. https://epi.dph.ncdhhs.gov/cd/hai/figures/hai_apr2015_consumers_annual.pdf

University, OpenStax, under CC BY NC-SA 4.0 license)

Critical Thinking

Critical thinking is the complex analysis of a problem or issue with the goal of solving the problem or making a decision. The entrepreneur analyzes and peels away the layers of a problem to find the core of an issue facing a business. The entrepreneur focuses on the heart of the problem and responds reasonably and openly to suggestions for solving it. Critical thinking is not only important for developing entrepreneurial ideas: it is a sought-after asset in education and employment. Entrepreneur Rebecca Kantar dropped out of Harvard in 2015 to found the tech startup Imbellus, which aims to replace standardized college admissions tests like the SAT with interactive scenarios that test critical-thinking skills. Many standardized tests may include multiple choice questions asking for the answer to a straightforward knowledge question or math problem. Kantar seeks to create tests that are more concerned with the analytic ability and reasoning that goes into the process of solving the problem. Imbellus says it aims to test "how people think," not just what they know. The platform, which has not yet launched, will use simulations for its user assessments.[6]

LINK TO LEARNING

Read more about problem solving and EnterpriseWorks/Vita's story (https://openstax.org/l/52ProbSolve) at *Harvard Business Review*.

Communication

Communication skills, the ability to communicate messages effectively to an intended recipient, are the skills entrepreneurs use to pool resources for the purposes of investigating solutions leading to innovative problem solving and competitive advantage. Good communication allows for the free association of ideas between entrepreneurs and businesses. It can illustrate a problem area or a shared vision, and seeks stakeholder buy-in from various constituencies. Networking and communication within an industry allow the entrepreneur to recognize the position of an enterprise in the market and work toward verbalizing solutions that move an organization beyond its current state. By "verbalizing," we mean communication from and with the company/entity. Internal communications include company emails, newsletters, presentations, and reports that can set strategic goals and objectives, and report on what has been accomplished and what goals and objectives remain, so that employees within an organization are knowledgeable and can work on solving problems that remain within the organization. External communications could include press releases, blogs and websites, social media, public speeches, and presentations that explain the company's solutions to problems. They could also be investor pitches complete with business plans and financial projections.

Ideation exercises, such as brainstorming sessions (discussed in Creativity, Innovation, and Invention, are good communication tools that entrepreneurs can use to generate solutions to problems. Another such tool is a **hackathon**—an event, usually hosted by a tech company or organization, which brings together programmers and workers with other degrees of specialization within the company, community, or organization to collaborate on a project over a short period of time. These can last from twenty-four hours to a few days over a weekend. A hackathon can be an internal company-wide initiative or an external event that brings community participants together. A business model canvas, which is covered in Business Model and Plan and other activities outlined in other chapters can be used internally or externally to identify problems and work toward creating a viable solution.

6 Romesh Ratnesar. "What If Instead of Taking the SAT You Got to Play a Video Game?" *Bloomberg BusinessWeek*. March 19, 2019. https://www.bloomberg.com/news/features/2019-03-19/a-harvard-dropout-s-plan-to-fix-college-admissions-with-video-games

Networking is an important manifestation of useful communication. What better method is there of presenting one's concept, gaining funding and buy-in, and marketing for the startup than through building a network of individuals willing to support your venture? A network may consist of potential employees, customers, board members, outside advisors, investors, or champions (people who just love your product) with no direct vested interest. Social networks consist of weak ties and strong ties. Sociologist Mark Granovetter studied such networks back in the 1970s, and his findings still apply today, even if we include social media networks in the definition too. Weak ties facilitate flow of information and community organization, he said, whereas strong ties represent strong connections among close friends, family members, and supportive coworkers.[7] Strong ties require more work to maintain than weak ties (as illustrated by the strong lines and weak dotted lines in Figure 6.4) and in a business context, they don't lead to many new opportunities. Weak ties, in contrast, do open doors in that they act as bridges to other weak ties within functional areas or departments that you might not have had access to directly or through strong ties.[8]

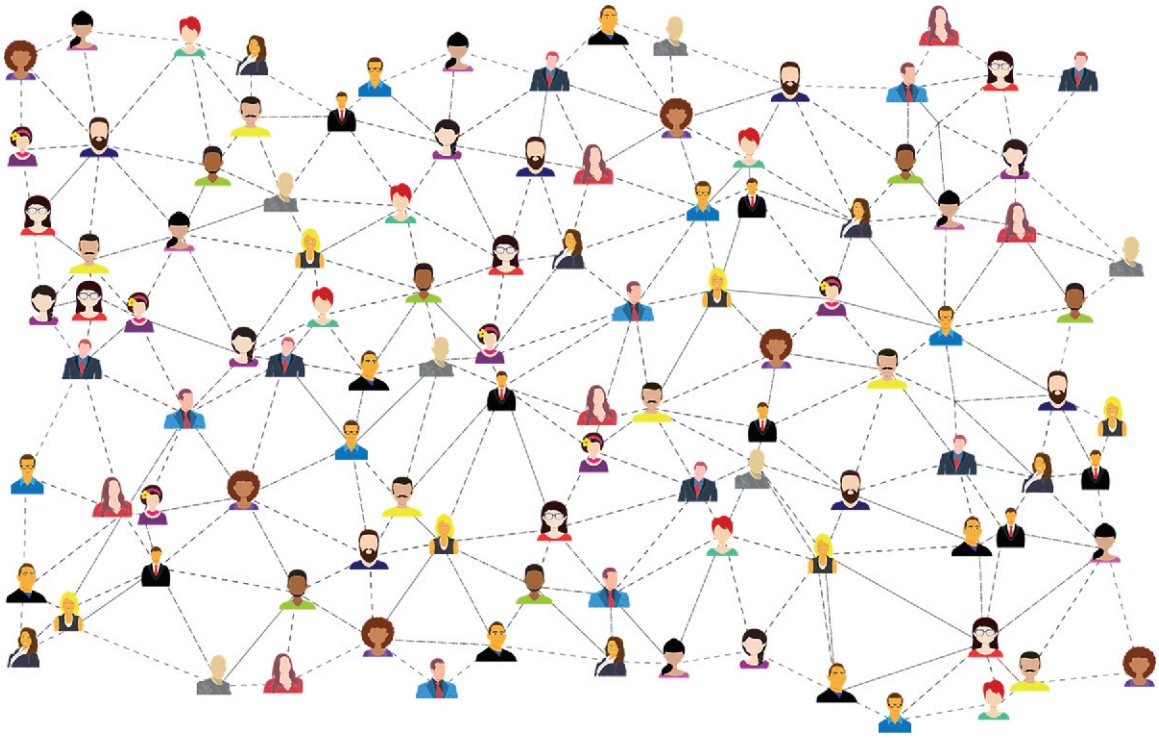

Figure 6.4 Networking results in connecting individuals who otherwise might not have met and who may be able to help each other solve problems. (credit: "social media connections networking" by "GDJ"/Pixabay, CC0)

In fact, many young entrepreneurs, including tech entrepreneur Oliver Isaacs, realize college is a great place to begin building teams. Isaacs is the founder of viral opinion network Amirite.com, which is widely credited as the place where Internet memes started and online slang got a foothold.[9] Amirite.com consists of a large network of pages and partnerships on Facebook and Instagram that reach 15 million users each month. Isaacs recommends using your alumni network to build a team and customer base for your own venture because you never know if you're talking to a future employee or partner.

Sharing of ideas and resources is highly valued in the entrepreneurial process. Communication is a vital skill in problem solving because the ability to identify and articulate the problem (define the problem space) is necessary to adequately address a problem. A problem can be too vague or broad or narrow. Thus, communicating the problem is important, as is conveying the solution.

7 Mark Granovetter. "The Strength of Weak Ties." *American Journal of Sociology* 5 (1973): 1360–1380.
8 Jacob Morgan. "Why Every Employee Should Be Building Weak Ties at Work." *Forbes.* March 11, 2014. https://www.forbes.com/sites/jacobmorgan/2014/03/11/every-employee-weak-ties-work/#277851063168
9 John White. "Top UK Influencer Oliver Isaacs Reveals What It Takes to Go Viral." *Inc.* August 6, 2017. https://www.inc.com/john-white/top-uk-influencer-oliver-isaacs-reveals-what-it-ta.html

Decisiveness

Decisiveness is as it sounds: the ability to make a quick, effective decision, not letting too much time go by in the process. Entrepreneurs must be productive, even in the face of risk. They often rely on intuition as well as on hard facts in making a choice. They ask what problem needs to be solved, think about solutions, and then consider the means necessary to implement an idea. And the decisions must be informed with research.

For example, as explained in Adam Grant's book *The Originals*, the co-founders of Warby Parker, a venture-backed startup focused on the eyewear industry, started their company while they were graduate students. At the time they knew little about the industry, but after conducting some detailed research, they learned that the industry was dominated by one major player—Luxottica. They used this information and other data to refine their strategy and business model (focusing mainly on value, quality, and convenience via an online channel). By the time they decided to launch the business, they had thought through the key details, and they attained rapid early success. Today Warby Parker has over 100 retail stores in the US, is profitable, and is valued at almost $2 billion.

Decisiveness is the catapult to progress. Amazon founder Jeff Bezos preaches the importance of decisiveness throughout his organization. Bezos believes that decisiveness can even lead to innovation. Bezos advocates for making decisions after obtaining 70 percent of the information you need to do so: "Being wrong may be less costly than you think, whereas being slow is going to be expensive for sure," Bezos wrote in a 2017 annual letter to stockholders.[10]

LINK TO LEARNING

Read this LinkedIn blog post on decisiveness (https://openstax.org/l/52decisiveness) to learn more.

Ability to Analyze Data

Data analysis is the process of analyzing data and modeling it into a structure that leads to innovative conclusions. Identifying Entrepreneurial Opportunity covered much of the sources of data that entrepreneurs might seek. But it is one thing to amass information and statistics. It is another to make sense of that data, to use it to fill a market need or forecast a trend to come. Successful founders know how to pose questions about and make meaning out of information. And if they can't do that themselves, they know how to bring in experts who can.

In addition to public sources of broad data, a business can collect data on customers when they interact with the company on social media or when they visit the company website, especially if they complete a credit card transaction. They can collect their own specific data on their own customers, including location, name, activity, and how they got to the website. Analyzing these data will give the entrepreneur a better idea about the interested audience's demographic.

In entrepreneurship, analyzing data can help with opportunity recognition, creation, and assessment by analyzing data in a variety of ways. Entrepreneurs can explore and leverage different data sources to identify and compare "attractive" opportunities, since such analyses can describe what has happened, why it happened, and how likely it is to happen again in the future. In business in general, analytics is used to help managers/entrepreneurs gain improved insight about their business operations/emerging ventures and make better, fact-based decisions.

Analytics can be descriptive, predictive, or prescriptive. Descriptive analytics involves understanding what has happened and what is happening; predictive analytics uses data from past performance to estimate future

10 Erik Larson. "How Jeff Bezos Uses Faster Better Decisions to Keep Amazon Innovating." *Forbes*. September 24, 2018. https://www.forbes.com/sites/eriklarson/2018/09/24/how-jeff-bezos-uses-faster-better-decisions-to-keep-amazon-innovating/#492c351b7a65

performance; and prescriptive analytics uses the results of descriptive and predictive analytics to make decisions. Data analysis can be applied to manage customer relations, inform financial and marketing activities, make pricing decisions, manage the supply chain, and plan for human resource needs, among other functions of a venture. In addition to statistical analysis, quantitative methods, and computer models to aid decision-making, companies are also increasingly using artificial intelligence algorithms to analyze data and make quick decisions.

Understanding of Business and Industry

Entrepreneurs need sound understanding of markets and industries. Often times, they are already working in a large organization when they see growth opportunities or inefficiencies in a market. The employee gains a deep understanding of the industry at hand. If the employee considers a possible solution for a problem, this solution might become the basis for a new business.

For example, consider a marketing agency that used traditional marketing for thirty years. This agency had an established clientele. An executive in the organization began studying social media analytics and social media. The executive approached the owner of the business to change processes and begin serving clients through social media, but the owner refused. Clients within the agency began to clamor for exposure on social media. The marketing executive investigated the possibility of building an agency in her locale servicing clients who wish to utilize social media. The marketing executive left the organization and started her own agency (providing, of course, that this is in compliance with any noncompete clauses in her contract). Her competitive advantage was familiarity with both traditional and social media venues. Later, the original agency started floundering because it did not offer social media advertising. Our intrepid executive purchased the agency to gain the clientele and serve those wishing to move away from traditional marketing.

A similar experience occurred for entrepreneur Katie Witkin. After working in traditional marketing roles, the University of Wisconsin-Madison graduate, pictured in Figure 6.5, left agency life behind four years out of college to cofound her own company, AGW Group. In 2009, Witkin had been interning at a music marketing agency that didn't have a social media department. She knew, both from her time at college and from observing industry trends, that social media was changing the way companies connected with customers. For her own venture, she expanded the focus to all supporting brands to manage all things digital. Today, the cultural and marketing communications agency has fifteen employees and big-name clients ranging from HBO to Red Bull.[11]

11 Stephanie Schomer. "How Getting Laid Off Empowered This Entrepreneur to Start Her Own Award-Winning Marketing Agency." *Entrepreneur.* January 15, 2019. https://www.entrepreneur.com/article/326212

Figure 6.5 Pictured is AGW Group cofounder Katie Witkin. (credit: photo provided by AGW Group)

Resourcefulness

Resourcefulness is the ability to discover clever solutions to obstacles. Sherrie Campbell, a psychologist, author, and frequent contributor to *Entrepreneur* magazine on business topics, put it this way:

> "There is not a more useful or important trait to possess than resourcefulness in the pursuit of success. Resourcefulness is a mindset, and is especially relevant when the goals you have set are difficult to achieve or you cannot envision a clear path to get to where you desire to go. With a resourcefulness mindset you are driven to find a way. An attitude of resourcefulness inspires out-of-the-box thinking, the generation of new ideas, and the ability to visualize all the possible ways to achieve what you desire. Resourcefulness turns you into a scrappy, inventive and enterprising entrepreneur. It places you a cut above the rest."[12]

Entrepreneurs start thinking about a business venture or startup by talking to people and procuring experts to help create, fund, and begin a business. Entrepreneurs are risk takers, passionate about new endeavors. If they don't have a college degree or a great deal of business experience, they understand there are many resources available to support them in the endeavor, such as the Service Corps of Retired Executives (SCORE) and the Small Business Administration (SBA). There are many sources available to fund the business with little or no debt and options, as you will see in the chapter on Entrepreneurial Finance and Accounting. The entrepreneur follows a vision and researches opportunities to move toward a dream.

For example, in the late 1990s, Bill McBean and his business partner Billy Sterett had an opportunity to buy an underperforming auto dealership that would make their company the dominant one in the market. Neither wanting to take cash from other ventures nor wanting to borrow more money and tie themselves to more debt, the entrepreneurs were resourceful by finding another path forward to obtaining the money necessary for the acquisition they both coveted. They changed banks and renegotiated their banking payback requirements, lowering their interest payments, reducing fees, and lowering their monthly payments, ultimately freeing up a significant amount of cash that allowed them to buy the new company.[13]

12 Sherrie Campbell. "6 Characteristics of Resourceful People That Bring Them Success." *Entrepreneur.* March 10, 2016. https://www.entrepreneur.com/article/272171

13 "Resourcefulness Is More Important Than Resources." *The Ecommerce Mindset: How Successful Store Owners Think.* n.d. https://www.oberlo.com/ebooks/mindset/resourceful-entrepreneur

Types of Problem Solvers

Entrepreneurs have an insatiable appetite for problem solving. This drive motivates them to find a resolution when a gap in a product or service occurs. They recognize opportunities and take advantage of them. There are several types of entrepreneurial problem solvers, including self-regulators, theorists, and petitioners.

Self-Regulating Problem Solvers

Self-regulating problem solvers are autonomous and work on their own without external influence. They have the ability to see a problem, visualize a possible solution to the problem, and seek to devise a solution, as Figure 6.6 illustrates. The solution may be a risk, but a self-regulating problem solver will recognize, evaluate, and mitigate the risk. For example, an entrepreneur has programmed a computerized process for a client, but in testing it, finds the program continually falls into a loop, meaning it gets stuck in a cycle and doesn't progress. Rather than wait for the client to find the problem, the entrepreneur searches the code for the error causing the loop, immediately edits it, and delivers the corrected program to the customer. There is immediate analysis, immediate correction, and immediate implementation. The self-regulating problem solvers' biggest competitive advantage is the speed with which they recognize and provide solutions to problems.

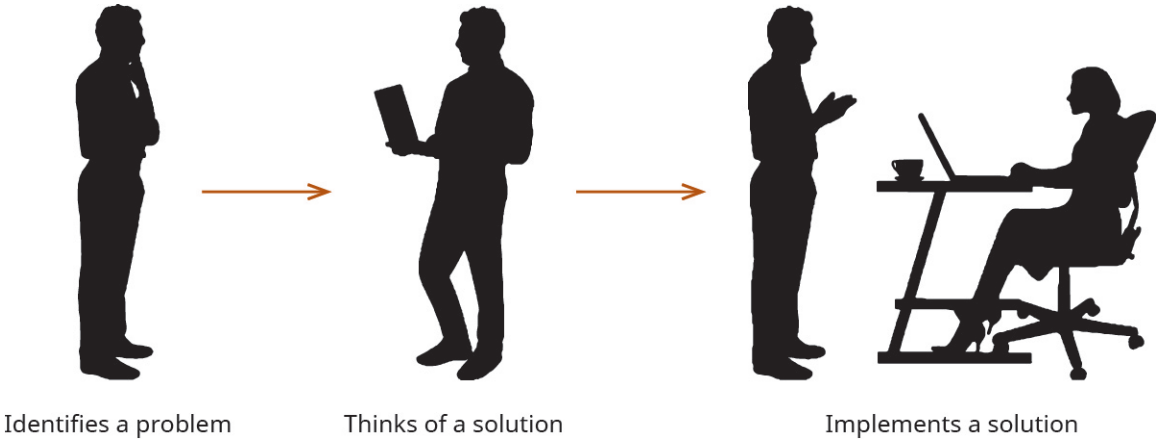

Figure 6.6 A self-regulating problem solver identifies a problem, thinks of solution, and then implements the solution. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Theorist Problem Solvers

Theorist problem solvers see a problem and begin to consider a path toward solving the problem using a theory. Theorist problem solvers are process oriented and systematic. While managers may start with a problem and focus on an outcome with little consideration of a means to an end, entrepreneurs may see a problem and begin to build a path with what is known, a theory, toward an outcome. That is, the entrepreneur proceeds through the steps to solve the problem and then builds on the successes, rejects the failures, and works toward the outcome by experimenting and building on known results. At this point, the problem solver may not know the outcome, but a solution will arise as experiments toward a solution occur. Figure 6.7 shows this process.

For example, if we consider Marie Curie as an entrepreneur, Curie worked toward the isolation of an element. As different approaches to isolating the element failed, Curie recorded the failures and attempted other possible solutions. Curie's failed theories eventually revealed the outcome for the isolation of radium. Like Curie, theorists use considered analysis, considered corrective action, and a considered implementation process. When time is of the essence, entrepreneurs should understand continual experimentation slows the problem-solving process.

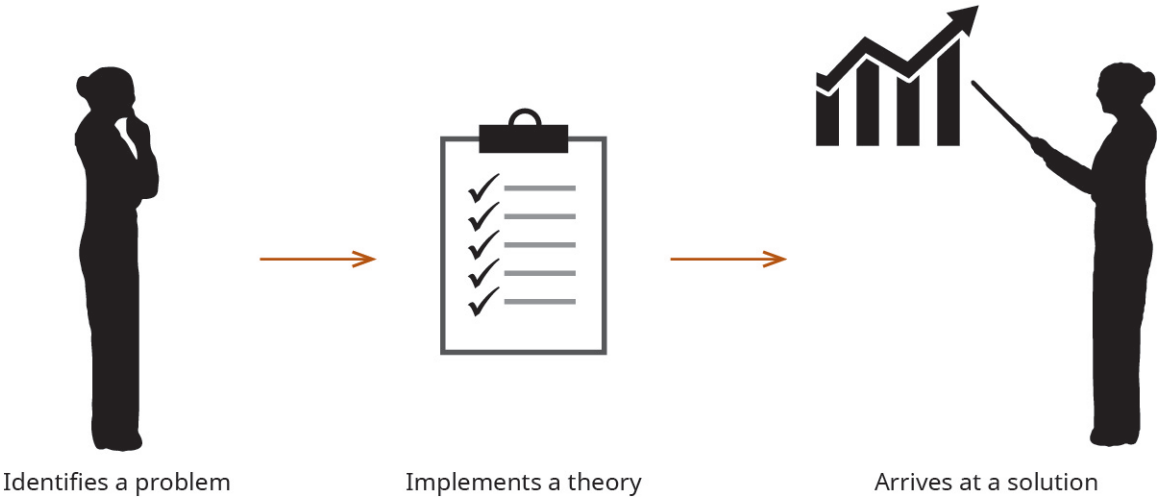

Figure 6.7 A theorist problem solver identifies a problem; implements a theory, sometimes repeatedly; and eventually arrives at a solution. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Petitioner Problem Solvers

Petitioner problem solvers (Figure 6.8) see a problem and ask others for solution ideas. This entrepreneur likes to consult a person who has "been there and done that." The petitioner might also prefer to solve the problem in a team environment. Petitioning the entrepreneurial team for input ensures that the entrepreneur is on a consensus-driven path. This type of problem solving takes the longest to complete because the entrepreneur must engage in a democratic process that allows all members on the team to have input. The process involves exploration of alternatives for the ultimate solution. In organizational decision-making, for example, comprehensiveness is a measure of the extent a firm attempts to be inclusive or exhaustive in its decision-making. Comprehensiveness can be gauged by the number of scheduled meetings, the process by which information is sought, the process by which input is obtained from external sources, the number of employees involved, the use of specialized consultants and the functional expertise of the people involved, the years of historical data review, and the assignment of primary responsibility, among other factors. Comprehensive decision-making would be an example of a petitioner problem-solving style, as it seeks input from a vast number of team members.

A *charette*—a meeting to resolve conflicts and identify solutions—is another example that employs a petitioner problem-solving approach. Often times, a developer of a new project might hold a community charette to aid in the design of a project, hoping to gain approval from elected officials. In the building example, this could consist of the developer and his team of architects, project designers, and people with expertise in the project working alongside community members, business executives, elected officials, or representatives like staff members or citizen-appointed boards like a planning board. Such an activity is representative of a petitioner problem-solving approach, as opposed to a developer representative designing the project with no input from anyone else.

Figure 6.8 A petitioner problem solver identifies a problem, discusses it with others, and arrives at solution agreeable to others. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

In summary, there is no right or wrong style of problem solving; each problem solver must rely on the instincts that best drive innovation. Further, they must remember that not all problem-solving methods work in every situation. They must be willing to adapt their own preference to the situation to maximize efficiency and ensure they find an effective solution. Attempting to force a problem-solving style may prevent an organization from finding the best solution. While general entrepreneurial problem-solving skills such as critical thinking, decisiveness, communication, and the ability to analyze data will likely be used on a regular basis in your life and entrepreneurial journey, other problem-solving skills and the approach you take will depend on the problem as it arises.

There are a number of resources online that can help analyze your problem-solving abilities. Mindtools.com is one such resource. These are useful to learn your general problem-solving tendencies before being called upon to apply them in a real-world setting. One of the problem-solving techniques available from mindtools.com offers that problems can be addressed from six different perspectives. Called CATWOE, the approach is an acronym for Customers, Actors (people within the organization), Transformative, Worldwide, Owner, and Environment (organizational).

LINK TO LEARNING

Learn more about the CATWOE technique (https://openstax.org/l/52CATWOE) for problem solving.

6.2 Creative Problem-Solving Process

Portions of the material in this section are based on original work by Geoffrey Graybeal and produced with support from the Rebus Community. The original is freely available under the terms of the CC BY 4.0 license at https://press.rebus.community/media-innovation-and-entrepreneurship/.

Learning Objectives

By the end of this section, you will be able to:

- Describe the five steps in the creative problem-solving process
- Identify and describe common creative problem-solving tools

Creativity can be an important trait of an entrepreneur, as the chapter on Creativity, Innovation, and Invention discussed. In that discussion, we learned about creativity's role in *innovation*. Here, we will look in more depth at creativity's role in *problem solving*. Let's first formally define **creativity** as the development of original ideas to solve an issue. The intent of being an entrepreneur is to break away from practical norms and use

imagination to embrace quick and effective solutions to an existing problem, usually outside the corporate environment.

The Steps of the Creative Problem-Solving Process

Training oneself to think like an entrepreneur means learning the steps to evaluating a challenge: clarify, ideate, develop, implement, and evaluate (Figure 6.9).

Figure 6.9 The process of creativity is not random; it is a specific and logical process that includes evaluation. The entrepreneur repeats the creative process until reaching a successful solution. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 1: Clarify

To **clarify** is the critical step of recognizing the existence of a gap between the current state and a desired state. This can also be thought of as having **need awareness**, which occurs when the entrepreneur notes a gap between societal or customer needs and actual circumstances. Clarifying the problem by speaking with clients and developing a detailed description of the problem brings the specifics of a problem to light. Failure to identify the specifics of a problem leaves the entrepreneur with the impossible task of solving a ghost problem, a problem that is fully unknown or unseen. To establish and maintain credibility, an entrepreneur must clarify the problem by focusing on solving the problem itself, rather than solving a symptom of the problem.

For example, a farm could have polluted water, but it would not be enough to solve the problem only on that farm. Clarifying would involve identifying the source of the pollution to adequately tackle the problem. After gaining an understanding of a problem, the entrepreneur should begin to formulate plans for eliminating the gap. A fishbone diagram, as shown in Figure 6.10, is a tool that can be used to identify the causes of such a problem.

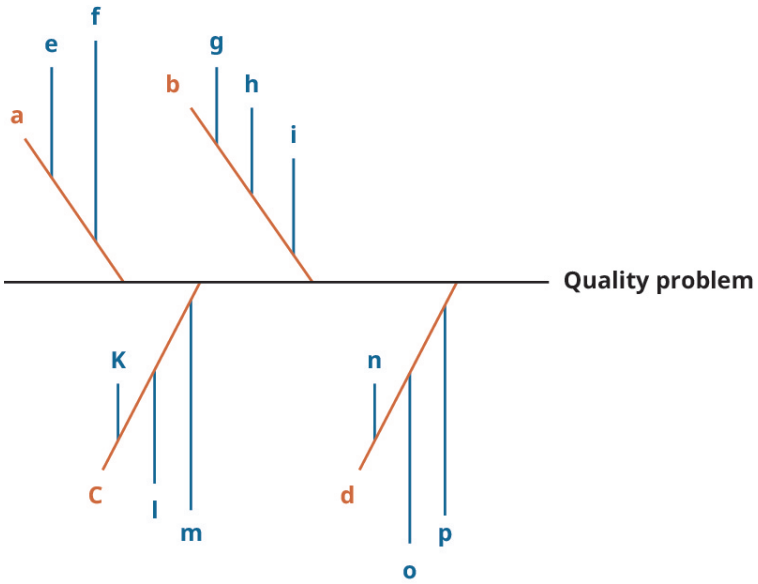

Figure 6.10 A quality problem has main causes—here designated as a, b, c, and d. Within these main causes, there are several causes that might need to be addressed to solve the quality problem. The goal of a fishbone diagram is to find the root causes of the quality problem. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

In the case of our water pollution example, a fishbone diagram exploring the issue might reveal the items shown in Figure 6.11.

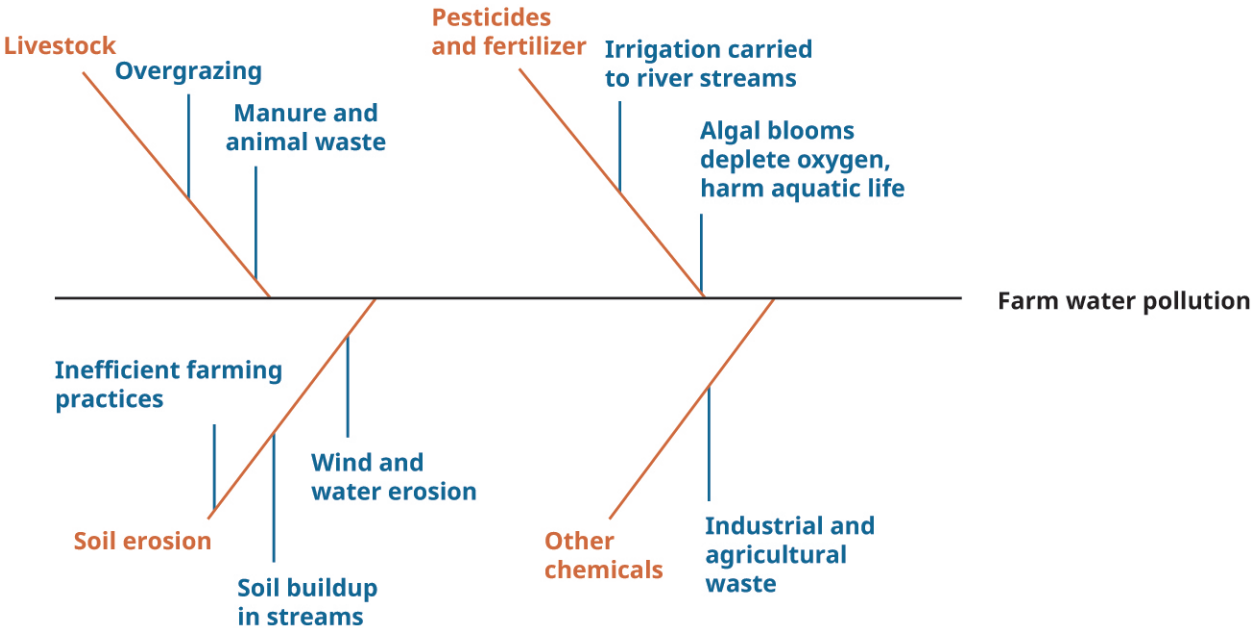

Figure 6.11 Farm water pollution could have four main causes, such as livestock, pesticide and fertilizer, soil erosion, and other chemicals. For each of those, there are other related causes. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Step 2: Ideate

To **ideate** is the step of the creative problem-solving process that involves generating and detailing ideas by the entrepreneur. After collecting all information relevant to the problem, the entrepreneur lists as many causes of the problem as possible. This is the step in which the largest variety of ideas are put forth. Each idea must be evaluated for feasibility and cost as a solution to the problem. If a farm does not have clean water, for example, the entrepreneur must list causes of toxic water and eliminate as many of those causes as possible. The entrepreneur must then move forward investigating solutions to bring the water back to a safe state. If, say, nearby livestock are polluting the water, the livestock should be isolated from the water source.

Step 3: Develop

To **develop** is the step in which the entrepreneur takes the list of ideas generated and tests each solution for feasibility. The entrepreneur must consider the cost of each idea and the obstacles to implementation. In the preceding example, adding a chemical to the water may not be a feasible solution to the farmer. Not every farmer wants additional chloride or fluoride added to the water due to the effect on both humans and livestock. These tradeoffs should be addressed in the feasibility assessment. The farmer might prefer a filtration system, but the cost of that solution might not be practicable. The entrepreneur should identify and assess alternative solutions to find one that is most cost-effective and feasible to the customer.

Step 4: Implement

To **implement** is the step in which the solution to the problem is tested and evaluated. The entrepreneur walks through the planned implementation with the client and tests each part of the solution, if a service, or thoroughly tests a developed good. The entrepreneur implements the solution and goes through a structured system of follow-up to ensure the solution remains effective and viable. In the water example, the solution would be reducing runoff from toxic insecticides by adding prairie strips, buffers of grass, and vegetation along banks of streams.

Step 5: Evaluate

To **evaluate** is the step in which the final solution is assessed. This is a very important step that entrepreneurs often overlook. Any fallacy in the implementation of the product or service is reassessed, and new solutions

are implemented. A continual testing process may be needed to find the final solution. The prairie strips, buffers of grass, and vegetation along banks of streams chosen in the farming water example should then be analyzed and tested to ensure the chosen solution changed the content of the water.

ARE YOU READY?

Implementing Creative Problem Solving

Removing waste is a problem, and it can also present an entrepreneurial opportunity. Try to examine ways in which waste products that you usually pay to have hauled away can now generate revenue. Whether it's recycling aluminum cans or cardboard, or garbage that could be used to feed animals, your task is to come up with solutions to this entrepreneurial-oriented problem.

- Try following the first step of the creative problem-solving process and clearly identify the problem.
- Next, gather data and formulate the challenge.
- Then, explore ideas and come up with solutions.
- Develop a plan of action.
- Finally, note how you would evaluate the effectiveness of your solution.

Using Creativity to Solve Problems

Entrepreneurs are faced with solving many problems as they develop their ideas for filling gaps, whether those opportunities involve establishing a new company or starting a new enterprise within an existing company. Some of these problems include staffing, hiring and managing employees, handling legal compliance, funding, marketing, and paying taxes. Beyond the mundane activities listed, the entrepreneur, or the team that the entrepreneur puts in place, is indispensable in maintaining the ongoing creativity behind the product line or service offered. Innovation and creativity in the business are necessary to expand the product line or develop a groundbreaking service.

It is not necessary for the entrepreneur to feel isolated when it comes to finding creative solutions to a problem. There are societies, tools, and new methods available to spur the creativity of the entrepreneur that will further support the success and expansion of a new enterprise.[14] Learning and using entrepreneurial methods to solve problems alleviates the stress many startup owners feel. The entrepreneur's creativity will increase using collaborative methodologies. Some entrepreneurial collaborative methodologies include crowdsourcing, brainstorming, storyboarding, conducting quick online surveys to test ideas and concepts, and team creativity activities.

Crowdsourcing

Professor Daren Brabham at the University of Southern California has written books on crowdsourcing and touts its potential in for-profit and not-for-profit business sectors. He defines it simply as "an online, distributed problem-solving and production model."[15] **Crowdsourcing** involves teams of amateurs and nonexperts working together to form a solution to a problem.[16] The idea, as cbsnews.com's Jennifer Alsever has put it, is to "tap into the collective intelligence of the public at large to complete business-related tasks that a company would normally either perform itself or outsource to a third-party provider. Yet free labor is only a narrow part of crowdsourcing's appeal. More importantly, it enables managers to expand the size of their talent pool while also gaining deeper insight into what customers really want. The challenge is to take a cautionary approach to the 'wisdom of the crowd,' which can lead to a 'herd' mentality."[17]

14 "Creating a World of Opportunities." *The Collegiate Entrepreneurs' Organization.* n.d. https://www.c-e-o.org/
15 Daren C. Brabham. "Crowdsourcing as a Model for Problem Solving: An Introduction and Cases." *Convergence: The International Journal of Research into New Media Technologies* 14, no. 1 (2008): 75–90.
16 Michael Houlihan and Bonnie Harvey. "How Crowdsourcing Is Shaping the Future of Everything." *Entrepreneur.* January 13, 2018. https://www.entrepreneur.com/article/307438

LINK TO LEARNING

Read this article that discusses what crowdsourcing is, how to use it, and its benefits (https://openstax.org/l/52CrowdSource) for more information.

This new business prototype, similar to outsourcing, features an enterprise posting a problem online and asking for volunteers to consider the problem and propose solutions. Volunteers earn a reward, such as prize money, promotional materials like a T-shirt, royalties on creative outlets like photos or designs, and in some cases, compensation for their labor. Before proposing the solution, volunteers learn that the solutions become the intellectual property of the startup posting the problem. The solution is then mass produced for profit by the startup that posted the problem.[18] The process evolves into the crowdsourcing process after the enterprise mass produces and profits from the labor of the volunteers and the team. Entrepreneurs should consider that untapped masses have solutions for many issues for which agendas do not yet exist. Crowdsourcing can exploit those agendas and add to the tools used to stimulate personal creativity. This type of innovation is planned and strategically implemented for profit.

For example, Bombardier held a crowdsourced innovation contest to solicit input on the future of train interiors, including seat design and coach class interior. A corporate jury judged the submissions, with the top ten receiving computers or cash prizes. Companies are often constrained, however, by internal rules limiting open source or external idea sourcing, as they could be accused of "stealing" an idea. While crowdsourcing outside of software can be problematic, some products such as MakerBot's 3D printers, 3DR's drones, and Jibo's Social Robot have used developer kits and "makers" to help build a community and stimulate innovation from the outside.

WORK IT OUT

A Crowdsourced Potato Chip

In an effort to increase sales among millennials, PepsiCo turned to crowdsourcing to get new flavor ideas for their Lay's potato chips (called Walker's in the UK). Their 2012 campaign, "Do Us a Flavor," was so successful that they received over 14 million submissions. The winner was Cheesy Garlic Bread, which increased their potato chip sales by 8 percent during the first three months after the launch.

- What are some other products that would work well for a crowdsourced campaign contest?
- What items wouldn't work well?

Amazon's Mechanical Turk is an online crowdsourcing platform that allows individuals to post tasks for workers to complete. In many instances, these tasks are compensated, but the payment can be less than one dollar per item completed. Mechanical Turk is one of the largest and most well-known crowdsourcing platforms, but there are a number of other more niche ones as well that would apply to smaller markets. In the case of innovation contests and outsourced tasks from corporations, those tasks may be hosted internally by the corporation.

Brainstorming

Brainstorming is the generation of ideas in an environment free of judgment or dissension with the goal of creating solutions. See Creativity, Innovation, and Invention to refresh yourself on this technique. Brainstorming is meant to stimulate participants into thinking about problem solving in a new way. Using a

17 Jennifer Alsever. "What Is Crowdsourcing?" *CBS News.* May 1, 2008. https://www.cbsnews.com/news/what-is-crowdsourcing
18 Daren C. Brabham. "Crowdsourcing as a Model for Problem Solving: An Introduction and Cases." *Convergence: The International Journal of Research into New Media Technologies* 14, no. 1 (2008): 75–90.

multifunctional group, meaning participants come from different departments and with different skill sets, gives entrepreneurs and support teams a genuine chance to suggest and actualize ideas. The group works together to refine and prototype potential solutions to a problem.

LINK TO LEARNING

Brainstorming is a highly researched and often practiced technique for the development of innovative solutions. One of the more successful proponents of brainstorming is the United Nations Children's Fund (UNICEF). UNICEF faces unique problems of solving resource problems for mothers and children in underdeveloped nations. See how UNICEF practices brainstorming to solve problems (https://openstax.org/l/52UNICEFbrain) including child survival, gender inclusion, refugee crises, education, and others.

The setting for a brainstorming session should remain as informal and relaxed as possible. The group needs to avoid standard solutions. All ideas are welcome and listed and considered with no censorship and with no regard to administrative restrictions. All team members have an equal voice. The focus of brainstorming is on quantity of ideas rather than on the ideal solution provided in every suggestion. A classic entrepreneurial brainstorming activity, as popularized by business software developer Strategyzer, is known as the "silly cow" exercise. Teams come up with ideas for new business models pertaining to a cow, with the results often outrageous, ranging from sponsored cows to stroking cows for therapeutic release. Participants are asked to identify some aspect of a cow and develop three business models around that concept in a short time period, typically two minutes or fewer. The activity is designed to get creative juices flowing.

LINK TO LEARNING

Watch this video from ABC's Nightline that shows how IDEO designed a new shopping cart (https://openstax.org/l/52IDEOshopcart) for an example of a design process that involves brainstorming.

Storyboarding

Storyboarding is the process of presenting an idea in a step-by-step graphic format, as Figure 6.12 shows. This tool is useful when the entrepreneur is attempting to visualize a solution to a problem. The steps to the solution of a problem are sketched and hung in graphic format. Once the original graphic is placed, images of steps working toward a solution are added, subtracted, and rearranged on a continual basis, until the ultimate solution emerges in the ultimate graphic format. For many years, entrepreneurs have used this process to create a pre-visual for various media sequences.

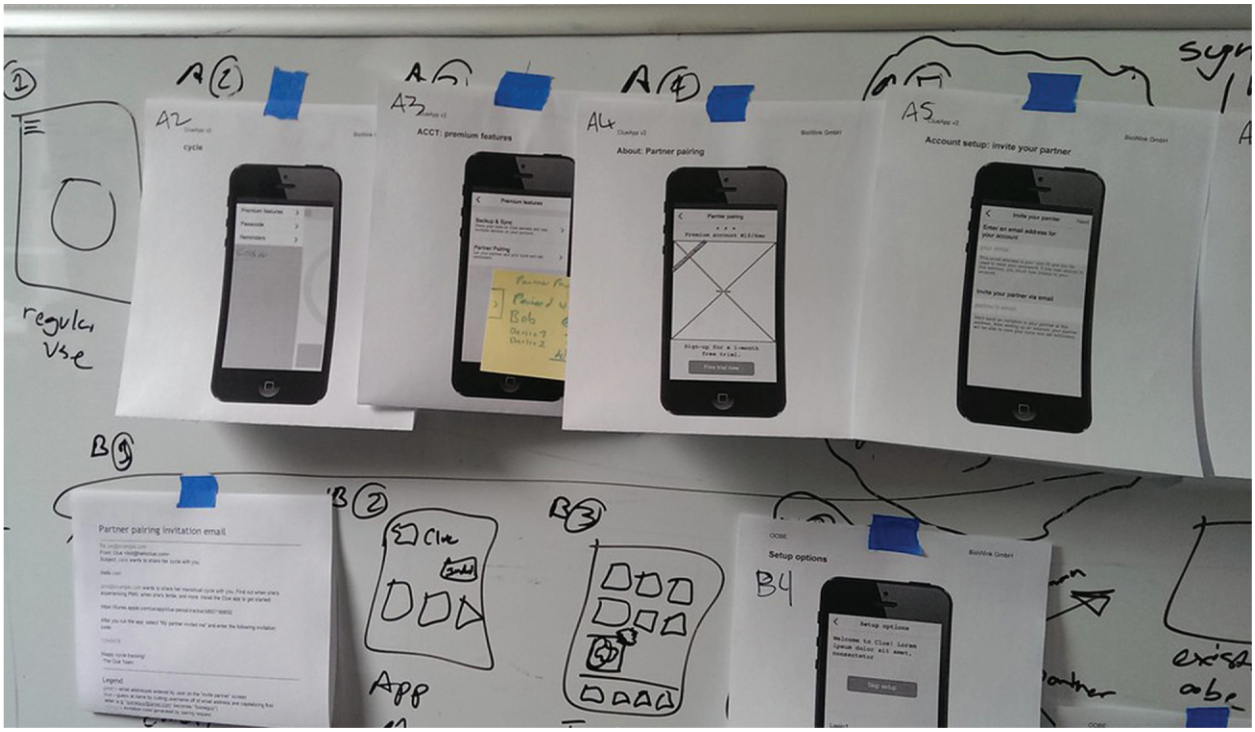

Figure 6.12 Storyboarding helps entrepreneurs and team members to visually represent steps in product creation and problem solving. (credit: "Clue storyboarding" by Adam Wiggins/Flickr, CC BY 2.0)

Team Creativity

Team creativity is the process whereby an entrepreneur works with a team to create an unexpected solution for an issue or challenge. Teams progress through the same creative problem-solving process described already: clarify, ideate, develop, implement, and evaluate. The main advantage of team creativity is the collaboration and support members receive from one another. Great teams trust in other team members, have diverse members with diverse points of view, are cohesive, and have chemistry.

Team members should work in a stress-free and relaxing environment. Reinforcement and expansion of ideas in the team environment motivates the team to continually expand horizons toward problem solution. A small idea in a team may spark the imagination of a team member to an original idea. Mark Zuckerberg, cofounder of Facebook, once said, "The most important thing for you as an entrepreneur trying to build something is, you need to build a really good team. And that's what I spend all my time on."[19]

ENTREPRENEUR IN ACTION

Taaluma Totes[20]

Young entrepreneurs Jack DuFour and Alley Heffern began to notice the beautiful fabrics that came from the different countries they visited. The entrepreneurs thought about what could be done with the fabrics to create employment opportunities both in the country from which the fabric originated and in their home base of Virginia. They decided to test producing totes from the fabrics they found and formed Taaluma Totes (Figure 6.13). DuFour and Heffern also wanted to promote the production of these fabrics and help underserved populations in countries where the fabric originated maintain a living or follow a dream.

19 "Three Tips for Entrepreneurs Creating the Perfect Team." *Virgin.* n.d. https://www.virgin.com/entrepreneur/three-tips-entrepreneurs-creating-perfect-team
20 "Backpacks That Carry a Country." *Taaluma Totes.* n.d. https://www.carryacountry.com/pages/about

Figure 6.13 This photograph was taken by a traveler, Kelsey Friedman, who studied abroad in Rwanda through Virginia Tech's International Business in Lugano: Combining Theory and Practice program. (credit: photo provided by Taaluma Totes)

The team continued to test the process and gathered original fabrics, which they sent to Virginia to create totes. They trained individuals with disabilities in Virginia to manufacture the totes, thus serving populations in the United States. The entrepreneurs then decided to take 20 percent of their profits and make microloans to farmers and small business owners in the countries where the fabric originated to create jobs there. Microloans are small loans, below $50,000, which certain lenders offer to enterprising startups. These startups, for various reasons (they are in poor nations, at poverty level), can't afford a traditional loan from a major bank. The lenders offer business support to the borrower, which in turn helps the borrower repay the microloan. The microloans from Taaluma are repaid when the borrower is able. Repayments are used to buy more fabric, completing Taaluma's desire to serve dual populations. If the process proved unsuccessful, the co-owners would revise the process to meet the plan's requirements.

DuFour and Heffern now have fabrics from dozens of countries from Thailand to Ecuador. The totes are specialized with features to meet individual needs. The product line is innovated regularly and Taaluma Totes serves a dual purpose of employing persons with disabilities in Virginia and creating employment for underserved populations in other countries.

6.3 Design Thinking

Portions of the material in this section are based on original work by Geoffrey Graybeal and produced with support from the Rebus Community. The original is freely available under the terms of the CC BY 4.0 license at https://press.rebus.community/media-innovation-and-entrepreneurship/.

Learning Objectives

By the end of this section, you will be able to:

- Explain the design thinking process
- Discuss some design thinking tools

David Kelley, founder of Stanford University's Design School and cofounder of design company IDEO, is credited as the originator of design thinking, at least within business and entrepreneurial contexts. You were briefly introduced to design thinking in Creativity, Innovation, and Invention, but we will delve into it in more depth here. IDEO grew from a merger of the creator of Apple's first mouse and the first laptop computer designer, David Kelley Design and ID Two, respectively. Almost a decade after the 1982 Apple creations, the 1991-merged company primarily focused on the traditional design of products, ranging from toothbrushes to chairs. Yet another decade later, the company found itself designing consumer experiences more so than consumer products. Kelley began using the word "thinking" to describe the design process involved in creating customer experiences rather than creating physical products. The term *design thinking* was born.

The current IDEO CEO Tim Brown defines design thinking as "a human-centered and collaborative approach to problem-solving, using a designed mindset to solve complex problems."[21] **Design thinking** is a method to focus the design and development decisions of a product on the needs of the customer, typically involving an empathy-driven process to define complex problems and create solutions that address those problems.

A common core of design thinking is its application beyond the design studio, as the methods and tools have been articulated for use by those outside of the field, particularly business managers. Design practice is now being applied beyond product and graphic areas to the design of digital interactions, services, business strategy, and social policy.

LINK TO LEARNING

Watch this 2009 TEDGlobal talk where Tim Brown describes design thinking (https://openstax.org/l/52TEDTimBrown) from a historical perspective to modern times.

Design Thinking Process

Business schools have typically taught a rational, analytic approach to thinking. It focuses on well-defined goals and constraints, and thought precedes action in a sequential process of planning and analysis. The design thinking process approaches problem solving differently. Thinking and doing are often intertwined in an iterative exploration of the design "space," and the process uncovers goals and constraints, rather than identifying them up front.

One design thinking approach that is taught at places like Stanford's Design School and organizations like the LUMA Institute (a global company that teaches people how to be innovative) is **human-centered design (HCD)**. HCD, as the name suggests, focuses on people during design and development. This speaks to the Tim Brown definition of design thinking. Inspiration for ideas comes from exploration of actual people, their needs and problems.

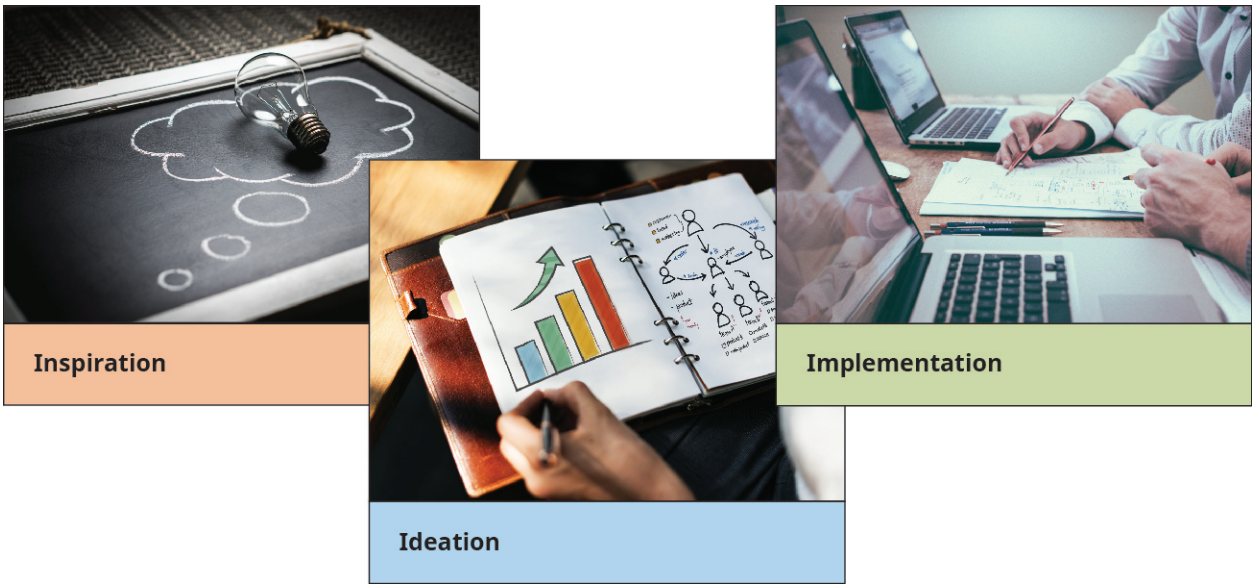

Figure 6.14 The design thinking process focuses on the spaces of inspiration, ideation, and implementation. (credit (left): modification of "thought idea innovation imagination" by "TeroVesalainen"/Pixabay, CC0; credit (center): modification of "document paper business chart" by "rawpixel"/Pixabay, CC0; credit (right): modification of "office business colleagues meeting" by "Free-Photos"/Pixabay, CC0)

Three spaces—inspiration, ideation, and implementation—compose the design thinking process (Figure 6.14).

21 Mark Logan. "Design Thinking for Entrepreneurs." *Medium*. September 29, 2018. https://medium.com/idealect/design-thinking-for-entrepreneurs-392c8cbdcc24

The process uses “spaces” and not “phases” because multiple spaces can happen simultaneously.

Nevertheless, inspiration usually occurs first. This entails identifying a problem or opportunity that motivates someone to search for solutions. Ideation is the process of generating ideas and solutions through various techniques such as brainstorming and sketching sessions. There are hundreds of ideation techniques available. A few examples of ideation exercises include Top Five, How Might We, Mash-up, and Co-Creation Session. In Top Five, everyone on the team writes down their top five ideas, shares them, and clusters similar ideas. In How Might We, the team looks at insight statements and reframes them as “How Might We” questions by adding that phrase at the beginning. The goal is to find opportunities for design that also allows for a variety of solutions. Mash-up involves combining existing brands or concepts to create something new. The team identifies those brands or concepts that represent a quality they desire in their solution, and they “mash up” those ideas to create a new idea. A co-creation session incorporates the desired market into the creation process by recruiting a group of people from the market to work on the design with the team. The goal is to capture the feedback the group provides by treating them as designers, not as interview subjects. Implemented solutions evolve from interactions with users and from the ongoing creation and refinement of possible solutions. Design thinking incorporates experience-based insights, judgments, and intuition from the end users’ perspectives, while in a rational analytic approach, the solution process often becomes formalized into a set of rules.

Nesta is a UK-based innovation foundation that offers many design thinking tools and resources similar to IDEO. Named for the acronym NESTA, the National Endowment for Science, Technology and the Arts, the organization was established in 1998 with an endowment from the UK National Lottery and became an independent charity in 2012. Nesta’s strategy focuses on health, government innovation, education, arts, and creative economy and innovation policy. Nesta offers a set of five criteria to ascertain that an occupation is creative:[22]

1. Novel process
2. Mechanization resistant
3. Nonrepetitive or nonuniform function
4. Makes a creative contribution to the value chain
5. Involves interpretation not merely a transformation in the service or artifact

As the name implies, design thinking originates from design. As design is one of the identified creative industries, there’s a clear connection between creative industries and design thinking. In fact, Nesta offers inspiration and ideation exercises that are freely available for users wishing to implement design thinking practices.

Human-Centered Design Thinking Spaces

The Stanford Design School uses human-centered design thinking (HCD) as its design thinking approach. HCD emphasizes the following spaces of the design thinking process:

- Empathizing: As illustrated by the human-centered approach, it is important to have empathy for the problem you are attempting to solve. Empathy, as the chapter on Creativity, Innovation, and Invention defined, means observing and immersing yourself in the surrounding environment to engage with and understand people’s experiences and motivations.
- Defining: This aspect involves describing the core problem(s) that you and your team have identified. Asking “how might we?” questions helps narrow the focus, as the ultimate aim here is to identify a problem statement that illustrates the problem you want to tackle. “Frame Your Design” is one such challenge in what IDEO calls its “toolkit” that works well here. Frame Your Design asks you to write down your problem and then refine it by following specific steps so that you end up with a design question that

22 Christine Harris, Margaret Collins, and Dennis Cheek. *America’s Creative Economy: A Study of Recent Conceptions, Definitions, and Approaches to Measurement across the USA.* National Creativity Network and Creative Alliance. August 2013. https://www.centerforcreativeeconomy.com/wp-content/uploads/2015/10/AmericasCreativeEconomyFULLReport.pdf

serves as a starting point but leaves room for creativity.[23]

- Ideating: This is where you begin to come up with ideas that address the problem "space" you have defined. There are hundreds of exercises aimed at the ideation process, ranging from brainstorming to "Five whys?" in the IDEO toolkit. The "Five whys" is a questioning method in which the researcher, in looking for information to solve a problem, asks a respondent a broad question, then asks "why" to get deeper into the respondent's thinking. IDEO puts it this way: "You'll use this method while you're conducting an interview and start with really broad questions like "Do you save much money?" or "How was your harvest this year?" Then, by asking why five times you'll get some essential answers to complicated problems. This can be a great method to use if you're trying to get at the human and emotional roots of a problem."[24]
- Prototyping: In this space, the entrepreneur creates and tests inexpensive, scaled-down versions of a product with features or benefits that serve as solutions for previously identified problems. This could be tested internally among employees, a process known as *dogfooding*, or externally with potential customers. This is an experimental phase.
- Testing: Designers apply rigorous tests of the complete product using the best solutions identified in the prototyping space.

WHAT CAN YOU DO?

Every Day a Little Closer

Some examples of everyday items that can be improved through design thinking are sinks on top of toilet cisterns that save water by refilling the cistern with the water you wash your hands with, video doorbells, and smart lightbulbs. Try to think of an improvement to one of your everyday items.

Design Thinking Tools

There are numerous design thinking tools aimed to aid or stimulate your design thinking activities. They stem from organizations dedicated to design thinking like IDEO and Google Ventures. While methodologies incorporate processes and techniques, tools are resources that enable such approaches. These may be activities, or templates that facilitate the approach.

- Innovation Flowchart: A sample innovation flowchart may map out the details of the process. The structured overview serves as an organizational tool in the development process.
- Question Ladder: A tool that helps you ask the "right" questions by refining your questions (Figure 6.15). Asking the "wrong" questions can yield meaningless or less-than-adequate results.

23 IDEO.org. *The Field Guide to Human Centered Design*. 2015. https://bestgraz.org/wp-content/uploads/2015/09/Field-Guide-to-Human-Centered-Design_IDEOorg.pdf
24 "The Five Whys." *Design Kit.* n.d. http://www.designkit.org/methods/66

Simple ← QUESTION COMPLEXITY → Complex						
	IS	DID	CAN	WILL	WOULD	MIGHT
WHO	Who is	Who did	Who can	Who will	Who would	Who might
WHAT	What is	What did	What can	What will	What would	What might
WHERE	Where is	Where did	Where can	Where will	Where would	Where might
WHEN	When is	When did	When can	When will	When would	When might
HOW	How is	How did	How can	How will	How would	How might
WHY	Why is	Why did	Why can	Why will	Why would	Why might

Figure 6.15 A question ladder can help refine questions. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

- Design Thinking Tool Kit: There are various tool kits for select audiences. For example, the "design thinking for educators" toolkit has design thinking resources related to education. A typical tool kit includes a wide assortment of resources with methods and instructions to help you put design thinking into action.
- IDEO Design Kit: IDEO offers an approximately 200-page free PDF, "The Field Guide to Human Centered Design," with activities on mindsets, ideation, inspiration, implementation and a few case studies: http://www.designkit.org/resources/1.
- Google Ventures Design Sprint: A five-day design-thinking exercise that helps resolve questions through design, prototyping, and testing: https://www.gv.com/sprint/.
- Design Thinking Mix Tapes: Stanford's Design School offers three "mixtapes" that serve as guides through a half day of design thinking work in the areas of understanding, experimentation, and ideation: https://dschool.stanford.edu/resources/chart-a-new-course-put-design-thinking-to-work.
- WE THINQ: Software designed to enable collaboration in innovation management: https://www.ideaconnection.com/software/we-thinq-258.html.

ENTREPRENEUR IN ACTION

BitGiving and Design Thinking

At age twenty-two, Ishita Anand created India's first live social crowdfunding platform that enabled artists, engineers, and creators to collaborate and raise funds for special causes by verifying causes and how the funds would be used, while charging a small percentage of the funds raised as a fee. Within five years of its inception, her social enterprise, called BitGiving, has led efforts to address problems through social change. The firm has contributed to various social campaigns related to children, women, education, health, and disaster among others. The firm partnered with charities and other organizations to raise funds for India's National Ice Hockey team to compete in Kuwait at the World Cup and for the victims of the 2015 Nepal earthquake through the crowdfunding platform and other social media platforms such as Twitter.[25]

As India's first social crowdfunding platform, BitGiving literally aimed to solve problems through social change. Describe some design thinking activities that would have been useful to Anand at BitGiving's inception.

As of September 2018, the company closed its website abruptly and reportedly shut down. While the exact reason for its failure is unknown, some reasons the venture could have failed were insufficient capital, regulation, management problems or strategic misalignment, or even poor timing. Failure is common in entrepreneurship, and conferences dedicated to failure are even conducted around the globe (FailCon is

25 "BitGiving." Crunchbase. n.d. https://www.crunchbase.com/organization/bitgiving#section-overview

sort of the TED Talk of failure).

- How could the design thinking process have helped BitGiving from the outset?

6.4 Lean Processes

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Learning Objectives

By the end of this section, you will be able to:

- Discuss the lean process methodology
- Understand the phases of the lean problem-solving process.

You have learned about different problem-solving approaches that entrepreneurs take to lead their startups and work with others. Most of these approaches have had to do with the entrepreneur's cognitive or creative mindsets. Now we will learn about an approach that is more rooted in process, called *lean process*. Lean problem solving has been used as an entrepreneurial methodology in new and emerging ventures, and it's interesting that it comes from a large corporate, manufacturing background that focuses on efficiencies. The Six Sigma methodology, pioneered at Motorola in the 1970s and 1980s, and adopted by many companies, is a disciplined, data-driven approach that provides companies tools to improve the capability of their business processes. According to the American Society for Quality, "Six Sigma views all work as processes that can be defined, measured, analyzed, improved and controlled. A set of qualitative and quantitative tools is used to drive process improvement. This increase in performance and decrease in process variation helps lead to defect reduction and improvement in profits, employee morale, and quality of products or services."[26] GE copied it and created the "Process Excellence" programs that millions of managers and others have taken to get certified at various "belts." Although Six Sigma and Process Excellence do not fit strictly in terms of entrepreneurship, as they are used mainly by large, mature companies, many of the methods fit in the lean model.

Toyota pioneered the lean process in the 1980s. The term "lean manufacturing" is the most common, but it is much more than manufacturing. The **lean process** is a systematic method for the maximizing of continuous improvement and the minimization of surplus or unused material in the production of a process. The entrepreneur begins the startup with a sense the original product will be the product carrying the organization to success in the long term. In most cases, the good or service will require modification to maintain a process, technology, or up-to-date product offering. Lean problem solving means the entrepreneur's entire team scans both the company's internal and external environments for continuous improvement and methods for bringing additional revenue to the startup by cost improvement processes that promote sustainable value. The **external environment** encompasses customers, industry trends, and competition. The **internal environment** comprises the factors inside the enterprise, such as employees, and internal practices and processes. In lean manufacturing, for example, improving efficiencies in the internal environment should lead to advantages in the external environment (whether that be cost savings to customers, competitive advantage from more output/superior product, etc.).

26 American Society for Quality. "What Is Six Sigma?" n.d. https://asq.org/quality-resources/six-sigma

For example, every mile saved per day per UPS truck driver results in approximately $50 million in savings per year, according to Juan Perez, the company's chief information and engineering officer. Using customer data and artificial intelligence, the company created a system dubbed ORION, which is an acronym for On-Road Integrated Optimization and Navigation.[27] To date, the system has resulted in $400 million in savings to UPS. By applying the lean process, everything that UPS saves on the input (by reducing mileage) leads to savings on the output, which leads faster deliveries, lower costs for consumers, and more profit for UPS.

Lean Problem-Solving Process

The lean problem-solving process is a cycle of observation, assessment, and continual evaluation. As shown in Table 6.1, this cycle typically involves eight specific steps.

Steps in the Toyota Lean Problem-Solving Process

Step	Action
Step 1	Clarify the problem.
Step 2	Analyze the problem (genchi genbutsu is the Toyota practice of thoroughly understanding a condition by confirming information or data through personal observation at the source of the condition; the Japanese phrase essentially means "go and see").[28]
Step 3	Set targets.
Step 4	Identify root causes. Asking, "Why?" repeatedly can narrow down the factors to a root cause.
Step 5	Develop countermeasures by asking, "What is the specific change we want to make?" and involving others in the problem-solving process.
Step 6	Implement the countermeasures and see them through.
Step 7	Monitor results.
Step 8	Standardize processes that succeed. Lean problem solving is about learning more about the problem itself and its deep causes in context.

Table 6.1 The lean problem-solving, step-wise process allows the business to observe, assess, and continually evaluate.

ARE YOU READY?

Too Much Too Late?

Many entrepreneurs create a startup with an idea that they develop without any feedback from potential customers, relying on their own knowledge or assumptions about the market. Consider the story of Rapid SOS: https://hbr.org/2018/05/do-entrepreneurs-need-a-strategy. What would most likely happen when they decided to go forward with their product? Will it be a fit to the customer's needs or solve their problems? How is lean process different from this?

27 Juan Perez. "UPS' Approach to Innovation and Technology." Presentation sponsored by J. Mack Robinson College of Business, Georgia State University, Atlanta, GA. March 28, 2019.
28 "Genchi Genbutsu." *Lean HE Glossary*. n.d. http://www.leanhe.org/lean-he/glossary#TOC-Genchi-Genbutsu

Lean Problem-Solving Phases

Observation is the phase in which the entrepreneur studies the challenge and notes all facets of the challenge requiring solution. In this phase, the entrepreneur asks questions and conducts research about the change needed for a successful product, outcome, or service. The entrepreneurs must determine why the change is needed. What is the purpose of the endeavor? Feedback is extremely important in this phase.

For example, a community asked a group of entrepreneurs to help address the youth obesity problem in a middle school. The entrepreneurs began to study the intake of food by the children and determined that both the content of the school lunch menu and the lifestyle of the majority of the children were affecting the obesity rate in the community. They then defined the purpose of the project as finding a low-cost, low-risk method of changing the lunch menu and agreed that the primary outcome would be a 30 percent reduction in the obesity rate of the children. The entrepreneurs began to assess the cost of changing the lunch menu and observing what else the kids ate. The entrepreneurs discovered that the lunch menu change required to reduce the obesity rate was beyond the financial capability of the school district. Research also showed that many of the children, products of single-parent homes, were eating high-calorie, high-fat, take-out foods for dinner. Further observation revealed that the children did not engage in physical activity after hours because the local surroundings were not safe. The community needed a process to transform the wellness of the children, and the entrepreneurs recommended using a lean process approach to help the children as quickly as possible.

After the observation of the problem comes **assessment**, the phase in which the entrepreneur experiments and analyzes the potential process and its capabilities. The entrepreneur leverages creative tools and resources to arrive at a solution and assesses each step of a possible solution. Each step must add value to the solution, or that step in the solution is unnecessary. In addition, the step must be capable of solving the issue and add flexibility to the solution. How is the process or product being improved? In this phase, a prototype of the product is developed and delivered. The entrepreneur must ask the customer if all needs and wants are satisfied with the prototype. If the prototype is being developed for mass production, surveying customers about potential sales is essential. In the school lunch example, the school system would have been the customer of the new food menu (prototype) in the assessment phase.

Evaluation is the phase in which behaviors are analyzed to assess success. The entrepreneur continually studies each phase of the solution to observe the effectiveness of outcomes desired by the client. The entrepreneur ensures that transformation is built into the habits of the school to obtain, maintain, and develop the desired outcomes.

In a real-world example of a company applying lean processes, the New Balance Company, which designs and manufactures both athletic and casual shoes, used a batching approach in the early 2000s that organized production by departments, so that all of the cutting took place in one department, all of the stitching took place in another, and so forth. While it seems that batching tasks would improve efficiency, at New Balance, it meant that production of one pair of shoes took nine days. Executives observed piles of inventory sitting between floors and departments, and noticed employees waiting while there were delays in the production line. They also noticed that the pay structure contributed to the piles of works in process because employees were paid by the piece, which encouraged them to produce as much as possible.

The company applied lean principles to rearrange the production floor by value streams, or the making of a product by sharing similar processing steps. On one side was “cut and stitch” products using US materials of leather and mesh, while another side used premade products from overseas for soles, inserts, and kits. This change cut the time to make a pair of shoes down to four hours, meaning that domestic plants could ship some orders in twenty-four hours, while competitors may need as much as 121 days to ship when they outsourced manufacturing to Asia.

An often-used lean problem-solving tool is whiteboarding (Figure 6.16). **Whiteboarding** is a type of graphing

that permits the entrepreneur to plot each step in a process to build comprehension and detailing of the process. The entrepreneur draws each step on the whiteboard using a linking-type diagram, and draws arrows to show how processes affect other processes. Seeing the flow of the process allows the entrepreneur to note where functions in the process are duplicated or inconsistent.

Figure 6.16 Whiteboarding is a technique that can help entrepreneurs visualize and analyze processes. (credit: "whiteboard man presentation write" by "StartupStockPhotos"/Pixabay, CC0)

For example, in a community garden, storing tools, such as hoes and hand trowels for weeding, in different sheds wastes time when preparing to begin the process of weeding. These tools should be stored collectively to eliminate multiple trips and wasted time. Seeing the process on a whiteboard or other medium brings awareness to how processes can be improved. After the process is changed, it is graphed again for further scrutiny.

ENTREPRENEUR IN ACTION

The Origin of Lean

Would it surprise you to know the origin of lean, in modern times, is considered to be Henry Ford's production line? Although we don't necessarily think of the creation of automobiles as an entrepreneurial venture in today's world, Henry Ford was truly an entrepreneur for his time when the manufacture of automobiles was just beginning. Not only did he recognize the opportunity inherent in the sale of automobiles, he recognized the need to create an efficient process for automobile production that could decrease costs and, consequently, the selling price of the vehicle. As the first entrepreneur to join the use of interchangeable parts with moving conveyance to develop fabrication processes, Ford was able to turn over inventory in a very short time; however, Ford's process could not deliver variety. In fact, Ford was quoted as saying of the Model T's color, "You can have any color as long as it's black."[29] It had the fastest drying time; hence, it was the only color he used for a number of years.

The Ford system was built around one static product. In the 1930s, when the market demanded product variety, the company was not set up to address this challenge. Kiichiro Toyoda (Figure 6.17), the second president of Toyota Motor Corporation, visited the Ford plant in Michigan to learn more about their application of the assembly line concept. After observing, he proposed a new production system that would strive to "right size" equipment to better match tasks and the volume of work, as well as introducing quality assurance steps in each sequence of the work process. Toyoda's approach shifted the focus from machinery

29 Diana T. Kurylko. "Model T Had Many Shades; Black Dried Fastest." *Automotive News.* June 16, 2003. http://www.autonews.com/article/20030616/SUB/306160713/model-t-had-many-shades%3B-black-dried-fastest

to process, optimizing efficiency while maintaining quality.

Figure 6.17 Kiichiro Toyoda introduced new ways to improve processes. (credit: “Kiichiro Toyoda” by “Scanyaro”/Wikimedia Commons, Public Domain)

Key Terms

adaptive model method of entrepreneurial problem solving that seeks solutions in ways that are tested and known to be effective

assessment lean problem-solving process phase in which the entrepreneur experiments and analyzes the potential process and its capabilities

brainstorming generation of ideas in an environment free of judgment or dissension with the goal of creating solutions

clarify first step of the creative process, which involves recognizing the existence of a gap between the current state and a desired state

communication skills skills entrepreneurs use to pool resources for the purposes of investigating solutions leading to innovative problem solving and competitive advantage

creativity development of original ideas

critical thinking complex analysis of a problem or issue with the goal of solving the problem or making a decision

crowdsourcing teams of amateurs and non-experts working together to form a solution to a problem

data analysis process of analyzing data and modeling the data into a structure that leads to innovative conclusions

decisiveness ability to make a quick, effective decision, not letting too much time go by in the process

design thinking method to focus the design and development decisions of a product on the needs of the customer, typically involving an empathy-driven process to define complex problems and create solutions that address those problems

develop stage in which the entrepreneur takes the list of ideas generated and tests each solution for feasibility

entrepreneurial problem solving process of using innovation and creative solutions to close the opportunity gap by resolving complex societal, business, or technological problems

evaluate stage in which the final solution is assessed

evaluation lean problem-solving process phase in which behaviors are analyzed to assess success

external environment outside the enterprise and encompasses customers, industry trends, and competition

hackathon event, usually hosted by a tech company or organization, which brings together programmers and workers with other degrees of specialization within the company, community, or organization to collaborate on a project over a short period of time

human-centered design focuses on people during design and development

ideate stage of the creative problem-solving process leading to the detailing and formation of idea generation by the entrepreneur

implement means to enact the plan and test for success

innovative model method of entrepreneurial problem solving that uses techniques unknown to the market and that bring competitive advantage to an organization

internal environment comprises the factors inside the enterprise, such as employees, and internal practices and processes

lean process systematic process for the maximizing of continuous improvement and the minimization of surplus or unused material in the production of a process

need awareness occurs when the entrepreneur notes a gap between societal or customer needs and actual circumstances

observation lean problem-solving process phase in which the entrepreneur studies the challenge and notes all facets of the challenge requiring solution

petitioner problem solvers problem solvers who see a problem and ask others for solution ideas

resourcefulness ability to discover clever solutions to obstacles

self-regulating problem solvers problem solvers who are autonomous and work on their own, without

external influence; they have the ability to see a problem, immediately visualize a possible solution to the problem, and seek to devise a solution

storyboarding process of presenting an idea in a step-by-step graphic format

team creativity process of a team creating an unexpected solution for an issue or challenge

theorist problem solvers problem solvers who see a problem and begin to consider a path toward solving the problem using a theory

whiteboarding type of graphing that permits the entrepreneur to plot each step in a process to build comprehension and detailing of the process

Summary

6.1 Problem Solving to Find Entrepreneurial Solutions

Problem solving involves more than making decisions. Problem solving is a necessary component of entrepreneurial genesis, used to manage your business and helpful in addressing everyday personal situations. Entrepreneurs must know their personal strengths and capitalize on applicable problem-solving methods to create innovative products. Moving a startup ahead of the competition requires the entrepreneur to use all problem-solving sources and skills in the entrepreneur's tool box. Problem-solving models can be adaptive or innovative, the latter being more common among entrepreneurs. Problem-solving skills include critical thinking, communication, decisiveness, resourcefulness, business and industry awareness, and an ability to analyze data. There are various types of problem solvers, including self-regulating, theorist, and petitioner problem solvers.

6.2 Creative Problem-Solving Process

The creative problem-solving process is a logical process. The steps to the creative problem-solving process are clarify, ideate, develop, implement, and evaluate. Each step is an aid to creating a solution. The steps are repeated cyclically until the entrepreneur develops an innovative solution. When entrepreneurs experience creativity block, tools to alleviate the block are available. These tools include crowdsourcing, brainstorming, and storyboarding. Each of these tools assist the entrepreneur in innovative thinking.

6.3 Design Thinking

Design thinking in business and entrepreneurship was made prevalent by David Kelley, founder of Stanford University's Design School and cofounder of design company IDEO. Design thinking, which espouses an HCD approach, can be applied beyond product and graphic design to include the design of social policy, business strategy, services, and digital interactions. The five stages as espoused in Stanford's design thinking model are empathizing, defining, ideating, prototyping, and testing. There are numerous design thinking tools that help develop and carry out these processes from various organizations and companies, ranging from IDEO to Google.

6.4 Lean Processes

Lean process is a systematic process for maximizing continuous improvement through minimizing surplus or unused material in the production of a current process. With origins in manufacturing, the lean process can be applied to internal organizational processes as well as external product development. Lean process uses observation, assessment and evaluation, and whiteboarding techniques to solve problems.

Review Questions

1. What is the relationship between entrepreneurial thinking and problem solving?
2. What are the key aspects of the two types of problem-solving methods the entrepreneur uses to problem solve?
3. What are the key skills entrepreneurs need to arrive at innovative solutions?

4. What are the differences in the three major types of entrepreneurs?
5. List and describe the steps an entrepreneur uses in the specific and logical process of creativity?
6. What are the key aspects of the brainstorming process?
7. What is the main advantage of using teams to create a solution?
8. Discuss the advantages of storyboarding.
9. What are the differences between the design thinking process and the problem-solving process and why are they important?
10. What are the steps in human-centered design thinking? Briefly describe each.
11. What is human-centered design?
12. Observation is the phase in which entrepreneurs explore problems that requires solution. Which is not a step in this phase?
    A. talk to clients and conduct research for potential solution
    B. determine if change is needed
    C. experiment and analyze potential solution
    D. None of these options is correct.
13. What are some advantages of the lean process?

Discussion Questions

1. Which method do you think applies more to entrepreneurship, the innovative or adaptive problem-solving method? Do you see yourself as using one method more than the other in your entrepreneurial endeavors? If so, which one and why?
2. Do you think it is important for the entrepreneur to understand and develop all the problem-solving skills to manage a successful startup? Why or why not?
3. Which of the three types of entrepreneurs relies more on the innate skill of the entrepreneur?
4. How does the fishbone process aid entrepreneurs in finding the root cause to problems worth solving?
5. Discuss the different methodologies an entrepreneur might use when experiencing creativity block.
6. Discuss the crowdsourcing process, including how contributors to the solution are rewarded and how different platforms fit with different types of businesses.
7. Why is empathy needed in defining problems?
8. Why is it important to continuously ask for feedback and improve the current design?
9. What are some ways you can determine the true root cause of a problem and not just its symptoms?
10. What are the best ways to implement lean thinking in your company?

Case Questions

1. The team at AMD, the manufacturer of a chip processor, has a good grasp on how software giants build products around its processors. The teams at AMD design processors to feature attractive capabilities to the software giants by seeking input from researchers and designers on the AMD team who possess knowledge of current and upcoming trends. New processors will incorporate these trends in design. After identifying what type of problem-solving style this would be an example of, incorporate the key skills entrepreneurs must have according to the chapter and apply them in terms of the AMD team.

2. Tamika, a young entrepreneur, has been purpose-driven toward social change in their rural community. They have created solutions for pesticide runoff, erosion problems, and toxic well water. Tamika has decided to focus more on energy conservation and local air quality. Their first client is interested in wind as a power source. Tamika is unfamiliar with wind power and needs to learn about innovative solutions for residential application. How might Tamika use creative problem solving methods to develop solutions for the client's request?
3. Based on input from his second-grade students, New York teacher Michael Schurr was able to redesign his classroom to better serve the students' needs. In the book *Design Thinking for Educators*, he redesigned the cubby space to make the room semi-private and lowered the boards so that students could see the content. He made all of these changes after asking the students for input. What are some ways you could improve your classroom if your instructor asked your opinion, using design thinking tools?

Suggested Resources

6.1 Problem Solving to Find Entrepreneurial Solutions

Tony Robbins' tips on decisiveness: https://www.tonyrobbins.com/stories/unleash-the-power/be-decisive/

6.2 Creative Problem-Solving Process

https://www.nngroup.com/articles/storyboards-visualize-ideas/

https://www.studiobinder.com/blog/downloads/storyboard-template/

https://www.mturk.com/

https://www.mindtools.com

6.3 Design Thinking

Google Ventures Design sprint: https://www.gv.com/sprint/

IDEO Design Kit: http://www.designkit.org

Stanford Design Thinking Mix Tapes: https://dschool.stanford.edu/resources/chart-a-new-course-put-design-thinking-to-work

Stanford Design Thinking Process Diagram: https://dschool.stanford.edu/executive-education/dbootcamp

6.4 Lean Processes

Lean Enterprise Institute: https://www.lean.org/WhatsLean/

7

Telling Your Entrepreneurial Story and Pitching the Idea

Figure 7.1 A pair of entrepreneurs pitches their venture at the "Risk City" Global Entrepreneur Week in Memphis, Tennessee. (credit: modification of "Risk City. Global Entrepreneur Week." by Brad Montgomery/Flickr, CC BY 2.0)

Chapter Outline

7.1 Clarifying Your Vision, Mission, and Goals
7.2 Sharing Your Entrepreneurial Story
7.3 Developing Pitches for Various Audiences and Goals
7.4 Protecting Your Idea and Polishing the Pitch through Feedback
7.5 Reality Check: Contests and Competitions

Introduction

Sara Minkara, a Muslim American of Lebanese decent, lost her eyesight at age seven because of a genetic disorder. She grew up experiencing ethnic discrimination and mistreatment because of her disability. As a college student in the United States, Minkara realized that she had access to privileges that other children in her native Lebanon did not. Her desire to make things better for youth like her developed into a passion for empowering blind children to get engaged in their communities. The problem: Many societies marginalize visually impaired people and may even see them as a burden. This bias can be attributed in part to physical and cultural constraints and habits that create de facto limitations on their ability to function freely and effectively in those societies. The solution: educational programs and public awareness campaigns that empower visually impaired persons from a young age and provide them with assertiveness training.

At 27, Minkara founded Empowerment Through Integration (ETI), a social enterprise that empowers youth with visual impairments in the Middle East-North African region and in the United States. The organization has grown from a summer camp to a small movement that assists more than 3,000 individuals across Lebanon and the United States. The mission and vision of ETI are to develop an inclusive society that transforms the global social stigma against disabilities and empower blind youth.[1] One of Minkara's signature events is "Dining in the Dark," which is designed to expose participants to the life of a blind person and educate them about the potential in all people, particularly those with disabilities, including the visually impaired.

1 "About Eti." *Empowerment through Integration.* n.d. https://www.etivision.org/about-eti

7.1 Clarifying Your Vision, Mission, and Goals

Portions of the material in this section are based on original work by Mark Poepsel and produced with support from the Rebus Community. The original is freely available under the terms of the CC BY 4.0 license at https://press.rebus.community/media-innovation-and-entrepreneurship/.

Learning Objectives

By the end of this section, you will be able to:

- Clarify the vision statement, mission statement, and goals for your enterprise
- Define and develop a problem-solution narrative that is compelling
- Define and develop a value proposition that is credible and appealing to customers and investors

Entrepreneurs can sometimes be compared to superheroes: They solve problems. They wield great power and responsibility. They're willing to take on risks the way superheroes are willing to take on villains. They are undaunted in the face of failure. They seek solutions and continuous improvement of their products with their customers in mind so that their solutions go beyond addressing their individual needs. When an entrepreneur succeeds, others say "If only I'd thought of that!"

But thinking isn't enough. And even *doing* isn't enough. Successful entrepreneurs also understand the need to *communicate* the origin and value of their venture. They not only solve problems, they tell stories of crises averted, foes bested, and painful defeats from which they learned how to start anew. After all, what's a hero without an origin story and a list of tales, battles lost, and markets won?

In superhero narratives, these origin stories are sacred lore. For an entrepreneur, a problem-solution narrative is like the origin story for their offering. The **problem-solution narrative** concisely introduces a specific problem that affects many people and presents the good or service as an innovative, unique, and insightful solution. Here are some classic problem-solution narratives in advertising and in corporate origin stories to think about as you consider how to craft a quick, compelling problem-solution narrative.

- A young basketball player lacks muscle mass. The athlete drinks milk and gets stronger, earning the a place on the school team.
- Young people, pictured in silhouette, walk around a city looking bored with life. Then, they turn on their new MP3 players and start dancing in the streets. Their world is set ablaze in color and sound.
- A hardworking ballerina lands the lead in a school performance, only to have it canceled as a result of the 2020 pandemic. Family and friends order lights and stage a rendition on the street.

These may not be the greatest stories ever told. You're not going to get a National Book Award for a Snickers commercial, but these are memorable narratives about people who have a problem that the product in question can solve.

To stay focused through repeated series of successes and failures, you need more than a problem-solution narrative: You need a vision and, in turn, a mission statement and goals. You learned about these in The Entrepreneurial Perspective, but you should revisit them as you develop your story and refine how to *pitch* that story to potential investors, customers, and employees. A **pitch** is a formal presentation in which you ask for something. It is delivered (usually) to potential investors in a startup. More on pitches later in the chapter.

Sara Minkara's vision statement may be defined as wishing to live in a world where visually impaired people are not discriminated against. Her venture's *mission* is to establish a well-functioning nonprofit organization showing people in the United States, the Middle East, and North Africa the humanity and value in those with severely impaired eyesight. Minkara's *vision*, imagining the organization's long-term future, is to make it a global leader in providing services to visually impaired people. Specific *goals* include hosting events, developing educational programs, organizing awareness campaigns, and, of course, fundraising. Following this example of mission, vision, and goals, let's break down each concept and consider how they work broadly

and apply to your potential venture.

Vision

A vision statement, as you saw in The Entrepreneurial Perspective, outlines the venture's broader purpose, what the entrepreneur sees the venture growing into in the future. Before you can create a focused mission statement and goals answering who you are, what you do, and what you plan to do in the future, you must develop a vision statement that allows you look into the future to answer this question: "What might we become someday if our organization were the best possible version of itself?"

Drafting a vision statement is an exercise in **ideation**—a purposeful process of opening up one's mind to new trains of thought that branch out in many directions from a stated purpose or problem—in this case, with the goal of generating new possibilities for goods, services, or processes to make your venture sucessful. A vision statement is more open-ended than a mission statement. For example, Table 7.1 shows Amazon's vision and mission statements. Notice how they differ.

Amazon's Vision and Mission Statements[2]

Amazon's Vision Statement	Amazon's Mission Statement
To be Earth's most customer-centric company, where customers can find and discover anything they might want to buy online	We strive to offer our customers the lowest possible prices, the best available selection, and the utmost convenience

Table 7.1 Notice the differences in Amazon's vision and mission statements. The vision statement is broader than the mission statement and looks to the future.

To create a strong vision statement, look at the broader field in which your organization operates. Be general. State a dream that is not currently attainable but that defines what your collective outcomes would be in a best-case scenario. Crafting a vision statement enables your organization, as a team, to identify key areas for potential growth *and* key social influences you can have, but it is important to stay focused on changes in your industry or sector as a general rule of thumb and to revisit your vision when those may warrant a change. For example, Netflix started out with the goal of providing optimum value and convenience for customers renting DVDs but as entertainment consumption platforms evolved it needed to adjust, and it has since shifted into streaming content for television. The company's 2019 vision statement is "Becoming the best global entertainment distribution service."[3]

When crafting a vision statement, write questions beginning with, "How might we…?" or statements starting with, "In a perfect world, our organization would…" Craft a vision statement that hinges on the organization's service goals and turns it into a lasting social good. (You should not promise to create world peace or give everybody a puppy, but you should look at how businesses operate in your field and dream of doing better strategically and socially.) These steps provide a good starting point:

1. State how your organization would function in a dream scenario.
2. Connect your organization's dreams to broader hopes for progress.
3. Define how you're going to make the world a better place in the future through your products and services.

Dreams do not have to be wild to be broadly appealing or influential. The purpose of the vision statement is not to set unattainable goals but to open minds in the organization. If the vision statement has no grounding in reality, it can easily be written off; if it focuses on market share and product development (that is, tangible,

2 "Amazon Mission and Vision Statement Analysis." *Mission Statement Academy*. June 19, 2019. https://mission-statement.com/amazon/
3 "Netflix Mission and Vision Statement Analysis." *Mission Statement Academy*. July 12, 2019. https://mission-statement.com/netflix/

mission-oriented things), the point is lost. Imagine your best team doing its best work with future capabilities and affordances made possible by other entrepreneurs and creators like you, and then state clearly what your influence as world changers could be. Again, the goal is not to develop unmanageable expectations or demand constant innovation from employees and contributors who have jobs that sustain day-to-day operations. The purpose is to develop a conversation about what is possible for the enterprise. For smaller startup enterprises (a deli or coffee shop, for example), the vision can be simpler but still focused on a unique experience they want to create for their customers. In other words, it should still be aspirational, with a link to the mission statement. Table 7.2 lists the vision statements of some companies across a variety of industries.

Example Vision Statements

Entity	Vision Statement
Alzheimer's Association	A world without Alzheimer's disease
Teach for America	One day, all children in this nation will have the opportunity to attain an excellent education
Creative Commons	Realizing the full potential of the Internet—universal access to research and education, full participation in culture—to drive a new era of development, growth, and productivity
Warby Parker	To offer designer eyewear at a revolutionary price, while leading the way for socially conscious businesses
IKEA	To create a better everyday life for the many people

Table 7.2 Strong vision statements are forward-thinking.

A vision statement does not have to be long to be strong. One well-known vision statement contains only fifteen words: "At IKEA our vision is to create a better everyday life for the many people."[4] This vision statement focuses on what IKEA hopes to accomplish, and what its employees can aspire to be—people who make everyday life better for others. Note the phrase "the many people." This is purposeful: IKEA makes mass-marketed products and chooses to align its vision with its targeted consumers: many people. This vision statement is *not* framed as a political statement; rather, it is an ideal established for the global brand, and it indicates a broad positive outcome. IKEA's statement is almost pure vision. A vision statement should connect an organization's day-to-day work to a universal ideal rather than trying to draw a roadmap for implementation.

That being said, alongside its vision, the company follows up with what IKEA calls its "business idea." It states: "Our business idea is 'to offer a wide range of well-designed, functional home furnishing products at prices so low that as many people as possible will be able to afford them.'" This is something of a value proposition and a mission statement wrapped up in one. A **value proposition** explains what it is, exactly, that an organization or firm does that people will pay for (or contribute, to in the case of a nonprofit), and it is a central point in any pitch. We learned about value propositions in Identifying Entrepreneurial Opportunity as being integral to identifying opportunities, and you will learn how they figure into your business model in Business Model and Plan. But the discussion in this chapter is about how and why the value proposition needs to be articulated.

4 "Vision and Business Idea." *IKEA*. n.d. https://www.ikea.com/gb/en/this-is-ikea/about-us/vision-and-business-idea-pub9cd02291

An example of a complicated vision statement is Coca-Cola's.[5] While they are a very successful company, in the vision and mission statements published on their website, the distinctions between each can be difficult to discern. Figure 7.2 shows a large collection of statements and comments titled "Mission, Vision, & Values" on Coca-Cola's website that includes sections on workplace culture, market focus, and "working smart." These concepts, taken together, cover most of what is discussed in this section. Coca-Cola is not committing sins of omission with its "Mission, Vision, & Values" page. If anything, it tries to say too much. Also at issue is *how* these ideas are stated. For a company with massive global reach and some of the best, most memorable marketing moments, the relatively lifeless nature of its vision stands out.

Coca-Cola's Mission, Vision, And Values

Our vision serves as the framework for our Roadmap and guides every aspect of our business by describing what we need to accomplish in order to continue achieving sustainable, quality growth.

- **People:** Be a great place to work where people are inspired to be the best they can be.
- **Portfolio:** Bring to the world a portfolio of quality beverage brands that anticipate and satisfy people's desires and needs.
- **Partners:** Nurture a winning network of customers and suppliers, together we create mutual, enduring value.
- **Planet:** Be a responsible citizen that makes a difference by helping build and support sustainable communities.
- **Profit:** Maximize long-term return to shareowners while being mindful of our overall responsibilities.
- **Productivity:** Be a highly effective, lean and fast-moving organization."

Source: "Mission, Vision, and Values." The Coca-Cola Company. (http://www.coca-colacompany.com/our-company/mission-vision-values)

Figure 7.2 This is Coca-Cola's mission, vision, and values. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

This is a classic case of *telling rather than showing*. IKEA and Coca-Cola arguably have a similar vision. They want to make life a little bit better for people in an everyday way. But with this series of statements, Coca-Cola tries to cover all possible types of vision for almost every major relationship or facet of the corporation imaginable. Coca-Cola has a separate mission statement on its website, shown in Figure 7.3.

Coca-Cola's Roadmap

Our Roadmap starts with our mission, which is enduring. It declares our purpose as a company and serves as the standard against which we weigh our actions and decisions.

- To refresh the world
- To inspire moments of optimism and happiness
- To create value and make a difference

Source: "Mission, Vision, and Values." The Coca-Cola Company. (http://www.coca-colacompany.com/our-company/mission-vision-values)

Figure 7.3 This is Coca-Cola's mission statement. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

While this is shared as a mission statement, it reads like a vision statement. The value proposition is relegated to an afterthought in convoluted corporate-speak. This is all tied into a vague "2020 Vision," which is not truly a vision statement but appears more like a wrapper for the "Mission, Vision, & Values" content.[6] It is not clear what leadership, employees, business partners, or consumers are supposed to do with this information.

Coca-Cola is one of the world's most recognizable brands. The company can grow by creating new products and by recapturing market share from competitors. It is essential, if and when Coca-Cola revises these statements, that it succinctly speak to all of those groups with one voice rather than trying to address each independently.

5 "Mission, Vision, and Values." *The Coca-Cola Company*. n.d. http://www.coca-colacompany.com/our-company/mission-vision-values

6 "Mission, Vision, and Values." *The Coca-Cola Company*. n.d. http://www.coca-colacompany.com/our-company/mission-vision-values

ARE YOU READY?

Can You Help Coca-Cola Rework Its "2020 Vision"?

Can you revise Coca-Cola's vision statement so that it more clearly states how the corporation can be a force for good in the world? Read Coca-Cola's "Mission, Vision, and Values" page (https://openstax.org/l/52CokeMission) then draft a new vision statement that alludes to hopes and potential accomplishments in the context of broad, positive, future outcomes for everyone the corporation comes into contact with.

Crafting a vision statement for an entrepreneurial endeavor is different from redrafting Coca-Cola's vision statement. A startup is in the process of defining itself, which can make it challenging to establish a far-off vision, but crafting and adhering to a vision statement can remind leaders and employees what they are capable of and what their market is all about, so it is an important step. A good vision statement is sufficiently broad to allow for your organization to move within its marketplace while still aiming to do some good in the world.

Mission

In the chapter's opening vignette, you learned about a young woman seeking to battle social injustice. Minkara's mission was self-evident. It followed her experience facing prejudice in society. Other entrepreneurial missions may not be as personal or altruistic, but they can still be a force that drives passionate solution seeking. As we saw with Minkara, entrepreneurs often develop a product or service idea through a difficult or frustrating experience, whether a social injustice or a consumer frustration.

An entrepreneurial mission is a business or nonprofit organization's reason for being. It is expressed as a self-conceptualization in the context of a marketplace and includes a sense of action. In considering a venture's mission, relevant questions are: Who are we? What do we make or do? Why do we exist as an enterprise in the first place? Steve Jobs and Steve Wozniak, cofounders of Apple, had a mission to put personal computing in the hands of everyday consumers, which meant they had to create simple tools (a graphic user interface, mouse, and so on) in parallel with hardware.

A well-developed sense of mission establishes what an organization is and what it seeks to become. Even nonprofit organizations exist in marketplaces. They have to compete for resources and define themselves by the services they provide. Establishing a clear mission helps a nonprofit organization seek funding. It helps entrepreneurs in the for-profit world explain to investors, to customers, and to employees why their "thing," whatever it is, is worth doing.

For example, the American Red Cross, one of the oldest and most well-known relief organization in the United States, has a very specific mission statement: "The American Red Cross prevents and alleviates human suffering in the face of emergencies by mobilizing the power of volunteers and the generosity of donors."[7] Defining an organization's mission clearly and specifically is essential for success.

A **mission statement**, as you read in the chapter on Identifying Entrepreneurial Opportunity is a clear expression of an organization's reason for being that defines its primary long-term goal and often includes an abbreviated plan of action for how to reach that goal. A mission statement is written by answering these questions:

- Who are we?
- What do we make or do?
- Why do we exist as an enterprise?

Developing an effective mission statement and adhering to it puts members of an organization on the same

7 "Mission and Values." *American Red Cross*. n.d. https://www.redcross.org/about-us/who-we-are/mission-and-values.html

page, and it communicates to potential partners and consumers that your organization knows where it is going. Mission statements can be revised, but it's best to get it right at the start. A strong mission statement helps stakeholders prioritize the entity's action steps and should guide decisions.

LINK TO LEARNING

This Ted Talk from Simon Sinek (https://openstax.org/l/52TEDSinek) is entitled "How Great Leaders Inspire Action." Sinek is the author of two books: *Start with Why* and *Leaders Eat Last*.

When it comes to crafting an effective mission statement, clarity is key: It must be specific. What is left out of a mission statement is often as important as what is kept in. A good mission statement is focused, direct, and honest about the marketplace in question as well as the organization's capabilities. It strikes the right balance between practicality and hope. For example, Patagonia, a well-known outdoor apparel company, has a compelling mission statement: "Patagonia: Build the best product, cause no unnecessary harm, use business to inspire and implement solutions to the environmental crisis."

LINK TO LEARNING

Check out this article on HubSpot about what makes an effective mission statement and tips on how to write them (https://openstax.org/l/52EffectMission) to learn more.

An inadequate mission statement might say this: "At Toys Inc., we make the best wooden toys money can buy, and our mission is to continue to grow to be a market leader in the classic toy industry." A better mission statement might say this: "Toys Inc. is a market leader in North American wooden toy manufacturing. It is our mission to lead the global market in wooden puzzle and wooden toy car manufacturing and to serve customers with fresh versions of classic toys." Both mission statements leave room for growth, but the second one defines more precisely what the organization is and where it is headed in the long term.

A mission statement should refrain from using clichés since these constrain the specific and unique vision of the venture. It should not limit innovation or creativity, and it should reference consumers or clients.

To create a strong mission statement, start by defining what the organization is. Even in a startup, you have a core problem-solution and an idea of what the product—and therefore the brand—will be. Be specific when defining your organization's reason for being without limiting your avenues for growth. Include or embed the service mission within the broader mission. Again, the mission statement needs to do the following things with a tone of optimism:

- Define who you are.
- Define what you do now and for whom.
- Define what you want to do in the future.

In a startup, the mission may change substantially in the early phases. Mission statements should not be crafted in a way that limits an organization's ability to pivot—that is, to adjust the value proposition to better achieve product-market fit (see the Launch for Growth to Success for a more in-depth discussion of pivoting). And while they should not be impervious to change, revise the mission statement only when it is necessary and helpful to do so. Companies and organizations usually change their mission statement when they have made a major shift (due to an acquisition, pivot to another market, new growth strategy, etc.) or if their purpose has changed in a major way.

For example, the March of Dimes organization was originally founded to serve people afflicted by polio, but with the success of polio vaccinations, the disease was eradicated in the United States. As a result, the March of Dimes changed its mission to focus on preventing birth defects, premature birth, and infant mortality.[8] In another example, Slack, a venture-backed startup that went public in mid-2019, was founded as a way for online game developers to collaborate. The original venture failed (twice), but the founder noticed that his engineers used the tool for rapid collaboration and did not need email or other functions of Microsoft Windows. Slack quickly communicated this change in a simple mission statement: "Slack is where work flows. It's where the people you need, the information you share, and the tools you use come together to get things done."[9]

One thing should be clear: It is not the purpose of an organization to come up with better mission and vision statements. The purpose of an organization is to provide value to people and try to get paid or supported in doing so. The point of crafting mission and vision statements is to assist you to that end. Essentially, your vision statement is your dream, and your mission statement is your strategy in a real-world marketplace. The vision is a statement about why you matter as an organization with a view of what the organization will become in the future, while the mission is a statement about those who might be served by the venture. Refining these statements will help you clarify your entrepreneurial story.

Goals

An organization needs to establish concrete goals for its products and services to remain viable. Goals should be stated in precise terms that are appropriate for the marketplace. For example, a new "white table" Italian restaurant in Chicago needs an initial goal on how it will attract and retain new customers based on its vision and mission, relative to what is already available. A new company's initial goal is probably not to crush all competition and take over a monopoly position. Instead, it may hope to capture a percentage of a close competitor's market share or create a new product to reach a niche market. In those instances, goals would be stated as specific outcomes to attract competitors' customers, or in the case of a niche business (like Spanx), to define a new category of women's comfort apparel. Lululemon Athletica, which pioneered customer-centered designs for women's athletic apparel, recently established new growth goals that were consistent with its mission: "Management is hard set on growing the company to $4 billion in revenue by 2020. This involves growing historically small contributors to the top line, such as men's, international, and the digital business."[10]

Goals can be tactical in the short term too. They should be reasonable, influenced by a detailed understanding of the marketplace and the competition, and attainable. Nothing stunts growth and clouds the path to achieving your vision more quickly than setting unattainable goals and holding members of an organization to impossible standards. Instead, set SMART goals, which you first were introduced to in The Entrepreneurial Perspective. SMART stands for specific, measurable, achievable, relevant, and timely. The best goals clearly communicate all of these elements, as shown in Figure 7.4.

8 Kelly Medwick. "Why, When and How to Change Your Mission Statement." *Firespring.* February 13, 2018. https://blog.firespring.com/why-when-and-how-to-change-your-mission-statement/
9 "Slack Integration." *FounderHub.* n.d. https://founderhub.io/integrations/slack
10 John Ballard. "Lululemon Athletica Pushes Forward With Ambitious Goals for 2020." *The Motley Fool.* December 17, 2017. https://www.fool.com/investing/2017/12/10/lululemon-athletica-pushes-forward-with-ambitious.aspx

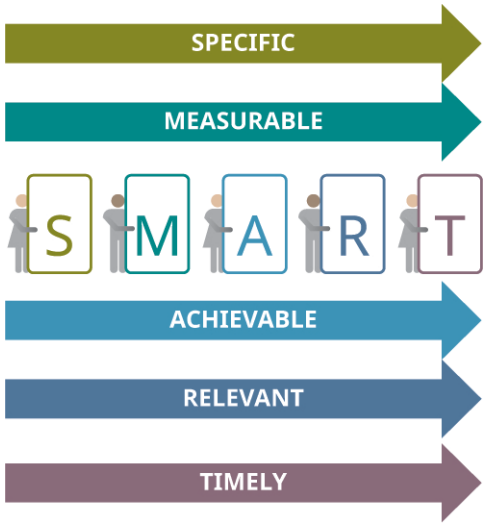

Figure 7.4 Creating SMART goals can help you realize your vision. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

To break these down, SMART goals should be:

- Specific: Your goals should be precise rather than overly broad.
- Measurable: You should be able to test, in some quantifiable manner, whether a goal has been met, meaning that there needs to be some method to determine whether the goal has been met.
- Achievable: The goal must be attainable; it cannot be so lofty that it cannot be accomplished. On the other hand, the goal should not be so easy that it can be accomplished quickly or with little effort.
- Relevant: The goal should be well suited for what you want to accomplish; this means that the goal should be relevant to the outcome needed.
- Timely: Each goal needs to have a defined deadline: the time when the goal must be accomplished. What time frame do you have for completing your goals? How does this timeline fit into your overall plan?

Is it a reasonable goal for a specialty soap company to strive to capture 1.5 percent of the global market share two years after incorporating? Let's deconstruct the goal to assess how SMART it is. It is *specific* because it establishes a clearly targeted amount (1.5 percent) of a defined market (global specialty soaps). Market share is *measurable*. We can assume that this is an *attainable* goal for our imaginary startup. Is it relevant? Capturing market share is always *relevant* because it translates to near-term earnings and potential for future earnings at the same time. The goal as stated is also *timely* (within two years). Thus, this is a SMART goal.

LINK TO LEARNING

Check out the University of Virginia's detailed exercise on writing SMART goals (https://openstax.org/l/52UVASMART) to learn more. It includes one example of a SMART goal, and, for each letter, it includes an explanation of how the concept is applied. Follow the link to write your own SMART goal and analyze it using a helpful questionnaire.[11]

SMART goals are not guarantees of success. As an entrepreneur, you could be wrong about whether a goal is attainable, for example. Or you may fail at measuring outcomes correctly, and your idea may not be as well defined or unique as you thought. Nevertheless, it is much better to set goals with all of these factors in mind than to practice wishful thinking or set abstract goals and hope to reach business benchmarks by luck.

11 "Performance Management Goal Setting." *University of Virginia.* n.d. https://hr.virginia.edu/career-development/performance-management-process/performance-management-resources/goals

WHAT CAN YOU DO?

SMART Goals for Social Activism

You can use SMART goal-setting methods to plan a peaceful social demonstration. Mobilizing people to speak out about an issue that they want political leaders to address is one of the most basic tasks social entrepreneurs undertake. Social entrepreneurs who go on to found successful nonprofit organizations often cut their teeth in this kind of base-level activism. But just because the concepts underlying demonstrating are somewhat straightforward—contact media, gather people, march, demonstrate, speak out, tell your story, clearly state your petition for change (also known as a "redress of grievances"), peacefully disperse, and strategize next steps—that does not mean that the process is always done according to SMART tactics. Protest organizers often vary immensely in their organizing skills.

Here is the task: Think of an issue that you want addressed on your campus or in your community. Define it and draft a plan for a peaceful demonstration wherein the demonstration is clearly goal-oriented.

- State the specific issue you want addressed, who you want to address it, and what you want them to do.
- State several ways you might measure the success of your protest. Are you seeking media awareness, legislative change, or specific action regarding an individual victim or perpetrator of a crime? Be sure to clearly state not only reasonable expectations regarding reactions to your demonstration but also measurable outcomes you can communicate to others as you work to gather interest in your cause.
- Note whether your demands target the right leaders and whether what you ask of them is something you can attain.
- Demonstrate clearly how the specific action you plan to take is relevant to the cause at hand. Will you demonstrate in one place? Will you carry out some form of active protest such as a "die-in" at a certain location?[12] Will you practice nonviolent civil disobedience? Clearly explain why your action is relevant to your requests or demands. If you are planning an act of peaceful civil disobedience, are you and everyone you are encouraging to participate aware of the possible consequences, such as arrest? If someone is risking arrest to help demonstrate for an important cause, they are right to demand of protest organizers that the action be relevant and easy for target audiences to understand.
- Is your strategy timely? Are you planning a demonstration with measurable outcomes that will occur according to a timeframe you can track? It is generally ill-advised to petition for general fixes to complex solutions without paying attention to existing legislative and/or communicative cycles.

Note that this is presented as an exercise only. Much more planning goes into successful demonstrations, but this should give you a sense of how SMART goal setting can be useful for social entrepreneurship. It is not only for taking business risks. You can use SMART tactics to peacefully push for important changes. Recognize, obviously, that the risks are quite different for this type of social entrepreneurship than for other types of endeavors.

Thinking like a business entrepreneur again, recognize that SMART goal setting is a tactic for getting things done in the short term. You can line up several attainable goals over a period of several weeks or months, and build your way to a complex, realistic business plan. The Small Business Administration (SBA) business plan template,[13] for example, includes eleven core sections and, as a blank outline, is thirty-five pages long. If you set a SMART goal to complete each section in about a week, in three months, you would have a comprehensive business plan.

12 Tamar Harris. "Road Safety Advocates to Hold 'Die-in' at City Hall." *The Star.* March 25, 2018. https://www.thestar.com/news/gta/2018/03/25/road-safety-activists-to-hold-die-in-at-city-hall.html

13 US Small Business Administration. "US Small Business Administration 8(a) Business Plan." March 31, 2014. https://www.sba.gov/sites/default/files/SBA%201010C.pdf

7.2 Sharing Your Entrepreneurial Story

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Learning Objectives

By the end of this section, you will be able to:

- Identify the importance of telling your own story
- Describe the advantages and disadvantages of using stories to build a startup

The popular reality TV show about entrepreneurs making pitches, *Shark Tank*, is sometimes erroneously described as a show about pitching. This is false. *Shark Tank* is a show about people, usually inventors, with interesting back stories who are now looking for help getting their product to its next step. The show offers them the opportunity to pitch their idea to a panel of investors who, if they like the idea, make a financial offer in return to help get the product to market. Every pitch is preceded with what reality TV producers deem to be the more interesting narrative—the entrepreneur's story. Viewers learn what inspires entrepreneurs, how hard they have worked on their prototypes and pitches, and what they have riding on those few minutes in the room with the "sharks." Only after the entrepreneur's story is set up do we get to the punch line, so to speak—the five-minute memorized pitch—which, if the entrepreneurs' ideas seem viable, is followed by further talk about valuation and mentoring.

Shark Tank is not a course in pitching products, but it does highlight an important aspect about the practice: Stories matter. They matter to both investors and customers. Many angel investors base their decision more so on the team giving the pitch than on the product itself.

Telling Your Story

As an entrepreneur, you need to be able to effortlessly discuss your product and its problem-solution narrative, its value proposition, its market niche, and the competition, but in your pitches, you also need to be able to tell *your* story. Prepare to tell your entrepreneurial story by applying the most universal story format: the fairy tale. Here is a template you can use:

> Once upon a time, we had a problem. Then, we thought of the most ingenious solution. We worked really hard and built several versions of the solution until we found The One. This, the innovation you see before you, is The One. We arrived at it through great personal cost, but here it is, and you can own part of it, not just the innovation on the table beside us, but the idea. You can own a sizeable portion of this business and its potential future growth. All you have to do is trust us, and you can be part of the magic. We will deliver this innovation to millions and make their lives better. We'll grow rich together and make the world a richer place at the same time. Join us. Invest, and live happily ever after.

Of course, the fairy tale format is not a formula for giving a practical, professional pitch, but it can help you put the pieces of your own entrepreneurial journey on paper so you can weave key details into your pitch as it develops.

WORK IT OUT

Writing Your Entrepreneurial Story

Take the preceding fairy tale template and use it to write the story of the entrepreneur behind your favorite product or brand. For example: "Once upon a time, Steve Jobs had a problem. He wanted to fit a computer into a box the size of an oversized cell phone…"

Conduct some biographical research on an entrepreneur and, after fleshing out the fairy tale, answer these questions:

- Why does the entrepreneur's story matter to investors?
- Is there a way to craft an entrepreneur's story so that it appeals simultaneously to both investors and consumers?
- How would you weave fairy tale elements about this entrepreneur into a mock pitch for their most ingenious invention?

Once a company grows, its story grows. But the original stories of the founders still play a part. This bigger story is called a corporate narrative. A **corporate narrative** is not a fairy tale but relays how a successful company grew from something small, perhaps starting in a garage in California, into a powerful firm or corporation serving millions of people. Companies craft narratives, often with several embellishments, for marketing purposes, but they also serve to remind leaders and employees about the vision and dreams the company's founders once had.

An example of a startup that still inspires many today is the Hewlett-Packard Corporation (HP). Its origins lie in the efforts of Bill Hewlett and David Packard, two Stanford University classmates in the 1930s. Much like members of a garage band, they started their company in a real garage, and the firm has outgrown its humble beginnings many times over. You can see the actual (restored) garage in Figure 7.5.

Figure 7.5 Hewlett-Packard has restored the original garage in Palo Alto, California, in which its two cofounders, Bill Hewlett and David Packard, former Stanford University classmates, began work in 1938 on the electrical switches and sound oscillators that became their new company's first products. (credit: "HP Garage in Silicon Valley" by "MGA73bot2"/Wikimedia Commons, CC BY 2.0)

The Advantages and Disadvantages of Using Stories

The primary advantage of using stories in pitch development is that they are relatable. Stories are how we make sense of our lives, so it's natural for stories to help others make sense of our new ventures. Stories are useful for transferring concepts with imagery told from a particular point of view.

When making a pitch, it is best not only to convey the value proposition of your product but to convey the value in the way that a loyal, enthusiastic consumer of the product (a brand advocate) would see it. Your goals become their goals. For example, Nike's Air Jordan brand has one of the most powerful advocate communities in the world. They are motivated by stories of being, in some small way, like one of the greatest athletes of all time. Inspired, they not only buy Nike shoes and clothes, they camp out and wait to be a part of the latest release—like people waiting for the next installment of their favorite film on opening night. Using narrative structures to get your pitch points across can inspire potential investors to see and share your vision and

goals. The downside to narrative-based customer development and marketing is that it can lead to a culture of manufactured need. A new form of consumerism, built on what marketers call the "fear of missing out," is another way of characterizing the euphoria people feel when they are enraptured by a brand. **Fear of missing out (FOMO)** refers to the sense that we need to keep up with our peers and the personas they represent in social settings, particularly on social media. They can say they were there and that they had the best stuff first. Critics would say that building such a strong identity to a brand, or even material goods, clouds people's sense of what is really important in life.

Even as you develop skills in pitching products by crafting inspiring narratives, be aware of the ethical implications of your work. You need to learn how to successfully make pitches to grow a brand and a company or nonprofit, but this is not a license to ignore the impacts of your work. Instead, consider this a call to action to balance your entrepreneurial, consumerist pitches and efforts with pro-social ones as well. Across a career, this kind of balance may be achievable, and, for both mass consumer products and purposeful social entrepreneurship efforts, good storytelling will help you achieve your objectives.

There is another type of narrative that can be pernicious—that of the wildly successful entrepreneur who has it all. Yes, this chapter starts by comparing entrepreneurs to superheroes. They do accomplish things other people only dream about, but many of the most famous ones have anomalous careers marked also by favorable conditions, luck, and hard work. The narrative that matters other than that of your entrepreneurial effort is your own personal one. The same way a successful startup is expected to iterate and overcome failures, so too are you encouraged and expected to persevere after setbacks when it is reasonable to do so.

As with the rapidly evolving tastes and habits of consumers in the face of "omnichannel" marketing practices in the US economy, it is impossible to be out in front of all of the latest information and communication technologies (ICTs). Even manufacturing technology evolves rapidly. If you make it an essential part of your corporate narrative that you are always "on top" of all technologies, you may be setting your business or service up for failure. ICTs and manufacturing are massive sectors in the global economy. You are not expected to know everything about them. If you can conquer your FOMO regarding the latest technological developments, your story may not be perfect, but you will be able to work from a personal and corporate position of balance.

Also, be realistic about your own entrepreneurial story. Entrepreneurs who focus too much on their own narrative might miss important market challenges or deep-seated problems with their design or key features. Issues may arise and be ignored, to the peril of the endeavor, if entrepreneurs believe their own stories are a matter of destiny. Ignoring hurdles, failures, and shortcomings within yourself, your value proposition, or your organization can seriously hinder your ability to grow your venture. Your role as a communicator is not to spin a fairy tale yarn and try to live in it. Rather, your role in telling your entrepreneurial story is to demonstrate your capability to overcome challenges and show your capacity for growth as it relates to perseverance, thoughtful inquiry, and providing value and solutions to others.

7.3 Developing Pitches for Various Audiences and Goals

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https://press.rebus.community/media-innovation-and-entrepreneurship/.

Learning Objectives

By the end of this section, you will be able to:

- Understand the various audiences an entrepreneur may pitch to and how the pitch goals vary for each
- Define and develop the key elements of a pitch
- Describe a pitch deck and pitfalls to avoid
- Create and create an elevator pitch

Let's look more closely at how to develop pitches. Remember that we defined a pitch as a formal but brief presentation that is delivered (usually) to potential investors in a startup. As such, a pitch is designed to be clear, concise, and compelling around key areas, typically the key problem or unmet need, the market opportunity, the innovative solution, the management plan, the financial needs, and any risks.

You will often need to craft different types of pitches for different audiences. Key audiences include potential investors, social connectors, potential partners, key employee recruits, and the broader community, particularly if one needs to request permits or regulatory concessions. One misconception about pitching is that it is always done to investors who are ready to fork over a few hundred thousand dollars to the team that presents the best idea of the day. While this is, more or less, the premise of *Shark Tank*, it is not how pitching works for most entrepreneurs.[14] Entrepreneurs may pitch to friends and family as they develop an idea, and, at another time, they may pitch to well-connected entrepreneurs and investors who have little interest in the market sector in question but who can make the right introductions or helpful connections. Entrepreneurs might make pitches in what is known as a pitch competition, hoping for a shot at funding and mentoring.

Pitches come in many forms, but underlying them is that to pitch is to *ask for something*. Table 7.3 provides an overview of different audiences you might pitch to, outlining how the approach and presentation may vary for each.

14 Bill Rader. "The Truth about Pitching (and Why Many Entrepreneurs Fail Here)." *Inc.* November 22, 2017. https://www.inc.com/bill-rader/what-theranoss-downfall-can-teach-entrepreneurs-about-pitching.html

Summary of Pitch Scenarios

Audience	Pitch Length	Pitch Approach	Key Content	Notes
Friends and family	Fifteen minutes	Usually verbal with a simple companion one-page handout explaining the concept, value proposition, and funds needed to get the enterprise off the ground	Should cover basic elements of the business model and concept, unmet need, and solution (including if it seems patentable), market and sales potential, and high-level risks	This common pitch can be emotional as founders are appealing to people they know well and are counting on their personal reputation and credibility vs. detailed data to sell the idea
Elevator pitch competitions	Two to five minutes	Usually a verbal pitch or single slide summarizing need, solution, market, opportunity	Should cover high-level innovation, value proposition, and a "call to action" to close the audience	Very common at accelerator or incubator events, university entrepreneurship events, etc. Prizes range from free services to $1,000–2,000
Judges for pitch competition	Five to fifteen minutes depending on venue/ rules	Varies from basic verbal to deck of one to eight slides, ending with a "call to action"; might require capital needs	Presentation that may include slides and/or video as specified in competition rules	These are very common and help the entrepreneur refine the pitch
Early Investors	Ten to twenty minutes, depending on venue/ rules	Standup presentation with slides and video or demo of product/ service	Presentation that may include slides and/or video; more formal than pitch competitions with a specific "ask" for capital needs and use	Very common with angel investors; often the deck is required to be sent before the event
Employees	Ten to twenty minutes	Standup presentation with slides and video or demo of product/ service	Major outcome is to inform and inspire; this can be a recurring event and should be informal	Very common in startups; usually monthly until company is profitable

Table 7.3

Audience	Pitch Length	Pitch Approach	Key Content	Notes
Trade groups/ associations	Ten to twenty minutes	Standup presentation with slides and video or demo of product/ service; may be tailored to the specific group	Major outcome is to inform and connect to other key groups (investors, customers, etc.)	Very common at trade conferences; some have their own pitch competitions
Grant-making agencies (such as NIH, NSF)	Ten to twenty minutes if in person but usually embedded in grant application	Usually written but can lead to face-to-face meeting, depending on agency rules	Outcome is to get "scored" to gain grant funding; if not awarded, company can reapply in the next grant cycle	Grants are often technical and usually awarded for research and cannot be used for any commercial activities

Table 7.3

Pitch Audiences

No matter to whom you are pitching, you usually need to include references to your problem-solution statement, value proposition, and key features, and how you prioritize that information will change for different audiences. As shown in Table 7.3, once those core sections are covered, your different presentations should be tailored for different ultimate "asks." The **ask** in a pitch is the specific amount of money, type of assistance you request, or outcome you are seeking.

Investors

You have been introduced to different types of investors and will learn about them in more depth in Entrepreneurial Finance and Accounting. For now, you just need to know the different types so you can start to think about how entrepreneurs structure their pitches to them. Individual investors want to know about team, product, value proposition, and potential return on investment. Angel investors are individuals who use their own money to invest in companies they're interested in. Venture capitalists are investors who pool money from others and use that money to invest in companies.

Pitching to many potential investors without success can be time consuming and disheartening, but in most cases, the investor's time is worth more than that of the people giving the pitch. If an investor offers feedback, it must be considered. You will probably not get all of the answers you need regarding how to make your venture an immediate success after giving a few pitches to individual investors and pitch competition judges, but if they take the time to offer a constructive critique, consider the pitch development and performance feedback a valuable experience.

LINK TO LEARNING

David S. Rose is the author of Angel Investing. Watch David Rose's TED Talk (https://openstax.org/l/52TEDRose) where he offers advice about how to pitch venture capitalists.

Friends and Family

Imagine asking friends and family for money to keep your startup going after you have maxed out your credit cards and secured a small business loan only to build a prototype and realize you do not have enough funds to get it to market. A common entrepreneurial journey starts with this sort of self-funded effort. Between 50 percent and 70 percent of startup companies in United States self-fund (savings, credit cards, or friends and family) their initial capital needs.[15,16] In one sense, you may be perceived as being more trustworthy with so much riding on the endeavor. Still, you would frame your pitch differently when going to friends and family than you would if preparing for an investor. You would probably make the tone less formal. You would focus on the value proposition and the immediate outcomes of the loan. You would point out tangible deliverables or milestones that this money would help you attain, and you would need to draw a roadmap from this contribution to likely, not just hoped for, revenues if you were to give yourself the best shot at raising money. Asking friends and family for, say, $10,000 might be more stressful to an individual than to ask an investor for ten times that amount. Your friends and family may want to invest in you, but they will also want to make their decision with a tangible narrative in mind. You want to build this narrative so that they can say: "I gave my family member X, so that they can finish building Y, to earn revenues of Z and continue forward with their innovation."

Potential Employees

Entrepreneurs also pitch to potential employees by focusing on why they are needed to help the team create something innovative and valuable. Once a product is under development, you must pitch to vendors. Prepare to explain the value proposition and key features in detail and explain how the vendor shares in revenues, such as options about accepting equity in part or in lieu of cash payments for services.

Entrepreneurs might also pitch to each other in hopes of building teams. Since most entrepreneurs are familiar with the structure of the pitch, you might be able to streamline proposals and simply state the value proposition and the ask. You will want to mention your team. The level of detail you share about who is working with you and what their contributions will be depends on the level of interest of the potential collaborator or investor. Future employees will likely want to know who they will be working with. Family and friends may not need to know the employment history of team members, but they, like other investors, will expect to know that there is a team capable of continuing to develop the product.

Other Audiences

Other types of audiences, which you can read more about in the Building Networks and Foundations chapter, include quasi-governmental bodies, individual investors, incubators, trade groups, and competition judges. (Pitch competitions are discussed at length in Reality Check: Contests and Competitions.) Understand that governments usually care most about creating jobs or retaining jobs in their communities. Advanced competitions and larger investment firms will want to see concrete numbers demonstrating product viability, market relevance, and previous growth. In other words, they will expect to see more details, and they will usually communicate ahead of time their specific interests. That being said, you must network and investigate which elements of your pitch to prioritize based on individual investor or investment firm preferences.

15 Laura Entis. "Where Startup Funding Really Comes From (Infographic)." *Entrepreneur.* November 20, 2013. https://www.entrepreneur.com/article/230011
16 Meredith Wood. "Raising Capital for Startups: 8 Statistics That Will Surprise You." *Fundera.* October 23, 2019. https://www.fundera.com/resources/startup-funding-statistics

Pitch Goals

Planning a pitch means researching region, potential investors, and current competitors working in the same or similar marketplaces. A good pitch explains not only what makes the product or service good but what makes a market good. Research markets in addition to the individual investors you would like to target. Angel investors are hard to find, but markets can be thoroughly dissected. Marc Andreessen, cofounder of Andreessen Horowitz, one of the most successful Silicon Valley venture capital firms in existence, once wrote, "In a great market—a market with lots of real potential customers—the market *pulls* product out of the startup."[17] This is presented as an answer to a question Andreessen posed to himself: "What correlates the most to success—*team*, *product*, or *market*?" He set up this question as a rhetorical tool to teach entrepreneurs that without a market, you do not have a product no matter how hard you work or how genius your team is. Investors specialize: Find investors in the right geographic location and find investors who know the market sector. Your goal should be to find mentors who can explain markets to you in significant, accurate ways. If you find a fertile marketplace, you can practice customer development, and learn and iterate your way to success.

Key Elements of the Pitch

A pitch is usually presented through what is called a **pitch deck**, alternately called a *slide deck*. This is a slide presentation that you create using a program such as PowerPoint, Prezi, Keynote, or Google Slides that gives a quick overview of your product and what you're asking for. As such, a pitch is designed to be clear, concise, and compelling, and should include the key areas shown in Figure 7.6.

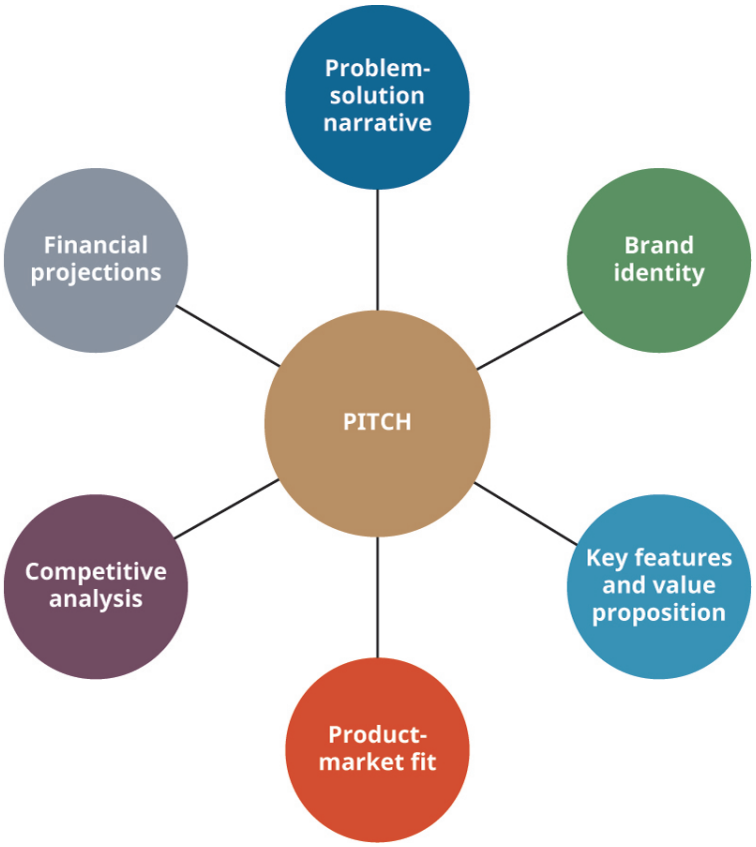

Figure 7.6 Key elements of pitch include identifying the need, the market opportunity, an innovative solution, how the venture will be managed, what funding is needed, and how risks will be mitigated. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

17 Marc Andreessen. "Part 4: The Only Thing That Matters." *The PMARCA Guide to Startups*. June 25, 2007. https://pmarchive.com/guide_to_startups_part4.html

Here are six key elements of an entrepreneurial pitch from *Media Innovation and Entrepreneurship*.[18]

- Element 1: Brand identity image and tagline. Your presentation slide deck should begin with a memorable brand image. It can be a logo representing your product in a stylized way, or it could be a screen grab of your product wireframe (a computer rendering if it is a product, and a schematic or flow chart if it is a software/service business model. The Entrepreneurial Marketing and Sales chapter covers these concepts in detail.
- Element 2: Problem-solution narrative. Some entrepreneurial ideas solve common problems. Some solve problems that users didn't know they had. Communicate the problem-solution narrative succinctly. Incorporate visuals and a "hook" (skit, emotional testimonial, deep question, etc.) to connect directly with the audience. An effective technique when addressing a generally common problem is to ask the question while raising your hand to prompt the audience: "How many of you have experienced this issue/problem/challenge recently?"
- Element 3: Key features and your value proposition. Your pitch can introduce potential investors, collaborators, employees, and others to your key features, your value proposition, and your user interface at the same time. Consider using a mockup of your product or images of a prototype to show your design capabilities while at the same time pointing out key features building to a value proposition. Or if you are a service or nonprofit venture, explain what you plan to provide to individuals or the community.
- Element 4: Product-market fit description. Define the market niche clearly and explain how your innovation serves the market purpose precisely. Not every problem is one people would pay to fix. Explain why there's a market to overcome this problem, how sizeable it is, and why your value proposition is the best. The chapter on Identifying Entrepreneurial Opportunity can help you hone in on this section and put your idea into words.
- Element 5: Competitive analysis. Demonstrate that your product is unique by defining its competition and illustrating how it will stand out in the marketplace. Investors will pay close attention to any missed or omitted competitors. They will want to see that you can establish barriers to entry, lest some immediate copycat eat up market share. The Entrepreneurial Marketing and Sales chapter covers these concepts as well.
- Element 6: Financial projections. The business model canvas (BMC) can help you understand and be able to visualize how your value proposition sits at the center of two dynamics: input and output cycles. This is covered in Business Model and Plan, but just know that you must pay for inputs and overhead, and that revenues from outputs, sooner rather than later, ought to catch up to initial expenses. Show what the overall market is worth: How big is this pie? Then, show how big your slice and your investor slice is going to be. The Entrepreneurial Finance and Accounting chapter gets into these issues in more depth. In many cases, you will want to end with a description of your team, demonstrating quickly why you are up to the task of growing this innovation. As mapped out here, this could be the basic framework for your pitch deck for a short competition. Some elements can be communicated in a single slide. Some will take more than one. Flesh out your essential pitch decks with further specifics or with data requested by competition organizers for longer contests. It is suggested that you keep your core deck to no more than ten slides and that you practice a two-minute version that covers all six of these concepts in case you meet an angel investor on the street.

If you have followed this discussion, you have established a vision for your innovation and the company you want to build around it. You have established a mission and identified a clear purpose for it. You should have a keen sense of your entrepreneurial story, but if you cannot express these things in a way that makes other people see the value, your innovation may not survive. You don't build pitch decks solely for the purpose of asking for money or support. That may be the primary objective, but when you work on your pitch, you build the narrative case again and again for why your idea has value and why other people should buy into your

18 Mark Poepsel. "Pitching Ideas." *Media Innovation and Entrepreneurship.* (Montreal: Rebus Community, Fall 2018). https://press.rebus.community/media-innovation-and-entrepreneurship/chapter/pitching-ideas/. This material is based on original work by Mark Poepsel, and produced with support from the Rebus Community. The original is freely available under the terms of the CC BY 4.0 license at https://press.rebus.community/media-innovation-and-entrepreneurship/.

vision.

The Pitch Deck

As you can see, the primary means entrepreneurs have of sharing their vision is the pitch deck. Usually ten to twenty slides can explain your company, its goals, and key information to persuade an audience to take action (usually investors to consider investing in the enterprise). Pitch presentations should be visual and engaging. They should be easy to edit and rearrange, and should engage viewers with art, panache, and reasonable appeals. In general, they communicate the inspiration behind the innovation, its future capabilities, and the strengths of the team. Incorporate as many visuals as you need and make sure the visuals match the script.

As an entrepreneur, you will be judged on your ability to develop and deliver a pitch. It can be taken as shorthand for your ability to research a marketplace, guide a team, and manage a product. Sharing your vision using slideshow software is not easy. Viewers are not impressed by status quo pitch presentations, but critical audiences will also quickly notice when a pitch is all flash and lacks a good value proposition. A strong pitch, content-wise, can be noticed, even if the slide design is less than stellar. In other words, developing a great-looking pitch deck is important, but there has to be substantial content.

LINK TO LEARNING

Explore a variety of foundational pitch decks (https://openstax.org/l/52PitchDeck) and learn what worked and didn't with each.

Let's use the slide deck from Airbnb as an example. It was presented after the company grew from its initial seed funding stage into a viable operation with high hopes for future revenue growth. That is, they were already established and making money when this deck was in use. It was presented after the initial investment stage, when the company had done a good deal of customer development.

The track record is always in question when small firms go asking for big money, so note how Airbnb describes its previous success and potential for future growth. When funded, AirBed&Breakfast would change its name and grow it into a global brand. This relatively straightforward deck from 2008–2009 is a popular example because of its simplicity and its powerful value proposition, although some experts note that the design could be better.[19] Nevertheless, this was a successful pitch deck.

Visit https://press.rebus.community/media-innovation-and-entrepreneurship/chapter/pitching-ideas/ to see a SlideShare page containing the following ten slides and two more add-ons from SlideShare. The description of this pitch deck comes from *Media Innovation and Entrepreneurship*.[20]

- Slide 1: Airbnb started out as "AirBed&Breakfast." Brand identity is established with a sans-serif typeface, use of color, and a clear tagline: "Book rooms with locals, rather than hotels."
- Slide 2: The problem statement is straightforward: Travelers need an affordable alternative to hotels.
- Slide 3: The solution statement focuses on the nature of the product, that is, that it's a web platform, and on key features and how they create value, both financial and cultural capital. Note that key features and the value proposition are already addressed through three simple slides.
- Slide 4: To establish product-market fit, you first have to have a market. The Airbnb pitch deck notes that at the time there were 630,000 users on couchsurfing.com and that there were 17,000 temporary housing listings on Craigslist in San Francisco and New York combined in one week. Thus, there existed a large potential traveler pool and a large pool of people with rooms for lease, but these groups were in need of a unified platform.
- Slide 5: The fifth slide details the size of the market and Airbnb's share, showing potential for growth.

19 "Airbnb Pitch Deck." *Slidebean*. 2009. https://slidebean.com/blog/startups/airbnb-pitch-deck

20 This material is based on original work by Mark Poepsel, and produced with support from the Rebus Community. The original is freely available under the terms of the CC BY 4.0 license at https://press.rebus.community/media-innovation-and-entrepreneurship/.

- Slide 6: Completing the case for product-market fit, this slide shows the attractive user interface and provides a mini-narrative for how the product works.
- Slide 7: This slide shows four years' of revenue totals as simple math: 10 million + trips × $20 average fee = about $200 million in revenue. This is evidence of product-market fit and whets the investor's appetite for potential future earnings.
- Slide 8: This slide shows how Airbnb has already beaten its competition to own the market for certain events and create partnerships.
- Slide 9: Here, investors get the full picture of the competition.
- Slide 10: The financial expectations are pretty well established by this point and were explained verbally. What this shows are the barriers to competition expected to help preserve Airbnb's position, future earnings, and growth expectations.

Consider what was involved in creating this Airbnb slide deck. The deck is not particularly complicated. AirBed&Breakfast, as it was called at the time, was a market leader in a niche that other companies had previously tried to exploit. The company's rapid growth was not a guarantee, but this offer was too good for investors to pass up, although at the seed funding stage, some investors did not see the potential in a service that helps people sleep in others' private residences.[21] By the point this deck was in use, the company had gotten past initial concerns about safety and viability, and was ready to grow quite quickly. A 2018 check shows Airbnb has secured funding through six rounds from a variety of major investors.[22]

As we have seen, pitch decks and pitches are developed and delivered for various reasons, to various audiences, with varying content. For example, you may prepare pitches to pursue different long-term visions for your product. Or, if you do not secure seed funding, you might scale back your idea, adjust your vision, and rework your pitch. What remains the same is the need to convey how you will bring value to users or customers, and demonstrate the core pitch elements, adjusted for each altered outlook.

Elevator Pitches

After looking at an exemplary pitch deck adapted by a niche market leader between seed funding and the venture capital quest, it may seem difficult to inspire investors via a one- or two-minute elevator speech for a project under development, but preparing for this type of pitch is essential. An **elevator pitch** is an abbreviated pitch, a memorized talk that can get you in the door to put your full pitch deck on display. The elevator pitch should touch on the key elements of problem-solution, value proposition, product-market fit, and team, and not much else.

Giving an elevator pitch is an art. The elevator pitch can be memorized and should be. It might be delivered informally at networking events or at dinner parties or other social engagements. You never know when you might need to give an elevator speech. You might find yourself talking to someone who'd be interested in your venture, and it might be at a golf outing, on the ski slopes, on the street, in a store, or, yes, in a giant investment firm's lobby as a courtesy, as in *The Big Short*. And of course, in elevators. That's why it should be memorized and up to date.

21 Alice Truong. "The Investors Who Passed on Airbnb's Seed Funding Had Their Reasons." *Quartz*. July 13, 2015. https://qz.com/452384/the-investors-who-passed-on-airbnbs-seed-funding-had-their-reasons/
22 "Airbnb Investors." *Crunchbase*. n.d. https://www.crunchbase.com/organization/airbnb/investors/investors_list#section-investors

The classic example of a good elevator pitch is the one job candidates give that lands them an entry level job in a company for they have always dreamed of working. Adapted from an article in *Forbes*,[23] there are six elements of a good job-seeking elevator pitch. First, the pitch must be targeted. It cannot sound as though just any job will do. You need to pitch yourself for the specific role the employer is trying to fill. It helps, second, to write your pitch down in order to edit it and perfect it. Third, it should be correctly formatted and, fourth, focused on the *company* where you hope to work rather than on *yourself*. Explain how you understand what they are hiring for and let that be the setup to a story that ends with you being the best person to fit their needs. Fifth, clear away the buzzwords and corporate-speak, and, finally, practice performing your pitch aloud. Elevator speeches, after all, are given in person.

LINK TO LEARNING

NPR's podcast *How I Built This* is a compelling collection of first-person accounts by entrepreneurs on all kinds of issues relating to their startups. This episode of "How I Built This" is about Sara Blakely and her elevator pitch for Spanx (https://openstax.org/l/52NPRBlakely) that turned into a bathroom pitch, and how she seized the moment for success.

However, a personal pitch is a relatively simple and straightforward task. If you're asked to write an elevator pitch for your proposed venture, start with about three sentences, or a 280-character Tweet. Write it first as a set of talking points so that you don't get hung up on trying to present the exact words in the exact order. Make your elevator speech broad enough that any member of your team could deliver it and any potential investor could comprehend it in passing. Delivering an elevator speech is a linear process, meaning a person can't be expected to read back or probe for more information the way they might with a written presentation or in a formal pitch presentation with time for follow-up questions. Be sure to bring business cards and keep your smartphone charged and ready for the exchange of contact information, a sign that you have succeeded in this first step.

WORK IT OUT

Developing and Practicing an Elevator Pitch

Part of the idea of an elevator pitch is that you never know when opportunity will strike: when might you have thirty seconds on an elevator with someone interested in supporting your business idea? That's why thinking through the pitch—including practicing it and getting feedback—can be so valuable.

- Gather a group of 2–3 classmates or entrepreneurially minded friends.
- Have each person spend a few minutes planning a 30-second elevator pitch.
- Take turns pitching your ideas. Take notes on others' presentations.
- Take turns providing feedback on the pitches. Feedback should focus less on the business idea and more on the *presentation* of the idea.

7.4 Protecting Your Idea and Polishing the Pitch through Feedback

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23 Nancy Collamer. "The Perfect Elevator Pitch to Land a Job." *Forbes.* February 4, 2013. https://www.forbes.com/sites/nextavenue/2013/02/04/the-perfect-elevator-pitch-to-land-a-job/#7843035b1b1d

https://press.rebus.community/media-innovation-and-entrepreneurship/.

Learning Objectives

By the end of this section, you will be able to:

- Understand why you need to protect your idea
- Describe both legal and unconventional tools to keep your ideas safe
- Understand the importance of feedback and how to manage and use it

When you start to pitch your idea, it means you are sharing it with a variety of people for different purposes. When encouraged to develop entrepreneurial ideas, students often ask, "How can I be sure no one is going to steal my idea?" The response often is that ideas come easily, while knowledgeable, driven leaders are hard to find. In other words, for those of you just starting out as entrepreneurs, it is important to recognize that coming up with ideas is much easier and much less important than learning how to turn those ideas into products that fit a market and that have a customer base already, or one you develop through painstaking customer development strategies. Many entrepreneurs find it is more important to sell an investor on their leadership potential and the strength of their team than on the strength of their idea or prototype. Even so, it is common for entrepreneurs to want to protect their intellectual property because more well-established companies might leverage deeper wells of resources and broader, more powerful networks to bring an innovative product or service to market in the time it takes an entrepreneur to move from securing seed funding to landing their first support for their first venture capital round (after seed funding).[24]

Protecting your business idea with a patent, should you choose to apply for one, is important. Patents are granted for the purpose of *encouraging* entrepreneurship. If innovators have some reassurance that others will be kept out of the marketplace for a certain amount of time, they may be more likely to take the risk to pursue an innovation in the first place. Intellectual property protection (patents, trademarks, copyrights) is covered in much more depth in the Creativity, Innovation, and Invention and Fundamentals of Resource Planning chapters.

Products in most fields need to be developed and brought to market more quickly than the time it takes to go through the standard patent process. For manufactured goods, it is important to seek a patent when a product is finalized to protect the design. For intellectual property, it may be best to build first and seek patents later, particularly in a highly competitive field where it would be difficult to show that you truly have a unique breakthrough.

Entrepreneur.com has some helpful suggestions[25] that are paraphrased and reframed here: First, recognize that almost nothing comes to market having been created by a sole inventor or innovator. Some ideas truly are unique, but even they are nearly impossible to keep "under wraps." Ideas have to be shared with many people for products or services to be developed. If nothing else, you will likely have to present your idea to investors at some point. Protecting initial ideas is not as important as protecting versions of products and services developed through iterative learning and testing processes because "know how" and trade secrets are considered intellectual property and must be protected since they are not always patentable. Aim to protect your successful value propositions, not your every technological whim. Most new business ideas are variations of solutions that others have anticipated or even written about, but others have not had the drive, the networking skills, or the fundraising ability of a true entrepreneur. Balance your time wisely between trying to protect your idea and working to develop it.

24 Some of this material is based on original work by Mark Poepsel and produced with support from the Rebus Community. The original is freely available under the terms of the CC BY 4.0 license at https://press.rebus.community/media-innovation-and-entrepreneurship/.

25 Stephen Key. "How to Protect Your Business Idea without a Patent." *Entrepreneur.* May 8, 2013. https://www.entrepreneur.com/article/226595

One way you can gain some peace of mind, again to paraphrase Entrepreneur.com,[26] is by thoroughly investigating everyone with whom you plan to partner. If you have some assurance that they have not "burned" collaborators in the past, you can proceed with a sense of security. Conduct research without invading anyone's privacy but use all of the public tools available to you. Search online to learn about potential partners and their previous endeavors. Request contact information and perhaps a list of references or former collaborators from potential partners. The level of formality is going to depend on the nature of the industry you are working to enter and the nature of the relationship you have with your collaborators, but if they resist being researched, that could be a sign that they will probably not prioritize you or your product's protection.

Legal Agreements

Outside of patents, there are additional legal means of protecting your intellectual property.[27] You may wish to require partners to sign a **nondisclosure agreement (NDA)**. Typically, NDAs carry with them a penalty should the partner disclose what they know of the proprietary information that lies at the heart of your value proposition. These can be time limited, meaning after a certain amount of time, someone will be free to discuss the business and its proprietary practices, or, for stronger legal controls, they may be open-ended. An open-ended NDA can require a person to stay silent about key information for life or face possible civil lawsuits worth potentially millions of dollars.

A **noncompete agreement** in a contract prevents an employee from working for the competition for a specified period of time after working for you. The intention is to prevent them from taking your secrets or their skills to a competitor. Some of these practices have been called into question particularly in industries where low-level workers who do not carry around trade secrets find they are asked to sign these types of agreements. However, they can help keep corporate espionage to a minimum, and they can prevent certain key employees from taking the organization's intellectual property with them to their new employer, or perhaps to create their own startup. Employees should only sign them if they are a condition for employment. These agreements can vary from state to state. California in general does not enforce noncompete agreements; this is due in part to the dynamic nature of startups, particularly in Silicon Valley. It also reflects a philosophy that working professionals should not be inhibited or restrained from pursuing their livelihood.

A **work-for-hire agreement** between an individual employee and a company states that ownership of innovations belongs to the company, even if an individual makes substantial contributions to the product, service, or process. You should expect to be required to list collaborators on patents, even those working under a work-for-hire clause, but the *purpose* of the contractual agreement is to ensure that you or your company maintains exclusive rights to the patent.

Unconventional Methods

One further suggestion is to apply creativity and mask your product or service's true nature. By de-emphasizing certain key features or by burying them in the user interface (UI), you might be able to turn attention away from your value proposition while still building your product, platform, or prototype. The **user interface (UI)** is what a customer sees when they use your product. A graphic user interface (GUI) is common for all Windows and Apple-based devices. Smartphones use application (app) interfaces built off the base operating system (mainly iOS or Android). UI's have become very common for many consumer and professional products, as they link to microprocessors, sensors, memory, and other embedded features. From a design standpoint, your team must decide where every button, search box, graphic element, and information display is placed and what it will look like. Good UI is useful and feels intuitive to the user.

For digital products and services, this aspect of your product is incredibly important, which is why manipulating it to mask functions or features is particularly risky. This is not a fool-proof approach by any

26 Stephen Key. "How to Protect Your Business Idea without a Patent." *Entrepreneur.* May 8, 2013. https://www.entrepreneur.com/article/226595
27 Stephen Key. "How to Protect Your Business Idea without a Patent." *Entrepreneur.* May 8, 2013. https://www.entrepreneur.com/article/226595

means, but in hyper competitive, rapidly evolving environments such as the web software and mobile app industries, where invention and iteration occur at a breakneck pace and where, as soon as you go to market, your competitors can see and try to re-create your service or platform, a little subterfuge can give your business an edge at a relatively low cost.

An example of masking the true intentions of a product, perhaps, is the development of the mobile game Ingress by Niantic, Inc. Ingress is a GPS-based augmented reality game played around the world where users join imaginary factions and take over imaginary portals tied to real geographical locations in order to link up those portals and help their faction gain territory and resources. But while Niantic was taking its global mapping expertise and making a SciFi game out of it, it was also developing Pokémon GO. After specific geographic "nodes" were mapped by users the world over, Niantic had a global network of points of interest indicated by users. In many cases, nodes in Ingress—places with public art, cool architecture, or historical markers, for example—later became PokéStops in the Pokémon GO game, where players of the global augmented reality game gather resources to catch and battle their pocket monsters.

One way to protect your intellectual property is to strategically mask dormant features or capabilities until they can be more fully exploited. While few startups have the technological clout of Niantic, almost every business makes decisions on what to push forward, what to hold back, and when to release new products or features.

Using Feedback to Refine Your Pitch

Pitching requires you to demonstrate that you have assembled a capable, professional team that can turn an idea into an innovation. Users, partners, investors, and others will offer thoughts on how your product or your organization should change. Investors consider it a warning sign if an entrepreneur cannot handle feedback.[28] Applying lessons learned from feedback is the purpose of business learning.

Entrepreneurial ventures often start out as problems with no easy solutions. Your initial idea involves your best guess at what will be an innovative solution, but that will evolve more quickly toward product-market fit if your response to feedback is to accept it with grace. Your pitch must demonstrate that you have a great product, that you have done your research, and that you are able to take feedback and apply it to your products to make them better.[29] In other words, you must show you are coachable.

Your venture's development depends on gathering data to find out what customers like and what investors are willing to fund, so you must seek out positive feedback and build on it, but you must also think critically about the positive messages you receive. Are consumers or users enthusiastic in their support or merely polite (this can especially be a concern when pitching to friends and family)? Can you clearly identify why you received positive feedback about certain features and not others? Be sure to gain feedback on many product variables and be sure you can isolate data points for meaningful analysis. The best feedback includes quantitative responses indicating what consumers like and what they don't, as well as qualitative information explaining why. Quantitative data relate to numerical measurements including actual purchase and behavior as well as opinion research about a product. Qualitative data are complex information that answers the questions "Why?" and "How?" It is often impossible to tell why people do what they do with your product unless you ask them.

28 John Rampton. "25 Reasons I Will Not Invest in Your Startup." *Entrepreneur.* September 15, 2014. https://www.entrepreneur.com/article/236999

29 Michelle Ferrier and Elizabeth Mays. *Media Innovation and Entrepreneurship.* (Montreal: Rebus Community, Fall 2018). This material is based on original work by Mark Poepsel, and produced with support from the Rebus Community. The original is freely available under the terms of the CC BY 4.0 license at https://press.rebus.community/media-innovation-and-entrepreneurship/.

In the short term, you can use feedback to decide which features to focus on early in the venture. Many entrepreneurs are faced with the dilemma of having too many good ideas.[30] If you pursue all of your good ideas at the same time, your organization can quickly run out of resources. Focus first on features that are most popular and relatively affordable to produce and deliver. Those high-return products, services, or features might not be what you use to define your brand in later years, but they can sustain a startup long enough to develop more elaborate products and features that require more time and investment. Over the long term, feedback helps you direct your company.

Feedback may also come from employees, market leaders, and your competition. Feedback from these sources may be more useful for guiding long-term growth projects. In this sense, feedback means more than advice or product ratings. It can mean tactical moves in the marketplace. Your competitors offer you feedback when they take actions in a marketplace in response to your actions. Be sure to attend to competitors' actions with the same open mind and the same air of thoughtful skepticism you apply to other forms of feedback.

Once you have the opportunity to pitch your idea, the next step is the careful measuring of quantitative and qualitative feedback about the pitch presentation, mockup, poster, or, in the case of many manufacturing processes, a 3D-printed model that approximates what the tangible finished product might look and feel like. Data from pitch competitions are sometimes out of your control, so it may be preferable to incorporate the learning you get from pitch feedback into this customer development process.

7.5 Reality Check: Contests and Competitions

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Learning Objectives

By the end of this section, you should be able to:

- Identify resources for locating contests and competitions
- Understand the opportunities and realities of contests and competitions

Now you have an idea of how to communicate the purpose of your innovation through clear mission and vision statements, while setting tangible SMART goals for your startup. You should also have a basic understanding of how to pitch your innovation to different groups using different types of pitches to garner financial support, to attract skilled talent, and/or to garner contributions if you are a social entrepreneur. You have some strategies to protect your idea, and you have reviewed how to incorporate feedback into an iterative process to improve and refine the concept or prototype. Now it is time for a reality check. What can you actually do as a student entrepreneur to enter the marketplace ready to innovate and make your first pitches?

First things first: Use your educational and professional background to conduct research to determine the kind of entrepreneurial environment that suits you. Do you wish to work for a startup and put your creative talents to work helping an existing team to build on their ideas? Are you looking to get in on the ground floor to help develop a startup from scratch, adding your knowhow about pitching to the mix? Or, are you looking to be an entrepreneur and build your own team around your own innovative ideas? You owe it to yourself to explore these options through careful research.

Regional Resources

Just as communities invest in schools to educate students for the improvement of the entire community's standing, some communities are starting to see the long-term value in investing in entrepreneurs. Here are some of the resources to look for:

30 Mayo Oshin. "5 Things to Do When You Have Too Many Ideas and Never Finish Anything." n.d. https://mayooshin.com/5-things-to-do-too-many-ideas/

- Shared workspaces where entrepreneurs come together to work on their independent projects as well as to build teams. HQ Raleigh in North Carolina is one such space that offers multiple membership options, office and kitchen facilities, and other perks. WeWork is another space, located in New York City, as is Spark in Baltimore, Maryland (Figure 7.7).
- Business incubators or accelerators that do more than offer office space. They offer mentorship rather than a good coffee bar.
- Pitch competitions to begin to garner the feedback you need to refine your value proposition(s) and develop a comprehensive business plan.

Figure 7.7 Workplace or clubhouse? Some companies offer playful perks in shared workspaces in an effort to attract the best employees and increase worker satisfaction. (credit: work by Jason Putsche Photography/Spark Baltimore, CC BY 4.0)

Depending on the size of the community where you choose to live, there may be different types of entrepreneurial niches for you to target, or there may be a more generalized entrepreneurship space. Regardless of the size of the community, it is the people in it and your ability to network that will most strongly influence your potential. One option to pursue is to be part of a product pitch within six months of landing in a new city. Perhaps you are pitching your own focused idea, or perhaps you take your talents to a team with a pitch already in the works. Regardless, as an individual with an interest in being an entrepreneur, if you are not collaborating and competing, you are not growing your business or social venture.

Contests

According to Entrepreneur.com,[31] it is essential to take the temperature of the contests available in a certain geographic region before diving in. An **entrepreneurial contest** is any entrepreneurial competition other than a pitch competition. They usually are run by nonprofit organizations and universities, but more companies are hosting them to open up to more outside innovation to attract diverse entrepreneurs and access nontraditional sources of new ideas with commercial potential. They usually entail submitting documentation about your business, items such as business models (covered in Business Model and Plan), prospectuses, and forms tailored to contest specifications.

There are many reasons for joining a contest. Finding a mentor is at the top of the list. Your first contests and pitch competitions provide a learning experience for yourself as well as an opportunity to network and look for mentors and potential collaborators. To prepare for a contest, find out exactly what is expected of you and do as much research as you can so that you are writing using the **iceberg principle**. Following this writing principle, each word or sentence in your contest submission should be backed up with a wealth of supporting information and details. Even if judges never see a long-form prospectus, a detailed summary of the business, the investment that the company is seeking, or the key risks that the company faces—ensuring you have the hard data to back up those points in your executive summary or introduction increases your chances of success in the competition.

31 "Entering a Small Business Funding Contest." *Entrepreneur.* January 25, 2017. https://www.entrepreneur.com/article/286209

Entering a contest is similar to deconstructing your pitch deck, backing up every point with careful research, and writing and presenting the information in the various formats requested. Contests may ask for papers, posters, videos, social media campaigns, and other materials. Whatever kinds of media product the contest requires, you must complete them in a professional manner. If you truly want to win a contest that requires multimedia or social media elements, you might want to hire a media professional to assist you in this, which is essentially a marketing effort.

If and when you win a contest, make connections with organizers and seek mentorship. Great mentorship, in the long run, is more valuable than a cash prize with strings attached. A good mentor and a good market niche are often better predictors of entrepreneurial success than a person's ability to develop compelling contest packets or highly charged pitch presentations. To be an entrepreneur, you need to know how a business sector functions within a social, cultural, and regulatory geographic context. To the extent that entering a contest can help you learn about these things, it is a valuable effort, but in most cases, the prize funding of $5,000, $10,000, or even $20,000 won't guarantee your startup much of a head start.

Contests on college campuses may be more worthwhile than others because of the number of mentors brought in to judge them. Mentors that understand regional markets and opportunities for networking can be quite valuable, and contests may be one of the few times that large numbers of professionals get involved in a college course or extracurricular exercise. Also, competitions may be put on by business groups or social entrepreneurship groups on campus that provide great networking opportunities. Some contests compose the preliminary phase before the pitch competition that follows. In that case, you would prepare your pitch deck as you prep your contest application to ensure that your pitch matches your claims. It may seem fairly straightforward, but when discrepancies exist between what you submit and what you ultimately present, judges will notice. Regardless, a contest on a college campus or in your niche market gives you a chance to research your market, scrutinize your own ideas, and build a team.

Building a team for a contest with the ultimate goal of creating a successful endeavor is one of the most exciting but trying aspects of entrepreneurship. Many entrepreneurs are reluctant to relinquish control and seek people who will do things only the way they want them done. This is not usually possible, and it is not advisable. You want to build a team of people who can see a problem from different points of view and can offer constructive, honest input. Your best hope is to establish an ethic of clear communication and respectful give-and-take when it comes to criticism because there will be differences of opinion and approaches. If a contest is nothing more than an impetus to build a good team, it is a worthwhile effort. There are many ready sources to find out about these contests; check most entrepreneurship programs at major universities (some are open only to students and/or alumni, but others may be open to others). Also check with major startup sources (such as TechStars or Y Combinator) as well as with local economic development entities. Finally, you might locate contests focused on particular groups for which you may qualify, such as women entrepreneurs or other historically underrepresented groups.

Competitions

Like contests, **pitch competitions** (Figure 7.8) may offer cash prizes or mentorship opportunities to the winners. Some larger pitch competitions have seed funding agreement contingencies that winners must sign before they can accept cash prizes. The key difference between a contest and a pitch competition is that in the latter, you are expected to present your business idea in the form of a presentation, usually with a pitch deck, whereas in the former, you are expected to provide a more informal summary of your idea, though the prizes in contests are less (e.g., $1,000 in free legal or other business services vs. a much larger cash prize).

Figure 7.8 Universities, communities, funders, and other interest groups offer pitch competitions to support entrepreneurial ventures. Shown are participants in the Road to GES (Global Entrepreneurship Summit) Heartland pitch competition in Overland Park, Kansas. (credit: "Pitch Competition at Road to GES Heartland" by "Global Entrepreneurship Summit Follow"/Flickr, Public Domain)

Look for competitions in your city and in locales within half-a-day's drive such that you could compete in pitch competitions without spending too much time or resources on travel. Seek out competitions that focus on the market sector you are most interested in. Play to your capabilities and strengths. Some pitch competitions are sponsored by regional economic development offices. Such offices are often associated with small business development centers, which are often based at or connected to major universities, local SCORE offices, and SBA offices. They often offer cash prizes in the hopes of attracting nascent startups to their region. Others connect entrepreneurs to investors waiting with seed money and a contract stipulating what percentage of the business they will own. Some offer money toward legal, accounting, mentoring, and other services. This is how seed funding works, but contest winners would do well to ask for legal advice before signing a contract tying up a portion of their business as a condition of receiving an award or a level of seed funding they might be able to secure through other venues.

This explains why some entrepreneurs seem to tank their own deal on *Shark Tank*. In some cases, perhaps they are foolish to pass up a deal, but in other cases, they have other avenues for seed funding in mind that may give them more control of the future of their company. The last thing you want to do is to win a competition and sign a contract for an investment in the business that does not lead to or protect your end goals. While the show *American Idol* has been a cautionary example[32] (winners of *American Idol* usually sign an exclusive recording contract that is restrictive for the artist and limits them from signing with a major recording company for several years), most investors will almost always want to own a piece of the long-term future of any entrepreneurial effort they help fund. Before entering a competition, learn whether the nature of the prize requires this type of seed funding agreement or not. Base your decisions on your own comfort level with this type of arrangement as well as research how previous winners have been treated and what successes and failures they have had.

To win a pitch competition, find out exactly who you are pitching to and what criteria they will use. Be sure to thoroughly read through the competition guidelines and learn what you can about the specific judges and their backgrounds. Tailor your pitch to fit contest objectives as much as you can without changing your value proposition or promising features or deliverables you cannot make good on. Match the ask with what the contest offers. Nothing annoys contest judges more than when the prizes and offers are clearly laid out in the contest guidelines and then pitch presenters ask for much more money or for something completely different than what they have on offer.

32 Nasir Pasha and Matt Staub. "The Prize for Winning American Idol? A One-Sided Contract." *Pasha Law*. February 6, 2015. https://www.pashalaw.com/prize-winning-american-idol-sided-contract-e148/

You should develop one core business model (which you'll learn about in the Launch for Growth to Success chapter), pitching several times to individuals, entrepreneur groups, investors, and competition judges (unless that is your day job). This will help you develop your pitch for the market niche. Over time, you will learn what to stress and what to downplay or cut, and this may help you win competitions.

As a college student, you can participate in campus pitch competitions to practice learning a market niche. Perhaps the market niche you explore in college will be similar to the ones in which you work after graduating. If you are in a college town, it may be a peculiar marketplace, but it will usually have an abundance of mentorship opportunities making up for what it may lack in business infrastructure. Make your pitch decks professional and rehearse your presentations until they are perfect. You must also be a studious audience member at such competitions. It is not uncommon for an entrepreneur to master their own approach after watching others present for a year or two.

The Collegiate Entrepreneurs' Organization, for which the initialism, CEO, is apt, has chapters in more than 300 universities around the United States. It champions entrepreneurship as a field unto itself rather than as a byproduct of an MBA program or a limited track in a business school, as it is treated in many universities. Regardless of the institutional infrastructure, many colleges have chapters.

ARE YOU READY?

Collegiate Entrepreneurs Organization

Research the CEO and whether there is a chapter on your campus. Table 7.4 shows the information from the national organization's website.

Collegiate Entrepreneurs' Organization Vision and Mission[33]

Vision Statement	Mission Statement
To serve more than 400 colleges and universities helping students achieve their entrepreneurial dreams and goals, CEO provides student entrepreneurs with opportunities, events, chapter activities, and conferences to help start businesses.	To inform, support, and inspire college students to be entrepreneurial and seek opportunity through enterprise creation. With a diverse entrepreneurial community and global network, CEO provides student entrepreneurs with opportunities, events, chapter activities, and conferences to help start businesses. The highlight of the year is the annual Global Conference hosted each fall.

Table 7.4

If your campus has a chapter, contact leadership and find out how to join. If you are already a member, explore how you can become a student leader in the organization. If you are in CEO and are a student leader, come up with a plan to leave a positive, lasting impact on your local chapter. If your campus does not have a local chapter, check with the Student Activities/Campus Life Office to see how you can start one there. There might be a similar group with this focus under a different club/organization title.

- What are some successful businesses that CEO chapters or groups within chapters have started?
- What one or two key changes might be made to make your local chapter stronger?
- Whom can you contact and work with to make that happen?
- What will your primary entrepreneurial objective as a member of CEO be? Can you use the group as a launch pad for your own startup? How?

33 The Collegiate Entrepreneurs Organization. "About Us." n.d. http://www.c-e-o.org/page/aboutus

The entrepreneur website resource AlphaGamma.com lists many of the largest business plan competitions for recent and student entrepreneurs. Here is a list of the top competitions that took place in 2019. Check its website for listings on future competitions.[34] In most cases, aggregate yearly awards are listed along with other information specific to the competition:

- Harvard Business School New Venture Plan Competition – $300,000
- Rice Business Plan Competition – $1.5 million
- Milken-Penn GSE Education Business Plan Competition – $1,000,000
- Utah Entrepreneur Challenge – $100,000
- Next Founders – $30,000
- Technovation world Challenge – $42,000
- CodeLaunch – $67,000
- Burton D Morgan – $100,000
- Edward L. Kaplan Business Model Competition – $100,000
- UPitch Competition – $10,000
- The Hult Prize Student Competition – $1,000.000
- Thiel Fellowship – $100,000

This list doesn't include some other valuable competitions. The George Washington University business plan competition, called the GW New Venture Competition, in 2017 awarded more than $300,000 worth of cash and in-kind services in all.[35] The Baylor University New Venture Competition is open to colleges across the country and awarded a total of more than $85,000 to student teams from Arkansas, Iowa, and Pennsylvania with finalists coming from California and Illinois as well.[36] Singapore hosts a global business plan competition with prizes totaling $1 million.[37] Smith College's Draper Competition for Collegiate Women Entrepreneurs offers more $60,000 in total prizes, including a top cash award of $10,000 plus a scholarship.[38] Arizona State, Indiana, and many other universities host these contests. Deadlines are staggered year-round. Competitions are sometimes open to nationwide competitors, but some are open to students in only a particular campus community or region. Competitions are not necessarily tied to academic schedules. Research the competitions that are most appropriate for you and your program, and collaborate with a professor to enter, learn, network, and ideally, win funding.

Successful entrepreneurship happens when innovative people find fertile ground, develop ideas and concepts, and persevere through learning to fit new products in appropriate marketplaces. College graduate entrepreneurs owe it to themselves to research the entrepreneurial community they would prefer to target. Economic development offices all over the world encourage entrepreneurs to come to their cities because they need innovative people with energy and a willingness to take risks to come up with the economic engines of the future.

One of the ways regions incentivize entrepreneurship is through contests, which are any means of competing for startup funding that does not involve a pitch competition. If you can build a team for a static contest, you are well on your way to building a team to pitch new innovations.

34 8 Kima Mayes. "12 Best Business Plan Competitions in 2019." *Alpha Gamma.* February 12, 2019. https://www.alphagamma.eu/opportunities/12-best-business-plan-competitions-in-2019/
35 "New Venture Competition." *George Washington University*. n.d. https://newventure.gwu.edu/history-mission
36 "Baylor New Venture Competition." *Baylor University*. n.d. https://www.baylor.edu/business/newventurecompetition/
37 "Lee Kuan Yew Global Business Plan Competition." *Singapore Management University*. n.d. https://www.smu.edu.sg/lky
38 "Draper Competition." *Smith University*. n.d. https://www.smith.edu/academics/conway-center/entrepreneurship/draper-competition

Key Terms

ask specific amount of money or type of assistance requested in a pitch
corporate narrative story about how a successful company grew from something small into something broad and powerful, serving thousands or even millions of people; it may have marketing purposes, and it may serve as an inspirational story for leaders and employees
elevator pitch abbreviated pitch, a memorized talk that can get you into the door to put your full pitch deck on display
entrepreneurial contest any entrepreneurial competition other than a pitch competition; contests may entail submitting business models, long-form prospectuses, or forms tailored to contest specifications
fear of missing out (FOMO) need to keep up with peers and the personas they represent in social settings, particularly on social media
iceberg principle writing principle useful for preparing contest documents and pitch decks; following this principle, each word or sentence in the submission or presentation should be backed up with a wealth of supporting information and details that go unspoken in the pitch or proposal, but which you have at the ready should an investor take interest in the details and your knowledge of them
ideation purposeful process of opening up one's mind to new trains of thought that branch out in many directions from a stated purpose or problem
mission statement statement of an organization's reason for being that defines its primary long-term goal, explains what the venture will do, what value it will provide to the end customer, and how it will accomplish that action
noncompete agreement formal agreement that the person signing the document will not work for another organization that is a direct competitor of their current employer during employment and usually for a specified length of time after employment ends
nondisclosure agreement (NDA) contract that carries harsh financial penalties should one party to the agreement disclose what they know of the proprietary information
pitch formal presentation in which you ask for something and that is delivered (usually) to potential investors in a startup
pitch competition competition that may have cash prizes or mentorship opportunities for winners; you are expected to present your business idea in the form of a presentation, usually with a pitch deck
pitch deck slide presentation that you create that gives a quick overview of your product and what you're asking for
problem-solution narrative brief story of a sentence or two that states a problem affecting many people and offering a solution that is innovative, unique, insightful, or all of these
user interface (UI) what a customer sees when they use your product; having a variant of a UI is not necessarily grounds for establishing a patent, but having unique design in the broader sense may help you to secure patent protection
value proposition summary describing the benefits (value) customers can expect from a particular product or service
work-for-hire agreement agreement between an individual employee and a company states that ownership of innovations belongs to the company, even if an individual makes substantial contributions to the product

Summary

7.1 Clarifying Your Vision, Mission, and Goals

The most basic formula for telling the story of your innovation is the problem-solution narrative. Entrepreneurs are problem solvers, but they need to strategize to battle competitors and to weather the risks inherent in starting a new venture. Vision and mission statements are crucial to planning a venture. Vision statements are broader than mission statements. Entrepreneurs can set attainable goals with the help of the SMART goals framework. All of these tools—vision statements, missions, and SMART goal formulation—help

build on the venture's origin story and serve as a general and specific organizing narrative.

7.2 Sharing Your Entrepreneurial Story

This section outlined the importance of conceptualizing and communicating your venture in narrative form. Not every startup venture is a fairy tale, but if you can recognize and apply trusted story formats, you can help establish prominence for your brand, your products, and their specific features. Eventually, your story might be the genesis of a corporate narrative if the startup grows to become one. There are advantages and disadvantages to crafting stories. The advantages are that stories help you communicate the problem your innovation addresses, the solution it offers, and its market need. The disadvantages are that a story can create the fear of missing out in consumers and can set unattainable, rigid goals that can cause you to miss key factors in the venture's development.

7.3 Developing Pitches for Various Audiences and Goals

A pitch is a request for support, either financial investment or some kind of support. A great pitch takes into account the intended audience and the goal of the talk, and prioritizes information accordingly. In other words, it answers the questions Who? (Who are we pitching?), What? (What are we pitching to them?), and Why? (Why are we pitching: What is the "ask"?). Once you establish these elements, you need to develop a professional pitch deck and include engaging materials that share your passion and communicate your vision. Your pitch should paint a picture of a successful product or service delivering strong returns for investors or for those who choose to work for you or do business with you.

This section offered an outline of elements for a professional pitch deck and provided a few details about what ought to be included. Pitches may vary in length and should take into consideration the demands of contest rules and the quirks of potential investors. That said, there are elements that almost every pitch needs to include, and they are presented in the approximate order in which they might appear in your pitch deck. In general, you should cover all elements of the pitch as outlined here, but the level of detail may vary based on the audience. The entrepreneur should ask the key contact what specific area(s) she should cover so as to make the best impact.

We also discussed crafting different pitches with different senses of vision in mind, which can be particularly helpful post-pivot when an organization has a product but needs to adjust it to target new markets. Finally, we looked at the elevator pitch, which is miniature version of your more complete professional pitch and an introduction to your vision. The pitch before the pitch, if you will, should be clear, concise, and catchy—enough to get an investor's attention without driving them to hop off the elevator.

7.4 Protecting Your Idea and Polishing the Pitch through Feedback

Protecting your intellectual property is something you must plan for as an entrepreneur. In crowded marketplaces, small innovations or variations on a theme might be difficult to patent, and the process takes time; thus, not every product or iteration needs to be patented. Investors are often more interested in the potential of a leader and team than the potential of an idea. With that in mind, the protection of an idea shouldn't supersede building a great team or pitching your idea widely enough to tap into appropriate funding channels.

A patent can protect your intellectual property. Other protections are nondisclosure agreements, work-for-hires, and noncompete agreements. If someone breaks a contract, your only recourse is through legal channels. It is better to conduct thorough research to be as confident in your team as possible before you share your ideas, designs, and prototypes with those who will be helping you make your innovation a reality.

Entrepreneurial learning comes from seeking feedback on your ideas from potential customers and investors. Feedback on your pitch itself can help you refine how you present those ideas.

7.5 Reality Check: Contests and Competitions

Pitch competitions may be global, national, or regional in scale. There is no single model for a pitch competition, but teams can prepare based on the terms that organizers set forth, and they can anticipate the need to demonstrate key core elements including value proposition, marketplace and competition, funding strategy, brand, and team. Winners of pitch competitions would do well to examine any contracts they must sign before accepting cash awards or investments; some deals are structured unfavorably for the entrepreneur.

If you lose a pitch competition or contest but enhance your network of contributors and collaborators and/or find a mentor, it has been a successful early effort. Consider developing your collaborator network while still in school using social media tools and entering into college competitions, some of which are listed in this chapter.

Review Questions

1. _____ is like the origin story for a brand.
   A. problem-solution narrative
   B. purpose
   C. mission statement
   D. vision statement

2. Identify the correct terms used in this text for setting SMART goals.
   1. specific, measurable, attainable, relevant, time-bound
   2. specific, marketable, attainable, relevant, time-bound
   3. specific, measurable, achievable, relevant, timely
   4. specific, measurable, attractive, relevant, time-bound

3. What is defined as the thing your organization does that people will pay for or contribute to?
   A. earnings statement
   B. profit proposition
   C. value for revenue proposal
   D. value proposition

4. When an entrepreneur's story becomes part of the mythology of a corporation and its purpose, this is known as a/an _____.
   A. mission statement
   B. vision statement
   C. purpose statement
   D. corporate narrative

5. When someone supports your products and your brand so much that they begin speaking on your behalf in person and on social media, they are known as a/an _____.
   A. brand advocate
   B. corporate narrative sponsor
   C. impetus
   D. entrepreneurial drive

6. In previous decades, a term for a related phenomenon was "Keeping up with the Joneses." This refers to a sense that if we are not living our best life, having the most fun, enjoying the best foods, fashion, and so on, then we are not living the life we should. This term can refer to both a short-term concern and a general anxiety that others are enjoying life more than we are.

A. brand advocacy awareness
B. FOMO, or fear of missing out
C. "Jonesing"
D. happy ever anxiety

7. Pitches have different purposes, depending on the target audience. The constant in every pitch is that it _____.
A. must be short
B. makes a request for support
C. includes six elements and about ten slides
D. is derived from a corporate narrative

8. An abbreviated pitch that you memorize is called an elevator pitch. Meant to be given in person, it should be _____.
A. brief
B. memorized
C. connected to a request for more time to make a more complete pitch
D. All of these options are correct.

9. A graphic worksheet that sets forth the value proposition of any startup and allows you to identify stakeholders, and key inputs and outputs is the _____.
A. business model generator
B. business model canvas
C. business mobility canvas
D. business meditation and creativity matrix

10. An agreement between an individual employee and a company that states that innovations belong to the company, even if an individual makes substantial contributions.
A. nondisclosure agreement
B. work-for-hire agreement
C. noncompete clause
D. patent

11. A _____ is a license granting exclusivity, as in the exclusive rights to manufacture and sell a specific product.
A. patent
B. UI
C. nondisclosure agreement
D. noncompete clause

12. Numerical measurements providing data on how people use a product or service results in _____ data.
A. qualitative
B. quantitative
C. lean
D. build-measure-learn

13. More complex data indicating *why* and *how* people use or might use a product or innovation is known as _____ data.
A. qualitative
B. quantitative

C. lean
D. build-measure-learn

14. The _____ is the specific request for funding, mentorship, collaborators, and/or business partners that appears in a pitch.
A. ask
B. request
C. pitch
D. contest

15. The student entrepreneurship organization highlighted in this chapter is _____.
A. CEO
B. CFO
C. Future Entrepreneurs of America
D. Pitch Competitors International

Discussion Questions

1. After a search, give examples of companies with clear vision but poorly defined mission statements.

2. What are the pitfalls in crafting a vision statement that is too broad or too narrow?

3. Place the SMART goals in order of importance and discuss why you chose that order.

4. How can telling your entrepreneurial story help build a brand?

5. What is the risk of falling in love with your own entrepreneurial story?

6. What would it take to rework a pitch deck created for a campus competition and present it to an individual angel investor?

7. In what ways is an elevator pitch an abbreviation of a longer professional pitch? In what ways does it differ?

8. Reflect on the Airbnb pitch deck. What would the elevator pitch version of that presentation sound like? What would the ask be for the new elevator pitch?

9. At what stage of product development for a manufactured good should you file for patent protection?

10. Are noncompete clauses fair in entrepreneurial work? Why so? Are noncompete clauses always fair for employees? Why or why not?

11. Research the average time it takes to win a patent in an industry you are interested in. What are some factors that contribute to delays in patent seeking?

12. It is common to develop a product based on limited feedback using as few resources as possible only to watch as no one uses or buys the product. Can failure be a valuable part of finding product-market fit? Why or why not?

13. This section advocates using qualitative and quantitative data to develop products and find the right market for them. When might it be appropriate to rely heavily or solely on quantitative data? Can you think of a product that had very high usage rates that was incredibly popular but that almost as quickly fell out of favor? Which is better at predicting a fad: qualitative data or quantitative data?

14. Imagine entering your campus pitch competition. What is your strategy to win?

15. If your campus does not have a competition, what national competition might you enter? What is your

strategy to win? Do some research online to find what has put past winners ahead.

Case Questions

1. The John Deere Company has one of the most enduring corporate narratives in the world. John Deere was a real person who developed an early, successful steel plow that in some ways contributed to the agricultural revolution the world over. Research and re-tell the John Deere story. What drove John Deere's success? How does the corporation foster brand advocacy today through its media presence and publications? Some would argue that the John Deere Company has achieved the entrepreneur's vision. Is it possible for a company to truly live up to its vision statement? Does that describe what John Deere the company did for John Deere the person, or is that an overstatement?

2. Princeton University professor, president, and CEO of New America, a think tank dedicated to "renewing America in the Digital Age," Anne-Marie Slaughter wrote an article for *The Atlantic* in 2012 called "Why women still can't have it all."[39] Slaughter starkly and personally lays out the challenges of maintaining the elusive work-life balance. She advocates for taking a long-term view in one's life and balancing the needs of family with career aspirations. Can a successful entrepreneur have it all? What do entrepreneurs' stories and corporate narratives suggest? What do you think of the serial entrepreneur who builds a company to sell it and then takes time between ventures to spend time with family and friends? Is this version of the entrepreneurs' story rare? If you find it to be rare, do you think this might be because it rarely happens or because it doesn't fit social expectations of workaholic success stories?

3. Design plays a major role in how investors and other audiences respond to your pitch deck, but for one startup, achieving near perfection in their slide design did not create a pathway to success. Wattage Inc. was pitched as a modular electronics company that would allow users to design their own electronic equipment from modular parts, add art and other customized pieces, and have it shipped directly to them. To take a massive market—consumer electronics—and add a customization element was incredibly ambitious. The deck made for an aesthetically pleasing failure.[40] Potential investors would not open their checkbooks, but would smile and suggest that these guys could always go into business making pitch decks for other startups.[41] The innovation that promised to make us all inventors failed, at least for now, but it can teach us many lessons about developing pitches. View Wattage's pitch deck (https://openstax.org/l/52WattPitchDeck) to learn more.
   A. Can great design *hurt* a pitch presentation? How, or if no, why not?
   B. What do you think was missing if investors loved the pitch deck, appreciated the tactile prototypes, and yet decided not to invest?
   C. There is a "go-big-or-go-home" sentiment to this kind of startup that tries to shake up a massive marketplace. After visiting these links and reviewing what Wattage Inc. was trying to build, could you come up with a scaled-down or more focused version of the concept that might work? One issue with this type of startup is that it can only target very large investors. How might you build different pitch decks targeting different types of investors (electronics investors, those who invest in value-added customization products, modular tech enthusiasts, and so on)?

4. Zappos is sometimes cited as an example of the leanest of lean startups conducting the build-measure-learn process successfully.[42] The company started with no inventory and instead started taking orders to ship shoes to customers who ordered online. They let the market pull the inventory needs out of their startup rather than buying a store of shoes and hoping to sell them all. Their inventory was their local shoe stores. They started out buying their inventory at retail price and then marking up a surcharge for the service of seeking, sorting, and shipping.

39 Anne-Marie Slaughter. "Why Women Still Can't Have It All." *The Atlantic.* July/August 2012. https://www.theatlantic.com/magazine/archive/2012/07/why-women-still-cant-have-it-all/309020/
40 Jeremy Bell. "Well, We Failed." *Medium.* May 5, 2017. https://medium.com/inside-wattage/well-we-failed-77e795e16ecf
41 Taylor Lorenz. "Everybody Kept Telling This Startup That Its Pitch Deck Was Beautiful—But They Didn't Invest." *Business Insider.* May 12, 2015. http://www.businessinsider.com/wattage-pitch-deck-couldnt-save-startup-from-failure-2015-5

There may not be many pairs of shoes worth more than retail price, but people were willing to pay for convenience, and Zappos could measure popular sizes, brands, and trends in ways that would help them anticipate inventory needs as they grew.

A. In what ways is the Zappos lean startup story about feedback?
B. Ideate a potential startup, besides a food delivery service, built around efficiently or conveniently packing and shipping something others have already made.
C. Ideate a potential startup where you could conceivably earn revenues even when buying your inventory at retail price. What makes you think some online customers would pay a premium? What kind of business learning would you have to do to improve on the Zappos lean startup model?
D. As soon as a retailer or other service provider notices that a startup is making a profit adding convenience to their existing business infrastructure, what is to keep them from entering the marketplace? Are there any protections for the service you propose? How might you protect such a business?

5. Entrepreneur.com is cited or referenced several times in this chapter, but even contributors to this publication, which relies on serving a culture of entrepreneurs as part of its value proposition, sometimes question its own community's trends. Their article, "We've Become So Obsessed with 'Innovation' That It's Now Meaningless" challenges a perceived overuse of the term "innovation." Read the article here: https://www.entrepreneur.com/article/249408.
Look for news of college pitch competition winners. Are they all truly innovations? Find a college pitch competition, business model competition, or elevator pitch competition winner who truly *is* innovative, and find ones, perhaps, who are variations of Uber—delivering stuff and charging a premium for convenience and little more.

A. Do you agree with the guest commentary published in Entrepreneur.com? If so, why? If not, why not?
B. What can you do in your work as an entrepreneur to develop value propositions that go beyond what can be dreamt up in a classroom?
C. What can you read and do to come up with truly fresh ideas? What places can you visit? What networks and mentors can you tap?
D. How can you as an individual move past an "innovation" obsession to solve people's problems.
E. Can you be more than another college innovator? Can you be a superhero entrepreneur?

Suggested Resources

7.1 Clarifying Your Vision, Mission, and Goals

This publication offers a thematic analysis of how mission statements are used in higher education: https://muse.jhu.edu/article/196947

This video provides a walkthrough for crafting your mission statement: https://www.entrepreneur.com/article/65230

7.2 Sharing Your Entrepreneurial Story

Using empathy in storybuilding: https://www.inc.com/craig-bloem/all-strong-startup-brands-have-a-great-story-heres-how-to-tell-yours.html

Harvard Business Review's how to craft a corporate narrative: https://hbr.org/2016/03/how-to-build-a-strategic-narrative

7.3 Developing Pitches for Various Audiences and Goals

Pitch deck templates: https://articles.bplans.com/what-to-include-in-your-pitch-deck/ and

42 Anastasia. "How the Build-Measure-Learn Cycle Really Works." *Cleverism*. July 26, 2015. https://www.cleverism.com/how-build-measure-learn-cycle-really-works/

https://www.forbes.com/sites/allbusiness/2017/03/04/how-to-create-a-great-investor-pitch-deck-for-startups-seeking-financing/#4bbce7c2003e and https://www.startupgrind.com/blog/the-quick-and-dirty-guide-to-creating-a-winning-pitch-deck/

7.4 Protecting Your Idea and Polishing the Pitch through Feedback

Patent pitfalls to avoid:

http://www.ipwatchdog.com/2016/01/23/patent-drafting-learning-from-common-patent-application-mistakes/id=65243/

Giving and receiving better: https://www.entrepreneur.com/article/219437

NDA templates: https://www.rocketlawyer.com/

7.5 Reality Check: Contests and Competitions

The International Business Model Competition that focuses on Lean Startup models, sponsored by BYU and Harvard: http://www.businessmodelcompetition.com/

8

Entrepreneurial Marketing and Sales

Figure 8.1 Birchbox founders Katia Beauchamp and Hayley Barna have disrupted the beauty and fashion retail industries with their monthly cosmetics sample boxes. (credit: modification of "487908877AP00050_TechCrunch" by TechCrunch/Flickr, CC BY 2.0)

Chapter Outline

8.1 Entrepreneurial Marketing and the Marketing Mix
8.2 Market Research, Market Opportunity Recognition, and Target Market
8.3 Marketing Techniques and Tools for Entrepreneurs
8.4 Entrepreneurial Branding
8.5 Marketing Strategy and the Marketing Plan
8.6 Sales and Customer Service

Introduction

Birchbox founders Katia Beauchamp and Hayley Barna loved shopping for beauty products but found the experience expensive and frustrating. So many brands making so many claims—how could anyone find the best beauty buys without wasting money on products they might not need? There had to be an efficient and cost-effective solution to this problem.

Their solution was to start Birchbox: an easy and affordable way to shop online for the best and newest beauty products by trying out samples first. Their entrepreneurial concept requires customers to share lifestyle and grooming preferences with Birchbox via an online form. The company then sends a personalized box of beauty product samples from brand partners along with information about each product. If customers like the offerings, they can purchase the full-size merchandise from big cosmetic manufacturers through Birchbox with a few clicks. Birchbox was a success from the start. Beauchamp and Barna were able to create relationships with cosmetic brands, fund their website, and hire the necessary workforce. However, they did not turn a profit until a few years later.

While Birchbox was initially an innovator and disruptor within the cosmetics and beauty supply market by supplying products in a new and different way, competition increased as retailers like Macy's, Target, and Walmart started to offer similar services to customers worldwide. Birchbox was valued at $485 million in 2014, but stiff competition plus the high costs of operations and customer acquisition pressured the new company. In 2016, Birchbox aggressively cut costs in marketing, logistics, production, and staffing, and invested in mobile platforms that allowed the company to secure their competitive advantage, resulting in the company turning a profit for the first time in 2017.[1] Birchbox has continued to expand its business, thanks to the founders' ability to distinguish their brand from competitors by collecting customer information to customize experiences and by providing the experience through platforms that reach a vast number of customers online.

8.1 Entrepreneurial Marketing and the Marketing Mix

Learning Objectives

By the end of this section, you will be able to:

- Distinguish between traditional marketing and entrepreneurial marketing
- Describe the seven elements of the marketing mix

Being a successful entrepreneur often means being able to balance the many different aspects of a business, such as financing, accounting, and management. One of the most important of those aspects is marketing. After all, if no one hears about the new product, how can it be successful? According to marketing research company CB Insights, in a survey of 101 companies that failed, 14 percent of them failed due to poor marketing.[2] **Marketing** is an umbrella term given to those activities that companies use to identify consumers and convert them into buyers for the purposes of achieving a profit. No matter the size of the enterprise, marketing lays the foundation for how a company reaches and serves its target customers. Whether it's a global brand such as PepsiCo or Apple, a small- to mid-size company such as Birchbox, or a small restaurant or local gym, marketing refers to the core strategies companies use to reach and sell to customers. As you might expect, the way entrepreneurs market their new product is somewhat different from how a large company markets an established brand.

Traditional Marketing

Traditional marketing for large businesses such as Coca-Cola, Disney, and Dell tends to focus on managing and growing existing programs and brands. Companies like these enjoy greater resources such as substantial financial support and large numbers of marketing professionals to steer their efforts. However, marketing for small- and medium-sized businesses (those with 500 or fewer employees and less than $7.5 million of yearly receipts, as defined by the Small Business Administration)[3] is different because financial resources are limited, and it is often the entrepreneur alone who is in charge of marketing efforts. If they do have funds for marketing expenses, they might use a small agency on a fee-for-project basis.

As you have learned in previous chapters, small start-ups are usually tight on resources, so they need to augment their resources through creativity and hard work. While having limited resources creates obvious challenges, being small also has its advantages. For example, it allows new companies to be more flexible, agile, and creative than their established competition. These qualities can allow new companies to disrupt their industries and become major global players by employing entrepreneurial marketing practices.

Entrepreneurial Marketing

On a basic level, **entrepreneurial marketing** is a set of unconventional practices that can help start-ups and

1 Clare O'Connor. "Pioneering Beauty Startup Birchbox Turns Profit after Tough 2016." *Forbes*. April 12, 2017. https://www.forbes.com/sites/clareoconnor/2017/04/12/pioneering-beauty-startup-birchbox-turns-profit-after-tough-2016/#1223b3c46fd5

2 Erin Griffith. "Why Startups Fail, According to Their Founders." *Fortune*. September 25, 2014. http://fortune.com/2014/09/25/why-startups-fail-according-to-their-founders/

3 "Meet Size Standards." Basic Requirements. U.S. Small Business Administration. n.d. https://www.sba.gov/federal-contracting/contracting-guide/basic-requirements#section-header-6

younger firms emerge and have an edge in competitive markets. The main difference between these and traditional approaches is that entrepreneurial marketing tends to focus on satisfying the customer and building trust by providing innovative products and services that disrupt or appeal to a specific market. Table 8.1 provides an overview of differences between traditional and entrepreneurial marketing.

Traditional versus Entrepreneurial Marketing

Traditional Marketing	Entrepreneurial Marketing
Greater amount of resources	Few to no resources; founder drives efforts (sweat equity)
Management of an established brand, reminder advertising	Must be ingenious, energetic, and persistent to develop story and brand; leads to trust
Financial and market share goals	Satisfaction and awareness goals
Manage existing customers	Capture first customers; develop a client base and long-term relationships
Manage existing products, promotion, pricing, placement, people, physical environment, and process (the "7 Ps")	Develop new products, price points, channels (placement), communication, process, training, and design
Continue doing what works	Trial and error; market pilots
Communication with customers standardized, one-directional; more difficult to create one-on-one relationships	Communication with customers is more fluid and spontaneous; two-way relationships

Table 8.1

As the table shows, entrepreneurial marketing emphasizes flexibility and innovation as a way to stake a claim within competitive markets. For example, consider how Drybar founder Alli Webb used her understanding of market needs to create a niche within the traditional hairstyling industry. A hairstylist by trade, Webb spent five years as a stay-at-home parent, drying hair for friends and family members at their homes to make extra cash. During this time, she realized there was a market need for "just" blowouts, or professional hair drying and styling.

Seeing this need, Webb developed a business model that would offer women a way to get a blowout without having to also get a cut or color. Webb didn't invent the blowout; she just reinvented the space to do it, focusing on that sole aspect of hair styling, and offering the service in trendy settings (Figure 8.2). By being flexible and innovative through a new space to provide this service, Drybar was able to carve a niche in the hairstyle industry. In business since 2008, Drybar is still expanding. Webb expected to open at least 20 new locations in 2019.[4]

4 Diana Blass. "Drybar's Rise to Success with NetSuite Has a Hidden Message for Partners." *CRN*. October 4, 2019. https://www.crn.com/news/cloud/video/drybar-s-rise-to-success-with-netsuite-has-a-hidden-message-for-partners

Figure 8.2 Simple innovative ideas such as Drybar can carve new market niches that weren't served before. Drybar has now grown to over 100 locations across the US.[5] (credit: work by ralph and jenny/Flickr, CC BY 2.0)

Marketing Mix

One of the biggest misconceptions people have about marketing is that it is all about promotion, or how a company sells or advertises something. But the truth is, promotion is just one facet of the **marketing mix**, which describes the basic set of strategies and approaches that marketers use to identify and reach their target market. A **target market** is the specific group of consumers for which a company seeks to provide a good or service.

One common way of understanding and remembering the components of the marketing mix for products and services is by thinking in terms of the "7 Ps." While each of these can be part of a company's marketing mix, the first four relate more to products: product, pricing, promotion, and place (and traditionally have been called "the 4 Ps of marketing"). The remaining three relate more to services: physical environment, process, and people. While the 7 Ps are conceptually the same for all businesses, how a company addresses each "P" will be specific to that company's needs and goals.

For a better understanding of the marketing mix, look at how Figure 8.3 breaks down the 7 Ps into their related activities.

5 DryBar. "About Us." n.d. https://www.thedrybar.com/about-us/

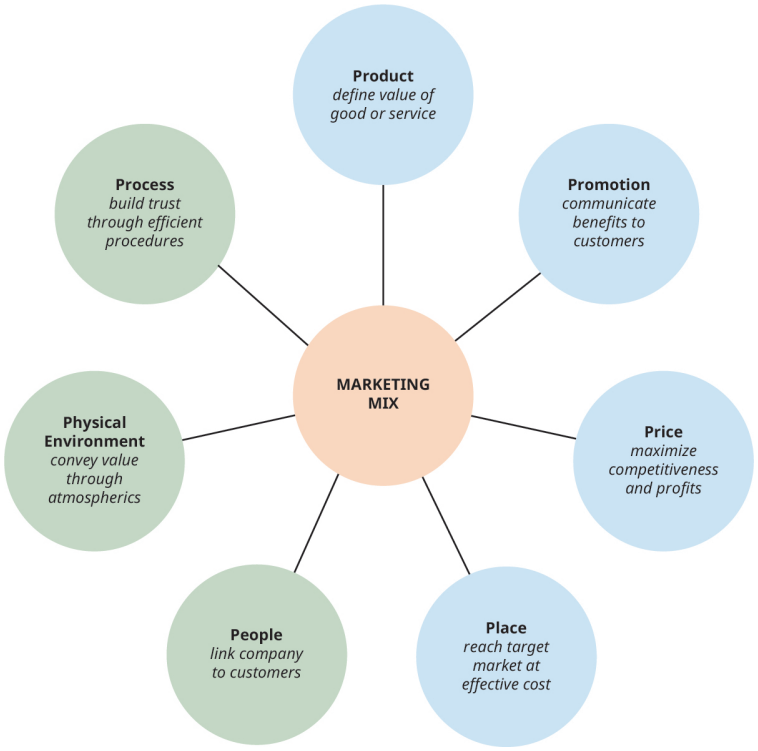


Figure 8.3 Each P of the marketing mix should work with the other Ps to create value for a business and its customers. *Product*, *promotion*, *price*, and *place* relate more to goods, while the *people*, *physical environment*, and *process* relate more to services. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Product

Within the marketing mix, **product** refers to a good or service that creates value by fulfilling a customer need or desire. Goods are tangible products that can be touched, smelled, heard, and seen, such as a pair of tennis shoes, a granola bar, or a bottle of shampoo. In contrast, services are intangible products. They usually entail paying an expert to do something for you, such as car repair or house cleaning.

Companies can bundle both goods and services together to create extra value for their customers. Birchbox, for example, provides goods (product samples) and services (customized product recommendations) to satisfy their customers' desire to be able to buy beauty products in a hassle-free manner. The value Birchbox provides to customers relies on their ability to do both. In the United States, service-oriented businesses are increasingly playing a larger role in our local and national economies.

For start-ups, defining the value of the products they are going to offer is an important step toward identifying their competitive advantage within a marketplace. On a basic level, if you don't know what benefit your product provides or what need it fulfills, neither will your customers. Kevin Plank, founder of Under Armour, knew that the value of his product would benefit many athletes who were tired of having to frequently change their wet sportswear. As a former football player, he had spent many hours training and enduring drenched practices, and wondered how he could alleviate this problem that companies didn't address well with cotton sportswear. After college, he decided to take his idea to the next level and started a company making athletic wear that had special microfibers that kept athletes dry throughout practice and games. He then embarked on a trip to try to sell his value proposition to college football teams on the east coast. Nearing the end of 1996, he landed his first sale of shirts to Georgia Tech, which totaled $17,000—and the rest is history. Under Armour became a strong competitor to Nike and Adidas by providing a new type of athletic wear that has revolutionized performance by keeping athletes dry.[6]

6 Under Armour. "Our Story." n.d. http://www.uabiz.com/company/history

In contrast, Jawbone, the company that manufactured Bluetooth speakers and other hardware, has gone out of business because it changed its focus from audio to health devices, which placed it directly in competition with FitBit and similar hardware companies. Product failures, among other problems, caused this tech company to flop.[7] The company is now working on reinventing itself and will use artificial intelligence and sensor hardware to provide customers information about their health through a subscription. The wearable sensors will record vital customer information that will be tracked on an online platform that will then provide suggestions for medical action.[8] The company's redesign is not yet complete, so it is not officially in business again yet.

Promotion

Communicating a product's benefits to customers is a significant aspect of any marketing mix. Even if a product is the best in its class, a company must communicate this value to customers, or it will fail. This is what **promotion** does: It is the process of communicating value to customers in a way that encourages them to purchase the good or service. Promotions must have a goal, a budget, a strategy, and an outcome to measure. Companies must use their promotional budget wisely to create the best results, which can include sales, profit, and awareness through the use of a cohesive message throughout the campaign.

Some typical forms of promotion are advertising, social media, public relations, direct mail, sales promotions, and personal selling.

Advertising is a form of mass communication that allows companies to reach a broad audience through TV, radio, newspaper, Internet, magazines, and outdoor ads. Many of these media can be quite expensive for small companies, forcing them to choose one strategy, or to opt for other less expensive tactics such as guerrilla marketing or viral marketing (which will addressed in Marketing Techniques and Tools for Entrepreneurs). As Table 8.2 shows, the advantages of advertising include reaching a mass audience and increasing sales, but on the downside, the cost may be too much to bear, and the company might face a difficult time reaching the right target. As we move from advertising to social media, we can see that social media allows for more accurate targeting and better metrics to assess results.

Social media is a must-use tool for entrepreneurs to connect with consumers, especially younger demographics. Many customers can be found online in one social media platform or another. The goal is to find the customers who fit your target market. The benefits of social media include targeting customers more accurately using the platform of their choice and being able to communicate directly with them. These platforms include networking sites such as Facebook, Twitter, and LinkedIn; photo and video sites such as Snapchat, Instagram, and Pinterest; blogs; and news sites. A business must find the time to connect with its customers wherever they are. As a budding entrepreneur, the best way you can start connecting with them is by identifying your target customers and by figuring out what kind of social media they frequent. You can ask your current customers about their social media habits; you can look up reports about the types of social media your customers frequent; or you can use special software that tracks conversations on social media that pertain to your business and industry.

For example, you may find out that your young customers hang out mostly on Twitter and Instagram, and not so much on Facebook. You could benefit from focusing on only those two platforms and finding out about their conversations. You may want to search hashtags and stories that pertain to your type of business so you can join their conversation. You could then set up your profile, write relevant content and hashtags that make sense to your consumer, and request to follow influencers who can help you create awareness of your business and product. Once you have a profile set up, there are many ways you can create campaigns: contests, discounts, or by simply providing useful content that your customer appreciates. The goal is to be

7 Lauren Goode and Chris Welch. "Jawbone Is Going Out of Business." *The Verge*. July 6, 2017. https://www.theverge.com/2017/7/6/15931080/jawbone-going-out-of-business-report
8 Conor Allison. "Jawbone Health: Everything We Know So Far about the New Premium Health Platform." June 17, 2019. https:www.wareable.com/health-and-wellbeing/jawbone-health-hub-medical-health-wearable-2144

part of the conversation and not sound like you are selling something.

In addition to posting good content and reaching out to influencers, you may also benefit from buying ads that can be geographically targeted to your customer and that are more affordable and effective because you're directly targeting someone who is specifically interested in your product. The disadvantages of targeting social media include the time and skills required to engage with customers, and the need for consistently fresh content. Many start-ups believe that having a Facebook page will be enough to reach their customers, but their customers may spend more time on other social media platforms. The time and effort required to find the right platform, develop good content, and connect with customers on a daily basis is worth it.

Public relations are the efforts and tools companies use to connect and develop goodwill with their constituents. Constituents can include customers, investors, employees, business partners, government entities, and the community at large. The goal is to highlight the company in a positive light by contributing as a community player. Tools can include newsletters, press conferences, community service, events, sponsorships, press releases, articles, and stories that help entrepreneurs create a positive image about their company and get its name out there. If participating in an event, for example, the sponsor will display the logo and name of the company in a place where everyone can see it. This shows the company as a supporter of the community and as a provider of not just products and services, but of intangible contributions, such as supporting the dreams of the event participants. The goal is not to make a sale at that point, but to impact the community and create positive relationships in general because it's the right thing to do—it may positively influence the consumer when they make a purchase in the future.

Direct mail, which is a way to connect to consumers via email or through printed, mailed pieces, is also a necessary tool to keep in touch with customers, especially when creating long-term relationships. The advantage of this strategy lies in connecting to a customer who is already interested in your product and would like to receive news and promotions from you; however, the disadvantage is that it usually takes time to create these lists because it involves collecting information about customers during events, through online requests, or at the cash register. It also can be expensive to send out pieces of mail that might end up in the trash.

Sales promotions are incentives that attract attention and push the customer to take action. These incentives include discounts, samples, rebates, rewards programs, gifts, and premiums. Sales promotions can attract new customers, but it may also reduce profits because coupons and discounts are offered for trying a product.

Personal selling is a tool that uses face-to-face interactions to communicate and influence a customer to make a purchase. It is especially suited for luxury goods. Usually, higher-priced products will need a longer selling process, and sales personnel will need more training on the product to learn about its unique qualities. This is one of the most expensive ways to reach and retain customers, but it can be worth the investment.

Overall, a good entrepreneur must find the right mix of marketing communications to reach customers. This will vary depending on the start-up's budget, goals, and strategies. Table 8.2 identifies the advantages and disadvantages of each, as they relate to small and new businesses.

Advantages and Disadvantages of Promotion Types

Table 8.2

Promotion Type	Examples	Advantages	Disadvantages
Advertising	• TV ads • Radio spots • Newspaper and magazine spreads • Internet ads • Billboards	• Can reach a mass audience • Great for creating brand recognition • Increased sales	• Can be expensive • Access can be limited • Some targeting is possible, but it is impossible to fully control who sees the ad
Public Relations	• Sponsoring community events • Charitable and civic involvement • Scholarships and grants • Press conferences	• Develops positive brand recognition • Creates goodwill toward company and brand within the community	• Big events and public relations campaigns can be resource intensive • Not focused on generating sales
Social Media	• Social networking sites such as SnapChat, Twitter, and Facebook • Blogs and vlogs • Influencers (industry experts who act as advocates)	• Pervasive and inexpensive access to massive audiences • Target markets are highly customizable based on available data • Easy access to young people • Can be used to create goodwill and a loyal fan base	• Many companies use social media, so it is hard to stand out from the crowd • Can be time-consuming • Success requires dedicated personnel with special expertise • It is often difficult to track conversion (customers taking a desired action, such as a purchase) and sales numbers • Requires the creation of unique/engaging content

Table 8.2

Promotion Type	Examples	Advantages	Disadvantages
Direct Mail	• Mailed letters, marketing flyers, postcards, and coupons • Email newsletters	• Subscribers are already interested in your product and thus more likely to convert to paying customers • Keeps already interested consumers up-to-date on product news, sales, product releases • Can target market based on location, average income, and other census-derived information	• Building an email list of interested customers can take time • Direct mail campaigns can be expensive • Results cannot be precisely tracked • Consumers often discard physical and digital "junk mail" without looking at it
Sales Promotions	• Sales • Limited-time offers • Coupons • Free samples • Rewards programs	• Incentivizes buying and encourages consumers to take action • Appeals to consumers' desire to "get a deal" • A good way to attract new and reluctant buyers	• Reduces profits in exchange for promotion • The promise of future sales and discounts can discourage regular buying
Personal Selling	• Sales meetings between a salesperson and a potential customer	• Personalizes the relationship between the business and the customer • Effective salespeople can convert reluctant parties into paying customers • Salespeople can customize purchase options for each buyer	• Can be resource intensive • Requires salespeople who are well-trained and effective • Consumers are turned off by sales tactics they perceive as aggressive • Requires constant lead generation

Table 8.2

Price

One of the most important and challenging elements of the marketing mix is pricing. **Price** is the value that must be exchanged for a customer to receive a product or service. This is usually monetary and has a direct impact on sales. Many entrepreneurs are intimidated by financials and the prospect of using statements and other information to make projections (you will learn about these in Entrepreneurial Finance and Accounting). Correctly pricing your product enables your company to be competitive while maximizing your product's profit potential.

Here are several methods that entrepreneurs can use to effectively price products:

Cost-led pricing is the easiest way to price a product. This involves taking the cost of making the product and

creating a **profit margin**, which is how much profit your business stands to make after costs have been deducted. For example, if you add the direct costs for materials and labor to the indirect costs of salaries, marketing, rent, and utilities, you determine that your product costs $5 to make. Adding, say, a 30 percent profit margin would give you a sales price of $6.50. The percentage added depends on the business's goals. This type of pricing is helpful when start-ups do not have much information about their target market and need more time to define their value proposition and business identity.

Another way to price a product or service is to consider what the competition is charging and determine whether to go above, below, or match their prices. If going above, or using **premium pricing** (also called perceived value pricing), you need a clear reason why customers would want to spend more on your product. While using **penetration pricing**, or pricing below competitors, can give you a competitive advantage, it may also lead to "price wars" in which competitors keep dropping prices in an attempt to beat each other. Obviously, the disadvantage is diminished profits for all. While pricing the same as your competitors seems like a logical choice, if your product offers no added value, this strategy is unlikely to entice customers to switch to your brand.

LINK TO LEARNING

Warby Parker is an example of a company that prices its eyeglasses below competition prices. Dave Gilboa and Neil Blumenthal started the online company in 2008 with the intention of providing attractive and trendy $95 eyeglasses for everyone. This was a departure from competition, which usually priced eyeglasses at hundreds of dollars. Listen to the interview with Warby Parker founders Dave Gilboa and Neil Blumenthal (https://openstax.org/l/52WarbyParker) to learn more about their venture and its pricing strategy.

Customer-led pricing is just as described: pricing led by the customer. You ask what the consumer is willing to pay and charge that. You can find this by doing research and asking customers what they would be willing to pay for a product. Many technology products are priced that way. Companies survey customers about what they are willing to pay, and they create products that deliver the value at the market price.

Loss leader pricing uses a below-standard price to attract business in the hope that customers will stay and shop for other, more profitable products. It is called a loss leader because companies lose money on the lower-priced product. Grocery store ads usually contain several loss leaders that are designed to lure you into their store in the hopes that you do the rest of your food shopping there.

Introductory offers use lower initial prices to attract new customers and build a customer base before prices return to "normal." This method is a form of penetration pricing, as its goal is to help new products penetrate markets with established competitors and brands. Many subscription-based products such as gyms are introduced this way to gain market share and revenue.

In contrast, **skimming** is a pricing strategy that leverages the newness of a product to justify the highest price possible in order to "skim" the most profits off the top, meaning in the first phase of sales. As time passes, the price is lowered to accommodate for more price-sensitive customers. Apple often introduces its products with this particular method, charging the highest price for them until it has exhausted the market willing to buy at that price and when newer and more technologically advanced products are introduced. Then, Apple slowly lowers its pricing.

In **bundling**, a discount price is set for a bundle of products to encourage customers to buy in bulk. While they pay more than if they were buying just one good or service, they do so because the overall price for a bundle reduces the individual price of that product, giving them a better deal than if they were to purchase items separately. An example of this strategy is used by DirectTV, which bundles its phone, Internet, and satellite services for a monthly fee. If a customer were to purchase these services separately, they would be more

expensive. The benefits of bundling include gaining more revenue per customer, as they would not have paid for some services separately, and making the order-taking task simpler. Take fast-food chains, for example. Instead of asking the customer to list everything separately from the menu, they give you the name or number of the bundle. They make more profit by including the drink and sides to the main entrée, and the customer saves money and time ordering.

The **odd numbers strategy** is a psychological pricing strategy often used in conjunction with other pricing methods to make a product's price point more attractive to consumers. Using odd numbers takes advantage of the idea that such numbers have a positive psychological effect on customers. For example, instead of pricing something at $20, the price would be set at $19.99, which consumers perceive as closer to 19 than 20.

LINK TO LEARNING

Explore the five strategies of psychological pricing (https://openstax.org/l/52PsycPrice) in an article published in *Entrepreneur* magazine.

While pricing must be established when starting a new business, pricing strategies should be reviewed on an ongoing basis. These occasions in particular merit consideration:

- When adding a new product or service to your offerings
- When demand shifts (due to market, consumer, or other factors)
- When entering a new market
- When competitors are making changes
- When your costs are changing
- When adjusting products/services or strategies

Place

Place refers to the channels or locations—physical or digital—where customers can purchase your products; it is sometimes called *distribution*. For the entrepreneur, the choice of place lies in figuring out which channels will create the most profit. In other words, which channels will reach the majority of the target market at the most efficient cost. Choosing the right distribution channels is one way to create a competitive advantage and generate more success for your business. Certain channels have specific capabilities such as reaching more customers, providing promotions, and providing credit.

As Figure 8.4 shows, distribution channels fall into two main groups: direct and indirect. Direct channels, such as physical or online storefronts, require no intermediaries and allow you to sell directly to consumers. For example, if you own a bakery, you would likely have a retail storefront that sells directly to consumers.

Indirect channels require intermediaries such as distributors or sales agents to sell your products to the end customer or to other physical or online retail outlets. Indirect channels often have more than one intermediary. For example, to acquire more customers than you could reach on your own, your bakery would use indirect channels such as wholesalers or agents to get your products into local markets and grocery stores across the country. These companies would also help with logistics, which include transportation, warehousing, and handling of products.

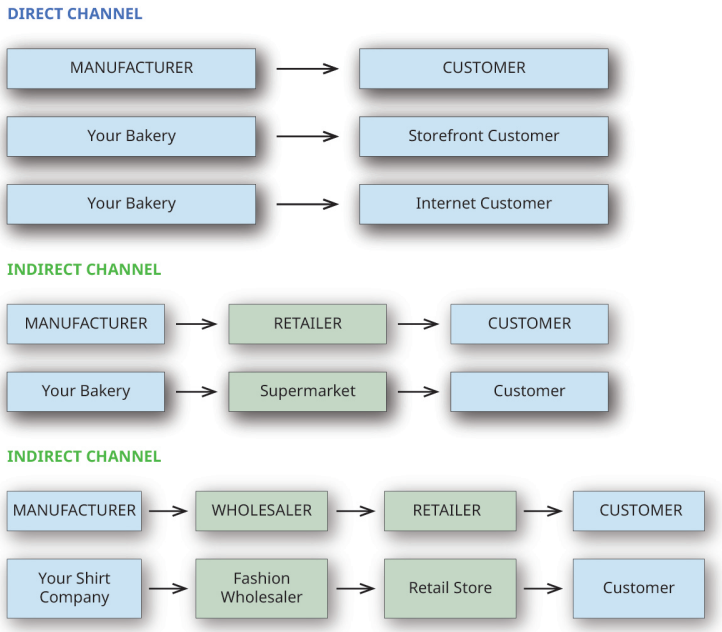


Figure 8.4 The "P" of "Place" may include distribution through direct or indirect channels. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Taking advantage of multiple distribution channels is one strategy companies use to expand their brand and grow their profits. This can include having a physical storefront, developing an e-commerce website to sell goods online, and distributing goods through wholesalers and retailers. Including multiple touchpoints with the customer can increase the likelihood that they will choose your product.

The longer your distribution channels, the longer it takes for your product to reach the end consumer, and the less control you have over the product and the price. As an entrepreneur, you must decide which channels best fit your product and pricing requirements.

Additional Ps for Services

As you have learned, products include services as well. These include legal, accounting, consulting, medical, entertainment, advertising, banking, and other professional services. When providing services, three additional Ps should be considered in the marketing mix.

People

People, or a company's human resources, will always be a key factor in any successful business. In a service-oriented business, the people who interact with customers are especially important. Because the service *is* the product, they are the face of the brand and a direct link between the company and the customer.

When an employee delivers an acceptable or outstanding service, customers are encouraged to return to purchase the service again and also share their positive experience with others. When customers go into a jewelry store and receive good service from the salespeople, they will likely let their friends and family know about the positive experience through a personal referral or on social media.

When service is poor, customers don't return. If customers have a bad experience at a restaurant, it is likely they will not patronize the establishment any longer and will probably share a negative review online. Sometimes, poor service has to do with factors other than employees, but as online review sites such as Yelp become more common, poor customer service reviews can have a devastating effect on a brand, especially for start-ups trying to break into a market. It is important to hire experienced people and have a good training system in place with rewards that will help employees deliver the best service to customers. Companies should take into consideration that no matter the size of a business, they must market not only to their customers but

also to their employees, as they are the face of the company and the ones who interact with customers. Employees can make or break the brand.

Physical Environment

The **physical environment** where a service is provided is an important part of the marketing mix. It can influence the company's image and convey a lot of information about the quality of a product, service, company, or brand. The old adage that you "get only one chance to make a first impression" is especially true for new businesses. Tangible cues—décor, smell, music, temperature, colors—send an immediate message to customers about quality and professionalism.

For example, if you walked into two dentists' offices (remember, they are also entrepreneurs), and one office smelled and looked clean, and one did not, which one would you choose? The same goes for restaurants, retail stores, and any other physical environment. Since a service cannot be inspected before it is received, these cues help customers make their decisions.

Process

Process is the chain of procedures or activities required to provide a service to the customer. It is all of the activities that take place between the service provider and the customer, from beginning to end.

In the case of a doctor's office, this would include making the appointment, filling out paperwork, waiting to be seen, seeing the doctor, and paying. Because processes can be long and involved, they need to be designed to flow as efficiently and logically as possible. In the case of services that are provided online, process includes the website's design and functionality, and all of the steps customers take from browsing through check out. A strong website design helps the entrepreneur say what the company is about, what it does and for whom, and what actions the customer can take. Actions can range from clicking for more information, the ability to purchase a product, or checking whether there is availability for a service and being able to book it or make an appointment. An example of a great website is Airbnb's website (https://openstax.org/l/52AirBnb) whose design is focused, inspiring, and to the point. What do you think is its main call to action?

ARE YOU READY?

Determining the Marketing Mix

Imagine that you are opening a new yoga studio in a local area. Based on your research, you found that certain styles of yoga are not taught by local studios but are increasingly being sought by women aged twenty-five years and older. Your task is to create a marketing mix that focuses on this market and has a clear competitive advantage over other studios. Develop a marketing mix that includes all 7Ps and define them as they relate to your business.

8.2 Market Research, Market Opportunity Recognition, and Target Market

Learning Objectives

By the end of this section, you will be able to:

- Distinguish between primary and secondary market research
- Define a research goal and the importance of research design
- Understand how to choose a sample, and collect and analyze data
- Identify common sources for secondary market research
- Understand how to identify the target market within the total available market and serviceable available market

Now you know the components of the marketing mix. But, as an entrepreneur, before you can make decisions about them, you need to roll up your sleeves and do some research. This type of research is similar to the concepts covered in Identifying Entrepreneurial Opportunity; however, that research focused on whether an entrepreneur has what is needed to move forward with an idea. This research is more market focused, and it's done after the entrepreneur has decided to move forward and start the enterprise or launch the product. Essentially it is about the product, not the entrepreneur's readiness.

Market research is essential during the planning phases of any start-up; otherwise, you're shooting in the dark. On a basic level, **market research** is the collection and analysis of data related to a business's target market. Market research can entail everything from information on competitors' products to the interpretation of demographic data related to potential customers.

The main purpose of market research is to gain an understanding of customer needs and wants in an effort to reveal potential business opportunities. When you have a clear picture of what your target market is and what it wants, you can more effectively design your marketing mix to engage that demographic.

Imagine that you are creating a cosmetic line that is organic, contains vitamins and minerals, and is easy to apply. Your target market is women who are interested in high-quality beauty products that are not harmful to themselves or the environment. But after conducting extensive market research, you learn that women aged eighteen to forty-five years tend to be interested in the benefits your product line provides, but that women over fifty years of age are not. In light of these findings, you can either adjust your line's benefits to serve the market you initially wanted to serve (all women), or you can cater to the needs of a smaller audience (eighteen to forty-five-year-old women).

A good exercise for better understanding your target market is to detail the everyday life of your ideal customer. You can do this by describing in detail a set of possible customers who would buy your product. Details could include demographic information such as gender, age, income, education, ethnicity, social class, location, and life cycle. Other information that would be helpful would include psychographics (activities, hobbies, interests, and lifestyles) as well as behavior (how often they use a product or how they feel about it). The better you know your ideal customer, the better you can focus on capturing their attention by matching their preferences with your offerings.

Market research also helps you understand who your competitors are and how they serve the target market you want to engage. The more you know about your competition, the easier it will be to determine and differentiate your offerings. Let's dive into how marketers gather all of these data and the value the data provide to entrepreneurs.

Primary Market Research

Primary research entails collecting new data for the purpose of answering a specific question or set of questions. While conducting your own research can be resource intense, it is also the best way to get answers specific to your business and products, especially if you want to penetrate niche markets that have not been studied. It also allows you to get specific. By asking the right questions, you can determine people's feelings and attitudes toward your brand, whether they like your product design, whether they value its proposed benefits, and whether they think it is priced fairly. Figure 8.5 shows the steps common in conducting primary market research.

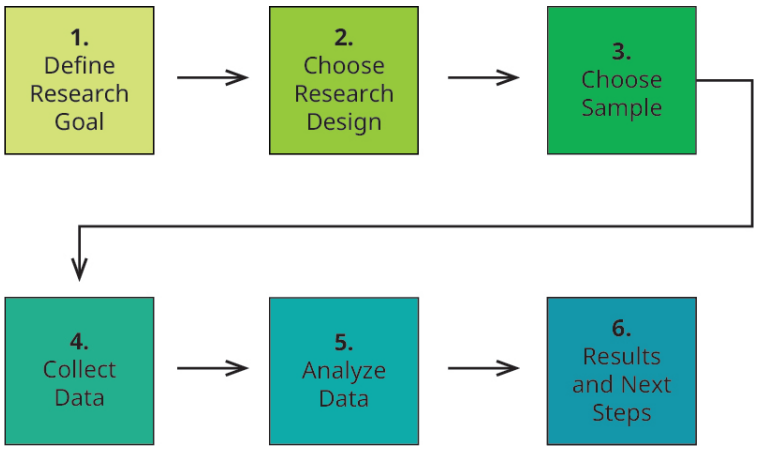


Figure 8.5 There are six steps in primary market research. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Define the Research Goal

You should start by defining the goal of your research project. What are you trying to find out? Do you want to know more about your target market, their preferences, lifestyle choices, and culture, or do you want to know more about your competitors and why your target market buys from them? What are your criteria for validation of the research goal or goals?

The more time you take to clarify your research questions, the more likely you will be to achieve your research goals. If you can't figure out exactly what you're looking for, that's okay. Exploratory research using a focus group can help you decide what kind of research questions to ask. A **focus group** is a gathering of people, typically six to twelve participants, who come together to discuss a topic presented by a moderator, who usually poses questions and collects qualitative data that can be used to answer questions or define research further.

For example, a manufacturer of water bottles might know there is a problem with their products as sales have been declining over time. The company doesn't know exactly why or where to start, so it would use a focus group to better define the research goal or problem. Using focus groups, they might find out that they are targeting the wrong segment or that there is a need for better water bottle designs. Talking to the focus group can uncover possible research questions to undertake.

Merkadoteknia Research and Consulting is a Hispanic-owned company that conducts research for different industries that cater to Hispanic consumers. This company helps fast-food companies, retailers, and pharmaceutical companies, among others, conduct focus groups and gather insights about specific groups of people that may have different cultural backgrounds. These companies may not know exactly how to start researching their target market, so they use Merkadoteknia Research and Consulting to learn more through the use of focus groups. This approach helps better define the research goal or problem.

Determine Research Design

The next step is to determine which research techniques will most effectively help you answer your questions. Considering what you want to learn and determining what your budget is will help you decide if qualitative or quantitative research best suits your needs. Well-designed research projects often use some combination of both.

Qualitative research uses open-ended techniques such as observation, focus groups, and interviews to gain an understanding of customers' basic reasons, opinions, and motivations. Simply observing potential customers, whether at a store or in daily activities, and noting their behaviors are a simple, effective form of ethnographic research that can help you better understand the lifestyles and habits of potential customers. **Ethnographic research** includes the personal observations of the subject by being immersed in the subject's

environment. Research like this helps companies see how people use their product over the course of a day.

For example, if you manufactured a water bottle and wanted to design a "better" water bottle, you could watch how people use their water bottles while working, exercising, during their commute, and so on to better understand their needs and habits. This "ethnographic" research can often uncover latent, or unstated, needs that you can use to build your concept. Unstated needs refer to those that are expected from a company, such as a certain level of quality or good customer service. These are default expectations that a customer has based on their experience with products in general.

Employing a mystery shopper, or pretending to be one yourself, is another way to learn how customers and employees act within a specific retail environment. A mystery shopper is a person who has been hired by the company or a third party to pose as a real shopper and has gone undercover with a specific goal of testing certain aspects of a business. This can take the form of purchasing a product, browsing and asking questions of an employee, interacting with other customers, or simply observing what is happening inside the store. After the experience, this person will provide feedback to the company.

Focus groups and one-on-one interviews can be useful to obtain more thoughtful answers and explore debatable topics. Both are good methods for digging deeper into the specific motivations and concerns of people, especially as they pertain to personal, privately held beliefs. This research is useful when trying to develop a more novel product, but you must do your best to eliminate "support bias" in that the panelists might seem favorable to new concepts to please or accommodate the moderator. For one-on-one interviews, it is important to develop a thorough interview or discussion guide, so other team members can also conduct the interviews. By doing this, you will ensure a consistent approach to asking key questions and documenting responses to help guide the next step of the development of your product.

Quantitative research focuses on the generation of numerical data that can be turned into usable statistics. This kind of research most often takes the form of surveys or questionnaires that pose multiple-choice questions with predefined answers. While these surveys do not allow for much free expression on the part of the participant, the focused nature of the answers means marketers can identify trends, such as which social media platforms are preferred by customers or potential customers. For example, the researcher may very well find that Instagram is the most used social media app because of its ease of use and its ability to incite emotional responses to pictures.

Sample survey questions can be anything from "How many times have you gone to the corner store this week?" to "Which age range do you belong in?" This kind of approach is an efficient way to collect a lot of data because once the survey is written, it can be distributed in person or online to as many participants as you like. Typically, the more people you survey, the more accurately your data will reflect the demographic you are examining.

Another way to generate quantitative results is through **causal research** and test marketing. In both cases, you present participants with a cause and record the effect. An example of this might be a taste test in which people's reactions to and preferences for different juice flavors are recorded. Given the limited resources of many start-ups, test marketing is a great way to make sure your product works before you start investing in its distribution.

An even more sophisticated—and expensive—method is **conjoint analysis**, in which respondents must rank, choose, or a rate a number of "conjoint," or linked, features or benefits. This real-life scenario approach will give you very useful results from potential buyers, often with features or benefits ranked relative to perceived value or importance.

For instance, let's say your company is trying to create a reusable water bottle to compete in a crowded marketplace. If you were to use conjoint analysis, you would create a survey that lists the water bottle attributes and prices to show consumers different choices. For example, customers could be given a set of very similar water bottles, each with a set of features the company would like to test. Features can include a

locking lid so the water doesn't leak, different bottle shapes for easier hold and water retrieval, and different colors and sizes. Each of the choices could have its own price point and the customer can choose, rank, or rate each of the choices based on those attributes and prices. Each of the choices could be described on a survey with words or pictures, and it would ask customers to choose their favorite or rank all of the choices. After collecting information and data from many consumers, researchers would use statistical analysis by applying linear regression (a predictive tool that measures the causality of one marketing variable on another) or other techniques to determine which attributes of a water bottle are more important to the customer and what price they would be willing to pay. Based on this knowledge, the company would create a product that could possibly beat the competition.

Choose a Sample

Next, researchers need to determine the sampling method. In terms of research, your **sample** refers to who you will survey and how many people you will include. In most cases, you will want a sample that reflects your target market, especially if you are trying to figure out your ideal customer's interests and how to get them to buy your product. Untargeted samples can be useful when trying to figure out who your target market might be, but they aren't an efficient way to get to know your ideal customer.

Generally speaking, larger samples provide more accurate data, although researchers should not feel like they need to survey everyone in a market. For example, if you have a list of 5,000 contacts, you might choose to contact 500 people who would be representative of the total group of contacts. Surveying all of your population could be time consuming and expensive, so choosing a subset of the right people can yield good results. The sample must be large enough to be statistically significant, meaning that the relationship between variables is not a result of chance. The sample can then show the researcher an accurate depiction of a specific phenomenon.

For example, you can test whether men and women actually have different or similar tastes in water bottle attributes. In this case, the significance rests on the gender of the potential customer. If your sample is large enough (say 500 out of 5,000), and you find that men look for different attributes than women do, it is unlikely that the differences found were by chance. The cause of the differences would be the gender.

Therefore, keep in mind that errors of reliability and validity can arise if your sample is not thoughtfully selected. Statistical significance is then important in measuring reliability because it means that there is an actual difference in what is being measured. If there is a difference between men's and women's responses in our water bottle example, checking the significance will determine whether the differences really matter or if they are due to chance. Significance is measured by looking at the probability value, or *P* value, of the result. If it is 5 percent or less, it is usually considered a significant difference that is not due to chance, and the researcher can determine that the answers are indeed different between the two genders. Validity, on the other hand, means that the item that is being measured is relevant to the research. This means that the questions that are being asked will actually answer your research objective.

While random samples can be useful for some types of research projects, many researchers intentionally choose their sample participants based on economic and ethnographic factors to make sure they accurately reflect the nature of the demographic they seek to understand.

Collect Data

Once you've identified your research goals, chosen your design, and determined your sample, you are ready to start collecting data. The data may be collected through observation and taking notes. For example, if you are trying to figure out if your store layout is yielding the most productive sales, you can observe traffic flow and note what people look at and what they actually purchase. Then, you may change the merchandise layout, or the aisle size or space, to see whether people peruse other merchandise that they hadn't seen before. Based on your observations and sales data, you can determine the best flow for your floor.

Interviews can also help secure open-ended answers. You might interview potential customers on what they think is the best way to communicate with them and what they like about certain competitors' products. This can help you obtain additional options that you may not have thought to add on a survey, which is another way to get aggregate data.

Surveys can be done by hand or through online tools such as Survey Monkey or Qualtrics. Surveys are very helpful because you can ask question to current or potential customers about your product, competitors' products, customer service, and any other information you may seek to create or improve your business. They are an easy way to collect large amounts of data from many customers, and they allow you to calculate responses. Online tools are particularly useful in providing repositories of data that can be later exported to other analytical tools such as Excel or SPSS.

Regardless of what research technique you use, be on the lookout for data collection errors. Recording the wrong answers, failing to convey the right instructions to participants, or having to translate on the fly can all create biases that skew the answers and give you inaccurate results.

Analyze Data

Once you collect your data, the next step is to make sense of it. How you analyze the data depends largely on what you want to get out of it. Typically, you will be looking for patterns and trends among the answers. Data analysis is a field unto itself, and when complex analysis is required, seeking the assistance of experts is often worth the extra cost. You can find experts within research marketing firms that specialize in collecting and analyzing data for businesses, such as Merkadoteknia Research and Consulting. These can be found online or through local business organizations, such as chambers of commerce.

Results and Next Steps

At this stage, the entrepreneur seeks to reconcile the results of their examination with the goals of their research. For example, if you were doing exploratory research about a potential product you wanted to bring to market, now would be the time to ask questions such as whether the research suggests market potential. Similarly, if the goal was to figure out what customers like about competing products, now would be the time to list those results and determine whether they are worth incorporating into your product. Regardless, it is important to be open to what the data say, even if they indicates results that are contrary to what you were hoping for. Research should be an opportunity for growth and a roadmap for the refinement of your idea.

Secondary Market Research

Secondary research is research that uses existing data that has been collected by another entity. Oftentimes, these data are collected by governmental agencies to answer a wide range of questions or issues that are common to many organizations and people. Secondary research often answers more general questions that an entrepreneur may have, such as population information, average purchases, or trends. If there is a specific question that cannot be answered, such as how many people would be interested in a new product with certain attributes, then primary research will have to answer that. While some of this kind of research must be purchased, much of it is free to the public and a good option for entrepreneurs with limited financial resources. Some commonly used sources for free data include the US Census Bureau, Fact Finder, Pew Research Center, Current Population Survey, the Small Business Administration (SBA), and the Texas State Data Center.

Other useful resources are trade organizations that provide information about specific industries, as well as newspapers, magazines, journals, chambers of commerce, and other organizations that collect local, state, national, and international data. Resources such as these can provide information about everything from population size to community demographics and spending habits. Table 8.3 lists several free databases that are rich sources of information.

Databases for Secondary Research

Database	Information	URL Address
Census Bureau	Economic, demographic, geographic, and social data	https://www.census.gov/
Fact Finder	Economic, population, and geographic data	https://factfinder.census.gov/
American Community Survey	Updated census data	https://www.census.gov/programs-surveys/acs/
Pew Research Center	Fact tank that surveys trends, issues, attitudes, and demographics	http://www.pewresearch.org
Pew Hispanic Center	Surveys on Hispanic trends, demographics, and issues	http://www.pewhispanic.org/
Current Population Survey	Monthly survey of US households on labor data	http://www.bls.gov/cps/home.htm
Texas State Data Center	State demographic data	http://txsdc.utsa.edu/
IBISWorld	US industry trends	http://www.ibisworld.com
Mergent Online	US businesses data	http://www.mergentonline.com/
Demographics Now	US demographic and business data	http://www.demographicsnow.com/

Table 8.3

While free sources can provide a lot of information, their research tends to be less specific than that by sources that charge for their data. Companies such as Nielsen/Arbitron, Simmons, and Geoscape can provide more detailed information about specific behaviors on media use, lifestyle choices, specific product consumption, geographic segmentation data, and others. Table 8.4 lists some sources for this research.

Syndicated Sites for Secondary Research

Site	Information	URL Address
Nielsen PRIZM	Geodemographic segmenting	https://segmentationsolutionsdev.nielsen.com/mybestsegments/Default.jsp?ID=20&pageName=ZIP%2BCode%2BLookup
Nielsen TV ratings	TV ratings, media, research	http://www.nielsen.com/us/en/insights.html

Table 8.4

Site	Information	URL Address
Nielsen Audio	Audio ratings, media, and research	http://www.nielsen.com/us/en/solutions/capabilities/audio.html
Experian Simmons	Consumer research, trends, and insights	http://www.experian.com/
Scarborough	Consumer research, trends, and insights	http://www.scarborough.com/
Geoscape	Multicultural consumer research	http://geoscape.com/

Table 8.4

In the end, there is no perfect way to conduct research. It all depends on what you are trying to find out and what the best approach is to do that. If you are just starting out, you may want to maximize secondary research because it is free. You can also try primary data collection by speaking to friends, family, and others you encounter in your local and online communities. If you are working at a university, you will likely have access to free market research reports (marketresearch.com, Frost & Sullivan, etc.).

ARE YOU READY?

Researching Your Market

Pretend you are an entrepreneur who would like to create a new, educational toy for toddlers to develop their motor skills that uses figures, shapes, or blocks. While in college, you worked in the children's section at a well-known retailer. From this experience, you learned that there might be a need for educational toys within the market that isn't being addressed, but you aren't exactly sure how to exploit it.

- Using the market research process, develop a research plan that will help you determine the viability of your idea.

Market Opportunity Recognition and Validation

One common goal of market research, which has been mentioned earlier in other chapters, especially the Identifying Entrepreneurial Opportunity chapter, is the identification of a **market opportunity**, or an unmet need within a target demographic that might be fulfilled by an existing or new product. Looking for gaps or unmet needs within a marketplace is one way to identify market opportunities for both goods and services. For new products, this entails looking at the needs of a demographic, identifying which of those are not being met, and determining what kind of product could fulfill it. Based on our earlier discussion on secondary research, there are many places where data can be found online or offline to determine these needs.

Similarly, you might identify common local, national, or global problems through observation and directly interacting with potential customers, and try to create services that would solve them. Social, economic, technological, and regulatory changes all have the potential to create market opportunities.

When inventor David Dodgen saw the suffering that Hurricane Katrina had left behind, he saw an unmet need that this event had created. By witnessing the disasters, he realized that when hurricanes or other disastrous events strike, they can contaminate the water supply in a region or city, or prevent access to clean water. As a

result, he created the AquaPodkit, a plastic container that can temporarily store fresh water for weeks at a time in the event of an emergency. The Federal Emergency Management Agency (FEMA) recommends that people fill their tub if they feel that there may be a chance that water will be scarce. Oftentimes, tubs can be dirty, and people may not have the time to clean them. With this in mind, Dodgen developed a plastic lining, or bathtub bladder, which is manufactured in the United States and is safe to drink from, together with a pump that helps seal and open the plastic when the water is needed. This kit can hold up to 100 gallons of fresh water in the tub and has proven successful; it has also been featured by CNBC, *Entrepreneur*, and the *New York Times*.

LINK TO LEARNING

View this video about the AquaPodkit (https://openstax.org/l/52AquaPod) to learn more. Dodgen also created smaller bags and pumps (https://openstax.org/l/52BagsPumps) that can be stored anywhere, not just in the tub.

WHAT CAN YOU DO?

Climate Change

Background: Earth's climate change is a topic of discussion with great importance these days. For many hundreds of thousands of years, Earth's temperature changes were attributed to tilts on its axis that allowed for more or less energy to enter our atmosphere. Recently, Earth's climate has experienced a dramatic increase in temperature, and most scientists around the world agree that it is attributed to human activities that emit carbon dioxide into the atmosphere.

Greenhouse emissions have increased the temperature of Earth to the point that glaciers in Antarctica and Greenland are now disappearing ten times faster than on a normal ice age recovery session, not to mention the many weather catastrophes that are seen around the world.[9] These changes in temperature have caused ice sheets to melt, snow caps to retreat, oceans to warm and become more acidic, water levels to rise, and severe weather to increase.

As harmful as it sounds, there is still time to change the negative effects of global warming. This can present some opportunities for social entrepreneurs who care about Earth's environment and business.

Your task: As a social entrepreneur, determine one or two opportunities for a business you could develop and test for market validity.

- What kind of opportunities are there to create positive change?
- How can you validate your assumptions?
- How would you test unmet needs?
- What kind of research would you conduct? Why?

Sometimes unmet needs are not uncovered immediately. One way to better understand a market's opportunities is to conduct a **market analysis**, which is an analysis of the overall interest in the product or service within the industry by its target market to determine its viability and profit potential. **Validation**, not to be confused with *validity*, is the act of verifying that a specific product is needed in a target market. This can be done by conducting formal or informal interviews or surveys with potential customers to gather their feedback. Dropbox is an example of a company that conducted validation over and over until they created a product that could work with a mainstream audience (see Launching the Imperfect Business: Lean Startup).

9 National Atmospheric and Space Agency (NASA). "Climate Change: How Do We Know?" n.d. https://climate.nasa.gov/evidence/

In addition to identifying competition and determining growth and profit potential, a good market analysis will identify the **total available market (TAM)** for a specific product, which is the total perceived demand for a product or service within the marketplace. It will also identify the **serviceable available market (SAM)**, which is the portion of the market that your business can serve based on your products, services, and location (Figure 8.6).

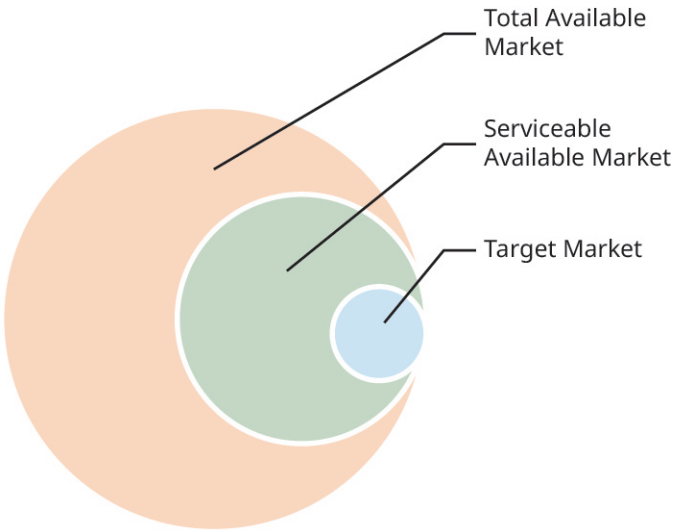


Figure 8.6 Entrepreneurs must focus on the target market within the TAM and the SAM and allocate resources to attract customers who can be satisfied by the value proposition. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

To calculate this, let's go to our water bottle example. Let's say that you are trying to figure out what your target market is based on this concept. To calculate the TAM, you would look at the whole industry and determine the total number of customers available for water bottles or total revenue available. To find the number, you can look up the industry numbers for the category on databases such as IBISWorld, mentioned earlier, or any other data available through the World Bank or World Factbook to see the potential number of customers or revenue. This is called the top-down approach, as you are looking at macroeconomic factors to determine an industry's potential.

Another way to calculate the TAM would be by using the bottom-up approach, which involves counting local market sizes and figuring out the competitors' number of customers. After collecting this information, then all the local markets would be added up and multiplied by the average amount they spend on the product per year. Since your company cannot service all markets, the next step is to figure out the SAM. You could estimate the number of customers you can service by splitting the market into those you can service given your product characteristics and geographic, demographic, and cultural factors, among others.

Finally, considering the constraints of the company and strength of the competition, you would determine your focused target market to avoid wasting valuable resources marketing to people who are generally not interested in buying your product.

As an entrepreneur, you want to segment the market and figure out if there are possible pockets of people that you can serve. Segmenting, targeting, and positioning (STP) will help you figure out who is your best customer and will allow you to allocate your resources so that you can more effectively serve that customer. Let's look at these processes now.

Segmenting means that you separate the total population by homogeneous groups of people that have similar tastes, backgrounds, lifestyles, demographics, and even culture. You may segment along lines such as age ranges, gender, ethnicity, line of work, earnings, or activities. There are many ways to separate these groups to choose the right one for your business.

The next step is **targeting**. You select a target based on their ability and willingness to buy. As stated earlier, a

target market serves to specify which group of the total market you will serve and how you will position yourself to distinguish your company or product from your competitor.

Positioning (value proposition) is a statement of how you want the customer to perceive your company, good, or service. For example, ModCloth is an online indie retailer that sells vintage, or vintage-looking, trendy, fun clothing that appeals to the global consumer who wants to be stylish. Another example is Wag! which positions itself as the app that lets the pet owner look for a walker on demand. Kind of like the Uber for dogs who want a walk when their owners can't take them!

ENTREPRENEUR IN ACTION

Wag! Dog-Walking App

Figure 8.7 The Wag! app allows busy people to choose from prescreened dog walkers so their furry friends will be well-taken care of while they're at work. (credit: modification of "A woman with her dog@Takayama" by JAR/Wikimedia Commons, CC BY 2.0)

As a dog owner, Wag! CEO and co-founder Joshua Viner struggled to find the time to walk his beloved dog after a long day at work. He knew it was unfair to keep her cooped up all day. He even considered finding her a new home. This canine conundrum led him to create Wag! in 2015 as a way to help people like him who loved their dogs but didn't always have the time to make sure they were properly exercised.

To start, Viner got together with Jason Meltzer, who, like himself, had experience creating consumer tech companies. Meltzer was the founder of pet services company Surfdog LA, which already had a proven track record of success. Together, they developed an app and website with the goal of making dog ownership easy and guilt free. Wag! gave customers access to trusted, prescreened walkers who could take their dogs out on short notice without them having to be present. Customers could even see their dog being walked via the app.

Since its inception, Wag! has been growing and entering new markets at a steady pace. After launching its service in Los Angeles and San Francisco in 2015, it continues to add cities across the United States.

Because the app's dog-walkers have access to their client's houses, one of the challenges Wag! faced was making sure customers trusted them and their dog walkers (Figure 8.7). Another challenge was the safety of the dog itself. What happens if a dog gets hurt or lost? It wouldn't take much for issues like these to turn

into major problems.

- Describe the target market for this service.
- Are there other potential customers who can be a good target for this service?
- How can Viner position his business to assure pet owners that their dogs will be well taken care of?

8.3 Marketing Techniques and Tools for Entrepreneurs

Learning Objectives

By the end of this section, you will be able to:

- Describe effective entrepreneurial marketing techniques (guerilla, relationship, expeditionary, real-time, viral, digital, word-of-mouth)
- Discuss the pros and cons of these marketing techniques

One of the hardest facts for entrepreneurs to absorb when starting a new business is that financial and human resources are limited. Fortunately, there are many marketing techniques available to entrepreneurs that require little more than a good dose of "sweat equity."

Guerilla Marketing

Coined by business writer and strategist Jay Conrad Levinson in 1984, **guerrilla marketing** refers to creative approaches to marketing that seek to gain maximum exposure through unconventional means. Guerilla marketing often means staging some sort of event or interaction that is designed to attract attention to a brand or product. The goal is to intrigue consumers by standing out from normal sales messages and the thousands of advertisements they are exposed to every day. These approaches usually have a component that encourages potential customers to interact with a company or product in a fun way.

Dennis Crowley, a serendipitous entrepreneur who taught himself to code and who was laid off by Google while working on his social networking site Dodgeball, was able to create and grow Foursquare through the use of guerrilla marketing techniques. Foursquare, the search and discover nearby businesses app, used this technique at the Austin, Texas-based South by Southwest film and music festival. The idea was to set a real game of foursquare in front of the convention hall that also raised awareness for the app (Figure 8.8). The games were an instant success and attracted thousands of participants who played all day long. If someone didn't know what the game was, a marketing team of 11 people helped them find it on their phones. Their efforts resulted in 100,000 views for the app that that day alone.[10] All of this was achieved for the cost of a box of chalk and two rubber balls. Although the company had plenty of investments to sustain its operations, guerrilla marketing was a clever and helpful way to get users to test it and enjoy it.

10 Knowledge @Wharton. "How to Generate Buzz on Social Networks." *Forbes*. April 23, 2010. https://www.forbes.com/2010/04/23/foursquare-facebook-yahoo-entrepreneurs-technology-wharton.html#13e159097b2d

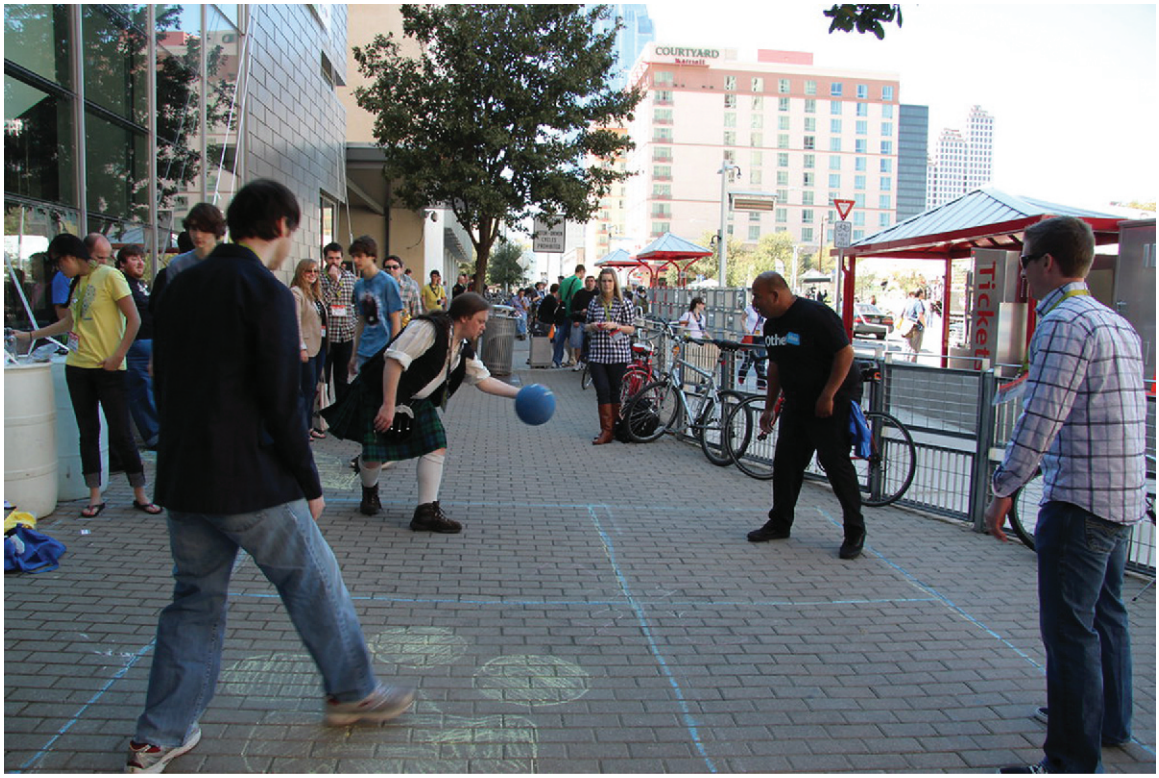


Figure 8.8 Foursquare's guerilla marketing idea generated 100,000 new views for the app at the South by Southwest film and music festival in Austin, Texas. (credit: work by betsyweber/Flickr, CC BY 2.0)

Another example of guerrilla marketing that has been prominent over the last few years is flash mobs. A flash mob is a gathering of people at a public place to perform an act, be it a dance, entertainment, political stance, or some sort of artistic expression that conveys a message to the public for a brief period of time. This is organized through social media calls or emails to gather enough people to perform them. Flash mobs have been effectively used by companies to create awareness and reminders about their brands.

LINK TO LEARNING

You can watch videos of some of the best choreographed flash mobs (https://openstax.org/l/52FlashMob) in business.

Relationship Marketing

One of the main differences between start-up companies and established brands is the need for start-ups to nurture and maintain relationships with new customers. One way to accomplish this is through **relationship marketing**, which seeks to create customer loyalty through personal interactions and long-term engagement strategies. A small company can try to have a closer relationship with clients by writing personal notes by hand or sending an email thanking them for their business, by acknowledging their presence by their first or last name when they come into the establishment, by offering beverages, and by offering other personalized services.

An example of successful relationship marketing from a larger company comes from MooseJaw, a retailer specializing in outdoor clothing for hiking and snowboarding. At one point, a MooseJaw customer returned a piece of clothing that he had bought as a gift for his girlfriend. In his explanation for the return, he wrote, "Girlfriend dumped me." Seeing this as an opportunity to engage with a customer, the company decided to send the man a care package.

A few weeks later, the man received a surprise shipment with a note saying they were sorry his girlfriend broke up with him so they decided to give him a gift. The box contained shirts, stickers, and other goodies. There was also a card with notes from MooseJaw's employees.[11] MooseJaw's efforts were rewarded when the situation went viral on social media, which generated more exposure and support for the company.

Another way companies maintain relationships with their customers is through regular email newsletters. By using sales history and other market data, companies are able to customize the content of these usually free newsletters to the needs, concerns, and desires of their target market. This allows them to stay connected to their customers while developing strong connections and brand loyalty. Start-up companies can take advantage of the free and affordable options offered by such newsletter management software companies as MailChimp, Constant Contact, Mad Mimi, Marketo, Insightly, Slack, and Salesforce.

Expeditionary Marketing

One of the toughest aspects of entrepreneurship is to stay in business and grow in a highly competitive landscape. Businesses are born every day with the goal of making a name for themselves by providing better goods and services. One way that companies big and small can stay relevant is through expeditionary marketing.

Expeditionary marketing refers to strategies that are aimed at moving established companies and their products into new markets and territories. As the name implies, there is an element of risk and discovery involved in expeditionary marketing strategies as they help a company grow into new areas. Determining where and how to effectively enter these new markets often begins with an analysis of a company's current market and its financial and human resources. Entrepreneurs will choose new markets based on where those resources might be able to fulfill an unmet need. Many small businesses need to leverage their gains as they move into new waters and perhaps more competitive landscapes. Having awareness of changes can foster planning and look for new ways to expand.

This type of marketing is very similar to entrepreneurial marketing, and the terms are often used interchangeably, except that expeditionary marketing involves existing companies continuing to innovate whereas entrepreneurial marketing also involves new companies. Companies that have succeeded in taking their businesses into new markets and consistently pivoting to create new products for current and new markets can be thought of as entrepreneurial companies. Big companies such as Apple, Google, and Dropbox Launch for Growth to Success have consistently developed products and entered new markets to keep abreast of the competition. Companies that did this while small like Birchbox (see Introduction) also use this method to grow and fight off competitors.

Real-Time Marketing

Real-time marketing attempts to turn immediately available sales data (often collected from social media, websites, point-of-sale systems, and the like) into actionable and timely strategies that target the shifting landscape of consumer tastes and trends. Some of the tools entrepreneurs can use to secure information include analytics from Facebook, Twitter, and Google, as well as internal sales data. The information can include preferences for one brand over another, lifestyles, behavior, purchase frequency, and dollar amount spent. This helps entrepreneurs set up strategies that focus on providing the customer what it needs in today's instant gratification society.

For example, a company such as Birchbox creates a post on Facebook or Twitter regarding a new promotion. It can then confirm the number of "clicks" the post gets and determine the depth of engagement for each of the posts. Clicks can be likes, shares, comments, and purchases that can be tracked immediately, minute by minute, hour by hour, or day by day, depending on the length of the promotion. Real time allows the marketer to assess the action followers take immediately after this happens. Success will depend on the goal that was

11 Joshua Kraus. "The Dos and Don'ts of Relationship Marketing." *Sitepoint.* April 16, 2015. https://www.sitepoint.com/relationship-marketing-examples/

set by the company. For example, if for one of their promotions, Birchbox expects 1,000 likes, 100 shares, and 30 conversions or purchases per day, it will be very easy to track whether the company is accomplishing its goal just by looking at the results every hour. This makes it very easy to gauge and to change. If a post is not getting the desired results in likes, shares, comments, or conversions in the desired timeframe, then the company can make changes to the communication sent to provide a different incentive, such as providing a deeper discount, or using different language, a new picture, and a better call to action. In addition, real-time tracking also allows for the company to answer tweets and comments from its followers immediately. This enables direct communication from customer to company without any interference or time constraints.

Viral Marketing

Viral marketing is a technique that uses engaging content in the hopes that viewers will share it on their personal and social media networks. Successful content then spreads like a virus, creating exponential exposure to a company's message.

The most important element of any viral marketing campaign is developing content that is not only engaging but that people also feel must be shared. Generally speaking, viral content is not "salesy" in nature; rather, it tends to be subtle about its presentation of branded items. In this way, the product or brand reaps the indirect exposure that comes with being part of content that people want to consume. A very successful campaign that included viral marketing is the Dove Real Beauty Sketches campaign (https://openstax.org/l/52DoveReal) where a real-life forensic artist sketches women's faces based on their own descriptions and sketches them again through other people's descriptions of their faces. When these sketches were revealed to the women who were asked to participate, they saw how much kinder and more beautiful other people had described them. This video never mentioned any Dove product at all. The result of this campaign was astounding, as it had more than 140 million views worldwide, becoming the best viral video of 2013 by connecting to the customer in an emotional way that was sincere and warm. This campaign also enabled the company to track results in real time and answer comments from viewers in a timely manner, while enhancing brand awareness.[12]

Another example of an effective viral campaign is that of Dollar Shave Club (https://openstax.org/l/52DollarShave) which has garnered more than 26 million views on YouTube in response to the low budget and entertaining video by the owner of the company. Founded in 2011 in California with the goal of providing low-cost razors to men every month through a membership, the company has been so successful that it has since been acquired by Unilever.

The benefit of this kind of marketing is that it can lead to massive exposure for little or no effort or investment once the content is developed. The challenge, though, is that it is difficult to predict what will be successful viral content. Viral marketers often create a lot of content that does not go viral before finding content that does.

Digital Marketing

Digital marketing refers collectively to all digital (online) marketing efforts, which can include social media, email communications, websites, blogs and vlogs, and search engine optimization (SEO). This is an important area for entrepreneurs to explore because learning how to leverage digital channels and online analytics is key to remaining competitive in this technological era.

12 Nidhi Dave. "Top 3 Viral Marketing Campaigns to Take Inspiration From." *SEMrush*. March 9, 2018. https://www.semrush.com/blog/viral-marketing-campaign-inspiration/

Digital ad spending has outpaced television ad spending in recent years.[13] Digital ads include display ads, search ads, and social media ads. These can be very successful at targeting specific people in your target market and are usually more affordable than a TV ad. They are cheaper to make and to place than TV ads, which can cost millions of dollars for production and air time to reach a wide number of people. Digital ads are important for entrepreneurs because they are an effective way to redirect traffic to their websites and gain conversions on a budget. It does not matter how big your budget is. These ads can be strategically bought to be as cost effective as possible. They can range from a few dollars to millions of dollars, depending on your resources. Display ads are those that resemble banners and showcase a product or company on a website in a noticeable way. They come in various sizes, and the entrepreneur may buy them on third-party websites or search engines that provide space for ads. These ads are usually paid using a pay-per-click model, which means that you only pay for the times that someone clicks on your ad, or you can pay for impressions, which means that you only pay for the number of times the ad appears on readers' screens.

Search ads, conversely, are those text ads you see while you are looking for something on a search engine, whether it's on your laptop, tablet, or mobile device. Google, Bing, and Yahoo! are the three biggest search engines in the United States that provide businesses the ability to create targeted ads to reach customers who are looking for something in particular. These ads are created using keywords that are strategically chosen to target people typing those specific words in the search engine and are paid through a bid system that allows the business to specify how much they will pay for an ad to be displayed in a better position on the engine's display pages. Google Ads and Google Analytics are tools that allow a digital marketer to search for popular keywords and create ads based on these terms to target the right consumer. These tools are so well designed and complex that it takes some time to get acquainted with all of their features and capabilities. Their main features, however, are to look for the right keywords, create the ad campaigns, and track their success.

Go to your favorite search engine and try to search for something (Figure 8.9). What kind of ads do you see on your screen? Someone on the other side has created these ads to connect with you. Did they do a good job?

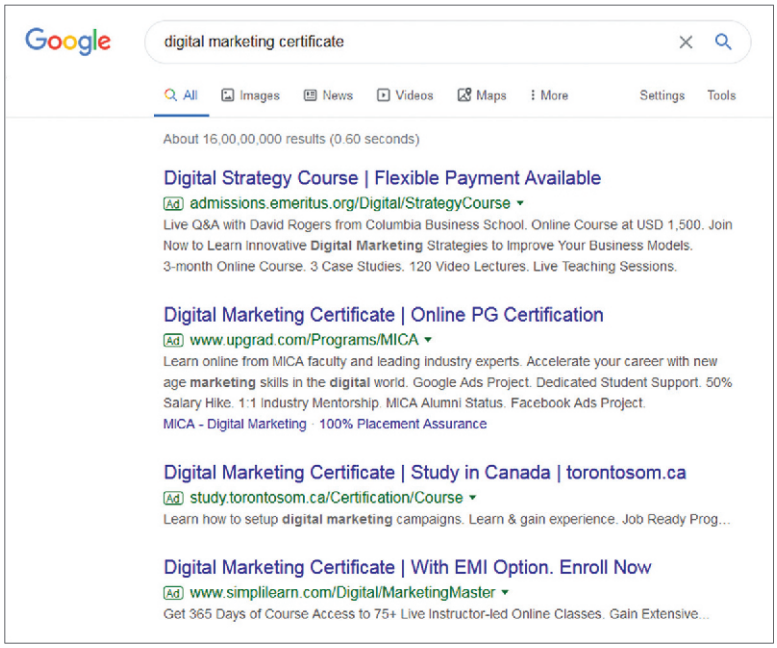


Figure 8.9 The Google Ads tool is effective for reaching targeted audiences searching online for specific products.

Social media platforms also have the capability for users to create similar ads on their systems to target people based on their behavior, likes, profiles, and searches for products online. Their popularity has increased as more people join the platforms and more information is gathered from them.

13 Greg Sterling. "Digital Now Makes Up 51% of US Ad Spending." *MarketingLand*. September 20, 2018. https://marketingland.com/report-digital-now-makes-up-51-of-us-ad-spending-248617

ARE YOU READY?

Solar Panels Are Hot

During the last ten years, solar panels have increased in popularity, as they are a great alternative to fossil fuels. Solar panels enable homes and organizations to transition from electricity generated from fossil fuels to clean energy. Given the current climate state and changes in the energy industry, solar panels have become an excellent way to save money on electricity over the long run, a great way to receive tax credits, an incentive to add equity to homes and buildings, and a help to the environment. The cost of installing such technology has decreased over the years thanks to the new technology available, the increase in competition, and the overall increase in demand of the product. Consumers can install the cells on their roofs at a more affordable price.

Given the recent trends and interest you have in helping the environment, you've decided to get a part-time job at a new local solar panel company. This company has a very small market share (less than 1 percent), or percentage of customers, compared to the rest of its competitors. Their goal is to increase that percentage to 2 percent of total customers by the end of the year. To reach that, they have hired you as their marketing coordinator.

As part of your job, you decide to create a plan for a promotion to reach a targeted number of people. This promotion must be conducted online and on a budget. On your first few days on the job, you research the various types of ads that could most effectively reach the most people looking for solar panels. Once your research is over, you come back to the owner and help her decide which ads to use. Focus on the following three areas and provide your advice to the owner.

- What are the best types of ads and platforms for this type of company?
- What is the average price per ad clicked or seen?
- What are five to ten common keywords that can be used in the ads?

Blogging has become an important tool for business owners. It allows them to share information about their companies, products, and their experiences in written or video form. Blogging enables entrepreneurs to create a name for themselves, especially when the content is useful and people are interested in what the blogger has to say. Strategies that help entrepreneurs include making the time to blog, having a specific niche, choosing interesting topics that matter to the blogger and the audience, and using other branding and SEO techniques that help the blog become more visible.

Content marketing is an important topic for digital marketing, as content has become more important in recent years. Content can be displayed as a story, a blog, a website, social media posts, a newsletter, an article, videos, or anything else that has the ability to convey a message to the consumer. This is a valuable tool to distribute content that is useful, which can engage the target audience and entice them to take some sort of action. The entrepreneur must take the time to create useful content to connect with current and potential customers online. Entrepreneurs can also tap influencer marketers to disseminate information about their brands. This includes tapping into social media celebrities, who usually have millions of followers on YouTube, Facebook, Instagram, or similar platforms. This has been one of the biggest recent trends in marketing.[14] When working with influencers, it's important that they disclose that they receive compensation for any product or service they are talking about to avoid legal risks.

Email marketing is a form of direct mail that connects to consumers in a personal way. Emails can contain useful content for consumers, promotions, and tips that entice them to try or be aware of a product. Many email marketing platforms offer services at an affordable price, including Constant Contact, Mad Mimi, Mail

14 Sumit Gharal. "7 Reasons Why Content Marketing Is Important! Number 7 Is a Must Read!" *Digital Doughnut.* April 4, 2019. https://www.digitaldoughnut.com/articles/2019/march/7-reasons-why-content-marketing-is-important

Chimp, and Drip. All of these platforms allow the entrepreneur to upload a list of customers or potential customers and create email marketing campaigns that are tailored to each target market. These platforms also offer useful metrics, such as open rates, click-through rates, time spent viewing the message, and conversion rates, which can measure the effectiveness of a campaign.

Word-of-Mouth Marketing

Word-of-mouth (WOM) marketing occurs when a satisfied customer tells others about their positive experience with a good or service. Although similar to viral marketing, WOM does not involve active participation from the marketer and almost exclusively involves only customers, whereas viral marketing attempts to build awareness and buzz mostly via videos or email.

When consumers are very happy with their purchases, they will let people know, whether it is in person or on social media. The company has less control over this type of marketing because it happens organically. While effective WOM marketing can have a huge impact on a brand's sales and visibility, creating WOM is tricky—people have to want to talk about your product.

One way to encourage WOM is to ask satisfied customers to help you spread the word by talking to their circle of friends and family, or by sharing comments online on the website, through portals, or through social media. Companies often include call-to-action cards in their shipments that direct customers to post reviews on their website, the website where they purchased the item (Ebay and Amazon), or on public review sites such as Yelp.

Entrepreneurs who do this need to make sure they monitor what is being said about their businesses so that poor reviews don't undermine their marketing efforts. Many of these sites allow businesses to address and resolve bad reviews, which is a good way to turn a potentially damaging situation into one that creates goodwill and positive brand recognition.

Lululemon is a yoga and athletic wear company that knows well about customer reviews. On its site, customers have the opportunity to leave comments about each of the garments regarding the size, fit, quality, and ease of use. Although the quality of Lululemon garments is high, some customers still have negative experiences and don't hesitate to share their comments on the site. The company responds with an apology for the negative experience and redirects the unsatisfied consumer to an email so they can move the conversation off the site. This allows the company to make amends with the customer and hopefully remove the negative comments if the issue can be resolved.

Table 8.5 summarizes entrepreneurial marketing techniques.

Entrepreneurial Marketing Techniques

Marketing Technique	Description	Example
Guerilla marketing	Aims to gain maximum exposure through unconventional means	Events, such as flash mobs
Relationship marketing	Creates customer loyalty through personal interaction	Personalized communication to individual customer
Expeditionary marketing	Strives to move established companies and products into new markets	Pivots that create new products or attract new markets

Table 8.5

Marketing Technique	Description	Example
Real-time marketing	Seeks to turn immediately available sales data into actionable and timely strategies that target the shifting landscape of consumer tastes and trends	Analyzing clicks or "likes" and modifying posts/ offerings in response
Viral marketing	Uses engaging content in the hopes that viewers will share it on personal and social media networks	Subtle branding embedded in stories users want to share
Digital marketing	Uses online marketing strategies	Online ads and use of search engine optimization (SEO)
Word-of-mouth (WOM) marketing	Relies on satisfied customers telling others about their positive experience	Online customer reviews

Table 8.5

8.4 Entrepreneurial Branding

Learning Objectives

By the end of this section, you will be able to:

- Understand the importance of customer-focused branding
- Explain the steps in defining and developing a brand
- Describe the benefits of brand advocacy

In a business context, the word brand has multiple meanings. First, a *brand name* is the name of a product or service offered by a company. For example, Coca-Cola and Goodyear are brand names. But the **brand** also means the image a company promotes and the connotations it fosters of itself and its products. For example, the Coca-Cola brand might be seen as refreshing, youthful, and quintessentially American. The Goodyear tire brand might be seen as performance-driven, affordable, and reliable. A logo, advertising messages, public perception, celebrity endorsements, promotional strategies, and other factors all play a part in promoting a company's particular brand.

Branding is often less about a product's actual benefits or value, and more about how it positions itself within its target market and connects with its loyal customers. Establishing a brand at a company's inception is more challenging than managing a brand that has been present for many years. In the case of a start-up, the initiatives undertaken must be customer centric and should speak directly to the heart of the consumer. These must have a trustworthy and emotional appeal to create a bond with the customer. Let's delve deeper into this.

Customer-Focused Branding

The image a company conveys to its customers is managed through what is called **brand strategy**, which can include advertising, public relations, customer service, and sales promotions.

One common branding strategy is the use of **taglines**, which are short and catchy positioning statements that quickly communicate some core aspect of the brand to the consumer. Taglines can be a powerful tool, and in

some cases can become as recognizable as the brand names themselves. Consider the list of taglines from recent start-ups in Table 8.6. Do they do a good job of communicating the key attributes or benefits of the brand name they are linked to?

Taglines of New Companies

New Companies	Tagline
Hello Fresh	Simply Delicious Meals
Airbnb	Belong Anywhere
Uber	Get There
BirchBox	Open to Beautiful
Snapchat	Life Is More Fun When You Live in the Moment
LuminAID	Makers of Brilliant Things
Uptown Cheapskate	Buy. Sell. Trade.

Table 8.6

Consider the taglines shown in Table 8.7. They have been around for a long time, and most customers are familiar with them. Why do you think these taglines have endured over time?

Taglines of Established Companies

Mature Companies	Taglines That Have Endured Time
Nike	Just Do It
Apple	Think Different
Subway	Eat Fresh
Walmart	Save Money, Live Better
State Farm	Like a Good Neighbor, State Farm Is There
Master Card	There are some things money can't buy. For everything else, there is Mastercard.
Maybelline	Maybe She's Born With It, Maybe It's Maybelline.
Red Bull	Red Bull Gives You Wings
General Electric	Imagination at Work

Table 8.7

Consider, also, how jingles can have a powerful effect on people's recollection of a message. A **jingle** is a very short song or sound that brands a product or company and helps promote it. These tunes are very easy to remember, bold, and fun. Jingles are similar to taglines in that they feature a sound that is catchy and easy to understand by the recipient. Which jingle do you remember off the top of your head?

LINK TO LEARNING

Taglines are not just visual. They can also employ sound. Consider the "Intel Inside" riff or the three notes of NBC's network chime. Sound plays a big role in brand recognition. And jingles are sure bets that entertain as well as forge a connection to a brand. Check out this website for a history lesson in some of the most famous radio and TV commercial jingles (https://openstax.org/l/52Jingles) of all time.

Other components in a brand include the website, social media, customer service, and packaging. These are important components of a branding strategy that use technology to convey the message. A website allows a company to create an image of its business pages that are linked to each other. These pages convey branding information about a company that sends a message to the consumer through the use of the business logo, colors, copy, ease of use, product information, and e-commerce capabilities. The LuminAID website conveys an image and at the same time has important calls to action (https://openstax.org/l/52LuminAID) and serves as an example of successful branding. This site uses colors, images, and fonts that create a specific image of modern lighting that entices customers to purchase the products and other stakeholders to give light to people who need it.

In addition to the ability of a business's website to convey the company's story, social media platforms reinforce the connection to the consumer. Social media platforms such as Facebook, Twitter, Instagram, and YouTube allow companies to invite customers to join the conversation by posting pictures of their use of products, making recommendations, participating in contests and giveaways, and obtaining coupons and other perks. Entrepreneurs have these tools at their disposal to continue creating the image of the business that perhaps got started as a brick-and-mortar business. Today, tools such as Wix, an easy, online website builder, can be used to develop this branding. Entrepreneurs with larger budgets can hire a website designer to create and help promote the site.

Customer service is another tool that can create a strong company image. Training salespeople and cashiers to be courteous, resourceful, and knowledgeable creates an image in the customer's mind about the product and the business. Wearing uniforms can also create a positive image. Customer service is particularly helpful when dealing with services because it gives some tangibility to the product that the customer cannot see. For example, a hairstylist cannot provide a tangible depiction of how a haircut might look on a customer, but the stylist's demeanor, attire, and hair can give the customer clues as to what treatment and results to expect. Packaging is an important component of branding. The design of the package, the color, the information that is conveyed on the package, and the practicality of the package all create an image of what is to be expected from the product.

Method, an environmentally conscious and customer-focused brand of cleaning products, is an example of a company that distinguished itself from the competition by employing effective branding strategies. By using recycled, environmentally friendly packaging and promoting their commitment to using plant-based, nontoxic chemicals, the company was able to attract the attention of, and eventually place their products in, Target stores nationwide.

First, Method convinced Target to use their products to clean their own stores; after a successful test, they convinced the company to carry its line, which includes soaps, detergents, and cleaners (Figure 8.10). Its quirky brand message helped land the account, as Target is a progressive and innovative retailer. The brand message that Method conveyed to them was that everything inside the cleaning bottles was plant-based, and no harsh

chemicals were used in creating the product. The products were either as or more effective than leading brands. In this case, the brand message conveyed the mission of the company in all of its products by integrating all the aspects together in a simple manner through the use of clear bottles, quirky fonts, and (nontoxic) colored liquid.

Figure 8.10 Method's quirky packaging, design, and plant-based ingredients were all part of its successful brand strategy. (credit: work by Carol Bleistine/Flickr, CC BY 4.0)

The benefits of developing a good brand are several. A brand is the image of a product or service that conveys to customers who when they purchase from a particular brand, they will receive the value (quality, price, and experience) they expect. The next time they see that brand, they will choose it again because their previous expectations were met, simplifying their buying-decision process. New products must also break through crowded marketplaces and be visible to consumers who already have an attachment to other brands.

Trust in a brand can save the consumer time and may create an emotional connection to the company. However, not all benefits work for all brands and all purchase decisions. When a customer is purchasing low-commitment products and services, like cleaning products, the decision process can be quick and heuristic. When purchasing more expensive items such as electronics, vehicles, or vacations, the brand is just one of many attributes the consumer will consider.

Defining and Developing a Brand

A brand should have a clear purpose derived from the company's mission. If the purpose is to provide plant-based cleaners that are not harmful to people, pets, or the environment, as in the case of Method, then the brand must communicate this throughout all of its interactions with its consumers. The unique selling proposition, as described in Identifying Entrepreneurial Opportunity, benefits, qualities, and overall image should be conveyed throughout the marketing mix to tell a story. In addition, the brand should have a well-designed logo, the company/product name, merchandise, promotional items, location of the business (that also provides an image or tells a story), and any other tools that communicate with buyers.

Keep in mind that there are differences in branding regarding business size and type. When starting a business, it is likely that you will brand your entire business with one logo, one name, and matching promotional items, business cards, and product packaging. As your number of products grows, you would likely develop different packaging and different images for other product categories.

Figure 8.11 provides a checklist of items that help develop a brand for your venture.

Branding Checklist
1. Develop value proposition based on mission and personality of business
2. Know target market and its identity cues
3. Craft positioning statement and develop tagline
4. Integrate marketing mix
5. Create logo, stationery, and promotional materials
6. Develop website and social media
7. Create related content
8. Monitor brand

Figure 8.11 When starting a business venture, following a few key steps will help in establishing a strong brand. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Promotion through Brand Advocacy

One way to promote your brand is to identify loyal customers who are willing to share positive feedback about it. A **brand advocate** is someone who is a fan of your products and passes on the word to others. Brand advocacy is a potentially inexpensive means of building a brand and one that entrepreneurs should explore. One simple way to motivate brand advocacy is by asking your best customers and fans to refer other customers to you, leave online reviews, and/or to blog or comment about your company and products online. Companies often offer discounts and promotional codes to encourage brand advocates to spread the word.

The key to effective brand advocacy is to know the goal of your advocacy campaign, look for ambassadors (there are many online and in-person events), ask them to perform a task, and reward them for doing so.

An example of advocacy branding is to create a contest to engage consumers who love your product so they can share pictures on social media. IKEA did this in 2016, when it started a contest to win a personalized wardrobe using the hashtag #JoyOfStorage to entice its most loyal fans to share their IKEA products online. The contest asked customers to post pictures of their IKEA products on Facebook (Figure 8.12). This campaign allowed IKEA to engage and reward loyal customers in a fun way, while also using word-of-mouth marketing to expand their marketing reach.

Figure 8.12 The IKEA #JoyofStorage contest engaged loyal fans and rewarded them for being brand advocates. (credit: work by this_could_be_my_house/Flickr, CC BY 2.0)

WORK IT OUT

Forever 21

After living in Los Angeles for a few years, South Korean natives Jin Sook and Do Wong Chang decided to open a clothing store. They named it Fashion 21. The store became a success, bringing in over $700,000 in revenue in 1984. Next, they decided to open new stores twice a year while at the same time changing the name of the store from Fashion 21 to Forever 21, expanding their brand globally. While the stores have historically generated over $3 billion in annual sales, the retailer recently filed for bankruptcy, citing struggles to pay vendors and landlords. The filing comes along with the closing of 178 underperforming US stores and allows Forever 21 to "simplify things so we can get back to doing what we do best."[15]

Bankruptcy aside, Sook and Chang have remained at the helm of the company and their children are also in management, one working in marketing and the other in branding. Branding helps the company remain relevant to its youth segment by positioning itself as trendy, innovative, and particularly adaptive to ever-changing tastes in fashion. The company uses its logo, retail stores, and website to showcase its trendy image.

Forever 21 has been sued several times for copyright infringement, as the essence of the company is to provide fashion looks inspired by runway designs but offered at a lower price point. Forever 21 has a long history of settling copyright suits, including a case involving H&M. It has been in legal battles with Adidas, Puma, and Gucci as well.

- If you were the branding manager, how would you prevent these suits from happening?
- How would you develop a better image of the company?

8.5 Marketing Strategy and the Marketing Plan

Learning Objectives

By the end of this section, you will be able to:

- Distinguish between a marketing strategy, a marketing plan, and a pitch
- Describe the elements of a marketing plan

Now that you have a better idea of what marketing is, you are ready to start developing a marketing strategy and plan. A **marketing strategy** describes how a company will reach consumers and convert them into paying customers. Having a solid-yet-flexible marketing strategy is a good business practice, no matter what kind of business you are in.

A **marketing plan** is a formal business document that is used as a blueprint or guide for how a company will achieve its marketing goals. A marketing plan differs from a business plan in that it focuses more on market research, attracting customers, and marketing strategies, whereas the business plan covers much more than that, as you will see in Business Model and Plan.

Marketing plans are important tools because they act as roadmaps for everyone involved in an enterprise. Writing a marketing plan forces you to specify goals and develop strategies to reach them, and encourages you to research markets and competition. A strong marketing plan will encourage entrepreneurs to think deeply about their business and profit potential, helping them make better business and marketing decisions. Additionally, a marketing plan can create greater involvement and cohesiveness among employees by clarifying goals and expectations.

15 Erica Gonzales. "Forever 21 Has Officially Filed for Bankruptcy." *Harpers Bazaar*, September 30, 2019. https://www.harpersbazaar.com/fashion/trends/a28849065/forever-21-bankruptcy/

A variety of marketing plan templates are available that can be modified to fit your business's product and/or services. One thing to consider is why you are writing your plan and who your audience is. In addition to planning for your venture, will it be used by employees or potential investors? Different audiences will require different kinds of information. If it's an employee, then you must include extra details about the operation of the business. If the plan is geared toward acquiring an investor, be sure to highlight the value that will be gained from investing.

Keep in mind that the various parts of a plan do not need to be written in a certain order. Plans should also be seen as flexible guides rather than absolute rules. All good marketing plans are living, breathing documents that help you measure success while allowing for course corrections when necessary. Table 8.8 provides the standard components of a marketing plan.

Sample Marketing Plan Sample

Marketing Plan Section	Description and Purpose
Executive Summary	Provides a snapshot of the whole plan, including profit potential and major strategic ideas
Situation Analysis	Overviews internal and external environments related to the business and product; internal environments include company background and mission; external environments can include market needs, competition, market research, and an analysis of strengths, weaknesses, opportunities, and threats (SWOT)
Marketing Opportunity (Unmet Need, Proposed Solution, Value Proposition)	Validates the market opportunity being exploited by the business and articulates the potential gain for stakeholders
Business Model	Presents the framework for generation of sales and the business's competitive advantage
Marketing Objectives	Specifies goals for sales (in units or dollars), market share growth, brand awareness, secured distribution channels, inventory, and pricing
Marketing Strategies	Explains target market, projected positioning, and strategies as they relate to the marketing mix (7Ps)
Action Program	Defines who will do what and when
Financials	Discloses sales estimates, projected budgets, and financials that will help readers understand the present and future economic condition of the company
Control Procedures	Describes procedures for measuring results, monitoring goals, and adapting the plan as needed

Table 8.8

Executive Summary

The **executive summary** is just that—a clear and concise summary of the major points of your marketing plan. Though it is placed first, it is generally written last because it is based on the information presented in other subsequent sections.

The executive summary is typically one or two pages long and includes key indicators of success for the business and its stakeholders, which may include company owners, managers, consultants, investors, and banks. Your goal is not merely to summarize everything in your plan but to highlight why people should be interested in your venture. Whether the reader is an employee or a potential partner or investor, the executive summary should seek to not only inform but to excite.

Focusing on the opportunity at hand, what makes your business model special, and the potential financial reward is a good way to capture a reader's attention. For example, if your business' strengths include a great marketing team and a significant competitive advantage, you should highlight them as reasons for success. Some readers may only read this section, so make sure you highlight what makes your company special and how you plan on turning that into profit.

Situation Analysis

In many ways, the basis of your marketing plan is found in your **situation analysis**, which is an examination of the internal and external circumstances relevant to your business and product. A good analysis will provide the logical support for the strategies you choose. For example, the research you conduct here explains why you will develop a certain product, how you will price it, and what you will do to reach your target market.

Good situation analyses often include a SWOT analysis, which looks at a company's strengths, weaknesses, opportunities, and threats. They also look at future and current competitors, and include market validation research that has surveyed potential customers. This information is critical because it proves that you have done your due diligence on your product and market.

Marketing Opportunity

Assuming your background research has led you to determine that there is a business opportunity, this is where you explain what and where that opportunity is. For example, if your research led you to discover a gap in the market for educational children's toys, this is where you explain the depth of the opportunity. Here you use your research as evidence to prove to your reader that there is a market gap and that you know how to fill it. If your goal is to get an investor interested, this is where you would let them know what they stand to gain and when they would gain that.

LINK TO LEARNING

The US Small Business Administration (https://openstax.org/l/52SBAMarketing) strives to help business owners initiate and succeed in developing enterprises. Their website is loaded with helpful information, classes, and templates that can help the entrepreneur navigate the intricacies of marketing, as well as provides helpful tips on developing a marketing plan.

Business Model

In this section, your job is to marry the opportunity you saw with the solution you have created. Here you articulate how your competitive advantage and points of differentiation (nature of the solution and its key features and benefits) will provide value to customers and earn profits that will sustain your business into the foreseeable future. What will you do to create value that attracts customers? How will you generate sales? Who is your target market? If you were opening a gym, this is where you would lay out how you will capture customers, the value they will receive, what types of membership contracts will be available to them, and so

on.

A great tool for capturing this information is the Business Model Canvas (Figure 8.13), which is discussed in Launch for Growth to Success and Business Model and Plan. The nine building blocks of this model will help you to determine the targeted customer segment, value proposition that you will present each of your segments, channels for the distribution of the proposition or touchpoints, type of customer relationship you will build with your target, types of cost structures and revenue streams based on pricing means, and key resources, activities, and partners that will help you to succeed.

The canvas also allows the entrepreneur to innovate and to change if something doesn't work out. The point of this tool is to put the pieces of a plan together.[16]

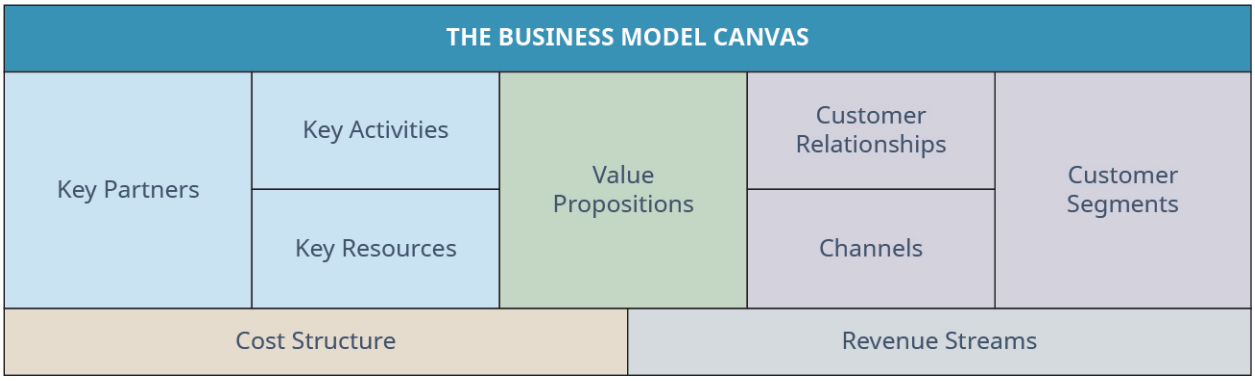


Figure 8.13 A business model canvas brings together key strategies about the product being launched. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Marketing Objectives

Here you present your specific goals and their tangible outcomes. It is not enough to say that you will be very successful without defining what exactly success means. The point of this section is to quantify your goals as units sold, sales/revenue, market share, or some other practical metric. Goals can also include creating measurable brand awareness and developing a certain number of distribution channels.

For example, good, measurable goals might be selling 300 units per month, selling $600,000 worth of product in a year, or gaining brand awareness of 10 percent of your target market in three months. Avoid goals that are unmeasurable or vague, as they won't help you now or later.

No matter what your goals are, they should be reasonably achievable and as specific as possible. The reason for this is so that later on, you can determine whether you have been successful. If you haven't, you will know something needs to change.

Marketing Strategies

As mentioned earlier, having a good marketing mix will help your business succeed. As an entrepreneur, you want to segment the market and figure out if there are possible pockets of people whom you can serve. The process of segmenting, targeting, and positioning (STP) will help you figure out who is your best customer and allow you to allocate your resources effectively to serve that market.

After going through this process, you can look at the marketing mix, and depending on whether you have a product, service, or a mixture of both, which is usually the case, you will outline your approach to the 7Ps of the marketing mix.

Action Plan

In the action plan, you detail how things will get done in your business on a day-to-day basis, when they will get done, and who will be doing them. Often, new business owners develop extensive strategies, but they

16 "The Business Model Canvas." *Strategyzer*. n.d. https://strategyzer.com/canvas/business-model-canvas

don't have the people power to implement them. Obviously, ensuring that you have the necessary human resources in place to execute your goals is important. This is the section where you make it clear that you do. For example, if you have a marketing team in place, highlighting their ability to execute your plans will help convince potential investors that you can put your plan into action.

Financials

Here you include budgets, forecasts, and any other information that will give readers and potential investors a clear picture of your business's financial situation. Being transparent and truthful will create trust and goodwill between your company and potential investors.

This section is also important because it will help you determine how profitable your business might be. One place to start is by determining your expenses and future profits. Since most entrepreneurs tend to overestimate these numbers, it is best to develop financial projections for best- and worst-case scenarios, as well as a projection for an average case scenario.

Many entrepreneurs develop one-, three-, or five-year projections to get a sense of future profits and to prove that their business model is sustainable over the long run. Figure 8.14 provides an example.

5-Year Financial Projections: Sammy's Grocery Store					
	2018	2019	2020	2021	2022
Sales/Revenue	$100,000	$150,000	$170,000	$190,000	$198,000
Cost of Goods Sold	$ 30,000	$ 50,000	$ 55,000	$ 57,000	$ 60,000
Sales and Administrative Expenses	$ 40,000	$ 55,000	$ 60,000	$ 60,000	$ 70,000
Depreciation	$ 10,000	$ 7,000	$ 8,000	$ 8,000	$ 10,000
Operating Profit	$ 20,000	$ 38,000	$ 47,000	$ 65,000	$ 58,000

Figure 8.14 Growth projections appear in the financial section of the marketing plan. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Key Performance Indicators

Finally, you need to determine your key performance indicators, or how you will evaluate the effectiveness of your strategies, by looking at the progress you have made during a specific timeframe. These include the quantitative milestones that will tell you if you are on the right track, help you analyze your decision-making process and focus on specific strategies, and make changes if these don't work.

For example, one of your milestones might be a sales goal of $50,000 within the first six months. If you are not on track by the time you hit this milestone, it can be an indication that you either overestimated your sales or your strategies are not working. In either case, you will need to make actionable steps to revise your projections or find more effective strategies.

8.6 Sales and Customer Service

Learning Objectives

By the end of this section, you will be able to:

- Explain the importance of sales strategy and provide an example
- Explain the importance of customer service

A **sales strategy** is a plan that the entrepreneur uses to identify and engage a consumer, from prospecting to securing the sale. This strategy should keep in mind the core benefit or competitive advantage that the product or service has and make sure this information filters through the entire sales execution process. The strategy should include a six-step process that is an integrated sales system for how to prospect, pitch, handle rejections, and the like.

Setting objectives is important before reaching out to prospects and current customers because they allow the salesperson to detail the strategy, have an end goal, and measure the results. For example, a salesperson may have a goal of closing one client out of ten prospects he or she sees per week (or through a sales cycle). So the detailed strategy would be:

1. doing research about prospective clients and creating a list,
2. calling them to set up an appointment to talk about your product or service,
3. meeting with them to present a proposal,
4. handling objections,
5. closing the deal, and
6. nurturing the relationship after close.

The end goal would be to gain a prospect as a client and develop a good relationship for future business. And the salesperson would measure the results by looking back at goals and outcomes.

There are many methods, tools, and techniques to sell, and there is no perfect set of strategies for a business. It depends on the goals and resources of the entrepreneur, as well as on the type of product they are launching. When selling to customers who are going to be spending a substantial amount on a product or service, like a piece of equipment, a luxury yacht, or an expensive software program, there must be a sales system in place to take consumers from prospects to customers. The preceding six steps are general stages in this system. Let's take a look at each step.

Sample Six-Step Sales Strategy

Figure 8.15 outlines an example of an effective sales system or strategy using a six-step approach.[17]

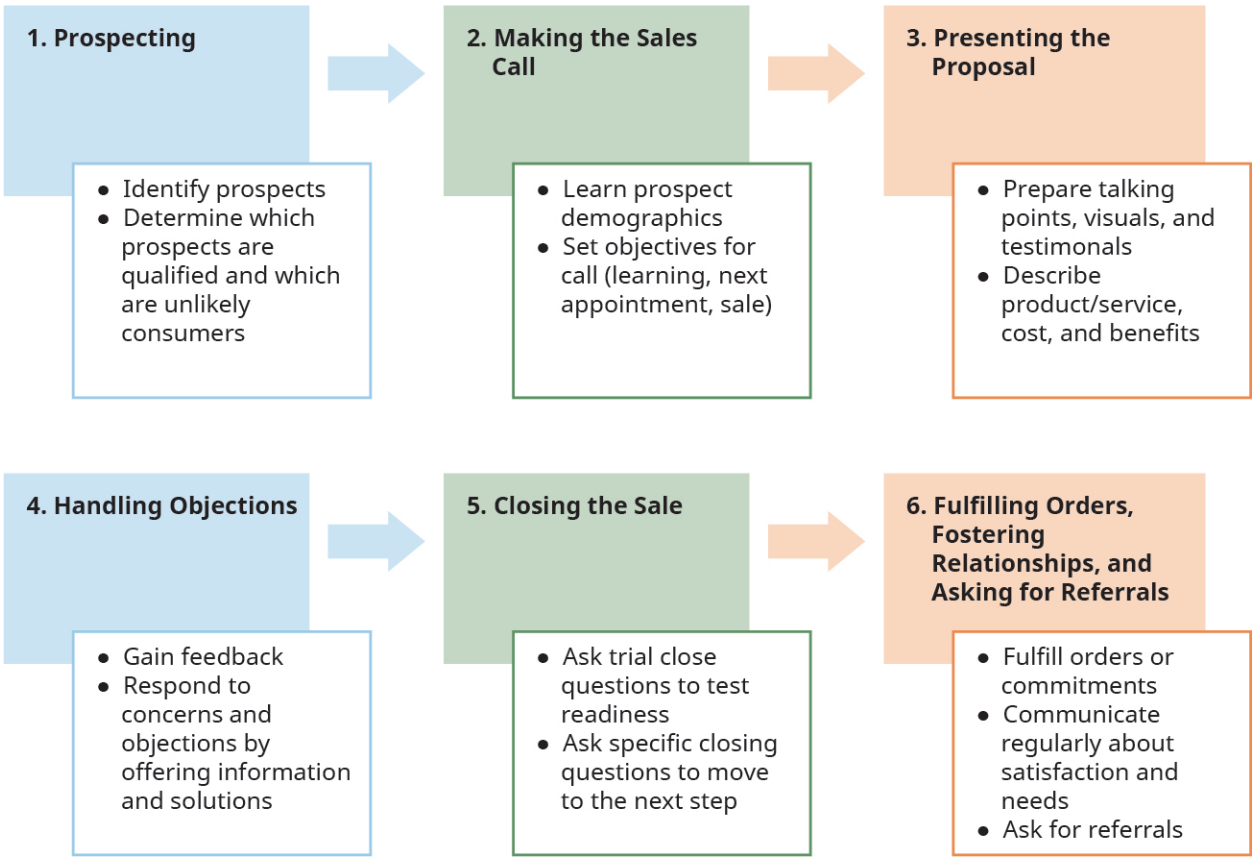


Figure 8.15 The six-step sales process does not end with the sale but with a positive customer relationship. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

17 Stephen Castleberry and John Tanner. *Selling: Building Partnerships*. New York: McGraw-Hill, 2019.

Prospecting and Preparing

Prospecting focuses on finding potential new customers for the product or service. This helps acquire new customers, replace customers lost to attrition, and expand sales from current customers. In essence, prospecting allows salespeople to collect information about potential customers and identify any who are not a good fit for the company. It is important to get as many prospects as possible to secure a few customers, as the pool of prospects diminishes through successive steps of the sales process.

You may need to have a list of twenty prospects to secure one or two customers. Prospecting also tends to be more important in certain industries such as financial advising or business-to-business industries. To determine whether a person or organization is a qualified prospect, the salesperson must consider several issues, such as whether this person/business needs my product or service, and if they can afford it.

Making the Sales Call

The next step of the sales system is to prepare for a sales call, contact, or meeting with a prospect. Effective sales people usually prepare well in advance of contacting a prospect. A salesperson can look for information regarding the company's demographics, its competition, clients, and other companies they purchase from. Information can be gathered from online sources or referrals. It is also helpful to set objectives before contacting the prospect. Some of those objectives can include securing an appointment for a presentation, understanding the prospect better, scheduling a second call/contact, or perhaps starting a sale.

LINK TO LEARNING

Neil Rackham wrote a book in 1998 called *Spin Selling*. It's a classic in the sales world. In it, he outlined a new way to approach winning big sales deals. SPIN stands for situation, problem, implication, and need payoff. Visit the SPIN site (https://openstax.org/l/52SPIN) to learn about Rackham's nontraditional approach to sales and the main principles he advocated.

Presenting the Proposal

Once the salesperson has made a connection with a prospect and understands the prospect's needs, the next step is to meet with the prospect for a sales presentation. A presentation is a great way to expand the prospect's understanding about the offering. Strong presentations include good communication skills with strong visuals and testimonials. In this step, the salesperson can make a better case for the value proposition, citing the strengths of the product and how those strengths would help the prospect in their life or how it would help a company's objectives. The presentation can also include the cost of the investment and a projection of the return on investment. In the case of a financial advisor, a presentation at a prospect's home would show the potential products that the prospect might invest in, such as a variety of retirement accounts, life insurance, a college savings plan, or long-term care insurance, along with the costs and benefits of each. In the case of a business, the presentation could take place at the prospect's office, and the meeting could include a slide presentation about a piece of equipment, with video showing how it is used and how it can benefit the company, including cost savings.

Handling Objections

During or after the presentation, a salesperson will likely encounter objections or questions from the prospect. This is a good way for the salesperson to gain feedback and respond to concerns from the prospect. Objections can arise during the appointment setting, during the presentation, or while trying to close the sale. The salesperson must be proficient at dealing with these in a truthful manner so the relationship that is established is based on trust. Some of those objections can include cost concerns, credit capabilities, product benefits, or plain rejection of the product. In this case, the financial advisor could answer questions about the potential benefits of one type of insurance over another, or handle objections on the monthly payment plan. If

dealing with a company, these questions can take the form of credit opportunities and amount of cost savings in comparison to a competitor.

Closing the Sale

Once the presentation and objections are handled, the next step is to **close**, or ask for the sale. This is as important as being prepared to present and handle objections because it signals to the prospect that the product is a good fit and the relationship can be created. A good closing includes a trustworthy and logical process. Doing a trial close by asking "How is this so far?" or "Can I answer anything else?" can help the customer feel more at ease with making a decision. The customer will help set the pace for a final closing. Then, the salesperson can set up the next steps or ask the following questions: "Can I place the order for you?" "Can we open the life insurance account for you?" "Can you come see the demonstration at our office?" "Can we meet next week for the financial terms?"

Fulfilling Orders, Fostering Relationships, and Asking for Referrals

Finally, the salesperson must fulfill the order and make sure that the customer is satisfied with the product or service. The salesperson, in the end, is the one who is the main contact for the customer and therefore is responsible for the fulfillment of a correct order. The order needs to be closely monitored in case there are any delays or issues with it, so the customer can be immediately notified. The process of the order fulfillment has to be monitored until it is fulfilled. Software has now made it easier to keep track of these orders, so the salesperson can spend more time selling and less time on the order process. Customer relationship management tools such as Salesforce (https://www.salesforce.com/crm/) can help a small entrepreneur or a larger business keep track of its customers, their orders, troubleshooting, and strategies for cost effectiveness.

Building a direct relationship with the customer is also important; therefore, calls or emails to check in consistently is important to assess customer satisfaction and t build the relationship bridge to ask for referrals. Customer retention is more important than ever, as even a small percentage of customers can make up the majority of your sales. Wooing new customers is 5 percent more expensive than keeping your current ones, and in the long run, those who are your VIPs will generate most of your sales.[18] Research shows that retaining even 5 percent of your current customers can generate anywhere from 25 percent to 95 percent of your sales.[19]

Customer Service

One of the most important aspects of making the sale, and one that often wins or loses customers, is customer service. If you have ever stepped into a business where you have been greeted with a smile and treated kindly throughout the purchase process, you will probably want to come back and purchase from that store or salesperson again. However, if the sales associate is rude and doesn't help you find what you need, chances are you will not return to the store a second time. For start-ups, customer service can be an advantage, as the business can focus on a few customers at a time in a more personal manner. The bigger a company is, the harder it is to manage many customers and sales associates on a personal level.

According to Hubspot's top statistics on customer service, 70 percent of the customer experience or journey depends on how they are being treated. The majority of customers fall in love with a brand and are willing to pay a premium for amazing customer service, and they feel that great customer service is more important than price. They will also share positive experiences with other people—an average of eleven, according to Hubspot.[20] When a customer has a negative experience, or feels unappreciated, they are more likely to switch brands, and a company has to work harder to counteract a negative experience. It takes twelve positive reviews to counteract just one negative, unresolved customer issue.[21]

18 Matt Mansfield. "Customer Retention Statistics: The Ultimate Collection for Small Business." *Small Business Trends*. August 22, 2019. https://smallbiztrends.com/2016/10/customer-retention-statistics.html
19 Jia Wertz. "Don't Spend 5 Times More Attracting New Customers, Nurture the Existing Ones." *Forbes*. September 12, 2018. https://www.forbes.com/sites/jiawertz/2018/09/12/dont-spend-5-times-more-attracting-new-customers-nurture-the-existing-ones/#723fd9e15a8e

As an entrepreneur, focusing on customer service before and after the purchase is an effective reminder that the company is trying to build trust and have a relationship with its customers. This also helps with the process of branding, as you've learned. Even in business-to-business sales transactions, the most important aspect of the sales process is building that trust relationship so the customer purchases from a "friend" again. Often when companies lose accounts, it is due to a change in sales personnel and the loss of the associated relationship.

One effective way to ensure great customer service is to create an operating manual for your employees that includes proper techniques for customer service. These techniques can include how to greet a customer, how to listen and help them get what they need, the philosophy of your company, how far to go when insuring great service, and how to be creative with customer service. Employees can review the manual when they are hired, and every year after that to ensure they continue to follow the procedures. Training programs before starting work and during the year can be facilitated by the entrepreneur or a consultant to sharpen the skills of the employees. These programs are a great way to energize salespeople to be more people oriented and to develop the proper attitude and positive thinking that is required when helping customers. Sales training programs are a great way to learn more about customer service. Zig Ziglar and Dr. Cialdini programs are designed with the salesperson in mind.

Also, when hiring, focus on candidates who already have customer service experience and those who come with good referrals. Incentives for great customer service such as an employee of the month/year award or financial incentives can also encourage employees to provide great service. Finally, the entrepreneur and any administrators are the leaders of a company who must show the same customer service to their employees. Walk the talk! If they realize that they are there to serve their employees and enable them to create a great customer service atmosphere, then the employees will share the same enthusiasm and energy toward their customers. Happy employees turn into profitable customers. Figure 8.16 shows a quick checklist for beginning entrepreneurs.

Customer Service Checklist for Beginning Entrepreneurs
1. Develop guidelines or an operation manual for how to handle customer service. 2. Train employees before and during their employment. 3. Hire employees with great customer service experience or those with the potential to learn. 4. Provide incentives such as awards and prizes. 5. Walk the talk! Provide great customer service to your employees. Your attitude and disposition matter and your employees will follow you if they feel appreciated.

Figure 8.16 The quality of customer service can make or break a company. Following a few basic steps can ensure great customer service. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Customer service doesn't happen just in person or on the phone. Technology has enabled people and companies to connect through email and social media, taking the conversation and interaction online. Customers can now talk to the company employees, voice their concerns, and get issues resolve through these avenues. These technological advances have provided a bigger platform for customers to rave about companies or complain about them.[22] This love or dislike can translate into social media posts, tweets, pictures, videos, and reviews for thousands or millions of people to see and can help or tarnish a company.

20 Swetha Amaresan. "31 Customer Service Stats to Know in 2019." *HubSpot*. March 19, 2019. https://blog.hubspot.com/service/customer-service-stats
21 Swetha Amaresan. "31 Customer Service Stats to Know in 2019." *HubSpot*. March 19, 2019. https://blog.hubspot.com/service/customer-service-stats
22 Liz Greene. "Social Media Is a Customer Service Channel Whether You Like It or Not." *Digital Marketing Institute*. n.d. https://digitalmarketinginstitute.com/en-us/blog/social-media-is-a-customer-service-channel-whether-you-like-it-or-not

Key Terms

advertising mass communication that allows companies to reach a broad audience through TV, radio, newspaper, Internet, magazines, and outdoor ads

brand image a company promotes and the connotations it fosters of itself and its products

brand advocate someone who is a fan of your products and passes on the word to others

brand strategy image a company conveys to its customers

bundling bundle of products that is discounted to encourage customers to buy in bulk

causal research identification of cause-and effect-relationships between two or more variables

close step in the sales process in which the salesperson asks for and gets the sale

conjoint analysis survey tool in which respondents must rank, choose, or a rate a number of "conjoint," or linked, features or benefits

cost-led pricing easiest way to price a product by taking the cost of making the product and marking it up to create profit

customer-led pricing pricing led by what the customer is willing to pay

digital marketing online marketing

direct mail connecting to consumers via email or through printed mailed pieces

entrepreneurial marketing set of unconventional practices that can help start-ups and younger firms survive in competitive markets

ethnographic research use of personal observation of the subject by being immersed in the subject's environment

executive summary initial section of a business plan document that summarizes the key elements of the entire plan

expeditionary marketing marketing designed to move established companies and their products into new markets and territories

focus group gathering of people, typically six to twelve participants, who come together to discuss a topic presented by a moderator, who usually poses questions and collects qualitative data that can be used to answer questions or define research further

guerrilla marketing creative approaches to marketing that seek to gain maximum exposure through unconventional means

introductory offers using lower initial prices to attract new customers and build a customer base before prices return to their standard amount

jingle short song or sound that brands a product or company and helps to promote it

loss leader pricing using a below-standard price to attract customers in the hope that they will purchase other, more profitable goods and services

market analysis analysis of the overall interest in the product or service within the industry by its target market

market opportunity unmet need within a target demographic

market research collection and analysis of data related to a business's target market

marketing umbrella term given to those activities that companies use to identify consumers and convert them into buyers

marketing mix basic set of possible strategies and approaches that marketers use to reach their target market

marketing plan formal business document that used as blueprint for how a company will achieve its marketing and business goals

marketing strategy company's game plan for how it will reach consumers and convert them into paying customers

odd numbers strategy psychological pricing strategy that uses odd numbers in the prices to make a product's price point more attractive to consumers

penetration pricing pricing below that of a competitor's price

people company's human resources
personal selling using face-to-face interactions to communicate and influence a customer to make a purchase
physical environment where a service takes place or a product is manufactured
place channels or locations—physical or digital—where products can be found by customers
positioning (or value proposition) statement of how you want the customer to perceive your company, good, or service
premium pricing charging a price above a competitor's price
price value that must be exchanged in order for a customer to receive a product or service
primary research research that involves gathering new data
process chain of procedures and/or activities required to provide the product to the customer
product good or a service that creates value by fulfilling a customer need or desire
profit margin amount by which revenue exceeds costs, typically described as a percent
promotion process of communicating value to customers in a way that encourages them to buy
public relations marketing that focuses on connecting with constituents by developing goodwill
qualitative research use of open-ended techniques such as observation, focus groups, and interviews to gain an understanding of customers' basic reasons, opinions, and motivations
quantitative research generation of numerical data through techniques such as surveys and questionnaires
real-time marketing seeks to turn immediately available sales data into actionable and timely strategies that target the shifting landscape of consumer tastes and trends
relationship marketing creates customer loyalty through personal interaction and strives for long-term engagement
sales promotion incentives such as coupons and discounts that help attract customers and help them take action
sales strategy plan that the entrepreneur uses to identify and engage a consumer, from prospecting to securing the sale and beyond
sample group of people participating in market research
secondary research research that uses existing data
segmenting separating the total population by homogeneous groups of people that have similar tastes, backgrounds, lifestyles, demographics, and culture
serviceable available market (SAM) portion of the market that a business can serve based on its products, services, and location
situation analysis examination of the internal and external circumstances relevant to a particular business
skimming high-pricing strategy that leverages the newness of a product in order to "skim" the most profits off the top at the beginning of a sale
social media online communication tool for entrepreneurs to connect with consumers, especially younger demographics
tagline short and catchy positioning statement that quickly communicate some core aspect of the brand to the consumer
target market specific group of consumers for which a company seeks to provide a good or service
targeting selecting a customer group based on their ability and willingness to buy
total available market (TAM) total perceived demand for a product or service within the marketplace
validation act of verifying that a product can be successful with a target audience
viral marketing marketing that uses engaging content in the hopes that viewers will share it on their personal and social media networks
word-of-mouth (WOM) marketing promotion in which a satisfied customer tells others about their positive experience with a good or service

Summary

8.1 Entrepreneurial Marketing and the Marketing Mix

Marketing refers to those activities companies use to identify consumers and convert them into buyers. Entrepreneurial marketing is a set of unconventional practices that can help start-ups and younger firms survive in competitive markets. One way to think of the marketing mix is to break it into the 7Ps: product, promotion, price, place, people, physical environment, and process. Entrepreneurs often don't have deep enough resources to use all of these marketing tools, so they need to be strategic in which ones they choose and how they execute them.

8.2 Market Research, Market Opportunity Recognition, and Target Market

Market research is an important aspect of being an entrepreneur. Research can help you vet ideas as well as reveal opportunities that you may not have seen before. Whether you are using secondary data or performing primary research, it is important to know your research questions and goals. Good market research and analysis can help you position your product within your target market.

8.3 Marketing Techniques and Tools for Entrepreneurs

Marketing doesn't have to be expensive; entrepreneurs have many affordable techniques at their disposal. The only input necessary for these techniques is plenty of passion, creativity, and energy. These tools include guerrilla, relationship, expeditionary, real-time, viral, digital, and WOM marketing. The pros of using these techniques are plenty, as you can see from the examples shared for each of the tools. They include being able to reach many people at the same time; leveraging the timeliness of feedback; and making real, sincere connections with people. In addition, affordability, creativity, and good results (clicks, shares, comments, purchases, and awareness) can stem from using these techniques. On the negative side, customer reviews that are not so positive can also make their way through these channels and damage the reputation of a company if they are not handled with care.

8.4 Entrepreneurial Branding

Branding gives an identity to the product and company to which the customer can identify. It is based on its mission, goals, and product benefits, and it must be integrated with the marketing mix for greater impact. Brands help communicate a message to the consumer about product quality, pricing, and overall benefits. When the communication strategy is not cohesive, the consumer may become confused by the different signals the company sends. The entrepreneur must work hard to create a unified message all the way through.

8.5 Marketing Strategy and the Marketing Plan

Once you have an idea of your marketing mix, the next step is to develop actionable strategies and write them down in a marketing plan. A marketing strategy describes how a company will reach consumers and convert them into paying customers. A marketing plan is a formal business document that is used as a blueprint or guide for how a company will achieve its marketing goals. A good marketing plan can be used to guide internal decisions and attract external investors.

8.6 Sales and Customer Service

Sales drives profit. They may require a simple sales approach or a complicated sales system. An example of a sales system is a six-step sales strategy: doing research about prospective clients and creating a list; making an appointment to talk about your good or service; meeting with them to present a proposal; handling objections; closing the deal; and nurturing the relationship after close. When selling luxury and expensive items, the sales approach is usually more thorough and requires more sales training and finesse. Customer service is a component that is linked to this process and with proper training can really differentiate a

company from the competition.

Review Questions

1. What are the differences between traditional and entrepreneurial marketing?
2. What is a target market? Why is it important to know the target before creating the marketing mix?
3. What are the components of the marketing mix? Explain each component.
4. What is the difference between pricing a product based on what a competitors charge and pricing a product based on the company's costs?
5. Check out the website http://www.flyzipline.com/. Who is the target market? What are their 7Ps?
6. What is market research? Why is it important to do research before you start a business?
7. How does primary data differ from secondary data?
8. How does STP help entrepreneurs?
9. How does guerrilla marketing differ from viral marketing?
10. What types of activities are involved in digital marketing? Choose one and explain.
11. What is a brand? Why is it important to work toward gaining recognition for the brand, especially for a start-up brand?
12. How does a tagline help with positioning?
13. How does a marketing plan help an entrepreneur?
14. What is the difference between a marketing objective and a marketing strategy?
15. What are the steps in the sales process?
16. How does customer service impact sales of a new business?

Discussion Questions

1. If you could open a business right now, what would it be? Who would be your target market?
2. Look at the Wag! website https://wagwalking.com/ and determine the 7Ps of this service. Do they work well together? Why or why not?
3. Give an example of a company that uses bundle pricing and explain why it uses this method.
4. Discuss how market research can benefit entrepreneurs.
5. What is the difference between qualitative and quantitative data?
6. Give examples of how entrepreneurs can leverage marketing activities even when strapped for cash.
7. If you had a business that was highly dependent on WOM marketing, how would you ensure the information passed along was positive? If the message passed along was negative, what would you do about it?
8. Describe how a brand advocate might help IKEA position itself as a cost-effective and design-oriented furniture store. Now discuss how a brand advocate can help a new product on the market establish a good reputation.
9. Discuss how the business model canvas can help an entrepreneur create a framework for generating sales. Think of a business you like and describe how it generates sales.

10. Negative referrals can have a great impact on a company's sales. Remember an instance where you were the source of a bad referral for a product or service, and determine what made the experience so negative. What would you have done differently as the sales person to prevent that?

Case Questions

1. Claire is a young artist who has decided to sell her paintings to make some money while she finishes college. She doesn't know much about promoting her work, especially through online channels. Since you are studying business, she has asked you for your advice on promoting her work to a young professional demographic who would be inspired by her message through the arts. Describe two types of promotional tools she can use to connect with her ultimate customer.

2. You have recently been hired to work as a marketing manager for a boutique hotel in San Diego. This hotel is the only one of its kind and is not part of a chain. It only has 50 rooms that have been carefully designed to fit a younger, eclectic, design oriented, and higher-income demographic. The owner needs help pricing the rooms and other hotel services (see the following). Determine which pricing strategy you would use (customer-led, cost-based, competition-based, premium, etc.) for each of the following items and explain why. If necessary, look at some industry reports on how hotels price their services and decide if you should go the same route or try something else.
   A. Room rate (weekly and weekend)
   B. Restaurant food
   C. Parking
   D. Internet and movie access

3. One of your classmates would like to open a food delivery service in town. This service would allow people to buy lunch or dinner through an app from a list of restaurants. She's in the early stages of her analysis and she is asking your advice on possible sources of data that she can use. What kind of resources would you direct her to? Why?

4. One of your classmates recently opened a new gym in an up and coming professional area. She is an accomplished trainer, but has little experience in business. She asks your help in coming up with a specific target market. You share with her the STP process.

5. Visit the current Birchbox website, its online promotions, social media, online ads, and anything you can find about its digital marketing strategies. If you were in charge of digital marketing for Birchbox, what would you include or delete from their current activities?

6. Visit the Method website at https://methodhome.com/ and describe all of the branding components they use to position themselves as the best cleaning products in the US market.

7. You have recently become a supplier of heavy equipment to manufacturing plants that build automotive components. You have acquired one customer and would like to add more within the next three months. How would you go about prospecting?

Suggested Resources

8.1 Entrepreneurial Marketing and the Marketing Mix

American Marketing Association: https://www.ama.org

Small Business Administration: https://www.sba.gov/

8.3 Marketing Techniques and Tools for Entrepreneurs

AMA Digital Marketing Certification: https://www.ama.org/events-training/Certification/Pages/digital-marketing-certification.aspx

AMA on Demand course: Digital Marketing: Delivering a Custom Experience: https://www.ama.org/events-training/virtual-events/Pages/digital-marketing-virtual-conference-051717.aspx

Google Ads: https://ads.google.com/home/

Google Analytics: https://analytics.google.com/analytics/web/provision/#/provision

Hubspot Google Ads guide: https://blog.hubspot.com/marketing/google-adwords-ppc

8.4 Entrepreneurial Branding

Hubspot's Beginner's guide to branding: https://blog.hubspot.com/agency/develop-brand-identity#.WgSASHcJI2E.mailto

8.5 Marketing Strategy and the Marketing Plan

Business Model Canvas: https://strategyzer.com/canvas/business-model-canvas

Hubspot Marketing Plan templates: https://blog.hubspot.com/marketing/marketing-plan-template-generator

Small Business Administration: https://www.sba.gov/business-guide/manage-your-business/marketing-sales

8.6 Sales and Customer Service

Cialdini online tools: https://www.influenceatwork.com/

Hoffman Sales Training: https://sellhoffman.com/

Neil Rackman: http://neilrackham.com/

Spin Selling: https://blog.hubspot.com/sales/spin-selling-the-ultimate-guide

Zig Ziglar: https://www.ziglar.com/

The State of Customer Service: https://offers.hubspot.com/state-of-customer-service?hubs_post-cta=anchor&hsCtaTracking=9c545446-aacf-47a3-bfb3-1998f78b79c8%7C4f98051f-03f6-4061-9a68-5de8fcbb40c1

Cialdini, R. B. (2001). *Influence: Science and Practice* (4th ed.). Boston: Allyn & Bacon: Explains some aspects of the sales process in a fun and fact-based manner.

9

Entrepreneurial Finance and Accounting

Figure 9.1 An advertisement showcasing the features of the iBackPack.

Chapter Outline

9.1 Overview of Entrepreneurial Finance and Accounting Strategies
9.2 Special Funding Strategies
9.3 Accounting Basics for Entrepreneurs
9.4 Developing Startup Financial Statements and Projections

Introduction

In 2015, Doug Monahan, the CEO and founder of iBackPack of Texas, Inc., introduced a revolutionary technology package encased in a typical backpack. The iBackPack boasted the capacity to incorporate WiFi/MiFi, a battery system, smart power transfer cables, and a car-charging system—while carrying four notebook computers and their accessories. Monahan promised that the iBackPack would be a "communication hub and corresponding electrical powerhouse for students and business professionals alike."[1] To bring the project to market, iBackPack sought crowdfunding through an Indiegogo campaign that raised $723,395 from 4,041 backers. An additional $76,694 was raised from 252 Kickstarter backers.

In 2016, iBackPack raised over $800,000 to fulfill investors' orders, but the product never materialized. The only update from the company was a Facebook post alluding to issues sourcing "safe" batteries. By 2017, the iBackPack crowdfunding campaign failed to deliver the product promised to its investors.[2,3] According to an article on the website The Verge in August 2018, the founders of iBackPack were under investigation by the Federal Trade Commission.[4] Although crowdfunding can be a great option for startups, those who abuse the system may find themselves subject to legal action.

1 "iBackPack Planning Kickstarter Launch on Black Friday." *Cision PR Newswire*. November 24, 2015. http://www.prnewswire.com/news-releases/ibackpack-planning-kickstarter-launch-on-blackfriday-300183934.html
2 Lewis Leong. "Sorry, iBackPack Backers. You Got Scammed." *Crowdtoolz*. January 9, 2017. http://crowdtoolz.com/sorry-ibackpack-backers-you-got-scammed/
3 Kylie McGovern. "Hundreds Still Waiting for Bulletproof 'iBackPack' Delivery a Year Later." *KXAN*. July 13, 2017. http://kxan.com/2017/07/13/hundreds-still-waiting-for-bulletproof-ibackpack-delivery-a-year-later/
4 Ashley Carman. "The FTC Is Investigating a Crowdfunding Campaign That Disappeared with More than $700K." *The Verge*. August 29, 2018. https://www.theverge.com/circuitbreaker/2018/8/29/17793720/ftc-ibackpack-investigation-indiegogo-kickstarter

9.1 Overview of Entrepreneurial Finance and Accounting Strategies

Learning Objectives

By the end of this section, you will be able to:

- Distinguish between financing and accounting
- Describe common financing strategies for different stages of the company lifecycle: personal savings, personal loans, friends and family, crowdfunding, angel investors, venture capitalists, self-sustaining, private equity sales, and initial public offering
- Explain debt and equity financing and the advantages and disadvantages of each

The case of iBackPack demonstrates that entrepreneurial success is not guaranteed simply because a company can secure funds. **Funds** are the necessary capital to get a business, or idea, off the ground. But funding cannot make up for a lack of experience, poor management, or a product with no viable market. Nonetheless, securing funding is one of the first steps, and a very real requirement, for starting a business.

Let's begin by exploring the financial needs and funding considerations for a simple organization. Imagine that you and your college roommate have decided to start your own band. In the past, you have always played in a school band where the school provided the instruments. Thus, you will need to start by purchasing or leasing your own equipment. You and your roommate begin to identify the basic necessities—guitars, drums, microphones, amplifiers, and so on. In your excitement, you begin browsing for these items online, adding to your shopping cart as you select equipment. It doesn't take you long to realize that even the most basic set of equipment could cost several thousand dollars. Do you have this much money available to make the purchase right now? Do you have other funding resources, such as loans or credit? Should you consider leasing most or all of the instruments and equipment? Would family or friends want to invest in your venture? What are the benefits and risks associated with these funding options?

This same basic inquiry and analysis should be completed as part of every business plan. First, you must determine the basic requirements for starting the business. What kinds of equipment will you need? How much labor and what type of skills? What facilities or locations would you require to make this business a reality? Second, how much do these items cost? If you do not possess an amount of money equal to the total anticipated cost, you will need to determine how to fund the excess amount.

ENTREPRENEUR IN ACTION

Ted Herget and Gearhead Outfitters

Gearhead Outfitters, founded by Ted Herget in 1997 in Jonesboro, Arkansas, is a retail chain that sells outdoor gear for men, women, and children. The company's inventory includes clothing, footwear for hiking and running, camping gear, backpacks, and accessories. Herget fell in love with the outdoor lifestyle while working as a ski instructor in Colorado and wanted to bring that feeling back home to Arkansas. And so, Gearhead was born in a small downtown location in Jonesboro. The company has had great success over the years, expanding to numerous locations in Herget's home state, as well as to locations in Louisiana, Oklahoma, and Missouri.

While Herget knew his industry when starting Gearhead, like many entrepreneurs he faced regulatory and financial issues that were new to him. Several of these issues were related to accounting and the wealth of decision-making information that accounting systems provide. For example, measuring revenue and expenses, providing information about cash flow to potential lenders, analyzing whether profit and positive cash flow is sustainable to allow for expansion, and managing inventory levels. Accounting, or the preparation of financial statements (balance sheet, income statement, and statement of cash flows), provides the mechanism for business owners such as Herget to make fundamentally sound business

decisions.

Once a new business plan has been developed or a potential acquisition has been identified, it's time to start thinking about **financing**, which is the process of raising money for an intended purpose. In this case, the purpose is to launch a new business. Typically, those who can provide financing want to be assured that they could, at least potentially, be repaid in a short period of time, which requires a way that investors and business owners can communicate how that financing would happen. This brings us to accounting, which is the system business owners use to summarize, manage, and communicate a business's financial operations and performance. The output of accounting consists of financial statements, discussed in Accounting Basics for Entrepreneurs. Accounting provides a common language that allows business owners to understand and make decisions about their venture that are based on financial data, and enables investors looking at multiple investment options to make easier comparisons and investment decisions.

Entrepreneurial Funding across the Company Lifecycle

An entrepreneur may pursue one or more different types of funding. Identifying the lifecycle stage of the business venture can help entrepreneurs decide which funding opportunities are most appropriate for their situation.

From inception through successful operations, a business's funding grows generally through three stages: seed stage, early stage, and maturity (Figure 9.2). A **seed-stage** company is the earliest point in its lifecycle. It is based on a founder's idea for a new product or service. Nurtured correctly, it will eventually grow into an operational business, much as an acorn can grow into a mighty oak—hence the name "seed" stage. Typically, ventures at this stage are not yet generating revenue, and the founders haven't yet converted their idea into a saleable product. The personal savings of the founder, plus perhaps a few small investments from family members, usually constitute the initial funding of companies at the seed stage. Before an outsider will invest in a business, they will typically expect an entrepreneur to have exhausted what is referred to as F&F financing—friends and family financing—to reduce risk and instill confidence in the business's potential success.

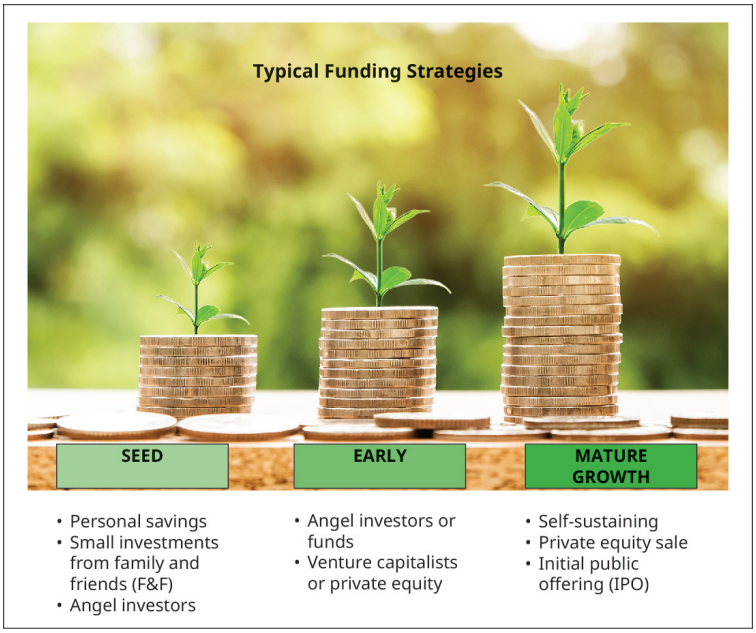


Figure 9.2 Funding strategies can change across different phases of the company lifecycle.

After investments from close personal sources, the business idea may begin to build traction and attract the attention of an angel investor. **Angel investors** are wealthy, private individuals seeking investment options

with a greater potential return than is traditionally expected on publicly traded stocks, albeit with much greater risk. For that reason, they must be investors accredited by the federal Securities and Exchange Commission (SEC) and they must meet a net worth or income test. Nonaccredited investors are allowed in certain limited circumstances to invest in security-based crowdfunding for startup companies. Among the investment opportunities angel investors look at are startup and early stage companies. Angel investors and funds have grown rapidly in the past ten years, and angel groups exist in every state.

An **early stage** company has begun development of its product. It may be a technical proof of concept that still requires adjustments before it is customer ready. It may also be a first-generation model of the product that is securing some sales but requires modifications for large-scale production and manufacturing. At this stage, the company's investors may now include a few outsider investors, including venture capitalists.

A **venture capitalist** is an individual or investment firm that specializes in funding early stage companies. Venture capitalists differ from angel investors in two ways. First, a venture capital firm typically operates as a full-time active investment business, whereas an angel investor may be a retired executive or business owner with significant savings to invest. Additionally, venture capital firms operate at a higher level of sophistication, often specializing in certain industries and with the ability to leverage industry expertise to invest with more know-how. Typically, venture capitalists will invest higher amounts than angel investors, although this trend may be shifting as larger angel groups and "super angels" begin to invest in venture rounds.

Private equity investment is a rapidly growing sector and generally invests later than venture capitalists. Private equity investors either take a public company private or invest in private companies (hence the term "private equity"). The ultimate goals of private equity investors are generally taking a private company public through an initial public offering (IPO) or by adding debt or equity to the company's balance sheet, and helping it improve sales and/or profits in order to sell it to a larger company in its sector.

Companies in the **mature stage** have reached commercial viability. They are operating in the manner described in the business plan: providing value to customers, generating sales, and collecting customer payments in a timely manner. Companies at this stage should be self-sufficient, requiring little to no outside investment to maintain current operations. For a product company, this means manufacturing a product at scale, that is, in very large volumes. For a software company or app provider, this means generating sales of the software or subscriptions under an SaaS model (Software as a Service) and possibly securing advertising revenue from access to the user base.

Companies at the mature stage have different financing needs from those in the previous two stages, where the focus was on building the product and creating a sales/manufacturing infrastructure. Mature companies have reached a consistent level of sales but may seek to expand into new markets or regions. Typically, this requires significant investment because the proposed expansion can often mirror the present level of operations. That is to say, an expansion at this level may result in doubling the size of the business. To access this amount of capital, mature companies may consider selling a portion of the company, either to a private equity group or through an IPO.

An **initial public offering (IPO)** occurs the first time a company offers ownership shares for sale on a public stock exchange, such as the New York Stock Exchange. Before a company executes an IPO, it is considered to be privately held, usually by its founders and other private investors. Once the shares are available to the general public through a stock exchange, the company is considered to be publicly held. This process typically involves an investment banking firm that will guide the company. Investment bankers will solicit institutional investors, such as State Street or Goldman Sachs, which will in turn sell those shares to individual investors. The investment banking firm typically takes a percentage of the funds raised as its fee. The benefit of an IPO is that the company gains access to a massive audience of potential investors. The downside is that the owners give up more ownership in the business and are also subject to many costly regulatory requirements. The IPO process is highly regulated by the SEC, which requires companies to provide comprehensive information up front to potential investors before completing the IPO. These publicly traded companies must also publish

quarterly financial statements, which are required to be audited by an independent accounting firm. Although there are benefits to an IPO for later-stage companies, it can be very costly both at the start and on an ongoing basis. Another risk is that if the company does not meet investors' expectations, the value of the company can decline, which can hinder its future growth options.

Thus, a business's lifecycle stage greatly influences its funding strategies and so does its industry. Different types of industries have different financing needs and opportunities. For example, if you were interested in opening a pizzeria, you would need a physical location, pizza ovens, and furniture so customers could dine there. These requirements translate into monthly rent on a restaurant location and the purchase of physical assets: ovens and furniture. This type of business requires a significantly higher investment in physical equipment than would a service business, such as a website development firm. A website developer could work from home and potentially begin a business with very little investment in physical resources but with a significant investment of their own time. Essentially, the web developer's initial funding requirement would simply be several months' worth of living expenses until the business is self-sufficient.

Once we understand where a business is in its lifecycle and which industry it operates in, we can get a sense of its funding requirements. Business owners can acquire funding through different avenues, each with its own advantages and disadvantages, which we will explore in Special Funding Strategies.

WORK IT OUT

Venture Capitalists

Consider this statement from John Mackey, the CEO of Whole Foods Market: "Venture capitalists are like hitchhikers—hitchhikers with credit cards—and as long as you take them where they want to go, they'll pay for the gas. But, if you don't . . . they will try to hijack the car and they will hire a new driver and throw you out on the road." He spoke on the NPR podcast *How I Built This*.[5]

How would you feel if the investors in the company you founded started trying to wrest control of the organization from you? What steps would you take to prepare for this situation?

Types of Financing

Although many types of individuals and organizations can provide funds to a business, these funds typically fall into two main categories: debt and equity financing (Table 9.1). Entrepreneurs should consider the advantages and disadvantages of each type as they determine which sources to pursue in support of their venture's immediate and long-term goals.

Debt vs. Equity Financing

	Debt Financing	Equity Financing
Ownership	Lender does not own stake in company	Lender owns stake in company
Cash	Requires early and regular cash outflow	No immediate cash outflow

Table 9.1

5 "Whole Foods Market: John Mackey." *How I Built This* (NPR Podcast). May 15, 2017. https://www.npr.org/2017/06/30/527979061/whole-foods-market-john-mackey

Debt Financing

Debt financing is the process of borrowing funds from another party. Ultimately, this money must be repaid to the lender, usually with interest (the fee for borrowing someone else's money). Debt financing may be secured from many sources: banks, credit cards, or family and friends, to name a few. The maturity date of the debt (when it must be repaid in full), the payment amounts and schedule over the period from securement to maturity, and the interest rate can vary widely among loans and sources. You should weigh all of these elements when considering financing.

The advantage of debt financing is that the debtor pays back a specific amount. When repaid, the creditor releases all claims to its ownership in the business. The disadvantage is that repayment of the loan typically begins immediately or after a short grace period, so the startup is faced with a fairly quick cash outflow requirement, which can be challenging.

One source of debt financing for entrepreneurs is the Small Business Administration (SBA), a government agency founded as part of the Small Business Act of 1963, whose mission is to "aid, counsel, assist and protect, insofar as is possible, the interests of small business concerns."[6] The SBA partners with lending institutions such as banks and credit unions to guarantee loans for small businesses. The SBA typically guarantees up to 85 percent of the amount loaned. Whereas banks are traditionally wary of lending to new businesses because they are unproven, the SBA guarantee takes on some of the risk that the bank would normally be exposed to, providing more incentive to the lending institution to finance an entrepreneurial venture.

To illustrate an SBA loan, let's consider the 7(a) Small Loan program. Loans backed by the SBA typically fall into one of two categories: working capital and fixed assets. **Working capital** is simply the funds a business has available for day-to-day operations. If a business has only enough money to pay bills that are currently due, that means it has no working capital—a precarious position for a business to be in. Thus, a business in this position may want to secure a loan to help see it through leaner times. **Fixed assets** are major purchases—land, buildings, equipment, and so on. The amounts required for fixed assets would be significantly higher than a working capital loan, which might cover just a few months' expenses. As we will see, loan requirements made under the 7(a) Small Loan program are based on loan amounts.

For loans over $25,000, the SBA requires lenders to demand collateral. **Collateral** is something of value that a business owner pledges to secure a loan, meaning that the bank has something to take if the owner cannot repay the loan. Thus, in approving a larger loan, a bank might ask you to offer your home or other investments to secure the loan. In a real estate loan, the property you are buying is the collateral. In a way, loans for larger purchases can be less risky for a bank, but this can vary widely from property to property. A loan that does not require collateral is referred to as unsecured.

To see how a business owner might use an SBA loan, let's return to the example of a pizzeria. Not all businesses own the buildings where they operate; in fact, a great many businesses simply rent their space from a landlord. In this case, a smaller loan would be needed than if the business owner were buying a building. If the prospective pizzeria owner could identify a location available for rent that had previously been a restaurant, they might need only to make superficial improvements before opening to customers. This is a case where the smaller, collateral-free type of SBA loan would make sense. Some of the funds would be allocated for improvements, such as fresh paint, furniture, and signage. The rest could be used to pay employees or rent until the pizzeria has sufficient customer sales to cover costs.

In addition to smaller loans, this SBA program also allows for loans up to $350,000. Above the $25,000 threshold, the lending bank must follow its own established collateral procedures. It can be difficult for a new business to provide collateral for a larger loan if it does not have significant assets to secure the loan. For this reason, many SBA loans include the purchase of real estate. Real estate tends to be readily accepted as collateral because it cannot be moved and holds it value from year to year. For the pizzeria, an aspiring

6 Small Business Administration (SBA). "Mission." n.d. https://www.sba.gov/about-sba/what-we-do/authority

business owner could take advantage of this higher level of lending in a situation where the business is buying the property where the pizzeria will be. In this case, the majority of loan proceeds will likely go toward the purchase price of the property. Both the high and low tiers of the SBA loan program are examples of debt financing. In Special Funding Strategies, we will look at how debt financing differs from equity financing.

Equity Financing

In terms of investment opportunities, equity investments are those that involve purchasing an ownership stake in a company, usually through shares of stock in a corporation. Unlike debts that will be repaid and thus provide closure to the investment, **equity financing** is financing provided in exchange for part ownership in the business. Like debt financing, equity financing can come from many different sources, including friends and family, or more sophisticated investors. You may have seen this type of financing on the TV show *Shark Tank*. Contestants on the series pitch a new business idea in order to raise money to start or expand their business. If the "sharks" (investors) want to invest in the idea, they will make an offer in exchange for an ownership stake. For example, they might offer to give the entrepreneur $200,000 for a return of 40 percent ownership of the business.

The advantage of equity financing is that there is no immediate cash flow requirement to repay the funds, as there is with debt financing. The drawback of equity financing is that the investor in our example is entitled to 40 percent of the profits for all future years unless the business owner repurchases the ownership interest, typically at a much higher **valuation**—an estimate of worth, usually described in relation to the price an investor would pay to acquire the entire company.

This is illustrated in the real-life example of the ride-sharing company Uber. One of the early investors in the company was Benchmark Capital. In the initial round of (venture capital) financing, Benchmark invested $12 million in Uber in exchange for stock. That stock, as of its IPO date in May 2019, was valued at over $6 billion, which is the price that the founders would have to pay to get Benchmark's share back.

Some financing sources are neither debt nor equity, such as gifts from family members, funds from crowdfunding websites such as Kickstarter, and grants from governments, trusts, or individuals. The advantages and disadvantages of these sources are discussed in Special Funding Strategies.

ARE YOU READY?

Researching Venture Capital Sources

Perform an internet search for venture capital firms. Review their websites to determine what specific industries each firm invests in. Would your idea for a business fit with any of these firms? What are some aspects that would indicate a good fit?

9.2 Special Funding Strategies

Learning Objectives

By the end of this section, you will be able to:

- Identify funding strategies used by charitable organizations
- Describe financing opportunities available to startups
- Define bootstrapping
- Describe the advantages and disadvantages of bootstrapping

It's important to recognize that not all startups are Silicon Valley tech companies. These companies create high-profile products, such as applications and websites, which can take years to become profitable or even generate revenue. Much more common are the small businesses founded every day by entrepreneurs seeking

to create value in their local communities. Moreover, not all startups are founded with a profit motive in mind.

Charitable organizations, or certain nonprofit companies, are often founded for altruistic purposes, such as advancing the arts, education, and science; protecting the natural environment; providing disaster relief; and defending human rights (Table 9.2).

Charitable Missions and Example Organizations

Mission	Examples
Advance education	Teach for America, Khan Academy
Protect the natural environment	Sierra Club, Wildlife Conservation Society
Defend human rights	Amnesty International, Human Rights Watch
Provide disaster relief	American Red Cross
Support the arts	Metropolitan Museum of Art, Americans for the Arts

Table 9.2

These goals supersede the profit motive that a traditional company would have. As a result, the funding strategies of these enterprises often differ quite dramatically from those of standard for-profit businesses. Without the emphasis on profit, it can be difficult to provide for the cost of ongoing operations. Thus, these organizations must develop a **sustainable strategy**—one that can maintain the organization's financial stability.

In the United States, such organizations can qualify for **tax-exempt status**, meaning that if there is a profit from operations, it is not typically subject to taxes. Organizations seeking this exemption must apply to the Internal Revenue Service for tax-exempt status and provide information about what kind of mission the organization carries out—charitable, scientific, educational, and so on.

Consider a museum. What is its purpose? Traditional companies provide a product or service to their customers in exchange for payment, and typically fill a need their customers have. A grocery store sells food because human beings need to eat food to survive. Although viewing paintings and sculptures is not a physical requirement for life, this experience arguably enriches our lives and helps educate and shape our society. That is why museums are founded. Consider the original mission statement of the Metropolitan Museum of Art (commonly known as the "Met") in New York City (Figure 9.3).[7]

NEW YORK'S METROPOLITAN MUSEUM OF ART MISSION STATEMENT

To be located in the City of New York, for the purpose of establishing and maintaining in said city a Museum and library of art, of encouraging and developing the study of the fine arts, and the application of arts to manufacture and practical life, of advancing the general knowledge of kindred subjects, and, to that end, of furnishing popular instruction.

Figure 9.3 The mission statement of New York's Metropolitan Museum of Art summarizes the purpose of this entity. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

7 Charter of The Metropolitan Museum of Art, State of New York, Laws of 1870, Chapter 197, passed April 13, 1870, and amended L.1898, Ch. 34; L. 1908, Ch. 219. https://www.metmuseum.org/about-the-met

This is a different goal than that of most small businesses (providing a product or service in exchange for a profit) and, as a result, requires different financing strategies, such as a combination of program services, donations, and grants.

LINK TO LEARNING

Go to the Internal Revenue Service's website and look at the most recently updated Pub 334 Tax Guide for Small Business (https://openstax.org/l/52IRSPub334) to learn more about the rules for income tax preparation for a small business.

Program Services

Program services are the basic offerings that a nonprofit organization provides that result in revenue, although not typically enough to cover the overall cost of running the organization. These services most closely resemble the customer interactions of a traditional business. The organization provides a product or service in exchange for a customer's money.

In our museum example, program services could take a few different forms. First, the museum likely charges a fee for admission to view the artwork and artifacts. The individual ticket price multiplied by the number of museum visitors equals the museum's ticket revenue. An established museum will have a good sense of how many visitors it has on average and can use these data to create a budget.

Another source of program service revenue for a museum could take the form of hands-on educational activities or events with guest speakers or presenters. Often museums will host local artists, or their own employees might conduct art classes or special-topic tours. These events and activities typically have a charge (revenue) beyond the regular admission cost.

Despite these revenue-generating activities, nonprofit organizations still face many funding challenges in covering all the operating costs of a normal business, such as employee wages, facility costs, and advertising. Thus, they need many different sources of income. To illustrate, the Met's 2018 program service income only made up 2.3 percent of its total revenue for the year.[8]

Donations

One benefit to a business with a charitable mission is inherent public support, which can foster community involvement above and beyond patronage. For nonprofits, this can translate into a willingness to donate money to the organization. A **donation** is a financial gift with no expectation of repayment or receiving anything in return. A traditional business must provide something valuable to create a customer exchange: Their customers demand value in exchange for their hard-earned money.

The benefactors of a charitable organization want to help further the mission of the organization. This type of entity—whether it's a museum, a hospital, or the Red Cross—relies on the goodwill of community supporters. For the Met, with such a low percentage of revenue generated by program services, it's clear that donations and charitable gifts are vital to the organization's **financial viability**.

8 Calculated from the 2018 IRS Form 990 available on the Met's website. https://www.metmuseum.org/-/media/files/about-the-met/990-forms/2017-irs-form-990-for-fy2018.pdf

Grants

Another source of funding for nonprofit organizations is grants. A **grant** is a financial gift given for a specific purpose by a government agency or a charitable organization such as the Bill and Melinda Gates Foundation. Like a donation, a grant does not have to be repaid. Unlike with donations, both nonprofit and for-profit organizations can compete for grants. Whereas donations are typically given without restriction to offset the general operating expenses of the organization, grants often specify how the funds are to be used. Most grant-providing entities have an agenda or purpose behind their funding. For example, the National Institutes of Health (NIH) provides grants "to support the advancement of the NIH mission to enhance health, extend healthy lives, and reduce the burdens of illness and disability."[9] This federal organization invests over $32 billion annually for medical research.

Grants can be very competitive, requiring a rigorous application process. Usually, multiple organizations apply for the same grant; the organization issuing the grant reviews the many competing applications to make its selection. Grantees generally must submit audited financial statements and are required to update the grantor subsequent to the grant award to ensure proper intended use. The NIH awards almost 50,000 grants annually, most of which are competitive. Although that is an enormous number of projects to fund, only 20 percent of applications submitted to the NIH in 2018 actually were accepted.[10] In other words, the NIH rejected four out of every five applications. For entrepreneurs, this means that when you identify a grant that is specific to your organization's mission, you should weigh your chances of being awarded the grant when considering it as part of your funding strategy.

To understand grants in practice, let's further examine the NIH. The NIH Small Grant Program provides funds for activities such as the development of new research technology. This specific grant can be awarded for up to a two-year period, with funds of up to $50,000 in direct costs per year. A grant like this could provide vital support to a nonprofit startup.

Some business ventures fall somewhere between organizations completely committed to charitable work and traditional small businesses with entrepreneurs focused on social entrepreneurship. Social entrepreneurs develop products and services as solutions to societal problems. For example, the TOMS shoe company was able to create a business model through which the company gives one pair of shoes to children in need in foreign countries for every pair of shoes that a customer purchases. This practice pioneered what they refer to as "One for One."[11]

The company's website describes the origins of both the company and this model, which are based on the experiences of its founder, Blake Mycoskie (Figure 9.4).[12]

TOMS ORIGIN STORY

While traveling in Argentina in 2006, Blake witnessed the hardships faced by children growing up without shoes. His solution to the problem was simple, yet revolutionary: to create a for-profit business that was sustainable and not reliant on donations. Blake's vision soon turned into the simple business idea that provided the powerful foundation for TOMS.

Figure 9.4 The TOMS origin story provides an example of social entrepreneurship. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Social entrepreneurship offers the ability to effect positive change in the world without simply relying on

9 National Institutes of Health. "Grant Basics." February 21, 2017. https://grants.nih.gov/grants/grant_basics.htm
10 National Institutes of Health. "Annual Snapshot." n.d. https://nexus.od.nih.gov/all/2019/03/13/nih-annual-snapshot-fy-2018-by-the-numbers/
11 TOMS. "One for One." n.d. https://www.toms.com/improving-lives
12 TOMS. "Blake Mycoskie." n.d. http://www.toms.com/blakes-bio

donations. It pairs a profitable, sustainable business model with a good cause. This combination often creates positive word of mouth. It gives potential customers a good feeling about the product beyond just its style or function.

WHAT CAN YOU DO?

Social Entrepreneurship

Like the founder of TOMS, sometimes in our everyday life, we are presented with an opportunity to help people. We may even find out that we're not alone in this desire to help. What opportunities to help—individuals, society, or environment—do you see in your own community? What are some ways that you could raise awareness around this issue?

No-Loan Finance Strategies

As you've learned, many startups come into being through the extensive use of debt. Although borrowing is a legitimate source of funding, it can be risky, especially if the entrepreneur is personally responsible for repayment. In practice, some entrepreneurs max out credit cards, take out home-equity loans against their primary residences, or secure other high-interest personal loans. If the entrepreneur fails to repay the loans, the result can be repossession of equipment, home foreclosure, and other legal action.

We now examine funding strategies attractive to many startups that do not require going into debt or exchanging ownership of the business for financial support (debt and equity financing). The financing methods described here are more creative funding strategies, including crowdfunding, bartering, and other methods.

Crowdfunding

Recall the story of iBackPack. This venture was originally funded by contributions through Indiegogo and Kickstarter. These websites are a form of **crowdfunding**, which involves collecting small sums of money from a large number of people. The people who contribute money are typically referred to as backers because they are backing the project or supporting the business idea.

Browsing these crowdfunding websites, you will see many different kinds of ventures seeking financial backing—from creating new board games to opening donut cafes. Each project identifies an overall specific funding goal in terms of a dollar amount. Some crowdfunding websites, such as Kickstarter, implement an "all or nothing" model in which projects do not receive any funds unless their overall funding goal is met. The amount can be exceeded, but if it is not met, the project receives nothing. For an entrepreneur utilizing this resource, selecting an attainable funding goal must be a core part of their strategy. The funding goal must also be appropriate to the scale of the project. For example, setting a goal of $50,000 may be reasonable for launching a food truck (which could be a prototype for a full restaurant), but it is a mere fraction of the cost of constructing an entire table-service restaurant, which would come closer to $750,000. An entrepreneur seeking to enter the culinary world should consider which target would be most achievable as well as most beneficial in meeting both short- and long-term goals. Also, remember that meeting the funding goal does not ensure success of the business, as was the case with iBackPack.

Entrepreneurs vying for crowdfunding usually employ some common tactics. First, they often post an introductory video that explains the project goal and the specific value proposition. (For example, a chef might seek $75,000 to open a food truck specializing in a relatively unknown cuisine.) Second, the entrepreneur provides a more detailed written summary of the project, often including specific items that the funding will pay for, such as $50,000 for a vehicle, $10,000 for graphic design and vehicle decals, and $15,000 for kitchen equipment for the truck. Last is the reward structure, which is what entices visitors to the site to fund the project, offering a return beyond their own passion for the venture. The reward structure establishes different

levels of funding and ties a specific reward to each level. For example, for a contribution of $5, the chef might thank the backer on social media; for $25, the backer would get a t-shirt and a hat featuring the food truck's logo; for $100, the backer would get five free meals when the food truck opens. Fees for these crowdfunding sites vary from 5 to 8 percent. Kickstarter now requires physical products or prototypes for some startups, as well as a short video to help represent and "sell" the product.

Although this financing source offers a lot of flexibility, businesses utilizing crowdfunding can run into trouble. Certain funding levels and rewards may have limits. For example, a reward structure might offer backers contributing $1,000 a trip to the grand opening of the food truck, including airfare and hotel. These top-tier rewards can generate a lot of excitement, but the expense of flying people around the country and providing accommodations could become unmanageable. One research study stated that 84 percent of Kickstarter's top projects delivered their rewards late.[13]

The advantage of crowdfunding is that the business receives cash up front to launch. The down side is that the reward requires a future payment to the backers. This payment may be in the form of branded merchandise, meals, or even events or travel, so it is important for entrepreneurs to set aside part of the investment money to fund the rewards. Depending solely on generating the reward funds out of future sales is a risk that might result in upsetting the very fans who made the business possible. Since crowdfunding is managed online, another risk is upsetting the project's vocal supporters. Crowdfunding usually provides only a "kick start" for a startup, so most seed-stage companies will need additional funding from other sources to get to their first commercial launch.

Although social media can backfire, entrepreneurs can take advantage of benefits too. Crowdfunding can allow an entrepreneur to build a community around a product before it is even sold. Like-minded fans of a product can connect with each other over the internet, in the feedback section of a website, or in shared social media posts. Additionally, backers of a project can become cheerleaders for it by sharing the idea—and their enthusiasm for it—with friends, family, and coworkers. Word-of-mouth marketing can lead to more backers or future customers after launch.

Dozens of crowdfunding portals exist, including WeFunder, SeedInvest, Kickstarter, and Crowdcube. Current SEC guidelines[14] for issuing and investing limits granted for Title III Crowdfunding include:

- A company can raise up to $1 million in aggregate through crowdfunding offerings over a twelve-month period
- Over a twelve-month period, individual investors can invest in the aggregate across all crowdfunding offerings up to:
  - $2,000 or 5 percent of the unaccredited investors net worth or yearly income if they make less than $100,000/year
  - 10 percent of the lesser of their annual income or net worth, if both their annual income and net worth are equal to or more than $100,000

ARE YOU READY?

Kickstarter

Visit the Kickstarter website at https://www.kickstarter.com/ and review a few projects. What did they do well in the video pitch? What unique rewards did they offer? How would you implement a Kickstarter page for your own business idea?

13 Francesco Schiavone. "Incompetence and Managerial Problems Delaying Reward Delivery in Crowdfunding." *Journal of Innovation and Economics Management*. February 2017. https://www.cairn.info/revue-journal-of-innovation-economics-2017-2-page-185.htm

14 Securities and Exchange Commission. "Crowdfunding." n.d. https://www.sec.gov/rules/final/2015/33-9974.pdf

Bartering

Startup companies often don't have a lot of cash assets on hand to spend, but they often have offerings that can provide value to other businesses. **Bartering** is a system of exchanging goods or services for other goods or services instead of for money. Let's consider the case of Shanti, a website designer who wants to start a business. She may want to have her business formally incorporated or may require other legal help, such as review of standard contracts. Hiring a lawyer outright for these services can be costly, but what if the lawyer needed something that a website designer could provide?

Whether the lawyer has just started their own business or has been established for several years, they may need a website created or have an old website redesigned and updated. This website overhaul could prove costly for the lawyer. But what if there were a way that both the lawyer and the web designer could get what they wanted with a resulting net cost of zero dollars? Bartering can achieve this. It should be noted that there are accounting and tax implications involved with bartering that can prevent a net zero offset of costs.

In a barter scenario, Shanti could create a website for the lawyer at the expense only of her time, which in the startup phase is often more abundant than actual cash. The lawyer could provide incorporation services or contract review in exchange, requiring no cash outlay. For many entrepreneurs, this type of exchange is appealing and enables them to meet business needs at a lower perceived cost. Although more mature firms can also use bartering, the opportunity cost is much higher. If a mature company is unable to take on a new paying client because it is doing too much free (barter) work, it may lose out on future revenue, which could potentially be a big loss. Startups, in contrast, often have excess capacity while they develop a customer base, so taking on barter work is often a low-risk, beneficial funding strategy.

Other No-Loan Funding Options

Beyond crowdfunding and bartering, startups have other options to help them get off the ground, such as funding competitions and pre-orders (Figure 9.5). Many organizations hold entrepreneurial finance contests provide financial awards to the winners. These prize funds can be used as seed money to start a new venture. For example, the New York City Public Library holds an annual business plan competition called the New York StartUP! Business Plan Competition.[15] Applicants must complete an orientation session, attend workshops that develop skills related to the creation of a business plan, and submit a complete business plan. The first-place award yields $15,000 in prize money, which can be a great start toward turning an entrepreneurial idea into a business reality.

Another way for startups to gain financial traction is to solicit pre-orders. Consider the launch of a new book or video game. Retail stores will often solicit pre-orders, which are advance purchases of the product. Customers pay for the desired item before they even have access. For example, the entrepreneur Mitchell Harper raised $248,000 in funds before his product launched.[16] This approach is not limited to existing, well-known franchises—startups can use it as well. Although established novel and video game franchises have big fan bases and often large advertising budgets, startups can still find effective strategies in this space.

15 New York Public Library. "New York Startup! 2019 Business Plan Competition." n.d. https://www.nypl.org/help/services/startup
16 Mitchell Harper. "How I Got $248,000 in Pre-Orders before I Even Had a Product." *Medium.* November 25, 2015. https://blog.markgrowth.com/how-i-got-248-000-in-pre-orders-before-i-even-had-a-product-b4080a3eb8ae

Figure 9.5 Entrepreneurs can explore a variety of no-loan funding options. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Companies with a prototype model of their product or a first manufacturing run can showcase the new product to potential customers, who may be interested enough to place an order. The company can use the funds received from these pre-orders to pay for the inventory. In addition to having sales staff make sales calls, new companies can attend trade shows and exhibitions to garner interest in the product. Many new products are launched in this fashion because it allows access to many potential customers in one place.

Why Bootstrapping Hurts, Then Helps

The process of self-funding a company is typically referred to as **bootstrapping**, based on the old adage that urges us to "pull ourselves up by our bootstraps." It describes a funding strategy that seeks to optimize use of personal funds and other creative strategies (such as bartering) to minimize cash outflows. In recent years, this strategy has been the fodder for shows like *Shark Tank*. These shows may make entrepreneurs think that being on TV is glamorous, or the shows may glorify the financial backing of millionaires and billionaires. We have seen that for many entrepreneurs, the reality is that there are drawbacks to bringing in outside investors to launch your venture. These drawbacks include loss of future profits and possible loss of control of the company, among others. Potential business owners must weigh the advantages and disadvantages—both short and long term—for funding their specific dream.

You've learned about financing strategies predicated on finding a willing investor or lender, but many small businesses simply don't have access to large amounts, or any amount, of capital. In these cases, aspiring business owners need lean business strategies that will yield the greatest benefit.

Bootstrapping requires entrepreneurs to shed any preconceived notions of the popular-culture image of startups. Most startups don't have trendy downtown offices, foosball tables, or personal chefs. Bootstrapping reality looks more like late nights spent clipping coupons. It involves scrutinizing potential expenses and whether each cost is really worth the investment. It can be a difficult and trying process, but without any angel investors or wealthy family backers, bootstrapping is often an entrepreneur's only option. The good news is that this approach can pay substantial dividends in the long run.

The Basics of Bootstrapping

When entrepreneurs risk their life savings, they must stretch every dollar as far as possible. Having a limited amount of capital to work with requires optimizing creative strategies to get the business launched and keep it afloat. This creativity applies to bringing customers and sales in the door as well as to managing expenses.

Understanding the ongoing costs of the business is key. In an interview on NPR's show *How I Built This*, Barbara Corcoran, one of the investors on *Shark Tank*, shares her humble beginnings in real estate brokerage.[17] One of things she touches on is being constantly aware of how long her money would last, given her monthly expenses. If she had $10,000 in the bank and the cost of her rent and employees was $2,500 per month, she knew that the money would last her four months. Such constant information and vigilance are required when bootstrapping a business for success.

Employee costs are typically one of the largest expenses facing a business. Hiring traditional full-time employees can be costly; onboarding them too early can be fatal to a business's bottom line. Creative approaches to minimizing labor costs can be enormously helpful. One strategy for controlling these costs is utilizing independent contractors (freelancers) and other part-time employees. They do not work full time for the business and may serve other companies as well. Their compensation is generally lower than that of a full-time, salaried employee, often in part because these positions do not usually come with any benefits, such as health insurance or paid time off. Using these workers to fill resource needs can help minimize costs. Once operations have begun to stabilize, it may be possible and ideal to offer full-time employment to these individuals.

Marketing is another key area for new business investment, but billboards, web ads, TV ads, and radio spots can be expensive. TV and radio ads can also be ineffective if they are aired during low-volume times, which is typically all that startups with lower budgets can afford. Fortunately, there are many low- or no-cost marking opportunities, such as word-of-mouth marketing. Doing a good job for one customer can easily lead to referrals for more business. Some social media efforts can also provide a strong return for minimal investment, although typically it is nearly impossible to gauge an effort's potential impact or success.

A new enterprise that is bootstrapping must also carefully manage operational expenses. At the beginning of operations, an entrepreneur can often minimize unnecessary expenses—even if that means forgoing an actual business location. Working out of a home office or a co-working space (such as WeWork or Impact Hub) can lead to significant savings. Renting office space can cost hundreds or thousands of dollars a month, whereas a home office typically requires no additional investment. Depending on the location, co-working spaces can provide a single workspace and technology access for as little as $50 to $100 per month, yielding substantial savings over a dedicated office suite. In larger cities, or in locations with more amenities, the monthly costs can run between $100 and $500 per month.

The Boston Beer Company, which today produces the Samuel Adams line of beers, provides a classic example of minimizing these costs in its early days. When this company first started, it owned no office space—or even a brewery. It employed other breweries as contract brewers to manufacture its beer. Its founder, Jim Koch, invested most of his time in selling to bars and restaurants, working from his car and phone booths. (This was during the 1980s.) His lean strategy was a successful application of the bootstrapping mindset. From its humble beginnings, the Boston Beer Company has become one of the largest American-owned breweries—ranked second based on 2018 sales volume by the Brewers Association.[18] Whereas traditional thinking may dictate that a company must have an official office or headquarters, a bootstrapping mindset evaluates what the space would be used for and the trade-offs for its cost.

17 National Public Radio. "Real Estate Mogul: Barbara Corcoran." *How I Built This*. May 14, 2018. https://www.npr.org/templates/transcript/transcript.php?storyId=610491305

18 Brewers Association. "Brewers Association Unveils 2018 Rankings of Top US Brewing Companies." 2019. https://www.brewbound.com/news/brewers-association-unveils-2018-rankings-of-top-us-brewing-companies

How Bootstrapping Hurts

The process of bootstrapping is not an easy one. It is fraught with tight budgeting and sacrifice, which can take its toll on an entrepreneur. One of the simplest bootstrapping strategies is to start a business by **moonlighting**, or treating your business venture as a second job. Employing this strategy, the entrepreneur continues to work at their regular job, say from 9:00–5:00, and then dedicates the rest of the evening and weekends to working on the business. Whereas this strategy has the obvious benefit of maintaining a comfortable level of income, this approach has a few drawbacks (Table 9.3). Moonlighting entrepreneurs cannot dedicate 100 percent of their time and energy to their new business. The time they can dedicate to it may be less efficient. After working all day at another job, a person may feel tired or burned out, so it can be difficult to change gears and press forward with full productivity.

In addition to the exhausting time investment, moonlighting can exact tolls on personal relationships. This strategy is easiest when an entrepreneur is in a life stage with few commitments. It may have an adverse effect on friendships, but in other life stages, this impact can be more significant. For example, it can detract from relationships with a partner/spouse or children, in both a decrease in focus/investment in these relationships and day-to-day challenges in work-life balance and household management for all affected. Additionally, at some point, to attract serious investors, a founder will have commit to the project full time.

Bootstrapping Advantages and Disadvantages

Advantages	Disadvantages
• No ownership given up • Forces creative solutions • Keeping costs low fuels growth	• Slow to start • Less glamorous • Owner must make personal sacrifices

Table 9.3

Other bootstrapping strategies include negotiating the terms for payments on expenses. Often when businesses sell to other businesses, the vendor allows the customer to buy on **credit**. This means that the buyer does not have to pay at the time of purchase. Although retail customers are required to pay at the register during checkout, purchases between businesses can work on different terms, sometimes extended up to thirty, sixty, or ninety days. This extra time to pay for purchases can be a real advantage for businesses. When a business buys inventory on credit, it has the opportunity to begin selling it before it has even paid for it. For example, a clothing retailer could sell its product in stores or online, and receive cash before it had to pay its vendors. Unfortunately, when a business's cash becomes tight, an ethical dilemma can arise. When a business has more bills to pay than money to pay them with, the owner will need to make tough decisions. It can be easy to forget about or ignore amounts due to vendors, but this problem is compounded when it occurs with more and more vendors. Ultimately, it can get to the point where vendors will no longer sell to you on credit, or even at all. When a company can no longer buy inventory to sell to customers, it won't be long until it's out of business. An ethical entrepreneur will be alert to this concern and resolve it with aboveboard business decisions.

How Bootstrapping Helps

Although bootstrapping can be painful in the early years of a business, it yields significant benefits for the business owner in the long term. One of the most valued benefits of bootstrapping a business is the fact that the founder can maintain control of the company and typically retain 100 percent ownership. Although it can be easy to give up ownership in an idea because ideas come freely and don't require financial sacrifice, entrepreneurs who accept an equity financing opportunity and give up a significant portion of ownership of

the business may not realize the potential detrimental outcomes. What seems glamorous on *Shark Tank* may cost a business owner more control than desired. Once you give up any amount of equity in a business, it can be difficult or expensive to get it back. Once the deal is accepted, the investor is entitled to that percentage of the profit every year the company is in business, even if that person never lifts a finger to support the enterprise. Entrepreneurs usually make those financing deals because of the benefits of the money and access to the investor's contacts. It's unlikely that Mark Cuban is going to roll up his sleeves in your food truck when things get tough. If you can avoid outside financing, you will maintain complete control and full ownership of the business, and you should weigh this benefit in your financing decisions.

Another benefit of bootstrapping is avoiding taking on debt. Whether it's in the form of credit cards or personal loans, repayment of debt can take a serious toll on any business and can be especially burdensome for new businesses. Considering that some of the debt financing sources available to entrepreneurs can bear higher-than-average interest rates, digging yourself out from underneath this financial burden is no easy task. Also, delaying outside investments allows your business to grow not only in revenue and profit, but also in market value. When potential investors come along, they will consider a higher contribution for a smaller percentage in the business.

LINK TO LEARNING

One of the most common forms of debt financing is simply a credit card. Although it may seem wise to charge many of the upfront expenses and simply pay the card's minimum monthly payment, this can be a treacherous road to go down. Try the credit card calculator (https://openstax.org/l/52CreditCalc) to calculate how long it takes to pay off a credit using only the minimum payment. It may shock you. Try a few different amounts: $1,000; $5,000; and $10,000.

9.3 Accounting Basics for Entrepreneurs

Learning Objectives

By the end of this section, you will be able to:

- Explain the accounting equation and define its parts (assets, liabilities, and equity)
- Define revenue, expenses, and income

Although financing and accounting complement and rely on each other, they are distinct. As we have seen, financing is the process of raising money. **Accounting** is the system of recording and classifying financial transactions related to a business, and summarizing and communicating those transactions in the form of financial statements. Accounting is essentially documenting what happens to money once a company receives it and thereby makes that information available for reporting to stakeholders and regulatory agencies, and informing business decisions.

At the most fundamental level, an accounting system accomplishes two goals:

1. It summarizes a business's financial performance
2. It communicates that performance to owners, managers, and outside parties

The most common approach to accounting used in the United States, and around the world, follows the basic formula shown in Figure 9.6.

Figure 9.6 The accounting equation provides the foundation of a company's financial status and outlook. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

This formula is referred to as the basic **accounting equation**. First, we'll define each of these terms, and then

we'll look at an example of a simple transaction recorded using the equation.

Assets are items—such as equipment, cash, supplies, inventory, receivables, buildings, and vehicles—that a business owns and derives future use from. Potential investors want to know what resources a company has at its disposal. Business owners want to see where their money has gone. Let's return to the case of Shanti, the website designer who starts her business by purchasing a new laptop computer. The computer is an asset that Shanti has acquired for her business.

A **liability** is a debt that a company has incurred with another party, as when it borrows money from a bank or purchases materials from other suppliers. The business is required to make a future payment to satisfy that debt. For accounting purposes, we want to be able to see what the business owns (assets) compared with what it owes (liabilities). For example, if Shanti does not have sufficient cash to pay for the laptop, she may have the electronics store charge her credit card for the purchase. In that case, the credit card company pays the store, and Shanti's business now owes the credit card company for the amount of purchase (a liability).

Equity is the owner's claim on the assets of the business, that is, the difference between what they own and what they owe. Essentially, equity tells a business owner or investor how much the firm is worth after all the debt is repaid. Returning to the example of Shanti's website design business, let's compare two scenarios of startup purchases to see the effects on the accounting equation. In both cases, Shanti contributes some of her own money to the initial purchase of a laptop.

In the first scenario, shown in Figure 9.7, she contributes $1,000 to the new business.

Assets	=	Liabilities	+	Equity
Cash				Owner's Capital
+1,000		0		+1,000

Figure 9.7 An initial $1,000 contribution by the owner is recorded in the accounting equation. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Each element of the accounting equation has its own account in an accounting system or software package, and all changes are tracked within its account. The accounting equation must stay in balance after every transaction with assets equaling liabilities plus owners equity. In this case, Cash is an assets account, and Owner's Capital is an equity account. The $1,000 cash contributed is a cash asset and becomes equity that is recorded as owner's capital. At this point, Shanti can claim 100 percent of the assets of the business, which right now consist only of the cash.

If she uses all of her cash assets to purchase the laptop, the accounting equation will record this as shown in Figure 9.8.

Assets		=	Liabilities	+	Equity
Cash	Computer				Owner's Capital
+1,000			0		+1,000
−1,000	+1,000				
0	1,000		0		1,000

Figure 9.8 The purchase of a laptop computer using existing cash is recorded in the accounting equation. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

When the cash is spent, reducing the assets column to zero, a new asset account for the computer is created to record the dollar amount paid for the laptop. Again, because Shanti doesn't owe another party at the end of the transaction (because she didn't make any additional contribution), the balance of the owner's equity account remains the same. The equation shows that Shanti still owns 100 percent of the assets.

Now consider how to account for a situation in which Shanti does not have a significant amount of cash to contribute to the business. She can afford to contribute only $100 and deposits the money into the business's

bank account. Fortunately, she also has access to a credit card that can be charged for business purchases, increasing her investment options.

The initial contribution to the business is recorded in the same way but with the new amount, as shown in Figure 9.9.

Assets	=	Liabilities	+	Equity
Cash				Owner's Capital
+100		0		100

Figure 9.9 An owner contribution of $100 is recorded in the accounting equation. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The laptop still costs $1,000, but the business has only $100 in cash assets. Shanti purchases the laptop with a credit card, and the clerk finalizes the sale. Figure 9.10 shows the impact of the sale on the accounting equation.

Assets			=	Liabilities	+	Equity
Cash	Computer			Credit Card		Owner's Capital
+100	0			0		+100
−100	+1,000			+900		0
0	1,000			900		100

Figure 9.10 The purchase of the computer asset using cash and a credit card is recorded in the accounting equation. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

In both examples, Shanti reports the computer as an asset of the business that is valued at its $1,000 cost. In the first scenario, she exchanged the cash for the computer. In the second, she exchanged a smaller amount of cash for the laptop and charged the remaining amount of the purchase on a credit card. This creates a liability for the business that Shanti will need to repay in the future. Since this is an equation, both sides must be equal to each other, and this proves to be the case in both scenarios. The total assets are $1,000, and the total liabilities plus equity are also $1,000.

ARE YOU READY?

The Accounting Equation

On a sheet of paper, use three columns to create your own accounting equation for your personal assets, liabilities, and expenses. In the first column, list all of the things you own (assets). In the second column, list any amounts owed (liabilities). In the third column, using the accounting equation, calculate the net amount of the asset (equity). When finished, total the columns to determine your net worth.

Here is something else to consider: is it possible to have negative equity? It sure is . . . ask any college student who has taken out loans. At first glance there is no asset directly associated with the amount of the loan. But is that, in fact, the case? You might ask yourself why make an investment in a college education—what is the benefit (asset) to going to college? The answer lies in the difference in lifetime earnings with a college degree versus without a college degree. This is influenced by many things, including the supply and demand of jobs and employees, and the field in which you plan to work.

9.4 Developing Startup Financial Statements and Projections

Learning Objectives

By the end of this section, you will be able to:

- Understand the three primary financial statements: balance sheet, income statement, and statement of cash flows
- Understand how financial projections are made and how to use the run rate and the burn rate
- Understand how to create a break-even analysis

You have learned how an accounting system classifies transactions in terms of assets, liabilities, and equity; what those transactions mean in terms of the accounting equation; and what that information says about an entity's overall financial health. Now we'll examine how to summarize those transactions in financial statements that can be shared with stakeholders. Internally, these statements are used to make decisions about the management of the company and its operations. Externally, they provide existing and potential investors with data to inform their financial support of the venture.

The information entered into the accounting system is summarized in **financial statements**, which are the output of an accounting system. We will examine three basic types of financial statements:

- The balance sheet
- The income statement
- The statement of cash flows

Each type of statement communicates specific information to its audience. Investors around the world use financial statements every day to make investment decisions.

LINK TO LEARNING

If you like quizzes, crossword puzzles, fill-in-the-blanks, matching exercises, or word scrambles, go to My Accounting Course (https://openstax.org/l/52MyAcctCourse) for some fun ways to reinforce the accounting information you are learning. This website covers a variety of accounting topics including financial accounting basics and financial statements.

The Balance Sheet

The first financial statement is the balance sheet. The **balance sheet** summarizes the accounting equation and organizes the different individual accounts into logical groupings. As you previously learned, the components of the accounting equation are:

- assets—items the company owns or will benefit from; examples include cash, inventory, and equipment
- liabilities—debt or amounts the company must repay in the future; examples include credit card balances, loans payable, and so on
- equity—the share of the assets due to the owners after debt is repaid

The accounting equation itself (assets = liabilities + equity) is spelled out on the balance sheet. It is shown in two portions. On one side, all of the assets are spelled out and their amounts totaled. This total is compared to the totals in the second and third portions, which show liabilities and equity. Just as the accounting equation itself must balance, so must the balance sheet.

Figure 9.11 shows the 2020 balance sheet for Hometown Pizzeria. This is the same kind of financial statement that real-life investors use to learn about a business. You can see the main aspects of the accounting equation in each half of the statement, as well as many detailed individual accounts. This financial statement gives the reader a quick summary of what the company owns and what it owes. A potential investor will be interested in

both items. The amount of liabilities is an indicator of how much the business needs to pay off before the investors will see a return on their investment.

Unlike the accounting equation shown in Accounting Basics for Entrepreneurs, most balance sheets display data vertically rather than horizontally. But the vertical format still presents the two sides of the equation—except that liabilities and equity are on the bottom half of the statement. Note that the two sides still must equal each other, or balance—hence the name "balance sheet."

HOMETOWN PIZZERIA Balance Sheet For the Year Ended December 31, 2020	
Assets	
Cash	3,918
Ingredient supplies	1,720
Furniture and fixtures	5,654
Restaurant equipment	15,890
Total assets	27,182
Liabilities	
Accounts payable	1,890
Credit card payable	3,759
Total liabilities	5,649
Equity	
Owner's capital	21,533
Total liabilities and equity	27,182

Figure 9.11 This is Hometown Pizzeria's balance sheet. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

A review of the Hometown Pizzeria balance sheet lets us see what kind of assets the company has. We see cash, ingredients, and restaurant equipment—all things that would be necessary to make pizzas and sell them. We also see some liabilities. **Accounts payable** is an account that covers many different vendors that the company buys from on credit, which means the vendors let the pizzeria pay them after they have delivered their goods. These vendors could be companies that sell flour, produce, or pizza boxes. "Credit card payable" is the balance due on the credit card, which could have also been used to stock up on supplies or pay other bills.

One of the first things an investor will do is compare the total assets of a company with the total liabilities. In this case, the pizzeria reports total assets of $27,182 and total liabilities of $5,649. This means that the pizzeria owns more than it owes, which is a good sign. It actually has several times more assets than liabilities. Although it does not have enough cash to pay off all the liabilities right now, other assets have value and could be sold to generate cash.

To recap, the balance sheet summarizes the accounting equation. It tells the business owner what the company has and how it was paid for. Investors also want to understand where the company has spent its money and where that money came from. If a company is laden with debt, any investment may be immediately spent trying to get caught up with creditors, with no real impact on helping operations. Ultimately, investors want to read these financial statements to know how their money will be used.

The Income Statement

The second basic financial statement is the income statement, which provides the results of a company's operations. At the most basic level, the **income statement**—also called the **profit-and-loss statement**—describes how much money the company earned while operating the business and what costs it

incurred while generating those revenues. An investor wants to know how much money the company brought in from customers and how much it had to spend to get those customers. Revenue minus expenses results in **net income**, or profit if there are funds left over.

After identifying total revenue and expenses, a business can calculate its profit margin. The **profit margin** is the profit divided into the total revenue, described as a percent. For example, if we opened a pizzeria and generated $100,000 in sales our first year and incurred $90,000 in expenses, that would result in $10,000 of net income. If we divide that net income by our $100,000 in sales, the profit margin is 10 percent. So for every dollar of sales that was generated, ten cents remained as a profit. We could save this resulting profit for future renovations, an expansion, or payment to the owners as a distribution.

A pizzeria—or any business that sells a physical product—has costs that are specific to the product sold. For example, pizza requires flour and yeast to make the dough, tomato sauce, and cheese and other toppings. We refer to these expenses as the **cost of goods sold**. These costs are the primary driver that determines whether the company can be profitable. If the selling price of a pizza is $12 and our cost of ingredients is $12, the transaction nets to zero. The company wouldn't make any money on a sale and is simply recouping the money paid for the ingredients. This is not a feasible business model because there are many costs in addition to ingredients, such as rent on the building, employee wages, and other items.

The selling price of an item minus its direct costs—or cost of goods sold—is the **gross profit**. In a product business, this is the most important operational figure. A business needs to know how much money it makes on each sale because that gross profit pays for all other expenses. If the pizzeria sells a pizza for $12, the cost of its ingredients might be $4, so the gross profit of selling one pizza is $8. Every time the company sells another pizza, the gross profit increases. If the business sells 1,000 pizzas in a month, its sales would be $12,000, the cost of goods sold would be $4,000, and $8,000 would be left for profit (Figure 9.12).

HOMETOWN PIZZERIA
Income Statement
For the Year Ended December, 2020

Revenue	
Food and beverage sales	32,593
Expenses	
Cost of goods sold	9,777
Paper products	1,201
Rent	3,000
Salaries and wages	4,809
Utilities	2,753
Total expenses	21,540
Net income	11,053

Figure 9.12 This is Hometown Pizzeria's income statement. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Results from Operations

As you learned earlier in this chapter, a business can create assets through debt or equity financing. After the initial investment, those assets can be employed to operate the business. For example, when Hometown Pizzeria opens, after the initial build out of the kitchen and dining area, the business can make and serve food to customers in exchange for money. This process creates new assets in the form of cash collected from customers and becomes a third way to generate assets in a business—from operations, which we call revenue. In an ideal situation, the business would require little outside investment once operations have begun.

The amount a business earns from selling a product or providing a service is referred to as **revenue**, or sales.

The costs incurred in the normal course of operations are referred to as **expenses**. For the newly opened pizzeria, payments from customers for their meals are the business revenue, whereas the cost of food ingredients, beverages, dinnerware, and paper goods—such as napkins—are the operating expenses. The balance of business revenue minus operating expenses is the profit of the business, or net income.

Before moving on to visualizing operational income, let's pause here to review some of the basic distinctions between these key terms. When a company gains new assets, those assets have to come from somewhere, usually from one of three sources. We will see these options on the right side of the equation, as we move from left to right. First, if we gain a new asset, but we have not paid for it, we have created a liability—something the business owes. This was the case when Shanti paid for her computer with a credit card. In the future, she will have to pay the credit card company, but this is different process from an expense, as we will see later. For right now, we are gaining something new and must repay someone later.

The second source of new assets is owner investments. This was the first example we saw when Shanti deposited money in the business's bank account from her personal savings. In terms of the business, assets increased because she now had more cash than before, and on the right side of the accounting equation, we record the source of those assets—Shanti herself. So investments by the owner are another source of new assets.

The third way that the business gains new assets is from operations. When Shanti uses the assets of her business (a computer) to perform work for a customer (creating a website), this results in a sale, or revenue. Assets of the business increase because the customer pays for the work; thus, Shanti's cash increases. Again, on the right side of the equation, we record the source of that asset: revenue. Revenue is an increase in assets from customers paying for goods and services.

To illustrate, let's continue with Shanti's website design business. She purchased a computer with her personal savings and has been hired to create a website for a local business. This client agrees to pay $5,000 for the website, due on completion of the site. Once the work on the website is complete, Shanti records the receipt of $5,000 cash as an increase to the cash account. On the right side of the equation, this is added in an account under equity for revenue (Figure 9.13).

Assets		=	Liabilities	+	Equity	
Cash	Computer				Owner's Capital	Revenue
+1,000	0		0		+1,000	0
–1,000	+1,000		0		0	0
+5,000	0		0		0	+5,000
5,000	1,000		0		1,000	5,000
Total Assets = $6,000					Total Equity = $6,000	

Figure 9.13 This shows recording a customer sale of $5,000. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The total company assets have grown to $6,000 with the addition of the $5,000 earned and collected from this client. On the right side of the equation, equity has increased in a new column representing revenue and expenses, where revenues are positive amounts and expenses are negative amounts.

The accounting equation describes how transactions are classified within the context of balancing what a business has (assets) with how it paid for those assets (liabilities and equity). In the next section of this chapter, we will explore how this information is summarized in financial statements and how entrepreneurs and potential investors use that information.

LINK TO LEARNING

Accounting is the system of communication that allows for decision making by individuals both inside and outside the company. For an overview (https://openstax.org/l/52Accounting) of accounting, please see the video at the Investopedia website.

The Statement of Cash Flows

The third basic financial statement we will discuss is the **statement of cash flows**, which explains the sources of and uses of a company's cash.

You may wonder how the statement of cash flows differs from an income statement. The short answer is that the income statement captures events as they happen, not necessarily when the company gets paid. It records certain items, such as sales, when the work is completed. Let's return to Shanti, the website designer. As soon as she completes the client's website, the accounting system will record the *revenue*, the amount that is due from that client; this second item is referred to as **accounts receivable**. If Shanti's client is struggling financially or even goes out of business, she may never get paid for that work, but the income statement would show sales, and therefore possibly a profit. If the customer goes out of business, the business bank account will not have any evidence of a profit.

It is for this reason that the statement of cash flows was developed. It accounts for these differences, only showing activities that result in cash received or cash paid. To better understand the purpose and use of the statement of cash flows, let's first look at this statement again in the context of a pizzeria (Figure 9.14).

HOMETOWN PIZZERIA
Statements of Cash Flows
For the Year Ended December 31, 2020

Cash Flows from Operating Activities	
Cash received from customers	50,000
Cash paid for ingredients and supplies	(18,000)
Cash paid for employees	(12,500)
Cash paid for interest	(3,300)
Cash paid for taxes	(3,900)
Net provided by operating activities	12,300
Cash Flows from Investing Activities	
Purchase of equipment and furniture	(55,000)
Cash Flows from Financing Activities	
Proceeds from long-term debt	60,000
Net increase (decrease) in cash	17,300

Figure 9.14 This is Hometown Pizzeria's statement of cash flows. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

As we can see in the statement of cash flows for Hometown Pizzeria, although the basic operations generate positive cash flow, a major purchase was required. This is common at the inception of a business. Not every location will come equipped with a commercial kitchen and dining area, so the business may need to purchase items such as a pizza oven and dining chairs and tables. Note that although the income statement approximates the cash flow from operations, it would not show the large outflow resulting from the initial purchase of equipment. That purchase would have been treated as an asset within the context of the accounting equation and would have been recorded on the balance sheet. So from that large difference alone, we can see why some people say that the statement of cash flows is the most important of the financial statements. It bridges the gap between the income statement and the balance sheet.

As you can see in the figure, the statement of cash flows is broken into three sections. The first is **operating activities**, the day-to-day activities of the business, including purchasing supplies, paying rent, and receiving cash from customers. This section tells a reader how effective the company's business model is at generating cash flow.

Investing activities include major purchases of equipment or facilities. For example, when Amazon develops its second headquarters, those billions of dollars spent will be recorded as investing activities. Additionally, if the company has an excess of cash, it may purchase securities such as stocks and bonds, which have a higher return on investment than a traditional bank savings account. This section tells a reader where the company spends money in terms of large acquisitions.

The third section of the statement of cash flows is **financing activities**. This section tells a reader where new infusions of cash come from. The owners of Hometown Pizzeria need to find a way to pay for the kitchen equipment and furniture. If they have such an amount in their personal savings, then they can simple contribute it to the company themselves. If they don't have the money already, they will need to seek other sources, such as loans or the types of investors discussed in Overview of Entrepreneurial Finance and Accounting Strategies. Generally, any financing activity is also booked in the balance sheet as well. This section of the statement explains which sources the owners used to generate outside funds coming into the business. It always indicates future requirements as well. For example, if a bank loaned the pizzeria the money, then we know it will have to be repaid in the future. So the business will need to ensure it is setting aside money to make monthly repayments. If new investors contribute money, what manner of return on investment will they be seeking? If they decide to seek regular distributions of profit, they will have to factor that in.

LINK TO LEARNING

It is a good idea to familiarize yourself with the type of information companies report each year. Peruse Best Buy's 2017 annual report (https://openstax.org/l/52BestBuy2017) to learn more about Best Buy. Take note of the company's balance sheet on page 53 of the report and the income statement on page 54. These reports have much more information than the financial statements you've seen, but as you read through them, you will notice some familiar items.

Projections

Among the most powerful tools business owners can use are projections. A **projection** is a forecast of the future operations of the business. It is a landscape for the business: What do the next few months look like? What about the next year? A projection would outline what level of payments are expected to come in and the timing of costs incurred. This lets the business owner understand what potential financing needs to be secured.

Two key concepts related to projections are the run rate and burn rate. The **run rate** helps extrapolate into the future. For example, if the pizzeria is generating sales of $10,000 per month, that translates into an annual run rate of $120,000 per year. Multiplying the monthly amount by twelve tells us the annual amount; if we wanted quarterly projections, we would multiply the monthly amount by three. This is useful for explaining to investors what the company will look like now that it has achieved traction in generating sales.

The **burn rate** is the rate at which cash outflow exceeds cash inflow, or essentially how much money the company is expending overall each month. Before generating revenue, or generating enough to just break even, startup companies will incur losses. Understanding the pace at which the expenses exceed revenue helps business owners plan accordingly. For example, if it takes six months to renovate the pizzeria and the monthly rent is $2,000, then the burn rate is $2,000 per month and forecasts that the business will need an additional $12,000 ($2,000 × six months) available in financing on top of the cost of renovations. The location's rent must be paid, even if the pizzeria isn't yet open for business.

During the seed stage of a company, projections can also be used to show potential investors how quickly the company will make money and hopefully inspire them to invest in the venture. Just as on *Shark Tank*, projections are used during the "pitch." Investors and lenders want to see exactly how they can expect the business to perform and how quickly the company generates positive financial results.

Break-Even Analysis

Another critical part of planning for new business owners is to understand the **breakeven point**, which is the level of operations that results in exactly enough revenue to cover costs. It yields neither a profit nor a loss. To calculate the break-even point, you must first understand the behavior of different types of costs: variable and fixed.

Variable costs fluctuate with the level of revenue. Returning to Hometown Pizzeria, we see that the cost of ingredients would be a variable cost. In a previous section, we also referred to these as the cost of goods sold. Variable costs are based on the number of pizzas sold, with the goal being to buy just enough ingredients that the business doesn't run out of supplies or incur spoilage. In this example, the cost of making a pizza is $4, so the total variable costs in any given month equal $4 times the number of pizzas made. This differs from a fixed cost such as rent, which remains the same every month regardless of whether the pizzeria sells any pizzas or not.

The first step in understanding the break-even point is to calculate the contribution margin of each item sold. The **contribution margin** is the gross profit from a single item sold. Therefore, selling price minus variable costs is the contribution margin. Hometown Pizzeria's selling price of a pizza is $12. The variable cost is $4, which results in a contribution margin of $8 per pizza. This $8 will go toward paying other expenses; when those are covered, the remainder will be added to the profit. Once we understand how much each item sold contributes to other expenses, we understand how those other costs behave (Figure 9.15).

HOMETOWN PIZZERIA	
Selling price of a pizza	$12
Cost of ingredients	(4)
Contribution margin	$ 8

Figure 9.15 This is Hometown Pizzeria's contribution margin. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The other main category of costs is fixed costs. **Fixed costs** are a set amount and do not change, regardless of the amount of sales. Previously, we referred to rent as such a cost, but most of the business's other costs operate in this manner as well. Although some costs vary from month to month, costs are described as variable only if they will increase if the company sells even one more item. Costs such as insurance, wages, and office supplies are typically considered fixed costs.

Once variable and fixed costs are determined, this information can be used to produce a break-even analysis. Calculating the break-even point is simply a matter of dividing the total fixed costs by the contribution margin. To illustrate, let's assume that Hometown Pizzeria still sells pizzas with a contribution margin of $8 each. Let's also assume that the only fixed cost is the rent of $2,000 per month. If we wanted to know how many pizzas the owner needs to sell each month to pay the rent, we divide $2,000 by $8. This results in a break-even point of 250 pizzas. Now we know that if the pizzeria sells 250 pizzas a month, its rent is completely paid. Any additional pizzas sold add to the company's profit. If the business sells fewer than 250 pizzas, it will not generate enough income to cover the rent and will incur a loss. Whenever a business incurs a loss, the owners will need to contribute more of their own personal savings or potentially go into debt (Figure 9.16).

HOMETOWN PIZZERIA	
Total fixed costs	$2,000
Contribution margin of a pizza	÷8
Break-even point (in number of pizzas)	250

Figure 9.16 This is Hometown Pizzeria's break-even point. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Understanding the break-even point for a business provides a great deal of insight. At the most basic level, it demonstrates how many units of a product must be sold to cover the expenses of the business and not incur a loss. It may also help business owners understand when costs are too high and decide how many units need to be sold to break even. Realizing this up front can help entrepreneurs avoid starting a business that will result only in losses.

WORK IT OUT

Calculating Break-Even Analysis

Consider the break-even analysis tool. Using the same contribution margin provided ($8/pizza), calculate the break-even point if we chose a more expensive city. How many pizzas would we need to sell each month to break even if our fixed costs were $5,000 a month? What if they were $10,000 a month?

Key Terms

accounting system of recording and classifying a company's financial transactions and summarizing and communicating those transactions in the form of financial statements
accounting equation assets = liabilities + equity
accounts payable account that includes vendors that the company owes money to
accounts receivable account that includes customers that owe the business money
angel investor wealthy, private individual seeking investment options with a greater potential return than is generally available with traditional publicly traded stocks
assets items a business owns and derives future use from
balance sheet financial statement that summarizes a company's financial condition according to the accounting equation
bartering exchanging goods or services for other goods or services instead of for cash
bootstrapping funding strategy that seeks to optimize use of personal funds and other creative strategies (such as bartering) to minimize cash outflows
breakeven point level of operations that results in exactly enough revenue to cover costs
burn rate rate at which cash outflow exceeds cash inflow
charitable organization nonprofit company founded for altruistic purposes
collateral something of value pledged to secure a loan
contribution margin gross profit from a single item sold
cost of goods sold cost required to produce the product or service
credit lending of funds in exchange for a promise to repay
crowdfunding financing with investments of small amounts of money from a large number of people
debt financing borrowing funds that must be repaid, usually with interest
donation financial gift intended to support an organization's general operations
early stage company lifecycle stage in which the product or service has begun development
equity owner's interest in the assets of the business
equity financing funds provided in exchange for a share of ownership in a business
expenses costs incurred in the normal course of business operations
financial statement output of an accounting system that is used to make financial decisions
financial viability long-term financial sustainability of an organization to fulfill its mission
financing raising money to fund the startup and operation of a business
financing activities section of the statement of cash flows that shows where new infusions of cash are coming from
fixed assets major purchases with a long life, such as buildings, land, and so on
fixed costs costs that do not change, regardless of the amount of sales
funds financial resources for acquiring assets
grant financial gift intended to fund a specific goal or project
gross profit selling price of a product or service minus its direct costs
income (profit-and-loss) statement financial statement that describes how much a company earned while the business was operating and what costs were incurred to generate those revenues
initial public offering (IPO) process by which a company lists its ownership shares on a public stock exchange
investing activities section of the statement of cash flows that shows major purchases of equipment or facilities
liability company's debt to another party
mature stage company lifecycle stage in which the business has reached commercial viability
moonlighting earning income from a source outside of one's primary employ
net income revenue minus expenses
operating activities section of the statement of cash flows that shows day-to-day activities of the business,

such as purchasing supplies, paying rent, and receiving cash from customers

profit margin amount by which revenue exceeds costs, typically described as a percent

program services basic offerings that a nonprofit provides to generate a portion of its revenue to sustain operations

projection forecast of the future operations of a business

revenue amount a business earns through product sales or providing a service

run rate cost of running a business over a specified period of time

seed stage company lifecycle stage in which the business is largely still an idea

statement of cash flows financial statement that explains the sources and uses of the company's cash

sustainable strategy strategy that can maintain an organization's financial stability

tax-exempt status treatment under U.S. tax law that removes the burden of taxes from nonprofit organizations

valuation estimate of a company's worth

variable costs costs that fluctuate with the level of revenue

venture capitalist individual or investment firm that specializes in funding startup companies

working capital funds available for day-to-day operations

Summary

9.1 Overview of Entrepreneurial Finance and Accounting Strategies

Entrepreneurial financing is concerned with understanding the funding requirements for a new business and what sources of funds are available. Each source comes with different expectations and requirements. Equity financing provides the entrepreneur with maximum flexibility: Dividends are not required and can be made when cash flow is strong enough to meet all obligations of the firm. Debt financing restricts financial flexibility but can be cheaper under some circumstances. For example, SBA loans can be subsidized by the federal government. Financing is not a one-size-fits-all procedure.

9.2 Special Funding Strategies

For nonprofit organizations, achieving a sustainable funding strategy requires hard work, creativity, and a delicate balance of financial resources. These types of organizations need to create programs that will interest patrons who are willing to pay for activities. They also rely on the generosity of their benefactors beyond simple patronage in the form of donations, and they vie for extremely competitive grant funding.

Although loans and liabilities such as credit card debt can fund a new business, the repayment and additional interest charges are a real challenge to many entrepreneurs. Financing strategies that avoid loans, such as crowdfunding websites and bartering, offer opportunities for funding that are often more manageable.

Bootstrapping is the process of self-funding a startup business. Sometimes entrepreneurs will have no financial resources beyond their personal savings. This method of funding a business requires creative approaches to problem solving, generating business, and managing expenses. It can be a slower, more difficult process than a company with more funding might face, but in the long run, it can benefit the company's strength and growth, and provide robust dividends to the founders.

9.3 Accounting Basics for Entrepreneurs

Accounting is concerned with how transactions are recorded in a way that helps entrepreneurs share information with stakeholders, including potential investors, and helps business owners make decisions about running their company.

9.4 Developing Startup Financial Statements and Projections

Entrepreneurs can use financial information for multiple purposes. These projections can help plan a new business. By forecasting the income and expenses of the first year, an entrepreneur can have a reasonable

idea of the level of financing that may be required. Second, these projections can also show potential investors what the business will look like in the future and how long it might take them to get a return on their investment. Break-even points help illustrate a minimum amount of sales to cover expenses.

Review Questions

1. What are the different stages in a company's lifecycle?
2. How do financing requirements change at different stages of a company's lifecycle?
3. What are the two most common categories of financing available to an entrepreneur?
4. What is the Small Business Administration?
5. What is an SBA loan?
6. What is a charitable organization?
7. What is a sustainable funding strategy?
8. What is social entrepreneurship?
9. What is crowdfunding?
10. What is bartering?
11. What does the term *bootstrapping* mean in terms of startups?
12. What purpose does an accounting system serve?
13. What key terms are used in the accounting equation?
14. How does accounting differ from finance?
15. What are the basic financial statements? What information do they provide?
16. What are projections used for?
17. What is a break-even point?

Discussion Questions

1. How do funding requirements differ in each stage of a company's lifecycle? Why?
2. What are the advantages and disadvantages of different sources of financing?
3. How does collateral factor into your financing options?
4. What challenges do nonprofits face in securing financing?
5. What are some potential benefits of a crowdfunding campaign aside from the funding itself? What are some potential drawbacks?
6. What are some of the sacrifices you could see yourself having to make to bootstrap your potential business?
7. How would you work around having limited access to capital in starting your own business? What difficulties can you see in trying to do so?
8. Which external parties would be interested in obtaining a firm's financial statements?
9. Why would investors require access to financial statements?
10. How do companies use financial statements in communicating with potential investors?

11. How can an entrepreneur use preliminary financial information in planning a new business?

Case Questions

1. Crowdfunding platforms, such as Kickstarter or GoFundMe, allow startups to access many different investors who may be able to contribute only small amounts in return for relatively small rewards. In the case of the iBackPack, those providing funds through Kickstarter were largely unaware of the company's postfunding operations.
   A. How did the lack of oversight harm investors?
   B. How might this situation have been different if a single angel investor had been involved?

2. Put yourself in the shoes of the manager of a nonprofit organization, such as a homeless shelter. The ultimate goal is to help people who have suffered misfortune get back on their feet. They likely cannot afford to pay or otherwise contribute to the costs of running the shelter. Thus, you must look to other sources to help pay the bills. Visit the website https://blog.hubspot.com/marketing/engage-major-donors-foundations-list. What are some ways you might be able to attract donors for the shelter?

3. While thinking about or visiting the coffee shop in your area, look around (or visualize) and identify items or activities that are the expenses of the coffee shop. Remember, expenses for the coffee shop are related to resources consumed while generating revenue from selling coffee and related items. Do not forget about any expenses that might not be so obvious—as a general rule, every activity in a business has an associated cost.

Suggested Resources

9.1 Overview of Entrepreneurial Finance and Accounting Strategies

Small Business Administration lending program: https://www.sba.gov/funding-programs/loans

"The Top Twenty Venture Capitalists Worldwide," *New York Times* (March 27, 2017): https://www.nytimes.com/interactive/2017/03/27/technology/Top-20-Venture-Capitalists.html?_r=0

National Public Radio "How I Built This" podcast series (example episodes: Instagram, Airbnb, Spanx): https://www.npr.org/podcasts/510313/how-i-built-this

TED Radio Hour (example episodes: Big Data Revolution, Disruptive Leadership): https://www.npr.org/programs/ted-radio-hour/?showDate=2019-07-05

9.2 Special Funding Strategies

Tax information for charitable organizations from the Internal Revenue Service: https://www.irs.gov/charities-non-profits/charitable-organizations

Information from the National Institutes of Health on grants and the application process: https://grants.nih.gov/grants/about_grants.htm

Small Business Administration, "How to Start a Non-Profit": https://www.sba.gov/blogs/how-start-non-profit

Kickstarter: www.kickstarter.com

Indiegogo, "The Essential Guide to Crowdfunding": https://learn.indiegogo.com/the-essential-guide-to-crowdfunding

Startupfest, "The $100K Investment Prize": http://www.startupfestival.com/news/100k-investment-prize/

G-Startup Worldwide's global startup competition: https://www.f6s.com/g-startupworldwide/

Extending Credit to Your Customers: https://fitsmallbusiness.com/invoicing-extending-credit-to-customers/

7 Ways to Bootstrap Your Business to Success: https://www.entrepreneur.com/article/254217

4 Must-Follow Tips for Moonlighting as an Entrepreneur: https://www.entrepreneur.com/article/298310

5 Ways Nonprofits Can Engage Donors: https://www.ama.org/publications/MarketingNews/Pages/5-ways-nonprofits-engage-donors.aspx

9.3 Accounting Basics for Entrepreneurs

Small Business Administration Introduction to Accounting Course: https://www.sba.gov/tools/learning-center-view-course/364071

Accounting Coach free Accounting Basics Explanation: https://www.accountingcoach.com/accounting-basics/explanation

Khan Academy Accounting and Financial Statements Course: https://www.khanacademy.org/economics-finance-domain/core-finance/accounting-and-financial-stateme

9.4 Developing Startup Financial Statements and Projections

U.S. Small Business Administration: https://www.sba.gov/blogs/3-essential-financial-statements-your-small-business

U.S. Securities and Exchange Commission: https://www.sec.gov/reportspubs/investor-publications/investorpubsbegfinstmtguidehtm.html

Forbes, 5 Financial Reports You Should Be Running: https://www.forbes.com/sites/sageworks/2018/03/26/here-are-5-financial-reports-you-should-be-running/#183ae98d6548

Medium, 3 Phases of Financial Indicators for Startups: https://medium.com/@DanielleMorrill/3-phases-of-financial-indicators-in-startups-b18ddb97f5f0

10

Launch for Growth to Success

Figure 10.1 Dropbox, founded by Drew Houston and Arash Ferdowsi, has realized unprecedented growth, as the company is valued in the billions of dollars. (credit: modification of "Dropbox" by Ian Lamont/Flickr, CC BY 2.0)

Chapter Outline

10.1 Launching the Imperfect Business: Lean Startup
10.2 Why Early Failure Can Lead to Success Later
10.3 The Challenging Truth about Business Ownership
10.4 Managing, Following, and Adjusting the Initial Plan
10.5 Growth: Signs, Pains, and Cautions

Introduction

Dropbox, a company founded in 2007 by Drew Houston and Arash Ferdowsi, has revolutionized the way consumers and businesses store and share electronic files. The idea came one day when Houston—on a commuter train—realized he left his thumb drive at home. This was not the first time he had forgotten that tiny electronic filing cabinet, and he was sure others forgot often as well. So he hit on an idea: storing his files on a "cloud" on the Internet that anyone could access from anywhere with any device.[1] He wanted to manage file storage at faster speeds and in larger quantities than the few existing online storage systems, through an easy-to-use interface. Although Houston came up with the idea of cloud *storage* during his commute, cloud *computing* had been talked about in industry circles a few years prior.[2]

Hopeful, he introduced his idea to Y Combinator, a venture capital firm in California that helps fund startups by hosting, training, and helping them define their pitches to investors. Even though they had rejected a business idea he'd presented earlier, they told him the new idea was promising and asked him to secure a co-founder before pitching. A co-founder would help to secure funding because it showed the idea had legitimacy, support, and the expertise of another person. Houston quickly found Ferdowsi, a fellow MIT student studying engineering and computer science.[3] Together, they raised $1.2 million from investors, even though their prototype wasn't fully functional. They then hired developers and engineers who created a more functional version that worked across most computer operating systems.

1 Sarah Buhr and Katie Roof. "A Brief History of Dropbox." *TechCrunch.* March 6, 2018. https://techcrunch.com/gallery/a-brief-history-of-dropbox/slide/1/
2 Johnson Hur. "History of Online Storage." *BeBusinessEd.com.* n.d. https://bebusinessed.com/history/history-of-online-storage/

Dropbox was soon using *lean startup* principles, which meant releasing an early version to early adopters. Houston had a difficult time explaining the product to initial users, so he developed a video with a quirky narration to entice them. The early product release was a hit: In one day, their customer base increased from 5,000 to 75,000 users, who could also provide them with feedback for subsequent versions.

Thanks to its massive success, Dropbox was valued at $10 billion in 2014.[4] However, some analysts believed the number was inflated as Dropbox's competitors started gaining market share. The company continues to receive customer feedback to make the iterations necessary for better versions.

10.1 Launching the Imperfect Business: Lean Startup

Learning Objectives

By the end of this section, you will be able to:

- Describe how businesses use lean startup principles to develop products and test markets
- Identify how the *build-measure-learn* method helps companies understand what potential customers want in a product
- Determine what a minimum viable product (MVP) is and explain why companies don't need to have a perfect product to launch
- Explain why companies need to learn to construct a lean pitch to investors and potential customers
- Explain what pivoting is and when it is necessary for companies to undertake

As you can see from the Dropbox example, businesses can function without being perfect. The company initially provided a short video description of the Dropbox product (https://openstax.org/l/52Dropbox) without even having it coded to the actual program first.[5] This way, they could test the idea and receive customer feedback without losing time or money on products that wouldn't work. If any changes were needed, they had the flexibility to make them because it was just an early prototype and no big investment on the product had been made yet. Many of the early changes were to the interface design that involved buttons and actions that could be taken, and storage capabilities that customers consistently gave feedback on.

New businesses need time to develop their identities, engage their target market, create and develop the right products, and sharpen their strategies. Startups don't have fully developed and proven business models like established companies do. A business's starting focus or idea may evolve into something else because the initial feedback from the prototype points in a different direction.

Houston (pictured in Figure 10.2) and Ferdowsi knew they did not have the perfect product, so they employed a system called **lean startup**, a methodology entrepreneurs use to help them innovate by continuously testing their products and getting feedback from customers in real time. This methodology calls for a product to be shared with early adopters in its beginning stages of development and gain immediate feedback. It ensures that people actually like a product and are willing to buy it. Tech companies primarily use this method because they have learned that too many years working on a product without measuring is highly risky, especially in a rapidly changing technological environment. Lean strategy, though, is applicable to almost every business and industry.

Even with Dropbox's reported $1 billion in revenue and 500-plus million users, Houston's journey still has its ups and downs. He learned that the CEO's job changes as the venture progresses because the company's needs vary across its lifecycle. The CEO has to shift focus, such as on building prototypes, testing users, exploring the best distribution channels, and managing cash flow. These hurdles need to be tackled when they arise.[6] Let's take a closer look at lean startup, and how it got its own start.

3 "How I Met My Co-Founder: Drew Houston, Dropbox." From *Finding Your Way as an Entrepreneur*. May 30, 2012. https://ecorner.stanford.edu/in-brief/how-i-met-my-co-founder/

4 Eliot Brown and Jay Greene. "Dropbox Files for IPO Three Years after $10 Billion Private Valuation." *The Wall Street Journal*. January 11, 2018. https://www.wsj.com/articles/dropbox-files-for-ipo-three-years-after-10-billion-private-valuation-1515708036

5 "The Original Dropbox MVP Explainer Video." *Allen Cheng*. n.d. https://www.allencheng.com/dropbox-mvp-explainer-video/

Figure 10.2 Andrew Houston believes that, as a CEO, you must shift your focus as your business needs change. (credit: "Drew Houston (Dropbox) by Financial Times/Wikimedia Commons, CC BY 2.0)

Lean Startup

Author and entrepreneur Eric Ries developed the lean startup methodology after spending much time, effort, and money when his first tech company had to close down. Fortunately, Ries' frustration led him to study other successful companies and lean manufacturing programs, including the highly successful Toyota lean manufacturing process, which taught him how to be flexible and quick while building products. He learned that he didn't need to have a fully designed product resulting from years of development; instead, he could have something imperfect that worked without the bells and whistles, something that people could test and provide feedback on over time.

LINK TO LEARNING

Steve Blank is the creator of the customer development methodology that is considered a cornerstone of the lean startup movement. Watch his presentation on the methodology's most important concepts (https://openstax.org/l/52BlankLean) to learn more. These components are the heart of Toyota's 14 management principles (https://openstax.org/l/52ToyotaWay) known as the Toyota Way.

He advocated a step-by-step approach on how to maneuver a startup, how to change course if necessary, persevere, and accelerate its expansion. This is also called the **build-measure-learn loop**, which means that a prototype is built, or at least the idea is written down, it is then pitched to customers who provide feedback so the company learns what to keep and what to change, then it makes the changes to the prototype, and starts all over again, repeating the process until the prototype is good enough to go to market. Figure 10.3 illustrates this loop. Even after it hits the mass market, this loop can continue to be used to enhance the product.

6 Scott Rosenberg. "Inside Dropbox's Identity Overhaul." *Wired*. January 30, 2017. https://www.wired.com/2017/01/inside-dropboxs-identity-overhaul/

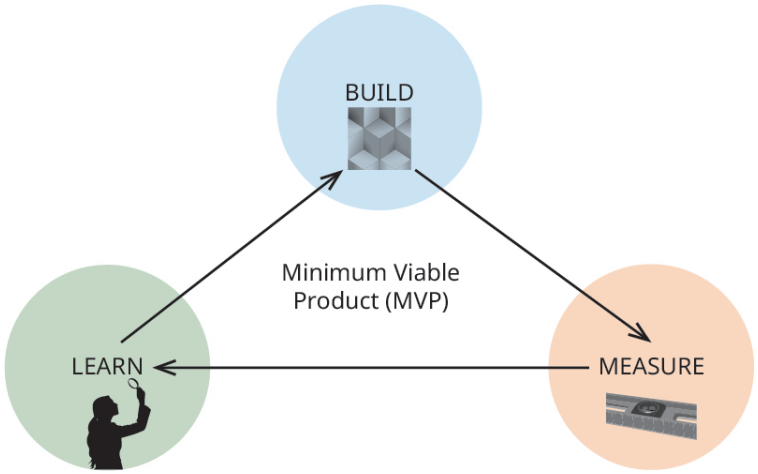


Figure 10.3 The build-measure-learn loop is a framework that helps entrepreneurs develop their idea into a minimum viable product (MVP), measure its impact on people, and learn if there is a need to pivot (change) or persevere. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

After his first startup proved unsuccessful, Ries created a second company called IMVU.[7] IMVU is an avatar platform, or "metaverse," for people who want to shop for clothing, furniture, and accessories in an online community and keep their identity safe. Essentially, IMVU is a virtual reality world with an e-commerce engine, user-generated content, and 3-D characters. While Ries was building IMVU, he and his co-founders worked endless hours for six months to create a prototype of 3-D avatars that they later learned no one wanted. During their first month, they made a total of $300. The next month they made $400 after begging friends and family to try it.

After Ries saw their faithful first customers disappear, he and his co-founders decided to shift from feeling frustrated to talking to potential customers. They tested their product with teenagers and heavy users of technology, as well as with mainstream customers. The mainstream customers never knew what to do with the product. They thought it was too strange. But those that were more tech savvy and younger were happy to try it. They gave a lot of feedback that resulted in creating a better version of the avatar community.[8]

The initial platform was designed as a **minimum viable product (MVP)**, which is a very early prototype of a product.[9] According to Ries, an MVP can be the bare minimum to help people understand what the product is about. A product doesn't even have to be built to be an MVP; instead, it can be represented in sketches, videos, and explanations of how it might look. MVPs also can include a basic version of the product, just like IMVU's website, which was not very good at first. The point is to have a basic product to show to potential users, with enough substance to elicit feedback on what people find useful and what attributes are important without having to invest a lot of money and time. There is no right or wrong type of MVP. It is up to the owner to decide how to showcase the idea and test it to find out what people like and don't like, and how to take the idea to the next level.

Through this MVP experience, Ries (shown in Figure 10.4) realized that his first platform had bugs and issues that could crash users' computers; however, in spite of the bugs, he was determined to get customer feedback without spending lots of cash or time. Once he and his co-founders had the low-quality platform running, they decided to charge a fee for the service. They would send dozens of changes to their loyal followers until they developed a product that would work for a larger customer base. These changes included adjustments such as adding new avatars, new avatar movements, choices of clothing, and new worlds for avatars to explore. IMVU pioneered this lean startup approach, which new ventures all over the world now use. Today, IMVU is a successful enterprise with over $55 million in revenue and 50 million users.[10]

7 Eric Ries. *The Lean Startup* (New York: Crown Business, 2011), 1–8.
8 Eric Ries. *The Lean Startup* (New York: Crown Business, 2011), 43.
9 Eric Ries. *The Lean Startup* (New York: Crown Business, 2011), 43.
10 IMVU Inc. "IMVU Inc. Celebrates Nine Years of Connecting People around the World, Expands Profitable Business to Mobile." *PR*

Figure 10.4 Eric Ries, third from left, speaks at a conference about the lean startup process he developed while creating his second business. (credit: modification of "Eric Ries TechCrunch Disrupt" by "kawanet"/Wikimedia Commons, CC BY 2.0)

A lean startup begins with the first stage of *building* a basic product (MVP) that has only its core benefits and no extra features. Houston and his developers created a basic platform for early adopters to test. **Early adopters** are people who like to try new products as soon as they come out. They don't mind, for example, buggy software or cumbersome designs because they are innovators and like to test new things. Dropbox did not create a perfect product initially because the developers did not know what it would be until they got user feedback. After early signups and feedback on the first prototype, they were able to create the first version of the product. Later, they conducted **iterations**, or additions or changes to the version of the product, using customers' ideas and suggestions.

Zappos is another example of an MVP development project. Nick Swinmurn, creator of the online shoe company, launched the idea in 1998 by creating a bare bones website to sell shoes and measuring traffic to the site.[11] The idea started after he took a trip to the mall and could not find shoes in the styles or colors he wanted. He figured other people had equally frustrating experiences. His first hypothesis was that people were interested in buying shoes online, so he asked Tony Hsieh, current CEO of Zappos, to invest in this new project. Hsieh provided half a million dollars to get the company started. Swinmurn then created a plain webpage that started with basic photos of shoes and their prices. Swinmurn also ran ad campaigns, measured web traffic, and adjusted the webpage. Instead of spending so much time in building a detailed plan about his business, this method helped him make quick adjustments to the product, the target market, and strategies using the build-measure-learn loop and starting with an MVP, just as Houston did.[12]

WORK IT OUT

Five Lean Principles

Go to the website http://theleanstartup.com/#principles and click on the link "Lean Startup Process In Detail."

- Pick one topic that interests you and write a one-page summary of the concept.
- Add an example to illustrate the topic.

Going deeper into this *build* stage, we can see that the steps take an entrepreneur through a cycle or loop that begins with defining the problem at hand and building the MVP to show potential consumers a sample of the

Newswire. April 8, 2013. https://www.prnewswire.com/news-releases/imvu-inc-celebrates-nine-years-of-connecting-people-around-the-world-expands-profitable-business-to-mobile-201920201.html

11 "Lean Startup Zappos: The Basics." *Bullet*. n.d. https://www.bullethq.com/lean-startup-zappos-how-zappos-validated-their-business-model-with-lean/

12 "The Lean Startup Methodology." *The Lean Startup*. n.d. http://theleanstartup.com/principles

product and see how they react. In many cases, selling this low-quality product can also help measure user reactions. Metrics, or measurements, are developed to test the product assumptions of the engineers who created it. The goal is to test the MVP with its target market by asking questions about the design, usability, core or bundle of benefits, and other attributes that enhance the customer experience.

For example, different design attributes can be measured by asking customers if they like a feature or set of features of the product they are testing. The number of likes or dislikes can be tallied, and comments can be collected on what additional features should be added or deleted. Once the feedback comes in, entrepreneurs can make changes. Then, they can move into the next stage, which is to *measure* whether the changes to the product based on the feedback are actually helping make progress.

Along with a minimal product offering, Ries advocates using a minimal financial evaluation concept called **innovation accounting** to assess whether the changes made to the product are creating the desired results. This means that entrepreneurs should not look first to the basic financial measurements traditional to businesses—such as sales, profits, and return on investment—because these traditional measurements aren't the most relevant metrics at this stage. Instead, they should measure progress in a different way. Measurements may include testing assumptions about the business, attributes that customers like, sign-ups, and retention rates that can be separated into cohorts and tested, say weekly, as changes to the products are made.

LINK TO LEARNING

Read this article on innovation accounting (https://openstax.org/l/52InnovAccount) and notice the available metrics that measure progress and the instances in which they are effective.

During the *learn* stage, the entrepreneur uses the feedback obtained to assess the progress of the product in an objective manner. The entrepreneur makes changes to the MVP and starts the cycle over again until the process has reached a point where it either accelerates or needs to pivot.[13]

As a learning component for the company, feedback is very important in the lean process. Feedback helps companies design better products and make iterations, or newer versions, which better serve the customer base. Companies will work with early adopters for a while before they expand their reach with a better product and entice more people to use it.

ENTREPRENEUR IN ACTION

General Electric Is Big *and* Lean

General Electric (GE) is a company that has been around for many years and boasts a tremendous portfolio of businesses under its parent company. Eric Ries managed to encourage this giant to take advantage of the lean startup movement by collaborating with him in a new program called Fast Works. This program was essentially created to imbue its product development method with the principles of lean innovation by training thousands of employees in the methodology and helping them develop desirable products at a faster pace.

13 Eric Ries. *The Lean Startup* (New York: Crown Business, 2011), 76–183.

For example, GE improved a turbine using the lean approach by asking for customer feedback. Many customers needed different features, such as improved reliability, better fuel efficiency, and faster operation. The team working on this project decided to use Fast Works to fulfill all of the customers' requests. This approach would allow them to shorten the development process and save the customers money. Three hundred members of the GE turbine team knew that this would be a difficult task given their locations around the world and the processes involved in approvals, so they got to work. Some focused on streamlining the approval process, while some worked on bottlenecks and encouraged low-level engineers to make difficult decisions without asking upper management. These two changes allowed them to pivot quickly, while gathering feedback and making changes to the turbine effectively. After using FastWorks, the team reduced development time by a quarter—from four to three years. They saved $5 million dollars in fuel per year for their customers, while increasing their revenues by $6 million per year.[14]

Iterating, Pitching, and Pivoting

Many companies invest significant time and effort on projects that seem like great ideas in theory but flop when taken to market. The lean startup method is a new way to develop and manage products that people want in a shorter period of time. Companies are able to learn from customer discovery and validation that the offer or value of the product is not working and needs to be enhanced or changed.

After Ries experienced his first business loss, he recognized the problem of companies devoting time and money on projects rejected by consumers, and he wanted to identify a solution. As he started his new company's avatar community, he enabled his teams to put the product through iterations—those small changes to the current version of a product to make it better fit consumer needs. At this phase, and using lessons from his first failure, he strove to create a bare-bones version of a product that worked well enough to provide core value to the customer, garner customer feedback, and make small adaptations around what users considered most essential. This allowed IMVU to enhance the product in a way that brought the company, step by step, closer to providing the best value.

One iteration that proved enormously successful was adjusting how the avatar moved through its virtual reality world. The original avatars didn't have the ability to walk around like they do in, say, popular multiplayer video games. Even though he knew this was a disadvantage, he sent the version to early adopters and asked for feedback. Customers responded that the lack of movement suggested the software was low quality. Reluctant to make the major tech investment for this movement, Ries and his team decided to try a very small iteration as an alternative: They made the avatar disappear from its starting point and reappear in its new location. Customers responded positively, seeing this as superior to what existed and as a high- quality variation. The quick and low-cost iteration turned out to be the best path to success.[15]

In addition, while this process is ongoing, the entrepreneur is constantly pitching the idea to potential consumers and investors. Pitching can be intimidating for entrepreneurs, as they can get nervous speaking in front of people. However, pitching can be as important as building the right product for the right target: It needs to be practiced and mastered.

Pitching is the verbal delivery of an idea or business plan, and a request to a group of investors, customers, or potential business partners by an entrepreneur (Telling Your Entrepreneurial Story and Pitching the Idea). As an entrepreneur, knowing how to pitch your business concept to investors is one of the keys to success. However, if you're using the learn startup approach, your pitch likely needs to be quite different from a regular pitch.

14 Bruce Watson. "The Startup Power Plant: These Engineers Are Building Turbines the Silicon Valley Way." *General Electric*. May 3, 2017. https://www.ge.com/reports/startup-power-plant-adapting-silicon-valley-methods-building-turbines/
15 Eric Ries. *The Lean Startup* (New York: Crown Business, 2011), 108.

The **lean pitch** requires the presenter to craft an exciting and well-developed story about the company, its product, and what makes the product unique, with enough detail to show that the company is more than a story in the presenter's mind. The lean approach is customer centric and tries to solve customers' problems and resolve issues, and it measures its product over and over again until it is right. The story must show the process of understanding their customers as well as their problems and issues. Then, there must be an explanation of iterations, design tests, and learning from customer feedback that demonstrates the customer-centric approach. Experiments, data, and insights are shared to show the company's progress. As you recall from Telling Your Entrepreneurial Story and Pitching the Idea, using a regular pitch approach, the presenter gives all of the details of the product and the future launch. This traditional pitch asks for an investment without having tested assumptions or having much data or experiments to show that the idea will work.[16] Increasingly, successful lean pitching requires the presenters to have some sort of validation of their business model because this shows more truth to the vision. Many investors look for companies that have some time invested and a seed customer base under their belt. They are particularly interested in those who know their sales numbers, their costs, their sales projections, and have a track record of increased sales, customers, and profit. Table 10.1 shows a step-by-step approach to pitching to investors and potential partners.

Lean Startup Pitching

Step	Tips
1. Tell an exciting story that quickly moves into tangible results	Don't do a sales pitch; be yourself by being open and authentic. Craft an exciting and well-designed story to capture your audience and introduce this as a business that is already up and running so investors know from the beginning that you are using lean startup techniques.
2. Describe the problem and solution at hand and what makes you unique.	Clearly define the problem you are solving and how you are already solving the problem with the best tested/measured solution.
3. Describe the target market and how it will benefit from the product.	Show that you understand your potential customer because you have gotten customer feedback. Give examples of early product development and share key customer feedback that helped you enhance or incorporate new benefits. Demonstrate the product, focusing on the benefits, not the features.
4. State your position with facts and achieved results.	Show additional tests, experiments, customer feedback, and anything that can back your claims. Show actual data and insights collected, emphasizing validated facts and assumptions you have made. Describe early challenges and how you adapted without giving up.
5. Be simple	Don't use jargon. Speak as if you were explaining it to a stranger sitting next to you in a coffee shop.

Table 10.1

16 Andy Cars. "How to Pitch to Investors Using a Lean Startup Approach." *Medium.* March 15, 2017. https://medium.com/lean-startup-circle/how-to-pitch-to-investors-using-a-lean-startup-approach-852f7a503d84

Step	Tips
6. Show current progress	Show what you have accomplished in sales/profit so far.
7. Finish with the ask	Close up your pitch by identifying what you are seeking. If you are looking for an investment, a partnership, a new member to join you, or an advisor, finish with the ask.

Table 10.1

After carefully going through the build-measure-learn loop, there comes a point where the company either accelerates or realizes it's time to pivot. **Pivoting** is a crucial and often difficult change done to test a hypothesis regarding the basic product, its growth potential, and business model. Once the product has been tested and retested for changes in consumer behavior, or any metric that the company sets itself to attain, if it's not attaining growth, then the next step is to pivot instead of continuing down the current path.

This is a time for tough decisions: Should you continue working on the business, product, or project—or should you change? Is the company making progress toward its goals, or do the strategies need major adjustments? While measurable data, such as attribute likes and dislikes, or number of sign ups, are gathered during the measure stage, the lean startup process also has a component that is creative, intuitive, and visionary. Knowing when to change cannot be determined solely through number crunching. It also requires human judgment, which, when coupled with the build-measure-learn formula, can lift a company out of mediocrity.

WORK IT OUT

Ten Ways to Pivot

Read this article from Forbes.com to see more examples of the kinds of pivots entrepreneurs can make: https://www.forbes.com/sites/martinzwilling/2011/09/16/top-10-ways-entrepreneurs-pivot-a-lean-startup/#3286d2422d2b.

- Which one(s) would be best for your current business project? Why?
- What product features would you have in place to ensure future growth without investing too much?

If a business is not growing, it is shrinking or stagnating.[17] A pivot, just like in basketball, requires one foot down on the ground, and the other moving. This means that you keep what you have learned from customers as your grounding foot but test out a different direction in which to move. Here are examples of famous pivots:

- Twitter transformed into a social media giant from a company called Odeo, a broadcast platform that was initially created to transmit video, sound, and podcasts. However, Apple beat them by launching iTunes podcasting, and it didn't make sense for the founders of the company to pursue that path, so they decided to create Twitter instead.
- PayPal (formerly Confinity) allowed people to send electronic payments or "beam" payments from their Palm Pilots (first personal digital assistants created by Palm Computing) as well as from other devices. At that time, PayPal users registered a card number, downloaded the beam application, and were able to make transfer payments from one device to another. As technology changed, it merged with X.com to

17 Eric Ries, *The Lean Startup* (New York: Crown Business, 2011), 149–178

become the preferred payment method on Ebay, helping the company go mainstream.
- Avon was created by a traveling book salesman who would add perfumes to his sales as perks for his woman customers. Eventually, he realized that women were more interested in the perfumes than the books, so he started a new business from a small office in New York.
- Fab.com, a design e-commerce website, was initially called Fabulis, and it started as a social media site to connect gay men. After the social media site failed, the co-founders took it into a new direction by selling their design picks for the best home goods, accessories, and clothing for everyone.[18]

WORK IT OUT

The Market for Experiences

Since the 2009 recession, people have spent more on *experiences* like travel and dining, rather than goods. Instead of owning many products, people, especially Millennials and Gen Zers, are transforming many industries. They prefer to travel by Uber and have an Airbnb experience where places and people are more important than things. They would rather freelance than work for a corporation and are more likely to try new foods and entertainment instead of accumulating possessions. This market trend has led many large retailers to downsize or close all together. Smaller retailers have been hurt as well. However, online retailers, home stores, and grocery chains have remained largely immune to the changes in buying habits.

- If you were a specialty retailer that focused on selling sports clothing and gear, and had several regional stores around the country, how would you pivot your business to avoid slowing sales?
- Create a step-by-step list of your main strategies and how each would help avoid closing down your business.

You may wonder, how many times can a company pivot? Ries likes to use a runway analogy: You must measure how long you have until your company can achieve its goals, and whether you fail to lift (burn through all your cash resources) or have a liftoff (generate sales, sign ups, add new customers). The runway can be calculated by taking the amount of cash that is in the bank and dividing that by how much is being spent or drained on that balance. So if your company has $550,000 in the bank, and it drains or burns $50,000 per month, then you have a projected time of 11 months (550,000/50,000). A way to slow down the cash drain—and to extend the runway—is to cut some costs or ask investors for additional cash.[19]

There are also different types of pivots for different needs. Table 10.2 shows ten pivots an entrepreneur can make according to feedback.

Types of Pivots[20]

Pivot Strategy	Description
Zoom-in	A product's single feature becomes a whole product.
Zoom-out	This is the reverse of zoom-in. A single feature is not enough for a customer, so the product needs added features.

Table 10.2 Eric Ries outlines these ten pivot strategies in *The Lean Startup*.

18 Jason Nazar. "14 Famous Business Pivots." *Forbes*. October 8, 2013. https://www.forbes.com/sites/jasonnazar/2013/10/08/14-famous-business-pivots/
19 Eric Ries. *The Lean Startup* (New York: Crown Business, 2011), 160.
20 Eric Ries. *The Lean Startup* (New York: Crown Business, 2011).

Pivot Strategy	Description
Customer segment	There is a need to change the customer segment, as the one studied is not representative of who will buy the product at a larger scale.
Customer need	Feedback from customers shows that the problem solved is not important. The product needs to be repositioned, or a new product needs to be created to solve a real problem.
Platform	A change from an application to a platform or the other way around is needed. Startups usually begin with what is called a "killer app" for their platform, which later becomes a way for third parties to create their own products.
Business architecture	This is a change from high margin, low volume to low margin, high volume. This happens in business-to-business (B2B) and business-to-customer (B2C), respectively.
Value capture	These are changes in monetization or capturing value (raising capital).
Engine of growth	A startup changes its engine of growth (sticky, paid, or viral paid growth models for revenue). Usually, the company requires a change in the way it collects revenue.
Channel	Distribution channels are changed when the product requires faster or broader alternatives to reach consumers. The Internet has become a great disruptor of channels.
Technology	Sometimes achieving a solution that serves an existing customer through cheaper means occurs when other technology is used (new production equipment, new software, etc.). This is more common with established businesses.

Table 10.2 Eric Ries outlines these ten pivot strategies in *The Lean Startup*.

ENTREPRENEUR IN ACTION

Nintendo

Nintendo could have gone sour in the gaming world had it not made a fateful pivot at a stark time. Created in 1889 (surprising, right?) in Kyoto, Japan, Nintendo manufactured "hanafuda," or flower cards (pictured in Figure 10.5) **(a)** used to play card games. It was humming along until the card game industry started to decline in the 1960s. Fusajiro Yamauchi, founder of Nintendo, tried to move into other markets by also providing hotel and taxi services. These pivots proved unsuccessful choices, and Nintendo almost closed its doors. However, it continued to manufacture its cards, which now had a plastic coating, and, thanks to a deal with Disney, had moved into the character cards market.

Still, the company hobbled along until, thankfully, one of the line assembly engineers created a device that would reboot sales. He designed a toy called the Ultra Hand, which children could manipulate to reach objects far and away. After successfully selling a million units, the company rebranded itself as Nintendo Games and entered the growing toy market.

Their foray into video games found its first success with the release of the Color TV Block Breaker game in 1977 (pictured in Figure 10.5 **(b)**). In 1981, when technology was changing the gaming industry, Nintendo created Donkey Kong, and later in the 1980s, Mario Brothers. Thanks to this great pivot, Nintendo is now worth over $22 billion and continues to thrive as one of the top gaming companies in the world.[21]

(a)

(b)

Figure 10.5 Nintendo started as a small company that created (a) Hanafuda cards and (b) the Color TV Block Breaker. Today Nintendo is one of the largest companies in the gaming industry valued at over $22 billion. (credit (a): modification of "Koi-Koi Setup" by "Aldaron"/Wikimedia Commons, CC BY-SA 3.0; credit (b): modification of "Nintendo-Color-TV-Game-Blockbreaker-FL"by "Evan-Amos"/Wikimedia Commons, Public Domain)

10.2 Why Early Failure Can Lead to Success Later

Learning Objectives

By the end of this section, students will be able to:

- Determine several reasons for business failure and explore strategies to overcome them
- Understand the root of fear of failure
- Learn to spot signs of fear of failure and take steps to overcome it

Your goal in your venture is to achieve success—ideally, fairly quickly—but most successful entrepreneurs experience some failures along the way. While these setbacks can be discouraging, they provide lessons and experiences that can lead to eventual success. Whether a new business is a retail store, restaurant, hair salon, consulting company, tech firm, or manufacturing plant, the truth is that many businesses fail within the first couple of years. According to Bloomberg, only 20 percent of new businesses find success within their first eighteen months.[22] Data from entrepreneur.com and the Small Business Administration suggest that only 30 percent of new ventures succeed to the ten-year mark.[23,24] For women and minorities, the percentages are even lower. Success and longevity are possible, of course, but it takes a lot of work, and sometimes it takes a second or third try.

Entrepreneurs recognize that failure is part of the success of being a business owner. **Business failure** is the ending of a business due to the lack of goal attainment, which can mean low levels of revenue and profits, or not meeting investors' expectations. Business failure can result in the loss of assets—such as revenue, equipment, and capital—and can cause trauma for the business owner. However, these failures often help entrepreneurs improve the outcomes for their next business, as they have now learned valuable lessons that

21 Mary McCoy. "5 Cases of Companies That Successfully Pivoted Business Models." *Continuum*. July 21, 2015. https://www.continuum.net/blog/5-cases-of-companies-that-successfully-pivoted-business-models
22 Eric T. Wagner. "Five Reasons 8 out of 10 Businesses Fail." *Forbes*. September 12, 2013. https://www.forbes.com/sites/ericwagner/2013/09/12/five-reasons-8-out-of-10-businesses-fail/#1c5fbca26978
23 Patrick Henry. "Why Some Startups Succeed (and Why Most Fail)." *Entrepreneur*. February 18, 2017. https://www.entrepreneur.com/article/288769
24 "Frequently Asked Questions." *US Small Business Administration Office of Advocacy*. June 2016. https://www.sba.gov/sites/default/files/advocacy/SB-FAQ-2016_WEB.pdf

can be applied to new projects.

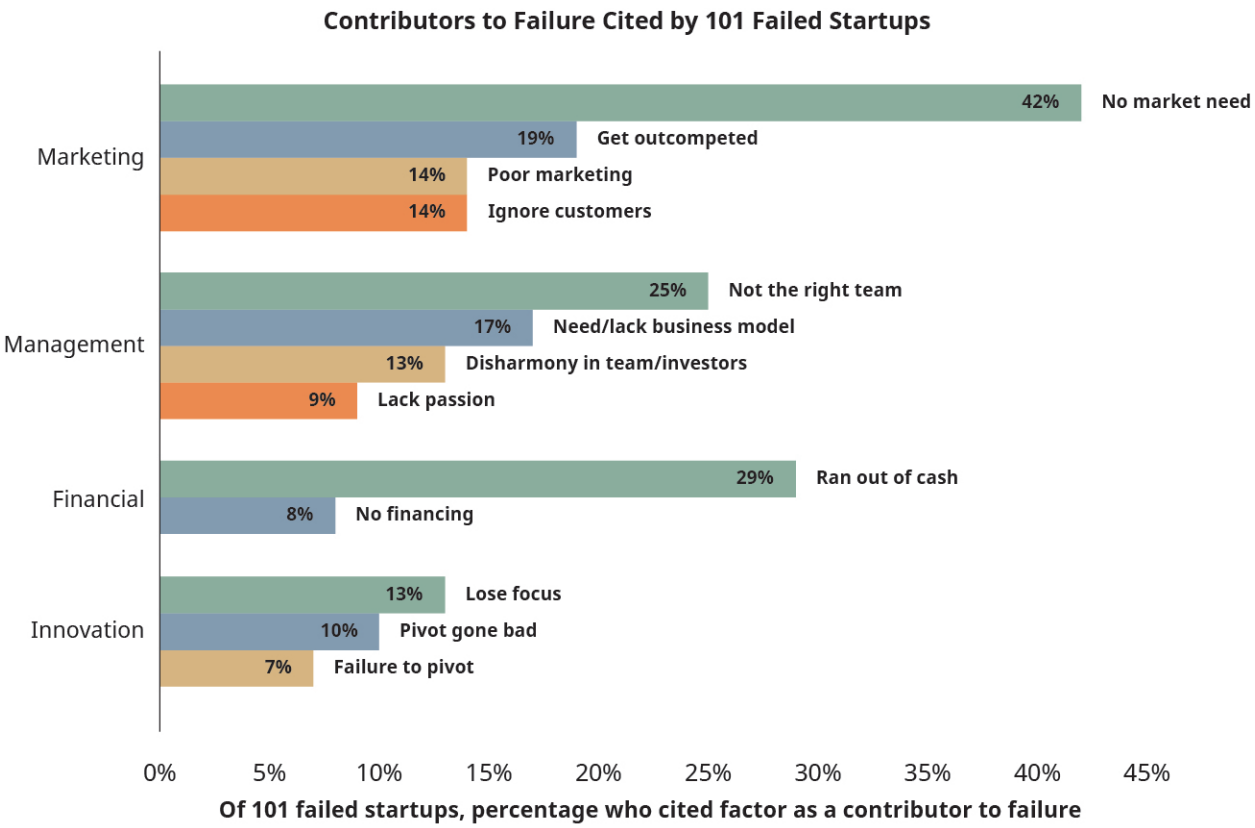
As Jack Ma, billionaire founder of Alibaba (the biggest and most profitable online retailer in China) said, "No matter what one does, regardless of failure or success, the experience is a form of success in itself."[25] Ma experienced many failures—including being rejected from job opportunities and universities he wanted to attend, and having his pitch rejected by all but one person in a room full of friends. But he persevered, founded Alibaba, learned as he went, and today runs China's largest online retailer with almost $24 billion in revenue.[26]

Another company, Quirky, launched by Ben Kaufman in 2009, was an initial failure. Quirky was a platform that allowed inventors to submit their ideas to a panel of Quirky experts who would then manufacture the product at a low price and sell it to different markets. Initially, Quirky gained $185 million in funding and had support partnerships from Amazon, Bed Bath & Beyond, and Best Buy. Thousands of people flocked to the site and submitted their inventions to get seen and voted on. Unfortunately, Quirky struggled to sell many of the products at a sustainable profit margin and filed for bankruptcy in 2015 after investors stopped funding the venture. Fortunately, one of its businesses, the smart-home business section, was spun off and sold as Wink in September 2017. The company was rebooted by a new set of entrepreneurs with a better business model.[27]

Common Contributors to Failure

There are some common reasons for failure that often combine to end a business. However, there are often ways to prevent these failures from happening. CB Insights, a company that mines and analyzes data for companies and uses machine learning to help them answer complicated strategic questions, researched the factors that contributed to the failures of 101 startups. Figure 10.6 shows some of the main factors they identified in their research.

25 Zach Ho. "Jack Ma: If You're Still Poor at 35, You Deserve It!" *Vulcan Post*. April 15, 2014. https://vulcanpost.com/7702/jack-ma-youre-still-poor-35-deserve/
26 Zach Ho. "Jack Ma: If You're Still Poor at 35, You Deserve It!" *Vulcan Post*. April 15, 2014. https://vulcanpost.com/7702/jack-ma-youre-still-poor-35-deserve/
27 Jessica Sylvester. "The Rise and Fall of Quirky: The Startup That Bet Big on the Genius of Regular Folks." *New York Magazine*. September 13, 2015. http://nymag.com/daily/intelligencer/2015/09/they-were-quirky.html



Source: CB Insights. "The Top 20 Reasons Startups Fail." n.d. https://s3-us-west-2.amazonaws.com/cbi-content/research-reports/The-20-Reasons-Startups-Fail.pdf

Figure 10.6 Startups that falter identify some common obstacles to success. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

In the following discussion, we expand on some of these reasons for failure and offer advice on how to avoid them. Considering the following failures will give you an idea of what may go wrong in a business but will also help you spot and correct them before you launch.

Marketing Failure

Some of the most common failures result from marketing missteps.

- *Lack of differentiation of product or service*. Creating or running a company with a me-too mentality and without a clear unique selling proposition or difference from other established businesses can be detrimental. Answering questions such as "Why should customers leave other companies to buy my product?" "What is a benefit I provide that no one else does?" and "If I open a yogurt parlor in a commercial area, what will help my business differentiate itself from all the other yogurt, ice cream, dessert, and fast food places?" can help create ways to be special rather than a me-too business. This also needs to be defined in your mission, within your products and their benefits, and a clearly defined competitive advantage that can be translated into a superior value proposition. The chapters on Entrepreneurial Marketing and Sales and Identifying Entrepreneurial Opportunity discuss competitive advantages and value propositions in more detail.
- *Missing the right customer*. Not reaching the target market can lead to failure. Perhaps for your travel tour business, you targeted single people ages 18–34 who like to experience travel in a different way, but maybe your true target—the people who want to book your tours—are couples with children and those 50 and over. You would have sent out marketing communications to the wrong age group. Or, the right message is not being conveyed and your positioning is off, preventing you from connecting with your true consumer. Conducting market research as discussed in Entrepreneurial Marketing and Sales and testing your communication with various targets can help better define your customer.

Management Failure

These are some typical management challenges that can prove detrimental.

- *Passion wanes or not the right business*. Sometimes the reason a business fails is due to a simple reason: The founder has lost excitement over the business and is no longer interested in making it succeed. Other times, the problem may stem from not having the right focus or idea, which can come from a lack of awareness about trends in the market. Joel Delgado, a young entrepreneur who started El Paso's first escape room called El Paso Disaster Room 915 in 2015, developed this business with three of his friends right after college. Although the business was very well received by young people who wanted this new form of entertainment, a few years later, he decided to close down the business and pursue a career in teaching. His passion had waned. Sometimes, entrepreneurs get bored with their startup, but there are ways to keep the business exciting by changing the product offerings.
- *Fighting founders*. Not agreeing over the strategies and direction of a business can deter companies from moving forward. If the founders are not working together and disagree too much, this can help dissolve the business quickly. Differing points of view can be healthy for a business, as these can bring other complementing perspectives, but when conflict doesn't get resolved, it can be difficult to continue moving forward. Some business partners have found themselves ousted by their business partners because the relationships have suffered a deep strain. This happened to Steve Jobs in 1985 when he was let go by his own company. Often, it is difficult to assess when conflict will arise, so it is recommended that business partners work with people who have the same love for the business and its core values, even if they bring different strengths and temperaments to the table. This may reduce fights and sustain relationships. Having a contract in place that defines who is in charge of what part of the business, their compensation, and what happens if anyone departs, is a good way to ensure that the investment won't be lost if partners decide to part ways.
- *Lack of planning*. One of the surest roads to failure is to not have a business plan or marketing plan. Even using the lean startup method requires some sort of planning before embarking on the process. Planning helps business owners flesh out ideas and understand the business better. Following the business plan in Business Model and Plan and the marketing plan in Entrepreneurial Marketing and Sales can help solidify where the business is headed, whether its viable, and what resources are required to make it work. For example, imagine a business owner who opens a restaurant in an already-crowded market only to realize how much competition existed in the area. If the owner had researched and planned ahead, the venture could have been differentiated through the type of food offered, the location, or different promotional tactics to build clientele. Failure to plan in a situation like this can result in struggling to keep afloat and can lead to successive challenges. For example, the owner might raise prices to compensate for lower-than-expected revenue, but higher prices may drive away an already fragile customer base, and the venture may not be sustainable.

Financial Failure

Cash flow, debt, and capital are just some of the many financial factors that play a large role in startup success or failure.

- *Lack of cash*. Lacking cash to operate the business can trample its operations and lead to a quick decline. If there is no cash flow, it can also indicate that perhaps the business model is not working. For example, consider our fictional restaurant owner. A lack of customers means a lack of cash flowing in as revenue. Loans can provide some assistance while working to build the clientele, but loans can go only so far. If the business doesn't grow and develop a sustainable cash flow, its ability to operate will come to an end.
- *Too much debt*. Significant debt can hurt a business because it needs to pay back its lenders. In the previous example, if the restaurant owner takes on too much debt, it may struggle to pay it back due to its lack of cash flow.
- *Lack of capital*. Not having sufficient capital can deter the business from expanding or even from meeting

customer demand. Having a clear business plan can help determine the financial requirements, which are the estimated sales and profits required for the successful attainment of goals. Financing for the business can come from an entrepreneur's own savings, bank loans, investors, and even friends and family. Having the right funding to start or grow a business can make or break the business. For instance, our restaurant owner would need enough capital to invest in kitchen equipment, appliances, and furniture to start the business. Undercapitalization in a startup could shut the business down before it even gets up and running. Once the business is running, ensuring that financial goals are met through metrics such as sales and profits can help prevent shortages of cash flow, which is essential to keeping a business alive.

Innovation Failure

Innovation can be tricky because it requires creativity, risk, and often some subjectivity, taking into consideration feelings and intuition in decision making. Lack of innovation and missteps in innovation can be obstacles to success.

- *Lack of innovation or failing to change effectively*. Companies that don't change their strategies, technology, or products run the risk of jeopardizing the business. Similarly, those that do change but not with the right adjustments risk failure. The build-measure-learn loop can help avoid these pitfalls by discerning what consumers really want and need by asking for their feedback.

Blockbuster, an instant hit out of the gates in the 1980s, failed to innovate, or pivot its business model, and went out of business. The video store revolutionized the media and movie industry by displaying empty boxes of its titles on shelves categorized by genre (the VHS tapes were kept behind the counter) and keeping late hours for night owls and last-minute weekenders wanting to catch a flick. Using a computer system to track videos as they were rented, most of its profit was made by the fees charged for late movie returns. In 1987, the company was bought by Wayne Huizenga, an American entrepreneur who owned several businesses in different industries and who developed Blockbuster into a successful business by modeling McDonald's approach. The enterprise grew from twenty locations to over 9,000 locations. Blockbuster was then acquired in 1993 by media giant Viacom in an intricate transaction. As streaming and related technology entered the market, Blockbuster failed to innovate by not making necessary pivots to its delivery of entertainment and so could not compete with new technology. Over the ensuing decade, it became more common to see Blockbuster stores with "store closing" banners, as shown in Figure 10.7, than it did to see a thriving store. There were other reasons why Blockbuster failed. Embedded with the lack of technology was the lack of fostering a culture of creativity from all of its employees, which hindered innovation. It lacked visionary leadership. It needed a culture of collaboration and teamwork to facilitate communication with stakeholders, such as employees, customers, and upper administration. Finally, it closed all but one of its stores in 2013.[28] By then, Netflix had completely changed the landscape of digital streaming services and left Blockbuster without a ticket to the show.

Figure 10.7 Blockbuster failed to change its distribution channel to cater to new generations of movie watchers. (credit: modification

28 Jeanine Poggi. "Blockbuster's Rise and Fall: The Long, Rewinding Road." *TheStreet*. September 23, 2010. https://www.thestreet.com/story/10867574/1/the-rise-and-fall-of-blockbuster-the-long-rewinding-road.html

of "Blockbuster Store Closing, Ypsilanti Township, Michigan" by Dwight Burdette/Wikimedia Commons, CC BY 3.0)

ARE YOU READY?

Proactively Considering Failure

Consider the list of reasons for failure presented in Figure 10.6. Come up with solutions to each of those reasons, focusing on a business of your choice.

- How would you avoid the failure?
- What strategies or goals can you have in place to avoid the pitfalls of failure?

Fear of Failure

Even the fear of failure can be enough to lead a business to fail. Fear can freeze entrepreneurs and force them into a corner instead of advancing their businesses; it can freeze them from reaching potential clients and being profitable. When companies struggle, the owners may experience many emotions, such as pain, grief, shame, humiliation, self-blame, anger, and hopelessness. Business failure is hard to separate from personal failure, as the business is often associated with the identity of the entrepreneur. Managing these emotions can help business owners heal and continue moving forward to their next business. Reaching out for help to a trusted mentor or therapist can help provide guidance in dealing with these feelings.

There are likewise many stories of entrepreneurs who, despite their fears, continued working toward their goal and were successful. They kept going, determined that fear would not run their lives. Tony Robbins, author and serial entrepreneur, says that people are afraid of failure because it is painful, and people try to avoid pain and suffering at all costs. "Failure," he says, "is the ultimate loss."[29] But overcoming fear doesn't have to be painful if you understand it as a program or detrimental thinking running in your mind. People are hardwired to believe they are not good enough or can't do it. These patterns can be embedded in people's minds and can deter creativity and success. Some signs of fear of failure are listed in Table 10.3.

Signs of Fear of Failure

• Believing you are not good enough, you don't belong, or you're not smart enough to be successful. • Feeling that you have to be perfect in everything you do and have a need for approval. • Not wanting to adapt or be flexible. Not wanting to take on difficult clients or projects. • Feeling anxious about performing, leaving things for later, and not following through with plans.

Table 10.3 Fear can freeze up entrepreneurs. The important thing is to let go of old thinking patterns and adopt a positive outlook. It also helps to move forward despite fear and have mentors who can help deal with negative thoughts and emotions.

Fear of failure often stems from thoughts of inadequacy or a belief that you don't have the experience and skills necessary to succeed, that you're not smart enough, and so on. Thoughts like these can prevent a person from starting or advancing their business. Individuals with a high level of stress about failure tend to lack self-esteem, have anxiety, be perfectionists, and tend to avoid new or unfamiliar things at all costs.[30] Fortunately, these traits and behaviors can be controlled and conquered.

Most entrepreneurs will tell you that, at some point, they had to fight their fears before they had any success.

Most entrepreneurs who succeed will tell you that behind every success there were many failures. Many people in general think that those who are great and successful were born that way. But that is simply not

29 Team Tony. "Overcoming the Fear of Failure." *Tony Robbins.* n.d. https://www.tonyrobbins.com/stories/overcoming-fear-failure/
30 Mind Tools Content Team. "Overcoming Fear of Failure." *MindTools.* n.d. https://www.mindtools.com/pages/article/fear-of-failure.htm

true.

Take Michael Jordan, for example. One of the most successful basketball players of all time, with five championship rings and thousands of points and assists, Jordan often said that he owed his success to failure. "I've missed more than 9,000 shots in my career. I've lost almost 300 games. Twenty-six times I've been trusted to take the game-winning shot and missed. I've failed over and over and over again in my life. And that is why I succeed."[31] Michael Jordan, a kid who didn't make the varsity team in his high school, got his act together and propelled himself to stardom because he didn't give up when he failed. The same goes for entrepreneurs: Just because it didn't work the first time, it doesn't mean that they can't try again.

James Dyson, founder and inventor of the Dyson vacuum cleaner, had failed 5,126 times before he came up with his Dual Cyclone vacuum cleaner in 1993, fifteen years after he created the first version. When asked about how failure helped him, he said, "Failure is interesting—it's part of making progress. You never learn from success, but you do learn from failure. When I created the Dual Cyclone vacuum, I started out with a simple idea, and by the end, it got more audacious and interesting. I got to a place I never could have imagined because I learned what worked and didn't work."[32] Dyson also says that he continuously embraces risk and failure, and allows his employees to explore that: "Nothing beats the thrill of invention. Letting people go out and try their ideas, getting them totally involved, and unleashing new thinking. They're not bound to any methodology—in fact, the stranger and riskier, the better."[33]

Fear of Failure around the World

According to research, fear of failure is influenced by people's upbringing and cultural backgrounds. The **Global Entrepreneurship Monitor (GEM)**, an organization that researches entrepreneurship around the world, has studied this topic. According to its 2018–2019 report, Americans are not as afraid to fail in business as people from many other countries are.[34] This report includes those who would like to start a business but feel stuck because of fear of failure. Fear of failure is highest in Greece, Italy, Russia, and Cyprus, and lowest in Latin America and Africa. Usually, the fear is lowest in countries where there are few jobs and where people have to become entrepreneurial to survive.

WHAT CAN YOU DO?

GEM Data

Go to the Global Entrepreneurship Monitor at http://www.gemconsortium.org/ and look up the report on entrepreneurship for the United States. Compare it with two other countries.

- What are the differences and similarities between the countries?
- What can you do to address some of the factors in the US that hinder entrepreneurial development? What can be done to improve entrepreneurial conditions in the two other countries you examined?

31 The Greatest Team. "Quote: Michael Jordan on Success through Failure." *The Greatist*. June 10, 2012. https://greatist.com/fitness/quote-michael-jordan-success-through-failure
32 Nadia Goodman. "James Dyson on Using Failure to Drive Success." *Entrepreneur*. November 5, 2012. https://www.entrepreneur.com/article/224855
33 Madison Malone-Kircher. "Dyson on the 5,126 Vacuums That Didn't Work—and the One That Finally Did." *New York Magazine*. November 22, 2016. http://nymag.com/vindicated/2016/11/james-dyson-on-5-126-vacuums-that-didnt-work-and-1-that-did.html
34 Global Entrepreneurship Monitor. "Fear of Failure." 2018–2019. *GEM*. https://www.gemconsortium.org/report

GEM also reports that women are usually more afraid of failure than men and show less confidence in their abilities (Figure 10.8). The research also shows that women tend to open ventures in consumer industries, whereas male-driven startups are often in manufacturing and tech sectors, and men receive more capital and incentives to open those businesses. This can be attributed to the lack of women in science and tech industries.[35] Other studies corroborate GEM's findings, showing that women are more afraid to start a business, they don't receive as much funding, and feel they have to prove themselves more than men to be taken seriously.[36]

Figure 10.8 Research shows that women tend to be more afraid of failure and have less confidence in their abilities than men. Getting support from business organizations, programs, and mentors can help women build their self-assurance to begin or grow an enterprise. (credit: "Accomplished Achievement Agreement" by "rawpixel"/Pixabay, CC0)

What Failure Teaches You

Some would argue that, in reality, failure does not exist. There is only perceived failure, or obstacles that can become steps up the ladder to a better outcome. The importance in failing lies in learning how to get back up again. As Eric Ries dove into failure with his first company and felt the deep pain and disappointment of having to let go of an unsuccessful idea, he applied his lessons to create his new virtual reality company IMVU. IMVU then became a very successful experiment from which he derived the lean startup method. He was able to pinpoint his shortcomings and find ways to better himself and his performance. With his new company, he was able to get the product to market faster without it being perfect and ask for much-needed feedback from customers that he hadn't received before.

Converting Lessons Learned to Success

Most successful business owners will tell you that success didn't come to them easily. They had to persevere in pursuit of their goals to attain them. Converting their failures to lessons often led them to higher success than they had imagined. Entrepreneurs who can turn their obstacles into positive lessons can resurrect from failure.

35 Catherine Clifford. "Lack of Confidence, Fear of Failure Hold Women Back from Being Entrepreneurs." *Entrepreneur*. July 31, 2013. https://www.entrepreneur.com/article/227631
36 Ruth Simon. "Women Started Smaller Percentage of Businesses in 2014." *The Wall Street Journal*. March 13, 2015. https://www.wsj.com/articles/women-started-smaller-percentage-of-u-s-businesses-in-2014-1431560888

Take Evan Williams, a visionary who launched a software tool to help users easily publish blogs. That venture, Blogger.com, was launched in 1999 and purchased by Google in 2003. The next year, Williams decided to establish Odeo, a platform for creating and sharing podcasts. Apple had been working on a similar platform and shared it earlier on iTunes to the demise of Odeo. Williams didn't want to go head to head with iTunes, as this could potentially destroy his company, so he found a way to go in a different direction and establish a new way of sharing status updates and other data. Williams took that failure, and with a few friends, co-founded Twitter. We all know how that worked out: Twitter is one of the most popular microblogging tech platforms.[37]

LINK TO LEARNING

Check out Evan Williams's TedTalk (https://openstax.org/l/52TedTalkWill) where he takes you through iterations from actual Twitter users.

Kathryn Minshew, shown in Figure 10.9, also experienced failure but has learned from it. In 2010, she quit her job to create Pretty Young Professionals (PYP). She invested $25,000 of her own money to develop a networking platform for women who were smart and passionate about their careers. After a few months, she and the three other co-founders started to disagree on some issues, including their approach to advertising. As they hadn't completely formalized the ownership of PYP, two of the founders lost their investments, including Minshew. After experiencing the loss of her investment, her friendships, and the original idea, Minshew persevered with a new opportunity and established The Muse. This platform is similar to PYP but added job listings, workshops, and advice. Currently, the site has over 4 million users and is a major competitor of LinkedIn. Minshew didn't let her first disappointment prevent her from starting a new venture. She applied the lessons learned in building the original platform to the creation of a new one—with the right contracts and right people in place.[38] Minshew now speaks at business conferences and events, sharing her mistakes and how she used them to lift herself up to launch a new venture properly. She hopes that her experience helps other entrepreneurs avoid the pitfalls she went through so they can be as successful.

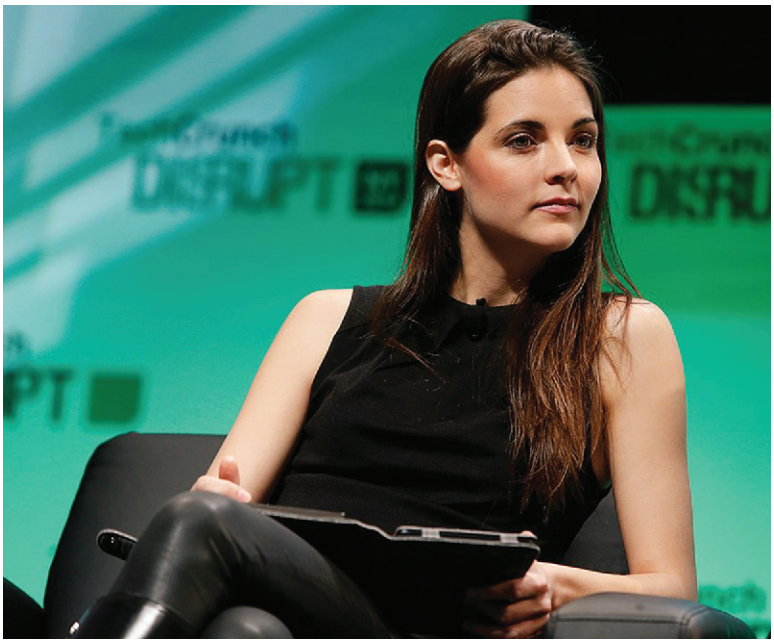


Figure 10.9 Kathryn Minshew, co-founder of The Muse, used the lessons from her first business's failure and built a successful platform for professional networking. (credit: modification of "Kathryn Minshew" by "Techcrunch"/Wikimedia Commons, CC BY 2.0)

37 Paige Cooper. "28 Twitter Statistics All Marketers Need to Know in 2019." *Hootsuite*. January 16, 2019. https://blog.hootsuite.com/twitter-statistics/

38 Doria Lavagnino. "Muse CEO and Co-Founder Kathryn Minshew: Journey of an Entrepreneur." *Centasi*. August 24, 2017. https://centsai.com/entrepreneurship-blogs/muse-ceo-co-founder-kathryn-minshew-journey-entrepreneur/

Being able to learn from different types of failure is as important as experiencing success because you get to know your strengths and how to leverage them. Failures can be seen as stepping stones rather than embarrassments. Feeling comfortable takes practice. Table 10.4 shares several tips on dealing with these dynamics.

Tips for Converting Lessons to Successes

- Let go of the fear of failure: It is not as bad as you think.
- Experiment with your business and try new things; take risks if necessary.
- Go for it, even if you're not ready. Listen to your gut.
- Ask for feedback, and don't be afraid to hear negative things.
- Be willing to change when things are not working out.
- Learn from others and be willing to ask for help.

Table 10.4

Coping with Fear

When coping with fear of failure, there are two strategies that entrepreneurs can use. The first way to reduce fear of failure is to modify your business strategy by changing the target outcomes for your business. Instead of aiming to make $50,000 in the first six months, you can be open to the idea of a leaner start, learning about your customers and how best to serve them. Learning/growth goals can be just as valuable as hitting a revenue target in terms of overall success and longevity. Also, if a goal is not met, don't consider it a total failure: Refocus and ask yourself what you learned from the experience and how to apply that knowledge to a revised goal. More than likely you will find this experience has enhanced your toolbox to help you make changes within the business or start a new one.

A second way to reduce high stress is to practice some sort of meditation or breathing exercise that can help lower the anxiety created by fearful thinking. Reaching out to a mentor, support group, therapist, or counselor can also help alleviate fearful thinking.

10.3 The Challenging Truth about Business Ownership

Learning Objectives

By the end of this section, you will be able to:

- Explain the pros and cons of business ownership before you launch
- Understand current trends in entrepreneurship in the US
- Determine the challenges women face in entrepreneurship and what resources they can use to overcome them
- Determine the challenges minority entrepreneurs face and resources available for them

People usually have different reasons for starting a business. Some of the reasons—other than the idea they've hit upon—include the freedom to set their own hours, spend more time with family, be their own boss, and make money. However, in many cases, they will probably work more than planned, be challenged to find the work-life balance, face fears and doubts, and perhaps struggle to make ends meet for the first few months or years. Prior to launch, they will need the support of family, friends, and mentors to understand the limitations of time and the pressures they face.

Pros and Cons of Business Ownership

Table 10.5 lists the positives and negatives that should be considered prior to opening a business and throughout its operation. Positives of entrepreneurship include having the freedom and independence to

expand your skills and develop your own ideas. Instead of working for another organization on projects and ideas that are not your own, you get to serve people in a way that feels right for you. You also have the opportunity to make a profit and have a better lifestyle. Having the freedom to set your own schedule and work at your own pace can be very satisfying as well.

On the opposite side, those "freedoms" translate into being in charge of the business and the significant responsibility that entails. You must resolve issues that arise every day, such as dealing with employees, customers, production, marketing, and financing, among others. Most of the time, you wear many hats, especially during the venture's early lifecycle stages, and most entrepreneurs usually work more hours than anticipated. In addition, you must deal with losses and risk if things don't go well. The important thing to keep in mind is that all of the negative aspects have solutions and can even be prevented if planning, mentorship, and a good support system are in place, which can alleviate many of the stresses that entrepreneurs experience. Also, having attainable goals in creating awareness of the business, number of clients, and sales or profit can be beneficial in alleviating some of that pressure.

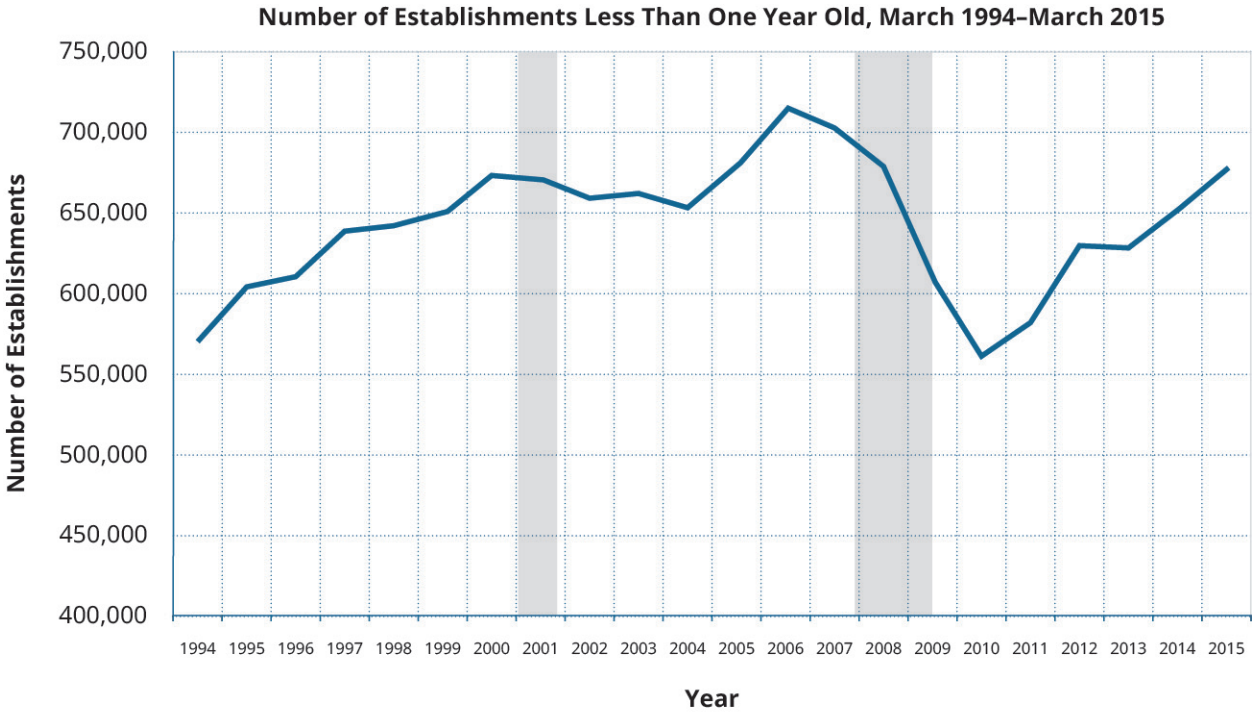
Pros and Cons of Business Ownership

Pros	Cons
• Being autonomous, being your own boss, expanding ideas, enjoying creative freedom • Lifestyle, making your own schedule, flexibility • Satisfied with career • Serving customers and employees • Profit • Being known in the community	• Being in charge, resolving issues, hiring/firing employees, and wearing many hats • Dealing with stress, time constraints, and management • Lack of focus, loss of passion • Customer and employee complaints • Money/cash flow problems • Must deal with losses and financial risk

Table 10.5

Entrepreneurship and Competition in the US

Entrepreneurs operate in an unbelievably competitive landscape. Although competition helps create better products and services, it also places many stresses on a business owner who must compete with new, more flexible businesses that may have lower prices and better products. As shown in Figure 10.10, the number of new establishments that are less than one year old has increased over the past two decades from 1994 to 2015. There was a dip during the 2009 recession, but the trend continued after 2011, and the number of businesses increased again. This means more competition for businesses that are already established.

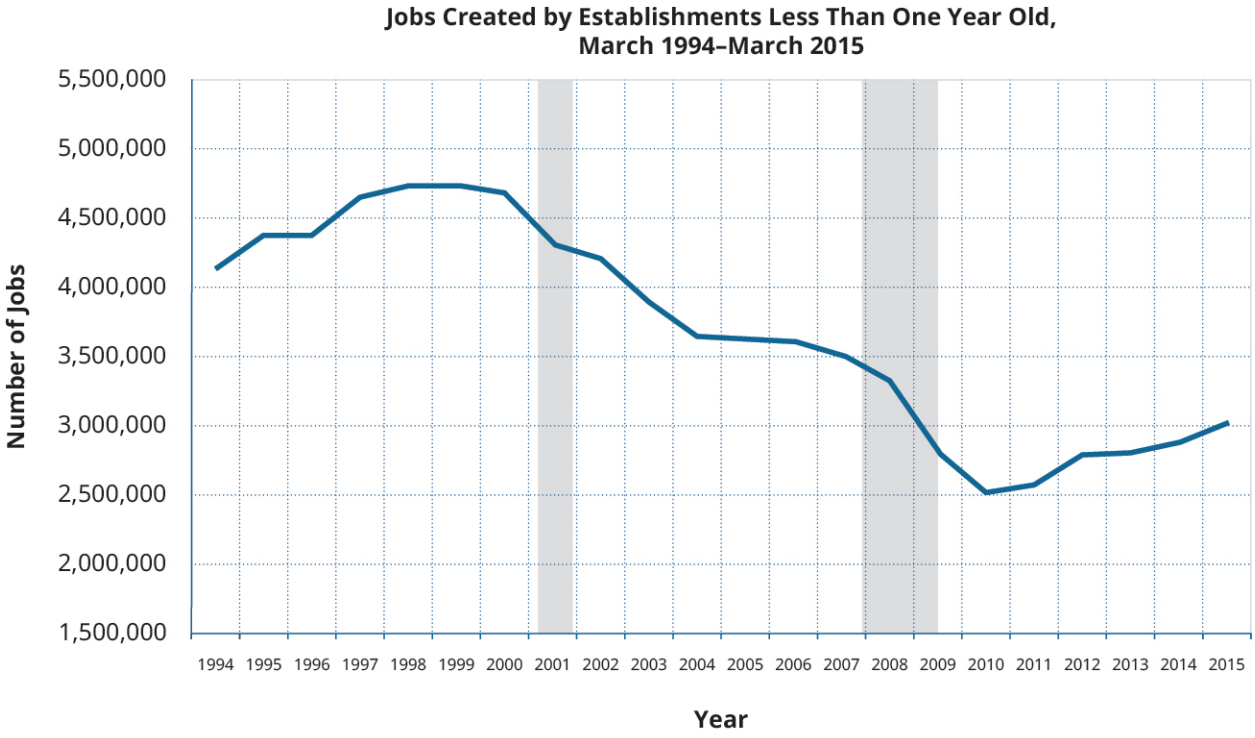


Source: "Chart 1. Number of Establishments Less Than 1 Year Old, March 1994–March 2015." Entrepreneurship and the U.S. Economy. Business Employment Dynamics. United States Department of Labor. April 28, 2016.

Figure 10.10 The number of new businesses usually rises and falls with the economy. This graph shows that the number of new establishments has risen in recent years.[39] (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The number of jobs created by these young establishments has also decreased in this period, which affirms the likelihood that entrepreneurs are wearing many hats in their own businesses. Figure 10.11 charts this trend.

39 Bureau of Labor Statistics. "Entrepreneurship and the US Economy." *United States Department of Labor*. April 28, 2016. https://www.bls.gov/bdm/entrepreneurship/entrepreneurship.htm



Source: "Chart 2. Jobs Created by Establishments Less Than 1 Year Old, March 1994–March 2015." Entrepreneurship and the U.S. Economy. Business Employment Dynamics. United States Department of Labor. April 28, 2016.

Figure 10.11 While the number of new business establishments has risen, the number of jobs and the survival of businesses (following) have decreased during the same period.[40] (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

As you've learned, only about 20–30 percent of businesses succeed to the five- or ten-year mark. Figure 10.12 shows that only half of businesses survive to the five-year mark, and only 20 percent are sustained for two decades. Their failures may be due to a number of factors such as cash flow problems, lack of passion, lack of support, lack of innovation, difficulty adapting to new technologies or customer demand, and environmental factors that can influence a business as well, such as the economy, trends, regulations, or sociocultural changes. Therefore, it's important for entrepreneurs to research their internal as well as their external environments before launching. The chapters on Identifying Entrepreneurial Opportunity and Entrepreneurial Marketing and Sales take a look at such research, as it pertains to both the entrepreneur and the marketing environment respectively.

40 Bureau of Labor Statistics. "Entrepreneurship and the US Economy." *United States Department of Labor*. April 28, 2016. https://www.bls.gov/bdm/entrepreneurship/entrepreneurship.htm

Source: "Chart 3. Survival Rates of Establishments, by Year Started and Number of Years Since Starting, 1994–2015, in Percent." Entrepreneurship and the U.S. Economy. Business Employment Dynamics. United States Department of Labor. April 28, 2016.

Figure 10.12 Survival rates of businesses from 1994–2015. This graph shows that as years go by, fewer businesses stay open.[41] (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Challenges of Business Ownership for Women

Challenges for business owners can be many. Female entrepreneurs, however, can face additional hardships. These can range from not being able to secure financing for their businesses, having a hard time breaking into an industry, and dealing with fears of starting and growing a business, and not being taken seriously.

Current research shows that the importance of female entrepreneurship is key to economic success. Women own 40 percent of the country's businesses,[42] generating over $1.4 trillion in sales.[43] Women entrepreneurs are closing the gender gap, as their ventures have grown substantially in the past few years. In the past two years, women entrepreneurship rates have gone up by 10 percent each year, compared to men's 5 percent growth. This surge has been spurred by increased available resources, including mentorship, funding, and programs to help women succeed.[44] Nonetheless, there are still great challenges to overcome, as women move into the next generation of business ownership. Some of the main challenges are:

- *Difficulty gaining entry in certain industries.* Women have made great strides in business, but they still face many obstacles, especially in certain industries. Women tend to be underrepresented in specific areas, notably in the tech industry, where they run only 9 percent of businesses.[45] Women tend to be underpaid in tech positions, they experience sexism, and they are often passed over for promotions, especially if they have families with young children. So, if there are no female role models, it is difficult for women to follow an entrepreneurial path that is already full of obstacles. Although young girls and women desire to study and expand their careers, historically, they have not been presented with the opportunities and encouragement to do so, especially in STEM. By the time they get into college, the number of women in these careers—which can be rich in entrepreneurial opportunities—is very small. However, more efforts

41 Bureau of Labor Statistics. "Entrepreneurship and the US Economy." *United States Department of Labor*. April 28, 2016. https://www.bls.gov/bdm/entrepreneurship/entrepreneurship.htm
42 Bernard Meyer. "Business Woman Challenges, Examples and Opportunities in 2107 and Beyond." *InvoiceBerry*. June 19, 2017. https://blog.invoiceberry.com/2017/06/business-woman-challenges-examples-opportunities/
43 National Association of Women Business Owners (NAWBO). "Women Business Owner Statistics." *NAWBO*. 2017. https://www.nawbo.org/resources/women-business-owner-statistics
44 Elaine Pofeldt. "Why Women Entrepreneurs Will Be the Economic Force to Reckon with in 2017." *CNBC*. February 28, 2017. https://www.cnbc.com/2017/02/28/why-women-entrepreneurs-will-be-economic-force-to-reckon-with-in-2017.html

are being made today to support young girls interested in scientific, technological, and mathematical careers.

- *Lower sales and fewer employees*. Women overall tend to struggle more to keep their businesses afloat, as they have fewer employees,[46] less revenue, and less profit than male-owned businesses. Only 2 percent of female-owned businesses make over $1 million in sales. Male-owned businesses, on the other hand, are 3.5 times more likely to hit that revenue target.[47] Some of the reasons why women experience this is because women may enter entrepreneurship part time, often striving to sustain a decent family work balance, which is difficult when children, especially young children, are part of the equation. This set-up usually includes one employee, who is the entrepreneur herself, and she may have attained her goals without wanting to make millions. Time, flexibility, and work-life balance can be reasons women become entrepreneurs, and they are happy with their goals of making some money while taking care of their family and household. Lack of experience in business or managing a family business, and lack of access to capital are also reasons for the lower metrics.[48]
- *Less access to capital*. Regardless of their success and prowess, women still have a harder time securing funding for their businesses. A recent Kauffman Foundation survey determined that more than 72 percent of women don't have the access to capital they need.[49] Nirupama Mallavarupu, founder of MobileArq says, "As a woman entrepreneur with a focus on helping non-profits and schools, it has been difficult to get investors. We have turned this around by pursuing customer acquisition organically and relying on direct revenues instead of investment growth."[50] Women usually don't ask for funding, or if they do but are turned down, they turn to funding from family and friends. They are more likely to finance their ventures this way than men.[51]
- *Not taken seriously*. Sometimes it's not that women don't have the opportunities, money, or mentorships to start a business: Sometimes, women are just not taken seriously. Research by Freshbooks Accounting and Software firm and Research Now asked 2,700 entrepreneurs about gender discrimination and the wage gap that exist today. Thirty percent of women pointed out that they are not taken seriously as business owners, as they must work harder than their male counterparts and have to charge less to get a client.[52] Emily Harsh, owner of Heart Move Collective, comments in her blog, "Because I am in the fitness industry and female, I am often not taken seriously as a professional. I think the number one most important thing you can do as a woman fighting to pave your own path is to continually stay authentic."[53]
- *Resources*. Fortunately, there are many resources that women can take advantage of. Organizations such as the Women's Business Center of the Small Business Administration, the National Association for Women Owners, the Female Entrepreneur Association, Ladies Who Launch, Minority Business Development Agency, the National Association of Professional Women, and the Women's Business Enterprise National Council strive to help women succeed in all industries by providing loans and programs that prepare them for a competitive landscape. Mentoring by other women has also proven to

45 Sahil Raina. "Research: The Gender Gap in Startup Success Disappears When Women Fund Women." *Harvard Business Review*. July 19, 2016. https://hbr.org/2016/07/research-the-gender-gap-in-startup-success-disappears-when-women-fund-women
46 Michael J. McManus. "Women's Business Ownership: Data from the 2012 Survey of Business Owners." *US Small Business Administration Office of Advocacy*. May 31, 2017. https://www.sba.gov/sites/default/files/advocacy/Womens-Business-Ownership-in-the-US.pdf
47 Eilene Zimmerman. "Only 2% of Women-Owned Businesses Break the $1 Million Mark—Here's How to Be One of Them." *Forbes*. April 1, 2015. https://www.forbes.com/sites/eilenezimmerman/2015/04/01/only-2-of-women-owned-businesses-break-the-1-million-mark-heres-how-to-be-one-of-them/#2a53233727a6
48 Robert W. Fairlie and Alicia M. Robb. "Gender Differences in Business Performance: Evidence from the Characteristics of Business Owners Survey." *SpringerLink*. May 5, 2009. https://link.springer.com/article/10.1007/s11187-009-9207-5
49 Elaine Pofeldt. "Why Women Entrepreneurs Will Be the Economic Force to Reckon with in 2017." *CNBC*. February 28, 2017. https://www.cnbc.com/2017/02/28/why-women-entrepreneurs-will-be-economic-force-to-reckon-with-in-2017.html
50 Bernard Meyer. "Business Woman Challenges, Examples and Opportunities in 2107 and Beyond." *InvoiceBerry*. June 19, 2017. https://blog.invoiceberry.com/2017/06/business-woman-challenges-examples-opportunities/
51 Elaine Pofeldt. "Why Women Entrepreneurs Will Be the Economic Force to Reckon with in 2017." *CNBC*. February 28, 2017. https://www.cnbc.com/2017/02/28/why-women-entrepreneurs-will-be-economic-force-to-reckon-with-in-2017.html
52 "New Research from FreshBooks Discovers a 28% Wage Gap among Self-Employed Men and Women." *FreshBooks*. n.d. https://www.freshbooks.com/press/data-research/women-in-the-workforce-2018?ref=10400&utm_source=sas&utm_medium=affiliate&utm_campaign=314743&sscid=31k3_f8pv3
53 Bernard Meyer. "Business Woman Challenges, Examples and Opportunities in 2107 and Beyond." *InvoiceBerry*. June 19, 2017. https://blog.invoiceberry.com/2017/06/business-woman-challenges-examples-opportunities/

be effective in women's success in entrepreneurship.[54] Having peers that can help and strong mentors can make a difference in the outcome of a business.

Other helpful tips to counteract the challenges facing women entrepreneurs include being assertive, being authentic, networking, and developing a thick skin for rejections and other challenges. Facebook COO Sheryl Sandberg, in her book *Lean In*, states that "being confident and believing in your own self-worth is necessary to achieving your potential" and she encourages women entrepreneurs to ask themselves: "What would you do if you weren't afraid?"[55]

Women bring great qualities to entrepreneurship such as strong leadership, as well as management, time, multitasking, and listening skills. Women also have a collaborative approach to relationships that works well in many industries.[56]

Challenges of Business Ownership for Minorities

Entrepreneurs from minority groups encounter additional challenges. Minority groups are a strong force in the economy of the country, yet they still experience additional challenges that sometimes prevent them from succeeding in their businesses. These can range from having lower capital access[57] due to little credit history, small or nonexistent business networks, and lower business knowledge.[58] According to the Census Bureau, minorities own about 29 percent of US businesses.[59]

Hispanic people[60] comprise 17 percent of the population and own approximately four million (13%) companies in the US with $661 billion in revenue. From 2007 to 2015, business revenue grew 88 percent for Hispanic people, which means that they have more power to employ more people to provide goods and services to a wider audience, and to purchase from other vendors. Given its growth and current size, this group is vital to the health of the economy.[61] Unfortunately, research shows that if measured by financial outcomes, Hispanic people still struggle to succeed in business ventures due to a lack of funding, less managerial/business education, and lack of mentorship.[62] A higher rate of foreign-born entrepreneurs can experience these challenges due to the lack of networks and financial history in the country.[63]

Black people make up 14 percent of the total US population, and their businesses represent about 7 percent of total businesses. Although they are opening businesses faster than their White counterparts, their businesses, as well as Hispanic businesses, tend to have higher failure rates than White- and Asian-owned businesses.[64] Similar to Hispanic people, Black people tend to lack funding, managerial/business education, and mentorship.

54 Robin L. Laukhuf and Timothy A. Malone. "Women Entrepreneurs Need Mentors." *International Journal of Evidence Based Coaching and Mentoring* 13(1): 70–86. 2015. http://ijebcm.brookes.ac.uk/documents/vol13issue1-paper-05.pdf
55 Sheryl Sanders. *Lean In: Women, Work, and the Will to Lead*. (New York: Knopf. March 12, 2013).
56 S. Mohan Kumara, H.S. Chandrika Mohana, Vijaya C., and Lokeshwari N. *International Journal of Current Engineering and Technology* (Special Issue 1): 100–104. 2013. http://inpressco.com/wp-content/uploads/2013/09/Paper20100-104.pdf
57 Minority Business Development Agency. "Access to Capital Is Still a Challenge for Minority Business Entrepreneurs." *US Department of Commerce: Minority Business Entrepreneur*. March/April 2010. https://www.mbda.gov/news/blog/2010/07/access-capital-still-challenge-minority-business-enterprises
58 David Kiger. "Minority Entrepreneurs Face Challenges in Business Development." *Business 2 Community*. April 2, 2016. https://www.business2community.com/small-business/minority-entrepreneurs-face-challenges-business-development-01497508
59 Aleks Merkovich. "30 Insightful Small Business Statistics." *FitSmallBusiness*. March 18, 2019. https://fitsmallbusiness.com/small-business-statistics/
60 "Of Hispanic or Latino Origin" as used in the 2010 Census refers to a person of Cuban, Mexican, Puerto Rican, South or Central American, or other Spanish culture or origin regardless of race. https://www.census.gov/prod/cen2010/briefs/c2010br-02.pdf
61 Geoscape. "Hispanic Businesses and Entrepreneurs Drive Growth in the New Economy: Third Annual Report." *Geoscape*. 2015. https://ushcc.com/wp-content/uploads/2015/11/HispanicBusinessReport2015_Final_Sept19.pdf
62 Denisse Olivas. *Entrepreneurship Success: A Hispanic Point of View*. Center for Hispanic Entrepreneurship. University of Texas at El Paso. Proceedings from the International Conference of Facets Doing Business in Emerging Markets. July 2016. https://www.utep.edu/business/_Files/docs/cfhe/newentrepreneurship-success-presentation-cfhe.pdf
63 Geoscape. "Hispanic Businesses and Entrepreneurs Drive Growth in the New Economy: Third Annual Report." *Geoscape*. 2015. https://ushcc.com/wp-content/uploads/2015/11/HispanicBusinessReport2015_Final_Sept19.pdf
64 "Race." *Kaufmann Foundation*. n.d. https://www.kauffman.org/microsites/state-of-the-field/topics/background-of-entrepreneurs/demographics/race

Asian Americans make up 5 percent of the population and own just over 4 percent of the businesses in the country. Although they are considered minorities, Asian Americans tend to be better educated and have more access to capital than Hispanic Americans and African Americans.[65]

Organizations such as the Hispanic, Black, and Asian American Chambers, the Minority Business and Development Agency (MBDA), and the Small Business Administration (SBA) have developed programs to help minority entrepreneurs succeed in various ways. These organizations hold workshops once or twice a month to provide helpful information and business plan templates so owners work through their preparation to launch a venture. Chambers are also helpful in matching companies with banks for loans based on their needs and industries. The 8a certification is also facilitated by the Chambers and the MBDA, and provides disadvantaged businesses with an assistance program.

LINK TO LEARNING

Go to the MBDA's page on the 8(a) Business Development Program (https://openstax.org/l/52MBDA) and read about the requirements and benefits of 8a certification. You can also see that the MBDA offers access to grant and loan programs, and many other helpful resources.

Disadvantaged businesses are those that are small, owned by someone economically disadvantaged (a person who has less than $250,000 in personal net worth, which includes assets such as cash, home, car, and real estate minus liabilities such as mortgages, credit card debt, and car and bank loans), with an owner demonstrating that the business can be successful. This program helps minority business owners access finances, mentors, counselors, and management assistance, among other resources.[66] In addition to this support, some organizations, such as the SBA, provide certifications on various business topics on marketing, finance, accounting, management, and production that usually take the form of short classes for business owners to acquire business acumen. These programs help entrepreneurs gain needed knowledge, grow professionally, and connect with people as they go through their entrepreneurial journeys.

LINK TO LEARNING

Read this article from Investopedia on challenges facing small businesses (https://openstax.org/l/52SmallBusChal) to learn more.

10.4 Managing, Following, and Adjusting the Initial Plan

Learning Objectives

By the end of this section, you will be able to:

- Explain the difference between a business plan and a lean plan
- Know how to develop a lean plan quickly and accurately
- Run the build-measure-learn loop

In this chapter, we've discussed how to start the imperfect business using the lean startup approach. We've looked at the build-measure-learn loop and how to test an MVP. We've also covered how to deal with fear of failure and how to overcome negative thinking. In addition, we've covered how minorities can tap into resources to help them be successful. Now it's time to build the lean plan to help you launch your venture.

65 "Race." *Kaufmann Foundation*. n.d. https://www.kauffman.org/microsites/state-of-the-field/topics/background-of-entrepreneurs/demographics/race

66 Minority Business Development Agency. "What Is the 8(a) Business Development Program." *US Department of Commerce*. n.d. https://www.mbda.gov/news/blog/2012/03/what-8a-business-development-program

As you must realize, having a lean plan is important to executing its process. A **lean plan** follows the path of lean methodology. It is a brief business plan shown to potential investors and employees that is a fast and effective way to set, manage, and evaluate goals and strategies in a business. Figure 10.13 shows its components.

Traditionally, a business plan requires a detailed document of the company's background, the target, objectives, financials, and marketing strategies. Developing this usually takes a long time, from a few months to a year, as you will see in Business Model and Plan. A full business plan requires robust information as it's developed for internal purposes, for banks or investors who need proof that the business is a good investment, and for other stakeholders. In contrast, a lean plan is short and includes only specific information, sufficient to go through the build-measure-learn loop. This plan is where you clarify initial ideas about the product to help you work through the loop and to share with potential investors and employees who need only so much information to decide on their role in the project.

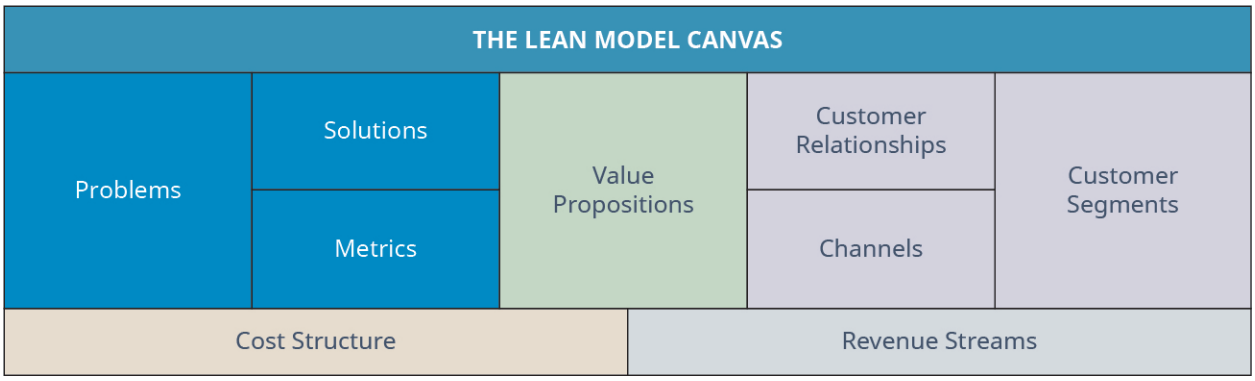


Figure 10.13 The founders of a business create a lean plan to help them set expectations and goals. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Developing a Lean Plan

As mentioned earlier, a lean plan uses lean methodology. This type of planning begins by drafting a short living set of lists to guide you, meaning you can update it as you go.[67] The plan shouldn't take months to develop; you can set it up in a few days. The plan focuses on the business core, so only important details about marketing, the business model, finances, the build-measure-learn loop, and the MVP are added to it.[68]

The following is a list of basic procedures and details to include in a lean plan.

1. Write a short and simple document.
2. Test your MVP through the build-measure-learn loop.
3. Review your results.
4. Revise your plan.

Once these steps are complete, the entrepreneur can start or continue the venture.

Write a Short and Simple Document

This plan does not need to include an executive summary, a company background, or team information. It is literally a short pitch that you can use to share with investors and potential partners. Focus on what is important and include the following:

- Basic strategies for product, price, place, promotion; add people, physical environment, and process if it is a service
- Basic strategies for target market and positioning

67 Tim Berry. "Business Planning for the 'Lean Startup.' " *Entrepreneur*. September 22, 2010. https://www.entrepreneur.com/article/217343
68 Noah Parsons. "An Introduction to Lean Planning." *LivePlan*. July 13, 2017. https://www.liveplan.com/blog/2017/07/an-introduction-to-lean-planning/

- Day-to-day tactics, which include specific tasks or actions that will get an objective done
- A schedule with dates for acquiring needed licenses, launch date, and when to review and revise the plan
- A business model that details how you will make money
- A basic forecast of sales, costs, profit, and break-even analysis

This plan is just a bare bones list of things that need to get done and by whom. It also includes a timeline, a cost, and a reward. It is less like a traditional document and more a series of lists and bullet points. In this case, the entrepreneur is only writing down the essentials of the business to achieve the goal at hand. Later on, when a document is needed for outside stakeholders or bank loans, then a full plan can be developed with research and details about the market, the environment, trends, and strategies that are more fleshed out.

For example, an entrepreneur who is just opening a prosthetics company can start a lean plan by describing its main product, which can focus on creating custom prosthetics for children. Then it can add a basic price or range of prices for its basic product since it's a custom product, and it will probably vary in price from customer to customer. Another strategy to keep in the plan is where to conduct the business. A central location would probably be a good idea, especially close to doctors and hospitals. Finally, basic promotional strategies used in reaching out to this market, which can include speaking to children's hospitals and local doctors who can refer the patients to the company, can also be listed. In addition, the entrepreneur may decide to create a basic website, online ads, and simple brochures to give information to potential customers. Once all the strategies are laid out, then the timelines can be added from the inception until the launch date, which includes assignments for everyone who will be in charge of the activities in this new business. These can include an office manager, the prosthetist, and a marketer.

Next, the entrepreneur may detail how the money will be made. Will the new business charge the client directly for the product? How about accepting insurance and copayments? These are questions that need to be written down. Then a basic forecast of the market demand will help forecast sales, expenses, and profit.

Test Your MVP through the Build-Measure-Learn Loop

Once the lean plan has been put into place, the next step is to execute it and test the MVP through the build-measure-learn loop. Here is where the rubber will meet the road, and all the assumptions that were made in the plan will be tested in real life.

- Build your MVP.
- Test your idea by sharing it with potential customers.
- Measure results by talking to customers and recording feedback.
- Ask questions such as: Are we building a product people want? What benefits do we need to add? Is this our target market?
- Test different versions and cohorts of users.

In our example, the entrepreneur will have a chance to build the prosthetics and ask questions that will help create a better product over time. At this time, the entrepreneur might find out that the product can be expanded to include orthotics and not just prosthetics, and perhaps that adults can also be included in the market.

Review Your Results

This step should be done at least once a month, where customer feedback, marketing, and outcomes are thoroughly reviewed. This is a great opportunity for the entrepreneur to assess if goals have been met and identify areas for improvement. However, many times, you will encounter that reviewing results can stir resistance from employees (if there are any), as they may become tired of planning, having meetings about planning, and demonstrating results. The reviewing process can inspire some fear or negative feelings over concerns of being blamed, but as a leader, you must always assure them that this process helps them get better at what they do and gives them the information and tools necessary to make the changes that will steer

the business onto a more successful path. This is about managing the results and not being deterred by them.

- Review customer feedback and go back to your plan to compare.
- Review target market, 7Ps of marketing, features, and benefits.
- Review numbers or outcomes, which may include sales, profit, customer signups, and even customer reactions to advertisements and product attributes.

In our example, if the prosthetics business is not bringing in enough customers to sustain it, then this is the opportunity to see where issues exist so changes can be made to the lean plan.

ARE YOU READY?

A Lean Scooter Plan

You are interested in opening a new electric scooter business in your small city, as there is no competition. You would like to enable your small town to have smart mobility that is environmentally conscious while reducing dependence on regular transportation such as buses and vehicles.

- Create a lean plan that details how you plan to start your business.

Revise the Plan

Make changes to the plan as needed. Once metrics have been measured against results, marketing is tested and measured, and customer feedback is received, then it is time to revise the plan and make adjustments. This can take the form of adding a feature to the product, adding new products, changing promotional tactics, or communicating differently with customers and consultants.

If there aren't enough customers to sustain the prosthetic business, here is where the founders can make changes to correct course. It may be that customers are not aware of the business, or there aren't enough pediatric customers and perhaps adults can be added to the target market. Once the plan is revised and the resulting changes are made, the business can continue and the process of testing restarts. As you can see in Figure 10.14, this is a continuous process. It requires constant updating and cooperation from everyone involved in the business. Once the process is set up, then it is easier to maintain it and see it as necessary within the business that helps it grow.

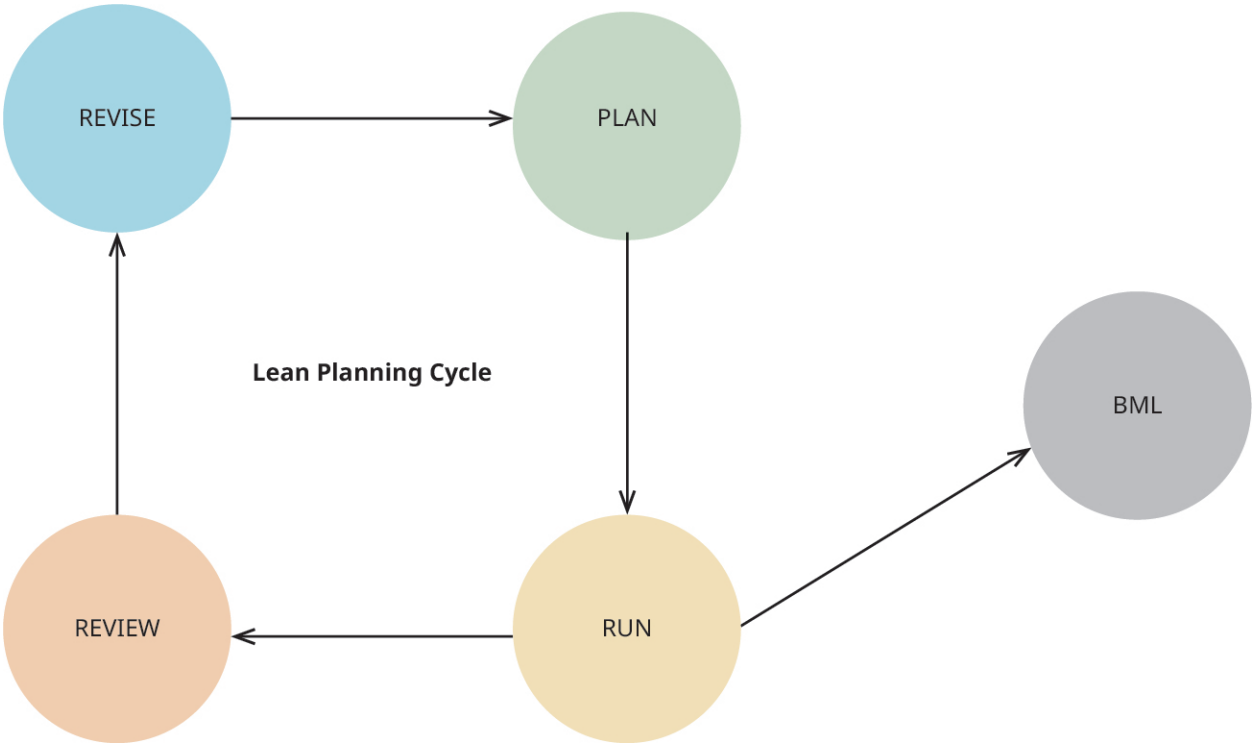


Figure 10.14 The lean plan cycle for small businesses. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Tim Berry—entrepreneur, former Apple employee, writer, and now a lean startup guru—advises businesses on the art of lean planning, as he does not like long planning himself and has little patience for extensive plans and coding. For Berry, lean planning does not contain elaborate information and details that are unnecessary for the business to run. It is not a document per se, but an assortment of short bullet points, some lists, and tables. For Berry, the most important steps to lean planning are to have the following:

1. A lean strategy or plan in place
2. Execution of the plan (or run it like in the Figure 10.14)
3. Review of the results and check against milestones
4. Revision of the plan—change what didn't work and start the whole process again[69]

ARE YOU READY?

Developing a Lean Plan

A local entrepreneur owns a print shop that has been in business for 20 years. The owner focuses mainly on printing business cards, flyers, posters, brochures, and banners for local businesses. They have noticed that sales have been declining for the past five years because promotions have been evolving into digital ads, social media, and other Internet marketing techniques rather than printed material. They will need to innovate if they want to stay in business.

Last week, the owner came to see one of your entrepreneurship professors to ask for a student or someone to help. Since you aced the class, your professor thinks that you can show the owner how to develop a lean plan, and they offer you an internship. You accept gladly and begin to work on the project.

- Develop a lean plan and explain to the owner how this can help them grow in the next three years.

69 Tim Berry. "Lean Business Planning Guide." *Lean Business Planning.* https://leanplan.com/

10.5 Growth: Signs, Pains, and Cautions

Learning Objectives

By the end of this section, you will be able to:

- Determine the lifecycle of a business
- Identify strategies to manage the main needs of each lifecycle stage
- Explain how businesses grow and adapt to changes in their cycles

The work of the entrepreneur is not over after the launch of a business. There are constant changes to manage. Sustained business growth requires a company to improve profits by increasing its revenue, cutting costs, or both. Increasing profit yearly indicates improvement and helps secure financing from banks, attract and reward investors, support opportunities for opening new business locations, and helps reinvest those profits in research and development. As a business matures and stabilizes, so do its revenues and profits, sometimes holding the company stagnant if changes aren't made.

At the beginning of your startup, everything is new, exciting, and sometimes (or seems) less complex than it will be as the venture grows. Perhaps you have one or two employees, and you manage the operation's day-to-day activities. Managing the business is still within your power, and the structure of the business is fairly straightforward. Once the business takes off and encounters the challenges of development, such as hiring more employees to keep up with demand, adding new products, or expanding to new locations, you will need more resources and a different strategic approach to managing the business. You must be aware of these changes and steer the business in the right direction to continue its growth. As you begin to understand the signs of growth, you can correctly assess the challenge and come up with solutions. Going through these changes is what is called the **business lifecycle**, a process of five basic stages: starting a business, growth (expansion to new markets and products), maturity, decline, and death or rebirth, as Figure 10.15, shows.

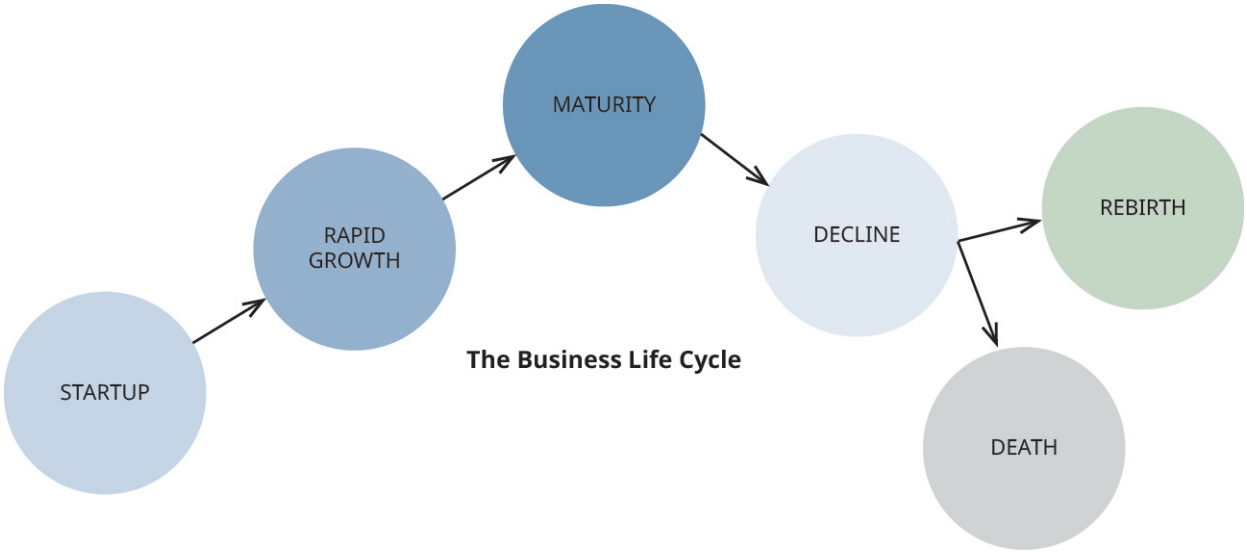


Figure 10.15 Businesses go through cycles of birth, growth, maturity, decline, and rebirth or death. Knowing the cycle of your business and industry will help you to take the steps in the right direction. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Lifecycle Stages

As companies reach new lifecycle stages, owners need to be on the lookout for change indicators. These may include rapid (growth stage), leveled (maturity stage), or diminishing (decline stage) sales. Or they may include the inability to keep up with demand without investing in capital, equipment, software, or technology. Other signs may be a need to increase staff and hire top- or mid-level managers to oversee an expanding workforce, or the need to grow by updating the product, introducing new products, or adding new markets.

Startup/Birth Stage

This stage centers around acquiring the first batch of customers. Entrepreneurs are focused on being able to actually provide and deliver the product, grow their customer base, and have enough cash flow to keep up with demand. The major concern is to survive by at least breaking even. This stage is simple in terms of ownership because there are usually only a few employees, if any. The processes are often informal, and technology and systems can be minimal. The owner usually wears many hats to launch the operation.

For example, an advertising agency might start operations with the co-founders and perhaps one or two employees who work as art designers and/or account executives. At the beginning, the point is to gain clients and deliver the services and products promised—such as TV ads, radio commercials, print ads, or digital ads—while consulting and managing client accounts. The goal is to gain client trust and make sure clients are paying for the services rendered so the agency can pay its employees and vendors. Breaking even is the most basic goal, which means that costs are at least covered, but no profits are seen just yet. Many times, the owner or owners of the company will not take a paycheck for many months, sometimes years, to ensure the business takes off.

Growth Stage

The growth stage, when sales rise due to higher demand, is full of change. There are increases in sales, profits, additional market/product penetration, and an expansion of professional staff. There is usually an increase in cash coming in and going out. A key factor in this phase is to avoid cash strain by paying close attention to costs and ensuring the payment from customers of product and services provided by looking at running reports on costs and sales daily, weekly, and/or monthly. At this stage, systems such as databases and software systems that help keep track of customers and sales, as well as formal processes, need to be put in place for marketing, technology, production, and human resources. Owners must also decide whether to continue with current strategies, sell, or perhaps merge with another company to continue growing. The owner will usually hire managers with experience to take the company to the next level. At this time, owners may need to take out loans and use equity power or shares of the company as capital to leverage further growth. The chapter on Entrepreneurial Finance and Accounting discusses these strategies in more detail.

At this point in our advertising agency example, there are more clients being served; the company is expanding as it adds new clients to the roster and hires more employees to keep up with demand. Revenue is higher, but costs are increasing as well. Processes need to be put into place so employees know what their tasks are and how to do them. Software that handles operations, such as accounting and project management, are put into place because the number of people and processes are increasing. Sometimes, the growth is so unprecedented that perhaps a merger with another company is necessary to be able to provide all the services that clients need.

Maturity Stage

As the business continues, it could enter maturity, which means it has grown to the point where revenues and profits level off. There is adequate staff and more management engaged in maintaining operations. Systems are well developed in all departments and working efficiently, with larger financials and management. The key to remaining active and spurring new life into the business is to remain flexible and continue being a creative and entrepreneurial company. Apple offers a great example of a company that, although its size and power have grown tremendously, continues to innovate as if it were a small company. Other companies such as GE and Procter & Gamble, although they are big corporations with many resources, are now mature and well balanced because they have been in business for a long time. However, they too must continue to innovate and shift with trends, and this is where the lean startup methodology fits well in both small and large businesses because it allows them to be creative and entrepreneurial, regardless of size.

Decline Stage

At this stage, as industries change or business owners fail to keep their offerings relevant, decline is imminent. Sales wane, and a rebirth or death of the business can be expected.

For example, Sears, Payless, Victoria's Secret, and JCPenney have recently been hit by the new technological and fashion trends that are affecting brick-and-mortar retailers. The way customers shop has been shifting from spending time browsing and shopping in a physical store to adopting new technology to shop from computers and mobile devices. Today, Amazon and other online retailers have developed strategic ways to help customers shop for items they want at an affordable price from the comfort of their devices. Retailers must come up with new, experiential ways to engage the consumer. Interestingly, companies such as GoPro and Fitbit are also struggling with declining sales due to competition, lower demand for cameras, and pricing. GoPro and Fitbit are still good brands that can benefit from a buyout from a bigger company, so they could have a rebirth.

Rebirth or Death Stage

When there are big changes in the decline stage that the company doesn't evolve to meet, or the business owner doesn't retain passion, focus, or ability for the venture, the business will end. Blockbuster failed to embrace the new era of video streaming and closed its stores in 2013. Similarly, small retailers, restaurants, tech companies, and manufacturers that fail to innovate cannot sustain a business and usually dissolve.

That is not to say that a rebirth is not possible. If a business innovates and changes to embrace new technology and ideas, it may restart the lifecycle. Polaroid, a pioneer in the instant camera market, saw its demise in the 2000s when the photography industry started to shift toward digital products. The company went bankrupt in 2001 and was sold to several holding companies (controlling companies that buy a stake in the business but don't operate the business), which licensed the name Polaroid to various electronics manufacturers. Recently, the company entered into an agreement with a holding company that specializes in brand resurrection to develop photography products. These products include a new instant camera and the Polaroid Swing app that allows people to create moving GIF photographs, which are several pictures rotated in a way that show movements and resemble very short videos.[70] Most recently, Polaroid has launched the camera OneStep+, which connects the camera to the phone through an app, allowing the photographer to use different filters and shoot and print instantaneously.[71] This camera, along with other lines of Polaroid instant cameras, have helped resurrect the brand.

The Pain of Growth

Expanding a business usually entails some growing pains. Professional stressors can include figuring out how to serve the customer in the best way possible, produce the right product, create a great brand, sell the right amount, manage cash, delegate tasks to others, and ensure the right people and systems are in place. And of course there are the personal stressors of managing a healthy work/life balance and meeting the demands of the venture.

70 Brian Mastroianni. "Polaroid Swing App Brings Moving Photos to Life." *CBS News*. July 27, 2016. https://www.cbsnews.com/news/polaroid-swing-moving-photos-smartphone-app/
71 "Meet the Polaroid OneStep+." Polaroid. n.d. https://www.polaroid.com/onestep-plus

In 2011, Jessica Thompson, owner of Johnson Security in New York City, felt the strains of growth. She had expanded from sixty to seventy employees and expected to hire ten to twenty more that year. News of her unprecedented business growth had catapulted Johnson Security into higher sales, thanks to better assessment of prospects (potential customers) and better written contracts, but it also heightened her concerns. She had to hire more people. She had to create the infrastructure needed to support the new positions. She had to make sure her liability costs were based on estimates of working hours, because if the number of employees grew, so did her costs. Her visible and public success also made her a target of the New York State Department of Labor, which audited the company to make sure she had classified her workers correctly as W-2 workers instead of as contractors. The audit results were fine and her growth proved organic, but the stress was something she had to go through to succeed as a business owner.[72]

Victor Clark of Clarke Inc., a consulting company, also knows a little about the pain of growth. When asked about his experience as a business owner, Clark said, "My biggest lesson would be 'profit is an opinion, cash is a fact.'" He says that he struggled many times with cash flow because he disregarded his checking account and because of late receivables. His advice is to pay attention to the checking account, never do a job that makes you lose money, know your costs, and review your numbers every single month.[73]

Strategies for Growth

What are some strategies for growth? Growth can mean increases in revenue and profits, and decreasing expenses. Here are various strategies that can help expand a business whether they are young or established companies.

Product Improvement

An inexpensive and easy way to increase sales of a new product can be done by enhancing a product. This can be in the form of updating the design, making it more durable, changing its size, adding a new feature, or increasing its quality. It is easier to enhance a product than to completely start from scratch.

Take appliances, for example. Rather than creating a new machine to wash clothes, Samsung continually adds features to its washing machines. Recently, the company changed its technology to high-efficiency (HE) technology to save water and energy, and included a separate feature that helps wash items by hand.

Usually, creative fragrance and perfume manufacturing companies can easily adjust their current fragrances by adding a new ingredient or scent instead of developing an entirely new fragrance. Artisanal perfume startups such as Phlur and Pinrose have recently developed their own lines of perfumes that are environmentally conscious, not tested on animals, and good for the body. Some of their perfumes now have new versions of their signature perfumes. In addition to improving their products, they also created new ones out of their original scents by adding them to body sprays, lotions, lip shimmer, and candles that smell exactly like the original.

LINK TO LEARNING

Read this *Forbes* article on Phlur perfume (https://openstax.org/l/52ForbesPhlur) and see how Phlur sold thousands of bottles of its perfume before customers could smell it.

72 Adrianna Gardella. "Growing Pains at a Growing Business." *New York Times*. November 3, 2011. https://boss.blogs.nytimes.com/2011/11/03/growing-pains-at-growing-businesses/
73 Andrea Lotz. "5 Entrepreneurs Share Their Business Growing Pains." *AllProWebTools*. October 9, 2015. https://www.allprowebtools.com/5-Entrepreneurs-Share-their-Business-Growing-Pains/

Market Penetration

Market penetration entails selling more to current customers by showcasing new uses for an existing product. This is the least costly way to attract more customers from within the market. A great example is the versatility of the common pantry staple you see in Figure 10.16, baking soda. Until the 1920s, baking soda was used only as a leavening agent for baking. The mid-century emergence of convenience foods, including premade baked goods, meant a decrease in demand for the product as people baked less at home. To boost sales, Arm & Hammer explored its other uses and began to sell it as a deodorizer, detergent, remedy for heartburn, and as an additive to other products such as detergents, toothpaste, and cleansers.[74]

Figure 10.16 Arm & Hammer penetrated the baking soda market by expanding uses for the product. (credit: modification of "Baking Soda Box White Powder" by "evita-ochel"/Pixabay, CC0)

New Distribution Channels

Adding new distribution channels gives current customers more ways to purchase the product. For instance, the Internet has provided opportunities for companies to expand their reach by selling items online. Consider a bakery that, in addition to distributing its cookies in its store and through retailers, adds an online store. While a large number of companies have websites and apps that can sell directly to customers, entrepreneurs who don't want or have an e-commerce function on their site can use portals such as Etsy, Amazon, and Ebay. A jewelry maker, for instance, can sell items through one of these websites without having to pay someone to create or manage a website for their business. Other more conventional ways of using different distribution systems include making products available in retail stores, kiosks, or grocery stores. Take for instance California Pizza Kitchen. It originally existed solely as a restaurant chain but now has created frozen pizzas that we can purchase at the grocery store.

Product Line Extension

A business can extend its product line to appeal to different customers with different needs and budgets. It can start with a basic, no-frills product for the low-end consumer. Then, it can provide a higher quality, higher-price product with a few more features. A step higher would be a high-end product that is more luxurious or has additional benefits and capabilities that are higher priced. This strategy is often used with cameras, software, vehicles, and hotels. Tech companies will have their basic products and will increase their gadgets' quality and benefits to make them more luxurious and capture different markets along the way. Uber, for example, offers its basic riding service to everyone who requests a ride. Drivers can pick them up in any type of vehicle they own. An upgrade to this service is the new Uber Black service, which gives the customer the ability

74 "A History of Innovation: Our Timeline." *Arm & Hammer*. n.d. https://www.armandhammer.com/en-ca/about-us

to request a luxury car or SUV. These vehicles must be newer than five years old, and they must be in excellent condition. This service is more expensive than regular rides, costing three or four times more than a ride in a regular vehicle.

Adding New Markets

Developing new markets is a riskier path to growth. A company that was catering to only local customers might open a second location in another town or region, or provide products online to reach distant clients in other cities, states, or countries.

Fast fashion companies have been at the forefront of this trend. These are retailers that design, manufacture, and distribute the product to customers quickly and cheaply by skipping the regular four seasons of the fashion year. Instead, they usually offer new designs every two or three weeks, and entice shoppers to purchase clothing at a faster rate. Retailer store Zara, (pictured in Figure 10.17), the fast fashion company from Spain, has seen unprecedented growth through expansion to other markets, for example.

Figure 10.17 Fast fashion company Zara has been successful at developing new markets. (credit: modification of "Zara 222 Broadway" by "Lollasp"/Wikimedia Commons, CC0)

Born Global Companies

As mentioned earlier, entering global markets is a common method of expanding a business. Some companies will turn to global expansion during a growth or mature cycle, and some companies will seek global markets from the start, as **born global** companies do. A born global company is one that has as its goal to serve the world with its products. Companies that have new products that have never been created before—today mostly technological and medical products—usually benefit from this kind of strategy. Other entertainment and consumer products can be thought of as global as well, especially when it's a new product category.

Red Bull is an example of a born global company that had its eyes set on the global stage, even before it started growing, because it had a new product that no other company had ever created. After Red Bull came up with its products, other companies followed suit, and a new product category of energy drinks was born. So far, the company has been around for 31 years, has more than 12,000 employees in 171 countries, and has sold more than 75 billion cans around the world.[75] The success that this born global company has experienced can be attributed to its grassroots marketing approach on college campuses, the sponsoring of events (Figure 10.18 shows two examples), as well as a massive distribution approach that targets young people, extreme sports athletes, and professionals who need an energy boost.

75 "Company." *Red Bull*. n.d. https://www.redbull.com/us-en/energydrink/company-profile

(a) (b)

Figure 10.18 Red Bull owes its success to its promotional efforts across the globe. The company has found success (a) targeting consumers interested in extreme sports, such as these spectators attending a cliff diving event in Massachusetts, and in sponsoring events like this (b) Motocross competition. (credit (a): modification of work by "{enry"/Flickr, CC BY 2.0; credit (b): modification of work by "GO Visual"/Flickr, CC BY 2.0)

LINK TO LEARNING

In its efforts to be a global company, Red Bull sponsors many events. In 2012 Red Bull sponsored Stratos, the highest jump (https://openstax.org/l/52RBStratos) ever recorded by a person from space, in a "beyond global" event. They also sponsored the "Can You Make It?" 2018 competition (https://openstax.org/l/52RBCanMakeIt) in which teams of students traveled across Europe to Amsterdam in a week using only Red Bull as currency.

Licensing, Franchising, Joint Ventures, Mergers, and Acquisitions

Other riskier ways to grow include the integration of outside ventures through licensing, mergers and acquisitions, joint ventures, and strategic alliances.

Licensing is a contract in which one enterprise gives permission to another entity to manufacture and sell its products for a royalty, which is a payment in exchange for the use of property or an asset, whether intellectual or physical that can be used to generate revenue. Some of the property that can be licensed can be in the form of a design, a copyright, an invention, a patent, or formula.[76] Instead of investing directly in manufacturing and marketing additional items, many companies such as Disney, Mattel, NBA, and Warner Brothers lend their characters and copyrights to other companies to use on their merchandise. They then receive a royalty payment for their license.

Licensing can also occur in reverse: Small companies with a technology, medical solution, software, or product that cannot be manufactured by them can seek other companies to which they can license their intellectual property. The smaller company can also license from another company and create the product or service because that is its core competency.

Franchising is a form of licensing that allows the business (franchisor) to share its business model to expand the business through various distributors (franchisees) for a fee. In turn, the franchisor provides the training, marketing, know-how, management, and support to help the franchisee fulfill its sales objectives. Franchising

76 "Licensing." *Entrepreneur* n.d. https://www.entrepreneur.com/encyclopedia/licensing

is common in industries such as restaurants, automotive, hotel, cleaning, and home services, to name a few. Popularly known franchises are fast-food restaurants, such as Chick-Fil-A or McDonald's, which have quickly expanded in the US—and around the world in the case of McDonald's. Smaller local and national franchises include Fit4Mom, Mosquito Squad, Chocolate Factory, and Soccer Shots.

A **joint venture** is the creation of a new business in which two different enterprises share the expenses and profit to achieve certain goals of a project. This approach reduces the risk of investing directly in capital equipment, and it also allows them to share each other's knowledge and expertise. You can see this done with small businesses that collaborate to save money and help each other out.

Larger companies do this as well to leverage a particular advantage and reduce risks and costs.[77] Google and NASA joined efforts to bring NASA's information about the weather, locations, and forecasting to the fingertips of people via a Google search. This joint venture proved fruitful, as they continue to collaborate on various projects including robotics and space exploration.[78]

In **mergers and acquisitions**, two companies combine or one buys the majority stake of the other. The goal is to enhance profitability and reduce their risk by diversifying their portfolios, combining resources such as boards of directors, combining efforts to achieve efficiency (for example, being able to increase production and thereby reduce production costs), broadening market access, sharing technology, and increasing access to capital. Usually, mergers and acquisitions are conducted by larger companies such as Dow Chemical and DuPont, Anheuser-Busch InBev and SAB Miller, Heinz and Kraft, and CVS and Aetna, but smaller companies can also benefit if they both have an opportunity for synergy.

Strategic alliances are arrangements that two or more entities create to work on a project by sharing some of their strengths and resources, but not actually creating a new entity like in the case of a joint venture. In this alliance, both entities are still considered independent and only pool their resources to work on a specific project because it may be faster and more cost effective to work together. Both companies' assets remain separate.[79] An example of this is Star Alliance, a strategic distribution alliance between many airlines such as United Airlines, Lufthansa, Air New Zealand, Turkish Airlines, Croatia Airlines, and 22 additional airlines, to connect customers all over the world through a shared booking system.[80]

Pros and Cons of Growth Strategies

Each growth opportunity has pros and cons, which are outlined in Table 10.6.

Pros and Cons of Growth Strategies

Strategy	Pros	Cons
Product improvement	Improving performance, quality, and cost of product; can also add to sales and profits	Fails to deliver a benefit; can turn out to be a lost investment
New product development	Staying ahead of the competition, increasing sales/profit, going into new markets	Create products no one wants, make costly mistakes

Table 10.6

77 "Joint Ventures." *Inc.* n.d. https://www.inc.com/encyclopedia/joint-ventures.html
78 "Google Moves into NASA's Space." *Financial Times*. November 10, 2014.
79 Will Kenton. "Strategic Alliance." *Investopedia*. September 5, 2019. https://www.investopedia.com/terms/s/strategicalliance.asp
80 "Proud Member of Star Alliance." *United*. n.d. https://www.united.com/web/en-US/content/company/alliance/star.aspx

Strategy	Pros	Cons
Market penetration	Increase sales by adding new benefits to existing products	Mispositioning the product, which will miss communicating to the right market or by communicating benefits the target doesn't care for
New distribution channels	Reaching target market multiple times or reaching them at least once	More channels to keep track of and to manage
Product line extension	Cater to different markets and different budgets; educate consumers to want better, more expensive products	Fails to differentiate between products, cannibalization (decrease in sales due to introduction of new product by same company)
Adding new markets	Expanding customer reach, adding to sales and profit	More customers to take care of, not engaging them correctly
Seek global markets	Serve global markets, reach more customers, increase sales and profits	Dealing with more customers, mistakes in many areas could happen
Integration of businesses	Add new capabilities, synergy, take on more projects	Losing investment, losing project, not getting along well, breaking up

Table 10.6

Key Terms

born global venture seeking to be a global company from its inception
build-measure-learn loop step-by-step approach on how to maneuver a startup, how to change course if necessary, how to persevere, and how to accelerate the expansion of a business
business failure ending a business due to the lack of goal attainment, which can include low levels of revenue and profit, or not meeting investors' expectations
business lifecycle stages companies go through: birth, growth (or expansion to new markets and products), maturity, decline, death or rebirth
early adopters people who like to try new things and can be found at the onset of the adoption process for a product
franchising form of licensing that allows the business (franchisor) to share its business model to expand through various distributors (franchisees) for a fee
Global Entrepreneurship Monitor (GEM) organization that researches entrepreneurship around the world
innovation accounting assesses whether the changes made to the product are creating the desired results
iterations small changes to the current version of a product to make it better fit consumer needs
joint venture temporary partnership in which two different enterprises combine for the purpose of mutual benefits such as sharing of expenses and to work toward shared goals and the associated potential revenue
lean pitch verbal delivery of an idea or business plan as a request to a group of investors by an entrepreneur
lean plan brief business plan shown to potential investors and employees that is a fast and effective way to set, manage, and evaluate goals and strategies in a business
lean startup methodology entrepreneurs use this method to help them innovate by continuously testing their products and getting feedback from customers in real time
licensing contract in which one enterprise gives permission to another entity to manufacture and sell its products for a royalty
mergers and acquisitions when two companies combine, or one buys the majority stake of the other
minimum viable product (MVP) early version or prototype of a product that may not be polished or complete but that functions well enough that you can begin to market it or test it with potential users
pivoting crucial change done to test a hypothesis regarding the basic product, its growth potential, and business model; if something is not working, then a change or a "pivot" needs to take place
strategic alliance arrangement created by two entities to work on a project by sharing some of their strengths and resources, but not actually creating a new entity as in the case of a joint venture

Summary

10.1 Launching the Imperfect Business: Lean Startup

There is no such thing as launching a perfect business. A startup requires time to clarify its identity, market, product, and business model through the build-measure-learn loop, which requires businesses to describe or *build* a prototype of a product, ask for feedback from potential and actual early customers, *measure* their responses, and *learn* from that feedback and make changes to improve the product to something customers want. Older companies usually have a more stable and developed set of strategies because they have been in business for a while, but even they have opportunities to innovate and grow. The lean startup method provides an opportunity for companies to approach management in a measurable and provable way. Customer feedback allows the companies to make iterations and pivots that are necessary to get back on the right track. Pitching to investors can yield better results when using the lean approach, because investors like to see experience-gained data. The lean startup method is a tested way for new and old companies to stay in business and operate, even when there is a lot of uncertainty.

10.2 Why Early Failure Can Lead to Success Later

Failure is common in business creation, especially in the early stages. Only a small percentage of ventures

make it to the two-, five-, and ten-year mark. Common reasons for this include mistakes and missed opportunities in marketing, financing, management, and innovation. However, there are steps the owner can take, such as making sure they are targeting the right customer, ensuring proper finances are in place to operate and grow the business, creating contracts when sharing the business with stakeholders, and innovating when needed. Fear of failure is also a major contributor to business failure. Some suggestions to manage fear include adjusting expectations and asking for help.

10.3 The Challenging Truth about Business Ownership

Entrepreneurs operate in an extremely competitive landscape. This space has positives and negatives, including being autonomous, being able to expand one's own ideas, and schedule flexibility. Serving people and employees well can be very satisfying as can the financial success of a strong profit. On the negative side, resolving constantly arising challenges, wearing many hats, dealing with challenges and issues, and having adequate time and cash flow can make entrepreneurship difficult. Women and minority entrepreneurs face additional challenges that can make the experience of being an entrepreneur much more difficult. These include lack of funding opportunities, lack of business education, not being taken seriously, lack of mentorship, and lack of resources. However, there are several organizations that provide the guidance and connections targeted to these groups.

10.4 Managing, Following, and Adjusting the Initial Plan

Having a lean plan is helpful in setting up expectations and measurements. This is a living document, so its creation and updating are a process. The process starts with building a short document that outlines the basics of product, market, and strategies, with a short schedule of tasks. After a trial run, where the prototype or actual product is tested with customers, the plan is reviewed and revised to incorporate the feedback.

10.5 Growth: Signs, Pains, and Cautions

A company goes through a lifecycle of birth, growth, maturity, decline, and death or rebirth. At each of these stages, there are opportunities and choices to make based on the owner's personal and business goals. Business growth requires the owner to innovate through various means to survive and to thrive. These strategies are meant to increase sales, cut costs, or a little of both. Some of these strategies include making changes to the product, adding new products and markets, adding new channels, and acquiring other companies.

Review Questions

1. What is pivoting?
2. How is pitching different in the lean startup method?
3. What is the lean startup process?
4. What are some examples of an MVP?
5. What is the success rate of businesses in the first two to ten years of life in the United States?
6. How can an entrepreneur learn from failures?
7. Which gender experiences more fear about opening a business? Why do you think it they are more fearful?
8. What are some of the realities of business ownership?
9. How can entrepreneurs deal with these negative realities?
10. What percentage of businesses last five years or more?
11. What percentage of US businesses are minority owned?

12. What is a lean plan and what are its components?
13. What are some of the items or sections that do not have to be included in a lean plan?
14. What kind of lifecycles do businesses go through? Why?
15. How does each phase affect business decisions?

Discussion Questions

1. Find an example of a video of a lean pitch online. What, in your opinion, makes it successful?
2. Find a company that has made a pivot and explain why the pivot worked.
3. If you were starting a business and had to create an MVP, what would that MVP be?
4. Are there any downsides to the lean startup method? If so, what might they be and what sorts of products or companies might fall prey to them?
5. If you were conducting a lean pitch to investors, which steps of the pitch would you find most difficult and why?
6. Discuss how you could identify and manage your fears as you start your own business.
7. What strategies do you think can help women overcome their fear of failure? Relate your answers, if applicable, to a woman you know who has such fear and describe strategies she uses to overcome it.
8. Discuss how minorities and women can use resources and strategies to deal with their additional challenges as entrepreneurs.
9. Pick three cons of business ownership and strategize how to turn them into pros.
10. Now choose three of the pros of business ownership and consider whether any of them could be cons in certain situations.
11. Discuss how a lean plan allows you the flexibility to change course if something is not working for your business.
12. Discuss the differences between making changes to a product for growth and creating a new product from scratch.

Case Questions

1. A friend recently heard that you won a pitching competition and she would like you to help her with her business pitch to investors. She started a company called “Fit for You,” a prosthetics company for children and adults that is using the latest materials and technology to help people live better lives. She has been in business for a year, and she uses lean methodology to innovate and create better products, but she needs capital to buy additional equipment to meet demand. She has determined that investors would be the best funding source for her needs. What should she focus on in a five-minute lean pitch to investors to secure the $120,000 for additional equipment?
2. One of your friends has recently opened a 24-hour gym for women ages 18–45. She is excited about the opening but wants to ensure that she is providing the right services to her customers and is wondering whether she did enough research up front to really figure it out. She comes to you for advice. What would you tell her?
3. Take a look at the GEM page http://www.gemconsortium.org/country-profiles and click on the US link. Determine how the United States ranks in several measures on its profile. How does its entrepreneurial ecosystem compare to that of another country, such as Mexico or Canada?

4. Your best friend is a kindergarten teacher who has decided to open a new learning center where toddlers and young children can play in an interactive environment to enhance their motor skills, cognitive development, and leadership skills. She is very excited about her new entrepreneurial experience, but has no idea about the challenges she may face as a young Hispanic woman in her 30s. She knows you have taken an entrepreneurship class before, so she asks for your help in figuring out where to find business resources and recommendations to overcome the challenges she may face. You are happy to help and you answer the following questions:
   What kind of overall advice would you give her? What groups and resources do you think she can tap into? What are some of the challenges she may face as a minority? How can she overcome them?
5. You and a team of students from your university are interested in creating a virtual agent (chatbot) that can interact with humans online. You have noticed that small businesses could benefit from adding a chatbot to provide great customer service at all times of the day at a fraction of the cost. Your goal is to create chatbots for a few industries that are very customer-service intensive (realtors, restaurants, doctors' offices, etc.), and you think you can come up with a product that can be sold to small- or medium-sized businesses. One of your team members who is a computer science major has already starting coding the first program, but you know very well that you will need lean planning to get your ideas down in writing and to pitch it to a few investors. Develop your 7Ps for one of the chatbots in bullet point format and include the target market, the positioning, and the business model that you would use to make money.
6. You and your business partner have been in business for five years selling cellphones and other accessories. Recently, you noticed that the market is quite saturated, and your competition is very high. Your sales have been flat for the last year and a half, and no matter what promotions or cellphones you carry, you can't seem to improve your sales. You also realize that the industry is mature and it will be difficult to make money unless something drastic changes. What kind of changes do you think you can implement to expand your business?

Suggested Resources

10.1 Launching the Imperfect Business: Lean Startup

Lean startup: http://theleanstartup.com/#principles

Toyota's Way: https://vimeo.com/44328452

14 Management Principles of Toyota: http://www.panview.nl/en/lean-production/toyota-way-j-liker-summary

Innovation accounting video: https://www.inc.com/eric-ries/entrepreneur-eric-ries-innovation-accounting-secret-to-fast-growth.html

10.2 Why Early Failure Can Lead to Success Later

Global Entrepreneurship Monitor: http://www.gemconsortium.org/

10.3 The Challenging Truth about Business Ownership

Asian American Chamber of Commerce: http://www.asian-americanchamber.org/

Black Chamber of Commerce: https://www.nationalbcc.org/

Hispanic Chamber of Commerce: https://ushcc.com/

Ladies Who Launch: https://www.ladieswholaunch.org/

Minority Business Development Agency: https://www.mbda.gov/

National Association of Professional Women: http://womenforhire.com/company/national-association-of-professional-women-napw/

National Association for Women Owners: https://www.nawbo.org/

Small Business Agency: https://www.sba.gov/

The Female Entrepreneur Association: https://femaleentrepreneurassociation.com/

Women's Business Center at SBA: https://www.sba.gov/tools/local-assistance/wbc

Women's Business Enterprise National Council: https://www.wbenc.org/

10.4 Managing, Following, and Adjusting the Initial Plan

Tim Berry's Lean Business Planning Guide: https://leanplan.com/

10.5 Growth: Signs, Pains, and Cautions

International Franchise Association: https://www.franchise.org/

US Small Business Administration Licenses and Permits: https://www.sba.gov/business-guide/launch-your-business/apply-licenses-permits

11

Business Model and Plan

Figure 11.1 The initial plan for Vita Coco did not work for its founders, Michael Kirban and Ira Liran, but the coconut water found later success, ultimately becoming the market leader, by using customer-focused design throughout the entrepreneurial process. (credit: modification of "Vita Coco at Vitality Show" by Zeyus Media/Flickr, CC BY 2.0)

Chapter Outline

11.1 Avoiding the "Field of Dreams" Approach
11.2 Designing the Business Model
11.3 Conducting a Feasibility Analysis
11.4 The Business Plan

Introduction

Michael Kirban and Ira Liran had no experience in their industry when they launched their business. After a chance encounter with Brazilian women in a bar who mentioned how much they missed having coconut water, Kirban and Liran decided to launch Vita Coco.

The Vita Coco founders promised to deliver a product they had not even created yet, and further, they had no experience in manufacturing, but they launched the business nonetheless in the early 2000s. The initial plan for the business did not work after the US Food and Drug Administration blocked shipments to the United States because they failed to register the business properly. The partners developed the business into a social movement with a specific mission: to make an impact on both their consumers and the people they work with and the communities in which they live. Things ultimately worked out for Kirban and Liran. Vita Coco became the market leader in this niche segment, as they turned their attention to putting customers first. Although customer-focused design is integral to the entrepreneurial planning process, you should avoid launching a venture with the attitude that if you build it, customers will automatically come, because it does not always work that way. There are tools available to entrepreneurs to use to plan their journey to make goals a reality rather than just a wish or a dream.

11.1 Avoiding the "Field of Dreams" Approach

Learning Objectives

By the end of this section, you will be able to:

- Understand the importance of planning
- Understand the concepts of product and service innovation, and define and understand key business models
- Describe and be able to construct a value proposition for a new business idea (product or service)

In the 1989 film *Field of Dreams*, Kevin Costner plays an Iowa farmer who hears a voice that tells him, "If you build it, he will come." Inspired by this vision, Costner's character turns his cornfield into a baseball field (of dreams), and eventually the ghosts of deceased baseball players such as Shoeless Joe Jackson appear on the field as younger versions of themselves. The movie coined the popular axiom that "if you build it, they will come," just as the players appeared after the field of dreams was built. Although it's a fun saying for film buffs and sports fans, this approach is one you will want to avoid in entrepreneurship. In fact, the entrepreneurial graveyard is littered with ghosts of startups that never gained traction with customers, never to be heard from again. (Seventy-five percent of venture-backed startups fail, according to one recent study.)[1] Thus, you don't want to blindly build a product and hope that customers will come. Juicero is one recent example of product that conducted little-to-no customer discovery before launch. A cold press juicer made by this San Francisco startup cost $699 at launch. The juicer squeezed packs of cut up fruits and vegetables, but customers found they could just as easily squeeze the juice out of the packs by hand and avoid the hefty price of the juicer.

Customer acquisition and customer retention are not easy processes by any means. You have to work to gain a customer and work even harder to get her to return. One study by the data analysis firm CBInsights of why 101 startups failed found that 42 percent of them joined the "entrepreneurial afterlife" because there was "no market need," which suggests a customer (or lack thereof) problem.[2] Current trends in entrepreneurial thinking reflect a customer-centric approach: From the start, entrepreneurs infuse their insights into the planning process through a process called "customer discovery." The entrepreneurial journey should begin with finding what the serial entrepreneur, author, and educator Steve Blank, one of the founders of modern entrepreneurship, calls the problem/solution fit.[3],[4] In a complementary approach, the Mosaic/Netscape founder Marc Andreessen discussed the need to achieve product-market fit.[5] In other words, don't just build a baseball field and expect players to show up. This is an oversimplification, but if we extend the *Field of Dreams* analogy before blindly believing in the magic, you would want to talk to prospective players and fans to see if a field is needed, what type of field (corn-to-baseball?), why that field is needed, how that field would be used, and what features of the field would be most useful—*before* you go to bat (Figure 11.2).[6]

1 Patrick Henry. "Why Some Startups Succeed (and Why Most Fail)." *Entrepreneur*. February 18, 2017. https://www.entrepreneur.com/article/288769
2 "298 Startup Failure Post-Mortems." *CBINSIGHTS*. February 28, 2019. https://www.cbinsights.com/research/startup-failure-post-mortem/#original
3 Steve Blank. "Driving Corporate Innovation: Design Thinking vs. Customer Development." July 30, 2014. https://steveblank.com/2014/07/30/driving-corporate-innovation-design-thinking-customer-development/
4 Hayley Leibson. "How to Achieve Product-Market Fit." *Forbes*. January 18, 2018. https://www.forbes.com/sites/hayleyleibson/2018/01/18/how-to-achieve-product-market-fit/#10814b68476b
5 Tren Griffin. "12 Things about Product-Market Fit." *Andreessen Horowitz*. February 18, 2017. https://a16z.com/2017/02/18/12-things-about-product-market-fit/
6 Mike Pinder. "Innovation Reality Check: Are You Building a 'Field of Dreams'?" *Board of Innovation*. December 31, 2017. https://www.boardofinnovation.com/blog/2017/01/31/innovation-reality-check-are-you-building-a-field-of-dreams/

Figure 11.2 This field in Dyersville, Iowa, was used in the filming of *Field of Dreams*. (credit: "FieldofDreamsMay06" by "JoeyBLS"/Wikimedia Commons, CC BY 2.5)

Business Model

Although there are countless varieties of business models, the *Scaling Lean* author Ash Maurya offers three common types: direct, multisided, and marketplace. Direct businesses are the most common and involve one-sided actors—that is, users—becoming your customers. A coffee shop is a classic example; other examples include retail stores, software as a service (SaaS), many mobile apps, hardware stores, and stores that sell physical goods. In multisided models, users and customers—multi-actors—are usually different people. Ad-based models, big data, and enterprise are common examples where the products are free to users, and their value is monetized by a different customer base. Marketplace models are a more complex variant of multisided models made up of two different customer segments of buyers and sellers. eBay and Airbnb are well-known examples of marketplace models.[7]

Although planning is important, adaptability within the planning process is equally important. That's what the business model approach is all about: outlining an approach but changing that approach throughout if or when you discover that your assumptions and educated guesses were wrong. For each new iteration, or version, the entrepreneur makes a minor change to the current business model to better capitalize on market opportunities.

Successful entrepreneurs are often multidimensional: part dreamer, part pragmatist. Adam Grant, Wharton School of Business professor and author of the best-selling book *Originals: How Non-Conformists Move the World*, explores how entrepreneurs are "capable of recognizing a good idea, speaking up without getting silenced, building a coalition of allies, choosing the right time to act, and managing fear and doubt."[8] *Entrepreneur* magazine tells the story of FedEx founder Fred Smith, who, while attending Yale University in the mid-1960s, wrote an economics term paper on the need for a new approach to overnight delivery in the computer age. His professor, unimpressed with Smith's idea, graded his paper a C because the idea was not feasible.[9] After graduation, using innovative thinking, dogged determination, and hard work, Smith would turn his "unfeasible" concept into the world's first overnight delivery company, and in so doing, change the transportation industry forever. Smith embodied the entrepreneurial concept of being part dreamer, part pragmatist.

LINK TO LEARNING

Read about the popular corporate narratives related to relatively new companies. Consider whether these stories involve inventor-founders. If so, what is the invention and how does that tie in with the current and

7 Ash Maurya. *Scaling Lean*. New York: Portfolio/Penguin, 2016.
8 "Bio." Adam Grant. n.d. https://www.adamgrant.net/bio
9 "Fred Smith: An Overnight Success." *Entrepreneur*. October 9, 2008. https://www.entrepreneur.com/article/197542

future narrative of the company?

Listen to the NPR podcast "How I Built This" with Guy Raz (https://openstax.org/l/52NPRGuyRaz) to hear stories about more than 100 startup companies and their founders.

Several more brief narratives on how to tell your company's story (https://openstax.org/l/52CompanyStory) are also available.

Sports metaphors offer important entrepreneurial lessons beyond insights on customer discovery and planning. In baseball and softball, you must field a team to enter the game. In boxing, you enter the ring alone to go toe to toe with your competitor (where some of the best-laid plans get thrown out after you get hit). The tides of entrepreneurial thinking have shifted from the twentieth-century economist Joseph Schumpeter's early belief that it is "lone individuals who carry novelty" for wider market exploitation and benefit to society to the notion that it takes a team to innovate and back to the idea that individuals can enact entrepreneurial change.[10] "Solopreneurs," for instance, are hard-working entrepreneurs who are comfortable working alone on all the requisite tasks of starting a venture.[11] At the same time, many successful investors preach the merits of teams in entrepreneurship. Venture capitalist Aileen Lee says that people are the second-most important factor behind addressable market when evaluating startups.[12] The cohesion, diversity, and makeup of the team all contribute to investable worthiness and potential entrepreneurial success (Figure 11.3). Many successful accelerator programs have typically required teams in order to be considered for entry into their programs. The accelerator Techstars has said that what they look for in a startup is "team, team and team,"[13] and the accelerator Boomtown requires at least two present founders for the duration of its accelerator program.[14]

Figure 11.3 While solopreneurs can certainly find success, many ventures find value in a team approach. (credit: "achievement agreement arms business" by rawpixel/Pixabay, CC0)

Multiple shifts in sources of innovations and rapid business model exploration may reflect high startup failure rates. Lack of planning is also a major reason for failure. Most small businesses fail within the first few years because of cash-flow issues. With more people today willing to field a startup team or enter the

10 Joseph A. Schumpeter. *Can Capitalism Survive?* New York: George Allen & Unwin, 1942.
11 John Rampton. "4 Differences Between Solopreneurs and an Entrepreneur Working Alone." *Entrepreneur*. May 15, 2015. https://www.entrepreneur.com/article/245766
12 Aileen Lee. "Investing and Business Lessons from Aileen Lee (Cowboy Ventures)." *25iq*. April 21, 2018. https://25iq.com/2018/04/21/investing-and-business-lessons-from-aileen-lee-cowboy-ventures/
13 Michael Cohn. "Team, Team, Team: Welcome Tyler Scriven to Techstars Atlanta." *Techstars*. April 13, 2016. https://www.techstars.com/content/accelerators/team-team-team-welcome-tyler-scriven-techstars-atlanta/
14 The Farm. "Accelerator FAQs." n.d. https://thefarmatl.com/about/faq/

entrepreneurial ring, failure is more often than not a part of the entrepreneurial journey. Serial entrepreneurs launch numerous ventures, many of which fail, before moving on to other efforts. Entrepreneurs are the modern-day equivalent of *Hamilton: An American Musical*'s Hercules Mulligan to the world: They get back up again after getting knocked down.

Innovation

One of the fundamental theories of entrepreneurship is that it brings **innovation**, which can be a new addition to the market or a novel change to an existing product or service. The famed management guru Peter Drucker put it simply: "Entrepreneurs innovate."[15] Of course, we should note that not all entrepreneurial ventures involve innovation. Even for those that do, however, the term *innovation* can be ambiguous. Further complicating the issue, a plethora of different extensions (or "types") has arisen surrounding the concept of innovations—such as radical, incremental, and disruptive—that have been used to describe and emphasize different innovations in different situations.[16] *Innovation* can also refer to products or processes because there are differences between product innovation and process innovation. In other words, not all innovations are created equal.[17]

As it pertains to entrepreneurship, the creative destruction of old markets with inferior technology and the creation of new markets, as defined by Schumpeter back in the 1930s, occurs through **disruptive innovation**.[18]

The adjective *disruptive* also became a bit of a catchphrase in the 1990s during the first Internet era, largely due to the popularity of Clayton Christensen's Figure 11.4 theory of incumbent failure in the face of what he first termed "disruptive technology" and later renamed "disruptive innovation."[19]

Figure 11.4 Clayton M. Christensen has contributed many ideas about innovation to the field of entrepreneurship. (credit: "Follow Business of Software - Clayton Christensen" by Betsy Weber/Flickr, CC BY 2.0)

As Christensen defines them, disruptive innovations are often more advantageous to new entrants than to incumbent firms. This is because once market uncertainty occurs as a consequence of the disruption around the disruptive product, established firms consider it irrational to abandon their existing paying customers for the smaller customer base of the new, initially small market for what they believe is inferior technology. New

15 Peter F. Drucker. *Innovation and Entrepreneurship: Practice and Principles.* (New York: Harper Business, 1985), 30.
16 Henri Simula. "Concept of Innovation Revisited: A Framework for Product Innovation." *International Association for Management of Technology 2007 Proceedings.* 2007.
17 Salem Baer. "The 3 Types of Innovation: Product, Process, & Business Model." *Differential.* January 16, 2017. https://differential.com/insights/the3typesofinnovation/
18 Joseph Schumpeter. *Theory of Economy Development: An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle* (Cambridge: Harvard University Press, 1934), 19.
19 C. M. Christensen. *The Innovator's Dilemma: When New Technologies Cause Great Firms to Fail* (Boston: Harvard Business School Press, 1997). C. M. Christensen, Taddy Hall, Karen Dillon, and David S. Duncan, *Competing Against Luck: The Story of Innovation and Customer Choice* (New York: HarperCollins, 2016).

entrants challenge incumbent firms by either creating markets where no markets exist, turning nonconsumers into consumers, or by targeting overlooked segments of the market and later moving up market as the product improves. Leading firms' decision criteria for developing new products and commercializing innovations are all biased toward supporting incremental innovations that build on their existing technology base and help maintain or grow revenue and profitability in established markets. This opens the door for startups to develop and introduce disruptive innovations and profit from them. Table 11.1 lists some disruptive innovations.

Disruptive Innovations

Area	Timeframe	Established Market	Disruptive Innovation
Medical imaging	1960s	X-rays	Ultrasound offered a new type of imaging; X-ray companies lost out to the market and could not match the innovation, although eventually they purchased many ultrasound companies
Screens	1990s–2000s	CRT (cathode ray tube)	LED/LCDs innovated to overcome their display limitations, replacing heavy and bulky CRTs. More recent innovations like foldable screens and retinal scans have added more functionality and "intelligence" to link to Internet of Things devices
Entertainment	2000s	Video rental	Streaming services ousted much of the video rental market and companies like Blockbuster found themselves irrelevant in the market. More recently, multiple streaming services along with proprietary content (and "Over the Top" menu options) have disrupted cable TV companies

Table 11.1

ARE YOU READY?

Netflix's Disruption

Netflix, founded in 1997 in California, disrupted video rental stores such as Blockbuster with its subscription service, which mailed DVDs directly to customers' homes. The rental stores, whose business model was predicated on revenue from late fees, could not compete with the ease and convenience of home delivery coupled with lower costs than the per-tape rental fees. But as streaming video content directly to televisions or over-the-top devices disrupted Netflix's original DVD-by-mail model, Netflix moved to offer a streaming service in addition to the DVD by mail model. In both instances, Netflix's prevailing model was predicated on serving as a distribution outlet for content created by other businesses. Netflix in recent years has begun not only distributing others' content but creating its own TV and movie content as well. (*Orange Is the New Black* and *The Unbreakable Kimmy Schmidt* are both original Netflix series; *The Irishman* is an original Netflix film.) Now content creators such as Disney and Marvel are creating their own streaming distribution platforms to exclusively deliver their own content, eventually pulling those shows from Netflix.

- What should Netflix do to counter this threat to the third iteration of its business model?

- What threats does the end of net neutrality pose to Netflix's business model?
- If you were in charge at Netflix, would you pay more to Internet providers to gain faster delivery of your content on the Internet? Why or why not?

In separate but related work, Christensen also developed the jobs-to-be-done theory, which aids companies in determining how to create products and services that customers want to buy by getting at the causal driver behind a purchase. Christensen uses the term *job* as shorthand for what an individual wants to accomplish in a given circumstance, often with social, emotional, and functional dimensions. For example, two jobs that a newspaper does for its readers are to inform and entertain, whereas the jobs to be done of a newspaper are completely different for another customer segment—advertisers. A newspaper's jobs to be done for advertisers, for instance, may include promotions, attracting customers, or selling products. The jobs-to-be-done approach has also been incorporated into the development of business models in the form of customer empathy maps and value proposition canvases covered.[20]

LINK TO LEARNING

Watch this video illustrating Christensen's jobs-to-be-done theory through a milkshake (https://openstax.org/l/52ChristenMilk) to learn more.

After you watch this video, think about how Christensen's definition of jobs relates to innovation. What are some jobs to be done for your entrepreneurial idea?

Disruptive innovations are contrasted with sustaining technologies, which improve the performance of established products through characteristics that mainstream customers adopt. Disruptive technologies allow for new entrants in the market, often with simpler, more affordable, more convenient products. Entrepreneurs and marketers have difficulty predicting or projecting how the emergence of an innovation will occur, and anticipating how customers will react to the new offerings. Predicting who the early adopters will be can also be difficult during the early stage of an innovation's emergence. The mainstream customer base initially fails to find value in the new product. New customer segments, however, see value in the new features and lower prices. Eventually, developments improve the new product's features to a level that will satisfy mainstream customers and thus attract more of the mainstream market.[21]

20 Clayton M. Christensen, Taddy Hall, Karen Dillon, and David S. Duncan. "Know Your Customers' 'Jobs to Be Done'." *Harvard Business Review*. September 2016. https://hbr.org/2016/09/know-your-customers-jobs-to-be-done

21 Christian Hopp, David Antons, Jermain Kaminski, and Torsten Oliver Salge. "What 40 Years of Research Reveals about the Difference between Disruptive and Radical Innovation." *Harvard Business Review*. April 9, 2018. https://hbr.org/2018/04/what-40-years-of-research-reveals-about-the-difference-between-disruptive-and-radical-innovation

WORK IT OUT

Ride Sharing

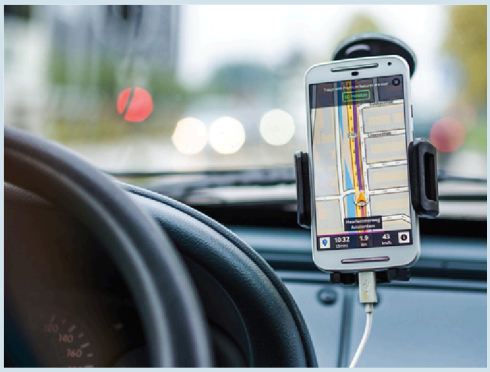


Figure 11.5 Uber and Lyft are popular ride-sharing services. (credit: "navigation car drive road gps" by "DariuszSankowski"/Pixabay, CC0)

Ride-sharing services disrupted the traditional taxicab business by providing a mobile platform that connected ride-seeking consumers with drivers willing to provide transportation. In rapidly becoming the market leader of ride-sharing services, Uber became the poster child for disruptive innovation. A customer using a ride-sharing service like Uber or Lyft no longer had to wave down a cab on the street, nor did she need cash in hand anymore through its mobile payment system within the app. An Uber ride usually costs less than a regular cab ride. Ride-sharing services also offer more versatility in choices and greater overall convenience. Now Uber continues to evolve its model, adding options like Uber Eats and Uber Copter.

- What are the jobs to be done that Uber addresses?
- What areas of a taxi cab's business model does Uber disrupt?

Christensen prefers the term *disruptive innovation* to *disruptive technology* because even in his original theoretical framework, technology was not the driving force disrupting existing markets, products, and models—rather, business models were.[22] The root of the tension in disruptive innovation is the conflict between the previously established business model for the incumbent technology and the new business model that may be necessary for exploiting the disruptive technology or process.

The efforts of incumbents to capitalize on a disruptive technology will fail in most instances because commercializing the new technology will require a different business model from the one that the incumbents currently use. When disruption occurs, incumbents struggle to commercialize, whereas new entrants take control through their mastery of the requisite new business models. Thus, a disruptive business model can fundamentally reshape profits within an industry because managers are faced with a technological disruption/innovation that alters their businesses, specifically their business models. This phenomenon is known as business model innovation.[23]

Business model innovation, as defined by Professor Constantinos Markides of the London Business School, occurs when an existing business fundamentally changes their business model.[24] In order to be an innovation, the "new business model must enlarge the existing economic pie, either by attracting new customers or by encouraging existing consumers to consume more." Disruptive innovations tend to require a business model that is not only different from but even in conflict with the traditional way of competing.[25] In contrast, radical innovations (see the preceding text) are new-to-the-world products that are disruptive to both consumers and producers.

22 C. M. Christensen. *The Innovator's Dilemma*. (Boston: Harvard Business School Press, 1997), 13.
23 C. M. Christensen and M. Raynor. *The Innovator's Solution*. Boston: Harvard Business School Press, 2003.

In the context of disruptive innovation, business model innovation is distinct from open business model innovation, which leverages external ideas together with internal ones. We also can define a business model innovation as a reformulation of an existing product or service, including a shift in how it is provided to the end user. A business model innovation "leads to a new way of playing the game" and can consist of new performance attributes on price or distribution outlets.[26] Stitch Fix uses data to offer personal styling at scale and ships customized clothing boxes from its own in-house label and from 1,000 brands in its collection directly to customers who want to avoid the hassles of in-store shopping. Despite volatility from investors, which dropped its initial $5.1 billion valuation at offering by two-thirds over three months, the company continues to reinvent the $334 billion US apparel industry.[27]

Value Proposition

Entrepreneurs play a key role in determining the value of their products. Of course, there are financial measures of value such as economic performance, job creation, wealth, and growth measures. But more often than not, value creation at the outset of a new startup venture lies outside these financial realms and addresses instead individual value to customers. The **value proposition** in a business model, for example, is a summary describing the benefits (value) customers can expect from a particular product or service. Your value proposition describes the benefits customers can expect from your products and services.[28] The value proposition is an integral part of the business model canvas, which we will discuss in Designing the Business Model.

ENTREPRENEUR IN ACTION

From Odeo to Twitter

Evan Williams and Biz Stone, both ex-Google employees, began a podcasting platform startup called Odeo around 2005. According to an early engineer in the company, Blaine Cooke, they built and tested Odeo but never used it. Shortly after co-founder Noah Glass created Odeo's podcasting platform, Apple announced plans to include a podcasting platform in all of its iPods. Faced with the reality that many of Odeo's fourteen employees weren't using the product they had built and the emergence of a giant competitor with a tremendous unfair advantage in Apple, Williams decided Odeo's future wouldn't be in podcasting.

The company held hackathons among employees and began searching for a pivot. One of those fourteen Odeo employees, Jack Dorsey, focused his efforts on the problem of status, the position of affairs at a particular time. In February 2006, Dorsey, Glass, and Florian Weber, a German contract developer, presented what they called Twttr, a system whereby a user could send a text message to a phone number, and it would be broadcast to the user's friends. A month later, Odeo had a working Twttr prototype, while obsessed employees were racking up hundreds of dollars in text messaging bills using the product. By the fall, Twitter (as it was now called) had thousands of users. Many began to see the product's utility after a San Francisco earthquake when it was heavily used to broadcast messages throughout the Bay Area.

- What type of innovation would you consider the original Odeo platform? Why?
- Why did Apple have an "unfair advantage" with its podcasting platform over competitors like Odeo?
- What value proposition did the early version of Twttr offer its users?

24 Constantinos Markides. "Disruptive Innovation: In Need of Better Theory." *Journal of Product Innovation Management* 23 (2006): 19–25.
25 Constantinos Markides. "Disruptive Innovation: In Need of Better Theory." *Journal of Product Innovation Management* 23 (2006): 19–25.
26 Constantinos D. Charitou and Constantinos C. Markides, "Responses to Disruptive Strategic Innovation." *MITSloan Management Review*. January 15, 2003. https://sloanreview.mit.edu/article/responses-to-disruptive-strategic-innovation/
27 Lauren Smiley. "Stitch Fix's radical data driven way to sell clothes- $1.2 billion last year—is reinventing retail." *Fast Company*. February 19, 2019. https://www.fastcompany.com/90298900/stitch-fix-most-innovative-companies-2019
28 Alexander Osterwalder, Yves Pigneur, Gregory Bernarda, and Alan Smith. *Value Proposition Design: How to Create Products and Services Customers Want*. Hoboken, NJ: Wiley, 2015.

11.2 Designing the Business Model

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Learning Objectives

By the end of this section, you will be able to:

- Define a business model and its purpose
- Describe a business model canvas
- Describe a lean model canvas
- Describe a social business model canvas

According to Alexander Osterwalder and Yves Pigneur, the authors of *Business Model Generation*, a business model "describes the rationale of how an organization creates, delivers and captures value." Nevertheless, there is no single definition of this term, and usage varies widely.[29]

In standard business usage, a **business model** is a plan for how venture will be funded; how the venture creates value for its stakeholders, including customers; how the venture's offerings are made and distributed to the end users; and the how income will be generated through this process. The business model refers more to the design of the business, whereas a business plan is a planning document used for operations.

Each business model is unique to the company it describes. A typical business model addresses the desirability, feasibility, and viability of a company, product, or service. At a bare minimum, a business model needs to address revenue streams (e.g., a revenue model), a value proposition, and customer segments. In non-jargon English, this means you want to address what your idea is, who will use it, why they will use it, and how you will make money off it.

A canvas is a display that would-be entrepreneurs commonly use to map out and plan different components of their business models. There are several different types of canvases, with the business model canvas and the lean canvas being the most commonly used. There are hard-copy canvases modeled after an art canvas as well as digital versions. The original physical canvases are meant to serve as visual tools, used with sticky notes and sketches.

As developed by Osterwalder and Pigneur, the **business model canvas** has nine components, as shown in Figure 11.6.

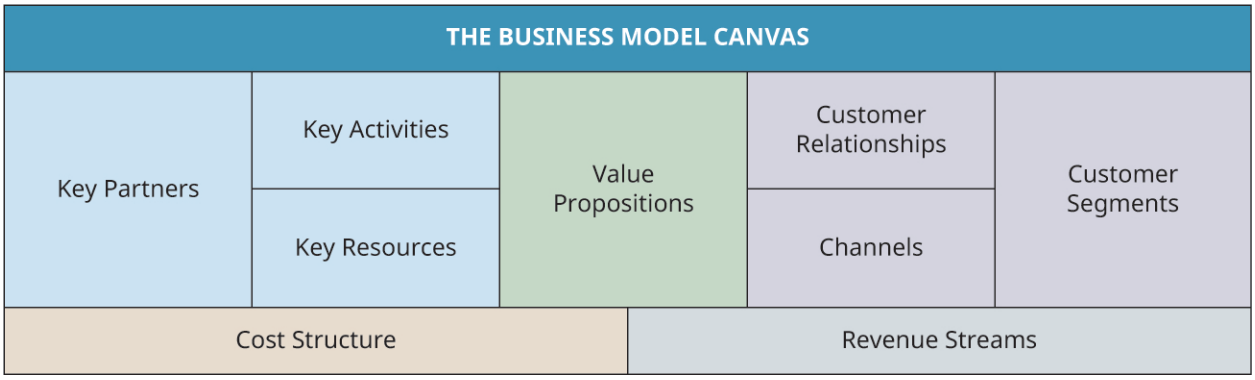


Figure 11.6 The business model canvas can be used to map or lay out the initial concept of your business. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

29 Alexander Osterwalder and Yves Pigneur. *Business Model Generation: A Handbook for Visionaries, Game Changers, and Challengers.* Hoboken, NJ: Wiley, 2010.

LINK TO LEARNING

Visit this site to see examples of completed Business Model Canvases for a variety of industries (https://openstax.org/l/52BMCsamples) for a deeper understanding of how the different categories are filled in.

Osterwalder and Pigneur wrote *Value Proposition Design* as a sequel to *Business Model Generation*. Their value proposition canvas is a plug-in that complements the business model canvas, going in depth on activities such as encouraging entrepreneurs to address and tackle customer pains, gains, and jobs-to-be-done trigger questions, and designing pain relievers and gains. The complementary and accompanying activities and resources can be useful for a deeper dive into and understanding of customer value creation in the form of value proposition, although there are other approaches to conceptualizing your value proposition. For Christensen, the originator of the disruptive innovation and jobs-to-be-done theories, a value proposition is a product that helps customers do a job they've been trying to do more effectively, conveniently, and affordably.

Finding the intersection of your customers' problems and your solutions is how you create a unique value proposition, according to the entrepreneur Ash Maurya, the author of *Scaling Lean* and *Running Lean*. In *Running Lean*, Maurya offers the following formula for creating an initial value proposition in the canvas, as shown in Figure 11.7.

Figure 11.7 Maurya's formula to determine value proposition considers customer needs and potential objections within a specific period of time. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Maurya deviated from the standard business model canvas to create the lean canvas. It overlaps the business model canvas in five of the nine components: customer segments, value proposition, revenue streams, channels, and cost structure (Figure 11.8]. Rather than addressing key partners, key activities, and key resources, the lean canvas helps you tackle problems, solutions, and key metrics instead.

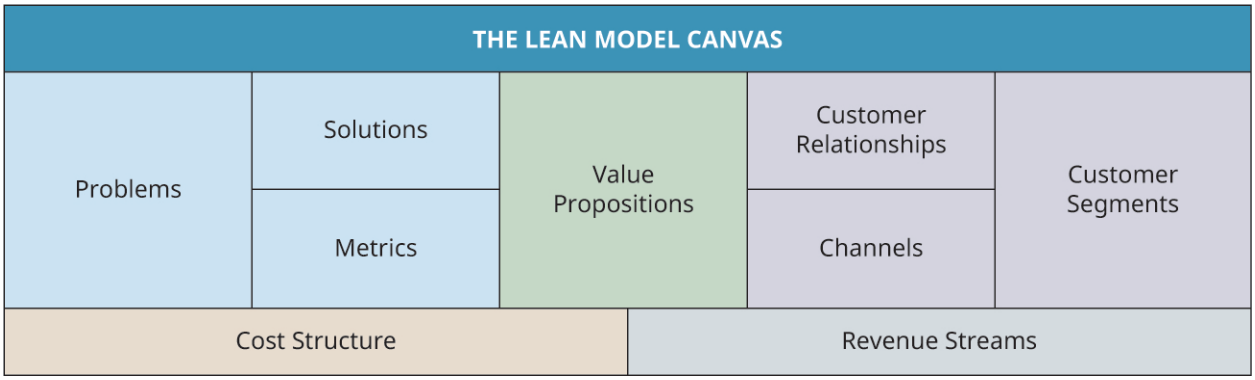


Figure 11.8 The lean model canvas is a modification of the Business Model Canvas. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

LINK TO LEARNING

Visit this site to see examples of completed Lean Model Canvases from some major companies

(https://openstax.org/l/52LMCsamples) for a deeper understanding of how the canvas can be applied.

While the business model canvas and the lean canvas are similar in format, there are differences in how they are used. It is generally accepted that the lean canvas model is a better fit for startups, whereas the business model canvas works well for already established businesses. The lean canvas is simpler; the business model canvas provides a more complete picture of a mature business.

LINK TO LEARNING

Watch this Railsware video that demonstrates how the lean canvas model might be applied to startups (https://openstax.org/l/52LeanCanvUb) to learn more. In the case example in the video, the lean canvas model is applied to the successful P2P ride-sharing app Uber, as if it were a startup.

Both the business model canvas and the lean canvas are designed for constant iterations, allowing for multiple versions and changes throughout the entrepreneurial process. Part of that process involves customer discovery; thus, the canvases invoke customer-focused design. The target customer is integrated into the canvas from the start through the use of a customer empathy map and a number of design-thinking ideation activities.[30] The **customer empathy map** is a portrayal of a target customer—the most promising candidate from a business's customer segments—that explores the understanding of that person's problems and needs (Figure 11.9). Osterwalder and Pigneur used a customer empathy map as part of the design ideation phase of developing a business model canvas. There are differing versions of customer empathy maps, but most seek to answer common questions pertaining to the customer, such as:

- With whom are we empathizing?
- What do they need to do?
- What do they see?
- What do they say?
- What do they do?
- What do they hear?
- What do they think?

Phillips, Proctor & Gamble, Microsoft, and Yeti are examples of well-known companies that make use of customer empathy mapping because, according to the journal *Entrepreneur*, every transaction can be turned into a meaningful and valuable customer interaction.[31] Once a company analyzes the results of customer mapping exercises, it may very well lead to new products that serve customer needs and/or wants.

For example, Philips used empathy mapping to detect a high level of fear in young patients immediately before an MRI medical procedure, so it invented a miniature version of the CAT scan equipment used in the procedure called the "kitten scanner" along with toy animal characters that were used to dispel the fear of MRIs among children. Proctor & Gamble created a new advertisement that was released for the 2012 Olympics visualizing the trials and tribulations of mothers raising young athletes, demonstrating Proctor and Gamble's awareness that some of its customers wanted or needed empathy for the sacrifices they had made to help their children succeed. Likewise, Microsoft has attempted to demonstrate empathy with customers' privacy concerns by developing an interactive website that explains not only how data is stolen but also how we can better protect our own data.[32]

30 Charlene Perrin. "Create A Customer Empathy Map in 6 Easy Steps!" *Conceptboard*. March 28, 2019. https://conceptboard.com/blog/create-a-customer-empathy-map-in-6-easy-steps/
31 Vineet Arya. "How to Infuse Empathy in Your Marketing?" *Entrepreneur*. June 28, 2019. https://www.entrepreneur.com/article/335987
32 Vineet Arya. "How to Infuse Empathy in Your Marketing?" *Entrepreneur*. June 28, 2019. https://www.entrepreneur.com/article/

On their company website, the now-famous Yeti cooler company publicly extols the value of empathy mapping, explaining that it leads to better products. Yeti doesn't just create one on its own, it actually asks its clients to work with the company to create an empathy map.[33] Thus, empathy mapping for Yeti is part of its product development process.

Customer empathy maps also strive to address customer pains (in this case, fears, frustrations, and anxieties) and gains (wants, needs, hopes, and dreams).[34]

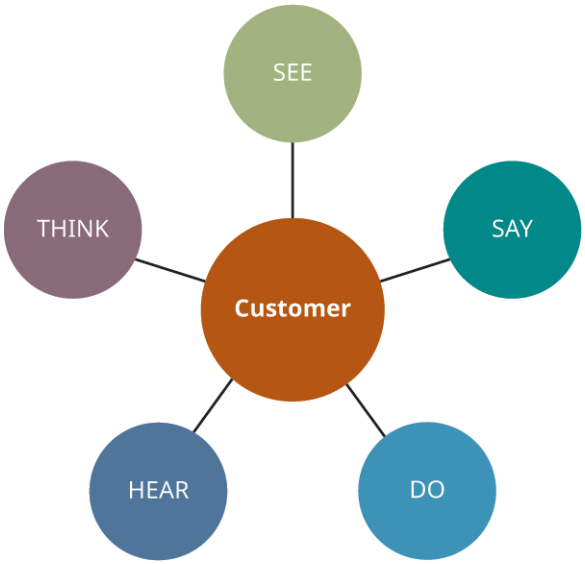


Figure 11.9 An empathy map portrays the target customer in order to understand the market needs. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

LINK TO LEARNING

Strategyzer offers six videos outlining the business model canvas (https://openstax.org/l/52BMCvideos) that total about 12 minutes; specifically they cover the prototyping journey from ideation to visualization of conceptualization.

Business Model Canvas[35]

As Osterwalder and Pigneur describe it, according to *Media Innovation and Entrepreneurship*, their business model canvas blocks include revenue streams, customer segments, value propositions, cost structures, channels, key activities, key partners, key resources, and customer relationships.

Early on, your greatest focus should be on the right side of the canvas because:

- These are, in many ways, the most critical aspects of starting a new venture (customer segments, value propositions, channels, and revenue streams).
- The most fluid (revenue streams, channels, and value propositions will likely differ for the differing customer segments and, as you iterate and adapt throughout the customer discovery process, could likely change).
- These follow a logical temporal order (there's no need to focus on the costs of building a company if you

335987

33 Mike Godlewski. "The Secret to Knowing What a Client Is Thinking? Empathy Maps." Yeti. February 8, 2016. https://yeti.co/blog/the-secret-to-knowing-what-your-client-is-thinking-empathy-maps/

34 Germán Coppola. "What Is an Empathy Map, and Why Is It Valuable for Your Business?" *Medium*. November 28, 2017. https://medium.com/swlh/what-is-an-empathy-map-and-why-is-it-valuable-for-your-business-14236be4fdf4

35 This material is based on original work by Geoffrey Graybeal and produced with support from the Rebus Community. The original is freely available under the terms of the CC BY 4.0 license at https://press.rebus.community/media-innovation-and-entrepreneurship/.

won't have customers).

In a follow-up to business model generation, the Strategyzer team created a second canvas, the value proposition canvas: https://www.strategyzer.com/canvas/value-proposition-canvas. The value proposition canvas is a new tool that pulls out the customer segment and value proposition blocks of the business model canvas, and encourages more in-depth exploration of those blocks to achieve a good fit between the two. The value proposition canvas tool looks at customer pains, gains and jobs to be done on the customer side and painkillers, gain creators, and products and services on the value proposition side.[36]

LINK TO LEARNING

Read this blog that provides a walk-through of how to fill in a value proposition canvas (https://openstax.org/l/52VPfillin) to learn more.

When you peel away the language used to describe business models, the early startup planning stages come down to a series of questions. When it comes to formulating a business model for a startup concept, another popular framework used in entrepreneurial circles is that of desirability-feasibility-viability Figure 11.10). This framework forces the entrepreneur to address broad questions about the startup concept:

- Desirability: How desirable is the product? Who will use it and why?
- Feasibility: How feasible is this idea? What are the costs of making it? How practical is the concept?
- Viability: Will this idea remain viable? How will it make money? How will it be sustained over time?

These questions then begin to connect to form a narrative about where the startup concept came from, whom it serves, why it's needed, how it will make money, and how it will be sustained in the future.

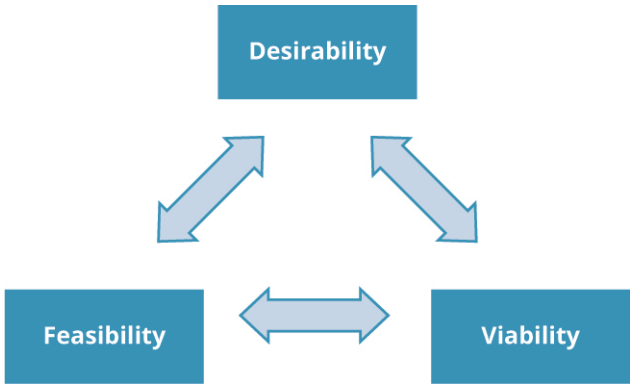


Figure 11.10 The framework of desirability, feasibility, and viability form a story about a company's startup. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The value propositions, customer relationships, customer segments, and channels address the assumptions that will create customer value (desirability). The cost structure and revenue stream blocks are aimed at viability, or overcoming flawed business models. The key partners, key activities, and key resources are about execution and address feasibility. The risk of poor execution can undermine your assumptions that you chose the right infrastructure to execute your business model (feasibility). The risk of solving an irrelevant customer job (sometimes derisively labeled "a solution in search of a problem") undercuts desirability in your business. The risk of a flawed business model would hamper the financial assumption that your business will earn more money than you spend (viability). Adaptability is about the assumption that you chose the right business model within the context of external factors such as technology change, competition, and regulation.

36 Michelle Ferrier and Elizabeth Mays. *Media Innovation and Entrepreneurship*. The Rebus Foundation, 2017. https://press.rebus.community/media-innovation-and-entrepreneurship/.

The business model canvas is not an exhaustive planning tool by any means.[37],[38] The risk of such external threats is not specifically addressed on the canvas blocks. The external threats not specifically covered by the canvas blocks can be designed for adaptability, that is, the business model canvas is a necessary but insufficient component of determining the viability of the business idea/concept. There are many elements not included in the canvas that entrepreneurs must address. Industry analysis, including a competitive analysis, for example, falls "off canvas" but is important nonetheless.

The Lean Model Canvas

The **lean model canvas** is Ash Maurya's adaptation of the original business model canvas. As we noted earlier, gone are the customer relationships, key activities, key partners, and key resources blocks. Instead, a problem block is added, because as Maurya explains, "Most startups fail, not because they fail to build what they set out to build, but because they waste time, money and effort building the wrong product. I attribute a significant contributor to this failure to a lack of proper 'problem understanding' from the start." Maurya next added a solution block to the lean model canvas, which corresponds well with features on a minimum viable product (MVP), which you will recall was covered in depth in Launch for Growth to Success. The lean model canvas also adds an "Unfair Advantage" block, similar to the block for competitive advantages or barriers to entry found in a business plan.[39]

Social Business Model Canvas

As you've noticed by now, the core canvas components are common throughout the various versions. Many of the blocks of the **social business model canvas** are similar to those used in the business model canvas and the lean model canvas.[40] A few differences, as developed by Tandemic, focus on areas unique to social entrepreneurship ventures. For example, the new areas added include measures of what kind of social impact you are creating or developing, measures of surplus to address what happens with profits and where you intend to reinvest them, and measures of beneficiary segments, and social and customer value propositions.[41] These could be measures such as the number of trees planted, number of refugees housed and fed, jobs created, or investments made—depending on the venture. Social impact looks at an organization's social mission beyond the bottom line. Measurement can differ among social entrepreneurs, but in terms of the canvas, impact measures are an effort to establish quantifiable metrics.

Social impact can be hard to measure, but nonetheless, many social entrepreneurs aim for long-lasting impact.[42] A 2014 report by the think tank, consultancy, and member network SustainAbility lists cooperative ownership, inclusive sourcing, and the "buy one, give one" model as three forms of social impact.[43] In addition to the Tandemic social business model canvas, there are other versions of similar canvases used for social entrepreneurship. For instance, Osterwalder adapted the business model canvas for mission-driven organizations into a mission model canvas.[44] There's also a social lean canvas that adds purpose (explaining your reason for creating the venture in terms of social or environmental problems) and impact sections (describing the intended social or environmental impact).[45]

37 Jennifer van der Meer. "Do You Suffer from Value Proposition Confusion?" *Linkedin*. October 19, 2016. https://www.linkedin.com/pulse/do-you-suffer-from-value-proposition-confusion-jennifer-van-der-meer/
38 "The Value Proposition Canvas." *Strategyzer*. n.d. https://strategyzer.com/canvas/value-proposition-canvas
39 Ash Maurya. "Why Lean Canvas vs Business Model Canvas?" *Medium*. February 27, 2012. https://blog.leanstack.com/why-lean-canvas-vs-business-model-canvas-af62c0f250f0
40 "Social Business Model Canvas." *Business Model Toolbox*. 2013. https://bmtoolbox.net/tools/social-business-model-canvas/
41 "The Business Model Canvas Reinvented for Social Business." *Tandemic*. n.d. http://www.socialbusinessmodelcanvas.com
42 Ayse Guclu, J. Gregory Dees, and Beth Battle Anderson. "The Process of Social Entrepreneurship: Creating Opportunities Worthy of Serious Pursuit." *Duke/Fuqua case*. 2002. https://centers.fuqua.duke.edu/case/knowledge_items/the-process-of-social-entrepreneurship-creating-opportunities-worthy-of-serious-pursuit/
43 Lindsay Clinton and Ryan Whisnant. "Model Behavior: 20 Business Model Innovations for Sustainability." *SustainAbility*. February 2014. https://sustainability.com/wp-content/uploads/2016/07/model_behavior_20_business_model_innovations_for_sustainability.pdf
44 Alexander Osterwalder. "The Mission Model Canvas: An Adapted Business Model Canvas for Mission-Driven Organizations." *Strategyzer*. February 25, 2016. https://blog.strategyzer.com/posts/2016/2/24/the-mission-model-canvas-an-adapted-business-model-canvas-for-mission-driven-organizations
45 Social Lean Canvas. n.d. https://socialleancanvas.com/

LINK TO LEARNING

This completed social business model canvas for the popular peer-to-peer lending platform Kiva (https://openstax.org/l/52SocialBMC) illustrates how the business model canvas can and perhaps should be adapted for social entrepreneurship ventures.

WHAT CAN YOU DO?

TOMS Shoes

Toms Shoes is perhaps one of the best-known companies for adopting a social entrepreneurship purpose into its business model. Part of its early success hinged on the fact that for every pair of shoes a customer bought, the company donated a pair of shoes to someone in need. The company won a prize in 2006 for its innovative solution to poverty. This "1-for-1 business model," sometimes commonly called the "Toms model" after the shoe company that popularized it, gained traction among other companies that followed suit in similar fashion, seeing both the social and the financial successes in the Toms model. Warby Parker is another example of a company that does essentially the same: A customer purchases a pair of eyeglasses, and the company donates a pair (although Warby Parker pays a third party to procure the glasses, as eyeglasses require an individual prescription, whereas shoes do not).

- Can you think of an innovative social entrepreneurship business model?

WHAT CAN YOU DO?

The Birthday Party Project

Figure 11.11 The Birthday Party Project helps provide celebrations to honor the birthdays of homeless children. (credit: modification of "children's birthday table" by "Efraimstochter"/Pixabay, CC0)

Paige Chenault wanted homeless children in Dallas to feel special on their birthdays. Many have never experienced a birthday party. So this professional event planner sprang into action in January 2012. She launched the Birthday Party Project (https://www.thebirthdaypartyproject.org/), a nonprofit group whose mission is to celebrate the lives of homeless children (ages one to twenty-two). The group organizes monthly birthday parties with partner shelters. Since its inception, the concept has spread beyond Texas to cities across the United States, including Atlanta, Chicago, Los Angeles, New York, and San Francisco. In six

years, the Birthday Party Project has celebrated 4,800 birthdays with 30,000 kids in attendance, eaten 40,000 cupcakes, cracked 30,000 glow sticks, and performed 1,100 renditions of "Happy Birthday."

- Identify a need in your community that could become a social entrepreneurship business, as Paige discovered with an initial passion project.

11.3 Conducting a Feasibility Analysis

Learning Objectives

By the end of this section, you will be able to:

- Describe the purpose of a feasibility analysis
- Describe and develop the parts of a feasibility analysis
- Understand how to apply feasibility outcomes to a new venture

As the name suggests, a **feasibility analysis** is designed to assess whether your entrepreneurial endeavor is, in fact, feasible or possible. By evaluating your management team, assessing the market for your concept, estimating financial viability, and identifying potential pitfalls, you can make an informed choice about the achievability of your entrepreneurial endeavor. A feasibility analysis is largely numbers driven and can be far more in depth than a business plan (discussed in The Business Plan). It ultimately tests the viability of an idea, a project, or a new business. A feasibility study may become the basis for the business plan, which outlines the action steps necessary to take a proposal from ideation to realization. A feasibility study allows a business to address where and how it will operate, its competition, possible hurdles, and the funding needed to begin. The business plan then provides a framework that sets out a map for following through and executing on the entrepreneurial vision.

Organizational Feasibility Analysis

Organizational feasibility aims to assess the prowess of management and sufficiency of resources to bring a product or idea to market Figure 11.12. The company should evaluate the ability of its management team on areas of interest and execution. Typical measures of management prowess include assessing the founders' passion for the business idea along with industry expertise, educational background, and professional experience. Founders should be honest in their self-assessment of ranking these areas.

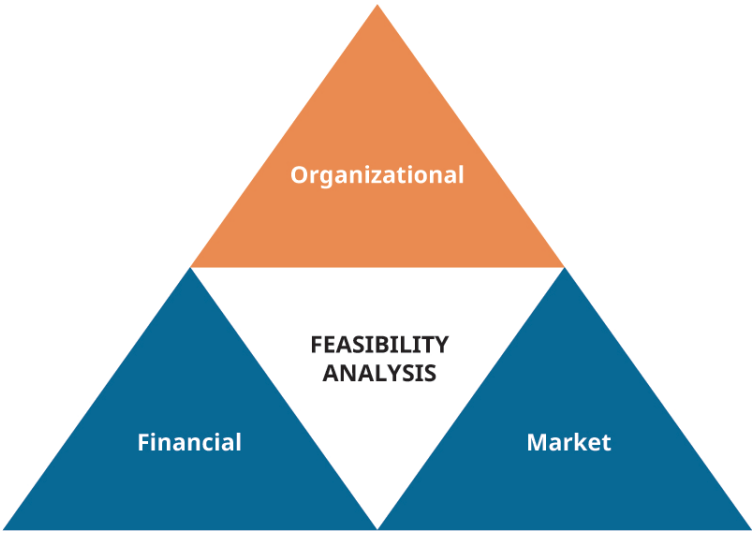


Figure 11.12 An analysis of organizational feasibility focuses on resource needs and management capabilities. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Resource sufficiency pertains to nonfinancial resources that the venture will need to move forward successfully and aims to assess whether an entrepreneur has a sufficient amount of such resources. The organization should critically rank its abilities in six to twelve types of such critical nonfinancial resources, such as availability of office space, quality of the labor pool, possibility of obtaining intellectual property protections (if applicable), willingness of high-quality employees to join the company, and likelihood of forming favorable strategic partnerships. If the analysis reveals that critical resources are lacking, the venture may not be possible as currently planned.[46]

Financial Feasibility Analysis

A **financial analysis** seeks to project revenue and expenses (forecasts come later in the full business plan); project a financial narrative; and estimate project costs, valuations, and cash flow projections Figure 11.13.

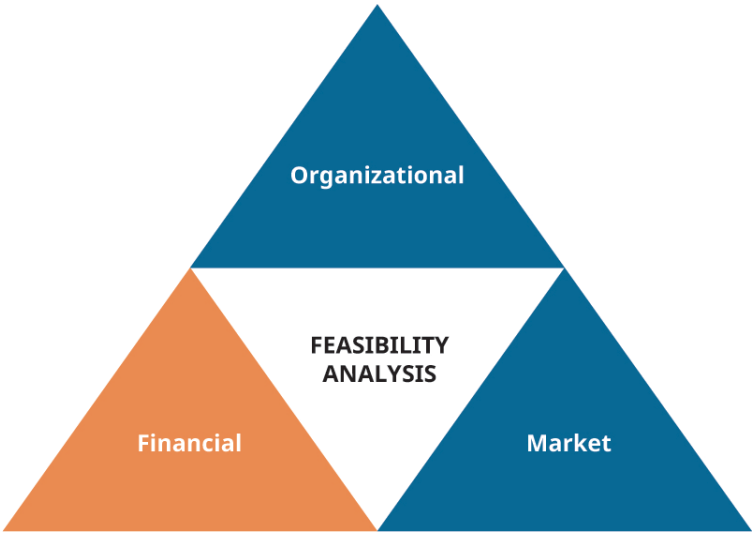


Figure 11.13 An analysis of financial feasibility focuses on expenses, cash flow, and projected revenue. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The financial analysis may typically include these items:

- A twelve-month profit and loss projection
- A three- or four-year profit-and-loss projection
- A cash-flow projection
- A projected balance sheet
- A breakeven calculation

The financial analysis should estimate the sales or revenue that you expect the business to generate. A number of different formulas and methods are available for calculating sales estimates. You can use industry or association data to estimate the sales of your potential new business. You can search for similar businesses in similar locations to gauge how your business might perform compared with similar performances by competitors. One commonly used equation for a sales model multiplies the number of target customers by the average revenue per customer to establish a sales projection:

$$T \times A = S$$
$$\text{Target(ed) Customers/Users} \times \text{Average Revenue per Customer} = \text{Sales Projection}$$

46 Ulrich Kaiser. "A primer in Entrepreneurship – Chapter 3 Feasibility analysis" *University of Zurich Institute for Strategy and Business Economics*. n.d. https://docplayer.net/7775267-A-primer-in-entrepreneurship-chapter-3-feasibility-analysis.html

Another critical part of planning for new business owners is to understand the **breakeven point**, which is the level of operations that results in exactly enough revenue to cover costs (see Entrepreneurial Finance and Accounting for an in-depth discussion on calculating breakeven points and the breakdown of cost types). It yields neither a profit nor a loss. To calculate the breakeven point, you must first understand the two types of costs: fixed and variable. **Fixed costs** are expenses that do not vary based on the amount of sales. Rent is one example, but most of a business's other costs operate in this manner as well. While some costs vary from month to month, costs are described as variable only if they will increase if the company sells even one more item. Costs such as insurance, wages, and office supplies are typically considered fixed costs. **Variable costs** fluctuate with the level of sales revenue and include items such as raw materials, purchases to be sold, and direct labor. With this information, you can calculate your breakeven point—the sales level at which your business has neither a profit nor a loss.[47] Projections should be more than just numbers: include an explanation of the underlying assumptions used to estimate the venture's income and expenses.

Projected cash flow outlines preliminary expenses, operating expenses, and reserves—in essence, how much you need before starting your company. You want to determine when you expect to receive cash and when you have to write a check for expenses. Your cash flow is designed to show if your working capital is adequate. A **balance sheet** shows assets and liabilities, necessary for reporting and financial management. When liabilities are subtracted from assets, the remainder is owners' equity. The financial concepts and statements introduced here are discussed fully in Entrepreneurial Finance and Accounting.

Market Feasibility Analysis

A **market analysis** enables you to define competitors and quantify target customers and/or users in the market within your chosen industry by analyzing the overall interest in the product or service within the industry by its target market Figure 11.14. You can define a market in terms of size, structure, growth prospects, trends, and sales potential. This information allows you to better position your company in competing for market share. After you've determined the overall size of the market, you can define your target market, which leads to a **total available market (TAM)**, that is, the number of potential users within your business's sphere of influence. This market can be segmented by geography, customer attributes, or product-oriented segments. From the TAM, you can further distill the portion of that target market that will be attracted to your business. This market segment is known as a **serviceable available market (SAM)**.

Figure 11.14 An analysis of market feasibility examines the overall market and focuses on the anticipated share of the target market. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Projecting market share can be a subjective estimate, based not only on an analysis of the market but also on

47 In a preliminary financial model and business plan, startup costs should be allocated, as they are intended for one-time investments in development; pre-launch costs and other necessary expenses will not carry over once the product/solution has launched.

pricing, promotional, and distribution strategies. As is the case for revenue, you will have a number of different forecasts and tools available at your disposal. Other items you may include in a market analysis are a complete competitive review, historical market performance, changes to supply and demand, and projected growth in demand over time.

ARE YOU READY?

Market Feasibility Analysis

You've been hired by a leading hotel chain to determine the market and financial potential for the development of a mixed-use property that will include a full-service hotel in downtown Orlando, located at 425 East Central Boulevard, in Orlando, Florida. The specific address is important so you can pinpoint existing competitors and overall suitability of the site. Using the information given, conduct a market analysis that can be part of a larger feasibility study.

WORK IT OUT

Location Feasibility

Figure 11.15 If you wanted to open a business in downtown Atlanta, you would need to research the feasibility of operating a location there. (credit: "Atlanta,Georgia,downtown skyline,dusk" by "tableatny"/Flickr, CC BY 2.0)

You're considering opening a boutique clothing store in downtown Atlanta. You've read news reports about how downtown Atlanta and the city itself are growing and undergoing changes from previous decades. With new development taking place there, you're not sure whether such a venture is viable. Outline what steps you would need to take to conduct a feasibility study to determine whether downtown Atlanta is the right location for your planned clothing store.

Applying Feasibility Outcomes

After conducting a feasibility analysis, you must determine whether to proceed with the venture. One technique that is commonly used in project management is known as a **go-or-no-go decision**. This tool allows a team to decide if criteria have been met to move forward on a project. Criteria on which to base a decision are established and tracked over time. You can develop criteria for each section of the feasibility analysis to determine whether to proceed and evaluate those criteria as either "go" or "no go," using that assessment to make a final determination of the overall concept feasibility. Determine whether you are comfortable proceeding with the present management team, whether you can "go" forward with existing nonfinancial

resources, whether the projected financial outlook is worth proceeding, and make a determination on the market and industry. If satisfied that enough "go" criteria are met, you would likely then proceed to developing your strategy in the form of a business plan.

WHAT CAN YOU DO?

Love Beyond Walls

When Terence Lester saw a homeless man living behind an abandoned, dilapidated building, he asked the man if he could take him to a shelter. The man scoffed, replying that Lester should sleep in a shelter. So he did—and he saw the problem through the homeless man's perspective. The shelter was crowded and smelly. You couldn't get much sleep, because others would try to steal your meager belongings. The dilapidated building provided isolation away from others, but quiet and security in its own way that the shelter could not. This experience led Lester to voluntarily live as a homeless person for a few weeks. His journey led him to create Love Beyond Walls (www.lovebeyondwalls.org), an organization that aids the homeless, among other causes. Lester didn't conduct a formal feasibility study, but he did so informally by walking in his intended customers' shoes—literally. A feasibility study of homelessness in a particular area could yield surprising findings that might lead to social entrepreneurial pursuits.

- What is a social cause you think could benefit from a formal feasibility study around a potential entrepreneurial solution?

11.4 The Business Plan

Learning Objectives

By the end of this section, you will be able to:

- Describe the different purposes of a business plan
- Describe and develop the components of a brief business plan
- Describe and develop the components of a full business plan

Unlike the brief or lean formats introduced so far, the **business plan** is a formal document used for the long-range planning of a company's operation. It typically includes background information, financial information, and a summary of the business. Investors nearly always request a formal business plan because it is an integral part of their evaluation of whether to invest in a company. Although nothing in business is permanent, a business plan typically has components that are more "set in stone" than a business model canvas, which is more commonly used as a first step in the planning process and throughout the early stages of a nascent business. A business plan is likely to describe the business and industry, market strategies, sales potential, and competitive analysis, as well as the company's long-term goals and objectives. An in-depth formal business plan would follow at later stages after various iterations to business model canvases. The business plan usually projects financial data over a three-year period and is typically required by banks or other investors to secure funding. The business plan is a roadmap for the company to follow over multiple years.

Some entrepreneurs prefer to use the canvas process instead of the business plan, whereas others use a shorter version of the business plan, submitting it to investors after several iterations. There are also entrepreneurs who use the business plan earlier in the entrepreneurial process, either preceding or concurrently with a canvas. For instance, Chris Guillebeau has a one-page business plan template in his book *The $100 Startup*.[48] His version is basically an extension of a napkin sketch without the detail of a full business plan. As you progress, you can also consider a brief business plan (about two pages)—if you want to support a rapid business launch—and/or a standard business plan.

48 Chris Guillebeau. *The $100 Startup: Reinvent the Way You Make a Living, Do What You Love, and Create a New Future*. New York:

As with many aspects of entrepreneurship, there are no clear hard and fast rules to achieving entrepreneurial success. You may encounter different people who want different things (canvas, summary, full business plan), and you also have flexibility in following whatever tool works best for you. Like the canvas, the various versions of the business plan are tools that will aid you in your entrepreneurial endeavor.

Business Plan Overview

Most business plans have several distinct sections (Figure 11.16). The business plan can range from a few pages to twenty-five pages or more, depending on the purpose and the intended audience. For our discussion, we'll describe a brief business plan and a standard business plan. If you are able to successfully design a business model canvas, then you will have the structure for developing a clear business plan that you can submit for financial consideration.

BUSINESS PLAN	
√	Executive Summary
√	Business Description
√	Market Strategies
√	Marketing Plan
√	Competitive Analysis
√	Operations and Management Plan
√	Financial Analysis
√	Design and Development Plan

Figure 11.16 Most business plans include the same important sections. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Both types of business plans aim at providing a picture and roadmap to follow from conception to creation. If you opt for the brief business plan, you will focus primarily on articulating a big-picture overview of your business concept.

The full business plan is aimed at executing the vision concept, dealing with the proverbial devil in the details. Developing a full business plan will assist those of you who need a more detailed and structured roadmap, or those of you with little to no background in business. The business planning process includes the business model, a feasibility analysis, and a full business plan, which we will discuss later in this section. Next, we explore how a business plan can meet several different needs.

Purposes of a Business Plan

A business plan can serve many different purposes—some internal, others external. As we discussed previously, you can use a business plan as an internal early planning device, an extension of a napkin sketch, and as a follow-up to one of the canvas tools. A business plan can be an organizational roadmap, that is, an internal planning tool and working plan that you can apply to your business in order to reach your desired goals over the course of several years. The business plan should be written by the owners of the venture, since it forces a firsthand examination of the business operations and allows them to focus on areas that need improvement.

Refer to the business venture throughout the document. Generally speaking, a business plan should not be written in the first person.

A major external purpose for the business plan is as an investment tool that outlines financial projections, becoming a document designed to attract investors. In many instances, a business plan can complement a formal investor's pitch. In this context, the business plan is a presentation plan, intended for an outside audience that may or may not be familiar with your industry, your business, and your competitors.

Crown Business/Random House, 2012.

You can also use your business plan as a contingency plan by outlining some "what-if" scenarios and exploring how you might respond if these scenarios unfold. Pretty Young Professional launched in November 2010 as an online resource to guide an emerging generation of female leaders. The site focused on recent female college graduates and current students searching for professional roles and those in their first professional roles. It was founded by four friends who were coworkers at the global consultancy firm McKinsey. But after positions and equity were decided among them, fundamental differences of opinion about the direction of the business emerged between two factions, according to the cofounder and former CEO Kathryn Minshew. "I think, naively, we assumed that if we kicked the can down the road on some of those things, we'd be able to sort them out," Minshew said. Minshew went on to found a different professional site, The Muse, and took much of the editorial team of Pretty Young Professional with her.[49] Whereas greater planning potentially could have prevented the early demise of Pretty Young Professional, a change in planning led to overnight success for Joshua Esnard and The Cut Buddy team. Esnard invented and patented the plastic hair template that he was selling online out of his Fort Lauderdale garage while working a full-time job at Broward College and running a side business. Esnard had hundreds of boxes of Cut Buddies sitting in his home when he changed his marketing plan to enlist companies specializing in making videos go viral. It worked so well that a promotional video for the product garnered 8 million views in hours. The Cut Buddy sold over 4,000 products in a few hours when Esnard only had hundreds remaining. Demand greatly exceeded his supply, so Esnard had to scramble to increase manufacturing and offered customers two-for-one deals to make up for delays. This led to selling 55,000 units, generating $700,000 in sales in 2017.[50] After appearing on *Shark Tank* and landing a deal with Daymond John that gave the "shark" a 20-percent equity stake in return for $300,000, The Cut Buddy has added new distribution channels to include retail sales along with online commerce. Changing one aspect of a business plan—the marketing plan—yielded success for The Cut Buddy.

LINK TO LEARNING

Watch this video of Cut Buddy's founder, Joshua Esnard, telling his company's story (https://openstax.org/l/52CutBuddy) to learn more.

If you opt for the brief business plan, you will focus primarily on articulating a big-picture overview of your business concept. This version is used to interest potential investors, employees, and other stakeholders, and will include a financial summary "box," but it must have a disclaimer, and the founder/entrepreneur may need to have the people who receive it sign a nondisclosure agreement (NDA). The full business plan is aimed at executing the vision concept, providing supporting details, and would be required by financial institutions and others as they formally become stakeholders in the venture. Both are aimed at providing a picture and roadmap to go from conception to creation.

Types of Business Plans

The brief business plan is similar to an extended executive summary from the full business plan. This concise document provides a broad overview of your entrepreneurial concept, your team members, how and why you will execute on your plans, and why you are the ones to do so. You can think of a brief business plan as a scene setter or—since we began this chapter with a film reference—as a trailer to the full movie. The brief business plan is the commercial equivalent to a trailer for *Field of Dreams*, whereas the full plan is the full-length movie equivalent.

49 Jonathan Chan. "What These 4 Startup Case Studies Can Teach You about Failure." *Foundr.com.* July 12, 2015. https://foundr.com/4-startup-case-studies-failure/

50 Amy Feldman. "Inventor of the Cut Buddy Paid YouTubers to Spark Sales. He Wasn't Ready for a Video to Go Viral." *Forbes.* February 15, 2017. https://www.forbes.com/sites/forbestreptalks/2017/02/15/inventor-of-the-cut-buddy-paid-youtubers-to-spark-sales-he-wasnt-ready-for-a-video-to-go-viral/#3eb540ce798a

Brief Business Plan or Executive Summary

As the name implies, the **brief business plan** or **executive summary** summarizes key elements of the entire business plan, such as the business concept, financial features, and current business position. The executive summary version of the business plan is your opportunity to broadly articulate the overall concept and vision of the company for yourself, for prospective investors, and for current and future employees.

A typical executive summary is generally no longer than a page, but because the brief business plan is essentially an extended executive summary, the executive summary section is vital. This is the "ask" to an investor. You should begin by clearly stating what you are asking for in the summary.

In the business concept phase, you'll describe the business, its product, and its markets. Describe the customer segment it serves and why your company will hold a competitive advantage. This section may align roughly with the customer segments and value-proposition segments of a canvas.

Next, highlight the important financial features, including sales, profits, cash flows, and return on investment. Like the financial portion of a feasibility analysis, the financial analysis component of a business plan may typically include items like a twelve-month profit and loss projection, a three- or four-year profit and loss projection, a cash-flow projection, a projected balance sheet, and a breakeven calculation. You can explore a feasibility study and financial projections in more depth in the formal business plan. Here, you want to focus on the big picture of your numbers and what they mean.

The current business position section can furnish relevant information about you and your team members and the company at large. This is your opportunity to tell the story of how you formed the company, to describe its legal status (form of operation), and to list the principal players. In one part of the extended executive summary, you can cover your reasons for starting the business: Here is an opportunity to clearly define the needs you think you can meet and perhaps get into the pains and gains of customers. You also can provide a summary of the overall strategic direction in which you intend to take the company. Describe the company's mission, vision, goals and objectives, overall business model, and value proposition.

Rice University's Student Business Plan Competition, one of the largest and overall best-regarded graduate school business-plan competitions (see Telling Your Entrepreneurial Story and Pitching the Idea), requires an executive summary of up to five pages to apply.[51],[52] Its suggested sections are shown in Table 11.2.

Suggested Executive Summary Components for Rice University Business Plan Competition[53]

Section	Description
Company summary	Brief overview (one to two paragraphs) of the problem, solution, and potential customers
Customer analysis	Description of potential customers and evidence they would purchase product
Market analysis	Size of market, target market, and share of market
Product or service	Current state of product in development and evidence it is feasible

Table 11.2

51 Jennifer Post. "National Business Plan Competitions for Entrepreneurs." *Business News Daily*. August 30, 2018. https://www.businessnewsdaily.com/6902-business-plan-competitions-entrepreneurs.html
52 "Rice Business Plan Competition, Eligibility Criteria and How to Apply." *Rice Business Plan Competition*. March 2020. https://rbpc.rice.edu/sites/g/files/bxs806/f/2020%20RBPC%20Eligibility%20Criteria%20and%20How%20to%20Apply_23Oct19.pdf

Section	Description
Intellectual property	If applicable, information on patents, licenses, or other IP items
Competitive differentiation	Describe the competition and your competitive advantage
Company founders, management team, and/or advisor	Bios of key people showcasing their expertise and relevant experience
Financials	Projections of revenue, profit, and cash flow for three to five years
Amount of investment	Funding request and how funds will be used

Table 11.2

ARE YOU READY?

Create a Brief Business Plan

Fill out a canvas of your choosing for a well-known startup: Uber, Netflix, Dropbox, Etsy, Airbnb, Bird/Lime, Warby Parker, or any of the companies featured throughout this chapter or one of your choice. Then create a brief business plan for that business. See if you can find a version of the company's actual executive summary, business plan, or canvas. Compare and contrast your vision with what the company has articulated.

- These companies are well established but is there a component of what you charted that you would advise the company to change to ensure future viability?
- Map out a contingency plan for a "what-if" scenario if one key aspect of the company or the environment it operates in were drastically is altered?

Full Business Plan

Even full business plans can vary in length, scale, and scope. Rice University sets a ten-page cap on business plans submitted for the full competition. The IndUS Entrepreneurs, one of the largest global networks of entrepreneurs, also holds business plan competitions for students through its Tie Young Entrepreneurs program. In contrast, business plans submitted for that competition can usually be up to twenty-five pages. These are just two examples. Some components may differ slightly; common elements are typically found in a formal business plan outline. The next section will provide sample components of a full business plan for a fictional business.

Executive Summary

The executive summary should provide an overview of your business with key points and issues. Because the summary is intended to summarize the entire document, it is most helpful to write this section last, even though it comes first in sequence. The writing in this section should be especially concise. Readers should be able to understand your needs and capabilities at first glance. The section should tell the reader what you

53 "Rice Business Plan Competition, Eligibility Criteria and How to Apply." Rice Business Plan Competition. March 2020. https://rbpc.rice.edu/sites/g/files/bxs806/f/2020%20RBPC%20Eligibility%20Criteria%20and%20How%20to%20Apply_23Oct19.pdf; Based on 2019 RBPC Competition Rules and Format April 4–6, 2019. https://rbpc.rice.edu/sites/g/files/bxs806/f/2019-RBPC-Competition-Rules%20-Format.pdf

want and your "ask" should be explicitly stated in the summary.

Describe your business, its product or service, and the intended customers. Explain what will be sold, who it will be sold to, and what competitive advantages the business has. Table 11.3 shows a sample executive summary for the fictional company La Vida Lola.

Executive Summary for La Vida Lola

Executive Summary Component	Content
The Concept	La Vida Lola is a food truck serving the best Latin American and Caribbean cuisine in the Atlanta region, particularly Puerto Rican and Cuban dishes, with a festive flair. La Vida Lola offers freshly prepared dishes from the mobile kitchen of the founding chef and namesake Lola González, a Duluth, Georgia, native who has returned home to launch her first venture after working under some of the world's top chefs. La Vida Lola will cater to festivals, parks, offices, community and sporting events, and breweries throughout the region.
Market Advantage	Latin food packed with flavor and flair is the main attraction of La Vida Lola. Flavors steeped in Latin American and Caribbean culture can be enjoyed from a menu featuring street foods, sandwiches, and authentic dishes from the González family's Puerto Rican and Cuban roots. *Millennial foodies* craving ethnic food experiences and *Latin food lovers* are the primary customers, but anyone with a taste for delicious homemade meals in Atlanta can order. Having a native Atlanta-area resident returning to her hometown after working in restaurants around the world to share food with area communities offers a competitive advantage for La Vida Lola in the form of founding chef Lola González.
Marketing	The venture will adopt a concentrated marketing strategy. The company's promotion mix will comprise a mix of advertising, sales promotion, public relations, and personal selling. Much of the promotion mix will center around dual-language social media.
Venture Team	The two founding members of the management team have almost four decades of combined experience in the restaurant and hospitality industries. Their background includes experience in food and beverage, hospitality and tourism, accounting, finance, and business creation.
Capital Requirements	La Vida Lola is seeking startup capital of $50,000 to establish its food truck in the Atlanta area. An additional $20,000 will be raised through a donations-driven crowdfunding campaign. The venture can be up and running within six months to a year.

Table 11.3

Business Description

This section describes the industry, your product, and the business and success factors. It should provide a

current outlook as well as future trends and developments. You also should address your company's mission, vision, goals, and objectives. Summarize your overall strategic direction, your reasons for starting the business, a description of your products and services, your business model, and your company's value proposition. Consider including the Standard Industrial Classification/North American Industry Classification System (SIC/NAICS) code to specify the industry and insure correct identification. The industry extends beyond where the business is located and operates, and should include national and global dynamics. Table 11.4 shows a sample business description for La Vida Lola.

Business Description for La Vida Lola

Business Description	La Vida Lola will operate in the mobile food services industry, which is identified by SIC code 5812 Eating Places and NAICS code 722330 Mobile Food Services, which consist of establishments primarily engaged in preparing and serving meals and snacks for immediate consumption from motorized vehicles or nonmotorized carts. Ethnically inspired to serve a consumer base that craves more spiced Latin foods, La Vida Lola is an Atlanta-area food truck specializing in Latin cuisine, particularly Puerto Rican and Cuban dishes native to the roots of the founding chef and namesake, Lola González. La Vida Lola aims to spread a passion for Latin cuisine within local communities through flavorful food freshly prepared in a region that has embraced international eats. Through its mobile food kitchen, La Vida Lola plans to roll into parks, festivals, office buildings, breweries, and sporting and community events throughout the greater Atlanta metropolitan region. Future growth possibilities lie in expanding the number of food trucks, integrating food delivery on demand, and adding a food stall at an area food market. After working in noted restaurants for a decade, most recently under the famed chef José Andrés, chef Lola González returned to her hometown of Duluth, Georgia, to start her own venture. Although classically trained by top world chefs, it was González's grandparents' cooking of authentic Puerto Rican and Cuban dishes in their kitchen that influenced her profoundly. The freshest ingredients from the local market, the island spices, and her attention to detail were the spark that ignited Lola's passion for cooking. To that end, she brings flavors steeped in Latin American and Caribbean culture to a flavorful menu packed full of street foods, sandwiches, and authentic dishes. Through reasonably priced menu items, La Vida Lola offers food that appeals to a wide range of customers, from millennial foodies to Latin natives and other locals with Latin roots.

Table 11.4

Industry Analysis and Market Strategies

Here you should define your market in terms of size, structure, growth prospects, trends, and sales potential. You'll want to include your TAM and forecast the SAM. (Both these terms are discussed in Conducting a Feasibility Analysis.) This is a place to address market segmentation strategies by geography, customer attributes, or product orientation. Describe your positioning relative to your competitors' in terms of pricing, distribution, promotion plan, and sales potential. Table 11.5 shows an example industry analysis and market strategy for La Vida Lola.

Industry Analysis and Market Strategy for La Vida Lola

Table 11.5

Industry Analysis and Market Strategy

According to *Mobile Food Trends and Insights*' first annual report from the San Francisco-based Off The Grid, a company that facilitates food markets nationwide, the US food truck industry alone is projected to grow by nearly 20 percent from $800 million in 2017 to $985 million in 2019. Meanwhile, an *IBISWorld* report shows the street vendors' industry with a 4.2 percent annual growth rate to reach $3.2 billion in 2018. Food truck and street food vendors are increasingly investing in specialty, authentic ethnic, and fusion food, according to the *IBISWorld* report.

Although the *IBISWorld* report projects demand to slow down over the next five years, it notes there are still opportunities for sustained growth in major metropolitan areas. The street vendors industry has been a particular bright spot within the larger food service sector.

The industry is in a growth phase of its life cycle. The low overhead cost to set up a new establishment has enabled many individuals, especially specialty chefs looking to start their own businesses, to own a food truck in lieu of opening an entire restaurant. Off the Grid's annual report indicates the average typical initial investment ranges from $55,000 to $75,000 to open a mobile food truck.

The restaurant industry accounts for $800 billion in sales nationwide, according to data from the National Restaurant Association. Georgia restaurants brought in a total of $19.6 billion in 2017, according to figures from the Georgia Restaurant Association.

There are approximately 12,000 restaurants in the metro Atlanta region. The Atlanta region accounts for almost 60 percent of the Georgia restaurant industry. The SAM is estimated to be approximately $360 million.

The mobile food/street vendor industry can be segmented by types of customers, types of cuisine (American, desserts, Central and South American, Asian, mixed ethnicity, Greek Mediterranean, seafood), geographic location and types (mobile food stands, mobile refreshment stands, mobile snack stands, street vendors of food, mobile food concession stands).

Secondary competing industries include chain restaurants, single location full-service restaurants, food service contractors, caterers, fast food restaurants, and coffee and snack shops.

The top food truck competitors according to the *Atlanta Journal-Constitution*, the daily newspaper in La Vida Lola's market, are Bento Bus, Mix'd Up Burgers, Mac the Cheese, The Fry Guy, and The Blaxican. Bento Bus positions itself as a Japanese-inspired food truck using organic ingredients and dispensing in eco-friendly ware. The Blaxican positions itself as serving what it dubs "Mexican soul food," a fusion mashup of Mexican food with Southern comfort food. After years of operating a food truck, The Blaxican also recently opened its first brick-and-mortar restaurant. The Fry Guy specializes in Belgian-style street fries with a variety of homemade dipping sauces. These three food trucks would be the primary competition to La Vida Lola, since they are in the "ethnic food" space, while the other two offer traditional American food. All five have established brand identities and loyal followers/customers since they are among the industry leaders as established by "best of" lists from area publications like the *Atlanta Journal-Constitution*. Most dishes from competitors are in the $10–$13 price range for entrees. La Vida Lola dishes will range from $6 to $13.

One key finding from Off the Grid's *Mobile Food Trends and Insights* report is that mobile food

Table 11.5

has “proven to be a powerful vehicle for catalyzing diverse entrepreneurship” as 30 percent of mobile food businesses are immigrant owned, 30 percent are women owned, and 8 percent are LGBTQ owned. In many instances, the owner-operator plays a vital role to the brand identity of the business as is the case with La Vida Lola.

Atlanta has also tapped into the nationwide trend of food hall-style dining. These food halls are increasingly popular in urban centers like Atlanta. On one hand, these community-driven areas where food vendors and retailers sell products side by side are secondary competitors to food trucks. But they also offer growth opportunities for future expansion as brands solidify customer support in the region. The most popular food halls in Atlanta are Ponce City Market in Midtown, Krog Street Market along the BeltLine trail in the Inman Park area, and Sweet Auburn Municipal Market downtown Atlanta. In addition to these trends, Atlanta has long been supportive of international cuisine as Buford Highway (nicknamed “BuHi”) has a reputation for being an eclectic food corridor with an abundance of renowned Asian and Hispanic restaurants in particular.

The Atlanta region is home to a thriving Hispanic and Latinx population, with nearly half of the region’s foreign-born population hailing from Latin America. There are over half a million Hispanic and Latin residents living in metro Atlanta, with a 150 percent population increase predicted through 2040. The median age of metro Atlanta Latinos is twenty-six. La Vida Lola will offer authentic cuisine that will appeal to this primary customer segment.

La Vida Lola must contend with regulations from towns concerning operations of mobile food ventures and health regulations, but the Atlanta region is generally supportive of such operations. There are many parks and festivals that include food truck vendors on a weekly basis.

Table 11.5

Competitive Analysis

The competitive analysis is a statement of the business strategy as it relates to the competition. You want to be able to identify who are your major competitors and assess what are their market shares, markets served, strategies employed, and expected response to entry? You likely want to conduct a classic **SWOT analysis** (Strengths Weaknesses Opportunities Threats) and complete a competitive-strength grid or competitive matrix. Outline your company’s competitive strengths relative to those of the competition in regard to product, distribution, pricing, promotion, and advertising. What are your company’s competitive advantages and their likely impacts on its success? The key is to construct it properly for the relevant features/benefits (by weight, according to customers) and how the startup compares to incumbents. The **competitive matrix** should show clearly how and why the startup has a clear (if not currently measurable) competitive advantage. Some common features in the example include price, benefits, quality, type of features, locations, and distribution/sales. Sample templates are shown in Figure 11.17 and Figure 11.18. A competitive analysis helps you create a marketing strategy that will identify assets or skills that your competitors are lacking so you can plan to fill those gaps, giving you a distinct competitive advantage. When creating a competitor analysis, it is important to focus on the key features and elements that matter to customers, rather than focusing too heavily on the entrepreneur’s idea and desires.

	La Vida Lola	Mix'D Up Burgers	Mac the Cheese	The Fry Guy	The Blaxican
Price	$6-$13	$10	$10-13	$13+	High end
Location	Varies	Rotate/Smyrna	Rotates	Buckhead	Midtown
Quality	Mid to high	Low	Mid	High	High
Food type	Latin	American/ Burgers	American/ Comfort	American	Soul/ Mexican fusion

Figure 11.17 This chart shows one sample format for a competitor analysis. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

COMPETITIVE ANALYSIS TEMPLATE							
	Price	**Benefits**	**Quality**	**Features**	**Locations**	**Distribution/ Sales**	**Customer satisfaction**
Competitor 1							
Competitor 2							
Competitor 3							
Competitor 4							

Figure 11.18 This chart provides a more complex template for creating a competitive analysis. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Operations and Management Plan

In this section, outline how you will manage your company. Describe its organizational structure. Here you can address the form of ownership and, if warranted, include an organizational chart/structure. Highlight the backgrounds, experiences, qualifications, areas of expertise, and roles of members of the management team. This is also the place to mention any other stakeholders, such as a board of directors or advisory board(s), and their relevant relationship to the founder, experience and value to help make the venture successful, and professional service firms providing management support, such as accounting services and legal counsel.

Table 11.6 shows a sample operations and management plan for La Vida Lola.

Operations and Management Plan for La Vida Lola

Table 11.6

Operations and Management Plan Category	Content
Key Management Personnel	The key management personnel consist of Lola González and Cameron Hamilton, who are longtime acquaintances since college. The management team will be responsible for funding the venture as well as securing loans to start the venture. The following is a summary of the key personnel backgrounds. *Lola González:* Chef Lola González has worked directly in the food service industry for fifteen years. While food has been a lifelong passion learned in her grandparents' kitchen, chef González has trained under some of the top chefs in the world, most recently having worked under the James Beard Award-winning chef José Andrés. A native of Duluth, Georgia, chef González also has an undergraduate degree in food and beverage management. Her value to the firm is serving as "the face" and company namesake, preparing the meals, creating cuisine concepts, and running the day-to-day operations of La Vida Lola. *Cameron Hamilton:* Cameron Hamilton has worked in the hospitality industry for over twenty years and is experienced in accounting and finance. He has a master of business administration degree and an undergraduate degree in hospitality and tourism management. He has opened and managed several successful business ventures in the hospitality industry. His value to the firm is in business operations, accounting, and finance.
Advisory Board	During the first year of operation, the company intends to keep a lean operation and does not plan to implement an advisory board. At the end of the first year of operation, the management team will conduct a thorough review and discuss the need for an advisory board.
Supporting Professionals	Stephen Ngo, Certified Professional Accountant (CPA), of Valdosta, Georgia, will provide accounting consulting services. Joanna Johnson, an attorney and friend of chef González, will provide recommendations regarding legal services and business formation.

Table 11.6

Marketing Plan

Here you should outline and describe an effective overall marketing strategy for your venture, providing details regarding pricing, promotion, advertising, distribution, media usage, public relations, and a digital presence. Fully describe your sales management plan and the composition of your sales force, along with a comprehensive and detailed budget for the marketing plan. Table 11.7 shows a sample marketing plan for La Vida Lola.

Marketing Plan for La Vida Lola

Table 11.7

Marketing Plan Category	Content
Overview	La Vida Lola will adopt a concentrated marketing strategy. The company's promotion mix will include a mix of advertising, sales promotion, public relations, and personal selling. Given the target millennial foodie audience, the majority of the promotion mix will be centered around social media platforms. Various social media content will be created in both Spanish and English. The company will also launch a crowdfunding campaign on two crowdfunding platforms for the dual purpose of promotion/publicity and fundraising.

Table 11.7

Marketing Plan Category	Content
Advertising and Sales Promotion	As with any crowdfunding social media marketing plan, the first place to begin is with the owners' friends and family. Utilizing primarily Facebook/Instagram and Twitter, La Vida Lola will announce the crowdfunding initiative to their personal networks and prevail upon these friends and family to share the information. Meanwhile, La Vida Lola needs to focus on building a community of backers and cultivating the emotional draw of becoming part of the La Vida Lola family. To build a crowdfunding community via social media, La Vida Lola will routinely share its location, daily if possible, on both Facebook, Instagram, and Twitter. Inviting and encouraging people to visit and sample their food can rouse interest in the cause. As the campaign is nearing its goal, it would be beneficial to offer a free food item to backers of a specific level, say $50, on one specific day. Sharing this via social media in the day or two preceding the giveaway and on the day of can encourage more backers to commit. Weekly updates of the campaign and the project as a whole are a must. Facebook and Twitter updates of the project coupled with educational information sharing helps backers feel part of the La Vida Lola community. Finally, at every location where La Vida Lola is serving its food, signage will notify the public of their social media presence and the current crowdfunding campaign. Each meal will be accompanied by an invitation from the server for the patron to visit the crowdfunding site and consider donating. Business cards listing the social media and crowdfunding information will be available in the most visible location, likely the counter. Before moving forward with launching a crowdfunding campaign, La Vida Lola will create its website. The website is a great place to establish and share the La Vida Lola brand, vision, videos, menus, staff, and events. It is also a great source of information for potential backers who are unsure about donating to the crowdfunding campaigns. The website will include these elements: • *About Us*. Address the following questions: Who are you? What are the guiding principles of La Vida Lola? How did the business get started? How long has La Vida Lola been in business? Include pictures of chef González. • *Menu.* List of current offerings with prices. • *Calendar of Events.* Will include promotional events and locations where customers can find the truck for different events. • *Social Media.* Steps will be taken to increase social media followers prior to launching the crowdfunding campaign. Unless a large social media following is already established, a business should aggressively push social media campaigns a minimum of three months prior to the crowdfunding campaign launch. Increasing social media following prior to the campaign kickoff will also allow potential donors to learn more about La Vida Lola and foster relationship building before attempting to raise funds.

Table 11.7

Marketing Plan Category	Content
Facebook Content and Advertising	The key piece of content will be the campaign pitch video, reshared as a native Facebook upload. A link to the crowdfunding campaigns can be included in the caption. Sharing the same high-quality video published on the campaign page will entice fans to visit Kickstarter to learn more about the project and rewards available to backers. • Promoted Post(s): Boosting/promoting a Facebook post for only $5 can go a long way for a business page the size of La Vida Lola's. Reach and engagement will be exponentially higher than it would have been organically. Promoting two or three posts during the first few weeks of the campaign would be highly effective. • Video Views Ad: Video ads are a little more ambitious than promoted posts and cost a little more. But the objective is the same: increase the number of people who watch the pitch video and drive them to the campaign page.

Table 11.7

Marketing Plan Category	Content
Crowdfunding Campaigns	Foodstart was created just for restaurants, breweries, cafés, food trucks, and other food businesses, and allows owners to raise money in small increments. It is similar to Indiegogo in that it offers both flexible and fixed funding models and charges a percentage for successful campaigns, which it claims to be the lowest of any crowdfunding platform. It uses a reward-based system rather than equity, where backers are offered rewards or perks resulting in "low-cost capital and a network of people who now have an incentive to see you succeed."[54] Foodstart will host La Vida Lola's crowdfunding campaigns for the following reasons: (1) It caters to their niche market; (2) it has less competition from other projects which means that La Vida Lola will stand out more and not get lost in the shuffle; and (3) it has/is making a name/brand for itself which means that more potential backers are aware of it. La Vida Lola will run a simultaneous crowdfunding campaign on Indiegogo, which has broader mass appeal.

Table 11.7

54 Foodstart. http://foodstart.com

Marketing Plan Category	Content
Publicity	Social media can be a valuable marketing tool to draw people to the Foodstarter and Indiegogo crowdfunding pages. It provides a means to engage followers and keep funders/backers updated on current fundraising milestones. The first order of business is to increase La Vida Lola's social media presence on Facebook, Instagram, and Twitter. Establishing and using a common hashtag such as #FundLola across all platforms will promote familiarity and searchability, especially within Instagram and Twitter. Hashtags are slowly becoming a presence on Facebook. The hashtag will be used in all print collateral. La Vida Lola will need to identify social influencers—others on social media who can assist with recruiting followers and sharing information. Existing followers, family, friends, local food providers, and noncompetitive surrounding establishments should be called upon to assist with sharing La Vida Lola's brand, mission, and so on. Cross-promotion will further extend La Vida Lola's social reach and engagement. Influencers can be called upon to cross promote upcoming events and specials. The crowdfunding strategy will utilize a progressive reward-based model and establish a reward schedule such as the following: • $5 or more (unlimited): Exclusive updates on fundraising progress • $10 or more (500): $1 OFF; a coupon for $1 off purchase • $20 or more (200): BOGO! Buy one entree, get one FREE • $50 or more (100): FREE entrée coupon • $250 or more (2): One-on-one with chef González! In addition to the publicity generated through social media channels and the crowdfunding campaign, La Vida Lola will reach out to area online and print publications (both English- and Spanish-language outlets) for feature articles. Articles are usually teased and/or shared via social media. Reaching out to local broadcast stations (radio and television) may provide opportunities as well. La Vida Lola will recruit a social media intern to assist with developing and implementing a social media content plan. Engaging with the audience and responding to all comments and feedback is important for the success of the campaign. Some user personas from segmentation to target in the campaign: • Influencer Isabel: Social media-savvy, college-age Latinx influencer • Food truck Freddie: An avid food truck follower, this thirty-three-year-old urban hipster professional seeks out the best food trucks around town on a regular basis looking for "noms" to satisfy his cravings. • Taco townies: In-town residents who religiously eat tacos on "taco Tuesday," as a family rite of passage for the partners and kids. The entire neighborhood turns out for the occasion as a community event of sorts.

Table 11.7

Financial Plan

A **financial plan** seeks to forecast revenue and expenses; project a financial narrative; and estimate project costs, valuations, and cash flow projections. This section should present an accurate, realistic, and achievable financial plan for your venture (see Entrepreneurial Finance and Accounting for detailed discussions about conducting these projections). Include sales forecasts and income projections, pro forma financial statements (Building the Entrepreneurial Dream Team, a breakeven analysis, and a capital budget. Identify your possible sources of financing (discussed in Conducting a Feasibility Analysis). Figure 11.19 shows a template of cash-flow needs for La Vida Lola.

INCOME		EXPENSES	
Daily Income		**Fixed Monthly Expenses**	
Monday	$	Facility rental	$
Tuesday	$	Personal loans	$
Wednesday	$	Insurance	$
Thursday	$	Credit cards	$
Friday	$	Farmer's Market overheads	$
Saturday AM	$	Planned savings	$
Saturday PM	$	Other	$
Sunday	$	*Total fixed monthly expenses*	$
		Variable Monthly Expenses	
		Food/Beverages	$
		Utilities (electricity, gas)	$
		Uniforms	$
		Wages	$
		Fuel (vehicle)	$
		Medical expenses	$
		Other	$
		Total variable monthly expenses	$
		Fixed Infrequent Expenses	
		Insurance	$
		Annual subscriptions	$
		Property rates/taxes	$
		Union fees	$
		Education	$
		Other	$
		Total fixed infrequent expenses	$
		Variable Infrequent Expenses	
		Gifts	$
		Holidays	$
		Vehicle repairs and registration	$
		Durable goods purchase	$
		Donations	$
		Other	$
		Total variable infrequent expenses	$
TOTAL Income	**$**	**TOTAL Expenses**	$
		DIFFERENCE = Income available	**$**

Figure 11.19 La Vida Lola can use a template like this to project cash flow. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

ENTREPRENEUR IN ACTION

Laughing Man Coffee

Hugh Jackman (Figure 11.20) may best be known for portraying a comic-book superhero who used his mutant abilities to protect the world from villains. But the *Wolverine* actor is also working to make the planet a better place for real, not through adamantium claws but through social entrepreneurship.

Figure 11.20 Hugh Jackman launched a social entrepreneurship venture called Laughing Man Coffee. (credit: "Hugh Jackman navy" by "U.S. Navy photo by Photographer's Mate Airman Dennard Vinson"/Wikimedia Commons, Public Domain)

A love of java jolted Jackman into action in 2009, when he traveled to Ethiopia with a Christian humanitarian group to shoot a documentary about the impact of fair-trade certification on coffee growers there. He decided to launch a business and follow in the footsteps of the late Paul Newman, another famous actor turned philanthropist via food ventures.

Jackman launched Laughing Man Coffee two years later; he sold the line to Keurig in 2015. One Laughing Man Coffee café in New York continues to operate independently, investing its proceeds into charitable programs that support better housing, health, and educational initiatives within fair-trade farming communities.[55] Although the New York location is the only café, the coffee brand is still distributed, with Keurig donating an undisclosed portion of Laughing Man proceeds to those causes (whereas Jackman donates all his profits). The company initially donated its profits to World Vision, the Christian humanitarian group Jackman accompanied in 2009. In 2017, it created the Laughing Man Foundation to be more active with its money management and distribution.

- You be the entrepreneur. If you were Jackman, would you have sold the company to Keurig? Why or why not?
- Would you have started the Laughing Man Foundation?
- What else can Jackman do to aid fair-trade practices for coffee growers?

WHAT CAN YOU DO?

Textbooks for Change

Founded in 2014, Textbooks for Change uses a cross-compensation model, in which one customer segment pays for a product or service, and the profit from that revenue is used to provide the same product or service to another, underserved segment. Textbooks for Change partners with student organizations to collect used college textbooks, some of which are re-sold while others are donated to students in need at

55 "Hugh Jackman Journey to Starting a Social Enterprise Coffee Company." Giving Compass. April 8, 2018. https://givingcompass.org/article/hugh-jackman-journey-to-starting-a-social-enterprise-coffee-company/

underserved universities across the globe. The organization has reused or recycled 250,000 textbooks, providing 220,000 students with access through seven campus partners in East Africa. This B-corp social enterprise tackles a problem and offers a solution that is directly relevant to college students like yourself. Have you observed a problem on your college campus or other campuses that is not being served properly? Could it result in a social enterprise?

WORK IT OUT

Franchisee Set Out

A franchisee of East Coast Wings, a chain with dozens of restaurants in the United States, has decided to part ways with the chain. The new store will feature the same basic sports-bar-and-restaurant concept and serve the same basic foods: chicken wings, burgers, sandwiches, and the like. The new restaurant can't rely on the same distributors and suppliers. A new business plan is needed.

- What steps should the new restaurant take to create a new business plan?
- Should it attempt to serve the same customers? Why or why not?

LINK TO LEARNING

This *New York Times* video, "An Unlikely Business Plan," describes entrepreneurial resurgence (https://openstax.org/l/52EntreResurg) in Detroit, Michigan.

Key Terms

balance sheet financial statement that summarizes a company's financial condition according to the accounting equation

breakeven point level of operations that results in exactly enough revenue to cover costs

business model plan for how venture will be funded; how the venture creates value for its stakeholders, including customers; how the venture's offerings are made and distributed to the end users; and the how income will be generated through this process

business model canvas developed by Osterwalder and Pigneur, used to develop a business model for a venture, including nine blocks that are mapped out to address customer segments, customer relationships, channels, revenue streams, value propositions, key partners, key activities, key resources, and cost structure

business model innovation occurs when an existing business fundamentally changes their business model

business plan formal document that typically describes the business and industry, market strategies, sales potential, and competitive analysis, as well as the company's long-term goals and objectives

competitive matrix shows how and why a startup has a clear if not measurable competitive advantage for relevant features/benefits by weight according to customers, such as price and quality in relation to competitors

customer empathy map portrayal of a target customer, the most promising candidate from a business' customer segments, which explores the understanding of that person's condition from their perspective to understand their problems and needs

disruptive innovation process that significantly impacts the market by making a product or service more affordable and/or accessible often by smaller companies in an industry

executive summary initial section of a business plan document that summarizes the key elements of the entire plan

feasibility analysis feasibility analysis is the process of determining if a business idea is viable; it includes testing the viability of your product or service, evaluating your management team, assessing the market for your concept, and estimating financial viability

financial analysis forecasts revenue and expenses; projects a financial narrative; and estimates project costs, valuations, and cash flow projections

fixed costs costs that do not change, regardless of the amount of sales

go-or-no-go decision determination to proceed with or abandon a plan or project

innovation new idea, process, or product, or a change to an existing product or process

lean model canvas developed by Ash Maurya as a derivation of the original business model canvas; this canvas differs by addressing unfair advantages, problems, solutions, and key metrics rather than customer relationships, key partners, key activities, and key resources

market analysis analysis of the overall interest in the product or service within the industry by its target market

projected cash flow outline of preliminary expenses, operating expenses, and reserves

serviceable available market (SAM) portion of the market that a business can serve based on its products, services, and location

social business model canvas modification of the business model canvas, designed for social entrepreneurship venues; new areas address impact measures around social impacts and its measurement, surplus, beneficiary segments and social and customer value propositions

SWOT analysis strategic analytical tool used to help a potential venture or existing company identify its strengths, weaknesses, opportunities, and threats related to business competition

total available market (TAM) total perceived demand for a product or service within the marketplace

value proposition summary describing the benefits (value) customers can expect from a particular product or service

value proposition canvas one of the nine blocks on the business model canvas, this additional tool developed by Osterwalder and Pigneur is designed to illustrate a deeper dive into customer understanding

and value creation of a business

variable costs costs that fluctuate with the level of revenue

Summary

11.1 Avoiding the "Field of Dreams" Approach

Business models and business plans are tools involved in the strategic process of charting a path for your entrepreneurial venture. When starting a company, it's best to avoid the *Field of Dreams* approach of building a business and hoping that customers will just show up. Innovation has been linked to entrepreneurship for at least nine decades. More recent theories suggest that disruptive innovations are disruptive because they disturb the underlying business model of the companies being disrupted.

11.2 Designing the Business Model

A business model, which is unique to a company, describes the rationale of how an organization creates, delivers, and captures values. A business model canvas is a popular tool used by entrepreneurs and intrapraneurs to map out and plan different components of a business model. The business model canvas addresses customer segments, customer relationships, channels (of distribution), revenue streams, value propositions, key partners, key activities, key resources, and cost structure. The lean model canvas and social business model canvas are derivations of the original business model canvas. They are designed more for tech/software/app endeavors and social entrepreneurial ventures, respectively.

11.3 Conducting a Feasibility Analysis

A feasibility study is a tool in the entrepreneurs' toolkit that can help determine whether to proceed on a venture early on. A feasibility study is usually more in depth than a business plan and focuses on analysis of real-world numbers and projections. The most common elements of a feasibility study include a market analysis, a financial analysis, and management analysis. Feasibility studies can be used to make a "go-or-no-go" decision for a new product or business, as well as help narrow the focus of what that venture should be (what the market would potentially support).

11.4 The Business Plan

The business plan is a formal document used for long-range planning of a company's operation that typically includes financial information, background information, and a summary of the business. Business plans can be used as internal guiding documents early in the entrepreneurial process. They also can be presentation documents for raising funds from prospective investors later in the process, complementing an investor pitch and iterative canvases. A brief business plan functions somewhat like an extended executive summary that summarizes key elements of the entire business plan, such as the business concept, financial features, and current business position. A full business plan can range from ten to twenty-five pages. It includes a business description, industry and marketing analyses, and descriptions of management, marketing, and operational and financial plans.

Review Questions

1. According to Ash Maurya's typology, Airbnb is an example of what type of business model?
   A. direct
   B. multisided
   C. open
   D. marketplace

2. Which startup grew from a failed podcasting company called Odeo?
   A. Instagram

B. Twitter
C. StubHub
D. Groupon

3. What is the job to be done of a milkshake according to Christensen's team's customer observation research in the Link to Learning video: https://www.youtube.com/watch?v=m3mVM_koAio&feature=youtu.be?
A. employ Chick-Fil-A cows
B. accompany on a long morning commute
C. placate children
D. satisfy hunger

4. What is a change, typically minor, of the current business model in an attempt to capitalize on a closely related market opportunity?
A. innovation
B. disruption
C. iteration
D. increment

5. A tool to identify your idealized target customer and develop a better understanding of their environment, behavior, concerns, and aspirations.
A. jobs to be done
B. business plan
C. business model canvas
D. empathy map

6. A _____ is a formal document that typically describes the business and industry, market strategies, sales potential, and competitive analysis, as well as the company's long-term goals and objectives.
A. business plan
B. business model
C. customer empathy map
D. revenue model

7. Select the item that does not belong to the business model canvas.
A. market size
B. revenue streams
C. value proposition
D. customer segments

8. The finished story benefit formula of [end customer wants] + [specific period of time] + [address objections] is designed for what component of the lean model canvas?
A. unfair advantage
B. unique value proposition
C. early adopters
D. high concept pitch

9. How does the social business model canvas differ from the business model canvas and lean model canvas?
A. is only used by nonprofit company
B. doesn't have customer block and investment block

C. has profit block to talk about ways the company can makes more money
D. has impact measure, surplus, beneficiary segments, and social and customer value propositions

10. Which of the following has the purpose of evaluating the team, the market for the concept, the financial viability, and possible pitfalls?
A. feasibility analysis
B. market analysis
C. financial analysis
D. management analysis

11. Which of the following has the purpose of forecasting revenue and expenses, projecting a financial narrative, estimating project cost, and projecting cash flow?
A. feasibility analysis
B. market analysis
C. financial analysis
D. management analysis

12. Which of the following identifies competitors and quantifies target customers and/or users in a specific industry?
A. feasibility analysis
B. market analysis
C. financial analysis
D. management analysis

13. What assesses the prowess of the management and sufficiency of resources to bring the product or idea to market?
A. management analysis
B. operational feasibility analysis
C. financial analysis
D. cash flow

14. What are expenses that do not vary with the level of sales, such as rent, salaries, utilities, insurance and other operating expenses?
A. fixed costs
B. variable costs
C. balance sheet
D. cash flow statements

15. Which of the following is a formal document that typically describes the business and industry, market strategies, sales potential, and competitive analysis, as well as the company's long-term goals and objectives?
A. business plan
B. business model
C. customer empathy map
D. revenue model

16. Which of these is not the purpose of a business plan?
A. thoroughly explain a business idea and how it will be carried out
B. planning tool and working plan over the course of several years
C. requirement to start a business

D. planning for "what-if" scenarios and explore new options

17. Which of these components are not in a business plan?
A. business description
B. industry and market analysis
C. financial analysis
D. None of these options is correct.

18. Estimated profits and expenses of the business is included in which of the following?
A. financial analysis
B. industry and market analysis
C. operation plan
D. marketing plan

19. Who is best suited to write a business plan?
A. investor
B. founder(s)
C. consultant
D. chief financial officer

Discussion Questions

1. What role do customers play in innovation? Is innovation possible without customer support?

2. Do you believe that teamwork is important to entrepreneurship? Or do you prefer solopreneurship? Is one approach "better" than the other? Why or why not?

3. What are the advantages of using a canvas to plan your business?

4. What types of businesses fit best with each respective canvas type?

5. Why would impact measures be important in social entrepreneurship ventures?

6. How do the arts relate to the business model creation process?

7. What are the advantages of using a lean model canvas compared to the traditional business model canvas?

8. What components are in the breakeven analysis? How would you calculate your breakeven point?

9. Why is feasibility analysis important?

10. What are the different components of a feasibility analysis?

11. Explain the purpose and importance of business plan.

12. Describe the components of a business plan.

13. Should you write a business plan even if you do not need outside financing? Why or why not?

Case Questions

1. The National Association of Broadcasters launched its PILOT Innovation Challenge in 2016. The challenge is centered around a specific challenge question aimed at helping the association's primary customers, broadcasters. The most recent challenge question was, "What is an unconventional way broadcasters and other local media could serve communities?" The PILOT organizers have contracted you to help them design their next challenge. Using your knowledge of innovation and customer-centric entrepreneurship

processes, what would you advise? How would you go about determining the challenge question? What questions about innovation would you have regarding the Innovation Challenge?

2. The Guidewell Innovation Center at Lake Nona Medical Center on the outskirts of Orlando, Florida, is a 92,000-square-foot facility aimed at accelerating innovation within the healthcare industries. Guidewell, the parent company of Florida Blue, brings in outside companies to help with that innovation process. One of the features of the Innovation Center is its Collaborative Resource Ecosystem. Some of the center's strategic areas of focus are next-generation consumer engagement, computational health, well-being and human performance, digital health, and remote management, among other areas. How could Christensen's theory of disruptive innovation and jobs-to-be-done theory help guide Guidewell's mission? What are the prevalent business models in the strategic areas for incumbent businesses? What are opportunities for innovation for new companies?

3. As youth programs face severe budget cuts, many youth sports organizations respond by raising their fees, which shifts the costs to families. Good Sports was founded in 2003, to tackle this problem by providing new equipment, footwear, and apparel to those most in need. The organization's addressable markets include children ages five to eighteen living in low-income households, as defined by poverty data, and participating in youth sports in top fifty metropolitan service areas. This Boston-based organization has plans to expand from its three existing markets in Dallas, Chicago, and Boston to seven total markets by 2023 with a goal to serve 600,000 kids by that target date.
   A. What would a customer empathy map look like for Good Sports' target user? What about its target customer segment? Would it or should it differ in differing markets? Is the Boston area user any different from say, an Atlanta, user?
   B. Given its social mission, what are some impact measures Good Sports could use to gauge success and impact?

4. DoSomething.Org is a "global movement for good" among 6 million young people, transforming their communities across the United States and in 131 countries worldwide. This nonprofit organization constantly holds cause-based campaigns, ranging from receiving over 1 million pairs of donated jeans from teens to clothe homeless youth to cleaning up 3.7 million cigarette butts through its Get the Filter Out initiative. A past campaign, "Don't Be a Sucker," addressed the problem of Americans losing $5.8 billion annually and producing 8.7 billion pounds of carbon pollution by leaving unused devices plugged in. The campaign sought to slay those "energy vampires" not in use by having users unplug equipment and post a sticky note next to the outlet to remind others not to let them suck the energy dry. Further research the problem, solution and this campaign and answer the following:
   A. Identify what social impact(s) the campaign addressed.
   B. What impact measures could the campaign assess?
   C. Could a viable business be created around this problem?

5. In recent years, the entrepreneurial educator and author Steve Blank began applying lean startup principles to various US governmental agencies. Through a Hacking for Diplomacy course, students at Stanford University began tackling problems for the Department of State. A former US ambassador to the United Nations, a State Department representative to Silicon Valley and senior advisor for technology and innovation, a retired US Army colonel, and other entrepreneurial educators joined Blank in applying lean startup methods to State Department issues. Then-Secretary of State John Kerry even visited the Stanford students and said he was looking forward to the solutions students develop during the ten weeks. One project that emerged was from a group calling themselves Team Space Evaders. The team was tasked with working on the problem of satellite collision. Members charted satellite positioning data and explored how information about potential collision was shared by commercial operators and governmental entities ranging from the Federal Aviation Administration to the Department of Defense.

A. Apply the lean startup methodology to identify potential customer segments and problems and solutions that students such as yourself could identify for the State Department on the issue of satellite collision.
B. What would a unique value proposition for a State Department solution to this issue be? How could a high-level concept pitch work when selling the concept within the State Department?

6. Incorporated in 2003, Tesla declared in its mission statement that its goal is "to accelerate the world's transition to sustainable transport,"[56] and it has proven itself a leader in green technology in the automotive sector. In its initial business plan, by co-founder Martin Eberhard, the electric sports car company promised to provide the value of a high-end sports car at a lower cost to the customer and a lower environmental cost to the planet. Electric vehicles were seen as inferior to standard vehicles prior to Tesla's innovations in creating powerful cars that piqued consumer desire. The generic automotive manufacturing business model relies on collaborative manufacturing with industry partners and a distribution model dependent on third parties. Standard cars are aimed at people and businesses with individual transportation needs. This model is commercially viable because of custom-equipped add-on features to the per-vehicle prices.
A. Tesla's business model is different. Identify at least three ways in which the Tesla model differs from the traditional automotive business model.

7. In the mid-1990s, at least one newspaper company, the now-defunct Knight-Ridder chain, created the prototype for a tablet newspaper that very much resembles the present-day iPad. A 1994 video titled "The Tablet Newspaper: A Vision for the Future" shows off the design of a futuristic newspaper designed at the Knight Ridder Information Design Lab in Boulder, Colorado. The video went viral in 2011 after it was posted on YouTube and numerous websites and blogs. The person behind the tablet vision, Roger Fidler, had even published an essay describing a tablet future as far back as 1981. The Knight-Ridder lab shared a wall with its neighbor Apple, with executives swapping ideas and visitors. The newspaper company, focused on content creation and not the hardware side, decided to not patent its tablet design and scrapped the project because screens took too much energy, and it was too expensive.
A. Using the components of a feasibility study, consider how the newspaper company would stack up on go-or-no-go decisions for each component of the feasibility study.
B. How did the newspaper company in the 1990s fare in terms of management prowess, resource capabilities, financial viability, and market analysis?
C. Do you think the newspaper made a wise decision to abandon the project when it did? Why or why not?

8. Founded in 2013 primarily as a coding boot camp, Tech Talent South offers both part-time and full-time courses on topics like Ruby on Rails and Big Data Analytics. Most of the camp's programs are run out of cooperative working spaces and temporary locations throughout the cities it has a presence in. The primary focus of the Atlanta-founded and now North Carolina-based company as branded in the name was on coding in the South, but the company to date has expanded to eleven markets with plans to expand even more. The founder, Betsy Idilbi, jokes that she wouldn't have named the company Tech Talent South if she had known its full potential and growth, including being plugged into the entrepreneurial ecosystem in places such as Columbus, Ohio. The company even has offices in the northeastern city of Hartford, Connecticut.
A. Could a feasibility analysis have helped Betsy from the start?
B. The company has expanded its business to offer corporate trainings at existing companies, rather than teaching classes directly to student enrollees. How would you identify a new potential market for Tech Talent South to enter?

56 In 2016, it was changed from "sustainable transport" to "sustainable energy." https://www.tesla.com/about

C. What could be done with its existing business?
D. How would you advise the company on making go-or-no-go decisions for entering new markets?

9. You were introduced to The Cut Buddy, a plastic hair and beard grooming tool that began selling on Amazon in 2016, in The Business Plan. Following funding from the *Shark Tank* investor Daymond John, the company plans to expand into retail and extend its product line.
A. How would a business plan for the company's ecommerce business differ from a retail distribution outlet?
B. Discuss how changes to aspects of the original business plan affected the outcome of the success of The Cut Buddy.
C. What do you think should be the key markets and strategies moving forward for the company?

10. Pretty Young Professional, discussed in The Business Plan, failed because of disagreements among its four founders that emerged shortly after launch.
A. If you were to launch the venture today, outline what steps you would need to take in formulating a business plan.
B. What do you think the total addressable market would be, which industry classification would it fall under, and who would be the primary competition?

Suggested Resources

11.2 Designing the Business Model

Business model canvas and resources: Strategyzer.com

Lean canvas and associated resources: Leanstack.com

Social business model canvas and related resources: Socialbusinessmodelcanvas.com

Christopher Steiner and Brett Nelson. "The 20 Most Important Questions in Business." *Forbes*. June 17, 2010: https://www.forbes.com/2010/06/17/most-important-questions-in-business-entrepreneurs-management-small-business.html#7975585a3e93

11.3 Conducting a Feasibility Analysis

Bruce Barringer, *Preparing Effective Business Plans: An Entrepreneurial Approach*, 2nd ed. (Upper Saddle River, NJ: Pearson, 2015).

https://bizfluent.com/how-8048004-prepare-financial-feasibility-study.html

https://thebusinessprofessor.com/knowledge-base/financial-analysis-of-business-idea-overview/

11.4 The Business Plan

SBA Business Plan resources: https://www.sba.gov/business-guide/plan-your-business/write-your-business-plan

12

Building Networks and Foundations

Figure 12.1 US 1 is the route into and out of the Florida Keys that residents and visitors alike take to their intended destinations. But more importantly, US 1, a physical structure of steel-reinforced concrete, is the artery through which economic exchanges are created and enhanced. (credit: modification of "Seven mile bridge" by Tinsley Advertising/Wikimedia Commons, CC BY)

Chapter Outline

12.1 Building and Connecting to Networks
12.2 Building the Entrepreneurial Dream Team
12.3 Designing a Startup Operational Plan

Introduction

US Route 1 in southern Florida connects 43 islands of the Florida Keys via 42 bridges. It is a bidirectional economic path from the US mainland to its endpoint at Key West and for all points in between. Without the bridges it provides, residents, workers, and tourists would be required to ferry to their destinations, sacrificing time, money, economic efficiency, market productivity, and recreation. The bridges ensure an unimpeded flow of economic activities that benefit residents and visitors, increasing tourism across the entire state, and ensuring Key West is not economically and socially isolated.

Every entrepreneur can learn a few lessons from US 1. First, independent market players are stronger and more stable when connected to other independent market players. Second, connections are not always easy to establish. The idea of connecting all of the keys met resistance, and engineers had to solve many challenges. Third, you must be prepared to repair connections whenever they are severed. A hurricane destroyed the original railroad that connected the islands, but replacing it with an automobile highway was a major improvement. Other lessons are that benefits should outweigh costs, and that it takes time to build new connections: The original railroad took seven years to build. Costs of ongoing repair and maintenance have exceeded $1.8 billion[1] (adjusted for inflation) but produced $2.7 billion in annual economic activity for 2017.[2] Today, no one in Florida would dream of doing without the highway.

1 Alice Hopkins. "The Development of the Overseas Highway." *Tequesta: The Journal of the Historical Association of Southern Florida* 46 (1986): 48–58. http://digitalcollections.fiu.edu/tequesta/files/1986/86_1.pdf
2 Chris Mooney. "The Race to Save Florida's Devastated Coral Reef from Global Warming." *Washington Post*. June 25, 2017. https://www.washingtonpost.com/classic-apps/the-race-to-save-floridas-devastated-coral-reefs-from-global-warming/2017/06/25/a1bd899a-3fa9-11e7-adba-394ee67a7582_story.html

How are businesses similar to Key West? Every business includes people who produce goods and services for customers to purchase. In turn, businesses and those who work for them need to consume the products and services provided by their own vendors. Finding and establishing relationships with vendors and customers, in addition to the support of community organizations and educational resources, facilitates the exchange of information, products, and services. The connection between a business and its vendors or its customers makes up a network.

12.1 Building and Connecting to Networks

Learning Objectives

By the end of this section, you will be able to:

- Define networking and describe its role in entrepreneurship
- Describe networking opportunities
- Describe local and trade organization networking opportunities
- Identify nonprofit and governmental agencies offering networking opportunities

When you begin thinking about your new and exciting entrepreneurial venture, you may feel somewhat like the citizens of Key West did many years ago—isolated. No matter which way you turn, you eventually come to the end of your limited community, and what you have is not enough. You can either sit on the beach and dream about what could be or commence working on building personal and professional connections to broaden your scope and improve the depth of relationships with those individuals who will assist you in becoming a successful entrepreneur. Now is the time to start building bridges and connecting yourself with the greater business community. Networking is about building bridges not about collecting tolls.

ENTREPRENEUR IN ACTION

Colonel Sanders and Building Connections

Harland David Sanders, the founder of Kentucky Fried Chicken (KFC), was a successful entrepreneur who personally experienced and understood the value of roadways and customer access. Sanders, better known as “Colonel” Sanders, owned a successful Shell service station with a small restaurant. He perfected his recipe for fried chicken and added it to his menu. Demand from satisfied customers soon exceeded seating capacity. To increase customer capacity, he purchased a building across the street that had a larger seating area. Business was steady and profitable until the new interstate system bypassed his location. Sanders lost his connection to his customers and closed his business. He did not give up, however.

Sanders began scouring the country for restaurants that would buy his recipe in exchange for $0.04 per piece of chicken sold. He reestablished a connection with an acquaintance in Salt Lake City, Utah, who became the first KFC franchisee. With immediate success in Utah, Sanders began a nationwide campaign to connect with other successful restaurants and signed them on as franchisees. Eventually, Sanders formed a network of restaurants across the country that sold his chicken and grew a market that could never have been developed by one person in one location. In 2019, KFC had over 21,000 locations in 130 countries (www.kfc.com/about).

Sanders took his personal experience of losing easy customer access to his business and applied it to building a network of franchises where customers, across the United States and on multiple continents, could purchase his chicken. Just as tourists, residents, and businesses in Key West need roads and bridges to connect them to their destinations and suppliers, entrepreneurs need connections and networks to get supplies from their vendors and products to their customers.

For an entrepreneur, **networking** is finding and establishing relationships with business professionals with

whom you can exchange information, ideas, and products; more importantly, you can claim these networks as trusted business colleagues. Be ready to use the networks you already have. Be intentional in seeking out established business professionals in your local chamber of commerce or at SCORE (see the following). Position yourself to contribute to the larger community. Be active in expanding your sphere of influence.

A good way to get started is to begin brainstorming a list of people who can help you along the entrepreneurial path. These potential trusted advisors will be beneficial to you as you develop your idea and start your business. In these early stages, you will encounter challenges and obstacles in many areas. Having a "go-to" list of dependable consultants can help you find solutions, reduce mistakes, and hasten your success in your new business. Anyone can be on that list—don't exclude anyone, no matter how unlikely it seems that you will need their expertise. People you already know have knowledge and skills. They can be a valuable resource.

On the other hand, you too have knowledge and skills. You too can be a valuable resource. That is why you are starting your own business or developing a new product. Begin connecting with people who need you, perhaps even people who need you more than you currently need them. Present yourself as the expert, not the salesperson to be avoided at all costs. Become known as the "go-to" person: the person others will seek out and put on their list of experts. When you become respected as the professional expert, success will follow.

We begin developing personal connections—relationships with other people—early in our lives. (Later in life, these connections become our networks.) Typically, the first social groups we join are family, neighbors, and schoolmates. Playing with siblings and cousins, and learning to meet new friends in the neighborhood and at elementary school help us develop the social skills that we will need later in life when we meet and work with others in the professional world. As you enter adulthood, social connections that you establish and nurture become more complex and have longer-lasting benefits. You may establish some of those lifelong personal connections during your college years or perhaps in your first "big" job.

Campus Connections

During your college years, you will have many opportunities to make connections with new people. Taking advantage of these opportunities allows you to perfect your skills in initiating and developing new and even lifetime connections. You can establish new friendships with roommates, classmates, social club members, special interest groups, academic organizations, competitive and intramural athletic teams, and many others. All of these groups not only encourage new social relationships but also foster opportunities for developing and improving leadership skills.

Chances to meet and work with new people abound on college campuses. The diagram in Figure 12.2 shows some of the many social networking opportunities on college campuses.

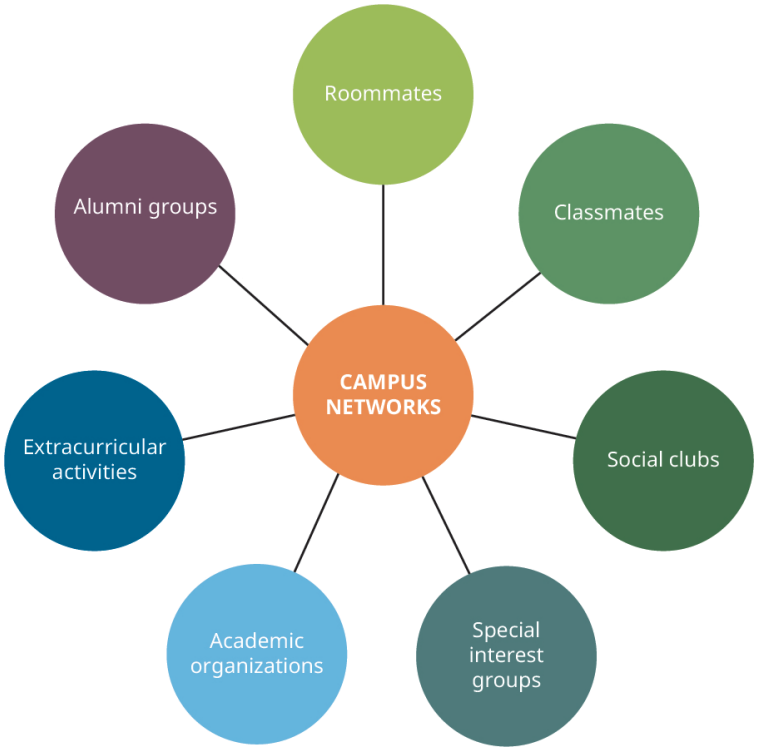


Figure 12.2 You can find many social networking opportunities through your college or university. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Your college or university is usually where you make the transition from student to professional. One method of learning to become a professional is through membership and leadership roles in academic or professional clubs. Leadership positions usually rotate annually. Academic clubs are formed around disciplines, departments, or professions. Professors, alumni, or industry professionals serve as sponsors and may provide connections to other industry professionals. Members learn the value of being active participants, discussing relevant topics. Fundraising or other special activities provide opportunities for developing leadership and organizational skills. Friendships and personal connections made in an academic club may become lifelong professional connections.

Honor societies are another type of academically oriented group, established to recognize the outstanding academic performance of students who have achieved a specific grade point average. Membership in an honor society brings with it the prestige of membership, opportunities for leadership roles, and access to professionals in many industries. Some honor societies offer scholarships for future studies in graduate school or study-abroad programs, which introduce members to students from other universities and countries with similar backgrounds and interests. Some honor societies open doors to conference memberships and presentations, and important access to other industry professionals.

Another type of collegiate organization is the special interest group. These groups may focus on social causes, promote and advance interests in the arts or other hobbies, or encourage participation in political, religious, or athletic events. Students from all disciplines and social backgrounds join special interest clubs. With such a broad spectrum of members, you have the opportunity to learn from many people from multiple backgrounds, expand your self-development, learn how to work with people who have different viewpoints, and potentially establish firm personal relationships.

Some clubs offer members the opportunity to perform or showcase their talent in a more relaxed and supportive atmosphere, or are centered around a personal interest. For example, a drama club for students not majoring in theater can offer a forum for participating in musicals and plays without the rigor demanded by the more structured academic program. Other groups that bring in nonacademic members include choral

groups, visual arts gatherings, astronomy clubs, and gaming societies. These groups provide opportunities for the maturation and perfection of the interpersonal skills you need for success in the professional world. You can develop key interpersonal attributes among friends and colleagues while enjoying a common activity or interest.

Social clubs—sororities for women and fraternities for men—provide other opportunities to expand your circle of friends, as these organizations focus on social activities. Although many social clubs concentrate strictly on "get-together" activities, you can learn and perfect acceptable public-protocol behaviors at formal events as well as mastering skills in organizational negotiations and compromise. A few colleges and universities are beginning to formalize clubs for online students, including access to and membership in campus-based Greek life. One of the first online Greek clubs is Theta Omega Gamma, founded in 2009 at the Florida Institute of Technology.

College groups have high turnover rates in their membership and involvement. This can make it easier for you to learn and perfect the skills necessary for establishing social and professional connections through constant repetition of introducing yourself to new people, learning their backgrounds, and describing your own. Learning how to introduce yourself and become acquainted with strangers is a soft skill that you can learn more easily early in life than in later years, and knowing how to develop a personal relationship with others will benefit you for many years to come. One unintended benefit is that mistakes can be quickly forgotten. If you make a social blunder one semester, many in the group will soon forget your faux pas, and new members will never be aware of it.

Perhaps the largest university club is one whose membership extends beyond graduation—the alumni association. Membership in alumni associations is higher among students who earned an undergraduate degree than among those with a graduate degree. Furthermore, members of the alumni association are more dedicated and loyal to their alma mater than nonmembers. Because of their commitment to past and current students, members of alumni associations have an automatic connection to other members. Loyalty is an important characteristic of active members of the alumni association, so bonding with them links you to established professionals who can help you in your new business. One way to connect with alumni is through LinkedIn, a social network of business professionals.

The campus setting—either traditional or virtual—is one of the earliest multifaceted environments to which you as a young adult will belong. Learning how to maneuver on the college campus and within the parameters of university culture prepares you for your future environment.

Nontraditional and virtual students also can benefit from their college campus experience. These students come from a variety of industry and professional backgrounds, and they are exposed to diverse operational methods and strategies during class activities or assignments. Furthermore, becoming personally acquainted with project team members opens opportunities for building connections that might be professionally beneficial in the future.

Institutions of higher learning have become fundamentally self-contained communities. Each one functions almost like a small city, with students mingling throughout the day with people at all stages of life, from multiple backgrounds, and in various roles. It is a great place to start building a foundation of personal contacts or enhancing your current portfolio of contacts before entering a competitive world.

ARE YOU READY?

What I Need and Who I Know

Create a table with two columns. On the left, list questions or issues associated with starting a new business, such as: How much money do I need to start? What licenses should I get? Do I lease or buy? Where do I find customers? Where do I find employees? How does payroll work? What kind of insurance

should I get?

On the right side, write down specific answers that you already know. For questions and issues that you can't answer, write down the name of a person you could ask to help answer that issue. If you do not know someone, who might help you get to the person who can give you an answer?

Local Organizations

Every community includes groups of individuals who have something in common. People group themselves together around shared beliefs, objectives, responsibilities, goals, or situations. Joining a local organization can place thousands of potential connections within your reach. Before seeking acceptance into a specific group, consider the type of group that fits your own personal and professional goals, and what you can contribute to the group's continuity.

An **open group** has a fluid membership; people may freely join or separate at any given time. Open groups tend to be informal, operate around a loose structure, and frequently focus on a personal or social cause. Open-membership groups include activities-oriented groups such as bridge clubs, scrapbooking groups, or photography clubs. Some open groups, such as Mothers Against Drunk Drivers (MADD) or People for the Ethical Treatment of Animals (PETA), focus on a specific topic or cause.

A **closed group** typically has either formal or informal criteria that you must meet before you can become a full member. Some organizations require sponsorship by a current member. Examples of closed groups include religious organizations, homeowners' or renters' associations, community performing arts groups, or sports groups.

Some community groups have features common to both open and closed groups. These **hybrid groups** have barriers or criteria that you must meet prior to joining, but those barriers are low, and prospective members can easily meet the criteria. Frequently, low barriers are an administrative feature to distinguish between participants who are serious about the group's activities and those who have an impulsive interest with no long-term commitment to the cause. Table 12.1 shows the differences among open, closed, and hybrid groups.

Open, Closed, and Hybrid Groups

Open Groups	Closed Groups	Hybrid Groups
• Fluid membership • Loosely structured, informal • May focus on personal/ social cause	• Membership criteria/ process • Structured • Formal purpose	• Low barriers to membership • Maintain barriers to ensure members are serious

Table 12.1

Groups that have a formal legal structure, an oversight board, and a professional management staff are more effective than those groups that are impulsively formed around a good idea. Professionally organized groups have skilled employees who set long-term goals and handle day-to-day activities. With the increase in structure and management, costs increase. To cover employee wages and benefits along with operational expenses of the group, many professional groups have membership dues and revenue-generating activities that members are expected to participate in. Some professional groups are self-supporting, whereas others are joint efforts among local and regional governments, universities, and the private sector.

One of the most successful private-public partnerships is the chamber of commerce arrangement. Local business entities establish a chamber of commerce organization to enhance the local community while expanding their own businesses. In some instances, the local government provides some type of monetary support for the chamber, but the chamber is neither an agency nor a function of government. For major community events, business members of a local chamber of commerce may provide their employees as volunteer staff who use their professional skills to organize and plan the event's activities. The community benefits, because a professionally managed event is held with minimal labor costs. The company receives publicity and exposure to potential customers within the local community at nominal costs. A close working partnership between the local chamber of commerce and government can produce outcomes that are mutually beneficial to local businesses and community citizens.

Trade associations are formed within specific industries and concentrate their efforts on issues and topics particular to one trade, profession, or philosophy. Functional trade associations include auto mechanics (Automotive Maintenance Repair Association, amra.org), architects (the Association of Licensed Architects, https://www.alatoday.org/), and marketing professionals (American Association of Advertising Agencies, aaaa.org). Education groups, such as the Association of American Educators, focus on defining competencies and qualifications for teachers and publicly advocating for standards and regulations that affect teachers. Specialized groups also form associations, such as the National Association for the Education of Young Children. Entrepreneurs who are looking for a franchise opportunity might consider an association that caters to franchisees, such as the International Franchise Association (franchise.org) or the American Association of Franchisees and Dealers (aafd.org). Companies interested in "going green" can join the Green Business Network at Green America (greenamerica.org/gbn/). The American Retirement Association (usaretirement.org) or AARP (formerly the American Association of Retired Persons, aarp.org) target retired individuals. Whatever the profession or industry, a trade association is certain to emerge to provide standards, training, support, and services to industry professionals and to be the industry's collective voice to legislatures and government officials in establishing regulations, laws, and licensure qualifications.

Businesses need a steady supply of new customers to replace former customers who no longer have an active relationship with them. The main purpose of *networking groups* is to help entrepreneurs gain new customers. These groups come in all kinds and sizes. Business Network International (BNI, www.bni.com) is dedicated to providing qualified referrals to members. BNI limits its membership to only one person per industry or profession. Members are expected to exchange contact information regarding a qualified potential customer.

Meetup (meetup.com) is a platform where people can meet others with similar wants and interests in an electronic or face-to-face engagement. Meetup's groups are social or professional, business or entertainment, or relational or transactional. Anyone can start a Meetup group if one doesn't already exist for their needs or interests. Each group's founders or members make the rules.

Whether a new entrepreneur needs a lot of support and guidance during the early stages of firm development, or a mature organization needs new potential customers, local organizations can provide an avenue to close connections and professionals who are committed to the local community and its businesses and people. As with all decisions, you must assess each opportunity in terms of the cost of membership and involvement in relation to the benefits you will receive over time.

Business Incubators

Business incubators are normally associations established by a consortium of local organizations such as a chamber of commerce, local banks and other traditional businesses, and universities to provide complementary support to startup businesses and those in the early stages of development. Services provided may include office space for rent at nominal charges; simple business expertise in accounting, legal matters, and marketing; and management support. Some incubators function as independent organizations, each with its own board of directors, whereas others may be stand-alone units of a university program. One of the best byproducts of being associated with business incubators is the communal contact with all the members'

connections. **Business accelerators** function much like business incubators. A key difference between incubators and accelerators is equity investment. Business accelerators usually make some type of equity investment in their members' companies. Because the financial commitment raises the stakes for accelerators, these organizations carefully screen their prospects and select only those businesses that have a reasonable chance of financial success. An entrepreneur who joins an accelerator can expect to receive a lot of support in exchange for a commitment to the organization and a share of the profits. Table 12.2 illustrates the differences between business incubators and accelerators.

Business Incubators and Accelerators

Functional Item	Incubators	Accelerators
Duration	One to five years	Three to six months
Cohorts	No	Yes
Business model	Rent; nonprofit	Investment; can also be nonprofit
Selection	Noncompetitive	Competitive, cyclical
Venture stage	Early or late	Early
Education	Ad hoc, human resources, legal	Seminars
Mentorship	Minimal, tactical	Intense, by self and others
Venture locations	On site	On site

Table 12.2

Service Corps of Retired Executives (SCORE)

The Service Corps of Retired Executives (SCORE) is a nonprofit organization based in Herndon, Virginia. SCORE partners with the federal Small Business Administration (SBA) and with retired executives from private businesses to offer education, training, and mentoring to small business owners. According to the SCORE website, it is the largest network of volunteer and expert business mentors, with around 350 chapters. Small business owners can attend a workshop or view training videos available on the website. Templates of financial statements and business and marketing plans are also available on the website. Perhaps the most valuable service SCORE offers is a one-to-one mentoring program that can align a mentor with the specific skills that the business owner needs the most.

LINK TO LEARNING

The SCORE website includes a wealth of online resources on starting a business (https://openstax.org/l/52SCORE) such as online courses and regional workshops. You can also fill out a form to request a mentor (https://openstax.org/l/52SCOREmentor) to help you start your entrepreneurial journey.

Government Agencies

Economic stability over the long term depends on a continual supply of new companies and organizations. A

business entity will close when the owner decides to cease operations or achieves the goals of starting the business. Sometimes a business is unable to sustain operations or is forced into closure by regulatory agencies or licensing requirements. Regardless of why businesses close, new businesses must continually arise to replace them and grow the economy. Governments at the federal, state, county, and municipal levels have established agencies and programs to encourage new business development, support new businesses in the early years of operations, and help young businesses mature to the point of self-sustainment. These include the SBA, Small Business Development Centers, Women's Business Centers, and HUBZones. Figure 12.3 illustrates some of the government agencies that assist small businesses.

Figure 12.3 Several government agencies exist to support entrepreneurs and small business owners. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Small Business Administration

One of the most popular agencies that helps businesses in the startup and early operations stages is the SBA. The SBA was established as an agency of the US federal government in 1953. In 2012, the SBA merged with the divisions of the Department of Commerce, the Office of the US Trade Representative, the Export-Import Bank, the Overseas Private Investment Corporation, and the US Trade and Development Agency. At that time, the leadership of the SBA became a cabinet-level position.

The purpose of the SBA at the macro level is to assist and safeguard small businesses, protect and defend a competitive environment, and fortify the national economy. At the micro level, the SBA helps individuals "start, build, and grow" their businesses and companies through direct counseling, educational seminars and webinars, and public-private partnerships with institutions of higher education and foundations with similar goals and objectives.

Some of the most important activities of the SBA revolve around finances for small businesses. The SBA provides education in finance and money management, and guarantees loans through private lenders for capital, inventory, and startup costs. A business must meet the SBA's qualifications for funding, but the application and approval of the loan is handled at the local level by officers of a local bank or other SBA-approved financial vendor.

LINK TO LEARNING

Are you looking for a lender to help you start your own business venture? The Small Business Administration's Lender Match page (https://openstax.org/l/52SBALendMatch) helps you find lenders.

Once a business is established and operating, ongoing activities are necessary to generate the cash flow to sustain the business. The SBA supports the ongoing operations of small businesses by being the liaison between small businesses and the federal government on bids and contracts. For fiscal year 2017, the federal government purchased a total of $105 billion[3] in products from small businesses.[4] However, becoming a vendor to the US government is not like selling to a private business or the general public. Free education and training materials are available from the SBA to introduce new businesses to the types of products that the government buys, the government's purchasing process for products and services, and the technical terms the government uses.

The SBA helps small businesses to maneuver through government purchasing processes through education, training, and support. Furthermore, the SBA has programs and funding operations that help economically disadvantaged individuals. These programs are self-contained within the SBA. Public-private partnerships or partnerships with universities or with other nonprofit organizations are also possible.

Small Business Development Centers (SBDCs)

Over one thousand SBDCs are funded through state grants with matching funds from the SBA.[5] Most SBDCs are located on the campuses of local colleges or universities. Others are located in entrepreneurial hubs or are connected with business incubator programs.[6] The coordinator of a local SBDC may be an employee of either the university or the organization that provides the office space. SBDC coordinators provide advice and information to small business owners at no charge because their fees and salaries are covered by the grants. Mostly, the coordinators provide information, steer business owners to other sources of information, and provide a context for making operational or strategic decisions.

Office of Women's Business Ownership

The Women's Business Center (WBC) is a program funded in part or in whole by the SBA to focus specifically on helping women start and operate their own businesses.[7] Women business owners face the same challenges that men encounter, but women normally must add the role of business owner to their list of other personal responsibilities. Also, women have more limitations in access to capital and other financial resources than men typically experience. The WBC can provide support and access to resources that are unique to women. The WBC is operated through independent and educational centers in most states.

3 Small Business Administration. www.sba.gov
4 Robb Wong. "New SBA FY17 Scorecard Shows Federal Agencies Award Record Breaking $105 Billion in Small Business Contracts." *US Small Business Administration*. May 22, 2018. https://www.sba.gov/blogs/new-sba-fy17-scorecard-shows-federal-agencies-award-record-breaking-105-billion-small-business
5 America's SBDC (Small Business Development Centers). n.d. https://americassbdc.org
6 US Small Business Administration. "Find Local Assistance." n.d. https://www.sba.gov/sbdc
7 US Small Business Administration. "Office of Women's Business Ownership." n.d. https://www.sba.gov/offices/headquarters/wbo

Veteran's Business Outreach Center (VBOC)

The SBA operates twenty VBOCs that focus on helping veterans and their families start and operate a new business.[8] A popular program of the VBOC is the Boots to Business program, which assists veterans making the transition from the military to the owner-operator role. Another program dedicated to veterans is the Service-Disabled Veteran-Owned (SDVO) Small Business Concern (SBC) program, administered through the Office of Small and Disadvantaged Business Utilization. To qualify for the SDVO SBC program, the disabled veteran must directly own and control, at minimum, 51 percent of the business and have input into the day-to-day operations as well as a long-term strategy. Requirements vary according to the legal structure that is chosen. Title 13, Section 125 of the electronic Code of Federal Regulations lists other requirements and restrictions to be recognized as an SDVO SBC.[9]

HUBZone

A HUBZone is a geographic location that has historically experienced low employment.[10] Many are also low-income areas because of limited transportation or educational opportunities. Through the HUBZone program, the SBA certifies and supports HUBZone businesses in acquiring government contracts and buying opportunities. Businesses that qualify may receive preferences in pricing. Qualifications for HUBZone designation are explained on the SBA/Government Contracting webpage. As of 2018, the federal government's goal is to award 3 percent of all federal contracting dollars to certified HUBZone business.

12.2 Building the Entrepreneurial Dream Team

Learning Objectives

By the end of this section, you will be able to:

- Understand key resource needs for entrepreneurial ventures: accountant, attorney, banker/financial institution, insurance agent, and industry expert
- Understand the value of developing a cross-functional team

Over the weekend of July 4, 1970, Casey Kasem started *American Top 40*, a radio broadcast that played songs listed in *Billboard* magazine's top 100 singles. What started as a simple compilation of popular songs that were played in ascending order of popularity ended thirty-nine years later on the July 4th weekend of 2009. When Kasem signed off for the final time, he gave credit to those with whom he worked. "Success doesn't happen in a vacuum. You're only as good as the people you work with and the people you work for. I've been lucky. I've worked for and with the very best."[11]

Jay Samit, a vice chairman at Deloitte Consulting LLP, specializes in exponential technologies, a revolutionary method of creating and manipulating information and data for learning, planning, and communicating. Working with multiple clients who each have their own unique limitations and face a wide variety of challenges, Samit and his colleagues at Deloitte devise tailored solutions that resolve each client's problems while overcoming each client's constraints.

Two professionals, two eras, two industries, and two vastly different technologies, but one concept: Entrepreneurial success is sustained by those around you. The concept that teamwork leads to individual success is evident in many other areas. All the great National Football League quarterbacks will tell you that they depend as much on their linemen as on their receivers. Pitchers in Major League Baseball need a very close relationship with their catchers, but the fielders are the ones who make most of the outs in the game

8 US Small Business Administration. "Office of Veteran's Business Development." n.d. https://www.sba.gov/offices/headquarters/ovbd
9 Electronic Code of Federal Regulations. n.d. https://www.ecfr.gov/cgi-bin/ECFR?page=browse
10 US Small Business Administration. "Office of the HUBZone Program." n.d. https://www.sba.gov/offices/headquarters/ohp
11 Cord Himmelstein. "Casey Kasem's Final Sign-Off." *Halo Recognition.* June 19, 2014. http://www.halorecognition.com/casey-kasems-final-sign-off

and can make a pitcher look very good. Surgeons need nurses and anesthesiologists, police officers need good partners as well as dispatchers, ground troops need air support, and airline pilots need fantastic ground crews and maintenance crews, and so on.

In reality, no one works alone. As an entrepreneur, you have the luxury of searching, soliciting, and selecting your own team (Figure 12.4). Entrepreneurial success depends on who is included on that team, and who is excluded from the team. In this section, we discuss advisors and cross-disciplinary teams.

Figure 12.4 Building the right team is crucial. (credit: modification of "Achievement American Analysis" by "rawpixel"/Pixabay, CC0)

Advisor: Accountant

One of the most important decisions that a business owner will make before beginning a new venture is hiring a good accountant (Figure 12.5). Businesses and their owners must be in sound financial health, or the company risks being closed because of financial difficulties. Just as doctors are trained to diagnose and treat health issues and symptoms, accountants are trained to recognize and treat symptoms and issues associated with the financial health of a company. And just as doctors can determine the health of an infant before birth, accountants can determine the likely financial health of a business before it begins.

Figure 12.5 A professional accountant's work is an important asset to any business. (credit: "Numbers And Finance" by "reynermedia"/Flickr, CC BY 2.0)

In the early stages of planning a business, the entrepreneur's personal financial history is the only financial picture that investors, creditors, vendors, or lenders can review. Therefore, it is essential to have a professionally prepared tax return in hand before you approach anyone about opening a new business. Having a professional accountant prepare and file personal tax returns establishes credibility and confidence in an aspiring business owner's financial decision making. Furthermore, when a business owner is willing to let someone else see all of their finances, it indicates to other professionals that the owner is willing to expose a very personal and sensitive realm—money management.

A highly skilled accountant will help any small business owner set up proper procedures that track cash

transactions and record financial activities. Accountants assist in creating a **pro forma**, a financial statement that shows how much and where monies will be collected and spent in the early stages of business creation. For an income statement, many of the figures used in a pro forma are hypothetical, a mere guess, but still are loosely based on historical industry or market data. Documenting debt service (explained in the following text) and other fixed expenses can be a simple task. However, projecting future sales with variable costs can clearly become complicated. Many times, approval for a loan or a building lease will depend on reasonable and sound projections of future sales and expenses. Too often, entrepreneurs overestimate income and underestimate expenses. An accountant frequently brings a reality check to the entrepreneur's wishful thinking and keeps income and expense projections credible.

Tax payments, especially payroll taxes, must be made on time to avoid large, costly penalties. Annual income tax for both a business—whether a sole proprietor, a partnership, or a corporation—and the individuals involved can become very complicated. Tax laws constantly change, but a good accountant will know how these changes will affect the company and how the company should respond. Often, the accountant's fees are lower than any penalty and fine assessed by tax authorities.

Besides tracking tax obligations, accountants can help identify trends within the financial picture. Many new business owners focus on profitability of the company and not cash flow. However, cash flow is far more important to the existence of a new company. **Cash flow** includes money collected by the business through revenue and funding versus money disbursed by the business through expenses. In other words, cash flow equals money in minus money out.

It's true that profitability can be affected by depreciation of assets, and an accountant can apply different depreciation rules to reduce profits and tax liabilities. However, the business must maintain positive cash flows to pay its weekly or monthly obligations. Although today's accounting software can easily generate cash flow reports, the expense of paying a professional pales in comparison to the money and time a business owner would spend in purchasing an accounting package, maintaining yearly upgrades, and learning how to run reports.

When a small business needs to expand or make **capital improvements**, major repairs or improvements that add to the life of an asset by improving its longevity, increasing its value or productivity, or extending its usefulness, it may be necessary for the business to take out a loan. Banks expect and require the company to have a professional accounting service prepare and file federal and state tax returns. Without the impartial eye of a professional accountant reviewing the financial health of the company, lenders may consider the business to be high risk and therefore would be unlikely to offer any loans. Expansion may be delayed or halted because lenders want to know if the company has properly managed its existing business before they are willing to finance additional operations and larger financial transactions.

Bankers will want to see not only income statements, balance sheets, and tax returns, normally for the past three years, but also cash flow statements over the same time period. If the company is functioning as a sole proprietor, LLC, or S-corporation (see Business Structure Options: Legal, Tax, and Risk Issues), the bank may require all individuals with management authority or ownership to submit copies of both federal and state individual tax returns plus personal net worth statements. Any investments outside the entrepreneurial company will need to be disclosed as well. All of these requests from lending officers at the bank indicate that they are looking for something. An experienced accountant will be able to interpret their requests, create documents that provide the information they ask for, and advise the entrepreneur on how to address the bankers' concerns.

Inventory management and debt service are other key financial areas where accountants can quickly identify problems that need attention and then offer advice to the entrepreneur. **Inventory management** consists of business operations that include managing the quantity of inventory units in stock, scheduling and cataloguing replacement inventory, organizing shelf location for unit storage, paying for inventory received, and processing, fulfilling, packaging, and shipping customer orders. **Debt service** is repayment of a loan,

including principal and interest.

Some vendors will require the same professionally prepared financial documents as bank loan officers do. **Creditworthiness**, or a lender's assessment of how reliable a company is in repaying a debt, is a valuable asset for a business. Being able to buy inventory on credit can greatly improve a company's marketing and overall performance. However, creditors have a different concern about a company's financial health. A vendor that sells inventory on credit may not be able to recoup a loss once the inventory is delivered to the new business. Banks can seize a building, equipment, land, and cash deposits, but creditors are not afforded that luxury. Therefore, creditors are skittish about releasing inventory to financially unstable businesses. Additionally, some businesses may owe inventory or personal property tax on inventory that is in stock.

Advisor: Attorney

If hiring an attorney to keep you out of trouble is expensive, hiring one to get you out of trouble will be exorbitant. Getting an attorney involved with a business in the very early stages, even in the idea development stage, can be a very good investment that will save a lot of legal expenses and protect the company's income. Areas of expertise and the ability to practice in certain areas of the law will vary among attorneys. Entrepreneurs must first determine what legal issue they need help with. Then, they would determine the cost of getting legal help as well as the cost of not getting legal help.

Hiring an attorney can be similar to hiring someone to do construction work on your home. Hiring a general contractor who can do most of the work will be cheaper than hiring a general contractor who subcontracts everything out to specialists. Some attorneys are generalists, with a practice that spans many areas in which the entrepreneur or small business owner will need help. Other attorneys are specialists who limit their practice to a few specific areas of expertise and refer clients with needs outside those areas to other specialists. Generalists are frequently less expensive than specialists, who charge higher fees for their in-depth knowledge of particular areas. In many situations, the entrepreneur or small business owner will not need a high level of legal expertise. When in doubt about hiring an attorney, the new entrepreneur can visit with a few members of their established network to get their input before making a decision.

One of the important questions to ask up front is how the attorney bills for services. Some may charge a flat rate for specific services, whereas others will bill at an hourly rate. Attorneys may add any additional costs and expenses to the client's bill. For example, when filing papers at the county courthouse to register a new company, the attorney may charge for copying, tolls to drive to the courthouse, parking, and mailing fees in addition to completing the actual registration papers. Knowing how the attorney calculates the bill—what fees will be charged and what additional costs will be added—is very important in deciding which attorney to hire.

Attorneys may be associates or partners of a firm. A large firm may have several equity partners and junior associates who are supported by paralegals. Larger firms offer a wider range of expertise and support for your attorney, but that extra help and larger resource pool are available at a higher price. On the other hand, an attorney who is in a stand-alone or small boutique firm may be less expensive but has fewer resources to tap into if necessary and may be unavailable for extended periods of time when actively working for other clients.

An attorney in your specific geographic area or community could be a valuable source of uncommon knowledge. Another consideration to think about when selecting an attorney is the location of their office. Office location may seem trivial, but attorneys in large office buildings probably have higher fees because they have higher office expenses. However, they are more likely to know other business professionals in their building, and those connections may be helpful at some point. Moreover, attorneys are often keenly aware of major developments in markets, such as real estate transactions and development, new roadways, and regulations.

Law practices can be divided into broad categories and specific areas. If you look at the landing pages of many of the country's prominent law schools, you will find only one commonality among all of them—they include specialized areas in their programs. Five broad categories of law that are relevant to the entrepreneur are

administrative, civil, corporate, criminal, and family law. For the entrepreneur, corporate and family law are probably the most important, because entrepreneurs may have family investors and personal assets at risk. An attorney who is skilled in family law would know how to protect the entrepreneur as well as family members if the startup business fails. If you are considering starting a business in a regulated profession, such as electrical repair, HVAC, or childcare, you will want an attorney familiar with the state's administrative code. Hopefully, a startup entrepreneur will not need a criminal defense lawyer. One of the first areas where you should consult an attorney is in determining the type of business structure. Any business structure has both legal and tax ramifications. A business attorney should help the entrepreneur select the legal structure that is best for the business, the industry, and the entrepreneur. Each legal structure—sole proprietorship, partnership, or corporation—has its advantages and disadvantages (see Business Structure Options: Legal, Tax, and Risk Issues). The attorney, in collaboration with the accountant, should help advise the entrepreneur about which legal form the business should take and why, not only for tax purposes but also for liability protection for the entrepreneur's personal assets and for ease of operations.

Other issues may arise during the startup stage that would require legal advice. These include branding, patents, trademark registration, and contracts. Will the entrepreneur be leasing a space or purchasing a stand-alone building? If leasing, who is responsible for the safety and well-being of employees and for protection of the equipment and inventory? In the excitement of getting started and making money, entrepreneurs may consider such questions to be unimportant. However, discussing these issues and making decisions before an adverse incident occurs can save the new business a lot of time and money. A good attorney will help keep the focus on important issues before they become catastrophic ones.

Another volatile area for new businesses involves employees and employment law. New business owners may also be new to management. Ignorance of employment laws can be very costly, especially if a disgruntled ex-employee seeks protection from state and federal agencies. Formulating company and employee policies is very important. Having an attorney help develop and use appropriate phrases will be a blessing that you will recognize long after the attorney has cashed your check.

LINK TO LEARNING

Visit the Society of Human Resource Management website with extensive resources for small business owners (https://openstax.org/l/52SHRMresource) on many topics related to employment law, including their Workplace Compliance Newsletter and articles on current news at their site.

Attorneys are professionally trained and educated to argue for their clients and to destroy the arguments of their opponents. Having a good attorney who confronts and debunks the naive beliefs and behaviors of the nascent entrepreneur can help that entrepreneur mature into a professional. As a new entrepreneur, you may not find it easy to leave behind the "employee" mentality and enter the "owner" mindset. The entrepreneurial lifestyle, responsibility, position, status, authority, and so on are foreign to the employee population. Therefore, you may need to undergo a trial by fire. A good attorney, like a good marine drill sergeant, has to destroy the old mindset and develop a new mindset within the new entrepreneur: It's all mine.

Although a good attorney is necessary to many aspects of a business, the entrepreneur also needs to set limits and not allow the attorney to tread into the owner's domain. Attorneys should focus on legal issues, not operational, strategic, or—under any circumstances—financial issues. Attorneys may be tempted to go beyond their realm to help out a client, but in reality, they should stay within the areas of law and regulation, and out of operational or strategic decisions. A good attorney will provide information, insight, and recommendations for managing risks, but will not bully a client by insisting on eliminating risks. An entrepreneur should always be ready to terminate the relationship with anyone, including an attorney, who seems to be interfering in areas beyond their domain.

Hourly rates for experienced accountants and attorneys can be frightening. Even if you readily acknowledge that the information and guidance provided by these two professionals is valuable, having the funds to pay for their work in the pre-startup stage of the business can be impractical. Successful entrepreneurs are known for solving problems, and at the very beginning of your own business, you can start solving your own business problems. The question is: How can I get professional advice at discounted rates?

Often, young lawyers and accountants who have just completed their education or received their license to practice will have very few clients. Likewise, those individuals who have been junior partners in larger firms and are branching out to start their own business will have limited clients. Those two scenarios are ripe for seeking discounted billing rates. Both the entrepreneur and the budding professional have a common need but few, if any, paying customers. Therefore, other business professionals or small business owners whose businesses are in the fledgling stage may be willing to offer special rates or payment terms.

Advisor: Banker or Financial Institution

All banks are not the same. Entrepreneurs need to select a bank or financial institution that can meet their current and future needs (Figure 12.6). Local banks that target a small geographic area are an excellent choice for small, locally centered businesses. Officers of the local bank may personally know local business owners, employees of the local businesses, and other key members of the local community. When a small business has a financial need, officers of the company may make decisions based on the reputation of the entrepreneur and the business. Sometimes a local bank will make loans and provide financial assistance with less scrutiny than an entrepreneur would face at a larger bank. For the small entrepreneurial business, banking is personal. Bankers like to see businesses in their backyard succeed.

Figure 12.6 Selecting the right financial institution for your venture will help create a path for security and growth. (credit: "Money Coin Investment Business" by "nattanan23"/Pixabay, CC0)

Large banks with multiple branches in numerous cities, states, or countries may be a better choice for banking services if your company will have broad geographic and financial needs. With employees, customers, and vendors scattered over a large market, a large company is better off having a bank that mirrors that broad reach. For example, if an entrepreneur starts a business in Hutchinson, Kansas, and banks with a local bank in Hutchinson, that intimate relationship between the business and its employees in Hutchinson probably works great. However, as the business grows into the Wichita and Kansas City markets, its banking services should expand too. Likewise, expanding a business across state lines should initiate a thorough review of banking arrangements to ensure that banking services will match the needs of the expanded business.

Large companies with multiple branches or employees over a larger area have bigger demands in banking products and services. They will be better off with larger banks that can respond faster and more effectively to market shifts or individual needs.

Advisor: Insurance Agent

Having insurance is a necessity for every business. Entrepreneurs, however, should not overlook the advantages of an insurance agent's knowledge and industry insight. Insurance agents ought to be in the entrepreneur's portfolio of industry professionals. Furthermore, insurance agents likely have other clients who

have been successful business owners for many years and may well introduce a new entrepreneur to seasoned veterans.

The insurance industry is a trove of data regarding almost every aspect of any industry or profession. All of that information is at the fingertips of your insurance agent. Agents can obtain information about any industry by running liability reports according to numbers compiled by the **North American Industry Classification System (NAICS)**, a standard used by US federal agencies to collect, analyze, and report statistical information about businesses[12]; the government provides a searchable database related to the codes as well (https://www.census.gov/eos/www/naics/). Every business in the United States is assigned a NAICS number, and insurance premiums are determined by the risk associated within each classification. You can obtain your NAICS number from your federal income tax return form 1120S or 1040 Schedule C. Knowing your business classification and the risks associated with it, your agent can assist you in reclassifying your business and lowering your insurance premiums, a potentially big financial savings.

Advisor: Industry Expert

Studies show industry expertise and skills are vital to successfully launching and operating one's own business. However, a lack of industry skills is not an impenetrable barrier to entrepreneurship. In fact, about 15 percent to 20 percent of successful entrepreneurs have no industry experience or have limited knowledge about an industry before entering entrepreneurship.[13] In the service professions, the entrepreneur's lack of skill is hardly noticeable, but technical industries have a higher success rate for entrepreneurs who already possess the skills needed in the industry.[14] Even if you do have those skills, you are more likely to succeed if you select industry experts who know the ins and outs of your profession (Figure 12.7).[15]

Figure 12.7 An industry expert can advise you and your team. (credit: "woman standing in front of sitting people" by Unknown/ Pexels, CC0)

With the industry professional doing the work, the new entrepreneur can focus on the business aspects of the operation while gaining industry experience and insight through hands-on exposure. As many first-time entrepreneurs find out in their first year, they will spend less time on the technical aspects of working in the business and more time managing and working on the business itself. Good collaboration between a technician and an entrepreneur increases the chances of long-term success.

12 Executive Office of the President Office of Management and Budget. *North American Industry Classification System.* 2017. https://www.census.gov/eos/www/naics/2017NAICS/2017_NAICS_Manual.pdf

13 Dawn R. DeTienne and Gaylen N. Chandler. "The Role of Gender in Opportunity Identification." *Entrepreneurship: Theory & Practice* 31, no. 3 (2007): 365–368.

14 Paul D. Reynolds and Richard T. Curtin. "Business Creation in the United States: Panel Study of Entrepreneurial Dynamics II Initial Assessment." *Foundations and Trends® in Entrepreneurship* 4, no. 3 (2008): 155–307. https://www.academia.edu/19325466/Business_Creation_in_the_United_States_Panel_Study_of_Entrepreneurial_Dynamics_II_Initial_Assessment

15 Jeen Wei Ong and Hishamuddin Bin Ismail. "Human Capitals Make Entrepreneur More Entrepreneurial? An Empirical Data from Small and Medium Enterprises in Malaysia." *Journal of Asia Entrepreneurship and Sustainability, 4*(1), 83–105. 2008.

As you begin searching for and interviewing professional advisors such as attorneys, accountants, or industry experts to make your team (Figure 12.8), you should follow a few fundamental principles. First and most important, you—the business owner—are the decision maker. Business owners, not members of the advisory team, reap the benefits of good decisions and bear the cost of poor decisions. Advisors inform, explain options and risks, share knowledge about others with similar situations and their outcomes, and make recommendations. An advisor's role is neither to make decisions nor to "sell" one particular viewpoint. Second, expectations and fees should be discussed before any actual work is done. Often though, a brief visit with a professional may be conducted at no charge so that each party can determine what is needed, whether the professional has the time and skills to meet the client's needs, and whether the client can afford the fees.

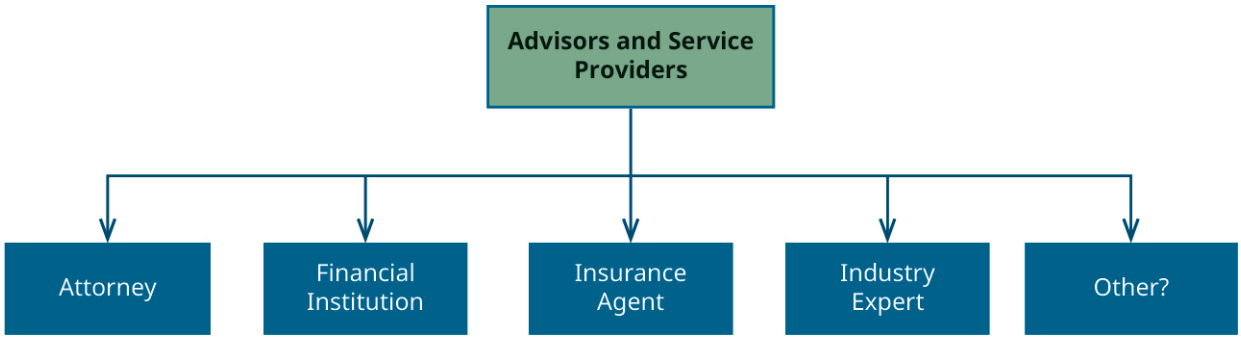


Figure 12.8 Your team should include advisors and professional service providers. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Another consideration is that all professionals have limitations. Licensed professionals such as attorneys and accountants are experts in their respective fields, but they are not necessarily experts in general business operations or strategy. Industry experts may be very knowledgeable in many aspects of the business, but they too have boundaries. Last, shopping for experts to advise you on crucial matters should be based mostly on competence and compatibility, not strictly on fees. Securing the services of a professional is a serious matter and should be treated as such. Yet, it is a business arrangement subject to traditional market factors such as service quality, affordability, accessibility, and change over time.

ARE YOU READY?

Who Am I? Who Am I Not?

Knowing what type of person you are can help you make good career choices. Knowing what type of person your potential employee is can help you make a good hiring decision. Create a list of personality traits that you think you possess. Ask close friends, family members, instructors, or others in your life who will give you their input about your personality. People with all types of personalities and traits can be successful entrepreneurs. The difference is in how you manage yourself and what you do to compensate for areas of weakness.

A reliable tool to identify certain personalities traits is the Sixteen Personality Factor Questionnaire (16PF) developed by Raymond B. Cattell. Visit the Sixteen Personality Factors Questionnaire site (https://openstax.org/l/5216PF) to take the 16PF questionnaire.

1. What factors are reflected that you expected?
2. What factors are revealed that you did not expect?
3. If your results show that you are timid, what might you do to overcome that when you become an entrepreneur?
4. If you tend to be a perfectionist, how might you manage the uncertainties of entrepreneurship?
5. Which traits or skills on your list match or are similar to those listed by your acquaintances? Which responses do not match?

Research the functional skills that you will need to start a business. Create a list of functional skills that you believe you possess. Ask close friends, family members, instructors, or others in your life who will give you their input about your business knowledge and skill. Then:

- Make a list of the functional skills you need for your new business. Add your name next to the functional skills that you have.
- Make a list of people you know who have different functional skills than you. Add their names next to the functional skills you do not have.
- Which of your friends and acquaintances appear on both the personality and functional lists? What do you think this means?

Building a Cross-Disciplinary Team

Rarely does an entrepreneurial venture start or function due to the effort of only one person. "Birds of a feather flock together" may be a popular saying, but it is a very poor organizational strategy for building a team to start a successful business. Diversity is a key feature of successfully managed organizations. Compatibility and collaboration are also important, as each employee is duty-bound to work with, support, and assist other employees when necessary. Having staff with complementary skills and who get along improves the likelihood of success for a new business.

A new restaurant provides a great example of how employees with assorted talents, expertise, and responsibilities are assembled to make a bustling organization profitable. For a new owner, the first hire is a manager. Hiring a good manager with experience means a larger payroll expense but produces better financial dividends over the long term. A good manager oversees all staff as well as all operational functions such as scheduling, buying, pricing, marketing, health code compliance, and business support functions. Perhaps the second key hire is the chef, who is responsible for creating the menu, distinguishing the restaurant from its competitors, and creating repeat customers who want high-quality, tasteful meals.

Front-house employees—the hosts/hostesses, servers, and bussers—play critical roles as the faces and voices of a restaurant. The first experience in a restaurant will leave a lasting impression, so those at the front are obliged to appear and act professional at all times. Servers, who have the most direct contact with customers, are the sales force of the business and the liaison with the chef. Servers' incomes depend on tips and turning tables, so it is essential for them to have tables cleared quickly and properly prepared for the next group. Servers, therefore, rely heavily on the bussers for those important tasks. In many restaurants, bussers receive a portion of the tips left for the servers, establishing a codependency between those two key positions.

Other positions in a restaurant are the bartender, dishwasher, custodian, payroll clerk, bookkeeper, and so on who must perform their duties accurately and efficiently. Subpar service in any one of these functions jeopardizes the viability of the restaurant. Every employee at each and every level is crucial, individually as well as collectively.

WHAT CAN YOU DO?

Make a List, Check It Twice

Building a team is a skill that you can learn. One of the first steps is to identify what tasks need to be completed and what skills are necessary to complete those tasks. People in all types of leadership positions build teams. Whether they are in government, large businesses, individual retail stores, small businesses, local athletic teams, or schools, leaders go through the same process of identifying tasks and the skills necessary to accomplish those tasks and then searching for people with those skills.

A key to learning is practice. You can practice building a team and then checking with people in charge of various organizations on how well you did. For example, select a local organization that you are somewhat familiar with—a local school, a community athletic league, a church, or a scout group. List the tasks and skills you think are needed to run the organization successfully. Then observe the organization in action. Make adjustments to your list. Ask to consult the manager in charge to see how well you did. How does your list compare with the actual operational structure? How is your list different? What did you overlook? How many people are doing more than one task?

After doing this a few times, you will begin to see organizations from a functional viewpoint. This is a skill any entrepreneur needs to have. What does my business do? What skills are needed to do those activities? Which person will I select to do those activities? If my first choice declines, who will be the backup?

Not only does a business need people to perform functional activities and day-to-day operations, but it also needs people to advise in other areas such as strategy, finances, management, staff, or legal. Should I have sales? Special promotions? Expand my product lines? Raise my prices? Get another investor for expansion? What are your long-term objectives? How will you achieve them? Having individuals you can talk to about your long-term goals is important. Surrounding yourself with those who can ask the right questions, confront you on weak areas, make you consider topics that you had not considered—all without judging you—is important if you have any plans to grow your business.

Create a second list of people you know and trust, a list solely for advising purposes. Members on this list can be from any industry as these are strategic questions, relevant across all industries and markets. They will help with your business strategy and structure, not operations.

A very common organizational structure for a new venture is the **flat organization**, consisting of family members, friends, or professional colleagues who take responsibility for different tasks. The bond that brings this group together in launching this new business is unlikely to bring to the table all of the skills, talents, personalities, perspectives, and viewpoints that can lead to long-term success. Therefore, expanding the team's human resources beyond the founding members who also manage the business is crucial. Although they do not have to become employees, access to them is as vital as having key personnel on your payroll.

An entrepreneur with a creative or big-picture mindset may not want to be bothered by day-to-day activities. If that is the case, then someone else in the business needs to be the analytical, linear-thinking individual who can process information and data to make sound decisions. After carefully considering a situation, collecting information, and studying all relevant facts affecting the business, a *problem solver* can recommend what action the entrepreneur should take, to whom should the tasks be assigned, when to implement the solution, and how much money to dedicate to solving the problem. In other words, the problem solver becomes a lead advisor to the entrepreneur, the manager. If the creative entrepreneur is one side of the coin, the problem solver is the other side. When those two minds work in tandem, good things can happen.

In contrast, an entrepreneur may be a functional expert or licensed professional who is obliged to perform the tasks personally—for example, an HVAC technician, dentist, or professional driver. In that case, a business manager is needed to run the business side of the company. Rules, regulations, and deadlines for business activities are beyond the functional entrepreneur's scope of interest, but they must be complied with accurately and in a timely manner, or the business may close. Like the creative founder who hires a day-to-day manager, a performance entrepreneur needs to hire someone dedicated to business functions.

Successful business owners keep careful track of metrics. They categorize and track expenses and analyze profit margins, production performance improvements or declines, employee attendance, and other measurable activities. Accurately interpreting the financial and operational performance of the company by the numbers provides the management team the information they need to make sound decisions. Having someone on the team with an aptitude for working with numbers is critical. The numbers must speak for

themselves. Personnel must remain inside the box when they draw conclusions from data.

However, solutions to problems are not always inside the box. Nonlinear thinking, also known as creativity, or "thinking outside of the box," is sometimes needed to solve problems (see Creativity, Innovation, and Invention). Creativity is the source of many new ideas, products, and processes. With companies facing shorter times of competitive advantage, the entrepreneur needs to be constantly reinventing both self and company.

Over time, as the business grows, the entrepreneur makes the transition from owner-operator of a startup through the small- business phase to being the owner-operator of a mature business. Entrepreneurs eventually need to make the cognitive shift from working in a state of ambiguity to performing methodically in a predictable environment. A business model where routine, repetitiveness, and predictability occur is more appropriate for established businesses because it brings stability and confidence to employees, customers, lenders, and investors alike. Using time-tested business methods and learning from previous experiences, an entrepreneur may avoid pitfalls that could doom a startup company in the early stages.

Every organization—whether a for-profit, not-for-profit, political, religious, or social organization—relies on revenue. For-profit businesses rely on sales as their main source of revenue. Nonprofit organizations, such as community organizations, political groups, or religious groups, depend upon donations, contributions, gifts, and grants. Some nonprofits, such as youth sports leagues, community performing arts groups, or scouting groups, bring in cash through fundraisers or through ticket sales for events. Governments customarily depend on various taxes as sources of revenue. Some local governments receive funds through block grants from their state and federal governments. Having multiple revenue streams improves cash flow and increases the prospects of long-term success.

Recruiting the person who will generate income for the organization should be a high priority during the earliest stages, perhaps even before formal operations, of the business. For a salesperson, grant writer, donor coordinator, or any other title referring to an income-generating position, a startup organization may have to offer a sweeter-than-normal compensation package. If the person can produce revenue and generate cash flow in excess of their total cost of employment, then he or she is worth the costs of higher commissions and bigger bonuses.

Trying to improve short-term financial performance and increase profits by reducing a key employee's compensation is likely to be detrimental over the long term. Losing a good sales rep may make the company vulnerable to losing very important and profitable customers. Failing to retain an effective grant writer could be the beginning of the demise, or at least a major downfall, for a nonprofit. Smart entrepreneurs pay their revenue producers appropriately, even if it means paying them more than the entrepreneurs pay themselves. As the old proverb states, "Never bite the hand that feeds you."

WORK IT OUT

Design the Business? Build the Product!

Stan enjoys building wooden patio furniture. He started his craft while in high school and worked with a cabinet maker during his college years. For the past twenty-five years, he has been a marketing and sales representative and sales division manager for a restaurant equipment manufacturer. Recently, his company was bought by an international company, and Stan's entire division was eliminated.

Stan was offered a new position with his current employer, but he would have to move to a new city. His family is against moving. His wife would have to quit her job teaching art in elementary school, his son does not want to miss his senior year of playing baseball, and his daughter has just started a new job at a nearby restaurant.

Stan decided to start his own business making customized outdoor patio furniture. He already owns most

of the equipment and tools needed to make the furniture. He has long-term relationships with his suppliers. However, his workshop in the backyard is not large enough to store raw materials or support an assistant. Besides, if he wants to make a living wage, he has to have a large place to handle the volume necessary to be successful yet safe.

Stan is comfortable with the technical aspects of making furniture. He knows how to do marketing and sales, including pricing and financing. What he is not comfortable with is everything else he needs to get the business started. Stan does not want to spend a lot of his retirement funds, so getting started with minimal expense is his goal.

What does Stan need to start his business? What type of professional help does he need and why? Who can help him?

12.3 Designing a Startup Operational Plan

Learning Objectives

By the end of this section, you will be able to:

- Identify the major areas of operations management (money, methods, machines, people, and leadership)
- Develop a checklist of operational needs

From the start, every entrepreneur needs a business plan. Your business plan will keep you focused on the very early stages of the business, when it is easy to be distracted. A written business plan can help redirect you back to your original idea.

Business plans can be divided into four different types: operational, strategic, tactical, and contingency. In this section, the focus will be on the operational plan, the activities that an entrepreneur-owner absolutely needs to do. The core business activities and how those activities interface with customers are key to a business's long-term success. Business plans are discussed in more detail in Business Model and Plan.

Operational Business Plan

In the early 1900s, the mechanical engineer and management consultant Frederick Taylor introduced *scientific management* techniques into manufacturing industries. Since then, operational planning has evolved into a major component of successfully managing a business. An operational business plan details the what, when, who, how long, with what, and how much of company activities. This type of plan may list specific functions: What the activities of the business are, when those activities occur, who is responsible for various tasks, how long each activity will occur, what tools or equipment are required, and how much time and funding are needed.

Operational business plans should be flexible enough to allow for challenges that will occur. Some changes must be made on a daily or even an hourly basis. Other changes may be necessary only occasionally throughout the year. However, the purpose of the operational plan is to provide direction and guidance. This way, everyone in the business knows their specific assignments, who is responsible for individual tasks, and when major events occur.

Creating a table or chart in an Excel or other spreadsheet format can help your planning and scheduling. Figure 12.9 illustrates how work station scheduling for a grocery store can be displayed in an Excel spreadsheet. Functional activities, specific job tasks, work shifts, or work stations are listed as column headings. Hours of operations are listed as row headings. Employees' names are entered into individual cells, showing who is assigned to each specific task or station. The table doesn't show every position, but enough positions are listed to give you an idea of how to use the same format for your own business.

Time	Manager	Front Counter	Produce	Dairy	Register #1	Register #2	Register #3
6:00	Keith	Jamal	Lewis	Justin	Gabriela		
7:00	Keith	Jamal	Lewis	Justin	Gabriela		
8:00	Keith	Jamal	Lewis	Justin	Gabriela		
9:00	Keith	Jamal	Lewis	Justin	Gabriela		
10:00	Keith	Jamal	Lewis	Justin		Shelby	
11:00	Monica	Eleanor	Lewis/Kate	Matt	Gabriela	Shelby	
12:00	Monica	Eleanor	Lewis/Kate	Justin/ Matt	Gabriela	Shelby	
1:00			Lewis/Kate	Justin/ Matt	Gabriela	Shelby	Eleanor
2:00			Lewis/Kate	Justin	Gabriela		Eleanor
3:00				Matt		Shelby	
4:00				Matt	Emily	Shelby	
5:00				Matt	Emily	Parvati	Jesse
6:00				Matt	Emily	Parvati	Jesse
7:00				Matt	Emily	Parvati	Jesse
8:00					Emily	Parvati	Jesse
9:00						Parvati	Kate
10:00					Carol		Kate

Figure 12.9 The table shows a schedule of work stations by hour. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

This type of schedule displays every functional position, the hours that each position has to be covered, and which employee is assigned to that function at what time. The manager can look at this schedule and know that each function has been assigned to an employee during a definite time period. If the work is not being completed, this type of schedule can help a manager make an informed decision about whether to hire more employees. Furthermore, if a problem occurs, the manager knows which employee(s) were working at that station when the problem occurred and can go directly to the employee(s) for information. When an employee is unable to fulfill a shift, the manager can change the schedule quickly to ensure that every task is being completed and every position is attended to.

Individual schedules and assigned work stations can also be displayed in a worksheet (Figure 12.10). This allows the manager to schedule an employee for the proper number of hours per week and helps budget payroll expenses. Employees know where they are expected to be and when they are scheduled to take lunch or dinner breaks, and the manager knows where the employee should be. When operational questions arise, the manager knows who was scheduled to be at the site and can go directly to that employee.

Time	Keith	Eleanor	Jamal	Lewis	Shelby	Jesse	Emily	Carol
6:00	Floor		FC	Produce				
7:00	Floor		FC	Produce				
8:00	Floor		FC	Produce				
9:00	Floor		FC	Produce				
10:00	Floor		FC	Break	R#2			
11:00	Floor	FC	Break	Produce	R#2			
12:00	Floor	FC	Break	Produce	R#2			
1:00	Floor	R #3	FC	Produce	R#2			
2:00	Floor	R #3	FC	Produce	Break			
3:00	Floor	FC	FC		R#2			
4:00	Floor	FC			R#2		R#1	
5:00		FC				R#3	R#1	
6:00		FC				R#3	R#1	
7:00		FC				R#3	R#1	
8:00						R#3	R#1	
9:00								
10:00								R#1

Figure 12.10 This table shows a schedule of employees by hour. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Using tools such as spreadsheets for scheduling and managing day-to-day operations brings organization and stability to daily operations. Managers know that each task has a person assigned to it, and employees know where they should be or what they should be doing throughout the day. Complex businesses with many employees and many functions need more planning and structure. Businesses with very few employees can be less structured. However, a written plan should list most tasks and activities that need to be accomplished, who will do them, and when.

LINK TO LEARNING

Many templates (https://openstax.org/l/52template) and spreadsheets (https://openstax.org/l/52spreadsheet) are available online that small employers can use to organize and schedule (https://openstax.org/l/52schedule) employees. Using key terms—for example, *employee*, *schedule*, *work station*, *template*—in popular search engines can produce multiple results.

ENTREPRENEUR IN ACTION

Scheduling Sounds Simple

Scheduling materials and parts for a fixed operation can be difficult. However, it can be even more challenging to coordinate your personal schedule with on-demand childcare needs near your workplace.

Avni Patel Thompson undertook this massive challenge when she started Poppy, an on-demand childcare service, in 2015.

Recruiting customers and employees for any business can be challenging, but when a company business model is centered around customers who have unscheduled demands and employees who want consistent income, the company needs a high-tech solution. Poppy was an app where parents could submit their request for a caregiver. The app's algorithm would then scan all available caregivers who were available during the window of time requested and were located reasonably nearby. After the app did its work, a staff member would make the final decision and confirm the caregiver with the family.

Unfortunately, Poppy succumbed to the overall market and economic conditions plaguing the child care profession and closed in December 2018, but the business model is an example of one way to solve complex scheduling issues.

Questions about Poppy and its scheduling procedures:

- How is an app better suited for this type of scheduling requirements than a full-time employee?
- What requirements are mandated for the customer? Employee? Company?
- Will a new application of technology overcome other economic and marketing factors?
- How reliable is the technology? What potential threats to the "established" method of scheduling are possible when technology is updated?

For tasks requiring attention on a monthly, quarterly, or annual basis, a simple organizer/calendar can be an excellent tool to help organize and remind you of what needs to be done and when. Tasks that you must complete on time throughout the year include payroll tax deposits and reports, insurance renewal applications, permits and license renewals, employee training and recertification requirements, and account billing to certain customers. A calendar also can help you schedule advertising and marketing activities. Some events occur regularly each year at the same time or within a known time frame. This can help remind you when to start your advertising and marketing campaigns.

You can plan for major maintenance and repair in advance or keep track of scheduled price increases, pay raises, adding or removing menu items, rearranging shelving for seasonal products, and major cleaning or maintenance activities.

As you start your business, you may need to make some adjustments to your operational plan. An entrepreneur might overlook factors that occur regularly. Or a new entrepreneur may have considered some factors to be minimally influential when in fact they may be significant. Entrepreneurs might give high priority to influences that never materialize. Once the business is open, customers and competitors may not behave as expected. Employees may have skill sets that were omitted from the written plan, or they may lack needed skill sets. Even a well-written operational plan will most likely need to be tweaked shortly after operations start. But if you formulate your plan correctly at the beginning, your functional operational plan should rarely need a complete overhaul.

Control

One element that should be included in every operational plan is control. In an operational plan, a marketing plan, an employee development plan, or any other type of plan used in business, control refers to the measurement of outcomes and an evaluation of the activities that led to those outcomes. The control element of a business plans answers the questions, "Have we accomplished what we wanted to accomplish?" and "Have we met our goals within the time frame that we wanted?" Without measuring performance outcomes, the entrepreneur does not know if the business is operating as expected, worse than expected, or better than expected.

If a business performs better than expected, the entrepreneur must consider if the original expectations were too low or if some other factor contributed to the better-than-expected performance. On the other hand, if the business performed worse than expected, two reviews must be conducted. First, why are outcomes less than expected and what can be changed to improve performance? Second, how do lower outcomes affect the viability of the business?

Comparing actual outcomes with expected outcomes is a form of internal comparison called **baselining**. Baselining is important because the entrepreneur must conduct a self-evaluation on what the business has done versus what it can or should do. An entrepreneur can decide to adjust a business's capability after conducting a baseline study. However, internal comparisons should be coupled with an external analysis, called benchmarking. By comparing your business with a close competitor's or with the industry average, you can get a better idea of how your business fits into the larger market.

Industry Benchmarks

If a basketball team scores sixty-eight points, do they win? If a baseball team scores four runs, do they win? If a soccer team scores five goals, have they lost? The answer to all three questions is simple: We need more information. Without knowing the other team's score, we don't know if a team has won or lost. There must be some other score for comparison; otherwise, the points scored are meaningless.

Similarly, businesses need to compare their individual performances with some external performance measurement. The comparison with an industry average, a leader within the industry, or a market segment is called **benchmarking**. Benchmarking allows a direct comparison of your company with the collective whole of the industry or market, or with an industry leader. By looking at several performance measurements, you can see if your company is performing at a level that will sustain itself over the long term or if your company's local market is atypical compared with another company's market. If the performance level of a startup company does not match the industry average or the industry leader, that does not mean that the company is poorly managed or cannot be profitable. Underperforming industry leaders indicates only that your company is not the same as those leaders. Frequently, benchmarking against a local market area is better than benchmarking against national leaders or the industry as a whole.

Operations Management

Operations management can be summed up in three words: Get it done! The foundation of operations management is the theory of scientific management. As we have seen, Frederick Taylor developed scientific management to introduce organization, scheduling, coordination, standardization, and cooperation among workers into the production process. Taylor saw a production plant as a large, multifaceted organization with many interrelated activities that should function as one large machine. The activities of each worker within one group had to be coordinated with other workers' activities within that same group. Each worker group had to be coordinated with other worker groups. Worker groups were clustered into larger cohorts. To keep materials moving through the manufacturing process, activities had to be planned, scheduled, and monitored.

Whether you are working in a manufacturing environment in which raw materials are converted into finished products or in a service environment in which customers receive experiences, these five components of operations management—organization, scheduling, coordination, standardization, and cooperation—must be the foundation your firm's activities. To have productive outcomes, the firm must have important inputs: money, methods, machines, people, and leadership (Figure 12.11). If any of these essential management elements are deficient or lacking, the company is probably functioning inefficiently and could be at a higher risk of failure.

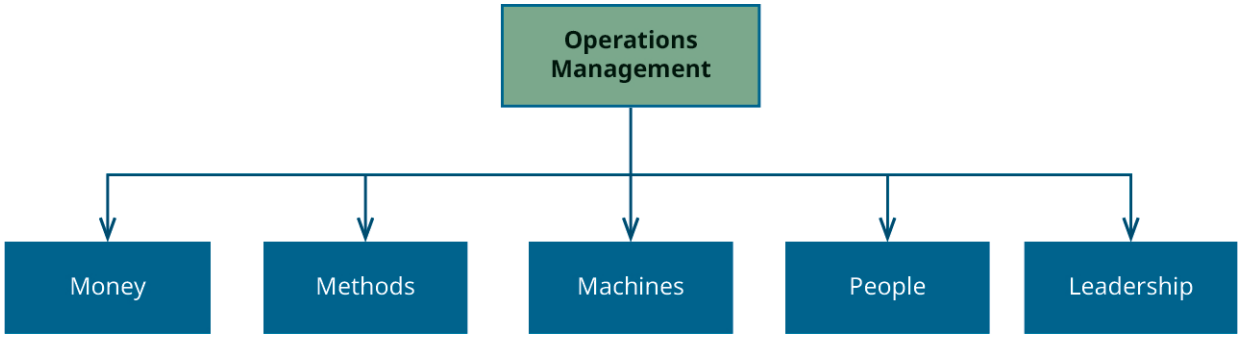


Figure 12.11 Money, methods, machines, people, and leadership form the foundation of operations management. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Money

Three terms—money, cash, and currency—are often used interchangeably, but each has its own distinct meaning and application. Money is any legal instrument that can be used in the exchange of goods and services. Money includes paper money or coins, but it also includes checks or money orders. In developing countries, money might be any physical item that is considered valuable to people wanting to exchange some goods or services. Most money, though, is in the form of cash.

Cash typically refers to physical money or currency, but it also includes deposits in an account (checking, savings, or certificate of deposit) at a financial institution. For example, customers can pay for their purchases with paper money, coins, checks, debit cards, or credit cards. The paper money and coins are taken to the bank for deposit. The debit card and credit card transactions are debited to the business's checking account by its bank. The cash balance of the business increases by the amount of the deposits, regardless of the form of the deposit. The cash balance is shown on the company's balance sheet and is the amount of money the company has available to pay its debts and obligations.

Currency is paper money or coins printed or minted, issued, and backed by a national government. Currency is divided into denominations or units in both paper and coin formats. With the expansion of international trade, along with the expansive movement of people among countries, it is important for an entrepreneur to know how global markets affect the value of money. Each national government decides what denominations of currency to produce. The value of a national currency is determined by the ability to exchange it for another national currency. Raw materials and supplies that originate in another country may increase in price significantly because of a decline in value of the US dollar or an increase in value of the country of origin's money. Likewise, raw materials and supplies may have a price decrease because of shifts in the value of money.

Knowing and understanding how international monetary policies and activities affect a local entrepreneur can be critical to long-term growth and survivability. You must have a clear understanding of projected costs of materials as well as enough funds available at the right time to meet your financial obligations.

Liquidity is a measure of a company's ability to meet its immediate and short-term (i.e., due within one year) debts and obligations. It's a way of describing how well you can cover your current liabilities using your current assets. When a company is liquid, it can meet its financial obligations on time, typically on a very short timeline. If the company pays its bills on time, the risk to lenders is lower, so lenders charge lower interest rates; insurance companies may set lower premiums; and vendors may offer cash discounts for early payments. Maintaining liquidity is vital to the success of a small business, as it may have limited access to other financial options.

Other sources of cash include credit accounts such as a line of credit, a company credit card, accounts payable, loans, or your own reputation and goodwill. A **line of credit (LOC)** is an agreement between a bank and a depositor in which the bank makes available a maximum amount of money the depositor can borrow at any time during the term of the loan. The borrower pays a fee during the term, whether or not there is an

outstanding balance, and also pays interest when there is a balance on the loan. All of these sources of cash are more cumbersome and involve more planning and preparation than liquid accounts. However, these nontraditional money sources are typically necessary for a new business owner in order to pay for business activities before the company begins collecting money from its own paying customers. Mismanaging these short-term debt accounts can easily become a burden on a small business. To better manage the financial obligations of the business, the entrepreneur needs to know which financial tools are available, how to use them, and which tool to use for which purpose. Financing is the use of money to conduct company activities. Payment sources for business activities and resources should match the life expectancy of the resource. Long-term debts—such as for land, buildings, equipment, and machinery—should be paid off through long-term financial instruments that are known as secured debt. Ordinarily, a loan used to purchase long-term assets will have a shorter life than the assets. For example, a machine that is expected to be useful for ten years should be financed with a loan that is paid in full in less than 120 months (ten years × twelve months). The purpose of long-term debt is to create revenue that exceeds the loan payment and interest. In this arrangement, the asset pays for itself by generating more cash than is needed to pay the principal of the loan, interest on the balance, costs to operate the equipment, and any additional insurance required or taxes assessed against the equipment.

Short-term or current liabilities, such as payroll, taxes, insurance, and all other operational activities, should be paid for through short-term cash resources. Most short-term payment obligations occur each week (payroll) or at least each month (insurance, rent). Short-term cash resources include sales, accounts receivables, down payments, and line of credit. Confusing long- and short-term financing strategies jeopardizes the financial stability of the company. Mismanagement of finances could create a situation in which the company is unable to pay its bills on time. When a company cannot pay its short-term obligations, it may not be able to operate much longer.

Managing cash collected and spent is one of the two most important responsibilities of the entrepreneur. A positive cash flow exists when cash received exceeds cash spent. A negative cash flow occurs when cash received is less than cash disbursed. All companies and organizations will experience a negative cash flow at some time. However, good managers will have a savings account or access to other cash in order to meet current financial obligations. What is important, though, is to have a positive cash flow over the long term.

Paying bills is not fun, especially when you have little cash to work with. Three popular methods of paying bills include credit, cash on delivery, and deposits on account. An entrepreneur's vendors may use all three payment methods. Likewise, the entrepreneur can use all three to collect monies from customers.

When bills are due and the company does not have enough cash to pay the bills or the timing is inconvenient, the company must use credit. Credit is the promise to pay later for something already acquired. Short-term credit may come with no interest charges or fees, such as accounts payable Entrepreneurial Finance and Accounting. Vendors will routinely allow established customers to take possession of inventory or products without paying for them at the time of delivery. Payment for products is due on a specific day or after a defined period of time.

Often, a vendor will offer terms of payment at the end of the billing cycle. For example, if the terms are net thirty, purchases that a small business makes during one month are expected to be paid for in full at the end of the next month. Payments made after the due date are subject to a penalty and interest. Sometimes a vendor will offer an incentive to pay early, such as a 2 percent discount if the payment is made in less than fifteen days.

Many startup businesses must make payments at the time of delivery, a form of transaction known as cash on delivery (COD). When the delivery is made, the delivery driver or the online agent will release the product to the customer once payment has been received. This payment method can burden a startup that does not have liquidity. On the other hand, a startup business can reduce its losses by requiring COD payments from its new customers, as it receives payments and has the funds to pay its own obligations.

For unique or specialized products, some vendors will require a deposit from the customer before the product is made. This deposit reduces the financial risk to the vendor for a custom product that may be difficult to resell if the original customer backs out of the purchase. It also provides cash to the producer, who needs to buy raw materials to make the finished product. For the startup entrepreneur, paying for products beforehand could strain the cash available for ongoing operations. However, if the entrepreneur's customers provide a down payment before the product is produced, the entrepreneur secures a noninterest loan from the customer.

All three of these payment methods are used in business transactions. Cash generated during each financial cycle must equal to or exceed the expenses paid during each cycle. Otherwise, the company may find itself without any money and be unable to afford to stay in business.

Methods

The study of how work is performed is called **ergonomics**. It involves designing, arranging, and coordinating tools and equipment so that the movement of workers who use them is safe and efficient, and products flow through the appropriate work stations in a timely and efficient manner.

Work methods are perhaps most important when complex machinery and equipment are involved. A progressive movement of products from one stage to the next should reduce the employees' time and effort, which reduces costs. Raw materials should be delivered to the location nearest where it will be used. Moving and storing large inventories at each point of assembly is easier and more efficient than storing parts at another location and moving them to work stations when they are needed. Timely delivery of inventory is equally important. Delivery of materials at the moment they are needed is called the just-in-time strategy. If component failure is detected, the point at which the part was assembled can be identified, and the deficiency quickly corrected.

LINK TO LEARNING

The just-in-time inventory system, developed in Japan during the 1960s and 1970s by the Toyota Motor Corporation, significantly changed production management. To develop a new system, Toyota took advantage of three crucial factors affecting post-war Japan: (1) limited resources, including cash; (2) value-added activities; and (3) reliance on business relationships that are mutually beneficial. They were able to avoid wasted investment and to effectively manage workloads. Watch this video on other common factors between startup entrepreneurs and Toyota (https://openstax.org/l/52FactorToyota) to learn more.

Service industries also apply the assembly line approach.[16] When workers become proficient at their tasks, they can perform the minimum actions needed to complete a task without sacrificing quality.[17] The assembly line approach has given birth to another ergonomic philosophy, lean project management.[18]

Many fast-food restaurants, such as McDonald's and Subway, use the assembly line approach to prepare food quickly and correctly. For example, in making hamburgers, one employee selects the bun, puts the appropriate meat patty on it, and then pushes it to the next worker, who may add onions, cheese, tomato, and lettuce before passing the order to the next station. Once the hamburger is complete, it is passed along to the last worker, who wraps the food and places it in a bag or on a tray.

When employees' tasks are limited to very few functions, repetition of movement makes their work quicker. This specialization results in higher quality. Specialization allows each worker to increase productivity, improve efficiency, and reduce mistakes. This division of labor has become a major component in Western economic

16 F. Abdi, K. S. Sohrab, and S. J. Seyed Mohammad. "Gleanlean: How to Use Lean Approach in Service Industries." *Journal of Services Research* 6 (2006): 191–206.
17 T. Levitt. *Production-Line Approach to Service.* (Boston: Harvard Business School Publishing, 1972).
18 G. T. Passwater. "Industrialization of the Industry." *BodyShop Business* 18, no. 11 (1999): 92.

models. Adam Smith first explained it in his work *The Wealth of Nations* (1776), using pin makers as his illustration. Smith theorized that reducing the number of tasks required of each pin maker would enable each worker to improve his efficiency of motion, resulting in both uniformity in quality and higher production levels.

This increase in quality and quantity of work increases the productivity and profitability of the worker. Collaboration among workers who work in close proximity occurs naturally. A weakness that materializes with one worker may be canceled out by an increase in another worker's efforts. However, human labor continues to be replaced by machinery and electronic instruments developed during the Industrial Revolution and the modern technology revolution. Nevertheless, human labor is essential on the production line, whether in creating or assembling products or performing services.

Machines

Beginning in the late eighteenth century, the Industrial Revolution shifted work from muscular power to mechanical power. Ever since, humans have used machinery to perform tasks greater than what they could achieve by themselves or using large animals. Machines provide consistency of work and higher volumes than human workers at lower costs per unit made. However, the initial outlay of cash for machinery can be large.

For a startup entrepreneur, purchasing machinery can be a difficult, time-consuming, and complicated task. First, one must look at the **total costs of ownership (TCO)**, which is the comprehensive cost of owning large capital items, including initial direct costs, operating direct costs, and indirect costs. Maintaining and repairing operational equipment is difficult, especially when production schedules demand the machine to be operational. Poor planning can be very costly, especially for a startup business, because your ability to produce and deliver products on time reflects on your reliability to both your customers and your employees.

When making equipment purchase decisions, you should consider all the costs associated with the purchase plus the machine's ability to produce income or lower costs. Such expenses include not only the purchase price but also delivery, installation and setup, calibration, and operational expenses. You should also consider the interest paid on the loan as part of the cost of acquiring the equipment, a factor that many new business owners overlook, but one that a good accountant should be aware of.

Hidden costs to major purchases periodically involve certain operating costs. Too often, new business owners focus on the purchase price, sometimes referred to as the sticker price, rather than on the total costs associated with equipment. Major equipment may require special delivery methods and other shipping costs. Once it is delivered to the site, it may have to be installed by skilled technicians. In some situations, the site flooring may need reinforcing to carry the new weight load, or the electrical supply may need to be upgraded to handle the necessary current. Local, state, or federal inspections may be required to obtain a permit to operate the equipment. Sometimes, liability insurance policies require inspections and permits in addition to government permits. All of these extra expenses add to the overall costs of acquiring the equipment. Many times, these expenses are considered sunk costs, never to be recovered in resale of the equipment or in producing more units.

Purchasing machinery and other major equipment is classified as a capital purchase or capital expense. A **capital expense** is a major purchase of a functional asset that is expected to last longer than three years or that still has financial value after being fully depreciated. Capital items, which include buildings, equipment, machines, and furnishings, are best purchased using borrowed funds so that the business can use its cash to pay for **operational expenses**, which are those associated with daily, ongoing activities of the business, such as inventory, office supplies, wages, insurance, and utilities. When an asset is used as collateral for a debt, the lender places a lien on the asset. The debt then becomes a secured debt, backed by the resale value of the asset. To ease the financial burden of major purchases, depreciation, a reduction in the value of an asset, is calculated as an expense on the income statement, which reduces taxable income and lowers taxable liability.

As a general practice, the payment schedule of a capital expense should be equal to or less than the life expectancy of the equipment. For example, a business may purchase an offset printer that is expected to last

twenty years and then finance it through a loan to be paid off before the twenty years are up. Although having the debt paid off before an asset is fully depreciated is ideal, in some instances terms of the loan may extend beyond the depreciation schedule.

Machines have limits to their performance. **Absolute capacity** is the highest volume of units that a machine can produce within a specified time period. **Operational capacity** is the number of units you can reasonably expect to be produced within a specified time period. The difference between the two is **operational reserve**. Because machines may need to be warmed up, materials loaded and unloaded, moving joints lubricated, belts and hoses checked and repaired, or other operational functions performed, machines cannot operate at absolute capacity for an extended length of time.

In calculating production levels, it is easy to overestimate the number of units produced. For an offset printer to work properly, paper has to be loaded, the rollers must be inked, feeder clamps may need adjusting, and one or two test sheets need to be printed to check for ink coverage and crispness of the image. All of these necessary activities take time, but they actually are unproductive. Because each business will have unique requirements and influences upon capacity, the best method is to track your own performance over time and calculate the average. Otherwise, getting input from one of your advisors or a friendly competitor would be sufficient for planning and budgetary purposes.

Machines cost money to operate. Improvement in efficiencies and in production volume is a major motivation in purchasing new equipment. You should consider the increase in units produced, operational costs per unit, decrease in waste, and improvement in quality of products. A grocery store owner who has an old freezer that still keeps food at the required temperature may decide it is worth replacing. Buying a new freezer, with all of the associated costs and improvements in efficiency, has no impact on the number of food items taken out of it and sold. Only the difference in actual cost of electricity between the two units can be considered. However, a die machine that reduces waste and improves the number of molded pieces produced per hour may be worth the investment.

All machines break down, usually at an inconvenient time and place. Trying to repair equipment when it is needed is like a road crew trying to fix potholes without shutting down traffic. Therefore, scheduling **production time**, the amount of time that a machine is actually producing products that are to be sold (also called *up time*), and **down time**, the time when production is not occurring due to repair, restocking inventory, or unscheduled work, are critical areas for management. A schedule of regularly planned maintenance that includes preventive repairs and inspections will reduce unexpected down time and equipment failures. Scheduling repairs before they are necessary keeps equipment running efficiently and smoothly, helps reduce costs over the long term, and allows for better management of expenses. Unexpected equipment failures not only interrupt operations but can delay delivery of products and services to customers. This can diminish your reliability and negatively affect customers' confidence in your trustworthiness, potentially affecting future sales.

Every machine will become obsolete at some time and will need to be replaced. Having the latest, greatest piece of equipment may be a temptation that your bank account cannot afford. Replacing equipment, whether major industrial equipment that needs professional installation or office equipment that can be set up by employees, is a critical decision. Too often, the criteria for selecting new equipment are the same criteria used to describe the old equipment's ability. Using old job requirements for new equipment may be acceptable in an industry that undergoes very few changes over a very long time. However, most industries change drastically and need up-to-date equipment.

WORK IT OUT

Generating Interest at Home

Going green is a popular trend today. One way in which power companies are going green is with wind-generated electricity. As of now, almost all wind energy programs are on a large scale, with wind farms consisting of hundreds of towers in rural areas. Stationing wind turbines at individual houses is currently impractical. Zoning restrictions limit the height of structures, costs exceed the benefits for homeowners, and potential sound and sight pollution are a concern for neighbors.

Those concerns apply to the current options for wind turbines. Can you think of other options that would be beneficial, cost effective, and socially acceptable in urban, residential areas? What physical properties would you need to consider? What type of functional capacity is needed? Can a household have more than one type of electrical circuitry for different types of needs? Do we need a product to generate electricity for today's household purposes? Or should we simply rethink household electrical systems entirely?

Entrepreneurs not only create new products and services, but also redefine the problem. They may need to make adjustments to resolve other environmental factors. For example, there was no need for paved roads before the advent of cars. Businesses that provide gasoline and repair work for automobiles were not necessary before the automobile became popular. The mass-produced automobile changed more than how a product was manufactured—it changed the way people moved.

Consider what happed with Avni Patel Thompson and her childcare business Poppy (Entrepreneur in Action: Scheduling Sounds Simple). What lessons can you learn from her experience as you look at home wind turbines? What similarities are there between a service-oriented company and a product-oriented company? What differences are there between the two? Do homeowners really want a new way to power their homes? What are the similarities of purchasing a major piece of equipment for a home and for a business? What differences are there?

Customer demands within an industry also may change significantly over time, just as a company's specific needs may shift appreciably. To meet external customers' new wants and the company's new internal needs, machinery with new technology and more advanced construction may be mandatory. You should plan three to five years into the future for major purchases of equipment, machinery, tools, facilities, and skill levels. The question is not "What do I need today?" but "What will I need five years from today?"

Trading in outdated equipment may have value that is not always recognized in financial documents. When sales representatives of major manufacturers need to meet quotas, they may be willing to offer a very positive financing plan to place their equipment in your business while removing a competitor's machine. But you should avoid making the mistake of ignoring your current vendor. Your current machine supplier may be very eager to keep customers and may offer to take your old equipment as a trade-in, which lowers the purchasing price of new equipment. Or your current supplier may be able to offer better terms than competitors or provide supplies as a reward for loyalty. All of these choices eventually lower both purchase and operating costs of new equipment.

To upgrade or keep the old machinery, to buy or lease, to sell or trade in, these are just a few of the questions that business owners contend with in making major purchases. Paying for big ticket items through vendor financing might be easier than borrowing from traditional banks. But when making major equipment purchases, always keep the professional sales representatives close. Their industry insight and knowledge could be more beneficial to you than the equipment itself. People are more flexible, more knowledgeable, and especially more valuable than machines.

People

Searching, recruiting, hiring, and supporting a workforce can be some of the most rewarding and frustrating interactions that a new business owner deals with (see the discussion on human resources in Fundamentals of Resource Planning for more information on hiring the right people for a business). Selecting the right people at the beginning can be the difference between succeeding or failing in the early years of a business. Many experienced business owners will say that waiting to hire the right person is better than hiring the wrong person now.

For the new entrepreneur, hiring people you know is appealing because it is easy, they are typically very amenable in the startup stages, and they share in the excitement of the new business. **Nepotism** is the hiring of family members and close friends, usually based on their relationship to the entrepreneur rather than on their ability to perform the job. Spousal support and involvement are important in the early stages of a business. Spouses routinely become employees of the new business, and there may be a difference in the outcome based on gender. Many times, a wife is an unpaid employee if her husband starts the new company.[19] Her commitment may vary from a sporadic involvement to a few hours per month or per week. Women entrepreneurs, however, are less likely to have their husbands participate in the business, especially if the husband is unpaid.[20],[21],[22]

Hiring other family members or friends because of their availability and personal commitment is enticing. Yet hiring family and friends just because they are willing and available can backfire and may produce more long-term harm than good. Sometimes hiring people close to you may discourage qualified candidates from seriously pursuing employment with your new business. Seeing that previous hiring decisions were based upon personal relationships is a discouragement to skilled personnel. Terminating employment of a family member can be truly difficult, especially if that family member is an immediate family member such as parent, spouse, child, or sibling. Difficulties within the family and the business are possible if the situation occurs. Moreover, failing to terminate a family member for cause will predictably destroy morale among nonfamily employees, especially skilled employees.

As a business is getting started, having someone is sometimes better than having no one. At other times, having no one is better than having the wrong one. Eventually, however, the ability to do a job supersedes who the employee is. Furthermore, traditional employees hired from the marketplace eventually will resent seeing more favoritism and leniency granted to family members than to nonfamily members. There is a stark difference between the integration of family and non-family members in a startup environment. The career path is usually short, with favoritism towards family members or longtime friends.[23] A delicate balance between family and nonfamily employees is difficulty to achieve, and new entrepreneurs do not need the additional distractions caused by rifts between family and nonfamily staff members.

Friends from previous employment, college, high school, or the old neighborhood are also popular sources for employees. In the early stages, the entrepreneur has so many issues to tackle and tasks to complete that hiring people they know seems like an easy solution. People build personal relationships through social and personal interactions, outside the needs of the new business. They establish friendships along personal commonalities such as attending the same school or being in the same club or on the same team, not along the subordinate-supervisor spectrum. A sure way to end a good friendship is to hire a friend who is unqualified for the job and place them in a supervisory role. Hiring a friend as a subordinate could lead to a confrontation that could cost the new entrepreneur the support of friends and family.

19 B. Ndemo and F. W. Maina. "Women Entrepreneurs and Strategic Decision Making." *Management Decisions* 45 (2007): 118–130.
20 J. Kirkwood. "Spousal Roles on Motivations for Entrepreneurship: A Qualitative Study in New Zealand." *Journal of Family Economics* 30 (2009): 372–385.
21 L. Philipps. "Silent Partners: The Role of Unpaid Market Labor in Families." *Feminist Economic* 14, no. 2 (2008): 37–57.
22 B. R. Rowe and G. Hong. "The Role of Wives in Family Businesses: The Paid and Unpaid Work of Women." *Family Business Review* 13 (2000): 1–13.
23 Dan Mcconaughy. "Family CEOs vs. Nonfamily CEOs in the Family-Controlled Firm: An Examination of the Level and Sensitivity of Pay to Performance." *Family Business Review* 13(2): 121–131. April 2004.

Every new owner must be willing to move past the startup phase and into the growth stage, where skills become more important than personal relationships. This natural progression in business maturity requires skilled workers to perform their tasks effectively. Those skills come at a price that may be difficult to match in the early stages of the business, but in the long run, skilled workers will produce more revenue than it costs to employ them. Also, customers expect more from established businesses than they do from an initial startup business.

Entrepreneurs must hire employees who complement them, not only in skills but also in personalities. In all of its various phases—from inception through startup, growth, and expansion—every business faces situations and obstacles that require an assortment of skills and talents to resolve. Some situations demand a strong, direct, or even confrontational approach, which can be comfortable for an extrovert. Other situations may need to be handled more softly and indirectly. An introverted employee who naturally is slow to react may take a passive approach that would be more appropriate in some settings.

A small business can strengthen its staff by hiring people with an assortment of backgrounds and experiences. The collective experiences of the whole staff benefit the business in ways that may not always be easily identifiable. Employees who fit together make a nice place to work and an enjoyable experience for customers.

Sales Force

In Building the Entrepreneurial Dream Team, the sales rep was discussed in the context of the value and importance of generating revenue and cash flow for the business. In this section, the discussion will be focused on the sales force as a component of the personnel working in a for-profit business. However, nonprofit organizations that are also dependent upon sales revenue, as discussed earlier, could apply the concepts as described as well.

Decisions involving a sales force may be some of the most critical decisions made, perhaps even more important than organizational structure and tax status. The sales force triggers the activities that generate revenue, which brings the business to life and sustains it. Without the sales spark, the business becomes a lifeless organization doomed to closure.

A sales force must fit within the overall operational and marketing strategy of the business. The product must be fully developed, its benefits to the customers clearly defined, and the primary target market selected before a sales force is needed. Furthermore, company goals of minimum production levels must be established, and a target revenue high enough to cover expenses needs to be calculated. It is imperative that each of these goals is patently understood and achievable for both the sales force and the company before the sales force is assembled.

The first consideration is identifying the stage of the company. Some entrepreneurs have a true startup business beginning from scratch, whereas others enter entrepreneurship through the purchase of an existing business with established customers and cash flow. The organization, structure, and role of the sales force will depend upon whether the business is in the startup, growth, mature, or decline stage). As the business progresses through each stage, requirements and abilities of the company change as does the external environment of the market.

Deciding whether to self-perform sales or outsource the sales function should be done very carefully and should include research into the tax implications and benefits of using employees versus independent contractors.[24] **Self-performing** involves the employees doing most of the work in a business. **Outsourcing** is the hiring of an outside company or third party to perform a specific task, job, or process, or to manufacture goods. Each option has benefits and limitations. The entrepreneur must consider many factors, ranging from financial strength to market knowledge to sales support capabilities. Hiring sales personnel as employees means the entrepreneur must use time and money to recruit, hire, train, supply with equipment and office materials, and regularly pay the sales force. Outsourcing the sales function to independent contractors may be a viable option, as the entrepreneur would have minimal upfront investment and they would be paid a commission only when they make a sale. Outsourcing is a preferred selection for businesses that are financially straining under cash flow, while self-performing sales is preferred for established, growing companies.[25,26]

Pay is always a touchy topic. Determining a person's compensation and income gives the entrepreneur a great deal of power and control over the sales force. It is a very important responsibility that ought to be handled with great care. Issues regarding pay affect not only the employees' or contractors' livelihood, but also the company's financial health and reputation. Furthermore, there are numerous laws and regulations, at both federal and state levels, that place the burden of doing it right upon the employer.

Sales force personnel who are employees must be paid with regular wages. Sometimes, a commission or bonus is paid if sales quotas are met. Regular wages, along with employer-matching payroll taxes and employee benefits, increase fixed expenses to the business. This arrangement may not be sustainable for a startup business. Yet the entrepreneur-employer can benefit from this arrangement by retaining control over employees' schedules and routines, earning loyalty from staff, and receiving immediate market feedback from the employee.

Outsourced or independent contractor sales reps are paid on commission. This arrangement adds a variable expense to the business, an expense that should only be recognized after a sale is made. In most situations involving outsourced independent contractors, the employer is not responsible for payroll taxes. A word of caution, though, to all beginning entrepreneurs: Determining whether someone is an employee or an independent contractor can become complicated. The burden of doing it right is on the employer. And not doing it correctly can add significant expenses to the business in the form of fines and penalties.

An important factor to contemplate when deciding what type of sales force to have is knowing your position in the market and your market's characteristics (Figure 12.12). If you are selling to other businesses, business to business, you will have to understand their decision-making processes and buying criteria if you expect to make any sales. On the other hand, selling direct to the consumer, business to customer, has a wholly different marketing strategy. For the nonmarketing entrepreneur, learning about marketing basics ought to be placed on the "to do" list so that conversations with sales force personnel will be productive.

24 C. Stephen Tobin, The Tobin Firm. "Understanding the Differences between Independent Contractors and Employees." Greater Houston Builders Association (GHBA). June 23, 2016. https://www.ghba.org/understanding-the-differences-between-independent-contractors-and-employees/

25 P. M. Madhani. "Managing Sales Force Compensation: The Strategic Choice between Direct Sales Force and Independent Reps." *Compensation & Benefits Review* 44, no. 2 (2012): 86–99.

26 P. M. Madhani. "Managing Sales Compensation: A Sales Force Configuration Approach." *Compensation & Benefits Review* 45, no. 2 (2013): 105–114.

(a) (b)

Figure 12.12 (a) In a business-to-business transaction, a farmer may sell their produce to a grocery store that in turn processes the food for consumer sale. (b) In a business-to-customer transaction, the producer sells their wares directly to consumers. (credit (a): modification of "spectacular salad bar at wholefoods HQ in Austin" by Kevin Krejci/Flickr, CC BY 2.0; credit (b): modification of "Honey" by Phil Whitehouse/Flickr, CC BY 2.0)

An additional market consideration is the sales territory. If you define territories by geographic markers, does each territory have the same potential number of customers? What is the variance in size and the distance from the home office? A similar set of questions arises if the sales force is established along product lines. How are the product lines alike? How are they different? When sketching out the sales force organization and responsibilities, it would be highly advantageous to receive input from potential sales reps or more experienced entrepreneurs who already know how to setup this division of your business.

Agreements made with the sales force must be honored, so make any agreement only after very carefully thinking through scenarios and obtaining insight from trusted advisors. The reputation of the business with employees and customers alike is at stake when employers do not honor agreements with employees, especially those employees who are the face and voice of the business to the market. If a sales rep, employee, or independent contractor decides to separate from your business, they could take their customers' business with them to their next place of employment. Although you could take legal action against a former employee who does this, the bottom line is that you have lost a sales rep and a customer. Avoiding that situation is best for everyone, especially you, the entrepreneur.

Getting the right sales people in place is critical. Having them work in a positive and effective environment is a necessity that cannot be ignored.

Leadership

Terms commonly associated with a leadership position include *owner*, *manager*, *supervisor*, *team lead*, *leader*, and *boss*. Many of these terms are used interchangeably, even though they have some minor differences in meaning, but normally one person will function as both leader and manager in a small business. Some entrepreneurs may be able to switch between these two roles flawlessly and fluidly, so that their followers and even they themselves are unaware that the roles are being filled simultaneously. Nevertheless, some traits and behaviors are associated more closely with leadership than with management.

A key difference between leaders and managers is their role in initiating action. Management is typically concerned with administering and directing an organization's activities. This includes planning, scheduling, coordinating, overseeing, and inspecting tasks performed by staff. The manager ensures that employees who have been hired to perform duties perform those duties as expected and at a level of quality and quantity acceptable.

A leader, on the other hand, instills within others a desire to perform. This is more of an internal motivation, a psychological approach, which the leader develops via words and actions. Like the results of the manager's approach, the results of motivation will be evident in the employees' performance. The difference lies within

the minds and souls of employees.

Employees will work for their manager because they are obligated to on the basis of assigned roles and positions of authority. Employees will work for a leader because they want to achieve the same goals and accomplish tasks to satisfy themselves as well as their leader.

You can find many lists that describe either characteristics or qualities of a good leader. Only a few have been included here. Descriptions of good leadership can be divided into the following categories: personality, competencies, locus of control, and style.

Personality describes the characteristics of a person as shown by their actions and words. Effective leaders typically are easy to get along with, have a positive attitude, engage others, and display self-confidence in their skills. When entrepreneurs begin looking for employees, working very closely together necessitates that they get along and enjoy each other's company.

Working for someone who does not know what they are doing can be very difficult, if not impossible. Therefore, good leaders know what their competencies are and are very good at what they do. Employees as well as competitors and regulators recognize high job-performance skills. Sometimes, a very skilled leader becomes an industry expert with a reputation throughout the industry and gives training at conventions, conferences, and trade shows. Good leaders are also keenly aware of the skills they lack and readily admit their incompetence in those areas. Hiring a skilled employee who compensates for your shortcomings is a high priority.

Locus of control is the belief that you have or do not have control over events that occur in your life. If you have an internal locus of control, you believe you have significant control and influence over events that occur in your life. An external locus of control—the opposing view—means you believe you have very little control, if any, over events that occur in your daily life. Effective leaders have an internal locus of control and feel certain that they influence and control events, situations, and people in their lives and, specifically, in their business. When crises arise, effective leaders take charge and begin making decisions to get control of events. Employees, customers, and others connected to your business will rally around you if they are confident that you can take control of the situation and directly deal with the challenges.

The three common leadership styles are autocratic, democratic, and laissez-faire. Each of these approaches to leadership is effective but can also be ineffective. The approach that works is best determined by the industry, structure, environment, and requirements of the job.

Autocratic leaders make decisions by themselves and view employees as subordinates who must follow instructions without hesitating or questioning. Autocratic leaders are necessary in situations where decisions are needed quickly, the leader is highly trained and skilled in the work requirements, and the outcomes can be very serious. Democratic leaders engage their staff and seek input before making decisions. This approach works well if the organization or industry is complex, many different departments or employees are affected by the decisions, and a broad range of information is needed to make good decisions. Laissez-faire leadership allows staff to work independently, mostly without supervision or direct input from the leader. This approach works best when the employees are highly educated and skilled, tasks among employees are not closely interrelated, and staff are self-motivated.

Leadership has been studied for many centuries, and the debate continues. You can find examples of good and bad leadership in many organizations including the military, sports, government, and business. Leadership traits are like hands in a poker game—they are all good and bad. The difference is the situation. For an entrepreneur, knowing the industry, the market, the competitive environment, the customer base, and the employee pool are starters for determining which leadership traits and style would be effective. If you decide you are not matched to the environment or situation, then you could engage someone who does possess the traits and skills that better match your current needs.

Operational Needs

When starting your business, the first question you need to ask is whether anyone wants to buy your product or service. Creating a new product or service is easy. In fact, 70 percent to over 95 percent of new products introduced every year are classified as failures.[27] With more than 30,000 new products introduced every year, you could reasonable guess that between 21,000 and 27,000 are failures.[28] On the contrary, only 5 percent to 30 percent of new products are successful. So the question is valid: Will anyone buy my product or service?

With such a low success rate, you will need to conduct careful research and small trial runs to determine the viability of your new products. You need to know not only whether anyone will buy your products but whether customers will pay your price, so that the business can make a profit, or at least break even. You need to ask these two very important questions up front, because if the answer to either one is "No," you have no need to do anything else.

A second series of questions that you need to address focus on the location of the company's operations. Where will you locate your business? Will you rent or buy a building or facility? Does your facility need to have easy access in a high-traffic area? Or can it be in a quieter area, where costs are lower? In addition to access and costs, will your business be located within a competitor's influence? It would be unfortunate if you negated all the positive factors of your great product and viable business plan by selecting the wrong location.

Besides deciding on a proper location, you also need to consider the size of your facility. Selecting a structure that is too small from the very beginning may handicap any growth in the early stages of your business. Having to move to a larger facility soon after beginning operations could be detrimental to your operations. On the other hand, selecting a facility that is too large puts pressure on cash flow, as you will pay rent or a mortgage for an unproductive building space. Finding the balance between "big enough to grow into" and "small enough to afford with low sales" is a predicament faced by many business owners, whether new entrepreneurs or seasoned veterans.

You will need to make similar decisions about furniture, equipment, and furnishings. These items are available for purchase or lease. Sometimes a lease is better, as the initial payments may be lower but over time, buying equipment and furniture can help improve cash flow once the items are paid for. However, deciding on how much, what quality, and what size can be difficult. Good equipment sales representatives can be a big help in making equipment decisions.

To get started, you will need to determine the proper inventory levels. How long is the shelf-life of your inventory? Some products have a long shelf-life, whereas others may perish quickly. Ask yourself "How much do I need?" and "When will I need it?"

Before beginning a business, you may need licenses and permits. Buildings must be inspected and approved prior to occupation for business activities. Building permits may require electrical, plumbing, HVAC, and structural inspections of building systems and physical features. Accounts for water, gas, and trash pickup must be made prior to occupying a facility. Table 12.3 summarizes the operational needs you should consider when launching a venture.

Checklist of Operational Needs

Table 12.3

27 M. Emmer. "95 Percent of New Products Fail. Here Are 6 Steps to Make Sure Yours Don't." *Inc.* July 6, 2018. https://www.inc.com/marc-emmer/95-percent-of-new-products-fail-here-are-6-steps-to-make-sure-yours-dont.html
28 J. Schneider and J. Hall. "Why Most Product Launches Fail." *Harvard Business Review.* April 1, 2011. https://hbr.org/2011/04/why-most-product-launches-fail

☐ Item 1	Determine the legal organization of your business for tax purposes (sole proprietorship, partnership, or corporation). Select the legal structure of your business for operations and management control [limited liability company (LLC), general partnership or limited partnership, C-corporation, or S-corporation].
☐ Item 2	Decide on a name for your company. The company name becomes its official legal name for federal and state purposes. A corporate name can be anything that is currently not in use by another company. A trade name may be different from the official name. The trade name should reflect the product or industry.
☐ Item 3	You and any other principals of your business write and approve articles of incorporation, bylaws, or management agreements.
☐ Item 4	File organizational papers with the secretary of state (SOS) or its corresponding office in the state in which the company is founded. The SOS returns the registration or charter documents to the company.
☐ Item 5	You and other principals make cash payments to the company for starting the bank account.
☐ Item 6	Obtain a federal employers identification number (FEIN) from the Internal Revenue Service. This is the company's federal tax number for income and payroll taxes and filings.
☐ Item 7	Obtain a state employer's identification number from your state's employment commission. This is the company's state tax number for filing unemployment and sales tax reports and payments.
☐ Item 8	Be sure your trade name or assumed name certificate is filed and approved by the appropriate county and state offices if it is different from the corporate name.
☐ Item 9	Secure your business phone number, website, email, and domain name. Order your business cards.
☐ Item 10	Open a bank checking account with the appropriate corporate and trade name, authorized signers on the signature card, and all other documents that your bank requires to open a business account. Order debit cards or credit cards as necessary. Deposit your startup funds. Set up and test your business deposit processes.
☐ Item 11	Both you and your officers and partners sign agreements regarding the business.
☐ Item 12	Buy or lease your office space. Your local or city government will grant you a certificate of occupancy to occupy the building. You may need additional inspections before final approval: building, fire, health, and plumbing.
☐ Item 13	Open utilities, water, electric, gas, garbage, and phone accounts.

Table 12.3

☐ Item 14	Post required notices in a prominent place according to regulations. Common locations are near the timeclock, break rooms, front cash register, or other public location.
☐ Item 15	Apply for and post as required your license for business, either by federal, state, county, or municipal government.
☐ Item 16	Apply for and post as required your license and permits for employees or specific types of products or services.
☐ Item 17	Obtain insurance for your building, liability for business, and worker's insurance. Some states allow businesses to exempt themselves from workers' compensation with proper notice to employees.
☐ Item 18	Order and install furniture, office equipment, shelving, and so on.
☐ Item 19	Order your inventory and make your product list with pricing, price sheets, or menu boards.
☐ Item 20	Recruit and hire your employees. Training and certification may be required for specific functions such as bartenders, cooks, drivers, forklift operators, or first aid personnel. Be sure employees' training in specific job functions is completed before opening. The first day of operations is typically a low-key event to ensure that everything is working as planned and that your staff know their roles and responsibilities. This gives you time to correct any weaknesses or shortcomings before the general public is aware that your business is open.

Table 12.3

Set the grand opening several days to a few weeks after the actual opening of business. Invited guests may include investors, city officials, family members, special customers, former employers, business neighbors, and competitors.

LINK TO LEARNING

Forbes magazine has various resources such as this step-by-step guide for entrepreneurs (https://openstax.org/l/52StepEntrepr2) and this list of eight steps for entrepreneurs (https://openstax.org/l/52StepEntrepr3) on starting a new business. The federal SBA list of steps (https://openstax.org/l/52SBAsteps) is also available. Review each list. Which one best matches your entrepreneurial situation?

Key Terms

absolute capacity highest volume of units that a machine can produce within a specified time period
baselining internal comparison of actual outcomes with expected outcomes
benchmarking comparing one's own company's performance with an industry average, a leader within the industry, or a market segment
business accelerator organization formed by an alliance of business professionals who assist entrepreneurs in their startup or early stage businesses in exchange for an equity investment in the entrepreneur's company
business incubator organization formed by a consortium of established professionals or organizations assisting startup or early stage businesses that provides office space, financial support, technical support, or advisors whose specialized skills in management and marketing complement the technical talents of the entrepreneur
capital expense major purchase of a functional asset that is expected to last longer than three years or that still has financial value after being fully depreciated
capital improvements major repairs or improvements that add to the life of an asset by improving its longevity, increasing its value or productivity, or extending its usefulness
cash flow money collected by the business through revenue and funding versus money disbursed by the business through expenses
closed group formal, structured group of individuals who have a strict process or specific criteria that applicants must meet before being accepted as members
creditworthiness lender's assessment of how reliable a company is in repaying a debt
debt service repayment of a loan, including principal and interest
down time time when production is not occurring due to repair, restocking inventory, or unscheduled work
ergonomics study of how work is performed
flat organization organizational structure where owners, executives, or key decision makers interact directly with staff at all levels, with very few if any mid-level managers
hybrid group group of individuals who have a loose and flexible set of criteria for membership and function within a very broad set of guidelines; certain criteria may be required of regular members, but guests are frequently accepted with no long-term commitment expected
inventory management business operations that include managing the quantity of inventory units in stock, scheduling and cataloguing replacement inventory, organizing shelf location for unit storage, paying for inventory received, and processing, fulfilling, packaging, and shipping customer orders
line of credit (LOC) agreement between a bank and a depositor in which the bank makes available a maximum amount of money the depositor can borrow at any time during the term of the loan; the borrower pays a fee during the term, whether or not there is an outstanding balance, and also pays interest when there is a balance on the loan
liquidity measure of a company's ability to cover its immediate and short-term (i.e., due within one year) debts and obligations
nepotism hiring family and close friends because of personal relationships rather than for their skill sets
networking process of establishing and maintaining bilateral relationship with other people to exchange information, ideas, products or services, and money
North American Industry Classification System (NAICS) standard used by US federal agencies to collect, analyze, and report statistical information about businesses
open group informal, loosely organized group of individuals who have no formal process for joining or leaving the group, and who focus on a specific activity or social cause
operational capacity number of units that can reasonably be expected to be produced within a specified time period
operational expenses expenses associated with daily, ongoing activities of the business, such as inventory, office supplies, wages, insurance, and utilities

operational reserve difference in unit capacity between absolute capacity and operational capacity
outsourcing hiring an outside company or third party to perform a specific task, job, or process, or to manufacture goods
pro forma financial statement that shows how much and where monies will be collected and spent in the early stages of business creation
production time amount of time that a machine is actually producing products that are to be sold; also called *up time*
self-performing when employees do most of the work in a business
total cost of ownership comprehensive cost of owning large capital items, including initial direct costs, operating direct costs, and indirect costs
trade association group of companies or employees of companies in a specific industry, business structure, or social cause

Summary

12.1 Building and Connecting to Networks

Entrepreneurial networking is interacting with other people who have a common interest that eventually leads to the exchange of goods and services for payment. You must be comfortable approaching, talking to, and working with other individuals in order to build the circle of associates, colleagues, and professionals that you will need to start and operate your business. Likewise, you must be willing to offer your expert knowledge and professional skills to others. A good networker supports others in the community through sharing information and passing along personal introductions to expand everyone's networks.

People do business with those they know and trust. Connecting with people in face-to-face meetings through group membership is valuable but so is the power of social media avenues dedicated to professional connections, exchange of information, and support, such as LinkedIn. Networking is not easy or free. Some of the costs other than money include time, fear, and dedication. Because entrepreneurs are willing to invest the money, spend the time, take the risks, and stay with it, economic success for communities and individuals is possible.

12.2 Building the Entrepreneurial Dream Team

The idea that entrepreneurs are isolated loners and solo performers in the market, doing everything themselves, having absolute self-reliance, is a myth. Successful entrepreneurs quickly seek outside advice, rely on professionals in supporting areas, and are very good at establishing and maintaining personal relationships with key individuals. Perhaps their essential skill is their ability to identify, connect, and trust those individuals who can help them succeed in their personal entrepreneurial journey.

Whatever the entrepreneur can do best is what they should focus on doing. Other required tasks can be assigned to employees, service providers, or consultants. However, it is very important that the functions having a direct effect on customers and sales are performed proficiently, because that is what generates revenue for the company. Entrepreneurs must assess their own skillset and willingness to execute tasks, then identify employees and outside professionals to fill in any gaps.

12.3 Designing a Startup Operational Plan

Success is best defined as achieving what you want. Without some kind of plan, you can never be successful. Whether they are entrepreneurial owners or management employees, business managers need to have a written plan so that everyone can be certain of what tasks are needed, who is assigned those tasks, and when those tasks are scheduled. Recording and tracking financials is imperative in any business. Knowing where money is coming from, to whom it was sent, how much, and why are crucial to being a responsible business professional.

Without a business plan that encompasses all major aspects of your business, you may find yourself without a

business. If that happens, you may very well ask, "How did I end up here?" Unfortunately, the answer is likely to be, "I don't know." On the other hand, a successful business professional can look back and say, "I did this, and this is how I did it."

Review Questions

1. What is "networking"?
2. What types of networks are created in a business relationship?
3. What types of organizations on college campuses can provide opportunities for building social networks?
4. What are some opportunities for you to develop the skills you need to establish personal relationships with people that you do not know?
5. What is most likely the largest social group connected with a university? Why is being a member of this group valuable?
6. How do government agencies at all levels support entrepreneurship?
7. Who selects the entrepreneur's team? Why is this important?
8. Why is selecting an accountant a critical decision?
9. For the startup entrepreneur, what finances are considered relevant?
10. What are some differences between large banks and small banks as they relate to an entrepreneurial startup business?
11. What resources do insurance agents have to gain industry specific information, especially about liability, operations, and challenges?
12. What relationships are possible for sales reps and small, startup businesses? What are the benefits to each?
13. Why is a functional or operational business plan necessary?
14. Many operational business plans provide some very specific steps to take and sometimes are very detailed. What are some situations in which rigid schedules can be a hindrance or a deterrent to effective operations?
15. What simple tools can an entrepreneur use to get organized and do what is necessary throughout the month or year?
16. What is benchmarking? Why is it important? What are some limitations of benchmarking?
17. What is cash flow?
18. What is credit? What are some "instruments" of debt?
19. What are some differences between "absolute capacity" and "operational capacity"? Why do they need to be distinguished?
20. Explain nepotism. Why might it beneficial to an entrepreneur? Why may nepotism be detrimental to an entrepreneur?

Discussion Questions

1. How are social connections made in early life the same as those made on the college campus? How are they different?
2. What are some benefits of professional associations that are not available from government agencies or

departments?

3. How is the role of government agencies with regard to entrepreneurship different from the roles of industry and trade associations?
4. How does the SBA help aspiring entrepreneurs?
5. Why is it important for government programs to offer grants to organizations, both public and private, to educate and assist entrepreneurs at no charge?
6. What are some risks associated with surrounding yourself with others who are similar to you in background? Industry experience? Education? Age? Personality? Ability to process information?
7. If the figures on a pro forma are hypothetical, then why go through the exercise of creating a document with fake numbers?
8. What are some disadvantages of having licensed professionals such as accountants and attorneys offering advice to an entrepreneur?
9. A young, very creative, artistic woman wants to start her own graphic design business. If she is out of the office looking for new clients, she is not producing any work that generates income. What are her options?
10. What can happen if a new business does not have any kind of business plan? What if the business plan that was originally written is not effective after the business starts?
11. Why are schedules important? If the new business owner keeps a schedule only in their head and does not write it down, what might be some weaknesses of that idea?
12. Why is benchmarking relevant? What are some conditions in which benchmarking against national figures would be less accurate? How would you find information regarding benchmarking?
13. Why is cash flow more important than profit? If a company does not have enough cash, what are possible ways for it to get more cash?
14. Why is money management so important to a business? What are the consequences if money is mismanaged?
15. When is the assembly-line approach appropriate in service-oriented businesses? What are the benefits of using the assembly-line approach in this type of work?
16. How does the term “division of labor” apply to the concepts of “jack of all trades” and “specialist”?
17. What is the difference between capital expenses and operational expenses? What type of financing should be used for capital expenses? Operational expenses? Why?
18. Why should hiring the right people take precedence over buying the right equipment?
19. How do the needs of a small business and its founder change from the startup stage to the growth stage?

Case Questions

1. Smart phones are everywhere today. You probably have one nearby right now. However, access to landline phone service has not been complete for very long, and wireless service is not as widespread as many people might think. The first phone lines (landlines) connected Boston and Somerville, Massachusetts in 1877. The last town in the United States to receive landline service was Mink, Louisiana, a small community 100 miles south of Shreveport, which received landline service in early 2005. Check any major US wireless carrier, and its maps have gaps in service. Building networks of any kind takes planning, money, and time.
   A. What are some similarities between an entrepreneur starting a new business in a new profession in a new market and a telephone service network?

B. How are the requirements for a telephone network infrastructure like those for a new entrepreneur?
C. What are some estimated costs, not necessarily monetary ones?
D. What are some benefits to an entrepreneur who enters a market with established networks?
E. How do established networks save the entrepreneur valuable money and time?
F. With limited resources, what criteria should an entrepreneur use to determine priorities of spending time, effort, and money in developing networks?
G. Does each criterion have equal weight? Why or why not?

2. The Internet Association (IA, https://internetassociation.org/) was founded in 2012 as a trade association devoted to Internet-based companies. Founding companies included Google, Amazon, eBay, and Facebook. These Internet-based companies founded this new trade group because they did not have a voice in Washington, DC, with respect to potential regulations and laws. The IA has synergy—more influence as a group than each company would have individually.
A. What prompted the formation of the IA?
B. Was it for marketing purposes?
C. Management support?
D. Industry advancement?
E. Regulatory influence?
F. What are some secondary purposes for the IA?
G. How might the original purpose of the organization shift as the industry matures?
H. Will small companies enjoy the same benefits of the larger founding organization?
I. Any new venture involves substantial risks and costs. How might a new Internet startup benefit from joining the IA?
J. How else do the large corporations benefit besides having a say in the political discussion in Washington, DC?
K. What time commitment should a new business make before expecting any positive return on investing time and money in a trade association?
L. If joining the IA requires a membership fee, what determinants should you use to place a value on the amount spent for dues?
M. What benefits of a trade association may be not easily linked to membership expenses?

3. In 1989, the new NFL owner of the Dallas Cowboys, Jerry Jones, fired the legendary coach Tom Landry and hired one of his former college football teammates, Jimmy Johnson, as the new head coach. Johnson faced the same problems that a new entrepreneur has: Who should be on my leadership team? What should be their responsibility? Out of twelve key coaching positions, Johnson kept only three coaches from Landry's staff in the same positions and moved one coach to a different position. Within four years (1993), the Dallas Cowboys, under head coach Jimmy Johnson, won Super Bowl XXVII with six of the original coaches Johnson hired his first year still in the same positions.
A. How is a startup similar to an existing organization that needs to be turned around? How are they different?
B. What are some reasons to surround yourself with others instead of taking the attitude that "I can do it myself?"
C. For any leader, what are some reasons that skills in identifying and recruiting key people are more important than technical skills?

4. Every four years, the United States elects a president. Although the incumbent might be reelected, the United States is guaranteed to have a new president at least every eight years. On winning the election, the new president must identify candidates for cabinet positions. Some potential candidates decline the invitation and voluntarily withdraw themselves from consideration. Those who accept the invitation are put through an intensive screening process. The president then submits cabinet-level nominees to the US

Senate for confirmation. As in any close group, recruiting and selecting individuals to join the presidential cabinet is critical for the president to achieve any objectives or goals.

A. What kind of experience is beneficial to members of a board of directors for a local performing arts group? Should they be experienced in industry? Government? Fundraising? Management? Marketing? The arts?
B. Besides experience, what other type of backgrounds should be considered? What about board members' ages? Education? Gender? Residency? Financial Status? Connections to local or regional major employers?
C. What can a new entrepreneur learn from an executive director of a nonprofit about selecting candidates to build a winning team? How important is it that some candidates decline to join the board? How long should members be on the board?
D. How important is diversity in building a winning team? What skills must the entrepreneur perfect? What skills can be learned and developed later by the entrepreneur? Why is a variety of backgrounds, in the technical field and outside of the industry, important?
E. Who is the actual team leader? (1) Entrepreneur? (2) Strongest personality? (3) Smartest? (4) Most technically skilled? (5) Financier? (6) Most experienced in management?

5. Narciso Gómez has worked in the service department at an auto dealership for about twenty-five years and has served as the service manager for the past seven years. He is qualified for retirement through the dealership but wants to open his own business. He is looking at buying a franchise, either a Jiffy Lube quick oil-change franchise that is for sale or a new SuperGlass Windshield Repair franchise. Both are automotive service and repair related, where he has plenty of experience.

A. Besides his technical skills, what does Narciso need to consider before purchasing a franchise business?
B. How might the estimated volume of work required to generate enough sales to cover his financial obligations affect his decision?
C. The Jiffy Lube business model requires a four-bay facility. What does Narciso need to calculate in developing his business plan?
D. The SuperGlass Windshield Repair is an on-site repair model whereby the technicians drive to the vehicle's location for work. What should Narciso's main concerns be in developing a business plan for this business model?

6. Han Jia-ying was an office manager for a construction company until she decided to be a stay-at-home mother with her kids. Her former employer has called her to take over some administrative work at home, such as payroll processing, payroll tax filings, bookkeeping, and other general administrative work. Her employer has said that some of his customers probably could employ her for their general administrative tasks.

A. If she works from home, what type of scheduling issues does Jia-ying face? What might be some interruptions to her ability to meet specific deadlines, such as processing paychecks each week?
B. If Jia-ying needs additional help, what options does she have? Would she be wise to hire an employee or seek some support from someone else? Who might that be? What problems might Jia-ying encounter when seeking a nonregular employee?
C. Jia-ying will need new office equipment, including a new computer, a new scanner/printer, phone service, Internet connections, and so on. However, she is not tech savvy. How might she best manage working from home by herself, especially is something goes wrong or does not work?

Suggested Resources

12.1 Building and Connecting to Networks

Association of Chamber of Commerce Executives: acce.org

BNI: Business Network International: https://www.bni.com

HUBZone: https://www.sba.gov/offices/headquarters/ohp

Service Corps of Retired Executives (SCORE): https://www.score.org

Small Business Administration: https://www.sba.gov

Small Business Development Centers: https://www.sba.gov/sbdc

Women's Business Centers: https://www.sba.gov/offices/headquarters/wbo

Veteran's Business Outreach Centers (VBOC): https://www.sba.gov/offices/headquarters/ovbd

12.2 Building the Entrepreneurial Dream Team

Traits: Personality and Instinct

Cattell's 16PF: https://openpsychometrics.org/tests/16PF.php

Kolbe Conation Index: http://www.kolbe.com

Typical Traits & Characteristics of Entrepreneurs:

https://smallbusiness.chron.com/typical-traits-characteristics-entrepreneurs-18325.html

Good Characteristics of an Entrepreneur:

https://smallbusiness.chron.com/good-characteristics-entrepreneur-18385.html

Attorney: State Bar Associations for attorneys in specific states:

New York: http://www.nysba.org

California: http://www.calbar.ca.gov

Texas: https://www.texasbar.com

Florida: https://www.floridabar.org

Accountant: National Association of State Boards of Accountancy (All fifty states Accountancy Boards are here with active links): https://www.nasba.org

Team Building Activities:

Three Teambuilding Exercises: http://www.entrepreneur.com/article/224212

Seven Team Building Ideas: http://www.entrepreneur.com/article/330594

Success Factors for Entrepreneurs:

Fifteen Entrepreneurial Key Success Factors:

http://www.entrepreneurshipinabox.com/852/entrepreneurial-success-factors/

Ten Qualities of Successful Entrepreneur:

https://www.under30ceo.com/10-qualities-of-a-successful-entrepreneur/

12.3 Designing a Startup Operational Plan

American Customer Satisfaction Index: https://www.theacsi.org/

North American Industry Classification System: https://www.census.gov/eos/www/naics/

US Census Bureau: https://www.census.gov/

US government contracts: https://www.sba.gov/federal-contracting/contracting-guide/basic-requirements

US Department of Commerce Homepage: https://www.commerce.gov/

US Department of Commerce, Bureau of Economic Analysis: https://www.bea.gov/

US Department of Labor Homepage: https://www.dol.gov/

US Department of Labor, Bureau of Labor Statistics: https://www.bls.gov/bls/blswage.htm

Yahoo Finance: https://finance.yahoo.com/

Scheduling programs and templates:

https://getsling.com/blog/category/scheduling/

https://wheniwork.com/features

https://schedulebuilder.org/

Employer hiring costs of employee: https://gusto.com/tools/employer-tax-calculator

Payroll program: https://onpay.com/payroll-calculator-tax-rates

13

Business Structure Options: Legal, Tax, and Risk Issues

Figure 13.1 Focusing time and energy on planning a business can help an entrepreneur avoid or minimize legal issues. (credit: modification of "hammer books law court lawyer" by "succo"/Pixabay, CC0)

Chapter Outline

13.1 Business Structures: Overview of Legal and Tax Considerations
13.2 Corporations
13.3 Partnerships and Joint Ventures
13.4 Limited Liability Companies
13.5 Sole Proprietorships
13.6 Additional Considerations: Capital Acquisition, Business Domicile, and Technology
13.7 Mitigating and Managing Risks

Introduction

Entrepreneurial businesses are the heart of the US economy. Small businesses—those with fewer than 500 workers—employ almost one-half of the US workforce (47 percent according to the US Census Bureau's Annual Survey of Entrepreneurs)[1] and are responsible for offering thousands of new products and services each year. The information in this chapter can help entrepreneurs successfully start and operate a business. Startups function best when the owners have a strong understanding of the legal aspects of entrepreneurship. Important legal issues such as business structure (entity selection), incorporation process, taxation, capital acquisition, and employment policies require that entrepreneurs obtain good advice and make sound decisions before they commence operations. They must make additional decisions that relate to the role of the business in the community, which is a key component of corporate social responsibility. The combination of good advice and sound decisions will help entrepreneurs successfully navigate a complex matrix of considerations.

1 US Census Bureau. *Annual Survey of Entrepreneurs (ASE).* 2016. https://www.census.gov/programs-surveys/ase.html

13.1 Business Structures: Overview of Legal and Tax Considerations

Learning Objectives

By the end of this section, you will be able to:

- Understand why a business's purpose is an important role in the initial business structure decision
- Identify major types of business structures (corporation, LLC, partnership, sole proprietorship, joint venture)
- Distinguish between for-profit and not-for-profit purposes and structures

The structure of a new business creates the legal, tax, and operational environment in which the business will function. In order to choose a business structure, entrepreneurs need to have a clear understanding of the type of business they seek to establish, the purpose of the business, the location of the business, and how the business plans on operating.

For example, a business that plans to qualify as a nonprofit—Section 501(c) of the Internal Revenue Code—will be treated differently from a business that aims to earn a profit and distribute the profits to its owners. Therefore, the first step in any entrepreneurial endeavor is to establish the nature and purpose of the business (Figure 13.2).

Figure 13.2 There are several basic business structures: sole proprietorships, partnerships, corporations, and hybrid forms. Partnerships may be structured as a general partnership (GP), a limited partnership (LP), or a limited liability partnership (LLP). Hybrids are usually formed as a limited liability company (LLC) or a joint venture (JV). The designations of "C" and "S" corporations refer to which chapter of the Internal Revenue Code they appear in; B corporations are structured to meet standards of serving certain social purposes. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

One of the most important initial decisions an entrepreneur must make, from a legal perspective, is the legal organization of a business, called the **business structure** or *entity selection*. The choices are varied, with several basic entities, each with several variations, resulting in multiple permutations.

Many business ventures, regardless of humble beginnings, may have the potential to evolve into significantly larger business ventures. This is what makes the initial decisions so important. The founders should think through every step of business development, beyond the inception or formation, and consider the possible

paths of the business. How an entrepreneur organizes the business, or which business structure they choose, will have a significant impact on both the entrepreneur and the business.

Business structure options include traditional choices such as corporations, partnerships, and sole proprietorships, and hybrid entities such as limited liability companies (LLCs), limited liability partnerships (LLPs), and joint ventures (JVs). Each structure carries different requirements to set up, different requirements to fulfill (such as taxes and government filings), and varying ownership risks and protections. Entrepreneurs should consider these factors as well as the expected business growth in selecting a structure, while being aware that the structure can and should change as the business venture grows.

For example, if you think you want to share authority, responsibilities, and obligations with other people, your best choice would likely be a partnership, in which other people contribute money and help manage the business. Alternatively, if you prefer to manage the business yourself, a better choice for you might be a single-member LLC, assuming you can borrow money from a lender if needed. Conversely, if you think your idea is so popular that you may grow rapidly and want the ability to raise capital by selling interests in your business through equity or debt, then a corporation would be your best choice. You should obtain legal and tax advice about your structure.

ARE YOU READY?

Becoming an Informed Entrepreneur

If you are an entrepreneur with an idea for a startup, ask yourself if you are ready to make important decisions. How much do you know about taxation, incorporation, or liability? If you don't know at least some of the basics, you may have to depend on a lot of advice from accountants and attorneys, and that is very expensive. If you spend too much money on advice, you have too little left for something else such as advertising and marketing.

Establishing a Business Purpose

A clear understanding of the business purpose helps direct the entrepreneur toward the most appropriate business structure. The **business purpose** is the reason the entrepreneur forms the company and determines who benefits from it, whether it is the entrepreneur, customers, or some other entity. (The business purpose is different from a business mission or vision.) Drafting the expectations of the entrepreneur and how the business will operate, with a careful analysis of how the business will generate cash flows, realize profits, and to whom the business will owe its primary obligations, is the start of determining the appropriate business structure. A written business plan (see Business Model and Plan) will help the entrepreneur develop the best legal structure in which the business is to operate because the legal structure of the business should be tied to the nature of the business.

Once the entrepreneur is clear on the nature and purpose of the business, consideration of the business structure follows. The first consideration is whether the entity is being created to produce a profit for its owners or shareholders, or whether it will be structured as a not-for-profit entity. A second factor is the state of incorporation, as state law defines each business's creation, with different states permitting different types of entities and various legal protections. Additional considerations include how the structure facilitates bringing in new investors, allows the owners to transfer profits out of the business, and supports a potential subsequent sale of the entity. Taxation is also a crucial aspect of business success, and the business structure or entity directly affects how it is taxed.

ARE YOU READY?

Drafting a Business Purpose

Can you write an outline of a business purpose? Try this: Your university's tutoring center is crowded, and those students who need extra help are struggling to find it. You have decided to start a new company to match those students with student tutors at your university. Who determines how much a tutor can charge? Is it a set price, a surge pricing model like Uber, or is it up to the tutor? How much of a profit do you make? In essence, you must determine the purpose of your business. Read this IRS article about shared-economy businesses (https://openstax.org/l/52IRSsharedbus) to learn more.

For-Profit versus Not-for-Profit Businesses

Owners form businesses for one of two purposes: to make a profit or to further a social cause without taking a profit. In either case, there are multiple options in terms of how a business is structured. Each structure carries its own tax consequences determined by the owners' financial requirements and how the owners want to distribute profits. The structure, in turn, determines the appropriate income tax return form to file.

Characteristics of For-Profit Businesses

A **for-profit business** is designed to create profits that are distributed to the owners. There are multiple entity structures used in for-profit business entities including corporations, LLCs, partnerships, and sole proprietorships. Many for-profit business owners seek some form of limited liability, and thus form a corporation or an LLC, each of which carries with it specific legal attributes. Additionally, for-profit business entities are subject to a variety of local, state, and federal taxes and filings. Liability and tax issues will be discussed later in this chapter.

For-profit businesses are commercial entities that generally earn revenue through the sales of products or services, whereas nonprofits are organized for social purposes. Nonprofits are allowed to provide assets or income to individuals only as fair compensation for their services. For-profit businesses can be either privately owned (such as an LLC) or publicly owned and traded (such as a corporation). Publicly held and traded corporations sell stock or interests, and must abide by special rules to protect shareholders, whereas privately owned businesses may be less regulated. Regulations may vary by state and by type of incorporation.

Characteristics of Not-for-Profit Organizations

A **not-for-profit organization (NFPO)** is usually dedicated to serve the public interest, further a particular social cause, or advocate for a common shared interest. They must follow particular regulations regarding eligibility, government lobbying, and tax-deductible contributions. In financial terms, a not-for-profit organization uses its surplus revenues to achieve its ultimate objective, rather than distributing its income to the organization's shareholders, partners, or members. Common examples of not-for-profits include educational organizations such as schools, colleges, and universities; public charities such as the United Way; religious organizations such as places of worship; foundations; trade organizations; and issue-advocacy groups. Other organizations also considered NFPOs include nongovernmental organizations, civil society organizations, foundations that provide funding for various activities, and private voluntary organizations.[2]

Nonprofits are usually tax-exempt as categorized by the US Internal Revenue Service (IRS), meaning they do not pay income tax on the money they receive for their organization. These types of organizations are created under state law (but also subject to federal and local laws) and are typically created for the common good.

To operate as a not-for-profit business, most states require that the entrepreneur create a corporation that has

2 International Center for Not-for-Profit Law (ICNL). "What Is the Difference between 'Non-Profit' and 'Not-for-Profit'?" 2013. http://www.icnl.org/contact/faq/index.html#difference

the specific purpose of acting in the public interest. This type of corporation does not have owners but has directors charged with running the organization for the public good, subject to bylaws. Some states only require a minimum of one director, whereas other states may require three or more directors. This is an important consideration for an entrepreneur because the nonprofit corporation will need the approval of all of the directors, and not just one person for its creation. Careful vetting of the directors is the best policy of any entrepreneur since directors have a duty to the corporation.

Because state laws vary, a not-for-profit corporation created for the common good in one state needs permission from another state to operate in that state. The permission is typically an approval from the other state's secretary of state memorialized in the form of official documents or permits. When operating in different states, the entrepreneur needs to make sure that the business follows all laws, rules, and regulations for each state.

Another issue to consider is the creation of a not-for-profit business organization for a particular purpose. One example of a special-purpose organization is an alumni organization, usually incorporated as a 501(c)(3) nonprofit, which incorporates to raise money for a college or university for a specific reason, such as student scholarships. Alternatively, a booster club may incorporate to receive donations for a single function, such as the women's soccer team. These organizations may need additional approvals prior to the creation or start of operations, depending upon state and local legal requirements. Each state typically has different requirements; depending on the federal tax regulation under which the entrepreneur is attempting to qualify, there may be additional federal regulations. This is why the entrepreneur needs to fully understand the purpose of the business they are starting and the legal operating environment before selecting the business structure. While NFPOs play an important role, most entrepreneurs form for-profit businesses; therefore, the remainder of this chapter will focus primarily on for-profit business entities.

ENTREPRENEUR IN ACTION

Determining the Purpose of Your Business—Profit versus Non-Profit, or a Little of Both?

The Approach Used by Gravity Payments' Entrepreneur Dan Price

Figure 13.3 Gravity Payments has led the way in exploring how employee and C-level salaries function for the company in terms of profits, living wages, and ethical considerations related to those issues. (credit: modification of photo provided by Gravity Payments)

Sometimes, a business may be a for-profit company yet act in a way that some may think exhibits a not-for-profit philosophy. Most startups must address their business purpose. In other words, is the primary purpose of the business to enrich the owners or is it to spread the benefits of success to the workers? The history of Gravity Payments (Figure 13.3) illustrates this issue.

In 2011, an employee earning $35,000 a year told his boss at Gravity Payments, a credit-card payment business, that his earnings were not sufficient for a decent life in expensive Seattle. The boss, Dan Price, who cofounded the company in 2004, was somewhat surprised, as he had always taken pride in treating

employees well. Nevertheless, he decided his employee was right. For the next three years, Gravity gave every employee a 20 percent annual raise. Still, profit continued to outgrow wages, so Price announced that over the next three years, Gravity would phase in a minimum salary of $70,000 for all employees. He reduced his own salary from $1 million to $70,000 to demonstrate the point and help fund the company-wide salary increase. The following week, 5,000 people applied for jobs at Gravity, including a Yahoo executive who took a pay cut to transfer to a company she considered fun and meaningful to work for.

Price recognized that low starting salaries were antithetical to his values and to what he felt was a large part of his business purpose. A majority of the initial cost of his approach to employee salaries was absorbed by making less profit, yet revenue continues to grow at Gravity, along with the customer base and the workforce. Price believes that managers should measure purpose, impact, and service as much as profit.

- Do you think an entrepreneur can successfully operate a for-profit business while paying its workers substantially more than the competition?

13.2 Corporations

Learning Objectives

By the end of this section, you will be able to:

- Distinguish between C Corporations, S Corporations, and B Corporations
- Distinguish between privately and publicly held corporations
- Explain how corporations are taxed

A **corporation** is a complex business structure created by filing the appropriate documents with the state of incorporation (Figure 13.4). They are created when the original incorporators (owners) file a formal document called the articles of incorporation, or other similar documentation, with a state agency, often the secretary of state's office or the state division of corporations. Corporations operate as a separate legal entity apart from the owners. The owners are called shareholders and can be individuals, other domestic or foreign corporations, LLCs, partnerships, and other legal entities. Corporations may be for-profit or not-for-profit, as discussed previously.

STATE OF [STATE]
CERTIFICATE OF INCORPORATION
A STOCK CORPORATION

The undersigned Incorporator, desiring to form a corporation under pursuant to the General Corporation Law of the State of [State], hereby certifies as follows:

1. The name of the Corporation is _____.
2. The Registered Office of the corporation in the State of [State] is located at _____ (street), in the City of _____ , County of _____ Zip Code _____. The name of the Registered Agent at such address upon whom process against this corporation may be served is _____.
3. The purpose of the corporation is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of [State].
4. The total amount of stock this corporation is authorized to issue is _____ shares (number of authorized shares) with a par value of $ _____ per share.
5. The name and mailing address of the incorporator are as follows:
   Name _____
   Mailing Address _____
   _____ Zip Code _____

By: _____
Incorporator

Name: _____
Print or Type

Figure 13.4 This is a sample short form of the document that is filed with the Secretary of State's Office to form a corporation. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Incorporating a company means that the corporation operates as an entity that has some of the same rights as an individual. For example, individuals and corporations can sue and be sued, and corporations have the rights to own property, to enter into and enforce contracts, to make charitable and political donations, to borrow and lend money, and to operate a business as if the corporation were an individual. Most states require a corporation to be registered in that state in order to conduct business operations and to enter into and defend lawsuits in that state, especially if the business was incorporated in a different state. Registration is not the same as forming the initial corporation; it is simply the process of filing informational documents by entities that have already been incorporated in another state. States also tax the operations or sales a corporation makes in the state in which it has certain operations.

Overview of Corporations

Corporations are the only type of entity that the law allows to sell shares of stock. No other entity, like an LLC or a partnership, may do so. Those individuals or other entities that buy stock become shareholders and own the corporation. Some corporations have millions of shareholders, and others have as few as one. State incorporation laws vary: Some require at least three shareholders, but others allow a one-owner business to incorporate. Thus, an entrepreneur may start a company as the sole owner of the company and later incorporate and sell shares of stock or bonds to other investors in the company.

Corporations sell, or issue, stock to raise **capital**, or money, to operate their businesses. The holder of a share of stock (a shareholder) purchases a piece of the corporation and has a claim to a part of its assets and earnings. In other words, a shareholder is now an owner of the corporation. Thus, a share of stock (also called equity) is a type of security that signifies proportionate ownership in the issuing corporation. Stocks are bought and sold predominantly on stock exchanges, although there can also be a private sale between a seller and a buyer. These transactions have to conform to a very complex set of laws and government regulations (e.g., the Federal Securities Acts of 1933/34), which are meant to protect investors.

Use of a corporation allows the entrepreneur to shield themselves, and other owners, from personal liability for most legal and financial obligations. The benefit of limited liability is one of the primary reasons entrepreneurs incorporate. However, the administration of a corporation requires more formality than other types of entities, such as sole proprietorships and partnerships. A corporation must follow the rules for such entities. The requirements include maintaining bylaws, holding annual shareholder and director meetings,

keeping minutes of shareholder and director major decisions, ensuring that officers and directors sign documents in the name of the corporation, and importantly, maintain separate bank accounts from their owners and keep detailed financial and corporate records. A failure to follow the rules could lead to the loss of limited liability, known as "piercing the corporate veil."

WORK IT OUT

Piercing the Corporate Veil of Limited Liability

As we have discussed, entrepreneurs should generally form a separate legal entity to limit personal liability arising from business obligations, such as contracts. Incorporating or organizing as an LLC can limit owners' personal liability to the extent of their investments. This liability shield is not without exception, however: in particular, a situation called "piercing the corporate veil." A recent 2018 case example (Woodruff Construction, LLC v. Clark, No. 17-1422 [Iowa Ct. App. Aug. 15, 2018]) demonstrates this point.

Factual Overview: The defendant was the sole owner of a corporation and entered into a contract to remove sludge for the plaintiff at a waste treatment facility. The defendant never completed the work. The plaintiff sued and won a $400,000 judgment against the corporation for breach of contract. However, the plaintiff was not able to collect from the corporation due to insufficient assets. The plaintiff then asked the court to pierce the veil of the corporation, which would allow recovery from the corporate owner's personal finances.

Piercing the Veil: Evidence showed that although the defendant kept a separate bank account for the corporation, he had commingled its funds with his personal finances, which is a distinct violation of fiduciary duty. He used the bank accounts for the corporation interchangeably with other bank accounts. Furthermore, the defendant did not follow required corporate formalities because he had no bylaws or resolutions, no voting records, and no documentation of or minutes from shareholder meetings.

Finding: The court allowed the plaintiff to pierce the corporate veil. This means that the defendant, the sole owner of the corporation, had to pay over $400,000 out of his personal funds. (Note: Although it is true that LLCs have fewer formal requirements, this case would likely have had the same result if the owner were an LLC because the rules are essentially the same for piercing the veil of limited liability.)

Critical Thinking:

- How can you protect yourself from this happening to you?

Most corporations use a three-part (or tripartite) approach to ownership and management (Figure 13.5). After the corporation is created and operations start, the shareholders typically elect a board of directors, and the board has oversight responsibilities for the operations of the company. The board then appoints officers who are responsible for the day-to-day operations of the corporation.

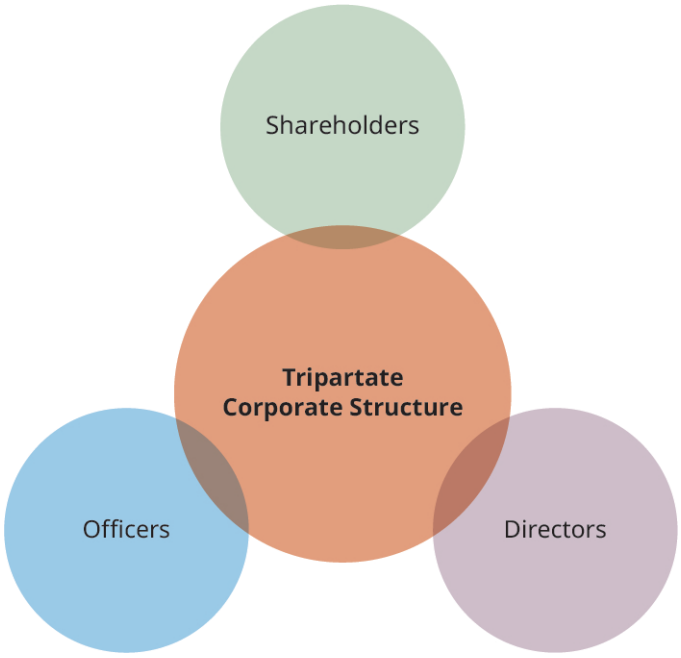


Figure 13.5 In a tripartite approach, three groups are involved in owning and managing a corporation. Shareholders elect directors who appoint officers. Shareholders are owners, and directors/officers may be, and typically are, shareholders. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

For small organizations, state law allows shareholders to directly manage a company without using a board of directors. This type of corporation is a closed corporation or a closely held corporation, and is common for entrepreneurial startups. State incorporation law, coupled with federal tax law under the IRS, regulates the formation and operation of a closely held corporation. The basic rules state that, generally, a closely held corporation is a corporation that has more than 50 percent of the value of its outstanding stock owned (directly or indirectly) by five or fewer individuals at any time during the last half of the tax year.[3]

C Corporations, S Corporations, and B Corporations

The categorization of corporations as either C corporations or S corporations is largely a tax distinction. An **S corporation** is a "pass-through" entity, where shareholders report and claim the business's profits as their own and pay personal income taxes on it. Alternatively, the government taxes a **C corporation** at the corporate level, and then levies taxes again on the owners' personal income tax returns if corporate income is distributed to the shareholders as dividends.

Conversely, the distinction between B corporations and C or S corporations is not one based on taxes at all, but rather on purpose and approach. A certified **B corporation** is a business that meets a very high standard of social and environmental performance, public transparency, and accountability to balance profit with social purpose. B corporations can also be C corporations or S corporations. Figure 13.6 summarizes these types of corporations.

3 US Internal Revenue Service. *Publication 542 Corporations*. n.d. https://www.irs.gov/faqs/small-business-self-employed-other-business/entities/entities-5

The Unique Nature of B Corporations and/or Benefit Corporations

A new form of nontraditional, for-profit corporation is the benefit corporation, which may or may not also be a B corporation. While *B corporations* and *benefit corporations* share some common goals, B corporations go through a certification process. Becoming a certified B corporation is a formal process that involves compliance with various standards and an audit of this compliance (managed by the B corporation organization).[4] The essence of these new B corporations is that "they recognize the imperative to do no harm and create positive impact throughout the value chain."[5] According to the B corporation organization, these certified businesses are legally required to consider the impact of their decisions on their workers, customers, suppliers, community, and the environment. As of 2019, there are approximately 3,000 certified B corporations in sixty-five countries, covering 150 different industries.[6] The B corporation certification is somewhat like a seal of approval for businesses voluntarily trying to be socially responsible. A benefit corporation is a corporation recognized by a governmental agency under state law (about thirty states now recognize benefit corporations with legal requirements of higher purpose, accountability, and transparency) but does not carry the certification of a B corporation. However, in terms of purpose as related to corporate social responsibility, the two entities are very similar.

The benefit corporation's objective is directed toward maximization of benefits for all stakeholders, meaning that the company benefits any person with an interest or concern in the business. It does not only maximize stockholder profits. Maximization of stakeholder benefits is directed through the corporate charter of a benefit corporation. The state of incorporation directs how benefit corporations are created, but generally, this "new governance model broadens the perspective of traditional corporate law by incorporating concepts of purpose, accountability, and transparency with respect to all corporate stakeholders, not just stockholders."[7] This means that the use of this type of business structure needs to be carefully considered by the entrepreneur because the responsibility of the business will include consideration of the stakeholders outlined in the corporate charter, not just the profit maximization for the shareholders.

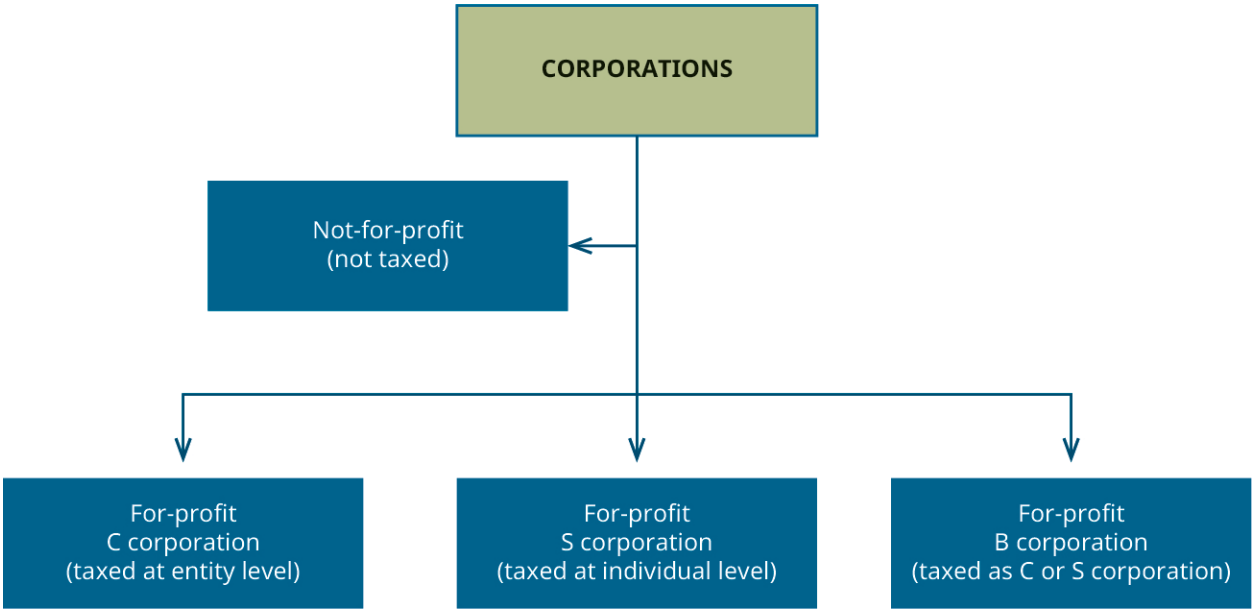


Figure 13.6 C corporations, S corporations, and B corporations are all types of for-profit corporations, in contrast to a not-for-profit corporation. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

4 Certified B Corporations. n.d. https://bcorporation.net/
5 Network for Business Innovation and Sustainability. "B Corporations, Benefit Corporations, and Social Purpose Corporations: Launching a New Era of Impact-Driven Companies." October 2012. http://nbis.org/wp-content/uploads/2012/10/ImpactDrivenCompanies_NBIS_Whitepaper_Oct2012.pdf
6 Certified B Corporations. n.d. https://bcorporation.net/
7 Morris, Nichols, Arsht, and Tunnel. *The Public Benefit Corporation Guidebook*. n.d. http://news.mnat.com/rv/ff00272e4c8b3699806e25d24c48a286df5bf926

ARE YOU READY?

B Corporation Certification

The B corporation website explains the process for becoming a B corporation. This involves three specific steps: Verified Performance, Legal Accountability, and Public Transparency. Go to https://bcorporation.net/about-b-corps and read about B corporations to learn what requirements they need to meet to be allowed to display the following B corporation logo shown in Figure 13.7.

Figure 13.7 In order to become a certified B corporation, a company must go through an external audit of compliance with each of the requirements of the B corporation. (credit: modification of "Runa B Corp Label" by "Lelepanne"/Wikimedia Commons, CC0)

Privately Held versus Publicly Held Corporations

Terminology relating to whether a company is publicly or privately owned can sometimes be confusing. For example, large corporations such as Exxon or Amazon are private corporations, but their stock is publicly held. This means that any member of the investing public can own stock in the corporation. A true **public corporation** is, in reality, a quasi-governmental entity, an entity owned or sponsored by the government. Government-owned corporations include the US Postal Service, the Corporation for Public Broadcasting, AmeriCorps, and Amtrak. Government-sponsored corporations include Freddie Mac and Fannie Mae, mortgage-related entities. A **privately held corporation**, common in Europe, is a company that does not allow members of the investing public to own stock. The founder's family or friends, or perhaps a private group of investors such as a venture capital firm, may hold it. Examples include Facebook before it went public in 2012, or Cargill or Mars.

Publicly Traded Corporations

A **publicly held corporation** is, as described, an entity in which members of the investing public own the stock. A term commonly applied to such corporations is a *publicly traded corporation*, meaning that the stock can be bought and sold in the public marketplace, such as the New York Stock Exchange. A publicly traded corporation has more access to investors and thus more capital, but it must operate under a formal set of rules established by the Securities and Exchange Commission and Congress, assuming the shares are sold publicly in the United States. Audits of publicly traded companies also have to follow the rules of the Public Company Accounting Oversight Board (PCAOB). "The PCAOB oversees the audits of public companies and broker-dealers in order to protect investors and the public interest by promoting informative, accurate, and independent audit reports."[8] Following the SEC and PCAOB rules emphasizes investor protection but can be complex, as it increases both startup and operating costs for the venture due to increased regulation and reporting.

8 PCAOB. "Protecting Investors Through Audit Oversight." n.d. https://pcaobus.org/

A publicly traded company is required to have a board of directors with a dual mandate to both consult with management regarding the strategic direction of the company and oversee company performance. The board of directors does not manage the company, and the members are separate from management.[9] The board will have numerous committees to assist in its functionality, and one of the committees is the audit committee. The audit committee of a publicly traded company must hire an outside auditor approved by the PCAOB to audit the books of the publicly traded company. Further, the chief executive office and chief financial officer of the publicly traded company must sign a certification of earnings report, guaranteeing their truthfulness. The rules and regulations with which compliance is required are more demanding for a publicly traded company than for a privately held or closely held company.

Closely Held Corporations

A closely held corporation, also known as a close corporation, is the same as a privately held corporation for the purposes of securities laws. However, the concept has a secondary meaning related to management structure. A close corporation is also a management structure for a corporation that is often selected by small companies that use the less-formal management style of a general partnership yet retain the limited liability of a corporation. In essence, there are fewer formalities for a close corporation, and it allows greater control for the small group of shareholders.

A close corporation is required to have an annual shareholder meeting and keep corporate minutes. All of this detail is required to be recorded in the corporate records, even if there is just one shareholder. Sole proprietors using a corporation as a business structure must follow the rules regarding corporations in the state in which they were incorporated. Some states may even dissolve a corporation that does not have an annual meeting or keep proper corporate records. When a corporation is dissolved, the shareholders become personally liable for corporate debts, and shareholders' limited liability is lost. Managing a closely held company requires the entrepreneur to follow state guidelines while operating the corporation accordingly.

The shares of a closely held corporation are not traded on the open market and typically have just a few shareholders. Closely held corporations have fewer reporting requirements than publicly traded companies and typically are not required to have audited financial statements, unless the corporate charter says otherwise. Audited financial statements are costly and are required for publicly traded companies. The audited financial statements help investors buying and selling stock in the stock market value shares and are not necessarily needed for a closely held corporation. However, it is difficult to value a closely held corporation because there is no ready market for the ownership shares.

Not-for-Profit Corporations

Nonprofit corporations are created in one a state but may operate or solicit donations in other states. A nonprofit corporation operating or soliciting donations in multiple states needs to register to operate as a nonprofit corporation in every state in which it operates.

Not-for-profit corporations are organized in a similar fashion to for-profit corporations, with a board of directors and officers, but they have no shareholders, stock, or owners. The stakeholders of a non-for-profit corporation play an important role, monitoring overhead and allocation of funds. Since most of the funds are donations and are tax deductible, public watchdogs may monitor the financial statements of federally tax-exempt organizations. The fact that the Internet provides easy access to financial data related to federally tax-exempt nonprofits provides watchdog organizations easy access to financial data and the ability to analyze the operations and compensation for the nonprofit's organizers and employees.

9 Stanford Business Graduate School: Corporate Governance Research Initiative. *Board of Directors, Duties and Liabilities.* n.d. https://www.gsb.stanford.edu/sites/gsb/files/publication-pdf/cgri-quick-guide-03-board-directors-duties-liabilities.pdf

ENTREPRENEUR IN ACTION

Bombas: Achieving Profit and Nonprofit Goals

In a 2017 interview with Robin Roberts of ABC News, Bombas socks (Figure 13.8) co-founder David Heath said: "Back in 2011, I came across a quote on Facebook that said…that socks were the number one most requested clothing item in homeless shelters."[10] So he decided to start a new company that was an overnight success, boosted by an appearance on *Shark Tank* in 2014. He created his company, Bombas, with co-founding entrepreneur Randy Goldberg. They founded their company with the goal of giving back to the community by donating socks to the homeless, with its actual product idea as a secondary goal.[11] They have donated over 25 million items through more than 2,500 partners across the country.[12]

Figure 13.8 This is a pair of Bombas socks. (credit: modification of "Bombas Socks" by Tony Webster/Flickr, CC BY 2.0)

Bombas is now a successful sock company that uses a business entity as a way to address the shortage of sock donations in homeless shelters. Heath and Goldberg spent two years inventing pairs of high-quality socks with extras such as reinforced foot beds and anti-blister tabs, coupled with contoured seaming. For these entrepreneurs though, it was not just about sock technology, it was about doing something meaningful at the same time—a combination of profit and nonprofit goals. Therefore, they made a commitment to those in need, and since 2013, the company has donated more than 10 million pairs of socks to homeless shelters, due to their buy one, give one model of marketing socks.

The socks that Bombas donates to the homeless are not cheap throw-away token socks. Rather, they have been designed for their homeless wearers, for example, with antimicrobial treatment to prevent bacteria if they cannot be washed as frequently and reinforced seams for durability, since the homeless do not have the money to keep buying new ones.[13]

In essence, the company makes customers, and the company partners with the homeless.

- Is Bombas really paying for this project to help the homeless or is the customer?
- Is Bombas just facilitating the good idea and customers are paying for it, or do you think Bombas is also contributing some of its profit?

10 ABC News. "Q&A: Entrepreneurs behind the Socks Company Bombas Share Their Career Advice." August 2, 2017. https://abcnews.go.com/Business/qa-entrepreneurs-socks-company-bombas-share-career-advice/story?id=48954057
11 Mara Leighton. "B Corps Are Businesses Committed to Using Their Profit for Good—These 12 Are Making Some Truly Great Products." *Business Insider*. June 6, 2019. https://www.businessinsider.com/b-corp-charitable-business-2018-8?IR=T&r=US
12 Bombas. "Giving Back." n.d. https://bombas.com/pages/giving-back
13 Mara Leighton. "B Corps Are Businesses Committed to Using Their Profit for Good—These 12 Are Making Some Truly Great Products." *Business Insider*. June 6, 2019. https://www.businessinsider.com/b-corp-charitable-business-2018-8?IR=T&r=US

LINK TO LEARNING

Go to the Bombas website (https://openstax.org/l/52Bombas) to watch the video that explains what they do as part of their B corporation commitment.

Overview of Corporate Taxation

All for-profit corporations are subject to income tax at the federal level, and usually at the state level as well. Regardless of tax elections, both C- and S corporations are subject to taxation.

Tax planning is a major issue for most corporations and may explain some key decisions, such as where they are located. That could involve decisions about which state the corporate headquarters are in, or even in which nation the headquarters are located. This is because tax laws may vary significantly by both state and nation.

The current federal income tax rate for corporations in 2019 is 21 percent, down drastically from 35 percent, which was the rate prior to 2018. Many states add a state-level income tax, ranging from 2 percent to 12 percent, while some states such as Texas do not have a corporate income tax in an effort to attract corporations to the state.[14]

Taxation of C Corporations

C corporations pay corporate income taxes on profits made. Individual shareholders are also subject to personal income taxes on any dividends they receive. Most attorneys and accountants refer to this concept as the double taxation disadvantage. However, the historical tax disadvantage has been recently reduced because of the decrease in the income tax rate paid by C corporations by the Tax Cuts and Jobs Act.[15] This decrease, in turn, reduces the double tax disadvantage. Further, the ability to retain and reinvest profits in the company at a lower corporate tax rate is an advantage.

A C corporation does come with a degree of added formality, or as some may refer to it, red tape. According to most states' corporation laws, as well as federal tax and securities laws, the corporation must have company bylaws and must file annual reports, financial disclosure reports, and financial statements. They must hold at least one meeting each year for shareholders and directors where minutes are taken and maintained to display transparency. A C corporation must also keep voting records of the company's directors and a list of the owners' names and ownership percentages.

Despite the tax implications, the C corporation structure is the only one that makes sense for most large US businesses because it allows for the wide-scale sale of a large amount of stock to the general investing public without limits. A C corporation can have an unlimited number of shareholders that are individuals or other business entities, and are either US citizens or foreign nationals.

Taxation of S Corporations

As previously discussed, the S corporation is a corporate entity in which the firm's profit is passed through its stockholders (shareholders), usually in proportion to their investment—this is known as pass-through taxation. Essentially, this amounts to tax management by the corporate owners. The IRS taxes the corporate profits at the personal income tax rates of the individual shareholders. S corporations (S stands for "small"), also called subchapter S corporations, must comply with several important restrictions with which entrepreneurs must comply.

S corporations have a limit on shareholders. Unlike with C corporations, the Internal Revenue Code limits the number of S corporation shareholders to 100 or fewer, and owners can only be individuals, (or estates and

14 Tax Foundation. "State Corporate Income Tax Rates and Brackets for 2019." 2019. https://taxfoundation.org/state-corporate-rates-brackets-2019/
15 US Internal Revenue Code of 1986. 131 Stat. 2054.

certain types of tax-exempt entities). Additionally, the individual shareholders must also be US citizens or legal permanent residents. Furthermore, S corporations may only have one class of stock, whereas C corporations may have multiple classes. For example, in a C corporation, there might be voting shares, nonvoting shares, common shares (the type most people buy), and preferred shares (which are repaid first in the event of bankruptcy).

13.3 Partnerships and Joint Ventures

Learning Objectives

By the end of this section, you will be able to:

- Describe the ownership structure of a partnership
- Describe the ownership structure of a joint venture
- Summarize the advantages and disadvantages of partnership and joint venture structures

A **partnership** is a business entity formed by two or more individuals, or partners, each of whom contributes something such as capital, equipment, or skills. The partners then share profits and losses. A partnership can contract in its own name, take title to assets, and sue or be sued.

A **joint venture** is, in essence, a temporary partnership that two businesses form to gain mutual benefits, such as sharing of expenses and to work toward shared goals and the associated potential revenue. Joint ventures share costs, risks, and rewards. A joint venture, for example, can help speed up expansion of your business by gaining access to additional equity, new markets, or new technology. Partnerships and joint ventures share many similarities, but they do have some important differences.

Overview of Partnerships

State law governs the formation and operation of all partnerships. It would be too lengthy to cover the laws of all fifty states; therefore, this section contains some generalizations that may vary according to jurisdiction. Federal law has very limited applicability to partnerships, primarily in the area of federal income taxation. A **general partnership** is created when two or more individuals or entities agree to work together to operate a business for profit. A partnership generally operates under the terms of a written partnership agreement, but there is no requirement that the agreement be in writing. In many instances, the only requirement is that two or more parties come together to operate a business for profit.

Entrepreneurs need to be careful because a general partnership can be informally created by the actions of two or more people or entities pursuing a business for profit while sharing management duties. State courts may deem these actions the creation of an informal or even formal partnership. For this reason, if two entities or people come together to purse a joint business operation or strategy, the parties should document the pursuit of the business venture in a written agreement. Many state laws require that some forms of a partnership use a formal written partnership agreement or articles of partnership. If the venture is of a shorter duration, it might be better to enter into an agreement documenting a joint venture. In either case, the entrepreneur needs to have a clear understanding of the exact business relationship before embarking on a new venture, and a partnership agreement can and should outline those details.

A partnership agreement addresses many important topics, including the monetary investment of each partner, their management duties and other obligations, how profits or losses are to be shared, and all the other rights and duties of the partners.

Partnerships can take many forms, including general partnerships (GPs), limited partnerships (LPs), limited liability partnerships (LLPs), and, in some states, limited liability limited partnerships (LLLPs). All states require the registration of any limited liability entity. In GPs, liability of the owners is considered “joint and several,” meaning that not only is the partnership entity liable, so too is each general partner.

The liability of partners, therefore, may be limited by the creation of an LP. A **limited partnership** requires at

least one general partner and one or more limited partners. A limited partner's liability is typically capped at their investment, unless they take on the duties of a general partner. The general partner is personally liable for all of the operations of the LP.

LPs have been around for many years and allow investors to provide funding for a business, while limiting their investment and personal risk. LPs are commonly used in businesses that require investment capital but do not require management participation by LP investors. Examples include real estate where the LP buys commercial real estate, making and funding movies or Broadway plays, and drilling oil and gas wells.

Some states have relatively recently started to allow variations on the LP structure and offer businesses the option of forming a related type of partnership entity. These **limited liability partnerships** are common with businesses such as law firms and accounting firms. The partners are licensed professionals, with limited liability for financial obligations related to contracts or torts, but full liability for their own personal malpractice. The primary difference between LLCs and LLPs is that LLPs must have at least one managing partner who bears liability for the partnership's actions. An LLP's legal liability is the same as that of an owner in a simple partnership. Entities that are formed with a founding partner or partners—commonly law firms, accounting firms, and medical practices—often structure as an LLP. In this situation, junior partners typically make decisions around their personal practice but don't have a legal voice in the direction of the firm. Managing partners may own a larger share of the partnership than junior partners.

The final type of partnership is a limited liability limited partnership (LLLP), which allows the general partner in an LP to limit their liability. In other words, an LLLP has limited liability protection for everyone, including the general partner who manages the business.

Advantages and Disadvantages of General Partnerships

The GP is a very common business structure in the US. It is created when two or more individuals or entities come together to create, own, and manage a business for profit. A GP is not technically required to have a written agreement, or to file or register with the state government. However, GPs should have their business structures described in writing, so that the entities working together have an understanding of the business and the business relationship.

When a GP is created, one partner is liable for the other partner's debts made on behalf of the partnership, and each partner has unlimited liability for the partnership's debt. This creates a problem when one partner disagrees with the source or use of funds by another partner in terms of capital outlay or expenses. Each partner in a GP has the ability to manage the partnership; if something negative happens such as an accident (called a tort) that injures people and produces liability—like a chemical spill, auto accident, or contractual breach—each of the partners is personally liable with all of their personal assets at risk. Also, the partners are liable for the taxes on the partnership, as a GP is a pass-through entity, where the partners are taxed directly, but not at the partnership level.

It should be noted that GPs may be a useful structure in certain situations because they are relatively easy and inexpensive to form. The expanding use of LPs, LLPs, and LLLPs is discussed in the preceding text, but the popularity of GPs has been on the decline. However, as long as the business does not have a high likelihood of liability-producing accidents or situations, a GP can work. An example might be two partners offering graphic design or photographic services. However, due to the different risks associated with them, GPs are often not the best choice of business entity. Other types of entities offer the protection of limited liability and are thus better choices in most circumstances.

Taxation of Partnerships

Partnerships are considered pass-through entities, whether they are GPs, LPs, or LLPs. Therefore, the partnership's profits are not taxed at the entity level, like with a C corporation, but the profits are passed through to the partners, who claim the income on their own tax returns. The partners pay income taxes on

their share of distributed partnership profits (disclosed on a Schedule K-1 form from the partnership to the individual partners). Thus, there is no such thing as a partnership tax rate.

If the entity is a joint venture that is organized and run as a partnership, then it is taxed the same way, even if the partners are corporations. The profits are distributed, and each corporation pays its own taxes. If, in the alternative, the joint venture formed a separate distinct corporation, then it pays taxes as a corporation.

LINK TO LEARNING

See the University of Richmond Law School's good summary of the pros and cons of GPs (https://openstax.org/l/52URichLawGP) to learn more.

Joint Ventures: Business Entities Doing Business Together

A joint venture occurs when two or more individuals or businesses agree to operate a for-profit business venture for a specific purpose. A joint venture is similar to a legal partnership but different in terms of purpose and duration. Usually, joint ventures are used for a single purpose and a limited period. One example of a joint venture involved BMW and Toyota working together to research how to improve the batteries in electric cars, a single purpose, over a period of limited duration, envisioned to be ten years.

Companies enter into a joint venture often to avoid the appearance of the creation of a partnership, because partnerships tend to create long-term obligations between the partners, while a joint venture is a limited business enterprise. Typically, two business entities operate a business together on a joint project. The joint venture agreement allows the entities to pursue a specific business objective while keeping their other business operations and ventures separate.

A joint venture is not recognized as a taxable entity by the IRS. The entrepreneur can use a joint venture agreement to develop a business enterprise, and if the business enterprise is successful, a new entity can be created to take over the operations of the joint venture and move the business to the next level. For this reason, a joint venture can be a good way test a business concept. If successful, then the operations and assets can be rolled into another entity that supports investment from outside investors. The use of a joint venture also allows the parties to test drive the relationship between the entities: to develop a business venture with less risk.

Joint ventures can involve parties that are large or small, or from private or public sectors, or they can involve a combination of types of entities, most often resulting in a joint venture that is formed as a corporation or LLC. For example, the public company Google and the private entity NASA formed a joint venture to improve Google Earth. Likewise, a joint venture might be something smaller, such as an arrangement between a freelance IT engineer, a graphic designer, and a social media consultant to create a new cell phone app. Figure 13.9 summarizes the relationships of the businesses in a joint venture.

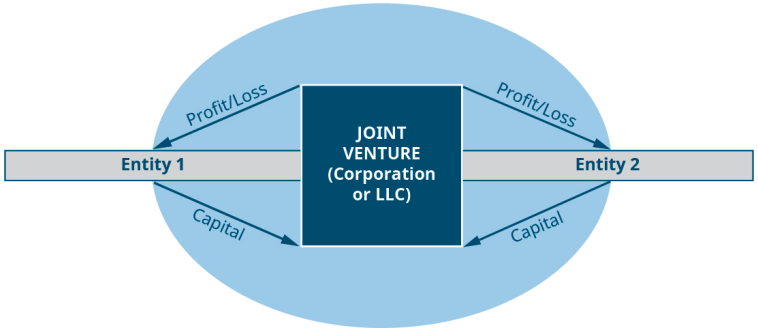


Figure 13.9 Joint ventures are separate business entities, most often owned and operated by two other business entities. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

WHAT CAN YOU DO?

Challenges Facing Small Farmers

Sometimes, small businesses are at a disadvantage due to size. We can see an example of this disadvantage in the field of agriculture. The cost of new agricultural equipment is very high, and land may be prohibitively expensive. These costs put small farms under pressure to compete by increasing the size of their operations. If you owned a small farm and were looking to expand, how could you use a joint venture?

13.4 Limited Liability Companies

Learning Objectives

By the end of this section, you will be able to:

- Describe the ownership structure of a limited liability company
- Explain how limited liability companies are taxed
- Summarize the advantages and disadvantages of the limited liability company structure

A **limited liability company** is a hybrid of a corporation and a partnership that limits the owner's liability. The big advantage that LLCs have over GPs is in the protection of owners from personal liability. Thus, an LLC is similar to a corporation in that it offers owners limited liability.

The advantage that LLCs have when compared to corporations, especially for entrepreneurs, is that they are easier to form and less cumbersome to operate because there are fewer regulations and laws governing LLC operations. Although LLCs tend to be easier to create, they still require a filing of articles of formation with the state and the creation of an operating agreement. Owners of an LLC can be individuals and other business entities. The entrepreneur can use the flexibility of an LLC to create a business structure suitable to the operational and tax needs of the business.

In 1977, Wyoming was the first state to allow the LLC format—most states started allowing them in the early 1990s. In contrast, corporations have been around since the early nineteenth century. LLCs now significantly outnumber corporations, with some estimates indicating that four times as many LLCs are formed as corporations,[16] with the total number of LLCs nearing 20 million compared to about 2 million corporations. Each state may permit varying types of LLCs, with different types of formation agreements and operating agreements.

When evaluating the use of an LLC as the structure for your business, it is important to know that there are some constraints on the use of an LLC. In most states, a nonprofit business cannot be an LLC. Additionally, most states do not permit banks or insurance companies to operate as LLCs.

Overview of LLCs

The owners of an LLC are called members. The owner (if a single-member LLC) or owners often run the company themselves. These are called member-managed LLCs. The daily operations of the LLC can also be delegated to a professional manager, which is called a manager-managed LLC. If the original organizer of the LLC chooses, they can organize an LLC in which the owners (members) will have little or no management responsibility because it has been delegated to a professional manager. These options when drafting an LLC's operating agreement allow an LLC to operate in different ways, so that an entrepreneur can develop a business structure best suited to the needs of the business.

As long as the members (owners) do not use the LLC as an alter ego and/or commingle personal funds with

16 Scott A. Hodge. "The U.S. Has More Individually Owned Businesses Than Corporations." *Tax Foundation*. January 13, 2014. https://taxfoundation.org/us-has-more-individually-owned-businesses-corporations/

LLC funds, the LLC provides the corporate shield of limited liability to the investors. If the LLC is operated to protect a sole proprietor, this might become an issue if the sole proprietor commingles funds. Commingling funds or assets gives rise to the sole proprietor or other members of a multi-owner LLC being liable for all of the debts of the LLC. Generally, the ownership of an LLC is represented by percentages or units. The term *shares* is not used in operating agreements because LLCs cannot sell shares of stock like a corporation can; thus, owners are not technically shareholders.

Taxation of LLCs

Entrepreneurs are able to make decisions regarding the taxation of LLCs. The government can tax the business as a corporation or as an individual. This choice may involve more than simply a tax rate decision; it might involve ownership and management issues, as well other financial considerations. However, this section will focus on the tax decision aspect of the issue.

A multi-owner LLC's default taxation is as a partnership, meaning profits pass through and are taxed on the owner's federal tax return. However, LLCs can elect to be taxed as either a partnership or a corporation. Single-member LLCs can also be taxed as a sole proprietorship or as a corporation. The fact that an LLC can select its method of taxation as either a C corporation, S corporation, or partnership allows the entrepreneur flexibility in creating the business structure of their choosing. Note, however, that tax laws change. For example, the Tax Cuts and Jobs Act of 2017 may make formation as an S corporation more attractive to some entrepreneurs than formation as an LLC, at least as far as taxation is concerned. You should seek advice from a tax accountant to ensure that you are able to make decisions based on the most current regulations.

13.5 Sole Proprietorships

Learning Objectives

By the end of this section, you will be able to:

- Describe the ownership structure of a sole proprietorship
- Explain the advantages and disadvantages of operating as a sole proprietor

A **sole proprietorship** is a business entity that is owned and managed by one individual and has very little formal structure and no mandatory filing/registration with the state. This type of business is very popular because it is easy and inexpensive to form. The owner, called a sole proprietor, is synonymous with the business and is therefore personally liable for all debts of the business. Sole proprietors do not pay separate income tax on the company, instead reporting all losses and profits on their individual tax returns.

Overview of Sole Proprietorships

Entrepreneurs solely operating their own businesses are called sole proprietors. According to the Tax Foundation, there are more than 23 million sole proprietorships in the US, far more than any other type of business entity.[17] This statistic means that the sole proprietorship is by far the most common business structure, even though the business is not legally separate from its owner. The primary reason that many entrepreneurs choose the sole proprietorship format is that they do not have to make a choice, get professional advice, or spend any money. An entrepreneur who just starts doing business is automatically a sole proprietorship unless they elect to become a different type of entity and file that paperwork. An entrepreneur who becomes a sole proprietor does not necessarily have to go to an attorney or an accountant, or file any documents, making a sole proprietorship quick, easy, and cheap to form and operate.

Another development related to the decision to be a sole proprietor is the rapid growth of the gig economy. Some individuals prefer to work on their own rather than become a full-time employee. Being a gig worker falls somewhere between being a business owner and being an employee, so many gig workers, ranging from drivers for a ride-sharing company to instructional designers, operate as de facto contractors who are sole

17 Scott A. Hodge. "The U.S. Has More Individually Owned Businesses Than Corporations." *Tax Foundation*. January 13, 2014. https://taxfoundation.org/us-has-more-individually-owned-businesses-corporations/

proprietors.

However, there remains a debate about whether these gig workers should be deemed sole proprietors. Recently, California passed a new law, signed by Governor Gavin Newsom, which extends wage and benefit protections to many thousands of workers who were previously self-employed sole proprietors working in the gig economy. The new law is based on the presumption that when workers are misclassified as independent contractors rather than as employees, they lose basic benefits such as a minimum wage, paid sick days, and health insurance.

The sole proprietorship is the simplest method to operate a business—often under the owner's name—and the owner is typically taxed directly by the IRS by attaching a Schedule C (Profit or Loss) form to the owner's individual tax return. In order to document one's income, instead of being provided a Form W-2 from one's employer, many self-employed individuals receive one or more 1099-MISC (Miscellaneous Income) forms from clients, which typically demonstrate that the taxpayer is operating a sole proprietorship. Sole proprietors are allowed to deduct their business expenses related to their income and, as both employer and employee, are required to pay the full amount of employment taxes for Social Security and Medicare.

An owner can also operate under a DBA or "doing business as" filing. A DBA is filed at the relevant state or local government office where the sole proprietor wants to operate under an assumed name. Technically, this is not a new organization: It is just a different name. Any business entity may file for a DBA to operate under an assumed name, and many individuals operate under a DBA to indicate the type of services they are providing, such as Smith's Roofing Company. It is not uncommon for an individual to name a sole proprietorship using LLC or Co. in its name; however, an individual operating under a DBA or assumed name is not provided any of the protections provided to a corporation of LLC, even if Inc. or LLC is used in the assumed name. A sole proprietor needs to consider the impact of using an assumed name prior to creating a DBA.

Advantages and Disadvantages of Sole Proprietorships

The sole proprietor is personally liable for everything. A sole proprietor is the investor, owner, and manager of the business enterprise. The sole proprietor is personally liable for all of the taxes and any unpaid debts of the business venture. The sole proprietor also has no business to sell and can sell only assets related to the business. The sole proprietorship is the easiest business to start but has almost no differentiation from the individual starting the business.

Taxation of Sole Proprietorships

A sole proprietorship is not taxed as an entity. All profits pass through to the owner who pays individual income taxes on all profits earned. It does not matter whether the owner takes the money out of the business or leaves it in the business; all profits are taxed to the individual owner. This is an area that requires significant planning and may be a potential disadvantage, depending on how the individual owner's personal rate compares to the corporate rate.

Other Low-Risk Entry Structures in Entrepreneurship

Over the past decade, various alternatives to traditional employment have become popular, leading many to become entrepreneurs rather than employees. The US Bureau of Labor Statistics reported that, in 2019, there are 55 million people in who are "gig workers," which is more than 35 percent of the US workforce. That percentage is expected to increase to 43 percent by 2020.[18] This offers both an opportunity and a challenge. There is a modicum of security when one is an employee of a company, which may not exist in the same way for someone who is freelancing or working as a contractor. There are many examples today of people becoming small entrepreneurs. This process goes by a variety of names, such as the sharing economy, the gig economy, the peer economy, or the collaborative economy. Maybe it means driving for a company such as Lyft, Uber, or GrubHub, or perhaps offering services through TaskRabbit, UpWork, or LivePerson.

18 Quora. "What Are the Pros and Cons of the Gig Economy?" *Forbes*. January 8, 2019. https://www.forbes.com/sites/quora/2019/

ARE YOU READY?

Online Resources for the Gig Economy

The website business UpWork provides a platform for individuals to offer their services to large companies on a freelance or contract basis. Do you have skills as a web, mobile, or software developer, or perhaps in the area of data analytics? The UpWork website (https://openstax.org/l/52UpWork) says that over 5 million businesses use people listed on UpWork, including companies such as Microsoft and General Electric.

Offering your services in this new manner is not controlling of what type of entrepreneurial enterprise you want to be. You can do most of these types of things as a sole proprietor, an LLC, or an S corporation. According to the Tax Foundation, over the past thirty-five years, the number of C corporations has declined significantly, while the total number of pass-through businesses including LLCs, S corporations, partnerships, and sole proprietorships has tripled to over 30 million. According to estimates, there are only 1.7 million C corporations, whereas there are 7.4 million LLCs, partnerships, and S corporations, and a whopping 23 million sole proprietorships.[19] The explanation for these statistics is really quite simple. LLCs have quickly become one of the most popular business structures due to ease of formation and operation. Likewise, sole proprietorships are quick, easy, and low cost compared to corporations, which are more difficult and expensive to form and operate. The choice is open and depends on the variables discussed in this chapter.

ENTREPRENEUR IN ACTION

Nic & Luc Jam[20]

In an interview with the Balance, entrepreneur Leroy Bautista summarized his path to becoming a small business owner. He worked in high-end restaurants and successful catering companies for two decades before he was laid off during the economic downturn. Bautista didn't sulk or settle for a lousy job. Rather, he saw it as a chance to finally do what his coworkers and friends had been telling him to do: go out on his own, making his sauces and vinaigrettes, and selling them at local markets. It was out of necessity that the Nic & Luc company was born.

Originally selling just a few flavors, he now sells almost twenty flavors. For many small businesses, the word "local" is used as a marketing ploy, but for Nic & Luc, it is part of the business purpose and a core value. Bautista thinks it is important to support other local businesses like himself.

This is not a story that someone like Bezos or Gates might tell: It is much more basic, but it demonstrates how people at all levels are becoming business owners. Each one of them, including Leroy Bautista in this story, must make decisions about mundane things such as taxes, and liability; it can't be all about jam.

01/08/what-are-the-pros-and-cons-of-the-gig-economy/#3e1dc24e1388

19 Scott A. Hodge. "The U.S. Has More Individually Owned Businesses Than Corporations." *Tax Foundation*. January 13, 2014. https://taxfoundation.org/us-has-more-individually-owned-businesses-corporations/

20 Alton, Larry. "4 Small Business Success Stories for New Entrepreneurs." *The Balance Small Business*. February 5, 2019. https://www.thebalancesmb.com/small-business-success-stories-to-learn-from-4151885

13.6 Additional Considerations: Capital Acquisition, Business Domicile, and Technology

Learning Objectives

By the end of this section, you will be able to:

- Describe the capital acquisition opportunities available to different types of business structures
- Explain how the advantages and disadvantages of where a business is registered should inform the decision of where to create a business domicile
- Understand the role technology considerations may play in selecting a business structure

In addition to the main entity selection topics already discussed, such as ownership structure and taxation, there are other considerations that entrepreneurs might want to consider. For example, when choosing a business format, a founder would be interested in how to raise capital to use in the business.

Another issue to consider includes where to form a new business, since formation is largely a state issue, and there are fifty different states from which to choose. This has the potential to affect multiple aspects of one's business, including income and sales tax issues, government regulation, and litigation situs (location). For example, some states, such as Wyoming and South Dakota, have no corporate income or gross receipts tax at all; other states, such as California and New York, do have a state corporate income tax. For more information on the variation between all 50 states, see the following website operated by Cornell Law School: https://www.law.cornell.edu/wex/corporations.

Capital Acquisition

Once an entrepreneur has created a business plan, the next requirement is to capitalize the business venture. If the entrepreneur wants to start out small, a sole proprietorship is all that is needed, although even for small businesses, this structure carries a high degree of risk. Basically, the entrepreneur can simply start working on the business venture. If the entrepreneur's business venture is larger, raising capital becomes a major issue. This can be done though bank loans or investors.

Entrepreneurs eventually need capital to grow their business. Capital typically comes in the form of cash. Entrepreneurs need to consider the business structure they select for raising cash in the future if they plan to grow their business. Banks, family members, friends, or others can lend cash to an entrepreneur. These types of loans may not give the lenders ownership rights in the company. The lenders may take a lien on the assets of the business venture but do not necessarily have the right to run the business. Management is typically left to the owners when borrowing funds, but when a company receives investment funds, the investor also receives an equity share in the business and may be involved in management.

Owners and investors may want to have the right to operate the business or may want the investment structured in such a fashion so that the investors only participate in the profits or losses of the business, but do not operate the business. Depending upon the type of the business and the expectations of the entrepreneur and possible owners, this needs to be considered before creating a company. An entrepreneur raising capital needs to consider what participation is desired from investors and the timing of the needed capital. Remember, investors become owners, whereas lenders are not owners.

Capital is required at every step of a business. There can be lines of credit to finance operations as receivables are collected, and there can also be long-term borrowing for purchases of big-ticket assets required to operate the business. The difference between a loan and an investment is that the loan principal and interest must be paid back. However, an investment allows the investor to participate in the profits and losses of the business, but does not need to be repaid because investors can get a return on their investment by selling their interest in the business. Finding a good balance between how much ownership the entrepreneur wants to relinquish versus how much of the profits need to be paid to finance the business is key. The entrepreneur needs to determine this balance as the company grows. For example, Amazon started as a Washington state corporation named Cadabra, Inc., operating out of Jeff Bezos' garage, and then through several transactions

became the world's largest online retailer incorporated as a Delaware corporation with its ownership shares AMZN traded on the NASDAQ.

Growing companies will have different rounds of outside investment. Never consider that the first outside investment received will be the last investment. There will be more than one round of financing in most companies. As the investment and financing changes, there will be changes in the corporate structure of the business venture. Just like Amazon, a company can start in one's garage and then go on to be a company listed on a major stock exchange with a worldwide reach. Each step of the way takes careful planning (see Entrepreneurial Finance and Accounting).

Legal and tax issues are directly related to the agreements between entrepreneurs and their investors. The written agreements should spell out the corporate structure with specific details of the arrangement between the two. The business structure will drive the tax circumstances of the investment, business, and owners. This may change with new investors, so agreements should be flexible. Many times, a new investment in the same business may be created in which the new business structure purchases the assets of the old business structure. This event will change all of the agreements evidencing the structure of the venture.

Agreements describing how the owners share in profits and losses, and how the owners share in making decisions about the business venture can and do change. Many owners and entrepreneurs desire that their company become a publicly held corporation. This is a company with its ownership shares traded on a public exchange. The ease of buying and selling shares on a public exchange typically increases the value of the company. Therefore, many investors desire that shares ultimately become publicly traded. A company may start as a sole proprietorship, become an LLC, and then be converted into a corporation with its ownership shares traded on a public stock exchange. In the circumstance where the company is growing, the business structure will change over time.

Many publicly traded companies start as a privately held corporation before going public through an initial public offering (IPO). A recent example is Spotify, which in a 2018 IPO raised $9.2 billion.[21] A closely held corporation, which is essentially the same as a privately held company, has no public market for its stock. The owners, as members or shareholders, have more control over the directions of the company, until the company is taken public.

The assets of a closely held company can be sold to a company that is publicly traded, such as a reverse merger, or can be used to create a company that will pursue an IPO. Both of these are complicated endeavors that require audited financial statements, the assistance of lawyers and outside accountants, and the use of an investment bank. Each step of the way, the entrepreneur gives up some equity and control in the company in exchange for investment money to help the company grow. Most small companies becoming public will (but are not required to) list on a stock market like the Nasdaq SmallCap market or the Nasdaq National Market System. This development provides the company direct access to international capital markets and many new investors.

The issues that investors tend to look at include transferability or sale of their ownership interest, ability to raise additional capital, and protection of the investors' assets outside of the investment. If the entrepreneur is unconcerned about investment from outsiders, these considerations are not as important. Another issue is the ability to raise capital through banks or by using the SBA to guarantee a loan through a participating bank. The first step in getting an SBA loan is determining that the "business is officially registered and operates legally."[22] This means that the borrowing business is a company that is registered in a state to do business. An entrepreneur can borrow up to $4.5 million (the SBA limit[23]), to fund operations. However, the first step is to create a proper business entity to which the bank can loan the money or in which an investor can invest. The typical entities to which banks lend money and investors invest money are partnerships, LLCs, or corporations. To create these entities, an entrepreneur needs to file the appropriate paperwork within a given state.

21 Samuel Stebbins. "The Top 26 Largest Company IPOs of the Year." *USA Today*. December 7, 2018. https://www.usatoday.com/story/money/business/2018/12/07/top-ipos-2018-26-biggest-companies-went-public-year/38611947/

In addition to traditional sources of funding, including borrowing, taking on partners, and selling stock through an underwriter, there is a relatively new source of capital for small business entrepreneurs that is an important addition to the capital acquisition options for startups. **Equity crowdfunding** involves a startup raising capital through the online sale of securities to the general public.

In 2012, Congress enacted new legislation called the Jumpstart Our Business Startups (JOBS) Act, which amended US securities laws to enable small businesses to use a variation on a technique known as crowdfunding (see Entrepreneurial Finance and Accounting). Crowdfunding is already in use as a way to donate money to consumers and businesses through web portals such as GoFundMe, but those sites do not offer SEC-compliant sales of securities in a business, as the JOBS Act now permits. Emerging growth companies (EGCs) seeking capital are now able to raise equity capital more easily and at a lower cost. This new type of funding should help level the playing field for EGCs and is viewed by many as a way of democratizing access to capital.

Recall that crowdfunding allows the entrepreneur to raise money from a large number of people and can be in the form of either non-equity or equity crowdfunding. To illustrate the difference between non-equity crowdfunding and equity crowdfunding, consider these two examples. An example of non-equity crowdfunding is Betabrand. Betabrand is an online women's clothing company that allows users to vote on styles. If enough people "pre-order," the design goes into production. No ownership/equity is exchanged between entrepreneurs and the backers. On the other hand, AngelList, SeedInvest, or WeFunder are examples of equity crowdfunding. They help business owners raise money from individual investors. Remember that this means the investor will end up owning an agreed-upon portion of the business they invest in. For example, LIVSN is a startup apparel company that is using WeFunder to raise capital via individual investors. By the end of 2022, LIVSN had raised $419,000 from 474 investors.

LINK TO LEARNING

The Crowdfunder website (https://openstax.org/l/52Crowdfunder) connects to one of several different business-oriented equity crowdfunding websites. It offers EGCs or small business several avenues of funding, including equity, convertible notes, and debt. The primary advantage is the ability to raise equity capital without big fees, lots of federal regulations, and red tape.

Business Domicile: State and Local Considerations

There are multiple reasons why an entrepreneur may want to consider geographic location when forming and operating a business. Of course, one practical consideration is where the entrepreneur lives, at least in terms of operating a small local or regional business. However, there are other important considerations, such as differing formation/incorporation laws, widely varying levels of regulation, different types of permitting, and other relevant factors. As a rule, a corporation is considered a citizen of both its state of incorporation and the state of its principal place of business.

The state where a person lives is not necessarily the state in which they must form and/or operate the business. For example, if a person lives in the New York City metro area, they might well have a choice of New York or New Jersey, or even Connecticut, Delaware, or Pennsylvania. The same may be true for the metro areas of other large cities. Additionally, even if a person lives in the middle of North or South Dakota, they might choose to start a business in another jurisdiction, such as Delaware, Alabama, or Wyoming, due to favorable formation regulations. The following section discusses the issue of choice of jurisdiction when forming a limited liability entity such as a corporation or an LLC.

22 U.S. Small Business Administration. "Funding Programs." n.d. https://www.sba.gov/funding-programs/loans
23 U.S. Small Business Administration. "Loan Fact Sheet: The SBA Loan Guarantee Program: How It Works." October 2011. https://www.sba.gov/sites/default/files/SDOLoanFactSheet_Oct_2011.pdf

Choice of State When Incorporating/Registering Your Business

Business entities seeking the protection of limited liability must be registered with a state. This typically includes corporations, LLCs, and LPs. Additionally, if a corporation seeks to sell stock to investors in a specific state (called an intrastate offering), it must be registered in that state. The first step is to select the type of entity to be created and then file the appropriate paperwork with the state. Each entity is typically created through the office of the secretary of state (or, in the case of Kentucky, Massachusetts, Pennsylvania, and Virginia, the secretary of the commonwealth), with each state having a different process for creating the entity. The Balance, a small business resource website, lists all state government offices in which to file the appropriate paperwork (https://www.thebalancesmb.com/secretary-of-state-websites-1201005).

Forming a business in the state where the entrepreneur is physically located is generally the easiest way to create the entity through which the entrepreneur will conduct business. Some entrepreneurs choose to create their business entity in other states for privacy reasons or for tax savings. The entrepreneur will still have to file and pay taxes in every state in which the business operates and will have to register its presence in the state in which it is physically located. Some investors might prefer out-of-state incorporation, and the entrepreneur needs to remember that the corporation will be subject to taxes, filing requirements, and other fees imposed by each state of operation and the state of incorporation.

Delaware is a particularly popular state in which to incorporate due to the ease of regulations regarding ownership structure and business-friendly laws; Nevada and Wyoming are popular as well for the same reasons. The reason these states are popular is that initial fees are cheap, there are little or no renewal fees, and the states emphasize asset protection. While Delaware, Nevada, and Wyoming offer good reasons to incorporate, they are not best choice for every business. If a business incorporates in one state but does business primarily in another, in all likelihood, it may very well have to pay the second state's fees and/or taxes in addition to those of the first state. Entrepreneurs need to consider cost and ease of operations when determining the state in which to create their business entity.

Multistate Taxation

Most businesses have a website and are glad to sell products to any buyer, regardless of where the buyer is located. Amazon is an example of a company that capitalized on the concept of Internet sales. Amazon collects sales tax from all forty-five states that have a statewide sales tax because it owes tax in every state and city in which it operates.

Multistate taxation is not something that most small businesses consider, but it is an issue that can arise in many different circumstances. For example, professional basketball players may be taxed by the state, or even the city, in which they play. This means that an NBA player could owe taxes in over 20 states if he went to every game. Just sitting on the bench in 20 different states could trigger multistate taxation, and, if the team plays in other countries, foreign taxes could also be owed. This is true for every sport and every business that operates in multiple states or other countries. It is not only multibillion-dollar corporations that are affected, but small businesses and individuals as well.

Most online multistate businesses now collect and pay sales taxes in those states with a sales tax. This was not always the case, however. For years, Amazon and other online retailers sold products without collecting any state or local sales taxes at all. The legal requirement that companies did not have to collect sales taxes in a state unless they have a "physical presence," such as warehouses, offices, and/or employees, gave online companies carte blanche to ignore state and local taxes for many years."[24] Until the 2018 US Supreme Court decision in *South Dakota v. Wayfair*, states generally did not require online sellers to collect and remit sales tax to the state. However, this case changed the rules by creating the concept of an **economic nexus**, a virtual connection with a state based on sales volume or number of transactions. This now means, in most states, that if your business meets a threshold of $100,000 in sales in that state, it may now require you to collect sales tax on online transactions. Therefore, your online business may have to collect and remit sales tax to as many as forty-five states (five states do not have a sales tax). All entrepreneurs need to develop an understanding of how the Internet and the related tax laws and regulations will affect their planned business operations. Creating a company in another state will no longer automatically avoid multistate taxes and regulations.

Technology Considerations

Most new entrepreneurs have some familiarity with technology, whether something as basic as social media or more advanced as extensive website development skills. However, most small businesses face challenges in the areas of information technology security and compliance with legal and regulatory requirements.

Not all small businesses face these challenges. They are most common in companies that handle private information, such as health records or credit card data. The storage and protection of this type of information must comply with government regulations. For example, a small government IT contractor that deals with any type of classified governmental information would need to ensure classified information was protected per regulations and not at risk of exposure. In the healthcare field, recent hacks of patient health data, some of which are handled by small businesses such as a solo practice physician's office, demonstrate the challenges of data protection. It is a significant challenge for companies with relatively small budgets to protect data. Technology security adds large costs and requires skilled personnel, for any business, large or small. Figure 13.10 summarizes the choices of business structure discussed throughout this chapter.

24 "Amazon's Local, State and Federal Tax Issues Explained." n.d. https://itep.org/amazons-local-state-and-federal-tax-issues-explained/

Entities	Owners	Liability	Taxes	Formation	Management	Capital
C Corporation	Unlimited number of shareholders allowed	No personal liability of shareholders for liabilities of corporation	Taxed on profits, shareholders also taxed on dividend	Articles of Incorporation, Bylaws, Resolutions, Stock Certificates	Board of Directors, Officers	Shareholders purchase stock, which creates capital for the corporation
S Corporation	100 shareholders allowed	No personal liability of shareholders for liabilities of corporation	Not taxed as corporation; profits are passed through to shareholders who pay taxes	Articles of Incorporation, Bylaws, Resolutions, Stock Certificates, IRS S Corp election form	Board of Directors, Officers; if close corporation, owners can manage directly without a board	Shareholders purchase stock, which creates capital for the corporation
Sole Proprietor	One owner	Total personal liability for liabilities of business	Owner pays taxes	Usually no government filing required; DBA form needed if using an assumed name	Owner manages business	Owner puts in own capital and/or borrows from bank
General Partnership	Unlimited number of general partners	General partners have personal liability	Profits passed through to general partners who pay taxes	Usually no government filing required; General Partnership Agreement	General partners have equal management rights unless they agree otherwise	Partners contribute capital
Limited Partnership (LP)	Unlimited number of general and limited partners	General partners have personal liability; limited partners do not have personal liability	Entity not taxed; profits passed through to partners who pay taxes	Limited Partnership Certificate, Limited Partnership Operating Agreement	General partner can manage the business; limited partners do not participate in management	General and limited partners contribute capital
Limited Liability Company (LLC)	Unlimited number of members allowed	Member does not have personal liability	Taxed as a partnership	Articles of Organization or Formation, Operating Agreement	Managed by members collectively or managed by a single member	Members contribute capital

Figure 13.10 The characteristics of different business entities [C-Corporation, S-Corporation, Sole Proprietor, General Partnership, Limited Partnership (LP), and Limited Liability Company (LLC)] are provided in terms of owners, liability, taxes, formation, management, and capital. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

13.7 Mitigating and Managing Risks

Learning Objectives

By the end of this section, you will be able to:

- Explain Enterprise Risk Management and how a company uses it
- Describe litigation and financial risks
- Describe common insurance needs

Risk management is key to operating any business in a profitable fashion. There are many risks facing an entrepreneur when starting and operating a new business venture. The trick is to eliminate risks that will hurt the venture, while taking on risks that will provide for long-term profitability. The risks facing the entrepreneur need to be initially identified as part of developing a business plan and revisited regularly in ongoing operations. Preparation for adverse events affecting a new business venture is necessary, but being too pessimistic or allowing fear of adverse events to stop an entrepreneur from taking any risk will keep a business venture from achieving it greatest potential and profit.

It is important that an entrepreneur develop an understanding of the risks of the business environment. The risks include liability risks stemming from contracts and torts, sometimes referred to as operating risks, regulatory compliance risks, financial risks, and strategic risks, including taxation. Understanding how the

business structure is used to operate the business venture allows the entrepreneur to develop a plan to manage business growth and understand business risk.

Enterprise Risk Management

Profitable ventures develop a strong **enterprise risk management** program, which is an integrated, cross-disciplinary approach to monitoring risk. An organization needs to look at both long-term and short-term risks at all levels of the organization, and these risks need to be evaluated from all stakeholders' perspectives and developed into an entity-wide program.

Enterprise risk management attempts to address the specific risks discussed in the preceding section by implementing a risk program that enables a business to identify and manage risk. Specifically, a business will go through a process that involves a multistage process of risk identification, risk assessment, and risk abatement. Examples of risks that businesses face include those from natural causes, economic causes, and human causes.

Natural causes of risk include disasters such as hurricanes and flooding, as well as earthquakes or other catastrophes that result in loss of life and property, as well as business interruption. For example, a business in New Orleans could be flooded by a hurricane. This results in damage to facilities and products, and threatens the lives of workers. In order to counter such causes, businesses need to plan ahead for business continuity, take out comprehensive insurance coverage, and have an evacuation/shut-down plan in place.

Economic causes of risk include global events leading to rising prices of raw materials, currency fluctuation, high interest rates, and, of course, competition from other companies in the same industry. An example of this would be unpredictable trade wars with China, leading to tariffs.

Human causes of risk refer to actions by employees, contractors, and those persons over which a company has control. These events can include torts stemming from negligence at work, labor strikes, shortages of qualified trained workers, and corporate mismanagement. An example of this type of risk would include embezzlement of money by an internal financial executive.

The use of a comprehensive approach allows a business entity to review and combine all risks into a functional perspective that allows the entrepreneur to evaluate risks and integrate new risks as different opportunities become more important to the business venture. Businesses sometimes use a risk matrix to assess or characterize the probability and impact of risk (Figure 13.11). The use of such a tool can help a business quantify risk and decide whether to undertake an activity based on its level of risk.

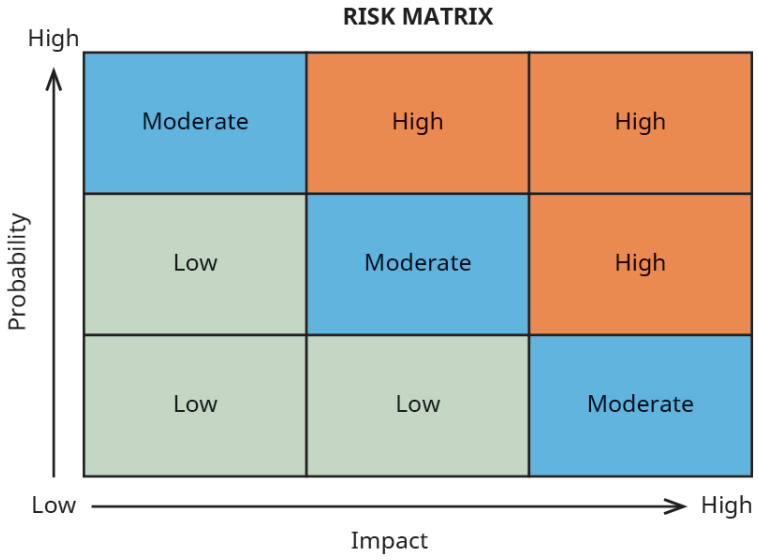


Figure 13.11 A risk matrix can be a useful tool to assess the likelihood and severity of risk that a venture may have. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Risk appetite is important for a business venture to consider, both when creating its business structure and during ongoing operations. Table 13.1 shows an overview of the considerations a business venture should entertain in both its creation and operation.

Risk Appetite[25]

Risk Item	Consideration
Existing risk profile	Current level and distribution of risks across the business and across risk categories
Risk capacity	Amount of risk the business can support while pursuing its objectives
Risk tolerance	Amount of variation the business can tolerate while pursuing its objectives
Risk attitude	Management's attitudes toward growth, risk, and return

Table 13.1 COSO's *Enterprise Risk Management, Understanding and Communicating Risk Appetite* outlines these considerations for assessing a business's appetite for risk.

This is the basic approach to evaluating a new venture's appetite for risk. Determining and understanding the risks facing a new venture should start during the preparation of the business venture's written business plan and should continue through the operations of the venture.

LINK TO LEARNING

The Committee of Sponsoring Organizations of the Treadway Commission, also known as COSO, deals with risk management. The mission statement of the COSO (https://openstax.org/l/52COSOmission) is "to provide thought leadership through the development of comprehensive frameworks and guidance on enterprise risk management, internal control and fraud deterrence designed to improve organizational performance and governance and to reduce the extent of fraud in organizations."

Legal Risk and Protection

Business operations of any sort need to follow business regulations and laws. The failure to follow business regulations may lead to fines, lawsuits, or even criminal penalties. **Legal risk** stems primarily from a breach of contract and/or the commission of a tort. Common examples of this type of risk includes product liability lawsuits. These lawsuits are frequently very expensive class action lawsuits or regulatory investigations of dangerous products. There are many famous case examples including automobiles, asbestos, pharmaceutical drugs, breast implants, and airplanes.

Other lawsuits stem from contracts, including borrowing money from a bank. The business has an obligation to pay it back, or it breaches a covenant within a contract. Other common types of contracts are those used in selling services and products, leasing real estate, and other similar contractual obligations.

Due to liability risks, business owners and investors are always looking for ways to limit their personal liability. Incorporation is a standard risk protection strategy for this potential problem, as are the use of other types of limited liability structures such as LLCs. This is one of the main advantages of properly operated corporations and LLCs, which allow for limited personal liability of owners and investors. Partners in GPs and sole

25 Rittenberg, Larry and Frank Martens. "Committee of Sponsoring Organizations of the Treadway Commission (COSO)". *Enterprise Risk Management, Understanding and Communicating Risk Appetite*. January 2012. https://www.coso.org/Documents/ERM-Understanding-and-Communicating-Risk-Appetite.pdf

proprietors are personally liable for all of the debts of the business, even beyond their own investment in the business.

However, a particular challenge for small business entrepreneurs is that even when they form a corporation or LLC, many lenders, landlords, and other entities providing credit to a small business circumvent the limited liability protection by requiring owners and investors to personally guarantee the debts of the business operations. This means that the owner who personally guarantees the credit will have to pay back the obligation if the business cannot. An owner can obtain insurance or borrow money for such guarantees. LLCs and corporations do protect their owners, shareholders, and members from a number of different tort claims, such as personal injury lawsuits and claims made directly against the organization.

Financial Risk and Protection

An entrepreneur needs money to launch a business, whether that comes in the form of loans from family, their own savings, or investors. The founder will be expected to put their own money at risk, whether in the form of a loan to their own business or equity in their own business. If they do not have any "skin in the game," then others will not be interested in loaning them money. This means that if the business fails, it will have repercussions for the owner, even if they operate as a corporation or LLC. This is the essence of **financial risk**: starting a new business with insufficient funds to sustain operations over an extended period of time.

Any new business owner needs to have a sound financial strategy as a part of the overall business plan. This should show income projections, the liquid assets that will be required to break even, and the expected return on investment for all investors in the first five-to-ten-year timeframe. Failure to accurately plan could mean that the entrepreneur risks business closure and bankruptcy, and investors get nothing.

Insurance Protection

Risk management and protection are enhanced with the purchase of different types of **insurance**, which involves spreading risk over a large number of people (policyholders). If a company is a corporation, it may need directors' and officers' liability insurance to indemnify the directors and officers if they get sued. Another insurance policy many companies get is called errors and omissions insurance, and this insurance coverage protects employees in negligence claims and cases if employee theft. Other types of insurance policies that most businesses carry include automobile insurance, health insurance, property insurance, and cyber/data breach insurance. Insurance coverage for a business venture needs to be specific to the business structure and its operations. Keep in mind that not all risks can be insured against—for example, a bad economy that leads to a loss of business or a bad decision by the owner to enter a market that does not work out.

Information Technology/Cybersecurity for Small Businesses

According to the SBA, the risk of hacking, ransomware, and customer privacy are equally as significant for most small businesses as for larger ones. The SBA has set guidelines related to cybersecurity for entrepreneurs. The SBA recommends the ten-step action plan shown in Table 13.2.

Small Business Administration Recommendations for Cybersecurity[26]

Step	Action
1	Protect against viruses, spyware, and other malicious code
2	Secure your networks
3	Establish security practices and policies to protect sensitive information

Table 13.2

Step	Action
4	Educate employees about cyber threats and hold them accountable
5	Require employees to use strong passwords and change them often
6	Employ best practices on payment cards
7	Make backup copies of important business data and information
8	Control physical access to computers and network components
9	Create a mobile device action plan
10	Protect all pages on your public-facing websites and apps, not just the checkout and sign-up pages

Table 13.2

The Federal Communications Commission joins the SBA in the preceding recommendations. For more information, see the following website: https://www.fcc.gov/general/cybersecurity-small-business.

WHAT CAN YOU DO?

Managing Payment Data

If you operate a small business, are you prepared to deal with hackers who break into your website and steal credit card data from consumers who bought your products online? Small businesses running an e-commerce site must comply with the Payment Card Industry Data Security Standard (https://www.pcisecuritystandards.org/). This is a regulation that could cause severe legal risk for entrepreneurs if your system is compromised, and credit card data are stolen. Consumers rightfully expect and demand a safe online experience when they visit your site. Have you paid an expert to evaluate your system and install the best security system? It may be costly, but perhaps not as expensive as the damages you could be ordered to pay by a court if credit card data are hacked.

26 Rebecca Martin. "Protecting Assets from Cyber Threats." *News Tribune*. November 7, 2016. https://www.newstribune.com/news/business/story/2016/nov/08/protecting-assets-cyber-threats/647637/

Key Terms

B corporation business that meets a very high standard of social and environmental performance, public transparency, and accountability to balance profit with social purpose
business purpose reason the entrepreneur forms the company and determines who benefits from it, whether it is the entrepreneur, customers, or some other entity
business structure legal organization of a business; also called *entity selection*
C corporation corporation taxed the corporate level, and then again on the owners' personal income tax returns if corporate income is distributed to the shareholders as dividends
capital money raised for operating a business
corporation complex business structure created by filing the appropriate documents with the state of incorporation
economic nexus virtual connection with a state based on sales volume or number of transactions
enterprise risk management integrated cross-disciplinary approach to monitoring risk
equity crowdfunding raising of capital through the online sale of securities to the general public
financial risk starting a new business with insufficient funds to sustain operations over an extended period of time
for-profit business business structure designed to create profits that are distributed to the owners
general partnership business created when two or more individuals or entities agree to work together to operate a business for profit
insurance spreading risk over a large number of people (policyholders)
joint venture temporary partnership in which two different enterprises combine for the purpose of mutual benefits such as sharing of expenses and to work toward shared goals and the associated potential revenue
legal risk risk stemming primarily from a breach of contract, a regulatory violation, and/or the commission of a tort
limited liability company (LLC) hybrid of a corporation and a partnership that limits the owner's liability
limited liability partnership (LLP) business arrangement for professional partnerships, such as law firms or accounting firms, in which partners are licensed professionals, with limited liability for financial obligations related to contracts or torts, but full liability for their own personal malpractice
limited partnership (LP) business arrangement that has at least one general partner and one or more limited partners
not-for-profit organization (NFPO) business structure that is usually dedicated to furthering a particular social cause or for advocacy related to a common shared interest by using its surplus revenues to achieve its ultimate objective
partnership business entity formed by two or more individuals, or partners, each of whom contributes something such as capital, equipment, or skills
privately held corporation company that does not allow members of the investing public to own stock; instead, it is owned by the founder's family or friends, or a private group of investors
public corporation quasi-governmental entity, a corporation owned or sponsored by the government
publicly held corporation entity in which members of the investing public own the stock
S corporation "pass-through" entity, also known as a small corporation, where shareholders report and claim the business's profits as their own and pay personal income taxes on it
sole proprietorship business entity that is owned and managed by one individual that has very little formal structure and no mandatory filing/registration with the state

Summary

13.1 Business Structures: Overview of Legal and Tax Considerations

Being an entrepreneur carries with it the responsibility to make significant decisions, the first of which is to decide the business purpose: For example, who should benefit from the creation of the entity? The second

important decision to make is whether you are going to be a for-profit or not-for-profit business. This decision is closely related to the business's purpose and is not necessarily controlled by how much revenue you think you might have but rather by who is going to "own" the entity and what it does with the profit it makes. A third decision to make is the type of business entity or structure. Choices include corporation, LLC, partnership, and sole proprietorship.

13.2 Corporations

When forming a corporation, there are numerous choices. One choice is whether to form a C- or S corporation. This is primarily a tax decision, with C corporations being taxed as corporations, and S corporations being taxed as partnerships. Which one is the best for you depends on a number of variables, including how many shareholders you aim to have and how much of the revenue you want to leave in the corporation versus take out of it in the form of dividends, considering possible double taxation issues. Another choice is whether you want to go through the process of becoming a certified B corporation through adherence to a number of social/sustainability guidelines. Finally, you must decide if you eventually want your equity (stock) to be publicly held, as it is in most large companies, or privately held, which may give you more control but limit access to capital.

13.3 Partnerships and Joint Ventures

Partnerships are a popular form of doing business. Within the structure of partnerships, there are multiple entities or structures. Making the choice can be rather complicated because an ill-informed choice could result in legal problems. Choices include a GP, LP, LLP, and LLLP, each with a different set of circumstances that might make it the right or wrong choice. The factors that would play a role in selecting which type of partnership to form include business purpose, management structure, taxation, and liability. In addition to partnerships, a related type of entity is a joint venture. Joint ventures can be combinations of two or more business entities that decide to come together for a limited period of time for a specified purpose.

13.4 Limited Liability Companies

LLCs have become, over the past twenty-five years, one of the most popular business entities for new startups. The phenomenal growth in LLCs is due to a straightforward equation: easy formation + easy operation + limited liability = popularity. LLCs offer entrepreneurs several qualities that they seem to like: They are low cost, low maintenance, protect the owner's personal assets from liability, and offer flexible taxation choices.

13.5 Sole Proprietorships

The sole proprietorship structure or entity is the most common form of doing business in the US. It is easy and inexpensive to form, is directly managed by the owner, and is subject to minimal regulation in terms of its formation and/or operation. However, with these good points are also some drawbacks. The owner has unlimited personal liability for all business-related obligations, which makes using this form of business very risky. Additionally, the only way a sole proprietor can remain that way and get access to capital is to borrow money from the bank or a perhaps a family member. Sole proprietorships cannot sell stock like a corporation can nor can they take on more partners as in a partnership or LLC.

13.6 Additional Considerations: Capital Acquisition, Business Domicile, and Technology

Multiple considerations play a role in the selection of the best business structure for each entrepreneur. This decision flows from the entrepreneur's vision of how the proposed business will operate and affects all aspects of business operations. The decision includes issues related to legal liability, taxation, and the ability to raise capital. This process may also include consideration of the best state to form and operate in, as a result of taxation, regulation, and other related matters.

13.7 Mitigating and Managing Risks

Risk is part of the equation for any startup business. There is no way to protect against every risk. However, there is a way to identify risk, plan for it, manage it, mitigate against it, and protect against it to an extent. The key to understanding and dealing with risk is not to take a utopian approach to a business startup, thinking that it will never happen to you. Risk is omnipresent. Statistically, some unexpected things will happen. Thus, the best approach to risk is to consider and implement strategies to help you and your business deal with it such as incorporation, insurance, and monitoring.

Review Questions

1. A not-for-profit business _____.
   A. is allowed to retain earnings for use within the organization
   B. must distribute profits to shareholders
   C. must turn over to the government any excess earnings
   D. can pay dividends to shareholders

2. The term "for-profit corporation" means which of the following?
   A. The business must make a profit or forfeit its status.
   B. The business may make or lose money without changing its status.
   C. The business is not allowed to sell stock to the public.
   D. The business must have more than 100 shareholders.

3. Which of the following business structures often involve two or more businesses starting a new business together?
   A. sole proprietorship
   B. general partnership
   C. joint venture
   D. corporation

4. How is an S corporation taxed?
   A. at the entity level as a corporation
   B. at the owner level as if it were a partnership
   C. at both the entity and owner levels
   D. at a special lower rate of income tax

5. A public corporation is _____.
   A. owned or sponsored by the government
   B. owned by member of the investing public
   C. owned by a combination of public and private investors
   D. none of these choices are correct

6. A C corporation is taxed _____.
   A. at the entity level
   B. at the individual level
   C. at both the entity and individual levels potentially
   D. only at the state level, not federal

7. Limited liability partnerships (LLPs) _____.
   A. are normally used for firms that consist of licensed professionals such as lawyers or accountants
   B. can be used for partnerships that sell services but not goods

C. are used for firms that do business across state lines
D. require that the stock be owned by fewer than 100 shareholders

8. A joint venture _____.
A. must be a corporation
B. can choose to be any type of entity
C. must be either a partnership or a C corporation
D. None of these choices are correct

9. General partners have what type of liability?
A. limited
B. joint and several
C. joint only
D. personal only

10. Of all the business entity choices, LLCs are the most like _____.
A. S corporations
B. C corporations
C. sole proprietorships
D. joint ventures

11. LLC owners are called _____.
A. members
B. shareholders
C. limited equity investors
D. directors

12. LLCs offer flexible tax treatment, meaning _____.
A. they can be taxed like corporation
B. they can be taxed like partnerships
C. they can be taxed like proprietorships
D. All choices are correct.

13. Sole proprietorships offer limited liability _____.
A. if you register it with the state
B. if you elect to be taxed as a corporation
C. if you have an SBA loan guarantee
D. Sole proprietorships never have limited liability.

14. A sole proprietorship _____.
A. pays taxes at the highest corporate rate
B. pays taxes at the lowest corporate rate
C. pays taxes at the individual rate
D. None of these choices are correct.

15. Sole proprietorships _____.
A. must register with the state
B. are similar to general partnerships in terms of liability
C. are similar to LLCs in terms of liability
D. are not allowed by law to operate outside of the US

16. States can levy a sales tax on items sold online to a customer in a different state if _____.
A. the business has a nexus with that state
B. there is a contract between the business and the state comptroller
C. the items sold are over $300
D. the business is one that only sells foreign-made items

17. As a general rule, LLCs, GPs, and SPs are taxed as _____.
A. corporations
B. not taxed
C. individuals
D. taxed twice, once as entity and once as individuals

18. Entrepreneurs can choose what state to incorporate in, and many choose _____.
A. New York
B. Delaware
C. California
D. Texas

19. Enterprise risk management includes _____.
A. identifying risk
B. risk assessment
C. risk abatement
D. All of the choices are correct.

20. A business owner can insure against all but which one of the following?
A. earthquakes
B. a bad economy
C. flooding
D. hurricanes

21. Examples of risk facing a business include _____.
A. human risks
B. economic risks
C. natural risks
D. All of the choices are correct.

Discussion Questions

1. Distinguish between for-profit and not-for-profit entities.

2. What are the distinguishing characteristics of a B corporation?

3. Why would an entrepreneur choose to operate an S corporation rather than a C corporation?

4. What are the choices of entities for operating as a group of engineers?

5. How does a joint venture differ from the other business structures?

6. Distinguish between LLC and LLPs.

7. Why are there more sole proprietorships than any other business entity in the US?

8. What are the general guidelines used to determine where your business must pay sales taxes for sales made online?

9. Identify the common types of risks that a business may face.

Case Questions

1. The Big University football team, a member of the Southeastern Conference (SEC), brings in over $100 million a year in revenue, including TV rights, ticket sales, and bowl games. Seats to a game cost well over $100, and coaches are paid millions of dollars (more than anyone else at Big U, including the president). However, despite enormous revenues, universities and their football teams are considered not-for-profit organizations and pay no taxes on the $100+ million their football programs bring in. Should a university football program be allowed to exist as a not-for-profit organization?
2. Jai started a new sustainability-oriented business six years ago, making single-serve coffee pods out of recyclable paper, rather than plastic. The company, Jai's Pod, is now experiencing rapid growth. Jai started the company as an LLC but has been considering making a decision to incorporate. What are some of the advantages of changing to a C corporation?
3. You are headed off to college. Some close family members decide it would be a good idea to buy a house in the college town and then rent it out to students, with you also living there and actively managing it. Assuming you and your family buy it, what form of business would you select?
4. Jackson owns and runs a small computer repair business, a sole proprietorship, out of his home, with one employee. He also goes to small businesses at their locations, mostly cleaning viruses and doing other small maintenance tasks and repairs. A family physician's office calls him in for a repair. He sends his employee to do the repair. Unknown to him, his employee makes a copy of patients' personal information and sells it on the dark web. Jackson ends up being sued, and the plaintiffs ask the court to allow them to access Jackson's personal, nonbusiness bank account that also has his spouse's funds in the account. Can the plaintiffs take that money?

Suggested Resources

13.1 Business Structures: Overview of Legal and Tax Considerations

The Small Business Administration (SBA) has a great "tool box" for entrepreneurs. Tools include information on how to create a business plan and how to qualify for government contracts. It also has free online training classes and a list of networking events. Go to this link, and then click on "Create a Business Plan" and get started. SBA: https://www.sba.gov/tools

13.2 Corporations

A cost-effective solution for obtaining business counsel is the Service Corps of Retired Executives (SCORE), which provides free advice for small businesses and entrepreneurs. The SCORE organization is the nation's largest nonprofit network of volunteer, expert business mentors, with more than 10,000 volunteers in 300 chapters. You can find them at: https://www.score.org/

13.3 Partnerships and Joint Ventures

The IRS website has a clear explanation of partnerships with regard to taxation, regarding both income tax and employment/payroll taxes. You might find enough information here to help reduce the time you spend with a CPA, saving your company a lot of money: https://www.irs.gov/businesses/small-businesses-self-employed/partnerships

13.4 Limited Liability Companies

The SBA has an excellent website for LLC owners. It has information about multiple topics including comparisons with other structures, and links to other websites that offer good advice: https://www.sba.gov/business-guide/launch-your-business/choose-business-structure

13.7 Mitigating and Managing Risks

North Carolina State University, Poole College of Management, has an excellent enterprise risk management initiative. It has a wealth of helpful information for entrepreneurs on this topic: https://erm.ncsu.edu/library/article/coso-erm-framework

14

Fundamentals of Resource Planning

Figure 14.1 New Story is changing the way social enterprises manage resources through an innovative business model that uses crowdsourcing to fund construction. (credit: modification of photo provided by New Story)

Chapter Outline

14.1 Types of Resources
14.2 Using the PEST Framework to Assess Resource Needs
14.3 Managing Resources over the Venture Life Cycle

Introduction

New Story, a forward-thinking social enterprise, set out to solve a global issue that affects more than one billion people[1] worldwide: homelessness and lack of adequate shelter. The organization has impressed many investors by revolutionizing homebuilding techniques. Its founders—Brett Hagler, Alexandria Lafci, Mike Arrieta, and Matthew Marshall—share a passion for "improving lives through safe homes and a shared vision to change the traditional charity model."[2] When its founders realized the global need for proper shelter, many people having been displaced by natural disasters, they decided to take advantage of an alternate charity model by connecting with other building organizations and using crowdfunding. These four innovators combined their skills to create an organization that emphasizes building sustainable homes at a quick pace and affordable price. New Story's business model includes an innovative approach to home building and design by incorporating the needs of each family, local partners and workers, and crowdfunding campaigns to pay for construction.

At their start, New Story knew they needed the support of great mentors and an accelerator to raise funds for overhead costs, so they applied to one of the most prominent accelerators in the United States—Y Combinator, a community of founders that funds startups in an accelerated three-month development process. Optimizing this opportunity, New Story built 113 houses through their "100 Homes in 100 Days" campaign in Haiti, a challenge that Y Combinator posed to them. This experience enabled the New Story team to identify global partners that extended their reach to developing communities in Bolivia, Mexico, and El Salvador.

1 Joseph Chamie. "As Cities Grow, So Do the Numbers of Homeless." *Yale Global Online*. July 13, 2017. https://yaleglobal.yale.edu/content/cities-grow-so-do-numbers-homeless
2 New Story. "Founding Story." n.d. https://newstorycharity.org/about/

One of the best technological advances that New Story has leveraged in its collaborations with companies is the 3-D printer by ICON, which allows a home to be printed in as little as twelve hours for only $6,000. The 3-D printer uses three main components to build a house: robotics, a special mix of materials that dry quickly, and a tablet that runs the software needed to design the home.

By securing funding and finding local community partners, New Story has built sixteen communities, with more than 2,200 homes in four countries.[3] [4]

14.1 Types of Resources

Learning Objectives

By the end of this section, you will be able to:

- Distinguish between tangible and intangible resources
- Determine the venture's tangible and intangible resource needs and how to attain them
- Describe the various funding resources available to entrepreneurs and discuss the pros and cons of each

You have learned about many opportunities for entrepreneurs to explore and the processes that ensure their success. This discussion focuses on the various resources that entrepreneurs need to start, maintain, and grow an enterprise, and, in general, how to procure those assets. Many entrepreneurs make the mistake of moving forward in their business endeavor without taking enough time to research their industry and determine what resources are required to help their business not only get off to a positive start but also the resources needed for its continued operation. Entrepreneurial Marketing and Sales covered primary and secondary sources of information and how to make use of the information gleaned from them for marketing purposes. Much of that research also applies to questions surrounding resource allocation. But before we delve into allocation, let's examine the general categories of resources needed in just about every new venture: tangible, intangible, and financial.

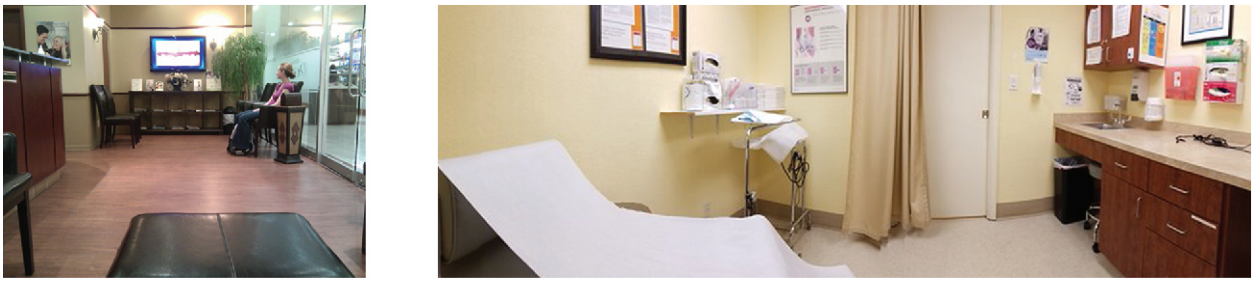
Tangible Resources

As you can imagine, resources needed for the enterprise are varied and can have different attributes. These assets are essential in the operation of the business enterprise. Assets (see Entrepreneurial Finance and Accounting) are property or resources that create a benefit to the person (or company) who owns them. They can be tangible or intangible. **Tangible resources** are assets that have a physical form. They can be seen, touched, and felt. Tangible resources differ between product-based and service-based businesses. A product-based business uses tangible resources in the production of goods sold to customers, such as raw materials, land, facilities, buildings, machinery, computers, supplies, and vehicles. The warehouse shown in (Figure 14.2) would be considered a tangible resource for a tire (product-based) company.

3 New Story. "Our Impact." n.d. https://newstorycharity.org/impact/
4 New Story. "Founding Story." n.d. https://newstorycharity.org/about/

Figure 14.2 Facilities, machinery, and other equipment are necessary tangible resources for a product-based company. (credit: "forklift warehouse machine worker" by "pashminu"/Pixabay, CC0)

Tangible resources for a service-based business include buildings such as a doctor's office, bank, movie theater, amusement park, retail store, or restaurant, which are enterprises that include both products and services (Figure 14.3). Facilities and resources that the business needs to provide its services and run operations may include computers, office equipment, furniture, and technological resources. As Figure 14.3 shows, the equipment and décor need to be taken into consideration because they becomes part of the product offerings, even if the core product is a service.



(a) (b)

Figure 14.3 Resources needed for a doctor's office include (a) furniture, decorations, and amenities for a waiting room and check-in areas, as well as (b) rooms with medical equipment and supplies in which to see and treat patients. (credit (a): modification of work by "icethim"/Flickr, CC BY 2.0; credit (b): modification of work by "osseous"/Flickr, CC BY 2.0)

Place of Operation

Your facility needs will depend on the type of product or service you are offering and vary in scope from office space to a food truck to a manufacturing facility to a storefront for sales. Knowing the limit of your budget (discussed in the next section) should help you focus on locations that you can afford. Experts recommend that you allocate only a certain percentage of your sales to your lease or purchase; some businesses use industry averages as guidelines. Factors to assess are location, visibility, foot traffic (how many potential customers walk by), how well the building has been maintained, the maintenance it will need in the future, how long you would want to stay in that location, and the insurance, property tax, and renovation costs, or the cost to build a new building. One approach is to make an assessment of your sales per square foot and compare those to sales of similar companies in the same industry or market. These data can be found through local commercial realtor offices, city or county government offices, and local associations.

Machinery/Equipment

Machinery and equipment are critical assets to helping launch a business. For service businesses, such as restaurants, dry cleaners, print shops, etc., the equipment can be expensive. In recent years, however, a larger

reseller market has emerged for many types of equipment that are still serviceable. It is important for tax purposes to report the current asset value of used equipment and have an accountant confirm its useful life for your income statement and tax returns. (See Business Structure Options: Legal, Tax, and Risk Issues for more information.)

For companies that manufacture products, you may have to order customized tooling and assembly equipment. Again, if you must acquire new equipment, you will need to understand what its useful life is and determine whether you must procure or acquire the equipment from a supplier who charges a "piece price" on top of each component or finished product they supply to you. If you choose this second approach, your supplier may insist on a long-term manufacturing agreement to manage their risk.

Vehicles

For some businesses, vehicles are necessary equipment to run day-to-day operations. You can use your own, which can be cost effective, or you can purchase or lease one. If purchasing a used vehicle, it is best to check the Kelley Blue Book (www.kbb.com), a reference guide that lists market prices, before purchasing it from a dealership; make sure that there are no defects or negotiate a lower price if you find them; and make sure to secure documentation on warranties. Other reliable valuation sources are carfax.com, nada.com, and edumunds.com.

Many small business owners are undecided as to whether buying or leasing a business vehicle nets better benefits. Let's assume for the purposes of this discussion that the vehicle is primarily a business vehicle and is not used a majority of the time for personal use. Relevant considerations include both tax and cost-related issues.

One difference between the purchase and lease of the vehicle relates to the tax deduction for depreciation. When you own a business vehicle, you can deduct a depreciation value over the life of the vehicle. Generally, you are not eligible to deduct depreciation on a leased vehicle. However, there is a corresponding difference with regard to the deductibility of monthly payments. With a leased vehicle, the monthly lease payments are tax deductible, whereas if the vehicle is purchased with a car loan, only the interest on the car loan is deductible as a business expense. Ultimately, the decision to lease or buy is one that an entrepreneur should make in concert with a tax advisor.

LINK TO LEARNING

There are also useful online calculators that can help small entrepreneurs explore the pros and cons of leasing versus buying a vehicle (https://openstax.org/l/52LeaseBuy) to inform these important business decisions.

Technology

No matter what business you are in, you must invest in technology to support your day-to-day operations. This typically includes computers and software, as well as Internet service and intranet/network functionality. The following list includes most of the basic investments you will need to make for your business:

- Computers: Laptops, desktops, and tablets are an obvious necessity for day-to-day tasks, communication, and even production of products or services. Think about the performance and attributes needed to operate the business for insight about what brand and quality to buy. A good operating system that can process calculations and requests faster can make your business operations smoother and more efficient.
- Internet: Every business must have strong and reliable Internet service to ensure connectivity of computers, routers, and peripherals. Communication in today's environment cannot happen without this technology, and there are many providers that have good packages for businesses to get the bandwidth necessary to operate a business and/or to provide connectivity to customers.

- Router: If you are using multiple computers, laptops, and printers that need to be connected to each other, you will need a wireless router. A wireless router will help you keep documents and printers accessible from anywhere in your office, even if it's a small home office. You can also have a hard-wired router, which blocks outside signal interference.
- Printer: Most businesses need a good quality printer for printing documents, marketing materials, and forms. Most printers now use color ink and come with the ability to scan and copy documents. They also vary in quality, so you will need to consider your printing needs and the costs of toner/ink to determine the level of quality you need.
- Server: If you need to store and retrieve data—such as customer profiles, emails, and sales information—you will likely need a server. The server is a hardware system with software that performs various functions that cannot be done from one computer.
- Cloud computing: Cloud services have emerged as a cost-effective way to process, store, and use data for company operations. Rather than host your data and systems on your own hardware services, many large companies like Amazon, Verizon, and Microsoft offer web services hosted on a network of computers. This option provides ongoing data integrity and security, while lowering the cost of IT services and equipment.
- Software: There are many software applications and tools that are essential for business operations. These tools support day-to-day tasks. Common software needs include accounting and billing software like QuickBooks, customer relationship management tools such as Salesforce or Marketo, word processing and spreadsheet software like Microsoft Word and Microsoft Excel, presentation software such as Microsoft PowerPoint, diagram tools like Draw.io, email marketing tools like Constant Contact or Mail Chimp, file management systems like Dropbox, online phone/meeting apps like Skype and Zoom, social media management systems such as Hootsuite, project management tools like Bootcamp, and more. Some of these tools are free. Others carry a cost but may have free trial periods if you need to test them before investing. Most offer easy subscription payment schedules that can be set up monthly or yearly, and include ongoing software updates.

Supplies

There are many other supplies needed to operate the business, mostly basic items that you might take for granted but that need to be expensed: paper, toner, files, staplers, writing utensils, cleaners, and so on. You will likely need basic office furniture too. You may also want to invest in certain amenities that create a working environment and set the stage for your envisioned company culture—whether that's a coffeemaker, a dartboard in a break area, or whiteboards for meetings and brainstorming.

Licenses and Permits

What types of licenses might be required to operate your business? You may need a basic business license or permit provided by the government for the business to be valid, such as registering as an LLC, partnership, or company (Business Structure Options: Legal, Tax, and Risk Issues discusses these business structures in more depth). These licenses let the government know what kind of activities the business performs and ensure taxes are collected properly. They also make your business a legal entity and prove that it exists in case you need funding or permits. Some businesses require a sales tax license for products and services, whether they are tangible or digital.

Other considerations include professional certifications that pertain to the industry you are working in, such as certifications in accounting (CPA), financial advising, cosmetic services, or healthcare. Many industries require licenses before you can begin to operate; such industries include healthcare, financial services, construction, real estate, insurance, transportation, and engineering. If you will be receiving customers in your home office or storefront, you may be required to undergo a home inspection, especially from the health department if you are in a foodservice industry. Signage outside your business location may also require a permit or compliance with local regulations.

Other permits that may be required for a building include a certificate of occupancy, fire, electrical, HVAC,

plumbing, and hazardous materials such as gasoline, diesel, oil, or compressed gas cylinders. Check the laws and regulations of your local and state governments to ensure your business meets the legal requirements for licensing and permits. You can do this by contacting the secretary of state in your state and also by contacting your local chamber of commerce. Importantly, these licenses and permits often carry a cost and should be part of your startup costs with renewals included in your operational budget.

ENTREPRENEUR IN ACTION

Service-Based versus Product-Based Resources

Go to bizjournals.com and select one of the small businesses profiled in the listings of current local business news. Select one service-based enterprise and one product-based enterprise. Make a list of all the different types of tangible resources they each need to start their enterprise and sustain it. How do the resource needs of each enterprise differ and how are they similar? What did you learn about resources from this activity?

Intangible Resources

Intangible resources are assets that cannot be seen, touched, or felt. Intellectual property—which includes creative imaginings such as formulas, designs, brands, and inventions—is an intangible resource, and so are the patents, trademarks, and copyrights that protect the intellectual property. For example, if you are a small business owner, you might want to protect your logo, company name, website, slogan, new product prototype, or maybe a newly developed manufacturing process that allows you to shorten production time.

In our current technological era, intellectual property has become more important than ever. The Ethical and Social Responsibilities of Entrepreneurs introduced you to intellectual property protection as an important measure to safeguarding creativity. Entrepreneurs must protect their ideas for as long as possible to sustain a competitive advantage. A competitive advantage for a business could be a formula for a product, like the recipes Kentucky Fried Chicken or Coca-Cola use for their food and beverage products. They protect their formulas so other companies do not replicate them and profit from them. Smaller companies can also invent new products, methods, and branding that will need to be protected. Patents, trademarks, and copyrights are three protections for this type of intangible resource.[5]

Patents

As Creativity, Innovation, and Invention discusses, a patent grants the owner the right to claim the ability to exclude others from making, selling, using, and importing a product or process to the United States for a period of time. This time is usually twenty years from the date the application was first submitted to the US Patent and Trademark Office (USPTO). This allows the inventor to recuperate the costs of researching and developing the novelty before competitors can copy it. Types of patents include utility, business process, design, and plant patents.

A utility patent is granted to an individual who invents or discovers something novel and purposeful such as a machine, a process, a product, an improvement to any of these, or even a composition of matter. Most patents awarded to inventors are utility or plant patents. The USPTO receives more than half a million applications each year.[6]

The application and approval process can take several years and can involve a substantial investment that can range from a couple thousand dollars to over $15,000, depending on the complexity and type of patent, as

5 United States Patent and Trademark Office. "What Are Patents, Trademarks, Servicemarks, and Copyrights?" *General Information Concern Patents.* October 2015. https://www.uspto.gov/patents-getting-started/general-information-concerning-patents#heading-2
6 United States Patent and Trademark Office. *Nonprovisional (Utility) Patent Application Filing Guide.* January 2014. https://www.uspto.gov/patents-getting-started/patent-basics/types-patent-applications/nonprovisional-utility-patent#heading-6

well as the fee for a patent lawyer. Lawyers can help with conducting a patent search and ensuring that the invention doesn't yet exist, while providing guidance on the application process. Patent attorneys are often expensive, charging between $200 and $800 an hour, but they can make the process easier.

Usually, the first application an inventor files is for provisional twelve-month patent protection, which covers the invention for the first year while the inventor waits for the approval of a final, nonprovisional patent. A patent examiner processes the application and determines whether to award the protection or not. Having the help of a patent lawyer is not necessary, but it usually makes the process easier and increases the odds of receiving the patent. Not having a lawyer can delay the process or prevent the inventor from getting the patent, especially if the inventor is not familiar with the process, or if the invention is complex. Choosing a lawyer carefully is important, as experience and knowledge of the process matters. If the patent is awarded, the final patent goes into effect retroactively to the filing date of the provisional patent, and the inventor has twenty years of protection against other companies copying the design. Figure 14.4 shows an example of a patent for the well-known 3-D printer, which was awarded in 1986 to its inventor Chuck Hull.[7]

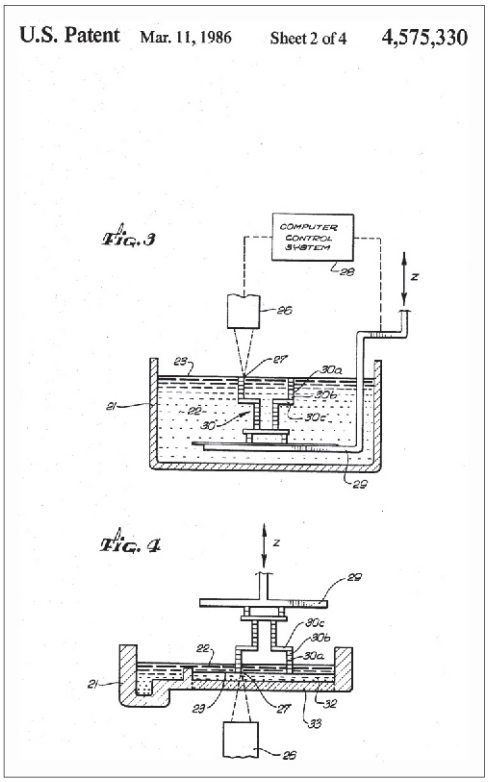


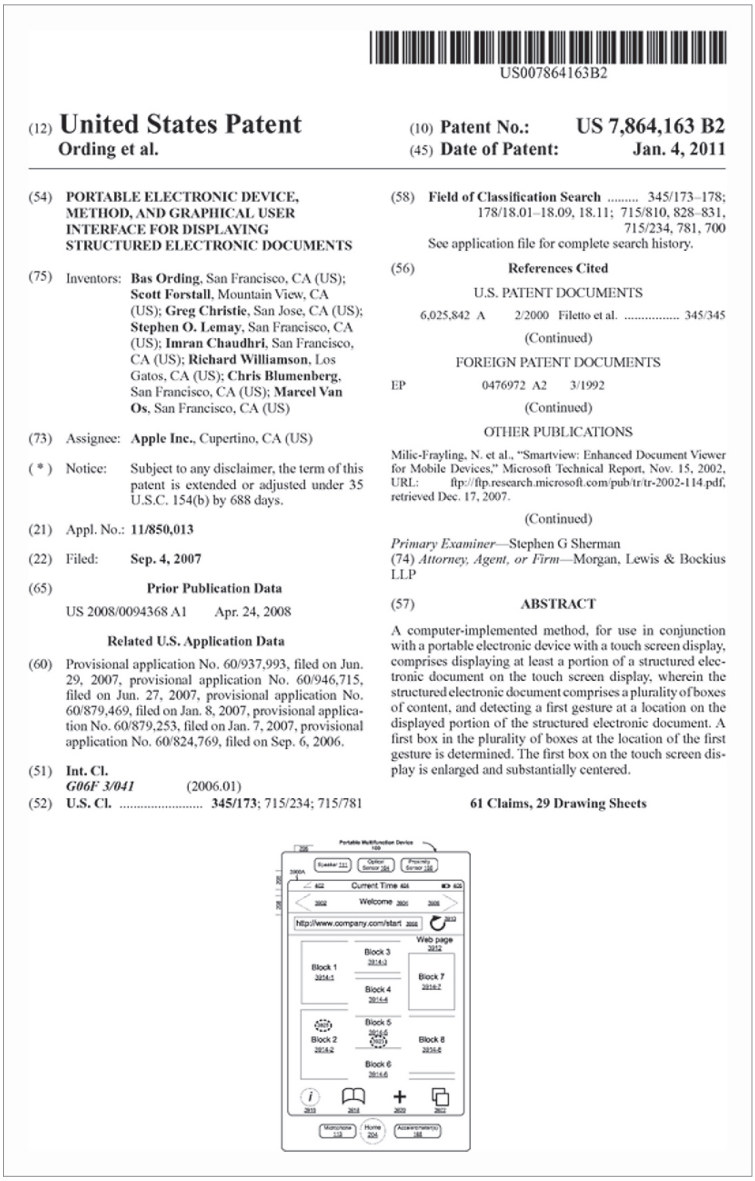
Figure 14.4 Here is an example of a schematic from Chuck Hull's 3-D printer patent provided by the US Patent and Trademark Office. (credit: modification of "US Patent US4575330A" by Charles W. Hull/Google Patents, Public Domain)

A business process patent is a type of utility patent granted to someone who develops a new business method, and just like a tangible product, the method must be new and nonobvious, and it must employ an equipment or type of technology to be valid. Nonobviousness is a legal requirement for a patent acquired under federal law (35 U.S.C. § 103), and generally means something that is not readily apparent. A proposed invention is obvious if someone of ordinary skill in a relevant field could easily make the invention based on prior art and thus would not be patentable, whereas a nonobvious invention is capable of being patented. The application must include a description of how the method works with the technology or equipment, and it must have a real-world application and not just be an idea. An example is Amazon's 1-Click shopping cart that enables people to store credit card and shipping information to enable speedy purchases.

A design patent is granted to an individual who creates something original and novel as an ornamental design.

7 Joseph Flynt. "A Detailed History of 3D Printing." *3D Insider*. n.d. https://3dinsider.com/3d-printing-history/

A design patent involves the actual design of an invention. For example, Apple has hundreds of design patents for its iPhone, and Samsung has hundreds of patents for its various products. (Figure 14.5) shows a patent granted to Apple in 2011. Read the "Abstract" portion. Does it describe something familiar? Every design element, like the LCD screen, the width and length of the phone, and many of its other features that are added to each of its generations, requires a new patent.



US007864163B2

(12) **United States Patent**
Ording et al.

(10) **Patent No.: US 7,864,163 B2**
(45) **Date of Patent: Jan. 4, 2011**

(54) **PORTABLE ELECTRONIC DEVICE, METHOD, AND GRAPHICAL USER INTERFACE FOR DISPLAYING STRUCTURED ELECTRONIC DOCUMENTS**

(75) Inventors: **Bas Ording**, San Francisco, CA (US); **Scott Forstall**, Mountain View, CA (US); **Greg Christie**, San Jose, CA (US); **Stephen O. Lemay**, San Francisco, CA (US); **Imran Chaudhri**, San Francisco, CA (US); **Richard Williamson**, Los Gatos, CA (US); **Chris Blumenberg**, San Francisco, CA (US); **Marcel Van Os**, San Francisco, CA (US)

(73) Assignee: **Apple Inc.**, Cupertino, CA (US)

(*) Notice: Subject to any disclaimer, the term of this patent is extended or adjusted under 35 U.S.C. 154(b) by 688 days.

(21) Appl. No.: **11/850,013**

(22) Filed: **Sep. 4, 2007**

(65) **Prior Publication Data**

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Related U.S. Application Data

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(51) **Int. Cl.**
G06F 3/041 (2006.01)

(52) **U.S. Cl.** **345/173**; 715/234; 715/781

(58) **Field of Classification Search** 345/173–178; 178/18.01–18.09, 18.11; 715/810, 828–831, 715/234, 781, 700
See application file for complete search history.

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Primary Examiner—Stephen G Sherman
(74) *Attorney, Agent, or Firm*—Morgan, Lewis & Bockius LLP

(57) **ABSTRACT**

A computer-implemented method, for use in conjunction with a portable electronic device with a touch screen display, comprises displaying at least a portion of a structured electronic document on the touch screen display, wherein the structured electronic document comprises a plurality of boxes of content, and detecting a first gesture at a location on the displayed portion of the structured electronic document. A first box in the plurality of boxes at the location of the first gesture is determined. The first box on the touch screen display is enlarged and substantially centered.

61 Claims, 29 Drawing Sheets

Figure 14.5 Here is an example of a US patent awarded to Apple. (credit: modification of "Sample patent to illustrate 'INID' numbers" by USPTO/Wikimedia Commons, Public Domain)

A plant patent is as it sounds—it's granted to someone who creates or discovers a new type of plant, as in the living organism, not facility. The patent applies to a plant or its contents, which must be innovative and nonobvious, and must have utility.

LINK TO LEARNING

Nolo is a legal resource for small businesses and consumers (https://openstax.org/l/52Nolo) that provides information on the basic requirements for utility, design, and plant patents.

Trademarks

A **trademark** provides the owner the ability to use a name, symbol, jingle, or character in conjunction with a specific good. A **service mark** is, according to the USPTO, a word, phrase, symbol, or graphic that identifies the origin or source of a service.[8] Both marks prevent others from using those same assets to sell their products. A trademark can be the most valuable asset a company owns. Customers will often pay more for a product or service if it comes from a specific brand with a good reputation. Customers view brands as a promise of the experience they will have: Brands promote confidence in the product and the benefits that the consumer may enjoy. Successful businesses create brand loyalty through these efforts, creating a relationship with customers. When users see themselves in the brand, they will choose that brand to create their own identities.

Protecting the name of the company and its products, jingles, logos, and even social media is therefore necessary to gain and protect a competitive advantage, because among competitors, the trademark is often the only way to distinguish among products. Can you think of a brand you are loyal to—perhaps your Apple iPhone, your Starbucks coffee, or your local entertainment spot? Consider what that company has done to earn your loyalty.

Usually, once the business begins to use its name, logo, character, and other assets, they are informally protected by trademark law and can use the ™ symbol. However, if a business wants extended protection, they should file for legal trademark protection.

Trademarks can be registered at the state or federal level. As the names imply, state trademark registration protects the business's mark within its own state, and federal trademark registration protects the business's mark across the United States. Once the registration has been filed and accepted at the federal level, the business can use the ® symbol after the protected item. Examples of trademarks include the Apple name and logo, the McDonald's logo, the talking GEICO lizard, and Nike's "Just Do It" slogan.

If you are opening your own candle and soap company, for example, you might want to register your company name and logo initially to prevent others from using it and benefiting from your reputation. If you decide to create a jingle, a slogan, a character, or another branding asset, you can do it while you develop and grow your business, as it can become cumbersome and expensive if it's done all at once. Getting a trademark itself is not as difficult as getting a patent, but just as with a patent, getting a lawyer's help can prove beneficial. Trademarks are not as costly—it may cost a few hundred dollars to file the application—but attorney fees can vary, depending on the type of project and the length of time it takes to process the application. This can range from a few hundred to thousands of dollars. This type of intellectual property can provide an opportunity for your company to be sustainable for years to come and avoid other businesses copying or using your ideas to promote themselves.

LINK TO LEARNING

Check out this video on the basics of applying for a trademark on the USPTO website (https://openstax.org/l/52tradeUSPTO) to learn more.

Copyrights

A **copyright** is provided to an author of an original work, including artistic, dramatic, architectural, musical, literary, and software works. Copyrights are granted by the Copyright Office, which is a part of the Library of Congress.[9] Table 14.1 summarizes the types of US intellectual property protection.

8 "Trademark Basics." United States Patent and Trademark Office. n.d. https://www.uspto.gov/trademarks-getting-started/trademark-basics

9 "What Does Copyright Protect?" Copyright.gov. n.d. https://www.copyright.gov/help/faq/faq-protect.html

Types of Intellectual Property Protection

Intellectual Property Protection	Protected Items	Office Providing Protection
Patent	Machine, process, improvement, plant, design, and matter composition	US Patent and Trademark Office
Trademark	Name, symbol, jingle, character, and logo	US Patent and Trademark Office
Copyright	Artistic, dramatic, architectural, musical, literary, and software	US Copyright Office

Table 14.1

The US Copyright Office's website offers a variety of publications that further explain what works are or are not eligible for copyright: https://www.copyright.gov/help/faq/faq-protect.html. While filing with the Copyright Office is not required for copyright (the rights exist when the work is created), the process provides more formal legal documentation to protect your business interests. Registration requires a fee (basic registrations are under $100), and other services or specialty requests may add additional expenses.[10]

Trade secrets are oddly similar yet completely different from traditional intellectual property (patents, copyrights, and trademarks.) Trade secrets derive their legal protection from their inherently secret nature, not from a grant of exclusivity by the government. In fact, patents and copyrights are required to be made public, whereas trade secrets are not.

Examples of trade secrets range from the formula for Coca-Cola to the Google search algorithm. An inventor has a choice: patent the invention or keep it as a trade secret. Some advantages of trade secrets include the fact that a trade secret is not limited in duration/time (patents generally only last for twenty years). A trade secret may therefore continue indefinitely as long as the secret is not revealed to the public. However, a trade secret is more difficult to enforce than a patent because the level of protection granted to trade secrets is generally considered weaker when compared with the protection granted by a patent. Additionally, a trade secret may be patented by someone else who developed the relevant information by legitimate means.

Determining Your Resource Needs and How to Attain Them

As you begin your entrepreneurial plan, start by developing a list of the basic tangible and intangible resources you will need and determine their availability. For example, let's say you are starting a solar panel manufacturing company called Helios Panels. Your new manufacturing plant will require you to have a 10,000 square foot factory, where you will need two or three specialized machines to build your solar panels. Unfortunately, the area of town that you like does not have buildings available. You will probably need to look for another location where there's a facility that fits your needs that is easily accessible for transport vehicles. If you don't make your list first, then you run the risk of ending up in a facility that is not suitable. Table 14.2 and Table 14.3 provide starting points for thinking through the tangible and intangible resources needs for your venture.

10 "What Does Copyright Protect?" Copyright.gov. n.d. https://www.copyright.gov/help/faq/faq-protect.html

Tangible Resource Needs

Resource	Considerations	My Needs
Location/ facility	• Will there be customer interaction, and if so, does the location meet the needs of the target market? • How much square space is needed? • How well will the location meet the needs of employees? • Does inventory need to be stored?	
Machinery/ equipment	• What equipment is needed to create the product or provide the service? • What quantity of equipment is needed to meet customer demand? • Are there any special requirements for machinery, such as level ground, vibration or sound protection, or water and electricity supplies?	
Technology	• What hardware is needed (computers, tablets, printers, or routers)? • What software is required? • What type of Internet service is needed? • What other technology architecture might be required (server, network, or cloud computing)?	
Vehicles	• Are vehicles needed, and if so, for what function (transporting goods or meeting clients)?	
Miscellaneous supplies	• What basic supplies may be needed (desks, chairs, wastebaskets, or whiteboards)? • What office supplies are needed for operations?	
Licenses/ permits	• Is the business licensed as a legal business entity if needed? • Does the location/facility require any licenses or permits to operate? • Do all parties involved in providing products/services have necessary licenses or certification to be in compliance with industry and government standards?	

Table 14.2 This table can help you determine your tangible resource needs.

Intangible Resource Needs

Resource	Considerations	My Needs
Patents	• Does the venture merit patent applications (utility, design, or plant)?	
Trademarks	• Do the immediate plans or long-term vision include elements that should be trademarked (name, symbol, logo, jingle, or character)?	
Copyrights	• Do the company's offerings include intellectual property such as artistic, literary, architectural, or software works that need to be protected?	

Table 14.3 This table can help you determine your intangible resource needs.

Business owners are constantly faced with difficult decisions about resources. A **decision tree** is a beneficial tool that *Business News Daily* describes as a "flowchart graph or diagram that helps explore all of the decision alternatives and their possible outcomes."[11] In other words, it uses a logical framework to help us make decisions. First, you determine what your different options are for use of resources, and then you can calculate the return for each option, using mathematical models that help estimate the probability of successful outcomes.

For example, let's say that you must decide which piece of expensive equipment to use in the manufacture of your solar panels. You can create a decision tree to determine the best course of action (Figure 14.6).

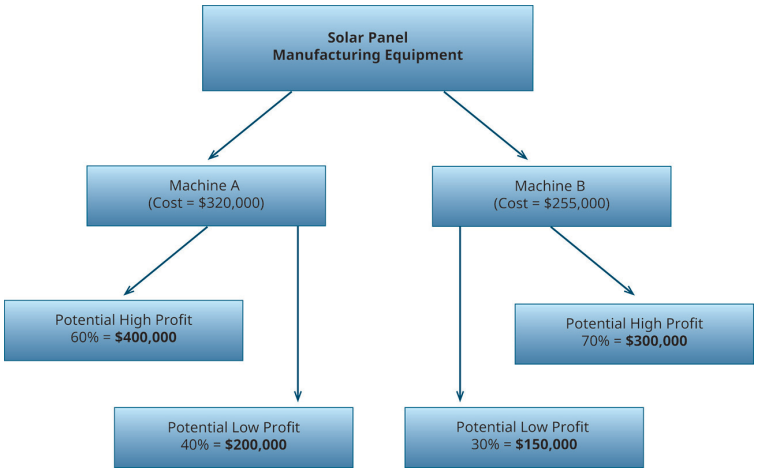


Figure 14.6 A decision tree can help estimate the probability of success when making a decision regarding how to allocate resources, sometimes including examining cost tradeoffs. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Working through these questions can help you be prepared prior to opening the business and identify additional resources you will need in the future. This takes time and effort, but the payoff is worthwhile in having a clear understanding of needs to support a path to success. Furthermore, the risk of expensive and unrecoverable mistakes can be mitigated when one uses management tools such as the decision tree tool. Creating a checklist with answers and details (Figure 14.7) can help sort through and organize your thoughts and your action steps.

11 Chad Brooks. "What Is a Decision Tree?" *Business News Daily*. March 28, 2014. https://www.businessnewsdaily.com/6147-decision-tree.html

Figure 14.7 Sample checklist for determining whether a location and other physical resources are appropriate for Helios. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

ARE YOU READY?

Get Organized

- Create a checklist of the various resources you might need for your own business idea. Categorize them into tangible and intangible.
- Prioritize them in order of importance to your growing enterprise and what cost factors to consider for each.
- Construct a decision tree that shows what choices you had to make as you made your checklist.

Often in the planning stages, entrepreneurs fail to identify all the resources they may need in the startup phase, and, as a result, the business suffers and opportunities are lost. This article from *Business News Daily* on decision trees (https://openstax.org/l/52BusNewDecTree) can be a helpful resource when completing this exercise.

Funding Resources

Funding resources are the monetary resources necessary to start and operate a business and are usually the biggest challenge that entrepreneurs face. If you don't have funding, you are not able to secure your basic resources—that is, to buy the raw materials to make a product, hire employees, purchase inventory, or secure facility space, furniture, or equipment. Entrepreneurial Finance and Accounting covers these funding sources in depth. Here, we consider how these can be best leveraged to acquire the other resources needed for your business.

Personal Savings

Most entrepreneurs start their business by tapping into their personal savings. Many entrepreneurs will work

another job while setting aside some savings money for their venture. Using personal savings can be a good idea if the business requires low startup costs (marketing material, software, equipment, products, and materials) and low maintenance costs for the first year. This can include businesses that don't require as much capital, such as professional services (engineers, accountants, and business consultants). Saving for major expenses like equipment can also help avoid paying fees and loans, but it may tie up the money in assets and will prevent you from covering payroll or other operational costs. Having cash reserves on hand can ensure that your basic business needs are met. The positive aspect of using your own savings is that you have the opportunity to use the funds as you see fit: You decide how you want to spend the money. A potential negative with this freedom is that if the business fails, your investment will be depleted as well.

Bootstrapping

Bootstrapping literally means to pull yourself up by the bootstraps with tenacity and "sweat equity" using the bare minimum resources.[12] This means that you do things as cheaply as possible until you start earning revenue that you can reinvest in the business. For example, entrepreneurs starting out might work from home to save on rent and utilities, might create a website and marketing materials themselves, and might use social media to promote the business. Once a customer base is established, the entrepreneur may explore options for outside-of-the-home office space and invest in professional services from a website designer and marketing printer.

Using credit cards can be an option to help the entrepreneur bootstrap and not take out loans. This can be risky, but if you are disciplined and only use them for the essentials of the business, such as production or marketing, they can really help get the enterprise off the ground. Paying off the balance every month and using credit cards that provide rewards and cash back can help develop healthy habits, while reaping the rewards to use on items that are highly needed.

An example of the savvy use of a credit card comes from Johnny Cupcakes, a "t-shirt bakery" in Boston, created by Johnny Earle, who started selling witty cupcake t-shirts, as shown in Figure 14.8, out of the back of his '89 Toyota Camry. He used his parent's credit card to charge the materials for his t-shirts and bootstrapped his operations out of his home with family help until his clever shirts started selling so well that he had to open his first retail store. Fortunately, Earl was smart enough to use the credit card only for production of his t-shirts, and once they sold, he used the revenue to pay off the credit card completely so as to not incur any more debt or interest charges. Eventually, his business started to flourish and he didn't need to use credit cards to operate. Today Johnny Cupcakes brings in millions of dollars. The company has expanded to locations in Los Angeles and London, and Earle speaks to entrepreneurs all over the world.[13]

12 Alejandro Cremades and Barbara Corcoran. *The Art of Startup Fundraising: Pitching Investors, Negotiating the Deal, and Everything Else Entrepreneurs Need to Know* (Hoboken, New Jersey: Wiley, 2016).
13 Johnny Cupcakes. n.d. https://johnnycupcakes.com/pages/about

Figure 14.8 Johnny Earle started his company, Johnny Cupcakes, using his mother's credit card to fund the production of the shirts. His car was his first storefront. (credit: photo provided by Johnny Cupcakes, work by Dave Green, @JOHNNYCUPCAKES, https://johnnycupcakes.com/)

Bank Loans

Bank loans are another funding option with different banks that focus on various industries and different interest rates available. Usually, these loans can be secured by some sort of equity. This can take the form of personal assets, such as the owner's home, cash, vehicles, other commercial property, or business assets like equipment, inventory, or cash. Rates can be high, especially for startups that don't have any credit history. The paperwork required can also be cumbersome, and the payments have to be made on time regardless of how much revenue the business is earning. Organizations such as the Small Business Association (SBA) and local chambers of commerce can be helpful in providing guidance and loans (see Entrepreneurial Finance and Accounting).

Bank loans are most helpful when the business does not have enough money to fund a particular part of operations, such as expanding production by means of buying new equipment. Although loans may be difficult to attain, there are local banks and large banks that provide help to small businesses and startups. Interest rates may range from 5 to 8 percent, and the loans can be used for the purchase of capital equipment or assets that are necessary for the business to take off, such as land/facilities, working capital, or marketing. Once a business has established making payments on the loan, it also establishes good credit. It may then qualify for larger loans or a **line of credit**, which is an amount of money that a bank allows a business to borrow on demand to expand a business or to have cash flow for required expenses. Usually, there is an interest rate attached to the line of credit that will have to be paid back within agreed terms, and often an annual fee for an open line of credit. Entrepreneurs with good credit ratings can access amounts around $25,000–50,000 without taking a term loan.

Friends and Family Members

Friends and family can be a great way to get quick funding because they usually believe in your skills and ideas, and they want to see you succeed. Entrepreneurs should have a specific strategy for asking friends and family for the amount they need to open a business. This can range from a few hundred to thousands of dollars. You will want to determine whether to ask many people to help you with small investments or have one or a few people provide larger amounts. It depends on the strength of your relationships and how much stress you're willing to introduce into the relationship. Many entrepreneurs have persuaded friends and family members to give small amounts, and some have persuaded a few to give large amounts of money. Regardless, it is important to have a strategy for asking and a plan for how to pay them back. You will also need to be prepared to discuss their expectations regarding the use of their money. Are they expecting to be part owners

of your company? Is this a loan that must be repaid? Is it a gift? It is always best to keep communications about funding the business professional. If they are investors, the expectation is that they will have a say in how you run your business.

Once you have figured out what interest you are willing to give up in return for the investment, make it professional by giving a presentation about the business and signing a contract to ensure that they will get paid back, whether in money or shares of stock. This safeguards the relationship by holding you accountable for paying back the money.

There are many contract templates available online, such as those at Loanback.com, Lendingkarma.com, Exilend.com, and Zimplemoney.com. These contracts should include the amount of money you're asking for, the interest rate, timeframe of payback, installment information, and any other necessary terms. If the money is a gift, it is recommended to get a statement in writing that those funds are a gift in case you need proof of where that money came from and whether payback was expected.

Angel Investors

Angel investors are usually professionals who have accumulated wealth and are open to sharing their wealth in exchange for some sort of equity. Many are former entrepreneurs who have harvested their business and enjoy providing guidance and support to new entrepreneurs. Others have worked in large corporations and have an abundance of knowledge and interest in new technologies. The name given to this type of investor began with those "angels" who helped fund Broadway shows in the last century.[14] The name stuck, and now they fund many industries, not just the arts. Many of these angels belong to groups of investors such as private equity groups, while others look for opportunities on their own. They also can range in their lending capabilities, as they are private individuals with differing amounts of wealth.

An example of an angel investor is Natalia Oberti Noguera (Figure 14.9), the CEO and founder of an organization called Pipeline Angels that helps provide capital for women and nonbinary entrepreneurs. She is not the typical angel investor, as she focuses on empowering minorities through her business coaching and providing capital opportunities for women.[15]

Figure 14.9 Natalia Oberti Noguera is founder and CEO of Pipeline Angels. Her goal is to change the face of investors and support women and nonbinary social entrepreneurs. (credit: modification of "TechCrunch Disrupt NY 2017 - Day 2" by TechCrunch/Flickr, CC BY 2.0)

14 Alejandro Cremades and Barbara Corcoran. *The Art of Startup Fundraising: Pitching Investors, Negotiating the Deal, and Everything Else Entrepreneurs Need to Know* (Hoboken, New Jersey: Wiley, 2016).
15 Natalia Oberti Noguera. n.d. www.nataliaobertinoguera.com

Venture Capitalists

Venture capitalists are usually large private or public firms that are interested in pooling funds to invest in high return, high-risk startups or growing firms. These investors want high payouts in an average span of three to five years, so they will likely fund promising businesses in technology sectors, pharmaceuticals, media and entertainment, and biotechnology.[16] The business must give up some of its equity to gain those funds. Usually, venture capitalists not only provide the funds necessary to start or grow the business, but will also provide guidance and expertise. More than likely if you are seeking funds this way, you will probably deal with an established venture capital firm, but occasionally, an individual may work alone as a venture capitalist.

For example, Birchbox received $90 million from their first rounds of funding from venture capitalists. This allowed them to fully develop their business model and grow to be valued at over $500 million. Most of the funds went to creating the technology that fueled their website, hiring customer representatives, and creating distribution systems.

Crowdfunding

Just like in the case of New Story (Introduction), there are instances where businesses rely on crowdfunding, which is a good vehicle for collecting large amounts of money made up of small donations. That's the beauty of crowdfunding: You can receive various amounts of money from many people through an online platform, with a request that can be shared not only with family and friends, but with many other people who are passionate about your idea. New Story created a new business model that allows them to crowdfund its home building projects entirely. This model, together with New Story's partnerships, has helped them create many communities in different countries, thanks to the donations from people who care about this cause. There are many types of online platforms that focus on specific industries. The most common platforms include Kickstarter.com, Indiegogo.com, CircleUp.com, and Fundable.com, among others. In 2012, Congress passed the JOBS Act to allow startups to raise money from people who were not professional investors. Crowdfunding was born from the ability to raise money without having to create an IPO.

LINK TO LEARNING

Visit the Financial Industry Regulatory Authority site explaining the details of crowdfunding and the JOBS Act (https://openstax.org/l/52FINRA) to learn more. Notice the rules for specific amounts raised.

Grants

A tougher way to get funding for your venture is by applying for grants from the government at the federal, state, and local levels.[17] Most require a match of funds by the entrepreneur and may have many more requirements, but they can be a good way to launch. You can start by looking up federal grants and work your way down to your local city level. Federal grants are broken down by industry. Usually, they focus on fields that have innovations in technology, science, or health. Some of those grants such as the Small Business Innovation Research Program or the Small Business Technology Transfer Program focus on these disciplines and can range from $150,000 to $1 million. Other governmental entities offer grants, such as the National Aeronautics and Space Administration, the National Science Foundation, and the Departments of Energy, Health, Defense, and Education; these grants focus on their fields, and their amounts and requirements vary.

16 Rachel Hallett. "These Are the Industries Attracting the Most Venture Capital." *World Economic Forum*. February 13, 2017. https://www.weforum.org/agenda/2017/02/these-are-the-industries-attracting-the-most-venture-capital/
17 Priyanka Prakash. "Small Business Grants: 107 Ways to Get Money for Your Business." *Fundera*. October 15, 2019. https://www.fundera.com/blog/small-business-grants

State grants, on the other hand, generally focus on economic, educational, or social issues. These can be smaller and easier to acquire since competition can be lower. Each state has its grants posted on the https://www.grants.gov/ website and includes requirements and funding opportunities. These focus on areas of growth and needs such as green technology, education, environmental initiatives, tax incentives, job retention, historic preservation, and tourism, among others.[18] Grants are also discussed in The Ethical and Social Responsibilities of Entrepreneurs.

Resource Funding Considerations

When evaluating resource needs, you can consider these questions:

- How will I obtain the money needed to operate the business on a daily basis?
- When might I need to hire staff, and how much would their wages and benefits cost?
- Where are these sources of money I can tap into for both immediate and long-term needs?
- Would a line of credit be a better option for my business or should I pursue a term loan?
- Is borrowing from friends and family a practical option?
- Are there angel investors who fund businesses in my industry who I can investigate?
- What will I need in terms of assets and financial reserves to open my business and keep the doors open for at least six months? One year? Five years?

Based on your needs, you will be able to choose from the type of funding that best suits you. Table 14.4 expands on the pros and cons of these different funding resources.

Pros and Cons of Funding Types

Types of funding	Pros	Cons
Personal savings	• Only risk your own funds • Use the funds as you see fit • Can take the time to save up funds • Can run a smarter business by making better decisions on a tight budget	• Risk losing all your savings/retirement accounts • Hard to save enough money to fund a business, so the amount is limited • Can cause cash flow challenges
Bootstrapping	• Requires the least amount of investment • Using credit cards can potentially provide rewards	• May not get paid until the business makes money • Requires “sweat equity” using minimal resources • May need risky use of credit cards

Table 14.4

18 Priyanka Prakash. “Small Business Grants: 107 Ways to Get Money for Your Business.” *Fundera.* October 15, 2019. https://www.fundera.com/blog/small-business-grants

Types of funding	Pros	Cons
Bank loans	• Ability to get greater amounts of funding than personal savings and bootstrapping • May be faster funding than waiting to save up • Builds credit history • Set payment rate • No loss of equity in venture	• Must qualify for loan on the business creditworthiness • Must qualify for loan based on personal creditworthiness of all spouses, partners, members, or stockholders • Must pay interest • May default loan • Cash outflow on interest and principal payments • Can jeopardize needed cash for other productive uses • Potential loss of collateral • Potential decrease in credit rating
Venture capitalists	• Potentially large sum of money • Ability to grow quickly • Not a loan, so no regular cash repayment plan • Access to useful connections and experience in the industry	• Give up ownership/equity • Have to take others' direction • Expectation of payoff • May cause company to grow too quickly • May relinquish management control or decision-making to an unknown person • Can be squeezed out of own company
Angel investors	• Useful investing networks and experience in the industry • Ability to guide you toward success • Invest funds in exchange for equity and participation in the venture's success • Not a loan	• Give up ownership • Have to take others' direction • Expectation of payoff • May relinquish management control or decision-making to an unknown person • Can be squeezed out of own company
Friends and family	• Can be easier and faster to acquire • People believe in your idea/skills • Ability to raise from many or a few • No credit check • Flexibility for payback	• Expectations need to be met • Risk losing their money • Usually will raise less funding • May complicate relationship • Might be embarrassing • Has tax implications if provided as a gift

Table 14.4

Types of funding	Pros	Cons
Crowdfunding	• Ability to raise cash from many people • Fast • Larger overall sums	• Requires significant planning/work • Requires some sort of reward • Can be stressful method • Transparency required and may need to be documented
Grants	• Range from small to large • May have little competition • May offer training • Free application	• May only focus on certain industries • Difficult to obtain • Long process • Reporting may be required • Repayment may be required if specific conditions are not met • Some conditions of the grant are outside the control of the benefactor

Table 14.4

WORK IT OUT

Informational Interviews

Do some research within your industry to see how your idea compares to those who have been in business five years or more (reaching success) and those in business five years or less (startups). Explore whether you can access needed resources to successfully launch the intended enterprise and reach the proposed customer.

If you can, interview others in the industry to get a pulse on the considerations of entry into this business. For example, you can ask them the following questions:

- What experience did you have in your industry before you started your own business?
- What made you consider opening a business?
- What were some of the positive aspects you saw about this industry? What were some negative aspects?
- What are the obstacles of entry into this industry?
- How much funding did you need to get started? How much to continue operating?
- What networks of business owners, mentors, and guides did you tap into before you started your business?
- What organizations did you join to get help with your business?
- How much time did you spend in your business each week?
- What did you give up in your personal life when you started your business?
- If you could start over, what would you do differently? Would you still open your own business?
- What advice do you have for someone who is just starting?

14.2 Using the PEST Framework to Assess Resource Needs

Learning Objectives

By the end of this section, you will be able to:

- Describe the components of the PEST framework (political, economic, sociocultural, and technological factors)
- Apply the PEST framework to assessing resource needs
- Understand how to assess typical resource costs at startup

As you venture into planning the resource allocation for your enterprise, you will learn that there are a variety of tools that can help you. It is important prior to launch to identify the minimum resources needed for startup. Some businesses will require more capital equipment (such as production machines); some require more technological resources, such as software (or software designers); some companies may require a lot of funding at the beginning of their quest, whereas some will require only a small investment of money. The level of resources needed for an enterprise changes over time, as well.

As the entrepreneur goes through the brainstorming process to identify the feasibility of the idea, they can simultaneously begin to think practically about what they will need to make this business operational: What raw materials are needed to manufacture the product? How many employees are needed at each phase? Will a physical site be necessary, and, if so, where will it reside?

Narrowing down the minimum resource needs of the enterprise in response to some or all of these questions is essential to a successful business launch. The entrepreneur can gather information and make an informed decision on what needs have to be covered at the beginning of the venture. This information can be condensed into the business plan, marketing plan, or pitch that can be shared with stakeholders. The information gleaned from the stakeholders' responses to the plans informs not only the entrepreneur and stakeholders internal to the business, but external stakeholders such as banks, investors, suppliers, vendors, and partners. The information is essential for the decision-making process. One tool that can help ensure that planning is comprehensive and well thought through is the PEST framework.

PEST Framework

The **PEST framework** is a strategic assessment tool that entrepreneurs can use to identify factors that may influence access to essential resources. PEST is an acronym for political, economic, sociocultural, and technological factors (Figure 14.10).

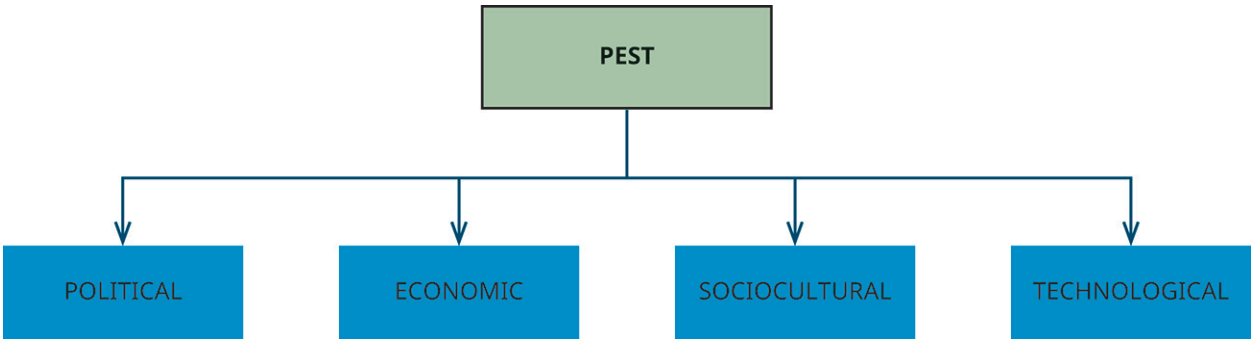


Figure 14.10 Gaining an understanding of these four factors can help entrepreneurs gauge access to important resources. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

LINK TO LEARNING

Watch the video about PEST (https://openstax.org/l/52PEST) to learn more. Why is it important to look at the outside environment? How does the PEST analysis work?

Political Factors

Although you may hope to be your own boss, make your own schedule, and follow your own rules, you must still work within the realities of outside factors that affect your business. **Political factors** stem from changes in politics, such as the policies of a new presidential administration or congressional legislation. Such policies can affect access to capital, labor laws, and environmental regulations. Moreover, these political changes can take place on federal, state, and local levels. Figure 14.11 lists several political factors that can influence a business. Tax reform law, for example, could influence the amount of taxes a business owes, while actions by the newly appointed chair of the Federal Reserve could affect how much capital may cost the small business owner because of interest rate changes.

SOME POLITICAL FACTORS INFLUENCING RESOURCES
• Tax laws • Interest rates • Protections/regulations • Labor expenses • Inflation • Insurance costs • Benefits costs • Environmental laws

Figure 14.11 Businesses must follow all laws and regulations, but political factors such as the ones listed here can influence the profitability of the organization. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Recently, the 2017 Tax Cuts and Jobs Act changed corporate tax rates, as well as the payments businesses make quarterly to the Internal Revenue Service (IRS). Other changes included the expansion of certain deductions and tax credits (including which specific business expenses can be deducted), and a new method to depreciate assets, as well as other rules related to employees who help businesses receive credits and minimize taxes.[19]

Businesses must also follow environmental laws, such as those from the Occupational Safety and Hazard Association[20] and the Environmental Protection Agency (EPA).[21] For example, these government agencies require businesses to train employees about materials that may be hazardous to people and provide notices and reports on these matters. The EPA also has regulations on air and water emissions that businesses must follow, as improper disposals can harm the environment. Smaller businesses may be exempt from some of the regulations under certain circumstances.

Imported products are regulated by the federal government through quotas and tariffs. Tariff laws have been used as political instruments to manage the flow of goods between countries. **Tariffs** are taxes or duties that are added to imported goods from another nation. **Quotas**, a limit on the number of items entering a country, are also used to restrict the volume of goods entering a country. For example, the US government in 2019 imposed tariffs on $550 billion of Chinese products, while China has imposed tariffs on $185 billion worth of US products. While it is likely that this ongoing trade dispute will be resolved, free trade remains an ongoing source of international economic competition.[22]

19 Internal Revenue Service. "The Highlights of Tax Reform for Businesses." October 2018. https://www.irs.gov/newsroom/the-highlights-of-tax-reform-for-businesses
20 Occupational Safety and Health Administration, United States Department of Labor. n.d. https://www.osha.gov/about.html
21 US Environmental Protection Agency. n.d. https://www.epa.gov/
22 Dorcas Wong and Alexander Chipman Koty. "The US-China Trade War: A Timeline." *China Briefing*. October 12, 2019. https://www.china-briefing.com/news/the-us-china-trade-war-a-timeline

For example, business owner Daniel Emerson, CEO of light manufacturer Light and Motion, described in a National Public Radio (NPR) interview that the latest round of tariffs on materials from China might push him to open a manufacturing plant overseas. Light and Motion manufactures lights for bicycles, headlamps, drones, and media production. According to Emerson, in order to get his parts from China, he has to pay the US government for importing them. He states that these tariffs might destroy his company, as his main competitors in China and other countries don't face those tariffs; therefore, his prices are forced higher. Emerson might have to move his company to the Philippines, which has no tariffs. He'll have to build them there and ship the completed lights to the United States.[23] As an entrepreneur, you should remain aware of political issues that may impact your operations and planning.

Economic Factors

Entrepreneurship has a direct impact on the economy by providing employment opportunities to many people. However, economic factors can also affect the success of a business. For example, they can deter customers from purchasing goods and services due to an economic downturn. On the other hand, when the economy is expanding and growing, people tend to feel confident about their jobs and income, and they may spend more than usual. **Economic factors**—which include inflation rates, interest, currency exchange (if the business operates or engages globally), state of the economy (growth or decline), employment rates, and disposable income—can impact the business owner's pricing of goods or services, the demand for such services, and the cost of production.

Taking the state of the economy, for example, when the economy is down, restaurants will see a decline in clientele as more people prepare meals at home to save money, or they will switch from fine dining restaurants to more casual or fast-food restaurants. In weak economies, consumers tend to purchase store (often called "private label") brands more often than national brands to reduce their grocery bill. When the economy is healthy, consumers spend more on entertainment and restaurants, which can be considered luxury items. The restaurant will need to adjust its resources to meet the economy-driven fluctuating demand. When demand is high, it is likely that the restaurant will need more supplies and more employees. These needs, in turn, result in the restaurant needing additional financial resources to buy more supplies and to pay employees. When demand is low, the opposite is true.

Sociocultural Factors

Knowing about your customers is key to delivering what they really want. Additional factors that need to be taken into consideration include changes in how society is moving and the direction of that movement as it relates to your customer base and potential new markets. These **sociocultural factors** include population growth rates, changes in where people live, social trends such as eating healthier and exercising, education levels, generational trends (millennial, baby boomer, or Gen X and Y), and religious culture. These factors can affect not only the seven Ps you learned about in the Entrepreneurial Marketing and Sales chapter, but also resource assessment more specifically. It is necessary to look at these factors closely in order to allocate marketing resources optimally. For example, if you are opening a restaurant and you see an increasing trend in healthy food, you may want to allocate your resources to fresh ingredients or more vegetarian and vegan options.

One far-reaching sociocultural factor is the impact that digital shopping has had on brick-and-mortar retailers. This online shopping trend has forced long-established companies such as JCPenney, Payless, Gap, Victoria's Secret, Radio Shack, Macy's, and Sears, to close thousands of stores, file for bankruptcy, or shut down the business altogether. These companies have faced enormous competition from entities such as Amazon and smaller businesses such as ModCloth and Birchbox that interact with customers virtually and stay on top of societal trends. Younger generations such as the Y and Z generations have triggered these social changes, as

23 National Public Radio. "U.S. Tariffs on China May Force California Company to Move Production Overseas." *All Things Considered.* September 24, 2018. https://www.npr.org/2018/09/24/651221317/u-s-tariffs-on-china-may-force-california-company-to-move-production-overseas

they are technologically savvier and expect to find exactly what they want, where they want it, and when they want it.

Technological Factors

In the case of **technological factors**, the enterprise needs to be sure it has equipment that allows it to operate efficiently. There are different types of technology that help with marketing, finances, productivity, collaboration, design, and production.

Being able to use technology to meet the needs of the customer, such as having an informational or an e-commerce website (so the customer can purchase from the comfort of home) is a "must" these days for most ventures. Digital marketing has allowed entrepreneurs to promote their businesses in many different ways, through e-mail marketing, digital ads on search engines such as Google or Bing, websites, social media groups, YouTube videos, and blogs. These tools are easy to use, available, and can be affordable, even on a shoestring budget.

WORK IT OUT

Social Media as a Resource

Leveraging social media technology is essential to building your brand and awareness in today's digital society. Create an idea sheet for a Facebook page for your Helios solar panel enterprise, which was mentioned earlier in the chapter. What are the types of information you want to include? Do you want the page to be operational or just informational? Will this social media tool be used as the main source for customers to learn about your business or will it be a supplemental tool to create deeper relationships?

Other technology can also be helpful in managing payments from customers, billing, human resources payments, and keeping the books. QuickBooks is a popular software program that a starting entrepreneur can purchase and use to manage the company's financials. Other products are available too—ZOHO Books, FRESH Books, GoDaddy Bookkeeping, and Kashoo—each has pros and cons.

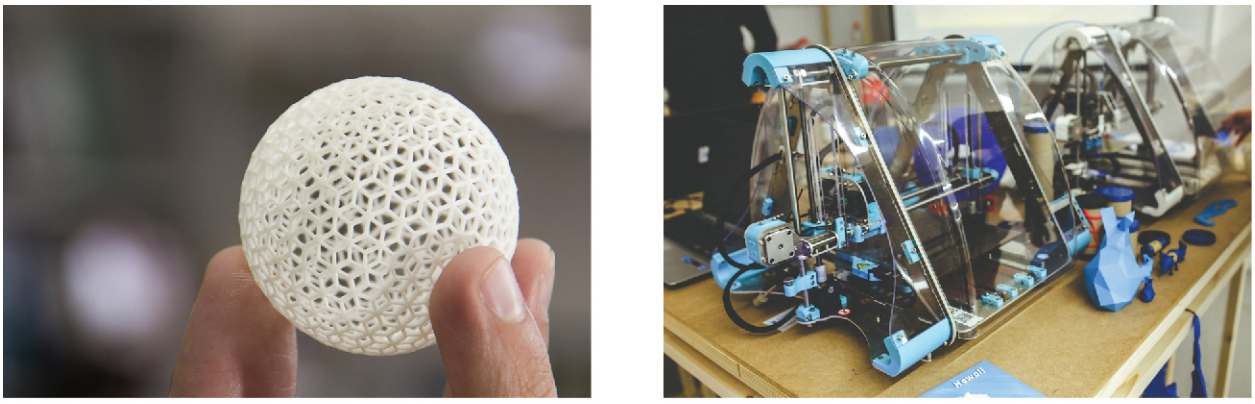
Other types of software such as UAttend help small businesses keep track of their employees' time and productivity, and Basecamp helps entrepreneurs keep track of the projects that everyone is working on, while allowing them to collaborate with each other and keep track of what is happening. These tools can make it easy for an entrepreneur to manage a project with contractors or employees.

Other technology that needs to be taken into consideration if you are manufacturing a product includes the tools and equipment that will create goods and services. Some examples are CAD (computer-aided design), 3-D printing for developing quick prototypes (Figure 14.12), CAM (computer-aided manufacture), robots, and new materials that allow faster and cheaper production of goods. 3-D printing, for example, is a manufacturing process that uses a technique of adding layers of material to create rapid prototypes. It can be used to create prototypes of products, toys, architectural models, prosthetics, tools, fashion, automotive parts, and even final products like homes, as in the case of New Story.[24] The use of prototyping allows for creativity, and these newer technologies allow users to create many prototypes. Nike, for example, uses 3-D printing to make their prototypes because it is faster than waiting for a full prototype to go through the manufacturing process. Using these technologies for prototyping can also avoid the expense of building the actual product, allow for the final product to be refined quickly, and help in the reduction of manufacturing errors.

The drawback is that some of these technologies can be expensive to purchase, and it can take a long time to recuperate the cost. (However, when wages and benefits costs rise quickly, they can pay for themselves rather quickly.) Entrepreneurs must be sure to acquire only those tools and materials that will help them get started.

24 "What Is 3D Printing?" *3DPrinting.com*. n.d. https://3dprinting.com/what-is-3d-printing/

Then, as the business thrives, more funding is available for more expensive equipment and software Entrepreneurs then need to have the skills and knowledge to operate specific software and consider upgrades and replacement costs. Questions include: What about support services? How long will support last? If the entrepreneur updates the PC, will the old software run on the new operating system? Can the data be easily copied to the new operating system or software program?



(a) (b)

Figure 14.12 3-D printing allows companies to develop prototypes quickly before investing substantial resources. (a) A 3-D sphere, for example, can be created using (b) a 3-D printer. (credit (a): modification of "ball 3d printing design" by "metalurgiamontemar0"/Pixabay, CC0; credit (b): modification of "3d printer printing technology" by "kaboompics"/Pixabay, CC0)

Assessing Resource Costs for Startup

Starting a business can be an exciting event, and one that requires thoughtful planning. Resource planning can help determine start-up costs, which helps determine an estimate of breakeven sales, profits, what types of funding to use, and how to plan for future expenses like tax payments. According to the SBA business guide,[25] there are several steps you should take to determine startup costs for different types of businesses.

First, figure out the type of business you want to open: brick and mortar, online, or services. Brick-and-mortar businesses have physical locations where a customer may purchase a product in one or several locations. Online businesses operate through e-commerce websites and sell products and services virtually. These may or may not also have a physical location. Service businesses provide services rather than a tangible product. Also, consider the type of business structure you will have (see Business Structure Options: Legal, Tax, and Risk Issues).

Next, make a cost list like the one in Table 14.5. There could be additional costs based on the resource needs identification discussion in Types of Resources. Many of the costs will be easy to determine, but others—like salaries, insurance, and improvements—might be more difficult to estimate. You can consult research sites, local business resources (such as the chamber of commerce), or speak to mentors or consultants (such as SCORE) for more guidance on how to estimate these numbers. Also see Building Networks and Foundations to see how industry professionals can help determine startup costs (Table 14.5).

25 US Small Business Administration. "Calculate Your Startup Costs." n.d. https://www.sba.gov/business-guide/plan-your-business/calculate-your-startup-costs#section-header-6

Examples of Common Costs Related to Starting a Business

Types of Costs	Examples for a Fictional Marketing Consulting Firm
Physical space for an office, building, factory	10' × 15' office space downtown building
Real estate, land	None
Furniture and fixtures	Two small desks, six chairs
Inventory	None
Equipment and supplies	Computers, color printer/copier/scanner, paper, ink, office supplies
Vehicles	Personal cars
Utilities	Electric, heat/air conditioning, water, cell/Internet
Rent/utility deposits	Rent, utility deposits
Licenses and permits	Business LLC license
Insurance for business and vehicles	Owned personally
Accountant and lawyer fees	Accountant and lawyer
Employee salaries and wages	One part-time assistant, one web developer
Advertising and promotion	One radio commercial
Market research	Customer databases
Printed marketing materials	Stationary, brochures, business cards
Digital marketing	Website, social media, e-mail marketing
Memberships	Chambers of commerce/networking groups

Table 14.5

Determine the estimated cost for each item. Once the list has been developed, finding out what each of those items costs will allow you to make an estimate of your basic needs. A good source of information is the US Bureau of Labor, which publishes a list of occupations and their wages and benefits by location and profession. Some costs may have a range to consider, and a decision tree such as the one shown in Figure 14.6 may be helpful. Many state governments have a labor and workforce department that tracks wages and employment data for specific industries and professions on an annual basis.

After you have identified all of the costs, determine which ones are one-time costs (pre-launch costs) and

which will be ongoing costs (typically monthly, quarterly, or annual). **Pre-launch costs** include everything you must have before opening the door of your business to the public. These include licenses and business permits, marketing materials, equipment, and inventory. Ongoing costs, on the other hand, are recurring. These may include rent, utilities, certain ongoing marketing costs like digital ads, and salaries. It is suggested to have at least one to two years of saved monthly expenses to make sure you give the business time to create a brand and a customer base. Add up your total pre-launch costs and your monthly costs to identify of how much capital you will need to start your business.

You should include this information in the financial section of your business plan. This data can help provide a clear picture of expenses and future revenues that banks and venture capitalists may find useful in making decisions about investing in your business.

Startup costs — Joe's Pizza Place

This worksheet is set up for a fictional business, Joe's Pizza Place. Use it to get started calculating the startup costs for your own business. Change expense categories or add new ones to fit your business. Enter one-time and monthly expenses in the appropriate columns. Your estimations should go into the Budget column, and the exact amount spent should go into the Actual column. Total funds required is the total estimated amount you need to start your company.

One-time expenses	Budget	Actual
Rent		
Security depoist	1,200.00	
First month's rent	1,200.00	
First month's utilities (including phone and Internet)	250.00	
Improvement costs		
Kitchen improvements	800.00	
Tables and furniture	1,500.00	
Utensils, dishes, and kitchen and bar equipment	350.00	
Inventory		
Food	1,250.00	
Beverage	700.00	
Alcohol	900.00	
Miscellaneous		
Licenses and permits	150.00	
Legal fees	300.00	
Signage	550.00	
Technology	300.00	
Software	400.00	
Total one-time expenses	**9,850.00**	**0.00**

Monthly expenses	Budget	Actual
Rent		
Monthly rent	1,200.00	
Property insurance	300.00	
Utilities	250.00	
Employees		
Payroll	3000.00	
Payroll taxes	1,250.00	
Health insurance	650.00	
Professional services		
Accounting	200.00	
Legal	250.00	
Consultants	200.00	
Other	50.00	
Supplies		
Office supplies	150.00	
Operating supplies	200.00	
Marketing		
Digital advertising	350.00	
Promotional materials	400.00	
Miscellaneous		
Liability insurance	400.00	
Repairs and maintenance	200.00	
Organizational dues	75.00	
Total monthly expenses	**9,125.00**	**0.00**

Source: modification of "Startup Costs Worksheet." Small Business Administration (SBA). n.d. https://www.sba.gov/sites/default/files/2017-07/Startup%20Costs%20Worksheet.pdf

Figure 14.13 This template from the Small Business Administration (SBA) is designed to help you capture the one-time and ongoing costs for your resource needs. Adding your total one-time expenses to your total monthly expenses will help you calculate your start-up costs (you should generally plan ahead for a few years of monthly expenses). (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

ARE YOU READY?

Specialty Pizzeria Costs

Imagine that you are interested in opening a pizza parlor in your town. Your idea is to provide specialty dietary choices such as vegan and gluten-free pies in addition to regular pies. You would like to open it in a new, busy shopping area where you can reach your target market.

Download the SBA's business worksheet to figure out your one-time and monthly costs for your business: https://www.sba.gov/sites/default/files/2017-07/Startup%20Costs%20Worksheet.pdf.

14.3 Managing Resources over the Venture Life Cycle

Learning Objectives

By the end of this section, you will be able to:

- Explain how resource dependence theory helps a venture grow
- Understand typical resource needs through the life cycle
- Describe the basic steps in securing human resources
- Understand the importance of educational and personal resources to the entrepreneur

The evaluation of needed resources does not end with the startup phase. This is an essential activity that the business owner must engage in throughout the life cycle of the business. Many entrepreneurs have failed to re-assess how their needs have changed as industry, technology, economic, political, or social changes emerge in the marketplace. This lack of timely assessment of operational needs can result in business struggles or even failure. Business owners need to be engaged in ongoing research, monitoring of the external environment, ensuring they have the ability to easily respond to changing circumstances.

When Birchbox, a business covered in Entrepreneurial Marketing and Sales, first entered the cosmetics sales market through an innovative business model, the founders (Katia Beauchamp is pictured in Figure 14.14), were able to fund their startup through venture capitalists who saw a great opportunity to tap into a new model of selling cosmetics. After it had been in business for a while, Birchbox grew not only in customers and employees, but also in competitors. The company struggled with cash flow as it grew its customer base and struggled to keep a healthy profit due to its tight margins from selling other brands' items. After talks of selling to QVC and Walmart, Birchbox sold its ownership to an internal investor who provided the cash for the company to continue to innovate its products and digital processes, and to add more cosmetic partners.[26]

26 Jason Del Rey. "Birchbox Has Sold Majority Ownership to One of Its Hedge Fund Investors after Sale Talks with QVC Fell Through." *Vox*. May 1, 2018. https://www.recode.net/2018/5/1/17305940/birchbox-recap-viking-global-qvc-merger-sale

Figure 14.14 Katia Beauchamp, owner of Birchbox, will stay at the helm of the company with the help of a hedge fund investor. (credit: photo provided by Birchbox)

As we can see from the Birchbox example, business operations are impacted by various internal factors such as increases in the customer base, employee growth, as well as changes in marketing needs and external factors, which include fierce competition that can curtail the venture's productivity, impact competitive advantage, or limit its access to key resources. In the case of Birchbox, cash flow was necessary for product innovations and digital marketing changes to combat their competition.

To counteract some of this, dependencies can be formed with others in a network of enterprises. This can aid in circumventing the impact of external factors such as an increase in competition in their respective market, limited ability to obtain credit for capital resources, shortages of the raw materials needed to produce their goods, or human resources to meet demanded service and production levels.

For example, many businesses within a particular industry are dependent on the same purchasers, vendors, raw materials, or other environmental resources. The **resource dependence theory (RDT) model** posits that forming networks such as mergers, vertical integrations, and joint ventures, or engaging in joint political activities, can help mitigate dependencies among member groups.[27] This classic model remains relevant today.

As Launch for Growth to Success discussed, mergers occur when two companies have the same specific goal and create a contract to become one company, with the shared goal usually of gaining new customers, growing market share, improving purchasing power, or reaching new markets.

In vertical integration, a company acquires members of its supply chain, which helps gain economies of scale, improve deliveries of inventories, reduce costs, and may also stifle competition.

A joint venture (see Business Structure Options: Legal, Tax, and Risk Issues) can be less taxing to the companies involved, as each of them retains their identities and management teams while pooling their assets to create synergy through a new project or engagement in political activities. Being able to gain control over their external environment through these alliances is essential to aid a small business toward growth and sustainability.

27 Pfeffer and Salancik. *The External Control of Organizations: A Resource Dependence Perspective* (Stanford: Stanford University Press, 1978).

In the case of Birchbox, there could be a time when a cosmetics brand and Birchbox could merge to create a new line of products, or Birchbox could acquire one of its cosmetics brands in vertical integration. However in more recent years, cooperative ("coop") arrangements have emerged to help small businesses share resources collaboratively based on a common interest and trust. For example, Community Supported Agriculture is a popular way for farmers and other commodity growers to gain selling power through their combined efforts.[28] In particular, Red Hen Bakery, a small artisanal cheese making company in Ontario, has supported its business by partnering with both local pig farmers and craft breweries to help manufacture their cheeses. They also sell vouchers to customers in advance to help manage seasonality.

In another example, farmers have turned to commercial aerial drones to help assess their crops' viability and optimize their use of fertilizers, irrigation, and other resources. Consulting firms have emerged to provide these monitoring services, despite the constraints that the Federal Aviation Administration (FAA) imposes on commercial drones. These common interests have helped them lobby the Farm Bureau and other trade associations to accelerate FAA permits for this type of commercial use.

WORK IT OUT

Auntie Anne's Pretzels and Strategic Partnership

Visit Auntie Anne's Pretzels (https://openstax.org/l/52AuntieAnne) to learn more about their story.

- Write a summary on how Anne Beiler leveraged relationships in the initial launch of her business.
- What strategies did Beiler use to identify strategic partners, resources and processes to protect her profitability?

Resources Needed Based on Life Cycle

Entrepreneurs need to identify and plan for their resource needs (Table 14.6) and costs for all stages of the venture's life cycle, which is shown in Figure 14.15. Evaluating the cost of the enterprise at each phase for both a good and a service helps the entrepreneur assess its feasibility (see the discussion on funding at various life cycle stages in Entrepreneurial Finance and Accounting).

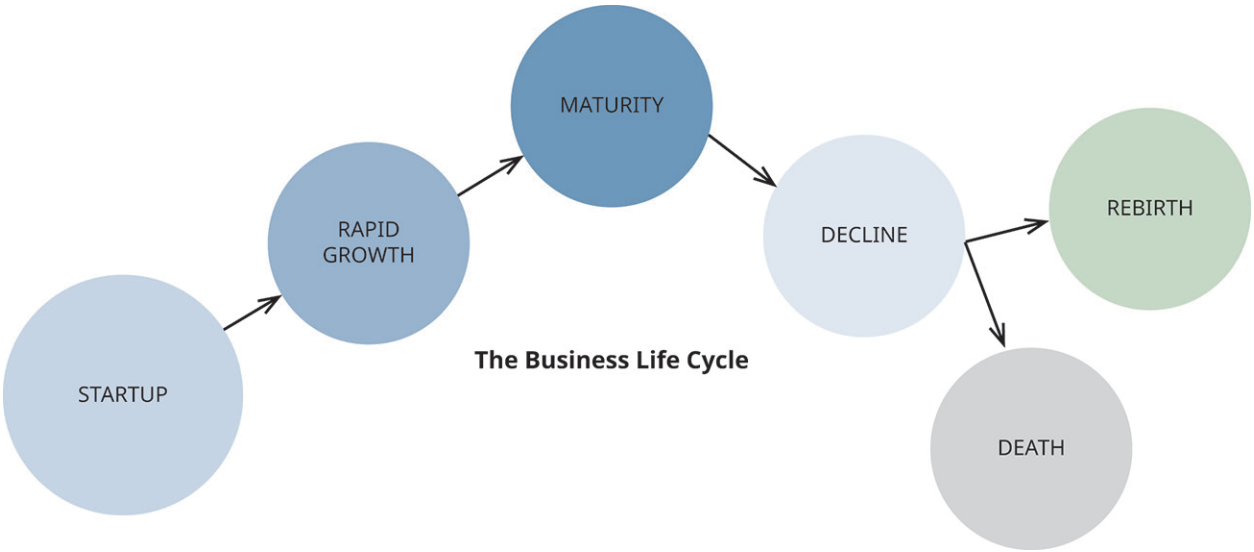


Figure 14.15 Entrepreneurs and business owners should plan for resource needs and their associated funding across all phases of the business life cycle. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

28 "The Growth of Community Supported Agriculture. *Morning AgClips.* February 7, 2018. https://www.morningagclips.com/the-growth-of-community-supported-agriculture/

Startup Phase

The startup phase is an exciting and exploratory time for the entrepreneur. In this phase, ventures are defining their identity, growing their customer base, learning more about their target market and how best to serve it, how to develop the products that will meet demand, and how to hire the people that will make it all happen. At this time, resources are often scarce, and the entrepreneur may be bootstrapping to keep costs low. This means that the entrepreneur might be working from home to save on rent and utilities, and may have only a part-time employee or none at all. The product may be created on a single piece of equipment that can produce on only a small scale. When a product is first developed, there are also costs to consider. These include costs of raw materials, production, packaging, and personnel for the production, or what is commonly known as *cost of goods sold*. Recall that the cost of goods sold is the accumulated costs of creating a product (materials, direct labor) or a service (direct labor). At introduction, there is packaging, marketing, promotions, and shipping, and, if inventory is maintained, warehousing.

Any sales revenue is immediately re-invested into the business with the aim of developing a cycle of growth. The entrepreneur at this point may forgo a salary while the business takes off and may also wear many hats to keep the ball rolling instead of hiring employees.

Advisory boards are crucial during this phase, as they bring current information to the table to inform entrepreneurs of trends, changes, or regulatory adjustments within the industry that could affect their enterprise. An **advisory board** is a group of knowledgeable people who aid an organization to make strategic decisions about the business and its issues without having the power to vote or make any legal decisions. Having access to key contacts, networks of professionals, and public resources are key to having a current toolkit from which to draw information to inform decision-making and resource management.

In the case of Christina's Confections, she started baking goods at home with her own oven. She did quite a bit of bootstrapping and used her savings to buy ingredients, utensils, packaging materials (boxes and containers), marketing materials (flyers, brochures, business cards), and a basic website, and to pay a part-time employee. For two years, Christina didn't collect a salary so she could save money for the next phase, which is growth.

Growth Phase

During the growth phase, the business has been around for a few years, its identity has been developed, its customer base has grown, sales are accelerating, and there is a need for more resources to sustain this growth. Resource needs can take the form of cash to invest in new equipment, new materials, more marketing, or new personnel. Additional equipment may be needed to help with a higher output, or perhaps the current location is too small to produce at a larger scale. The location might not be big enough for customers, or to welcome guests, so a new building may be required. More material might also be needed to create more products due to higher demand, and more people may need to be hired for production. There may be a need for management and administration to expand as the organization grows, too. Departments may now evolve and require processes to coordinate efforts between functions such as production, human resources, and marketing.

LINK TO LEARNING

Take a look at this checklist for growing a small business (https://openstax.org/l/52SmallBusCheck) from Visa and SCORE. Review the seven steps that address key issues that can affect business growth.

During the growth phase, the entrepreneur might need to change marketing strategy, advertising, production, or even packaging to keep up with demand.

Let us revisit Christina's Confections bakery. Two years into operations, she needs to identify a larger location

for her bakery. She now has ten employees and has several corporate accounts she services for special events. She recently partnered with a neighborhood catering company and has been retained to provide the baked goods for their catered events. These changes mean that Christina will need to obtain funding for the expansion, locate a space near her existing location, or expand on the location she is currently leasing. Part of her consideration at this point is determining if it is feasible for her to purchase a location, which would allow her to gain all the benefits of facility ownership as she often works long hours and needs flexibility for access. The ideal location would be one in which she could reside above the storefront so she can incorporate living expenses into her monthly expenses.

Maturity Phase

In maturity, when the product has perhaps saturated the market and there may be lower-cost alternatives, the entrepreneur has to deal with competition as sales level off and more companies are fighting for customers' dollars. At this point, spending resources in branding becomes very important, as customers have many choices available to them and having a reputable image and uniqueness as well as a brand that inspires brand loyalty helps businesses attract them.

As needs change with this growth, the entrepreneur must reconsider the resources, operationalize how these are used, and determine what efficiencies may be gained by retaining certain resources and outsourcing others. **Outsourcing** is the activity of hiring an outside company or third party to perform a specific task, job, or process, or to manufacture goods. This is common in human resources, where many companies outsource their workforce to reduce costs and focus on retaining tasks they excel at.

For example, if you are a digital marketing company and have several web design projects you are working on, outsourcing can help you pass some of the most challenging tasks in the design or coding process to another company, while your venture focuses on the steps in the process that are your company's strengths. Similarly, another company could seek to use your company's resources if they believe your company has a greater proficiency for specific tasks.

Decline/Rebirth Phase

During the decline phase of a business, if there is to be rebirth, resources must account for making changes to the product so it can have its renaissance. In Christina's case, if the traditional bakery industry were to decline, she could decide to use different ingredients and equipment to make a new kind of cake that uses only fruit and vegetables, or something completely different that would ensure the business would still be unique enough to come back to the life cycle. Most companies that have lasted many years in business have gone through this cycle several times and have been able to reinvent themselves. Small bakeries, clothing chains, and car manufacturers have been able to "come back" within industries that are easy to fail in due to their decline. Also, many tech companies such as Apple, Nintendo, and Polaroid were once in the decline phase, but their ability to shift allowed them to have a rebirth.

Summary of Resources for Each Phase of Business

Business Phase	Resources Needed
Startup	Initial capital, basic equipment, inventory, few employees, facility (home or location), cost of goods sold, marketing materials, mentorship
Growth	More capital, additional employees/departments, marketing, additional equipment, inventory

Table 14.6

Business Phase	Resources Needed
Maturity	Branding, outsourcing
Decline/ Rebirth	New equipment/technology, new products, new patents, equity funding for possible merger

Table 14.6

Human Resources

As you begin your entrepreneurial journey, you will realize that you cannot do everything on your own. You will need people to help. In the beginning, you may need office assistance or production assistance, and, initially, they could be part-time hires. As you grow, though, you will realize that you need to have a more sophisticated understanding of how to build a skilled workforce. **Human resources** are the people needed to support the current and future growth of the venture, and help the company increase production and the provision of services, as well as help with the administrative tasks required to operate the business. Employees add value to the enterprise in that they help the business generate revenue. Having the proper staff is a constant process that must have procedures in place and starts with having a plan set out to recruit and hire the people with the skills that match your venture's needs. In addition to hiring, a small business owner can consider getting human resource help through partner firms, outsourcing, and even outside consultants who are not actual employees of the company but provide support or specialized services for the company. Building Networks and Foundations discusses building a team. Here, we focus on the essentials of the human resourcing process.

First, figuring out why you need the help is an important step in assessing the needs of the company. Usually, entrepreneurs will need some sort of part-time help managing an office, manufacturing a product, or producing a service. The need and the outcome must be greater than the cost of hiring someone. This assessment ensures that current revenue can cover the addition of another person's compensation. For example, you may need to hire a part-time assistant who would cost $15,000 to $30,000 a year. If having that part-time assistant frees you up to sell $50,000 of product, then it is financially worth hiring that person. In addition, if you hire a salesperson at $40,000 to $50,000 per year, including benefits, and they sell $100,000 a year for you, then it is worth hiring that person because they are generating profit. Keep in mind that many entrepreneurs start with virtual assistants, bookkeepers, designers, web developers, or managers who can vary in price and only work when you need them. Using sites such as UpWork to hire freelancers to cover a portion of your business allows you access to dozens to hundreds of choices to find a resource that works for you, often at lower costs than hiring someone on staff.

Once you establish that hiring new employees is a need and a smart financial choice, you need to create a job description to attract the right candidates. This contains a statement of the employee's tasks and responsibilities, the processes used, and the desired outcomes. It will also include the parameters of how the job will be done, the environment, the hours, and the skills and experience necessary to perform well.

In preparation for determining your hiring needs and creating job descriptions, the following steps will guide you on topics and decisions to consider. After determining your resource needs, the remainder of the steps can occur in varying order depending on your specific situation.

Step 1: Determine Resourcing Needs

Understanding the needs of your business in terms of job functions is the first step to hiring. Defining the work that needs to be done based on your business strategies can help guide your business needs. If you are

a business consultant and need help managing the office, you can make a list of all the needs of the upkeep of the office. This can include answering phones, setting appointments, attending customers, making copies, paying bills, and ordering materials.

You will also need to determine whether you need full-time or part-time people, and what the budget is to clarify the direction of your hiring. Making a list of the tasks or goals for the business and estimating the time that it will take to finish them can help decide to hire a part-time or full-time person.

Keep in mind that needs may change, so even if you made a plan, the execution may vary, and you may need to make changes. By determining your costs and the benefits of those costs, you can figure out how many people you can bring on to accomplish the goals set in your business plan or marketing plan. If your plan calls for having sales of $100,000 the first year, you might want to hire one part-time employee at $25,000 who can help you achieve that goal. If your goal is to have sales over $1 million, then you likely might need more employees.

Figuring out what skills and experience your team should have is a good starting point for developing the job description, and setting the salaries and benefits you will offer. Once you set your descriptions and post them, whether online, at a job fair, or in a newspaper, you will see the applications coming in. If your industry calls for more sophisticated experience and skills, you may also want to hire a staffing agency to help you with the hiring.

Step 2: Hire a Team

Hiring a team of employees can be a daunting task, but if you first focus on understanding the needs of your business and the amount of time required to perform those tasks, this step will be a lot easier (Figure 14.16). It involves setting up the job description, deciding on a salary and benefits to pay, posting it on various job websites such as Indeed.com, careerbuilder.com, or monster.com, and any industry job portal that may be important to reach qualified people. Oftentimes professional networking—such as online sites like LinkedIn or local groups like your chamber of commerce—may result in additional leads. The alumni center at your local university or community college may also be a place to connect with qualified candidates. Technology schools or trade schools are excellent sources to find skilled workers looking for that first full-time job after earning certification or licensing.

Figure 14.16 Hiring the right employees for your business will ensure that they will help you start and grow the company. (credit: "job interview hiring hand shake" by "Tumisu"/Pixabay, CC0)

Once posted, you must decide how long to advertise the position. Also consider that the interview process can take a few days, weeks, or months, depending on how many people you are hiring and the quality of your prospects. If you are satisfied with the process, then you select the employee(s) and inform them of your selection. But before you extend an offer, you might want to conduct a background check first and then offer

and welcome them into your team. Conducting background checks, including criminal checks, should be a routine procedure in the hiring process. A formal job offer should never be made until the results of the background checks have been received and reviewed. If a potential candidate accepts a job offer and you are then required to withdraw that offer because results of a background check disqualify the candidate, many problems will be unnecessarily created.

LINK TO LEARNING

Before conducting any interviews, you should be aware of which questions are legal and which are not legal (https://openstax.org/l/52LeglInterview) to ask in an interview. Minnesota State Colleges and Universities website offers a repository of appropriate questions.

Step 3: Create an Employee Handbook

If you're starting your business from scratch with no sales, it is likely that you will only need one or two part-time people to help you with your business. An employee handbook at this time may not be necessary; however, once you have ten or more employees, and your business begins growing, you will want to create company employment policies and rules for all employees to follow. You could also create this handbook at the inception of your business. This handbook is a road map that may include rules about how to act as representatives of the business, attire expectations, hours required to work, proper etiquette, legal and regulatory compliance for full- or part-time employees, and sanctions for when these rules are not followed. Most companies today also need to create policies around social media use and statements made online via social media. Listing any benefits such as earned vacation, paid time off for jury duty, holiday pay, personal time off, and price discounts for employees and family members should also be included. Sometimes in filings for unemployment, the state workforce commission will require a copy of the employee handbook to help determine what the former employee is entitled to receive. Having written policies in a handbook and following them can save a lot of time and protect against conflicts with employees.

LINK TO LEARNING

Some companies have begun to create funny and memorable handbooks (https://openstax.org/l/52Handbook) to entice employees to read them and understand them.

Step 4: Secure Independent Contractors, if Necessary

As covered in Building Networks and Foundations, sometimes looking outside of your business to get help can be a good idea while building or growing your venture. **Independent contractors** are people who provide work without being part of the payroll for the contracting business. They may perform work similar to employees, but they are not employees of the company; therefore, the business does not have to pay for benefits or withhold taxes. However, these workers set their own time for work, can come and go as they need to, use their own equipment to complete assigned tasks, and can perform the work in their own way, as a service provided. You may want to consult with an accounting expert in tax issues before beginning work with independent contractors.

LINK TO LEARNING

Take a look at this checklist to determine whether a human resource should be considered an employee or an independent contractor (https://openstax.org/l/52ContractCheck) from the IRS. The distinction carries

important legal implications, and the burden is on the employer to make the correct classification. Failure to classify workers correctly can be an expensive mistake.

Step 5: Establish Benefits

When designing a position and hiring people, another important consideration is the benefit plan you will offer. Common benefits include contributing to or providing health insurance costs, paid vacation time and sick days, providing access to 401K retirement accounts and contributing to them on the employee's behalf, and insurance—including life, long- and short-term disability, and accident insurance. In addition, you might want to offer stock options to provide employees with a piece of your business and entice them to work for a company that they own. Each of these benefits is subject to state or federal regulations, or both. Seeking advice from professionals on these issues would be a valuable use of the entrepreneur's time and money. Getting these employee benefits wrong can doom a company quickly.

LINK TO LEARNING

Visit the Society for Human Resource Management site for examples of benefits and how to implement them (https://openstax.org/l/52Benefits) to learn more.

Once employees are on board, there is an ongoing process of training, promoting, and managing them, as well as developing relationships that will be key to the success of the enterprise. In the evaluation of human resources, you may need to consider these questions:

- Are the skill levels that I need available in the region where I plan to operate?
- What is the prevailing wage for the human resources I need?
- How much can I afford to pay employees at this phase in my business?
- Are independent contractors the best option or are employees a better fit?
- Will I need to provide ongoing formal training or maintain certifications or licensures for my staff or are employees responsible for these items themselves?
- How can I be competitive with other business to attract the talent I need?
- Will I need to provide benefits such as vacation, retirement plans, health insurance, or life insurance?

Educational, Support, and Mentorship Resources

Entrepreneurs need to be mindful not only of the resources needed to operate the business, but also of the resources needed to support them in their challenging role of being an entrepreneur. Ongoing education and mentorship are key supports. When entrepreneurs are asked what topics they need learn more about when starting and growing a business, often they request more educational support in management, leadership, communication, financial, and marketing education. Many owners are experts at their craft but don't know how to manage the business itself and must take courses or earn certificates to gain that "how to run a business" knowledge. Local chambers of commerce and other organizations provide training sessions, workshops, and educational programs in marketing, communication, management, and leadership. Other needs include finance, accounting, and software use. The SBA has a learning center where business owners can learn about many topics from how to write a business plan to the legal requirements and financing options that apply to their venture.[29] One important topic they address is digital marketing, a training most entrepreneurs need in this day and age. The Small Business Development Center and SCORE are organizations that also provide myriad workshops at no cost or for a very small fee.

Although some entrepreneurs do have business degrees and a few have advanced degrees, they still need to

29 US Small Business Administration. "Learning Center." n.d. https://www.sba.gov/learning-center

keep abreast of trends and changes in their industry. They have to continually educate themselves through various forms of research, by attending conferences, and through programs available through the chambers and other organizational networks. Maintaining a subscription to a major industry newspaper or trade magazine can be extremely beneficial. Another common trend is for starting entrepreneurs to work in the industry of their business to acquire the skills and knowledge necessary before they embark on their journey. For example, if you want to open a digital marketing business, you might first gain some experience by working for a digital marketing company prior to opening the business. However, you should make certain you abide by any noncompete or similar clauses in your employment contracts.

As we have seen throughout the text, being an entrepreneur is no easy task. It requires many hours to start and grow a business, not to mention the daily stressors from challenges that arise from interactions with employees, customers, and suppliers. High-performing entrepreneurs must have a good support system to help them overcome the ups and downs that owning a business might bring.

Having friends and family members who are supportive of the venture is important because these are people the owner trusts with personal and work issues on a daily basis. Their support is key to the success of the entrepreneur as they listen and understand the frustrations of being in business and may also help with the business itself. By the same token, the entrepreneur needs to spend time with friends and family to bring work-life balance to their lives.

Having mentors who have gone through similar issues and can listen and advise is a great advantage to entrepreneurs. Mentors act as counselors to the business and are genuinely interested and happy to help the business owner. Most mentors have been through similar challenges and have great knowledge and passion about the industry in which they work. SCORE can be a strong network for finding a mentor. This program is a partner of the SBA and provides free education and mentors to business owners. The mentors are volunteers who have many years of experience and now want to help other businesses for free. You can go to their website (https://www.score.org/) and type in your zip code or industry to find a mentor near you. Doreen Graves is an example of a marketing mentor in northeast Mississippi who feels that she is not only a mentor to her mentees, but a support system and confidante, as they share with her their most personal stories of struggle, family values, and business dreams. She feels fortunate to have the power to help them.[30]

WHAT CAN YOU DO?

Take a SCORE Course

Go to SCORE (Senior Core of Retired Executives) and take a look at Become a SCORE Volunteer (https://www.score.org/volunteer). It outlines four ways to donate your time:

- Mentor: Offer confidential business mentoring services, either in person or online
- Subject matter expert: Provide focused knowledge based on your professional skills or industry
- Workshop presenter: Lead local workshops, seminars and events to help entrepreneurs meet their goals and achieve success
- Chapter support role: Share your skills in marketing, tech, finance, fundraising and more to help expand the outreach of SCORE

Which of these roles do you see yourself fitting into some day and why?

30 Service Corps of Retired Executives (SCORE). https://www.score.org

Key Terms

advisory board group of advisors that helps an organization make strategic decisions about the business, and brings certain knowledge and experience that can bring a new perspective on issues without having the actual authority to vote or govern

copyright grants the creator of a work the exclusive right to reproduce the work, typically for a specified period of time

decision tree flowchart diagram used to explore the outcomes of different decisions

economic factors inflation, interest, employment, and currency exchange, rates, (among many other factors) that impact the business owner's pricing of goods or services, the demand for such services, and the cost of production

funding sources monetary resources used by the entrepreneur in the operation of the initial startup and early business

human resources people hired by the entrepreneur to perform various duties in the business, provide customer service, or produce the goods

independent contractors (also, freelancer) people or businesses that provide work similar to an employee without being part of the payroll for the contracting business, and who pay their own taxes and pay for their own benefits

intangible resources assets that cannot be seen, touched, or felt, such as intellectual property, patents, designs, and processes

line of credit lending of funds in exchange for a promise to repay

outsourcing hiring an outside company or third party to perform a specific task, job, or process, or to manufacture goods

PEST framework that can be used to distinguish political, economic, sociocultural, and technological factors influencing access to needed resources

political factors stem from changes in politics, such as the policies of a new presidential administration or congressional legislation, as well as of state and local offices

pre-launch costs cost of all the resources needed to open the business to the public

quota specific number of units allowed into a country; sometimes quotas are limited to one source, such as one country, and sometimes the limit is placed on aggregate quantity regardless of source(s)

resource dependence theory (RDT) model creating networks with business partners through mergers, vertical integration, joint ventures, or engaging in joint political activities to slow dependency among member groups

service mark word, phrase, symbol, or graphic that identifies the origin or source of a service

sociocultural factors changes in how society is moving and the direction of that movement as it relates to a customer base and potential new markets

tangible resources assets that have a physical form as they can be seen, touched, and felt

tariffs taxes or duties that are added to imported goods from another nation

technological factors technological equipment and tools the enterprise needs to be sure it operates efficiently

trademark registration that provides the owner the ability to use a name, symbol, jingle, or character in conjunction with a specific product or service, and prevents others from using those same symbols to sell their products

Summary

14.1 Types of Resources

Determining which resources a venture needs is essential to its success. Assets are types of property that benefit the person or company in possession of them. They can be tangible or intangible. Tangible resources can be seen, touched, and felt. They may include raw materials, land, facilities, buildings, machinery,

computers, supplies, furniture, information technology, and vehicles.

Intangible resources cannot be seen, touched, or felt. They include intellectual property such as designs, formulas, art, written work, brands, and inventions that can be protected by patents, trademarks, and copyrights.

Entrepreneurs oftentimes have novel ideas about how to provide a service or how to create a better product. These ideas are important to safeguard so other competitors don't copy those same characteristics of a product, process, machine, piece of writing, or any other of the works cited earlier. A way to protect them is to ensure that you have a patent, trademark, or copyright so others cannot benefit from your work. It is always beneficial to do a check before applying for one of the protections and make sure that the invention hasn't been created before. Searching the USPTO website and hiring an attorney will ensure you are the first one to register your idea and help you through the lengthy and often expensive process of protecting a new idea.

Funding sources are essential to starting and scaling a business. These include an entrepreneur's own savings, bank loans, venture capitalists, angel investors, crowdfunding, and friends and family. It is important to consider the pros and cons of your financing options in relation to your resource needs in order to plan for short- and long-term needs.

14.2 Using the PEST Framework to Assess Resource Needs

Business owners need to know what resources they need before launching. The PEST framework can help you become aware of outside forces that affect the procurement of resources you need to succeed. PEST looks at the political, economic, sociocultural, and technological factors that affect resource costs and availability. Different businesses require different resources, so going through a checklist of basic needs, finding the associated costs, splitting them into one-time costs and ongoing costs, and adding them up will ensure the entrepreneur is aware and ready to document for an investor or bank the resources needed.

14.3 Managing Resources over the Venture Life Cycle

The life cycle of the business requires resource allocation and planning at each stage. These stages include the startup phase, growth phase, maturity phase, and decline/rebirth phase. There are instances where a business has failed because the owner failed to re-assess shifting resource needs caused by changes in the marketplace and the overall environment. Research is an ongoing process, and keeping an eye on the external environment allows a business to be able to shift on time.

Resource dependence theory (RDT) is a model that explores creating networks with other companies through mergers, vertical integration, and joint ventures. RDT can help counteract the effects of competing with each other by optimizing collaboration.

Human resources include the labor that produces a product or service, and provides administrative support and customer service. Having good employees adds value to the enterprise because they help generate sales and profit. Education in marketing, management, and leadership are important topics to engage in as a business owner as well as having personal support from mentors.

Review Questions

1. What types of tangible, intangible, and funding resources exist? Give examples of each.
2. What is an example of a tangible resource and an intangible resource?
3. What is the PEST tool? How can entrepreneurs use it to their advantage before launching a business?
4. Why is it important to figure out costs before launching a business?
5. What are examples of costs that must be taken into consideration before opening a business?
6. What is the difference between one-time costs and monthly costs? How much should an entrepreneur

have of monthly costs in advance?

7. Define the resource dependence theory.
8. What is the life cycle of a business and how do resource needs and their associate costs shift over time?

Discussion Questions

1. Discuss how a small business can be bootstrapped at its inception. What kind of costs can the entrepreneur avoid or lower with tenacity and sweat equity?
2. If you were to start a small business, what would it be and what kind of resources would you need to get started?
3. Which do you think are more difficult to protect: tangible or intangible resources and why?
4. Discuss how political factors can impact a business.
5. What are some examples of sociocultural factors that may affect a business?
6. Explain how economic factors can increase the price of a product.
7. When is it a good time to hire an independent contractor and when is it a good time to hire an on-staff employee?
8. Explain how resource dependence theory helps a venture grow.
9. Discuss the steps required in hiring new employees. What sorts of factors must you think of before you hire a new team?
10. Discuss the importance of having personal resources, such as a strong support system, when starting a venture.

Case Questions

1. Christina has always wanted to open a small neighborhood bakery, Christina's Confections. She is currently working out of her home, earning income making cakes and baked goods for weddings, parties, and other special occasions. She would like to find a location for her bakery, as she believes there is a market, and she would like to expand her business to a retail operation. She has some money saved and her credit is good, but she is concerned that obtaining a loan will be challenging. Sales have been consistently increasing, and she now has one part-time employee, but she thinks that with a retail location she will need to hire an additional two people on a part-time basis. If she does hire staff, she will need to consider the cost of labor, how many hours she would need each of these staff, and the tasks she would need them to perform at this stage in her business operation. As a result, she will need to consider their wages as a cost of labor on top of all the other supplies, insurance, rent, advertising, point-of-sale equipment, and various other costs she did not have when she was operating out of her home. She needs to figure out how she will make money and how she will finance or pay for her new start-up costs in the retail location.
   Christina needs to evaluate all the resources she would need for this enterprise and create a checklist so that she can determine if the time is right for her to take this important step with her bakery. As she progresses through the process, the questions get more specific and the answers become much more detailed.
   Review Christina's resource needs and make a list of them.
2. Going back to this case question on Christina's Confections, go over the list of resources that you created. Now that you have additional information, determine if that is a good list; if not, add or delete items that are necessary for her to run her business. What additional resources did you come up with? What can she

do to ensure she can cover all her expenses?

3. Consider Christina's Confectionaries bakery example and focus on the maturity phase of her business. Describe how Christina can develop her brand to distinguish her from other bakeries and what kind of costs she can expect to incur while doing this.

Suggested Resources

14.1 Types of Resources

The Business Journals company profiles: https://www.bizjournals.com/profiles/company

Circleup: http://circleup.com

Exilend: https://www.exilend.com

Fundable: http://fundable.com

Indiegogo: http://indiegogo.com

Kickstarter: http://kickstarter.com

LendingKarma: http://www.lendingkarma.com

LoanBack: http://loanback.com

NewsLink: http://www.newslink.org

Society of Human Resources Management: http://shrm.org

US Small Business Administration: https://www.sba.gov/

US Securities and Exchange Commission Regulatory Actions: https://www.sec.gov/rules.shtml

Trade Show News Network: http://www.tsnn.com

US Census Bureau: http://www.census.gov

Copyright Office: https://www.copyright.gov/

US Chamber of Commerce: https://www.uschamber.com/

US Patent and Trademark Office: https://www.uspto.gov/

ZimpleMoney: http://www.zimplemoney.com

SEC Information on crowdfunding portals: https://www.sec.gov/divisions/marketreg/tmcompliance/fpregistrationguide.htm

Link to SEC (FINRA) crowdfunding portals: https://www.finra.org/about/funding-portals-we-regulate

New York University, Stern School of Business: https://www.stern.nyu.edu/

Link to data on margins by sector: http://pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/margin.html

Loopnet: https://www.loopnet.com/

Bizstats: https://www.bizstats.com/

14.2 Using the PEST Framework to Assess Resource Needs

SBA calculation of startup costs: https://www.sba.gov/business-guide/plan-your-business/calculate-your-startup-costs#section-header-6

US Department of Labor: https://www.dol.gov/general/topic/statistics/wagesearnings

https://www.businessnewsdaily.com/5-small-business-start-up-costs-options.html

14.3 Managing Resources over the Venture Life Cycle

Referrals and Associations

Tradeshows: http://www.tsnn.com/

Industry research publications: http://www.newslink.org

National Association of Women Business Owners: https://www.nawbo.org/

University and Organizational Resources

Small Business Development Centers: https://www.sba.gov/offices/headquarters/osbdc/about-us

New York University, Stern School of Business: https://www.stern.nyu.edu/

Governmental and Other Agencies:

https:///www.bls.gov

https://www.census.gov/

https://www.sba.gov/

https://www.ready.gov/business/implementation/resource

https://www.usa.gov/laws-and-regulations

https://www.sba.gov/video-series/2_minute_video_series#363481

15

Next Steps

Figure 15.1 Consider the importance of having a source of light when the sky is dark, or when disaster strikes and electricity is lost, or for some people, when the infrastructure for electricity doesn't exist. Andrea Sreshta and Ana Stork identified this situation as an opportunity to create a new product that provides light when the infrastructure does not. (credit: modification of work by LuminAID)

Chapter Outline

15.1 Launching Your Venture
15.2 Making Difficult Business Decisions in Response to Challenges
15.3 Seeking Help or Support
15.4 Now What? Serving as a Mentor, Consultant, or Champion
15.5 Reflections: Documenting the Journey

Introduction

"How can you know what you're capable of if you don't embrace the unknown?"—Esmeralda Santiago

In 2010, two graduate students participated in a project to assist post-earthquake relief efforts for Haitians. These two students focused on the need for light. For most people, we turn on a light switch and seldom ever consider how important light is to our safety and extending our sight beyond dependence on the sun for daylight. Andrea Sreshta and Ana Stork analyzed the problems people have after a disaster and noticed that no one addressed the challenges of lack of light. Recognizing the opportunity to solve this problem, these two social entrepreneurs created a reusable solar powered light source, LuminAID.

Now that you have learned how to create a business plan and understand more about entrepreneurship, we turn to the challenges that many entrepreneurs face as they start their venture, with advice to help you overcome them and consider your next steps beyond the current venture's successes.

In this chapter, we consider some of the challenges faced by entrepreneurs along the journey, identify reasons why these occur, and discuss what we can do to avoid these challenges through proactive problem solving and understanding biases and habits that get in the way of our success. Some of the themes in this chapter include being open-minded, possessing a willingness to re-evaluate and adapt to new information, and avoiding mistakes through learning from past contributors to the field of entrepreneurship.

15.1 Launching Your Venture

Learning Objectives

By the end of this section, you will be able to:

- Explain the importance of creating and discussing the vision statement
- Determine the documents necessary for managing risks
- Describe company culture and the purpose of a code of conduct
- Summarize how to outline and schedule the operational steps of the launch

The big day has arrived. Your opportunity recognition process noted that your idea solves a significant problem or need, you double-checked that the target market is large enough for potential profitability, you have a method to reach this target market, you have a passion to start this company, and you found resources to support the start-up. Knowing that you analyzed and addressed these topics, you now need to consider some of the more sensitive topics regarding the agreements within your team. Many entrepreneurs overlook the issues discussed here or act on them in a generic manner instead of fitting them to the specific needs of the venture. This lack of due diligence can be detrimental to the success of the business. The advice presented here can help you avoid those same mistakes.

To protect the interests of all parties involved at launch, the team should develop several important documents, such as a founders' agreement, nondisclosure and noncompete forms, and a code of conduct. Before these are drafted, the team should ensure the venture's vision statement is agreed upon. (See Entrepreneurial Vision and Goals for a discussion around creating a vision statement.) The entrepreneurship team needs to be in complete agreement on the vision of the venture before they can successfully create the founders' agreement. If some team members have an interest in creating a **lifestyle business** (a venture that provides an income that replaces other types of employment), while other team members want to harvest the venture with significant returns, there is a clash between these expectations. An angel investor will also have a strong opinion on the vision for the venture.

Founder's Agreement, Nondisclosure Agreement, and Noncompete Agreement

Honest and open discussions between the entrepreneurial team members, including your angel investor if an angel investor is part of your initial funding, must take place before opening the venture. These frank discussions need to include a founders' agreement as well as the identified vision for the venture. The **founders' agreement** should describe how individual contributions are valued and fit into the compensation plan and should consider and answer these questions:

- Will the entrepreneurial team members receive a monthly compensation?
- Is there a vesting plan with defined timelines aligned with equity percentages?
- What happens if a team member decides to leave the venture before an exit event? How will that team member be compensated, if at all?

Discussing the entrepreneurial team members' expectations avoids the problem of an entrepreneurial team member expecting a large equity stake in the company for a short-term commitment to the venture, and other misguided expectations. Such problems can be avoided by addressing the following questions:

- What activities and responsibilities are expected from each team member, and what is the process or action when individual overstep their authority?
- Is there an evaluation period during which the team members discuss each other's performance? If so, how is that discussion managed, and is there a formal process?
- What happens if a team member fails to deliver on expected actions, or if an unexpected life event occurs?

The founders' agreement should also outline contingency plans if the business does not continue. The

following questions help define those next steps and need to be answered prior to opening the venture:

- If the venture is unsuccessful, how will the dissolution of the venture be conducted?
- What happens to the assets, and how are the liabilities paid?
- How is the decision made to liquidate the venture?
- What happens to the originally identified opportunity? Does a team member have access to that idea, but with a different team, or implemented using a different business model?

Once the venture opens, discussing these topics becomes more complicated because the entrepreneurial team is immersed in various start-up activities, and new information affects their thoughts on these issues. Along with these topics, the founders' agreement should also state the legal form of ownership, division of ownership (this refers to the division of equity at either the next round of financing, or harvesting of the company), as well as the buyout, or buyback clause. (See Entrepreneurial Journey and Pathways for a discussion on the life cycle stages of a venture, including end stages of harvesting, transition, and reincarnation of the business.)

The **buyback clause** addresses the situations in which a team member exits the venture prior to the next financing round or harvesting due to internal disputes with team members, illness, death, or other circumstances, clearly stating compensation and profit distribution (with consideration of what is reinvested into the venture). Discussing these topics provides agreement between all team members about how to address these types of situations. The buyback clause should also include a dispute resolution process with agreement on how the dispute solution is implemented. Identifying exactly how these items are handled within the founders' agreement prevents future conflicts and even legal disputes.

If the entrepreneurship team includes an angel investor, the angel investor typically has the final say in these questions. In the best possible scenario, the angel investor has experience creating a founders' agreement and can provide valuable insights into working through this document. One common approach to creating this document, given the angel investor's available time, is for the entrepreneurship team to discuss and agree on the final document, then have the angel investor review the document for final approval. Making Difficult Business Decisions in Response to Challenges will help in finalizing your founders' agreement.

After completing the formal vision statement and the founders' agreement, you might want to have an attorney evaluate the documents. This checkpoint can identify gaps or decisions that were not stated clearly. After receiving the examined documents back, the team should once again review the documents for agreement. If everyone is satisfied with the documents, each entrepreneurship team member should sign the document and receive a copy. If, later, the entrepreneurship team decides a change needs to be made to either the vision statement or the founders' agreement, an addendum can be created, again with all parties agreeing to any changes.

Two other formal documents your team might want to consider include a nondisclosure agreement and a noncompete agreement. These documents can be applied to all employees, including the startup team, with consideration of extending to other contributors such as contractual personnel. A **nondisclosure agreement** agrees to refrain from disclosing information about the venture. Topics that might be included in this document include trade secrets, key accounts, or any other information of high value to the venture or potentially useful to a competitor. A **noncompete agreement** states that the person signing the agreement will not work for a competing organization while working for the venture, and generally for a set length of time after leaving the venture. Often, this time period is one year, but it can be longer depending on the know-how or intellectual property the exiting team member has.

Company Culture and Code of Conduct

In conjunction with these formal documents, the founding team should determine the culture they would like to build for their venture. Ideally, the organization's **company culture** is made up of the behaviors and beliefs that support the success of the organization. For example, when you walk into a business, is there a bustle of

noise and activity, or is the business calm and restrained? This impression results from the organization's culture. We could compare the difference between walking into a high-end jewelry store and walking into a fast food restaurant. Both businesses have distinctly different cultures. If the venture is highly dynamic with fast-paced decisions and constant change, then the culture should support this type of venture. Perhaps the team wants to create a work hard, play hard culture. In that case, standards that support ad hoc team creation for impromptu discussions should be encouraged, rather than setting up a bureaucratic culture that requires approval of all meetings and deliberation of decisions prior to action. Many tech companies support a work hard, play hard culture. This culture is reinforced with open office spaces that provide opportunities to collaborate with colleagues. Or perhaps ping pong tables and kitchens are provided to encourage interaction. Even the hours of operation contribute to culture creation by either encouraging employees to set their own hours or restricting work hours through regulated entry. In contrast, a more bureaucratically structured environment may fit a venture whose success relies upon compliance with external regulations and the use of highly sensitive or private information. An example of a bureaucratic culture aligns with many financial institutions. The culture within a bank conveys security of our deposited funds; we want a bank to have processes and systems in place that reinforce that we can trust the bank with our finances.

The culture-defining process should include the entrepreneurship team's creation of a **code of conduct**. Some organizations develop a code of conduct that includes guiding principles, while other organizations create detailed descriptions of what is acceptable and what isn't acceptable. Your venture's code of conduct should fit with your venture's vision, the culture desired, and the entrepreneurship team's values. Codes of conduct should be created as documents that include a sensitivity to people within the company as well as the greater community. A code of conduct addresses the values that the organization supports, as well as ethical considerations. The purpose of a code of conduct is to help guide employee actions to align with the desired behavior. Including uniquely specific examples that align with the specific venture, can further communicate the desired behaviors. There are many varieties of codes of conduct; the main point is to create a code that supports the values and behaviors that you want to advance throughout your organization. Figure 15.2 and Figure 15.3 show two approaches to developing a code of conduct that fits the company's culture and vision. The first example might be used by an advocacy-based venture that desires a principle-based approach to guiding employee behaviors through a code of conduct that provides general guidelines, rather than a more rule-based approach as presented in the second example. These two examples highlight the importance of creating a code of conduct that fits the beliefs and culture that you want to encourage within your venture.

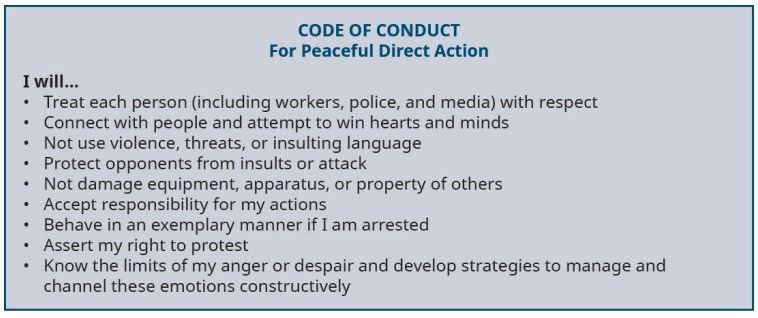


Figure 15.2 This sample code of conduct demonstrates how a code of conduct needs to fit the specific organization's needs. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

CODE OF CONDUCT	
Compliance with All Laws	Employees must comply with all laws, including bribery, fraud, securities, environmental, safety, and employment laws.
Corruption and Fraud	Employees must not accept certain types of gifts and hospitality from clients, vendors, or partners. Bribery is prohibited in all circumstances.
Conflict of Interest	Employees must disclose and/or avoid any personal, financial, or other interests that might influence their ability to perform their job duties.
Company Property	Employees must treat the Company's property with respect and care, not misuse it, and protect company facilities and other material property.
Cybersecurity and Digital Devices Policy	Employees must not use company devices or company-provided online access to download or upload obscene, offensive, or illegal material; to transmit confidential information to unauthorized recipients; to pirate movies, music, or software; or to visit potentially dangerous websites that can compromise the network and computers' safety.
Social Media Policy	Employees may [or may not] access personal social media accounts at work but are expected to act responsibly, follow company policies, and maintain productivity.
Sexual Harassment	Employees must not engage in unwelcome or unwanted sexual advances, requests for sexual favors, and other verbal or physical conduct of a sexual nature. Behaviors such as conditioning promotions, awards, training, or other job benefits upon acceptance of unwelcome actions of a sexual nature are always wrong.
Workplace Respect	Employees must show respect for their colleagues at every level. Neither inappropriate nor illegal behavior will be tolerated.

Figure 15.3 This code of conduct addresses more traditional and general topics than in the first example. In all cases, the code of conduct needs to address your unique venture including awareness of how the code of conduct aligns with the leadership and culture that you want to develop.[1] (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Earlier, we discussed the importance of the lead entrepreneur taking the initiative to discover the investor's business knowledge and learning about the investor's previous experience in funding an entrepreneurial venture. The code of conduct is another area that entrepreneurial teams frequently skip over by accepting a generic code of conduct rather than recognizing that there are a multitude of topics, phrases, and principles that should be uniquely designed to fit the venture. These two examples demonstrate the vastly different topics addressed within a code of conduct as evidence for why your code of conduct must fit your intentions for how you will conduct business and support the success of your venture.

These preparatory documents should be personalized to align with the entrepreneurial team and desired behaviors that support the success of the venture. Although standard language and forms addressing these topics are available online, these generic models aren't intended to meet your unique venture's needs or the entrepreneurial team's needs. Taking the time to discuss and prepare these documents pays off in well-crafted documents and aligns the entrepreneurship teams' vision, goals, and dreams for their venture.

ARE YOU READY?

Google's code of conduct

Review Google's code of conduct (https://openstax.org/l/52CodeConduct) as you think about developing your own code of conduct. What do you like about Google's code of conduct? What would you change? How does this example help you in creating a code of conduct for your venture?

1 Some language adapted from the U.S. Department of State Sexual Harassment Policy: https://www.state.gov/s/ocr/c14800.htm.

Operational Steps to Launch

The next action is outlining the operational steps in the venture creation process. A good approach is to create a chart that identifies how you should proceed. The goal in creating this chart is to recognize what actions need to be taken first. For example, if you need a convection oven for your business, what is the timeline between ordering and receiving the oven? If you need ten employees to manually prepare and package your product, how long will it take to interview and hire each person? According to Glassdoor, the hiring process took 23 days in 2014 and appears to be lengthening in time as organizations become more aware of the importance of hiring the right person.[2] What about training? Will your employees need training on your product or processes before starting the venture? These necessary outcomes need to be identified and then tracked backwards from the desired start date to include the preparatory actions that support the success of the business. You've probably heard the phrase that timing is everything. Not only do entrepreneurs need to be concerned about finding the right time to start the venture, they also need the right timing to orchestrate the start-up of the venture.

Below is a sample **Gantt chart**, a method to track a list of tasks or activities aligned with time intervals. You can use this tool to help identify and schedule the operational steps that need to be completed to launch the venture. One approach to creating a Gantt chart is for each team member to independently create a list of operational activities or tasks required to start the venture that fall under their area of involvement. Then the team can create a master list of activities to discuss: This helps clarify who is contributing to or owning each task. Next, have all team members create their own Gantt chart based on their task list: That is, the time required for each task should be spelled out, including steps that must happen sequentially (when one task cannot be started until another step is complete). Once again, bring all team members together to create one master Gantt chart. This will help ensure that dependencies from member to member are accounted for in the planning. These contingencies and dependencies need to be identified and accommodated for in the master schedule. For example, in Figure 15.4, we see that Mike Smith cannot perform system testing until Sam Watson has developed the system modules, and in turn, that task can't be done until Mike Smith has documented the current systems. After completing the chart, agree on assignments of responsibility to follow through on the activities, based on the timelines from the Gantt chart.

2 Glassdoor Team. "How Long Should the Interview Process Take?" June 18, 2015. https://www.glassdoor.com/blog/long-interview-process/

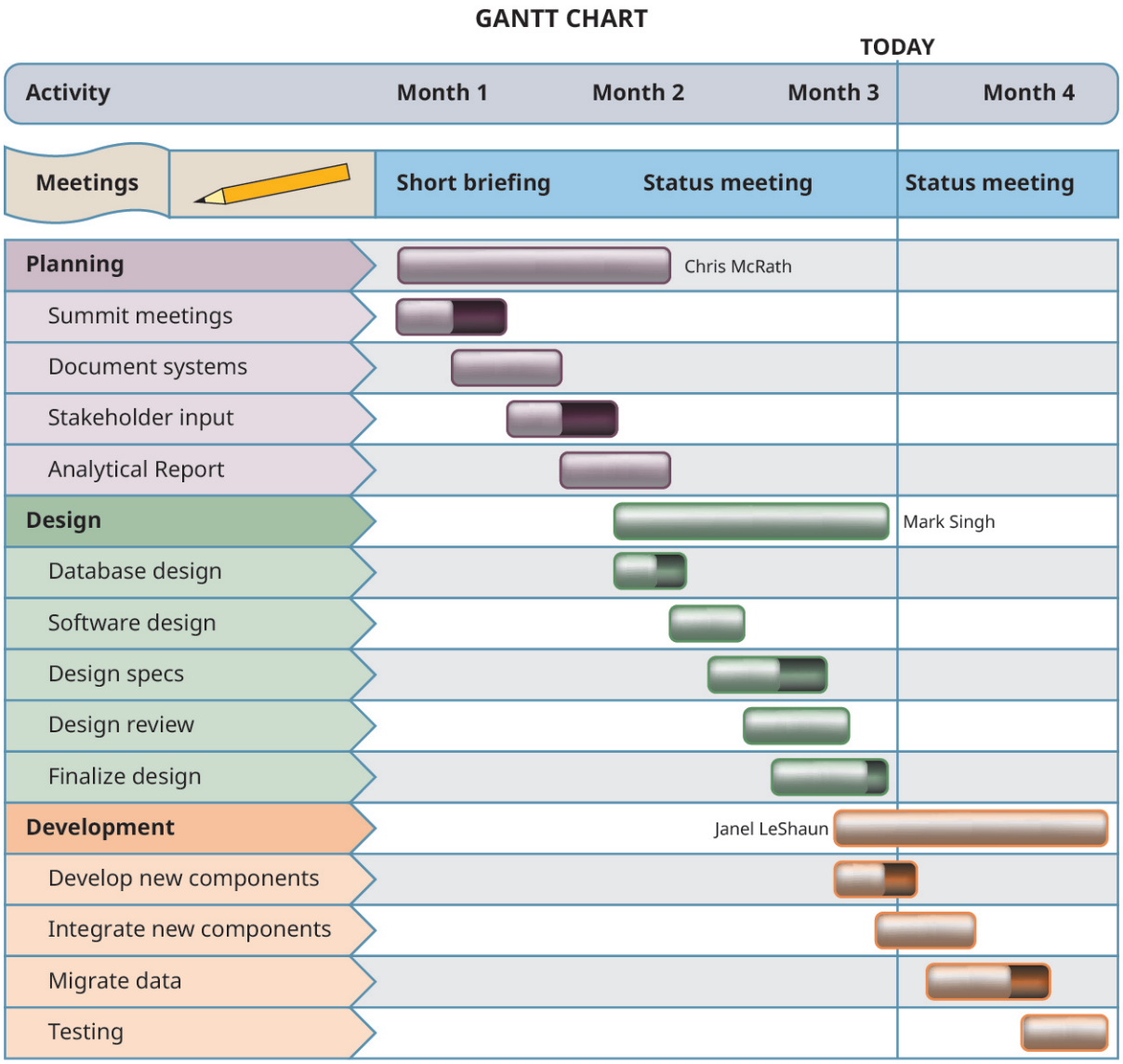


Figure 15.4 This sample Gantt chart demonstrates how activities are listed and tracked over time to assist in organizing and planning a sequence of activities. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

See the Suggested Resources for more information on how to use a Gantt chart to assist in tracking the actions needed to support the start-up of your venture and to organize each action based on your necessary timelines. You might want to reach out to other sources to find examples of how other entrepreneurs worked through their operational start-up steps.

LINK TO LEARNING

This TED Talk features Paul Tasner (https://openstax.org/l/52PTasnerTED) sharing how he found himself changing his career at the age of 66, reinforcing the idea that the world of entrepreneurship is open to all people regardless of age, race, background, health, or geographic location. In this presentation, he references a variety of activities he needed to experience in order to understand the process of starting his venture. Regardless of what we learned in our past experiences, launching a new venture includes new experiences and decisions.

After watching this video, do you have some ideas regarding starting a new venture around the idea of senior entrepreneurs? How could you support this group or build a network that creates a community of support for this large population?

Launch Considerations

Sage advice in launching the new venture is to quickly recognize when you don't have the answer or information to make the best decisions. In the early stage of launching the venture, the level of uncertainty is high, as is the need for agility and spontaneity. Even identifying the actual moment when the venture becomes a new venture can be difficult to determine. Should the venture be recognized as a new venture after receiving the necessary licenses or tax identification number, or when the first sale occurs, or when funds are first invested, or by some other method?

It is also important to keep in mind the end goal of the venture, often referred to as "begin with the end in mind." For example, many highly successful ventures never earn a dollar in sales. Depending on the entrepreneurial team's vision and the business model selected, the venture could be highly valuable from a harvest, or sale of the venture, perspective. Frequently, this decision is dictated by the angel investor. These people frequently started their own venture, harvested the venture, and as a result have funds available to invest in other new ventures. In most cases, the angel investor expects to cash out of the venture at some point in the future. These are investors who are not interested in holding a long-term equity position but rather expect to grow the venture into a position where another company buys out the venture. This buyout is also known as the harvesting of the venture and the point at which the angel investor receives a percentage of the harvested dollar sale to cover the equity stake in the new venture. Because of this pattern, entrepreneurs are often advised to "begin with the end in mind" when launching a new venture. If the goal is to sell the venture to another company, we want to identify that company before launching the venture. Of course, at this point, this is only a desire or hope, as you cannot require or expect another company to have an interest in your new venture. But you can design the new venture to align with this end goal by making decisions that support this end goal.

Consider the example of YouTube, a startup with zero dollars in sales but with a harvest price of $1.65 billion in stock from Google. The startup team, former PayPal colleagues, understood that the technology was being developed for video searching and recognized that creating a platform to house video-sharing would be desired by companies such as Google at some point in the future. Consider the tight timeline between 2005 when YouTube began supporting video sharing, and the harvest of YouTube to Google in 2006, 21 months later. This example clearly points to the importance of beginning with the end in mind.

ENTREPRENEUR IN ACTION

A New Greeting Card Concept

Is there a connection between ship architecture and greeting cards? Most people would quickly say there isn't any connection between these two disparate ideas. However, Wombi Rose and John Wise studied ship architecture, with Wise moving on to a boat-building start-up in Louisiana when they reconnected and decided to start a new venture. While traveling in Vietnam, the two ship architects came across the paper-cutting process of kirigami, similar to origami, but rather than folding paper, the paper is cut. The two engineers realized that the same design software used in building ships could also be used in creating these three-dimensional paper objects. Despite the declining greeting card industry's sales, these two entrepreneurs decided to enter the greeting card industry with a new approach to greeting cards. Pop-up kirigami art folds flat until the envelope opens, and a kirigami object pops up. Lovepop, the name of their greeting card line, has grown to 30 employees and $6.7 million in revenue.[3]

What evidence is there that Rose and Wise followed the concept of "begin with the end in mind"? If Rose and Wise followed this advice, and you were a part of this team, at what point would you begin seeking a buyer for this company? What milestones might you select for harvesting the company? Consider what actions you would accomplish to increase the sale amount to the maximum amount.

Launching your venture is a unique experience for every entrepreneurial team and for every venture. These novel situations and uncertainties create both challenges and new learning opportunities. Accepting that a multitude of possibilities exists and recognizing the importance of researching and discussing actions are valuable to the success of the team. Angel investors hold a wealth of knowledge, and with an equity stake in the venture, these investors should be included in all discussions. If you have an angel investor on your team, you have an added advantage to tap into the expertise available to support the venture. In conjunction with a well-aligned angel investor, conducting research to explore decisions will improve your venture's success. Although these decisions might seem difficult, the next section addresses how to approach difficult decisions and the role emotional connections for the venture and its team play in those decisions.

15.2 Making Difficult Business Decisions in Response to Challenges

Learning Objectives

By the end of this section, you will be able to:

- Recognize that cognitive biases can sabotage the success of the venture
- Identify key problem indicators
- Distinguish the emotional components involved in difficult decisions

Now that you are prepared to launch your business venture, let's look at your business plan and the assumptions you made while preparing it. Did you keep a list of assumptions? Did you update assumptions as new data and information suggested "retiring" some initial ideas? Did you identify milestone timelines within your business plan? Did you fully assess risks and have mitigation plans to address them? These are essential questions to consider before launch. As the business venture comes into existence, you should review your assumptions and identified milestones. Ask the following questions:

- Are your assumptions still realistic?
- Is your business venture on for the associated milestones?
- Do you need to consider any changes that have occurred in the industry you plan to enter? Has the competition changed? Are there new regulations?

Tracking any changes and comparing them to your earlier assumptions provides an opportunity to reconsider whether changes to your plan, assumptions, and milestones are necessary. After you begin your venture, you should continue to review your assumptions and milestones. If you are not meeting your projections and milestones, what has changed? What decisions should you adjust to situate your venture into a stronger position for success? If your venture is doing better than expected, analyze why the venture is exceeding your forecasted projections.

It is important to return to your business plan and consider what you will do if your assumptions are incorrect, so if your milestones aren't met, you can avoid the problem of escalation of commitment. The concept of **escalation of commitment** describes when an entrepreneur feels so committed to the plan of action that they end up losing their perspective on the reality of what is happening to the venture. They ignore the danger signs and think that if they just work harder, or pour more money into the venture, they can force the venture to become successful. Once an entrepreneur becomes this committed to the venture and is working passionately to keep the enterprise afloat, they can lose the focus and objectivity to make rational decisions.

3 Stephanie Schomer. "This Hot Greeting Card Company Uses 3-D Design and Origami to Beat Hallmark. *Inc.* June, 2017. https://www.inc.com/magazine/201706/stephanie-schomer/lovepop-greeting-card-design-awards-2017.html

They can begin to react to the situation, stubbornly persist, or begin to ignore the danger signs that should alert them that reevaluation of the situation is necessary.

Escalation of commitment negates the recognition that a pivot action is necessary. As you recall from Launch for Growth to Success, in the entrepreneurial world, pivot is the action in response to recognition that the current method, approach, process, or idea isn't working. Pivot is the point at which entrepreneurs realize that a change is required and pivot into something different.

Cognitive Biases and Problem Indicators

There is a fine line between believing in one's abilities and the value of the venture versus stepping into a perspective that ignores new information or results. Entrepreneurs often need to face criticism and challenges where their confidence in the opportunity and their ability to create a successful venture override the criticism, but there is also danger in not listening to new information and re-evaluating one's perspective to avoid biases. According to Cossette, in reviewing twenty-five empirical papers on heuristics and cognitive biases of entrepreneurs, overconfidence and optimism are the two most significant biases that contribute to an entrepreneur's failure to recognize the need to change or end the venture. Other causes for the entrepreneur's failure to end the venture include "the law of small numbers, the illusion of control, the planning fallacy, escalation of commitment, the status quo bias, and the hindsight bias,"[4] as shown in Figure 15.5. To avoid this failure to exit the venture, we can identify **fail-safe points** within the business plan. These are the points that trigger the entrepreneur to consider what actions are needed to bring the venture back to a healthy position and whether this action is reasonable and feasible. Identifying these trigger points and creating contingency plans *before* opening the venture can prevent the entrepreneur from becoming trapped by these biases, such as the dangers of becoming overly committed and throwing resources into an impossible situation. Let's look deeper into these biases and potential key problems that challenge our own decisions and the success of the venture.

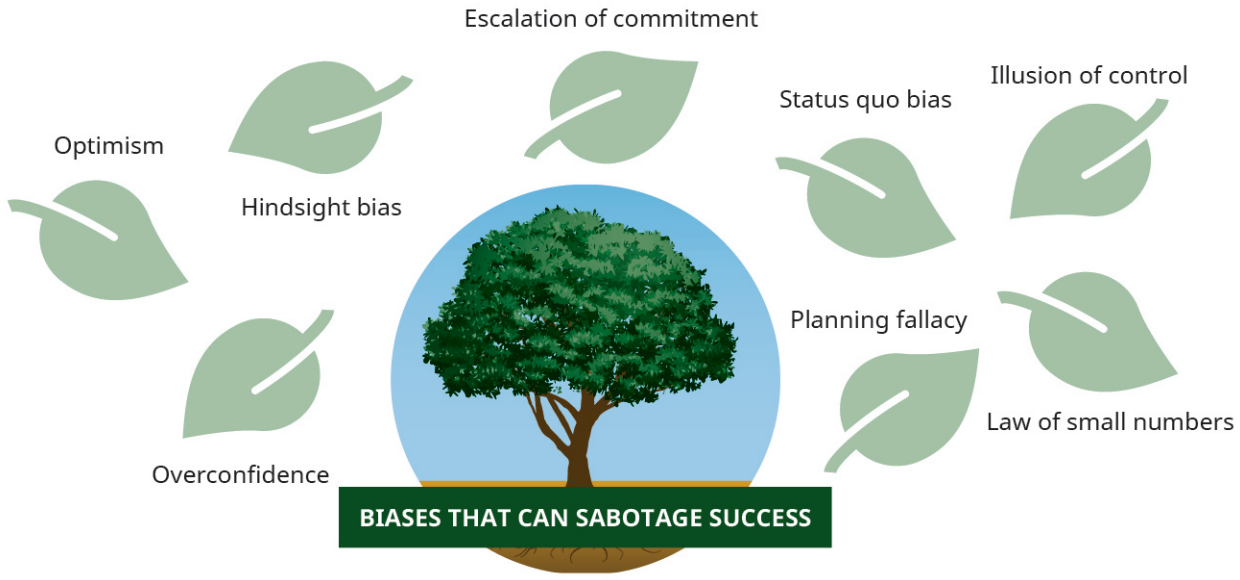


Figure 15.5 The biases shown in this image are areas that can contribute to the failure of the venture. Being aware of these biases provides a reality checkpoint. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

4 Pierre Cossette. "Heuristics and Cognitive Biases in Entrepreneurs: A Review of the Research." *Journal of Small Business & Entrepreneurship*, *27*(5), 471–96. November 2015. doi:10.1080/08276331.2015.1105732

As described in Cossette's research, the *law of small numbers* refers to the target market not being large enough, or failure to attract a larger target market. The *illusion of control* refers to the entrepreneur believing that he or she can force the market into realizing the venture is the best, or that additional persistence will result in positive results. The **planning fallacy** identifies the pattern of creating a business plan that is too optimistic. Gish noted that business planning is intended to present realistic decisions and projections; however, research suggests that confidence in the plan places entrepreneurs in a position of believing their plans are accurate, causing a heightened belief that the venture will succeed, when in fact, the business plan is overly optimistic.[5]

The **status quo bias** is a tendency to refer to a previously identified behavior or information as the ongoing habit to perpetuate. This bias can prevent the entrepreneur from recognizing that a new action is required—when a creative or innovative change is necessary to avoid economic distress rather than following a previously established pattern or habit—instead of continuing to follow the status quo. The **hindsight bias** is the belief that, in hindsight, the action or event was predictable, when in fact there was little if any indication that an event would occur.

As you can see, many of these problems are related to the **hubris** of the entrepreneur. Hubris is a strong belief in oneself, a belief of over-confidence or pride in one's ability to affect the outcome of decisions when other factors have the greatest influence.

Aside from these challenges, other key problem indicators include insufficient available cash. **Burn rate** is the rate at which the venture burns through the available cash needed to sustain the business: More cash is going out than is coming into the business (review burn rate in Developing Startup Financial Statements and Projections). Lack of control systems can be a contributor to excessive cash use, as can excessive waste in production, lack of follow through on collection of payment, or low inventory turnover creating excessive waste, such as with perishable products.

A misconnect between the target market's desires and the product or service provided, can also create challenges, as can incorrect pricing of the product, or not having the right talent in your personnel or start-up team. However, planning only for success can be the biggest problem an entrepreneur makes. Keeping an open mind provides opportunities to see the reality of how the venture deviates from the plan as an action item to reconsider the venture from a new perspective.

Decision Making to Overcome Challenges

Now let's look at how we can reevaluate the venture and consider what changes are possible to position the venture for a different future than first envisioned. Let's examine a real story from Stacy Madison's life. Stacy Madison is the entrepreneur who started Stacy's Pita Chips. Madison had a background in social work but wasn't happy with her career choice, so she decided to open a sandwich food cart business in downtown Boston. As her business became more popular, customers had to wait in line for longer times. When they reached the food cart window, they were often cranky and unhappy about the wait. Madison and her team discussed ideas on what to do for customers who grew tired of waiting in line. They came up with the idea of slicing bagels into chip size bites and baking the bagels with olive oil, then handing the bagel chips out to the customers waiting in line. Customers loved the bagel chips and requested the chips when they reached the food cart window. At first, Madison's team would explain that they did not sell the chips but only gave them away to help their customers who grew hungry waiting in line. After repeatedly hearing this request from customers, Madison reevaluated her sandwich business and considered that maybe she should be in the bagel chip industry. The success of this story is that Madison sold her pita chip company to Frito-Lay for $65 million.[6] And the purpose of this example is to remember that when we start a venture, we need to be open-minded to recognize unexpected patterns and new information that can lead us in a different direction from the original plan and intention.

5 J. Jeffrey Gish. "Failing to Plan but Not Planning to Fail: A Theory of Entrepreneur Optimism and Business Planning." *Academy of Management Annual Meeting Proceedings*, *2016*(1), 1. November 30, 2017. doi:10.5465/AMBPP.2016.10945abstract

Personnel Change Challenges

One area of potential problems in a new venture is the entrepreneurial team, the start-up people on the original team, and the need for personnel changes within the team. Where did the people on your startup team come from? Are some of them longtime friends or perhaps family members? What skills or knowledge do they bring to the venture? Are they aligned with the needs of the venture? And importantly, are they the best resource for their role once the venture is up and running? Answering these questions clarifies whether team members are a good fit within the venture over time. The startup team no doubt provided enthusiasm and ideas that helped to identify and formulate the potential new venture. Team members probably contributed ideas and content in building the business plan, but over time, the needs of the venture will change. Being aware that changing needs might also result in changes within the startup team, and employee skills, is part of managing the growing venture.

For success, the team and employees need to align with the needs of the venture. Sometimes, entrepreneurs begin their business with people who agreed that the idea was sound and that the opportunity existed and was worth supporting. But these people might not have the knowledge, skills, and abilities necessary to support the venture as it grows. Frequently, we share similar skills and interests with our friends and family members. This means that we might have a venture with too many people with the same skill sets. Or we might have disconnects between what the venture needed in the past and what the venture needs currently.

Another personnel problem is discovering unethical actions that violate the code of conduct created in the preparatory documents. According to the National Business Ethics Survey of the U.S. Workforce in their 2014 report, 60 percent of reported misconduct involved someone with managerial authority.[7] These findings alert us to the importance of creating a code of conduct that aligns with the values needed to support the success of the organization. When the entrepreneur feels pressure to act unethically in an attempt to bring in new business or prevent the organization from financial stress, unethical actions can become tempting. Knowing that 60 percent of unethical actions occur at the managerial level should provide evidence to support the need to proactively consider how to avoid this dangerous situation. The same report encourages addressing potential problems by including zero tolerance for abusive behavior, lying, discrimination, and sexual harassment. An interesting finding noted that egregious rule-breaking behavior was infrequent, while more subtle "ongoing and continuous behavior, such as abusive and intimidating behavior, seems to be more prevalent."[8] This result speaks to our earlier discussion on the importance of creating an appropriate culture. If an undesirable behavior is prevalent, this would seem to indicate that the culture supports this behavior. The study also noted that "frequency of misconduct reflects the strength of the company's ethics culture," noting that "60% of misconduct committed in companies with a strong ethics culture was a one-time occurrence," and that frequency of unethical acts rose as the culture of ethics declined.[9]

Recommendations from this same report for encouraging ethical behavior include the actions shown in Figure 15.6.

6 Katie Morell. "The Story behind Stacy's Pita Chips." Open Forum. May 11, 2012. https://www.americanexpress.com/us/small-business/openforum/articles/the-story-behind-stacys-pita-chips/
7 Ethics Resource Center. National Business Ethics Survey of the U.S. Workforce. 2014. https://www.bentley.edu/sites/www.bentley.edu.centers/files/centers/National%20Business%20Ethics%20Survey.pdf
8 Ethics Resource Center. National Business Ethics Survey of the U.S. Workforce. 2014. https://www.bentley.edu/sites/www.bentley.edu.centers/files/centers/National%20Business%20Ethics%20Survey.pdf
9 Ethics Resource Center. National Business Ethics Survey of the U.S. Workforce. 2014. https://www.bentley.edu/sites/www.bentley.edu.centers/files/centers/National%20Business%20Ethics%20Survey.pdf

POLICIES AND PROCESSES THAT ENCOURAGE ETHICAL BEHAVIOR

- Maintain commitment to ethics and compliance programs and seek industry leadership.
- Focus on efforts to empower employees and deepen their commitment to the company and its long-term success.
- Develop ongoing programs and structures to monitor misconduct within the company.
- Develop initiatives to address the most common forms of misconduct.
- Educate workers about Dodd-Frank and other laws designed to encourage whistleblowers and protect them from retaliation.

Source: Ethics and Compliance Initiative. National Business Ethics Survey 2014. http://ethics.org/research/nbes

Figure 15.6 The Ethics and Compliance Initiative from the National Business Ethics Survey outlines policies and processes that encourage ethical behavior. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Ethics and alignment of personnel to the venture's future growth and success are all reasons to reevaluate the entrepreneurial team and personnel. Frank conversations are required to protect the future success of the venture and the best decisions to support this success. Ethical challenges need to be addressed quickly and preferably proactively to avoid being pulled down into reacting to a crisis that could be avoided by creating a culture and code of conduct that encourages correct actions. Sage advice is to clearly state up front the vision for the venture and agreement from the start-up team that the survival of the venture is the priority. Ethical behavior is an important topic of these discussions.

Personnel and Growth Challenges

Before starting the venture, the start-up team should ask these two questions:

1. What happens if we are wildly successful?
2. What happens if we are horribly unsuccessful?

The purpose of these questions is to consider how resources and debts will be resolved before the venture begins to use or acquire resources. If your relative or friend contributed by letting you use her living room for your planning meetings and bought pizza to keep the team energized, does she have a stake in your venture? If your venture is wildly successful, she might believe that she should receive financial remuneration for her contributions. The point is, people often change when there is lots of money or when the venture is on the edge of disaster. Planning for both extremes provides a framework for the entrepreneurial team to consider their own expectations and the expectations of other people involved in the project *before* these types of situations happen.

This discussion should also address the agreed-upon method for making difficult personnel decisions. Is there a severance package? If so, who is entitled to the severance package? Does the exit of employees, and even people on the start-up team, exclude them from future expectations if the venture is successful? If the funding source includes contractual liabilities, how is the release of a start-up team member resolved? If new team members or employees are added, will these people be considered employees who earn wages, or are some positions identified as receiving equity positions with financial gains through the harvesting of the venture? Addressing these questions before starting the venture can preserve relationships by clearly stating and agreeing to these sensitive decisions that can carry long-term consequences. In considering these questions and awareness of how the venture's need will change in the future, you might want to revisit your founder's agreement for clarity and alignment with any new information or concerns that arise in the start-up phase.

Lack of Sales and Customer-Base Challenges

Perhaps the biggest disappointment is when the entrepreneurial team has completed the pre-planning,

received funding, and opened the venture for business, only to find out that sales aren't realized. The target market isn't rushing to the website or location to purchase the product or service.

There are many reasons this can happen, which can make finding a solution difficult. The first action is to bring the team together to discuss possible reasons why the projected sales aren't being realized. This could result from inadequate marketing, targeting the wrong market or audience, selecting the wrong distribution system, communicating the wrong message or benefit within the marketing plan, or perhaps lack of training for sales personnel or first responders who manage the venture-customer relationship.

Identifying the problem is one solution to consider. Some tools that help in problem identification include brainstorming, creating mindmaps, and conducting additional research. Brainstorming provides a free flow of ideas for further exploration and analysis. The most important part of brainstorming is not judging any ideas: the more ideas that are shared, the higher the probability for identifying the problem. A mindmap taps into a different approach to gaining a new perspective on thinking about the problem. A mindmap has a center that states the problem, such as lack of sales. Next, you create branches identifying all the possible reasons why the problem occurred, such as incorrect target market and incorrect marketing message. Then you create sub-branches that relate to these first-level branches. Including pictures and color diagrams contributes to the process. The goal in creating a mindmap is to be creative in *exploring the problem* rather than attempting to hone in on a solution. Adding visuals encourages people's brains to think creatively. After creating the mindmap, take a break from thinking about the problem. As strange as this seems, the process of focusing on creating the mindmap alerts your mind that this is a problem that is important. As you walk away from the problem, your mind is still thinking about the problem, but at a subconscious level. This opens the opportunity for an "aha" moment where you're better able to figure out what is happening and understand what you need to do.

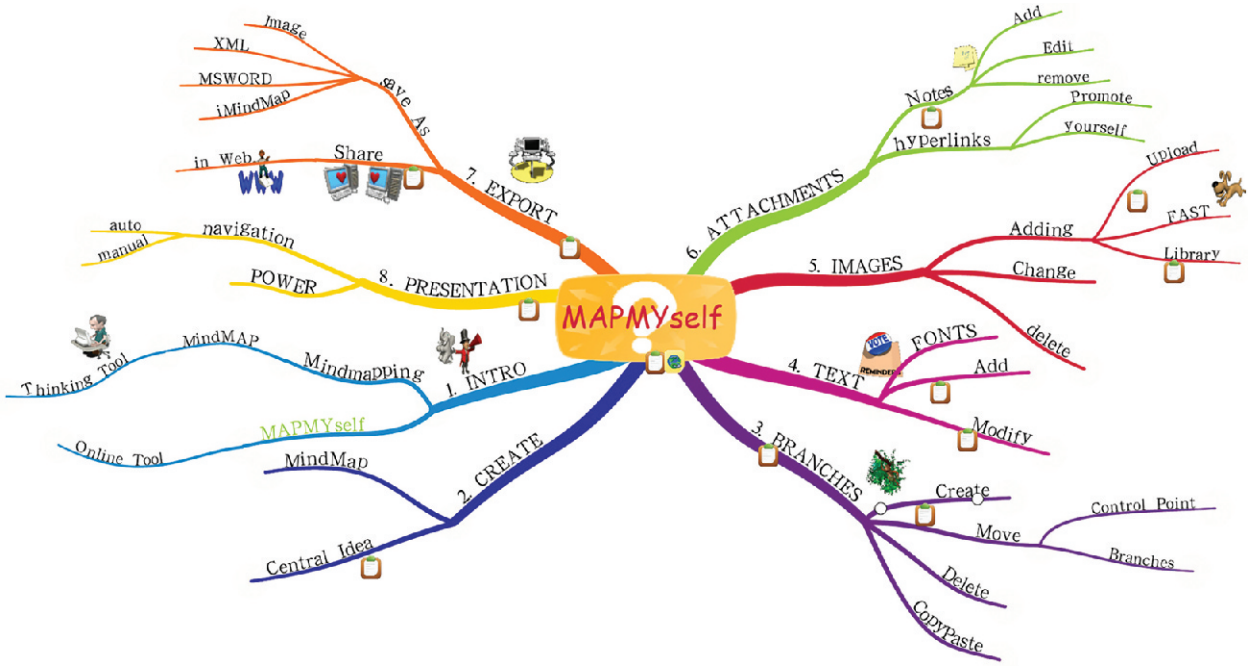


Figure 15.7 Example of a mindmap. Mindmaps can be created to inform and increase creativity in both understanding the topic or problem, and in discovering connections. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Both brainstorming and mindmapping are excellent tools that lead to conducting more research. After completing brainstorming and mindmapping, you should have a better understanding of the problem and a clear picture of topics to research, and possible methods to gain new insights into the problem of lack of sales or customer base, such as surveys, focus groups, or free samples. You can even go back to brainstorming and creating a mindmap around this newly discovered area identified through the first round of brainstorming or creating a mindmap. Or you might already have feedback that reveals a pivot for moving the venture in a new

direction, like Stacy Madison did in discontinuing the food cart and moving into the snack food industry. Another response to lack of sales or customers is to use social networking sites to draw attention to your business. You can offer short-term incentives to encourage your target market to react or provide feedback about your product.

ARE YOU READY?

Mindmapping

Practice either brainstorming or mindmapping by identifying a potential problem your venture might face. Include at least four branches and four sub-branches in your mindmap. After reviewing the completed mindmap, identify at least three methods you could use to research the most significant topic discovered through creating the mindmap. Was this activity beneficial? How might you use this method in the future?

15.3 Seeking Help or Support

Learning Objectives

By the end of this section, you will be able to:

- Identify sources for assistance
- Explain the benefits provided through seeking assistance
- Compare tools to assist in deciding what advice to follow

You've learned about some of the challenges in starting the venture and the types of decisions that the entrepreneurial team must make, as well as the importance of recognizing when you don't know something or that you have encountered a problem. Facing these issues is easier when you recognize that asking for help should be part of the process. Given the wide range of variables involved in starting a new venture, it's just not possible for one entrepreneur to have all the answers. Asking for help is an intelligent decision: It's an action that recognizes the complexity of starting and managing a venture.

Types of Assistance

Fortunately, there are many types of assistance available in the field of entrepreneurship starting with your own network of people. Additionally, there are local, regional, national, and even international groups available to help you navigate the entrepreneurial journey.

Ideally, the entrepreneurial team conducted due diligence in their quest for funding (see Entrepreneurial Finance and Accounting). For those entrepreneurs pursuing financing through angel investors, research on what angel investors contribute to the funded entrepreneur beyond the actual dollars invested highlights the importance of the angel investor's expertise and knowledge as a contributor to the venture's success.[10] While many entrepreneurs focus solely or primarily on receiving funding to start the venture, this study points to the importance in selecting an angel investor with knowledge of the industry, the distribution system, the technology, product, or the target market, as imperative to the success of the venture.

We've discussed the importance of finding an angel investor who has a background and experience in a similar area as your venture. Finding the right angel investor not only results in receiving the needed funding, but also access to this person's knowledge and personal network. Ideally, the angel investor has knowledge related to your industry, your target market, and your supply chain or distribution channel. This background knowledge provides you with key resources that can give your venture expertise that contributes to the venture's success. The angel investor's network also provides opportunities to gain key insights, seek advice, and discuss ideas or solutions that benefit the venture as a network of well-informed and experienced people.

10 Karla Peterson and William Mayfield. "Knowledge Transference in the Angel-Entrepreneur Relationship." *Frontiers of Entrepreneurship Research*: 27(2), Article 5.

The other primary network is the entrepreneurial team's network. These people include spouses/partners, family members, business associates, colleagues, and friends. These people can provide ideas and knowledge from a variety of perspectives and backgrounds. Connecting and reaching out for help requires both the ability to build relationships and the ability to recognize that seeking help reflects maturity and wisdom. As you tap into your network and seek advice, consider each person from a long-term relationship-building perspective. Consider how you might return the favor at a future time, if asked to help, or provide your expertise back to the people you access for help.

As you work with your network, keep track of the person's name, your conversation, and any commitments made during the meeting. A commitment might be a follow-up message on how you used the advice or response to the request, or an action that you will perform for someone else. Creating a formal network or contact system helps in developing this network into a long-term relationship-based perspective.

When seeking advice, be respectful of the other person's time. This means identifying exactly what type of help you want to request from the person. Are you requesting an introduction to someone else within that person's network, or advice about solving a problem, or access to physical resources? Setting up an appointment demonstrates respect, as does preparing for the meeting and explaining how you will use the advice. Remember to thank the person and follow up with feedback on what happened from using the advice.

The types of assistance that can be provided through networking include:

- advice or information
- access to other people's networks
- access to financial resources
- business services such as legal, accounting, or administrative support
- physical resources such as land, buildings, or equipment.

Other free sources of support are instructors of your business courses, other business owners, organizations such as the SCORE (originally called the Service Corps of Retired Executives) and resources within the Small Business Administration (SBA). SCORE is an organization with a network of volunteers across the U.S. and is a resource partner with the SBA. SCORE offers mentor consultants, workshops, and other assistance to support the success of small businesses.

The SBA is a federally funded organization charged with assisting small businesses from startup through their continued existence. The SBA can help in reviewing and improving your business plan, providing assistance in finding funding through loans or grants, and acting as a consultant throughout the venture's existence. The SBA provides help in complying with both state and federal regulations. Depending on your business model, you might need licenses or permits, and your local SBA office will be well informed on these topics and can help you acquire what is needed to support the success of your venture.

LINK TO LEARNING

Watch this video explaining various services offered by the Small Business Administration (https://openstaxcollege.org/l/52SBAServices) to learn about resources to support your venture.

Most states provide start-up help to small businesses, which can be found by searching the internet for your state's sponsored help in starting a business. In addition, there are often local meet-up groups and community-supported assistance to help you start your business. You might also find a virtual support group that provides advice from a diverse group of potential business owners.

A paid source of help—legal assistance—can save anguish, time, and money for the entrepreneurial team. In selecting an attorney, look for one with experience in entrepreneurial ventures similar to yours. Resources to help you find an attorney include checking with your network or angel investor for a

recommendation or contacting the local branch of the American Bar Association. Most states have an online directory of local member attorneys that you can use to search for a lawyer who fits your venture's needs. Once you have identified an attorney, research the best method for payment of these services. Some possibilities include a monthly retainer fee, payment for specific services, or payment on an hourly basis for work performed.

Other paid-for services include accounting, tax reporting, and human resource management areas. Opening and managing a business takes time, and assigning a professional accountant the responsibility of preparing monthly financial statements and tax reports can provide you with expert support as well as provide you with time necessary to position your venture into a successful growing business, as does outsourcing personnel tasks such as processing payroll. These supporting companies can be either virtual companies, or a local business, depending on your needs. Especially for payroll and other human resource activities, virtual companies specialize in meeting the administrative needs in a fast and efficient manner. Oftentimes outsourcing administrative areas is a more accurate and cost-effective than completing these tasks within the venture. Although these services cost money, these activities performed require knowledge of laws and regulations that many business owners are not equipped to be experts in, nor can they reasonably stay on top of frequent changes in these matters. This can result in legal problems, as federal and state laws and regulations must be followed.

Support System Development

You learned about a variety of support systems in Building Networks and Foundations. Some entrepreneurs may seek to work with a local incubator service. These incubator community groups provide a physical location to offer working space as well as the opportunity for interactions with other new startup owners and teams. The opportunity to be in a shared space with other inspired entrepreneurs can create excitement, sharing of ideas, and opportunities to talk through challenges. Potentially, there could be synergies between your venture and another venture realized through these discussions.

Companies like Y Combinator in Silicon Valley and Techstars in Boulder, Colorado, provide unique assistance to new startup ventures (Figure 15.8). These types of organizations are considered accelerator entities intended to fast track a select number of new ventures through information sharing, seed funding with a small equity stake in the funded venture, mentoring, and offering formal angel investor "pitch" events. The selection process makes being accepted into these organizations difficult. However, once accepted, your venture becomes more credible for having been accepted, as well as for the wealth of connections and information that will be received throughout the experience.

Figure 15.8 Y Combinator provides support for new startup companies. (credit: modification of "Max Levchin speaks to Startup School" by Robert Scoble/Flickr, CC BY 2.0)

Although each incubation program offers different—and sometimes uniquely specialized—help, they can be generally categorized by the types of support potentially available through these programs. Some incubators focus on one segment of an industry, or one segment of talent or interest. For example, there might be an incubator intended only for marketing start-ups. In this example, the incubator might assist with providing support in various marketing areas such as digital marketing, business-to-business marketing, global marketing, sports marketing, video creation, or other areas that fit within the topic of marketing. Oftentimes, incubators are sponsored by a municipality or government source.

Incubators are unique to a community's interests and available resources. Some communities have a vision for the community and desire the growth of the community to align with this vision. If a community has this perspective, their incubators would also align with this vision. Other communities create incubators around available resources, such as access and support from specific groups. Figure 15.9 illustrates the wide variety of approaches used in creating incubators. An incubator is supported by perhaps one or two of these sources, depending on the goal of the incubator.

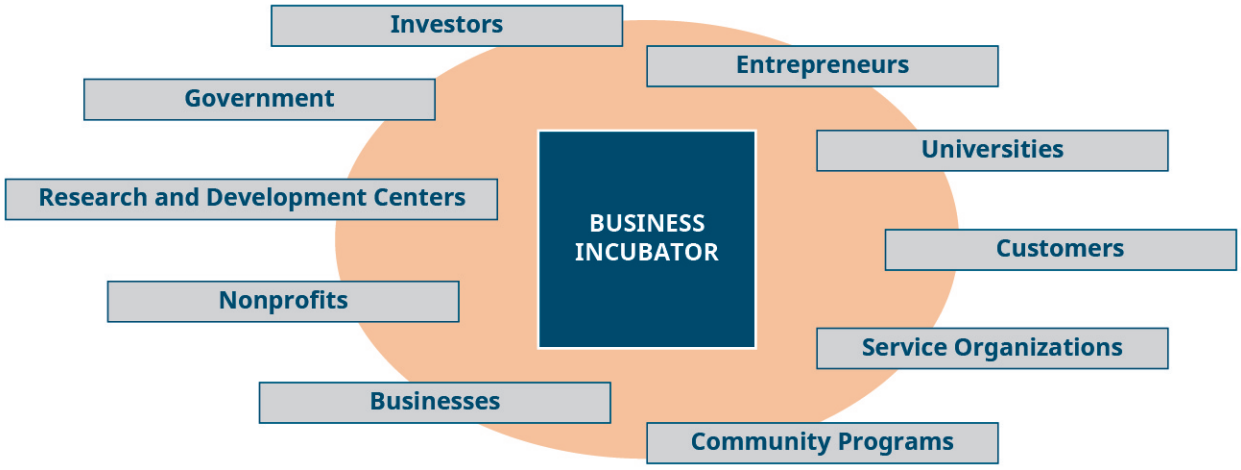


Figure 15.9 There are many potential contributors to business incubation programs. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

As you build your support group, you might want to create an advisory group, which is a formal group of people who provide you with advice. In building your advisory group, select people who demonstrate an interest in your venture and your startup team. You want resources who have expertise related to your industry, your target market, or your business model. You also want a diverse group of people who can provide insights that reflect different backgrounds and knowledge. This diversity of experience and knowledge provides you with the greatest breadth of advice, which leads to your difficult decision: what advice to follow.

Deciding What Advice to Follow

Once you have advice from a variety of sources, how do you decide which recommendations to pursue, which to consider, and which to rule out? One approach is to identify what information is qualitative versus quantitative, and evaluate one type first. Qualitative information is conceptual—about ideas—whereas quantitative information is statistical or numerical. In both qualitative and quantitative areas, the entrepreneur can create visualizations to clarify the information and support analysis and decision making. The brainstorming and mindmaps discussed earlier, and illustrated in Figure 15.10, highlight the different types of data you can work with.

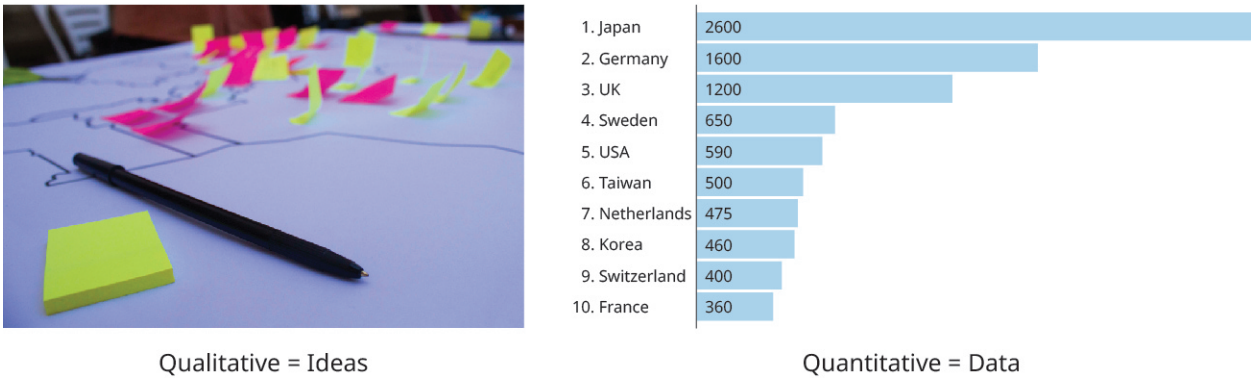


Figure 15.10 Both qualitative and quantitative factors inform decisions through ideas and numbers. (credit "left": modification of "Articulamos nuestras ideas" by Cultura de Red/Flickr, CC BY 2.0; attribution "right": Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

Two other tools for sorting through advice are the Delphi method and the Nominal Group technique. Both provide a structured methodology that can be applied to evaluate ideas. In the **Delphi method**, broad open-ended questions related to the decision being addressed are put into a questionnaire sent out to participants. For example, you might solicit input from your advisory group or another group closely connected to the topic. As responses come in, the questions are updated to align better with the first set of responses. The process repeats until there is a clear understanding of the participants' responses. Next, you create a list of possible options and request each participant to rank the options. Depending on these results, you either fine tune the list by dropping off low-ranked items, or, if the results are satisfactory, the options are narrowed to two or three top choices.

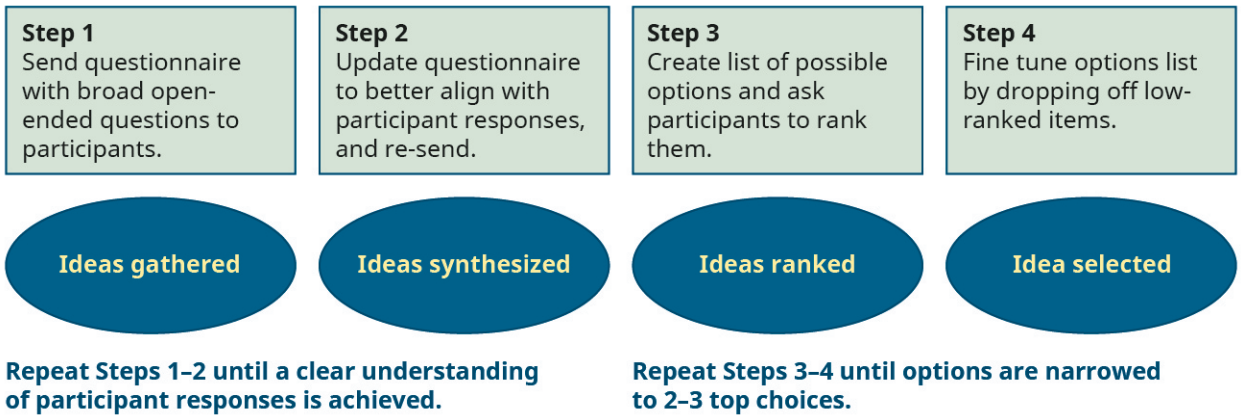


Figure 15.11 The Delphi process proceeds through repetitions of the process until an agreed-upon final answer is identified. (attribution: Copyright Rice University, OpenStax, under CC BY NC-SA 4.0 license)

The **Nominal Group** technique occurs in a group setting. Participants are presented with a question or topic and write their thoughts in response on a card. The participants do not share their comments. Once everyone has submitted the cards, the facilitator shares all feedback so that everyone can see all participants' input. The participants discuss all of the ideas. Next, the participants again write down their responses on a new set of cards. The comments are again recorded and shared so that everyone can see the results. The process continues until there is agreement on a final filtered, or narrowed, list or set of options. At this point, the participants vote or rank the remaining set of options with the goal of accepting one option.

Although these techniques and tools take time, the process of thinking through each decision and possible action helps your mind pause to reflect and to be alerted to the importance of the decision. Taking a break at this point allows you to process the information, perhaps while taking a walk or having a lunch break. At some point, you might suddenly have a feeling of knowing the right answer— the decision to make. Sometimes, this experience is attributed to a "gut" feeling or intuition that tells you what you need to do. Resources like Gary

Klein's *The Power of Intuition: How to Use Your Gut Feelings to Make Better Decisions at Work* explains how this process works in the human brain. Sometimes, this moment of recognition of the chosen decision results in a decision that wasn't produced through our processes but that offers a new and creative solution.

Taking the time to evaluate and deeply think about the problem, the advice, and possible solutions is an important part of decision making. Just as important are pausing and taking time to select a decision that is not reactive and that you feel comfortable with, keeping in mind that the decision you make might be unique, and the actual decision might not be within the advice provided to you by your support group. As the lead entrepreneur whose goal is the success of the venture, you are ultimately responsible for the decision. If the advice provided doesn't feel right, make the decision that does feel right and make sure you communicate that decision with your team.

15.4 Now What? Serving as a Mentor, Consultant, or Champion

Learning Objectives

By the end of this section, you will be able to:

- Evaluate potential next steps after exiting the venture
- Explain the roles of mentors, consultants, and champions

Depending on your experience as a first-time entrepreneur, you have a new set of choices in front of you. If you enjoyed the experience, felt the thrill and excitement of taking an idea from launch through to the successful harvesting of the venture, you might want to become involved in another new venture—that is, maybe your path is to become a serial entrepreneur. Or, after all that work, you might want to spend some extended time traveling or with family. You might want to consider ideas for giving back to the entrepreneurial community or becoming a social entrepreneur in your next venture. You might want to take some of your earnings from the harvest and become an angel investor. These decisions depend on your experience as an entrepreneur and money and less-tangible resources you gained through harvesting the venture. Having undergone a positive experience, gained significant learning, and harvested substantial funds often leads an entrepreneur into becoming a mentor, consultant, or champion for another entrepreneurial project. Think back to all the people who helped you get to where you are today. Where would you be without their help? Giving back to others continues the creation of **social capital**, the goodwill we create by giving back to individuals, organizations, and communities.

Mentors

Mentor motivation includes the satisfaction of helping and guiding other entrepreneurs through the challenges of starting, growing, and harvesting their venture. Mentors can participate through formal government organizations such as SCORE, or organizations similar to Y Combinator, or from an internal aspect such as an advisory group membership. Mentors provide assistance and advice based on their previous experience as an entrepreneur, or as a content expert within a narrowly defined area related to the new venture's product or service. Specific areas of expertise might include commercialization of a new technology, safeguarding intellectual property, marketing, or funding sources for a nonprofit social entrepreneurship venture. Just as there can be an alignment between an angel investor's knowledge and skill set to the entrepreneurial venture, mentors should also seek ventures where they can provide key insights and knowledge. Mentoring in this capacity as a former entrepreneur is more rewarding when there is an interest in the opportunity and the entrepreneurial team.

Identifying exactly what the mentor can provide and what the entrepreneurial team needs is an important part of this relationship. Both parties should discuss time commitments and expectations as part of this relationship. Mentoring requires considerable commitment and can include support for complex topics and difficult decisions. In return for this help, mentors receive satisfaction, rejuvenation, personal growth, new relationships and connections, and a feeling of philanthropic motivation.

There are also risks in taking on the role of a mentor. One risk relates to providing advice that later proves to be detrimental to the venture. Another risk is the perception that the mentor provided direction when the mentor in fact provided suggested options that the entrepreneurial team should consider in its decision. A third risk concerns confidentiality and non-compete covenants. New ideas generate additional ideas, and as a startup team fine-tunes its opportunity and venture, some ideas will be rejected. From your perspective as a mentor and former entrepreneur, you might realize that you could develop one of the rejected ideas into a successful business. This situation can present conflicts of interest between you as the mentor and the venture that you are mentoring.

Because of these risks, as well as the contributions made by the mentor, some sources believe that the mentor should receive financial compensation and enter into a contractual relationship that addresses these risks. Possible financial payments include equity in the venture, profit sharing, or a retainer fee.

Consultants

Another role you might want to consider is becoming a consultant, a position more formally defined than mentorship. You might even want to create your own consulting company focused on entrepreneurs as your target market, or select a narrower target market such as a segment within the entrepreneurial world. In considering starting your own consultant business, your start-up process is similar to the topics addressed throughout this book. Identify your own strengths and interests, identify other needs that your target market would value, and develop a business plan. Acting as a consultant contributes back to the entrepreneurial world, provides you with the enjoyment of active involvement in areas where you excel, and bolsters to your financial worth.

Champions

Great Britain offers an Entrepreneur Champion of the Year award in recognition of the importance of having support in starting a new venture. Although we don't have that award in the United States, we recognize how important support is to become successful. The Startup Champions Network is a startup organization located in Boulder, Colorado. This organization supports and connects entrepreneur-related champions: people who build and lead coalitions that create and advance resources for entrepreneurs. The Startup Champions Network seeks people who support a history of supporting entrepreneurship and innovation within their communities, recognize and model inclusiveness and collaboration skills, enjoy helping other people and work well with people, embrace humility, are action oriented, and focus on possibilities. Forbidden behaviors include being driven by self-interest, being focused on earnings or control of earnings, and lacking experience or a long-term focus.[11]

Regardless of your interest in joining a formal champion group or acting in an individual capacity, becoming a champion to promote and assist another entrepreneur provides personal growth, satisfaction, and rewarding involvement within the entrepreneurial community. Many of the characteristics desired by the Startup Champions Network reflect research related to effective leaders. Most states have organizations that support entrepreneurs, from business plan development and decision making through opportunities to give back to the entrepreneurial world in whatever capacity a person desires. Take a few minutes to research opportunities in your state and community, and consider how your own future might align with these organizations.

These choices give you some ideas on what you might want to do now that you have harvested your venture. After tasting the excitement of starting, growing, and harvesting your venture, you have a new set of options to consider from becoming a serial entrepreneur through adding value to other entrepreneur's potential successes to becoming a social entrepreneur.

11 Startup Champions Network. http://www.championsnetwork.co/

ENTREPRENEUR IN ACTION

Solving Global Health Issues

The American Society of Tropical Medicine & Hygiene (ASTMH) is the largest international scientific organization dedicated to reducing tropical infectious diseases and improving world health.[12] Diseases like malaria, Dengue fever and Zika are transmitted by mosquitoes and are increasing in frequency. These diseases reduce an infected person's quality of life and can impact their ability to earn a living by reducing energy and the capacity to carry out day-to-day activities. These afflictions can also result in other painful complications, coma, and even death through kidney failure. According to ASTMH, close to half of the world's population lives in areas at risk of contracting malaria. The map in Figure 15.12 provides a view of how vast the potential area is for malaria infestation. Even noting the shaded light green areas as formerly malarious, these areas could once again be infested with malaria-carrying mosquitoes. As the planet's temperature increases, disease-carrying insects become more pervasive, entering geographical areas where some of these tropical diseases never existed. Read this article about major tropical diseases (https://openstax.org/l/52TropDisease) to learn more.

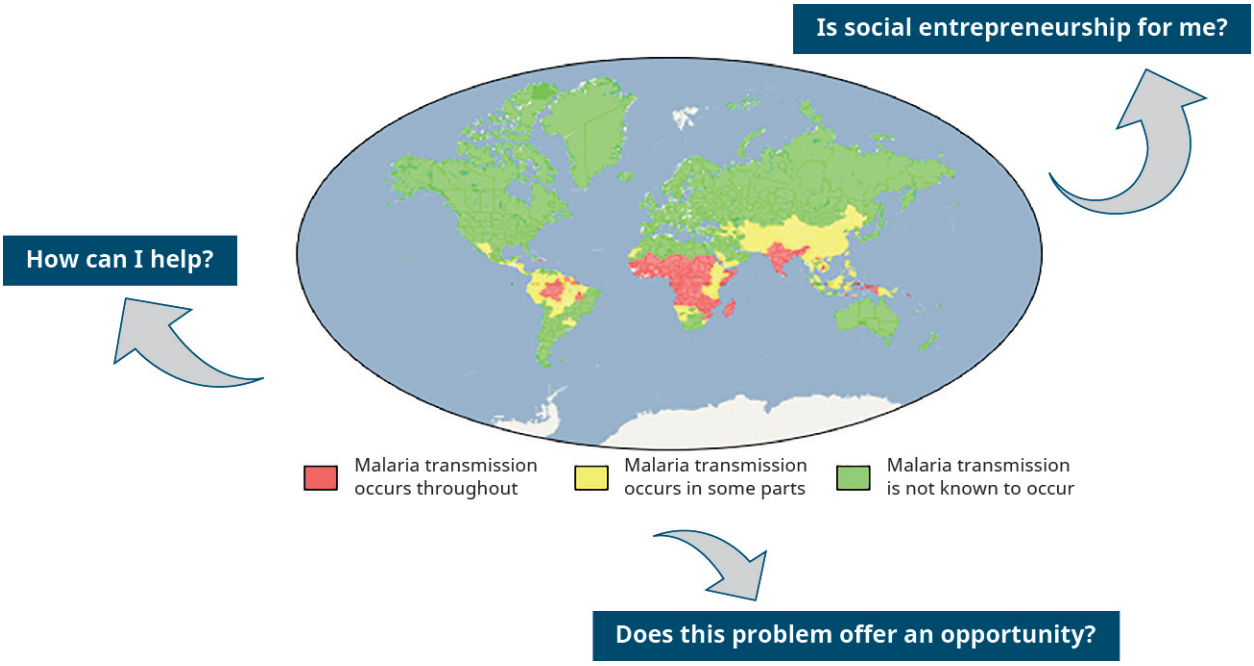


Figure 15.12 What can you do to help solve this global problem? What potential solutions might also be entrepreneurial opportunities?

15.5 Reflections: Documenting the Journey

Learning Objectives

By the end of this section, you will be able to:

- Examine the value of journaling and reflection
- Experiment with reflection as a daily habit

12 American Society of Tropical Medicine and Hygiene. https://www.astmh.org/about-astmh/who-we-are

Figure 15.13 Taking the time to record your thoughts and activities provides new learning opportunities. (credit: "Journaling" by Vic/Flickr, CC B 2.0)

Consider the journey of learning about entrepreneurship and of becoming an entrepreneur. What new knowledge have you gained about the world of entrepreneurship? What have you learned about your own interests in becoming an entrepreneur? Discovering your interest in specific areas helps to inform the possible entrepreneurial opportunities you might want to pursue and informs you of specific processes and actions where you might excel within an entrepreneurial endeavor. Consider how you can add value to an entrepreneurial team as a team member, or in the capacity of a mentor, consultant, or champion, as you reflect on your own interests, goals, passions and desires.

The Power of Journaling

Reflection supports personal growth through identifying actions that worked well and actions that didn't work out as well as hoped. A formal reflection journal for capturing daily thoughts, experiences, lessons learned, and other material, can lead to insights and identify patterns in thinking and in behaviors that may be helpful to recognize—both for personal growth and for growth as an entrepreneur.

In daily life, people seldom have the time or training to be mindful of their actions—to be aware of how they interact with others, or how they act in the variety of situations that fill their days. A daily practice of reflection can improve your ability to be mindful throughout the day and to grow through your documented reflections. Being mindful is the action of being in the moment, being aware of surroundings and fully engaged in awareness of the people around us, hearing their communications and understanding the complexity of their messages. Mindfulness moves us out of our *reaction* to situations from our own personal perspective into a more *objective awareness*—a bit like viewing your life as though you were watching it as a spectator on the sidelines. This change in perspective moves us away from reacting to situations and toward a clearer, unbiased, and focused understanding of the situation with awareness of the situation's nuances. As we develop the practice of mindfulness, we become skilled at being aware of our own emotions and patterns, which can make us aware of more options about how we want to respond: Rather than acting in a habitual or reactive manner, we can consider responses before we react. Reflection is the first step in developing this skill.

Take a few minutes to reflect on your life up to this point. Can you identify milestones, significant decision points, and understand why you made these decisions? Forming a daily habit of writing down your thoughts about the day, challenges you faced and how you responded to each, tracking what went well and what didn't go well is the process of reflection. Over time, you will begin to see patterns in your behaviors. Identifying these patterns or habits provides key insights into how you think, process information, make decisions, and react to decisions. Once you notice these patterns, you have the power to analyze them and decide which are helpful and which are not. The patterns that are not helpful should be removed and replaced with better patterns. You can write down the new patterns that you want to develop as a goal in your daily reflection

journal. You can then identify if you're moving closer to following the new pattern and achieving this goal.

This type of journaling activity might seem like busy work, or you might think that you don't have time for reflection. If this is how you feel, try following this advice for a couple of weeks and then reconsider, or conduct your own research to find articles that discredit reflection. There is a vast body of research that supports reflection as an important part of self-growth and self-realization. Some documented benefits in these studies include learning from mistakes, discovering new insights and ideas, and increases in reported happiness and satisfaction with life and relationships, increased mindfulness, and increased self-understanding resulting in feeling more power to choose how one interacts with the world—feeling empowered rather than the victim of a situation.[13,14,15]

The Impact of Reflection

George Washington University researchers Scheherazade Rehman and James R. Bailey interviewed over 400 executive leaders to understand which of their experiences had the most positive impact on their leadership abilities and pathways. The researchers used data analysis software to process and categorize the highly varied responses, then management professors validated the results. Three themes emerged: surprise, frustration, and failure.[16] Again, these were the experiences that *positively* affected the executives.

The reflections of surprise typically occurred after a major deviation from expectations. The reflections of failure often involved making mistakes that could have been avoided, such as being involved in "organizational politics," instead of focusing on a project's success. The reflections of frustration often involved mismatched priorities or miscommunication within the executives' organizations.[17]

Through the process of reflection, the leaders uncovered deep-seeded issues that became learning experiences for them. The most impactful experiences were negative ones, frequently ones that the executives characterized as mistakes—sometimes their own, sometimes others'. As Rehman and Bailey wrote, "Mistakes provide raw evidence of what we should *not* do in the future. Mistakes allow us to learn by 'negative example', otherwise known as 'errorful learning.'"[18]

For this learning to take place, however, the executives—and anyone seeking to improve—need to understand and process what they've experienced. Reflection is a critical process to gain that understanding.

Documenting Your Journey

As part of your reflection activity, another benefit is to document your journey. If you have identified an opportunity or have started to build your venture, now is the perfect time to keep a journal and document your journey. Each day you face new challenges and exciting ideas that stretch your own learning and growth. Tracking the daily events provides you with a roadmap to use for your next venture, or as a guide to build your knowledge base in moving into a mentor or consultant role. Have you ever asked yourself, why didn't I write that down? We assume that important and insightful ideas will stick in our minds and that we will readily remember them. But in reality we often forget these key insights and ideas. Through journaling, we can record and reflect on our daily activities and key insights.

Rehman and Bailey indicate that a journal should not simply be a collection of facts or a timeline of events. They recommend that whenever you feel a strong emotion at work—such as surprise, frustration, or failure—you should take a moment to add it to your journal. (Keeping the journal in a convenient place or

13 Cable Neuhaus. "The Multimedia Journal: More Than Just a Notebook." *Saturday Evening Post*, *289*(6), 16. December 5, 2017.
14 Deborah L. Starczewski. "Encouraging Students to Think Beyond the Course Material: The Benefits of Using Reflective Journals". *Teaching Professor*, *30*(8), 5. October 2016.
15 J. L. Nelson. Express Yourself. *Scholastic Parent & Child*, *19*(1), 52–54. 2011.
16 James R. Bailey and Scheherazade Rehman. "Don't Underestimate the Power of Self-Reflection." *Harvard Business Review*. March 2022.
17 James R. Bailey and Scheherazade Rehman. "Don't Underestimate the Power of Self-Reflection." *Harvard Business Review*. March 2022.
18 James R. Bailey and Scheherazade Rehman. "Don't Underestimate the Power of Self-Reflection." *Harvard Business Review*. March 2022.

format, such as on your phone or computer, will help.) Document what occurred, how you felt, and, if possible, *why* you felt that way. Set aside time to review your notes, and add to them as needed. Similar to many study techniques, such a detailed and active retrospective process will help you find more insights into cause and effect. Your reflection will have focus, outcomes, and the best possibility of success.

LINK TO LEARNING

This TED Talk on creatives by Adam Grant (https://openstax.org/l/52ThinkersTED) presents some of the concepts of this chapter, framed around Dr. Grant's research as a professor at the Wharton School of Business at the University of Pennsylvania, on creatives. His book, *Originals: How Non-Conformists Move the World*, shares more of his findings.

Are there biases and habits that hold you back from being a creative, as defined in this chapter and by Dr. Grant? If so, what methods can you use to break through these biases and habits?

Key Terms

burn rate rate at which cash outflow exceeds cash inflow
buyback clause legal agreement regarding an exit by a founding team member prior to the harvesting of the venture
code of conduct formal statement that provides guidance on how ethical conduct is demonstrated
company culture shared beliefs, values and assumptions held by people regarding how to behave or conduct themselves within the context of fitting into an organization
Delphi method group decision-making process that includes a diverse group of people who are located at different locations and willing to respond to a series of questionnaires to assist in providing ideas, information or solutions to a defined question or problem
escalation of commitment tendency to continue with a predetermined action based on the past efforts and contributions to the project rather than an analysis of the current realities that disclose a new solution or approach is necessary
fail-safe point identified point that triggers the entrepreneur to consider what actions are needed to bring the venture back to a healthy position and whether this action is reasonable and feasible
founders' agreement written document that addresses contractual topics such as division of equity, compensation, contributions to the venture, and commitments to the venture with timelines included
Gannt chart bar chart used to organize and plan sequential steps in a process
hindsight bias belief that, in retrospect, the outcome was predictable when the outcome wasn't predictable due to various uncontrollable factors
hubris overinflated belief in oneself
lifestyle business business that provides incomes similar to other forms of employment
Nominal Group technique group decision-making process that requests multiple rounds of responses and discussions of response
noncompete agreement formal agreement that the person signing the document will not work for another organization that is a direct competitor of their current employer during employment and usually for a specified length of time after employment ends
nondisclosure agreement formal agreement that the person signing the document will not sharing proprietary information with outside sources
planning fallacy creation of a plan that is too optimistic and not aligned with conservative assumptions
serial entrepreneur entrepreneur who becomes involved in starting multiple entrepreneurial ventures
social capital goodwill that is created through helping someone else
status quo bias pattern of relying on previous actions and results as the accepted pattern and outcome with a bias against change or new information or new results

Summary

15.1 Launching Your Venture

Before launching a venture, the entrepreneurial team should ensure its members agree on the vision and then develop a founder's agreement. The company culture should be defined, and a code of conduct developed. The team should identify all operational tasks needed to launch the venture and their associated time requirements and dependencies. Staying openminded and flexible at launch can help support the venture's success.

15.2 Making Difficult Business Decisions in Response to Challenges

Some of the same characteristics that make entrepreneurs successful (such as confidence and optimism) can sabotage success. Entrepreneurs should be aware of potential biases or thinking patterns that obfuscate the current reality of the venture so they are able to recognize key problem indicators and put solutions in place. Some of the more difficult decisions an entrepreneur makes are difficult because of the emotional connection

to previous decisions or decisions that affect other people involved in the venture. Early agreement that the success of the venture is the primary focus can help to work through these difficult decisions.

15.3 Seeking Help or Support

Entrepreneurs should recognize the wisdom in seeking help and support as they plan, launch, and grow their ventures. Sources of advice include the entrepreneur's own network, the connections of the start-up team, and angel investors and their resources. Tools to assist in decision making include the Delphi method and the Nominal Group technique.

15.4 Now What? Serving as a Mentor, Consultant, or Champion

Once you become an entrepreneur, you can consider giving back to the entrepreneurial community by becoming a mentor, consultant, or champion to support other people in their ventures.

15.5 Reflections: Documenting the Journey

Reflection and journaling are useful tools for entrepreneurial growth. These practices can help you to identify patterns that act as obstacles, to brainstorm solutions, to set goals, and to document ideas that may lead to your next venture.

Review Questions

1. A nondisclosure agreement protects the venture by _____.
   A. outlining confidential information or knowledge that the parties do not want to share with outside, or third, parties and is considered a legally binding contract
   B. sharing information that is not confidential
   C. identifying key people who can access confidential information
   D. identifying disclosed information for outsider use

2. Which of the following documents should be discussed and agreed upon prior to the start of the venture?
   A. nondisclosure and noncompete agreements
   B. nondisclosure and founder's agreements
   C. founder's agreement and a code of conduct
   D. founder's, nondisclosure, noncompete agreements, and code of conduct

3. The founder's agreement includes which of the following content items?
   A. non-disclosure clause
   B. personnel plan
   C. buyback clause
   D. marketing plan

4. According to some research on entrepreneurs, what is/are the most significant bias(es)?
   A. small numbers allow for niche markets
   B. entrepreneurs prefer taking action rather than planning
   C. entrepreneurs tend to be over confident and optimistic
   D. entrepreneurs fall for the planning fallacy

5. The law of small numbers refers to:
   A. an inability to attract a large target market
   B. a target market that is too small to lead to success
   C. a target market that aligns with key stakeholders
   D. both a and b

6. Why is it important to keep track of your assumptions?
   A. Knowing the assumptions provides background information related to the projected outcomes or numerical projections.
   B. Knowing the assumptions provides an opportunity support your biases.
   C. Assumptions are never accurate and are therefore discredited.
   D. Assumptions constantly change and therefore do not need to be tracked.

7. The Nominal Group technique _____.
   A. is only used in complex decisions
   B. has multiple uses for gaining feedback from participants
   C. can be used with only one participant
   D. restricts participant participation

8. The Delphi technique _____.
   A. requires participants to be in one location
   B. requires participants to come prepared to the activity by researching the problem
   C. requires time and commitment
   D. requires collaboration in answering the questionnaire

9. Acting as a mentor provides _____.
   A. expert assistance to the venture startup team and self-growth for the mentor
   B. opportunities to diminish relationships
   C. the mentor with professional development
   D. the mentee with peer recognition

10. A serial entrepreneur is someone who _____.
   A. wants to retire
   B. creates a pattern of starting multiple ventures
   C. plans for a low stress future
   D. plans to start the first venture

11. Benefits of a reflection journal include which of the following?
   A. identifying patterns, biases, habits and discovering new insights
   B. assigning new work responsibilities
   C. identifying wasted time
   D. avoid reviewing decisions that can’t be changed

12. Reflection journal is similar to _____.
   A. a post mortem
   B. a time log of your activities
   C. a scrapbook of pictures
   D. a record of assumptions

13. According to Dr. Grant, creatives are people who _____.
   A. are procrastinators
   B. act on multiple ideas
   C. plan out each detail
   D. are highly confident with no doubts about their success

Discussion Questions

1. Why should the entrepreneurial team begin with the end in mind?
2. How can a Gantt chart help in the preparation for starting the new venture?
3. Why would an angel investor stress to the startup team the importance of not getting too attached to the venture?
4. Should employees who are not part of the startup team receive an equity position in the venture? What are the benefits and drawbacks that inform this decision?
5. What biases might an entrepreneur encounter in starting the venture?
6. What actions can the entrepreneur take to avoid these biases?
7. What can be done to avoid personnel problems that occur after the venture has opened?
8. How can brainstorming and creating a mindmap improve problem recognition and follow through actions?
9. What are three methods you could use to find support for your new venture?
10. Why is it important to analyze and discuss decisions?
11. Why is it important to feel comfortable with a decision?
12. What are the benefits in becoming a mentor, consultant or champion?
13. What are the risks or drawbacks in becoming a mentor, consultant or champion?
14. How does a philanthropic desire align with entrepreneurship?
15. According to Rehman and Bailey, in which key moments is it highly important to reflect and journal?
16. What can you do to role model behavior that reflects your learning of the material in this chapter?

Case Questions

1. Review the information on YouTube in this section of the chapter and conduct your own research. What evidence is there that beginning with the end in mind was part of YouTube's founders original plan?
2. Review the LuminAid story. Why did Sreshta and Stork focus on light as their business idea instead of a focus on other areas needed by survivors of a natural disaster?
3. Refer to Stacy Madison's food cart story. What was the most important insight you gained from reading about Stacy's food cart business?
4. Everlane started as an online clothing store focused on ethical business practices. Part of their commitment to ethical practices includes regular visits to their factories to ensure people receive fair wages and work reasonable hours, addressing environmental concerns, and being transparent in decisions and transactions, such as disclosing the cost to produce an article of clothing. With $100 million in revenue in 2016 and over 44,000 people on the waiting list for a new line of denim available this September 2018, Everlane is shaking up the fashion industry. If your new venture faced this type of competition, what actions would you take? Consider if you would adopt this same transparency strategy, become more involved in the supply chain to determine how clothing factory workers were treated at your offshore factories owned by other entities, increase brand name marketing to support the profit markup on your clothing, or some other action? What process would you use to make these decisions?

Suggested Resources

15.1 Launching Your Venture

R. Nanda, L. Kind, K. Laws, & J. Lum. "Case Study: Is a Start-up's Strength Becoming Its Weakness?" *Harvard Business Review* 93, no. 11 (2015): 145.

Ablebit's instructions for making a Gantt chart in Microsoft Excel: https://www.ablebits.com/office-addins-blog/2014/05/23/make-gantt-chart-excel/

Smartsheet's step-by-step instructions for making a Gantt chart in Microsoft Excel: https://www.smartsheet.com/blog/gantt-chart-excel

Project Manager's Ultimate Guide to Gantt Charts: https://www.projectmanager.com/gantt-chart

The Startup Checklist by David Rose, founder of NY Angels and GUST.com

Shortcut: How Analogies Reveal Connections, Spark Innovation, and Sell Our Greatest Ideas by John Pollock discusses using analogies to think about unmet needs and innovative solutions.

15.2 Making Difficult Business Decisions in Response to Challenges

"How Fast Can Your Company Afford to Grow?" *Harvard Business Review*, 1998. Classic article serves as a good reference on cash flow and self-financed growth, covering key levers to help manage profitable growth without having to go "hat in hand" to investors again.

The Undoing Project by Michael Lewis provides a good reference on biases through the story of psychologists Amos Tversky and Daniel Kahneman.

"3 Steps to Determine Product-Market Fit", *Entrepreneur Magazine*, August 2014. Good reference on product-market fit.

What Customers Want, by Ullrich, discusses "Jobs to be Done" theory created by Clayton Christensen and practice by Strategyn.

https://www.npr.org/podcasts/510313/how-i-built-this

15.3 Seeking Help or Support

Service Corps of Retired Executives (SCORE): https://www.score.org/

Small Business Administration: https://www.sba.gov/

Y Combinator: http://www.ycombinator.com/

Techstars: www.techstars.org

G. Klein. *The Power of Intuition: How to Use Your Gut Feelings to Make Better Decisions at Work*. (New York: Doubleday, 2004)

15.4 Now What? Serving as a Mentor, Consultant, or Champion

The Case Foundation: https://casefoundation.org/

Startup Champions Network: http://www.championsnetwork.co/

15.5 Reflections: Documenting the Journey

F. T. Evers. Journaling: A Path to Our Innermost Self. *Interbeing*, 2, no.2 (2008): 53–56.

D. Ciampa. The More Senior Your Job Title, the More You Need to Keep a Journal. *Harvard Business Review Digital Articles* (2017): 2–4.

Worklife TED-sponsored podcasts: https://itunes.apple.com/us/podcast/worklife-with-adam-grant/id1346314086?mt=2

NPR podcast “How I Built This” founder/CEO podcasts: https://www.npr.org/podcasts/510313/how-i-built-this

A Suggested Resources

These suggested resources can help you review and refine your entrepreneurial plans.

Entrepreneurial and Small Business Support (General)

Small Business Administration (SBA): www.sba.gov

Small Business Administration site of local organizations that might assist you in launching or managing a venture: https://www.sba.gov/tools/local-assistance

Service Corps of Retired Executives (SCORE): https://www.score.org/

Small Business Development Center (SBDC): https://www.sba.gov/offices/headquarters/osbdc/resources

International Franchise Association: https://www.franchise.org/

US government contracts: https://www.sba.gov/federal-contracting/contracting-guide/basic-requirements

US Department of Commerce: https://www.commerce.gov/

US Department of Commerce, Bureau of Economic Analysis: https://www.bea.gov/

US Department of Labor: https://www.dol.gov/

US Department of Labor, Bureau of Labor Statistics: https://www.bls.gov/bls/blswage.htm

US Chamber of Commerce: https://www.uschamber.com/

Global Entrepreneurship Monitor: http://www.gemconsortium.org/

Entrepreneurial and Small Business Support (Specific Groups)

Women's Business Center (WBC): https://www.sba.gov/local-assistance/find/?type=Women%27s%20Business%20Center&pageNumber=1

Veterans Business Outreach Center (VBOC): https://veteransoutreachcenter.org/

National Association of Women Business Owners: https://www.nawbo.org/resources/women-business-owner-statistics

Asian American Chamber of Commerce: http://www.asian-americanchamber.org/

Black Chamber of Commerce: https://www.nationalbcc.org/

Hispanic Chamber of Commerce: https://ushcc.com/

Ladies Who Launch: https://www.ladieswholaunch.org/

Minority Business Development Agency: https://www.mbda.gov/

National Association of Professional Women: http://womenforhire.com/company/national-association-of-professional-women-napw/

The Female Entrepreneur Association: https://femaleentrepreneurassociation.com/

Women's Business Enterprise National Council: https://www.wbenc.org/

Vision Statement, Mission Statement, and Goal Setting

Website with ideas for developing your vision: https://www.executestrategy.net/blog/write-good-vision-statement

Video with walkthrough for crafting your mission statement: https://www.entrepreneur.com/article/65230

Eleven Free Goal Setting Software and Tools You Can Use: http://www.goal-setting-college.com/goal-setting-software/11-goal-setting-software-tools-you-can-use-for-free/

YouTube: Achieve More by Setting Smart Goals: https://www.youtube.com/watch?v=yA53yhiOe04

Business Models and Business Plans

SBA Business Plan resources: https://www.sba.gov/business-guide/plan-your-business/write-your-business-plan

Business Model Canvas: https://strategyzer.com/canvas/business-model-canvas

Business model canvas and resources: Strategyzer.com

Lean canvas and associated resources: Leanstack.com

Social business model canvas and related resources: Socialbusinessmodelcanvas.com

YouTube Video: Business Model Canvas Explained: https://www.youtube.com/watch?v=QoAOzMTLP5s

The Four Lenses Strategy Framework website: www.4lenses.org

List of Social Enterprise Business Models or Frameworks: http://www.thesedge.org/socent-spotlights/22-awesome-social-enterprise-business-ideas

YouTube Video: We have a dream, B-corp overview and mission: https://www.youtube.com/watch?time_continue=3&v=V-VFZUFJwt4

Sample business plans-www.bizplans.com: www.bplans.com

Funding, Finances, and Accounting

Small Business Administration (SBA) lending program: https://www.sba.gov/funding-programs/loans

Small Business Administration (SBA) calculation of startup costs: https://www.sba.gov/business-guide/plan-your-business/calculate-your-startup-costs#section-header-6

Small Business Administration, “How to Start a Non-Profit”: https://www.sba.gov/blogs/how-start-non-profit

US Department of Labor: https://www.dol.gov/general/topic/statistics/wagesearnings

Tax information for charitable organizations from the Internal Revenue Service: https://www.irs.gov/charities-non-profits/charitable-organizations

Grant information by state: https://www.grants.gov/

Information from the National Institutes of Health on grants and the application process: https://grants.nih.gov/grants/about_grants.htm

G-Startup Worldwide’s global startup competition: https://www.f6s.com/g-startupworldwide/

Extending Credit to Your Customers: https://fitsmallbusiness.com/invoicing-extending-credit-to-customers/

7 Ways to Bootstrap Your Business to Success: https://www.entrepreneur.com/article/254217

Small Business Administration Introduction to Accounting Course: https://www.sba.gov/tools/learning-center-view-course/364071

Khan Academy Accounting and Financial Statements Course: https://www.khanacademy.org/economics-finance-domain/core-finance/accounting-and-financial-stateme

U.S. Securities and Exchange Commission: https://www.sec.gov/reportspubs/investor-publications/

investorpubsbegfinstmtguidehtm.html

US Securities and Exchange Commission Regulatory Actions: https://www.sec.gov/rules.shtml

SEC Information on crowdfunding portals: https://www.sec.gov/divisions/marketreg/tmcompliance/fpregistrationguide.htm

Link to SEC (FINRA) crowdfunding portals: https://www.finra.org/about/funding-portals-we-regulate

Money and Interest Rates: https://www.federalreserve.gov/data.htm

Y Combinator: http://www.ycombinator.com/

Techstars: www.techstars.org

Kickstarter: www.kickstarter.com

Indiegogo, "The Essential Guide to Crowdfunding": https://learn.indiegogo.com/the-essential-guide-to-crowdfunding/

Startupfest, "The $100K Investment Prize": http://www.startupfestival.com/news/100k-investment-prize/

Circleup: http://circleup.com

Exilend: https://www.exilend.com

Fundable: http://fundable.com

LendingKarma: http://www.lendingkarma.com

LoanBack: http://loanback.com

Trade Show News Network: http://www.tsnn.com

ZimpleMoney: http://www.zimplemoney.com

Legal Issues in Entrepreneurship

SBREFA Small Business Resource Center's site on legal requirements and regulatory compliance: https://www.dol.gov/agencies/oasam/business-operations-center/osdbu/compliance-assistance

U.S. Patent and Trademark Office: https://www.uspto.gov/

Nondisclosure (NDA) templates: https://www.rocketlawyer.com/

US Small Business Administration on licenses and permits: https://www.sba.gov/business-guide/launch-your-business/apply-licenses-permits

Internal Revenue Service (IRS) information on taxation in partnerships: https://www.irs.gov/businesses/small-businesses-self-employed/partnerships

Information on variation between all 50 states in forming or incorporating a business from Cornell Law School: https://www.law.cornell.edu/wex/corporations

US Copyright Office: https://www.copyright.gov/help/faq/faq-protect.html

Federal Communications Commission on cybersecurity for small businesses: https://www.fcc.gov/general/cybersecurity-small-business

North Carolina State University Poole College of Management's risk management initiative: https://erm.ncsu.edu/library/article/coso-erm-framework

US Copyright Office: https://www.copyright.gov/

Marketing

Small Business Administration information on marketing and sales: https://www.sba.gov/business-guide/manage-your-business/marketing-sales

American Marketing Association (AMA): https://www.ama.org

American Marketing Association (AMA) digital marketing certification: https://www.ama.org/events-training/Certification/Pages/digital-marketing-certification.aspx

American Marketing Association (AMA) on-demand course: Digital Marketing: Delivering a Custom Experience: https://www.ama.org/events-training/virtual-events/Pages/digital-marketing-virtual-conference-051717.aspx

Google Ads: https://ads.google.com/home/

Pitching

Harvard Business Review's how to craft a corporate narrative: https://hbr.org/2016/03/how-to-build-a-strategic-narrative

Pitch deck templates: https://articles.bplans.com/what-to-include-in-your-pitch-deck/ and https://www.forbes.com/sites/allbusiness/2017/03/04/how-to-create-a-great-investor-pitch-deck-for-startups-seeking-financing/#630406bc2003 and https://www.startupgrind.com/blog/the-quick-and-dirty-guide-to-creating-a-winning-pitch-deck/

Operational Resources

Society for Human Resource Management: https://www.shrm.org

Scheduling programs and templates: https://getsling.com/blog/category/scheduling/, https://wheniwork.com/features, and https://schedulebuilder.org/

Employer hiring costs of employee: https://gusto.com/tools/employer-tax-calculator

Payroll program: https://onpay.com/payroll-calculator-tax-rates

Smartsheet's step-by-step instructions for making a Gantt chart in Microsoft Excel: https://www.smartsheet.com/blog/gantt-chart-excel

Project Manager's ultimate guide to Gantt charts: https://www.projectmanager.com/gantt-chart

FindLaw Small Business Center (business forms): https://smallbusiness.findlaw.com/

Research Sources for Demographic and Marketing Data

Small Business Administration (SBA) guide on researching your market: https://www.sba.gov/business-guide/plan-your-business/market-research-competitive-analysis#section-header-5

American Fact Finder (market research): http://factfinder2.census.gov/main.html

FedStats (statistics from more than 100 federal agencies): www.fedstats.gov

National Federation of Independent Business: https://www.nfib.com/business-resources

The Small Business National Center: https://sites.google.com/a/uca.edu/sbanc/home

Bureau of Labor Statistics: https://www.bls.gov/bls/demographics.htm

North American Industry Classification System: https://www.census.gov/eos/www/naics/

Statistical Abstract of the United States: https://www.census.gov/library/publications/2011/compendia/statab/131ed.html

US Census Bureau site on where to locate your business: https://cbb.census.gov/sbe/#

Consumer credit data: https://www.federalreserve.gov/releases/G19/

Consumer product safety: https://www.cpsc.gov/

Consumer price index: https://www.bls.gov/cpi/

Bureau of Economic Analysis: https://www.bea.gov/

Employment Statistics: https://stats.bls.gov/bls/employment.htm

Income Statistics: https://www.bls.gov/cps/earnings.htm

American Customer Satisfaction Index: https://www.theacsi.org/

North American Industry Classification System: https://www.census.gov/eos/www/naics/

US Census Bureau: https://www.census.gov/

Tools for Creativity and Problem Solving

Twenty-four essential mindmapping and brainstorming tools: http://mashable.com/2013/09/25/mind-mapping-tools/#jP47h7Q818qM

Open Innovation Community: http://openinnovation.net/

Ideation techniques: http://www.innovationmanagement.se/2013/05/30/the-7-all-time-greatest-ideation-techniques/ and https://www.ideou.com/pages/ideation-method-mash-up and http://www.designkit.org/methods/15

LUMA Institute's LUMA System of Innovation: https://www.youtube.com/watch?v=qDyElJ0xe2o

Analyze your problem-solving abilities: https://www.mindtools.com

IDEO Design Kit: http://www.designkit.org/resources/1.

Design Thinking Mix Tapes from Stanford's Design School: https://dschool.stanford.edu/resources/chart-a-new-course-put-design-thinking-to-work.

Lean Startup and Pivoting

Lean startup: http://theleanstartup.com/#principles

Toyota's Way: https://vimeo.com/44328452

14 Management Principles of Toyota: http://www.panview.nl/en/lean-production/toyota-way-j-liker-summary

Tim Berry's Lean Business Planning Guide: https://leanplan.com/

Lean canvas and associated resources: Leanstack.com

The International Business Model Competition that focuses on lean startup models, sponsored by BYU and Harvard: http://www.businessmodelcompetition.com/

Networking and Trade Organizations

LinkedIn: www.linkedin.com

Association of Chamber of Commerce Executives: acce.org

BNI: Business Network International: https://www.bni.com

HUBZone: https://www.sba.gov/offices/headquarters/ohp

Tradeshows: http://www.tsnn.com/

Industry research publications: http://www.newslink.org

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