CHAPTER 1 A Framework for Entrepreneurship

"Twenty years ago students who dared to say they wanted to start their own companies would be sent for counseling. Today entrepreneurship is the fastest-growing course of study on campuses nationwide."
—Jerome Katz, professor of management, St. Louis University

OUTLINE

LEARNING OBJECTIVES

After reading this chapter, you will understand

- how entrepreneurship may affect *your future*, whether you're an employee, a venture creator, or a consumer.
- how to define *entrepreneurship*.
- that entrepreneurship is a *worldwide phenomenon*.
- how the concept of a *new entrepreneur* has emerged.
- that entrepreneurship is a *multidimensional concept.*
- the *paradoxes* of entrepreneurship.

PERSONAL PROFILE 1

Entrepreneurship with a Purpose

She was well on her way to the top of the corporate game—a senior vice president for a high-tech firm with a successful 14-year career including stints at 3Com (formerly U.S. Robotics) and IBM.

But Cheryl Mayberry McKissack wasn't happy; in fact, she was stressed out. McKissack realized that what she really wanted was a job in Chicago with flexible hours that would also give her an opportunity to work with other African-American women. "It was clear to me that it would be difficult, if not impossible, to craft the perfect job, unless I did it myself," McKissack says. "I really wanted to use my technological expertise, but in a different way than I had before. And I wanted it to have a community element that I hadn't had the opportunity to pursue."

McKissack came up with not one, but two interrelated entrepreneurial solutions. Both of them take their names from *nia*, the Swahili word for "purpose." In 2000, McKissack founded Nia Enterprises, a market research and services firm that uses Web-based tools to provide online consumer research, delivering insights into the buying habits and consumer preferences of the U.S. ethnic group with the largest buying power: African-American women and their families. The firm's corporate clients include General Motors, Sears, Disney, American Airlines, Revlon, and State Farm Insurance.

That same year McKissack and Bonita K. Coleman, an automotive marketing and brand executive, also created an online community for African-American women with a Web site called NiaOnline™. They structured the site to become the premier Internet destination for African-American women by offering articles on women's health, careers, fashion, relationships, travel, and entertainment topics, with a special focus for their target audience. In addition, the site featured columns with "empowering advice" from other African-American women. The site claims to reach an online community of more than 100,000 black household members.

More important, NiaOnline is the vehicle for much of Nia Enterprises' market data collection. Web site users can "opt-in" to sample and evaluate products provided by manufacturers. They can voice their opinions through simple quick-response surveys. Or they can register for the Consumer Advisory Panel, where they agree to take surveys or participate in online focus groups, and are then rewarded with points that can be redeemed for merchandise, such as photo albums or briefcases.

McKissack, who received an MBA from Northwestern's J. L. Kellogg School of Management, got some help for starting her ventures from Springboard Enterprises, a national not-for-profit that educates, showcases, and supports women entrepreneurs trying to start high-growth potential enterprises. One of Springboard's most effective programs has been their Women's Venture Capital Forum, which gives fledgling women entrepreneurs access to sources of equity funding while providing an environment where they can refine their business strategy. McKissack was one of the 25 women selected for the first Springboard Forum in January 2000 at the Kellogg School. Since that time more than 350 women entrepreneurs have presented at more than 15 additional forums across the country, where they have raised over $3 billion for their ventures.

While McKissack notes that minorities are "frequently left out of the networks that provide the best advancement opportunities," she has obviously bridged the gap in her own career. Her marketing firm and Web site have helped her to reach her personal goal while she achieves her purpose of helping other African-American women. In addition to starting these businesses, McKissack has co-written three “Nia guide” books on careers, balance, and health, and serves on several corporate boards. She also shares what she has learned with aspiring entrepreneurs by teaching at the Kellogg School of Business at Northwestern University in Chicago.

SOURCE: Adapted in part from Louise Witt. “What’s the Right Time to Become an Entrepreneur?” *Fortune Small Business,*, 2005. Retrieved from the Web February 1, 2005. ~~http://www.fortune.com~~. Also, Cheryl Mayberry McKissack, “Practice: Funding and Hiring for Women and Minorities: The Challenges of Access and Inclusion,” *Kellogg World Alumni* magazine, Winter 2004. Retrieved from the Web May 8, 2006. ~~http://www.kellogg.northwestern.edu~~.

ENTREPRENEURSHIP AND THE FUTURE

IN the new millennium, the ideas, talents, skills, and knowledge that promote entrepreneurship are evident in people all around the globe, but especially in today’s generation. This new direction is a change from previous times when the forces for economic growth tended to favor more established businesspersons from the corporate world. But the face of the world economy has shifted, and young people today are well suited for entrepreneurial activity. For instance:

- The aspiring entrepreneurs of today are technologically precocious. They are comfortable with new technologies and are not fearful of change and the radical shifts that new technology can bring. Younger people are at home with computers and all sorts of consumer electronics. Over 80 percent of homes with children have computers and access to the Internet. A Carnegie Mellon study found that children and young adults are the authority on computer technology in the home.[1] Adults take a back seat to the kids. Even beyond their technical competency, young people are immersed in technology and have internalized its power.
- “It’s a great time to be an entrepreneur,” especially an Internet one. Compared to ten to fifteen years ago, hardware is 100 times cheaper, infrastructure software is free, there is easy access to global labor markets, and SEM (search engine marketing) has changed distribution and selling tactics.[2]
- This generation is passionate, inquisitive, and challenging. They welcome change and embrace the idea of progress. They have seen the improvement of information technology, new medical and biotech processes and products, and radical changes in the way people communicate and work. They believe that continued improvement and even revolutionary change await them in the future.
- They think differently. As *Fast Company* puts it, “Forget the experience curve. The most powerful force in business today is the inexperience curve. Young companies, born on the right side of the digital divide, are running circles around their older, richer, and slower rivals. If one wants his or her company to think outside the box, why not learn by working with people who don’t know there is a box?”[3] For example, Youtube.com began business without “knowing” it was a business. The founders created a Web site for videos, which developed into a business. Recently, the founders sold their interests for well over $1 billion.
- They are independent. More and more people starting out in professional business careers consider themselves free agents. They have portable skills and will take them

wherever they can do the most good or make the most money. These workers are international free agents and show little loyalty to companies that continue to make strategic mistakes or fall behind the market.

How Does the New Entrepreneurship Add Up?

The sum of these trends is more entrepreneurship and business start-ups for younger people. Many new ventures will be technology based. The traditional career path may become a rarity.[4]

Today's younger people are more entrepreneurial than those of any previous generation. More and more people are striking out on their own. According to the Opinion Research Council, 54 percent of 18- to 24-year-olds are highly interested in starting a business, compared with 36 percent of 35- to 64-year-olds.[5] A US News survey found that "entrepreneur" was the preferred career of Generation X.[6] A Newsweek poll asked "millenials" (people who have come of age within a few years of the millennium) to name their hero, and more than half named Bill Gates, the founder of Microsoft.[7]

In fact, most teenagers entering college know more about business than their parents ever did. Many more teenagers work today than their parents did at their age. According to the Bureau of Labor Statistics, more than half the teens in the United States have jobs and over 90 percent have summer jobs.[8] Many high school students belong to investment clubs and Junior Achievement and help raise money for charities through a variety of businesslike activities. Ever buy a Girl Scout cookie? Harvard University recently struck down a long-standing ban on operating businesses out of dorm rooms because they feared losing student entrepreneurs to Stanford or Columbia. *Vanity Fair* magazine has coined a new word—"enfantrepreneurs."[9]

Today's students and their peers (entrepreneurs or enfantrepreneurs) will take us into the future. It is only a matter of time before their entrepreneurial activity brings the innovations that will shape the new millennium. The spirit of entrepreneurship—the notion of human progress, development, achievement, and change—motivates and energizes people.

Innovations in the way we work and play, travel and eat, start our families, and raise our children all create opportunities for entrepreneurs to build businesses and organizations that will exploit new technology and trends. We can also say that entrepreneurship is a self-perpetuating phenomenon: If a society has it, more is likely to come. For example, Hong Kong is often cited as an example of a very entrepreneurial place. Even after the handover of Hong Kong to the mainland Chinese in 1997, it has remained entrepreneurial. However, most of western and central Europe has not been entrepreneurial throughout history and many years of government programs designed to correct this have not proved effective. In the United States, we have vast and growing entrepreneurial resources, as demonstrated by the tremendous increase in supply and demand for entrepreneurship classes and programs on campus.

An estimated 2,000 two- and four-year colleges now have entrepreneurship courses or programs. Universities and business schools have discovered that the entrepreneurship program has enormous potential for raising the school's profile and visibility, promoting economic activity and job creation, serving highly motivated students (who may be wealthy alumni one day), and engaging already rich and successful alumni.

Look at Mark Cuban, for example. He is the billionaire owner of the Dallas Mavericks basketball team and co-owns HDNet (high definition TV). He took his first entrepreneurship class at Indiana University's Kelley School of Business and says it was one of the best classes he ever took. "It really motivated me. There is much more to starting a business than just understanding finance, accounting and marketing. Teaching kids what has worked with startup companies and learning about experiences that others have had could really make a difference. I know it did for me."[10]

Michael Guerrieri would agree. He is a recent graduate of the University of Chicago Graduate School of Business. Guerrieri went back to school to change careers. He credits his MBA experience with giving him the confidence to start his own business, the quantitative skills needed for advanced analysis, and the network of people who gave him advice. He has two ventures in progress: a private label health food snack line, and a medical services business that will automate refilling prescriptions. "It is one thing to dream and another to execute it," he says.[11]

Of course, not every entrepreneur is made in the classroom. Some believe entrepreneurs are born with special personalities and characteristics that distinguish them from ordinary folks. Many feel that entrepreneurship cannot be taught at all, or that successful entrepreneurship is a function of luck or congenital "smarts." "I don't think in a million years you can teach it in the classroom," said Paul Fleming, founder of P. F. Chang's China Bistro.[12] But the fact is that students who take entrepreneurship classes have more successful business start-ups than those who don't. They also make fewer business mistakes and earn higher annual incomes. Moreover, the business and social networks that schools create and sustain to put students and entrepreneur-alumni together help the nascent entrepreneurs make connections. And school is a safe place to learn: Missteps in a classroom setting can cause a little embarrassment and affect one's grade, but they will not likely result in years of hard work, money, and loss of personal reputation.[13]

A former best-selling book, *Workplace 2000*, argued that entrepreneurship not only affects our lives through innovation but also represents the working future for many of us.[14] As large corporations continue to lay off middle managers to realize their goals of flatter, more responsive organizations, these middle managers must "go"—and the place they will go is into business for themselves. What will they do? They will fill the niches and markets of servicing their former employers—providing consulting, aftermarket service, and other support functions. These former middle managers will operate small entrepreneurial firms that provide high quality and value to their customers in a way that working inside the bureaucracy of a large corporation makes impossible.

There are other entrepreneurial alternatives as well. In a business environment where large corporations try to stay flat, lean, and responsive, a burst of growth is occurring in "micro-business" firms—firms with four or fewer employees. Some of these will be started by former middle managers and executives who have been let go. Some are started by current managers trying to beat the clock to the next wave of layoffs. Many are created by people who have never and will never work for *Fortune* 1000 companies. In addition to micro businesses, there are more corporate-backed ventures: spin-offs, joint ventures, intrapreneurial (corporate-based new ventures) units, and partnering arrangements. Although these types of ventures originate in larger organizations, they are being formed now specifically to stay small and entrepreneurial, to avoid bureaucracy, and to maintain their innovative edge.

Older people are also participating in a great wave of entrepreneurship. These people are the "silver entrepreneurs." Many corporate middle managers have left the ranks of the white collared to join the self-employed (voluntarily and through redundancy). Some are previously retired. A recent *Business Week Online* special report called "Second Acts" described the action. Tom Washburn was a researcher for a financial services company. After a year of study, he opened his own ice cream shop, which he named Moxley's after the family dog. Today he has three Baltimore locations and an award-winning ice cream brand. "My dream came true," he says. Amy Hilliard left a 20-year career as a marketing executive focused on consumer brands. She took a big risk as a single mother of two (she also has a Harvard MBA) to invest $300,000 in a cake-baking business. (Have a look at her business at http://www.comfortcake.com.) Hilliard concludes, "I didn't realize how hard it would be. Food is a very complex business. But it is gratifying to create something from scratch. It is never boring. Every day is something new, and I'm using all of my cylinders at once."[15]

Not all older entrepreneurs are constrained by technology and to entering the food and beverage industry. Many have discovered eBay, and they dig long and deep for treasure to be sold online. Selling on eBay helps these silver entrepreneurs earn extra cash and clean out their closets too. Marcia Cooper and Harvey Levine started an eBay selling business as 60-somethings. It was a low entry barrier situation because all they needed was a computer and an Internet connection. They went through the eBay training program and decided to specialize in event tickets. Then they expanded to sell just about anything, indiscriminately. Now they focus on quality items that yield a minimum of $100 in commissions.[16]

We really do not need to be a futurist, however, to see that entrepreneurship plays a large and increasing role in the future of our nation's and our individual working lives. The nature of organizations, work, and employment has changed, and individuals who recognize these changes and prepare for them will be best able to succeed in the new environment. Therefore, most people will encounter entrepreneurship through the marketplace, in new products, services, or technologies, or through their own employment. The better they understand the marketplace, the better they will be able to survive and thrive in the new entrepreneurial environment. Entrepreneurship is and will remain a normal, regularly occurring opportunity in everyone's professional career.

Before beginning our journey through the entrepreneurial adventure, let's listen closely to someone who has already been through the process—more than once. Steve Jobs gave a commencement address to Stanford University's graduates in the spring of 2005, and Street Story 1.1 summarizes his words and thoughts.

WHAT IS ENTREPRENEURSHIP?

There have been almost as many definitions of entrepreneurship as there have been writers on the subject. Translated from the French, entrepreneur literally means "one who undertakes." An entrepreneur is a doer. But what does this mean with respect to the businessperson? Some suggest that trying to define entrepreneurship may be fruitless because the term is too vague and imprecise to be useful.[17] Table 1.1 provides a short selection of definitions that have been offered.

STREET STORY 1.1

Lessons for the Hungry and Foolish

Steve Jobs, CEO of Apple Computer and astated at the time, Jobs now calls this “the
Pixar Animation Studios, began his com- best thing that could ever have happened to
mencement address at Stanford University by me” because it “freed me to enter one of the
admitting he was a college dropout. most creative periods of my life.” Within
five

Jobs not only confessed that he dropped years Jobs started both the NeXT company
out of Reed College after just six months, but and Pixar Animation Studios. Apple pur-
added that he doesn’t regret it. In fact, when chased NeXT, and Jobs returned to the com-
he looks back on his diverse but connected pany that had fired him. He now oversees
experiences (which explain how he got where what he calls Apple’s current renaissance,
he is now), Jobs sees leaving school as “one based on the NeXT technology.
of the best decisions” he ever made. Doing Jobs calls this a “love and loss” life
lesson; so enabled him to stop spending his adoptive he continued to do the things he
loved after parents’ carefully saved money on education he lost his job, and that passion
enabled him at a time when he had no idea how he might to reach a new pinnacle in his
career. Jobs’
use that education, and allowed him to infor- advice to grads is also appropriate for
aspiring mally sit in on courses that interested him entrepreneurs. He said that “work is
going to instead of enrolling in required courses that fill a large part of your life, and the
only way to bored him. be truly satisfied is to do what you
believe is

One of the courses that interested Jobs great work. And the only way to do great
was calligraphy. Learning how to create beau- work is to love what you do. If you haven’t
tiful letters didn’t seem like a very practical found it yet, keep looking. Don’t settle.”
skill at the time, but ten years later, when he The third life lesson Jobs spoke about
that was developing the first Macintosh computer, day is what he calls a death lesson. In
2004
Jobs drew on that calligraphy experience to he was diagnosed with pancreatic cancer,
and incorporate multiple typefaces and proportion- told he had three to six months to live.
Then ally spaced fonts as two of the Mac’s most dis- the doctors discovered that his tumor
was tinctive features. His competitor, Microsoft, actually a rare form of the disease that is
cur- was then quick to add those elements to its able by surgery. Now that he is cancer
free, Windows operating system. Jobs wants everyone to “have the
courage to

As Jobs reflected in his Stanford speech, “If follow your heart and intuition. Our time on
I had never dropped out, I would have never earth,” he reminds us, “is limited.”
dropped in on this calligraphy class, and per- In his closing remarks, Jobs reminisced
sonal computers might not have the wonder- about *The Whole Earth Catalog,* a
publication ful typography that they do.” The life lesson from the 1960s and 1970s, which
he
he extracts from this experience is that individ- described as a kind of “Google in
paperback.” uals must be willing to trust their gut instincts The catalog’s farewell advice,
printed on the when they make choices, and believe that back cover of the final issue,
was “Stay
those choices (or “dots”) will somehow con- Hungry. Stay Foolish.” Jobs says this is

TABLE 1.1 Definitions of Entrepreneurship

Source	Definition
Knight (1921)	Profits from bearing uncertainty and risk
Schumpeter (1934)	Carrying out of new combinations of firm organization—new products, new services, new sources of raw material, new methods of production, new markets, new forms of organization
Hoselitz (1952)	Uncertainty bearing...coordination of productive resources... introduction of innovations and the provision of capital
Cole (1959)	Purposeful activity to initiate and develop a profit-oriented business
McClelland (1961)	Moderate risk taking
Casson (1982)	Decisions and judgments about the coordination of scarce resources
Gartner (1985)	Creation of new organizations
Stevenson, Roberts, & Grousbeck (1989); Barringer & Ireland (2006)	The pursuit of opportunity without regard to resources currently controlled
Hart, Stevenson, & Dial (1995)	The pursuit of opportunity without regard to resources currently controlled, but constrained by the founders' previous choices and industry-related experience
Shane & Venkataraman (2000)	A field of business seeks to understand how opportunities create something new…
Kuratko & Hodgetts (2004)	A dynamic process of vision, change and creation…
Allen (2006)	A mindset or way of thinking that is opportunity focused, innovative and growth-oriented. Can be found in large corporations and socially responsible not-for-profits…

SOURCE : F. Knight, Risk, Uncertainty and Profit (Boston: Houghton Mifflin, 1921); J. Schumpeter, The Theory of Economic Development (Cambridge, MA: Harvard University Press, 1934); B. Hoselitz, "Entrepreneurship and Economic Growth." American Journal of Economic Sociology, 1952; A. Cole, Business Enterprise in Its Social Setting (Cambridge, MA: Harvard University, 1959); D. McClelland, The Achieving Society (New York: John Wiley, 1961); M. Casson, The Entrepreneur (Totowa, NJ: Barnes and Noble, 1982); W. Gartner. "A Conceptual Framework for Describing the Phenomenon of New Venture Creation," Academy of Management Review 10, 1985:696–706; H. Stevenson, M. Roberts, and H. Grousbeck, New Business Venture and the Entrepreneur (Homewood, IL: Irwin, 1989); M. Hart, H. Stevenson, and J. Dial, "Entrepreneurship: A Definition Revisited," Babson Frontiers of Entrepreneurship Research, 1995; S. Shane and S. Venkataraman, "The Promise of Entrepreneurship as a Field of Research," Academy of Management Review 25, 2000:217-226; D Kuratko,and R. Hodgetts, Entrepreneurship, 6th ed. (Mason, Ohio: Thompson-Southwestern, 2004); B. Barringer and D. Ireland, Entrepreneurship (NJ: Prentice-Hall, 2006) and K. Allen, Launching New Ventures (Boston: Houghton Mifflin, 2006).

Within these definitions, we might find the following common elements and characteristics:

- Creativity and innovation
- Resource identification, acquisition, and marshaling
- Economic organization
- Opportunity for gain (or increase) under risk and uncertainty

Entrepreneurship, then, is the control and deployment of resources to create an innovative economic organization (or network of organizations) for the purpose of gain or growth under conditions of risk and uncertainty.[18] What are the implications of this definition?

Creation and Innovation

The term **creation** implies a founding and an origin. Therefore, technically speaking, the purchase of an existing firm or its transfer to new owners does not represent entrepreneurship. As one group of authors point out, if founding was the only criterion for entrepreneurship, then neither Tom Watson of IBM nor Ray Kroc of McDonald's would qualify.

It is rare for an organization to change ownership without a change in its management and resource configuration; however, the degree of change and innovation determines whether entrepreneurship is present. To see how large a change is needed, we can rely on Schumpeter's categories of "new combinations."[19] Is:

- A new product or service offered?
- A new method or technology employed?
- A new market targeted and opened?
- A new source of supply of raw materials and resources used?
- A new form of industrial organization created? (This is, perhaps, the rarest of all innovations.)

Now we can see how Watson and Kroc can reapply for membership in the entrepreneur's club.

Control and Deployment of Resources

The foundation for this book is the resource-based theory (or view) of sustained competitive advantage.[20] This theoretical framework originally derives from the viewpoint of a large corporation.[21] The resource-based theory is the most appropriate to understand new venture creation because it best describes how entrepreneurs themselves build their businesses from the resources and capabilities they currently possess or can realistically acquire. Successful entrepreneurship is not simply an analytical exercise. Industry and competitor analysis—the application of the theory of industrial organization economics—alone is insufficient. The resource-based theory argues that the choice of which industry to enter and what business in which to be is not enough to ensure success. The theory says that the nature and quality of the resources, capabilities, and strategies the entrepreneur possesses and can acquire can lead to long-term success. In fact, one can argue that choosing the resources for a firm, configuring these resources into a consistent strategy, and deploying the resources (implementation) are the quintessential entrepreneurial acts.[22]

Economic Organization

The term **economic organization** means an organization whose purpose is to allocate scarce resources. An economic organization can be a firm, a business unit within a firm, a network of independent organizations, a social network, or a not-for-profit organization (NPO).[23] Though it may seem paradoxical, even governments can create entrepreneurial organizations under the right conditions.

The business organization can, of course, pursue gain and growth as its motivations. In fact, some firms use both profit and size as their main objectives.[24] Other businesses do not seek growth, which distinguishes entrepreneurial firms from small businesses.[25] Do NPOs seek gain and growth? You bet they do. Although NPOs may be prohibited by law from making profits for stockholders, they are allowed to accumulate surpluses in their accounts. NPOs certainly seek growth: More members, more services performed, more clients served—the list may be endless. Our collective agreement that all of these organizations can be examples of entrepreneurship illustrates the ubiquitous nature of entrepreneurship and contributes to its vague and imprecise definitions.

A relatively new phenomenon in entrepreneurship is the creation of the **virtual organization.** A virtual organization is a network of independent organizations fulfilling core functions "as if" they were operating within the framework of a single company. For example, let us say that we are starting a company to manufacture and distribute canoes. But our primary expertise is in designing the boats—like Walden Kayaks. We could raise the money and recruit the top managers to do everything in-house. Or we could contract with a manufacturer, a distributor, a marketing organization (for promotion), an accounting firm, and a legal firm. None of these other organizations is within our absolute control, yet each will perform "as if" it were because of its contracts and incentives. This is a virtual organization. The advantages are that everyone does what they are best at. The disadvantages are that there are extra communication and control costs, and each organization carries its own overhead.[26]

Risk and Uncertainty

Entrepreneurship exists under conditions of risk and uncertainty. The two terms are not the same. **Risk** refers to the variability of outcomes (or returns); if there is no risk, the returns are certain. A firm operating in a risk-free environment would continue to expand forever, because a negative outcome could not occur. Therefore, risk is a limit to ever-expanding entrepreneurship.[27] Risk can also be measured quantitatively by using statistics that measure dispersion, like the variance and the standard deviation.

Uncertainty refers to the confidence entrepreneurs have in their estimates of how the world works—their understanding of the causes and effects in the environment. If there is no uncertainty, the environment and future can be perfectly known. If the future can be known, then everyone can know it (at least for a price), and it will not be a source of lasting profit for anyone. Uncertainty is what makes markets and poker games. Who would continue to place bets on a hand if all the cards were face up?

There are three types of uncertainty.

1. State uncertainty is the lack of knowledge about current conditions. The world is a big place and no one can know all the information of all the elements in it. There is uncertainty about which technologies will prevail. Demand for a new product is highly uncertain. Sometimes there are simply no data. For example, in China there is currently a lack of statistical information about employment, income, growth rates, entrepreneurial start-ups, and productivity gains. No one has this data. It has never been collected and even if it existed, it would likely be a government secret.
2. Effect uncertainty is the lack of knowledge of cause and effect. Even if we can somehow identify and know all the elements in a complex situation, we frequently will not understand the cause and effect relationships. Which comes first, the chicken or the

egg? Is a business successful because it has targeted psychologically satisfied customers, or are the customers satisfied because the business is successful? In a laboratory situation, we can do experiments to determine causality, but in the messy real world these experiments are impossible. We often just substitute correlation for causality—but this is a logical error.

3. Response uncertainty is not knowing what the response will be to some action. Related to effect uncertainty, here we have uncertainty about what kind of responses our actions will provoke. In some business cases, expanding the product line will cause competitors to expand theirs as well. In other cases, the competitors might simply ignore the expansion. They may think that the core business is suffering and that any new offerings are a desperate attempt to save the business. With response uncertainty present, it is hard to predict competitor and customer reaction. Similarly, we are frequently uncertain how regulators will view a firm. Will its products pass regulatory scrutiny, will licenses be forthcoming, and will legal challenges be met?

These uncertainties are barriers to entrepreneurship for some people, because they greatly increase anxiety about the future. But entrepreneurs bear this uncertainty. They can manage it as well as the concurrent risks.[28]

Entrepreneurs definitely take risks, which means that they engage in activity that leads to very variable outcomes. For example, a study of Canadian inventor-entrepreneurs showed that of 1,091 inventions, only 75 reached the market. Six of these earned returns above 1400 percent while 45 others lost money. (All of the non-commercial inventions lost money for the inventors as well.) William Baumol, famed economist of both Princeton and New York Universities, believes that people who take risks like this must have a "touch of madness." Baumol has spent decades trying to integrate the entrepreneur into a theory of rational economics, but madness and rationality are incompatible so far.[29] Entrepreneurship is "economics with imagination."[30]

WHERE IS ENTREPRENEURSHIP?

Two conditions must exist for entrepreneurship to flourish. First, there must be freedom—freedom to establish an economic venture, and freedom to be creative and innovative with that enterprise. Second, there must be prosperity—favorable economic conditions that give an entrepreneurial organization the opportunity to gain and grow.

Economic Growth and Freedom

Entrepreneurship is a global phenomenon. Therefore, it is vital that the prospective entrepreneur understand the relationship between the country in which the business will be located and the climate for business success. The Heritage Foundation and *The Wall Street Journal* publish an annual "Index of Economic Freedom." The index examines the trade policies, taxation levels, government intervention and regulation, monetary policies, and six other categories of over 150 countries. Data from all the years that these rankings have been made are available online at http://www.heritage.org/research/features/index/. The 2007 rankings show that once again Hong Kong is number one despite the 1997 return of Hong Kong to the People's Republic of China under the "one country–two systems" formula. Other countries in the top of the rankings of "free" economies are (in order): Singapore, Australia, United States, New Zealand, United Kingdom, Ireland, Luxembourg, Switzerland, and Canada. The seven countries with the lowest rankings and categorized as "repressed" were: North Korea, Cuba, Libya, Burma and Turkmenistan.

Data collected by the index support several conclusions that are important for entrepreneurs and the study of entrepreneurship. First, the study indicates the strong correlation between a high level of economic and political freedom and a high standard of living. Second, a comparison of data over several years indicates that as wealthy countries become richer, they often impose fiscal restrictions that reduce economic freedom, such as higher taxation and social welfare programs. This is why the relatively well-off countries in Scandinavia and Western Europe are mostly missing from the top 10 list. The poorest countries are poor because of the lack of economic freedom, not because of a lack of aid from richer countries or a lack of natural resources.[31] Some of these poor countries are now the targets of social entrepreneurs who are trying to jumpstart economic growth from the perspective of feeding the poor or treating and preventing AIDS.

Two examples from formerly communist economies illustrate how important economic freedom can be to entrepreneurship. After years of exile in France, Anoa Dussol-Perran returned to her native Vietnam to open a passenger-helicopter service in Hanoi. To avoid a possible three-year wait for government approval, Ms. Dussol-Perran attempted to smuggle her first helicopter into Vietnam without filing the proper paperwork. The helicopter was discovered and impounded by the Vietnamese government. It was released to Ms. Dussol-Perran only after a long wait, followed by a grueling six-hour interview. When the time came to add a second helicopter to her service, Ms. Dussol-Perran elected to fly the new equipment from Paris to Hanoi herself rather than risk importing another machine.[32]

In contrast, Jake Weinstock and his two partners have enjoyed relatively smooth sailing as they set up Gold's Gym franchise in Moscow. Although Russia (#122) is still ranked as mostly unfree in the Index of Economic Freedom, it did place 20 slots above Vietnam (#142) in the 2006 survey. Weinstock was able to avoid customs problems with his imported equipment—reportedly the toughest hurdle for new businesses in Russia—by letting his Russian partner, a former athlete and sporting goods trader, handle those negotiations. He was also able to avoid the organized crime threats that plague other foreign businesses. "We built up many relationships and alliances, which meant we were less susceptible to shakedowns," explains Weinstock. "We made sure important people were interested in our success."[33]

Yet even in the "free" United States, entrepreneurs can run into problems concerning their economic freedom. . Consider the case of Andrew Beebee. Beebee is an Internet entrepreneur who started his dot.com in the largely Hispanic Mission district of San Francisco. He signed a five-year lease for five floors of a nine-story building when his business began to skyrocket. When Beebee moved in, his landlord told many of the other tenants that they would not have their leases renewed due to asbestos removal and because the building was going high-tech. These tenants, however, had their freedoms too. Over the next several months they conducted sit-ins, acts of civil disobedience, and picketing to protest what they saw as the gentrification of the area. Mr. Beebee was stymied and his company hemmed in by political activity and zoning ordinances. "Aqui estamos, y no vamos" ("Here we are, and we are not going") chanted the demonstrators.[34]

Another indicator of "where" entrepreneurship flourishes is found in the ease of starting a business. The World Bank has a global index for this indicator. Table 1.2 presents a top-10 list of best countries in which to start a business. Note there are other business indicators on the list as well.

WHO IS THE NEW ENTREPRENEUR?

Ask any group of businesspeople today if they consider themselves entrepreneurs. According to Bill Sahlman, professor and senior associate dean at the Harvard Business School, "most of them will raise their hands. That doesn't mean that they are entrepreneurial, but they would certainly not like you to think they aren't."[35] If entrepreneurship is one of the hot labels today, it is because the concept of being an entrepreneur has changed.[36] Fifteen years ago, an entrepreneur might have been described as a business version of a John Wayne cowboy (tough, gutsy, and male), who steered his business through the rodeo of commerce without the help of training or education and without the assistance of bankers or other experts. Entrepreneurs were once seen as small business founders with a strong independent streak and perhaps a flair for the dramatic. Entrepreneurs were thus born, not made.

Things are different now (see Table 1.3). A class of *professional entrepreneurs* is emerging today who rely more on their brains than their guts—and who have been trained to use both methods and technology to analyze the business environment. Some of the firms created have been named **gazelles.**[37] A gazelle is a fast-growing, innovative company that creates buzz and jobs. Gazelles are distributed in all industries and environments. It is estimated that of the more than 18 million small businesses in the United States, there are only about 340,000 gazelles. They even have their own Web site: http://gazellesInc.com.[38]

A look at Table 1.3 reveals some significant trends. First, there is increased emphasis on leadership. Leadership is a complex phenomenon and although most of us have some capacity for it, the pundits agree that outstanding leadership is always in short supply. The entrepreneur has to lead his or her organization and its people. He or she needs to be a motivator and a model for behavior. He or she must be out in front inspiring people to follow.

A second trend is better management. The days of building a better mousetrap and leaving it at that are gone. The entrepreneur must be a manager—planning, monitoring the business's achievements, controlling the flow of work and information through the organization, and staffing the venture with other leaders and competent managers.

According to Bill Wetzel, professor emeritus at the University of New Hampshire, the difference is like night and day. Wetzel says that the old-style entrepreneur or business founder was thought primarily to be concerned with earning a living, while today's

TABLE 1.2 World Bank Economic Rankings

Economy	Ease of Doing Business	Starting a Business	Dealing with Licenses	Employing Workers	Registering Property
Singapore	1	11	8	3	12
New Zealand	2	3	18	10	1
United States	3	3	22	1	10
Canada	4	1	32	13	22
Hong Kong, China	5	5	64	16	60
United Kingdom	6	9	46	17	19
Denmark	7	14	6	15	36
Australia	8	2	29	9	27
Norway	9	21	14	109	6
Ireland	10	6	20	83	80
Japan	11	18	2	36	39
Iceland	12	16	30	42	8
Sweden	13	20	17	94	7
Finland	14	18	35	111	15
Switzerland	15	27	38	24	11
Lithuania	16	48	23	119	3
Estonia	17	51	13	151	23
Thailand	18	28	3	46	18
Puerto Rico	19	8	91	33	46
Belgium	20	37	48	23	158

SOURCE: Adapted from the World Bank, "Doing Business Economy Rankings," 2006. Retrieved from the Web May 1, 2006. http://www.doingbusiness.org/EconomyRankings/Default.aspx?direction=asc&sort=2

entrepreneur "has the intention of building a significant company that can create wealth for the entrepreneur and investors."[39]

Street Story 1.2 describes the start-up process for Jeremiah Hutchins. He has built a significant company by being prepared, doing some commonsense research, and using technology to his advantage.

The new entrepreneurs come from different backgrounds too. Many of them are corporate-track dropouts, pushed out by downsizing or lured out by the quest for status, big money, or control of their personal lives. Globalization has promoted an entrepreneurial spirit in both big and small companies, while information technology now enables many small start-ups to compete against big business.

Academia has also contributed to the creation of this new professional entrepreneur class. Harvard Business School, which once had three or four professors teaching courses about small business, now has 17 full-time faculty members in its entrepreneurial-studies program. Staffing at other colleges and universities reflects the same trend. The content of much finance, marketing, and other business courses has also been adjusted to reflect new venture concerns and development methods. The new entrepreneurs don't just do; they understand what they're doing.[40]

TABLE 1.3 Entrepreneurs

Then	Now
Small-business founder	True entrepreneur
Boss	Leader
Lone Ranger	Social and business networker
Secretive	Open
Self-reliant	Inquisitive
Seat of the pants	Business plan
Snap decisions	Consensus
Male ownership	Mixed ownership (In 1993, women owned one-third of all sole proprietorships, up from one-quarter in 1980.)
Idea	Execution
In 1982, 80% of the CEOs of the Inc. 500 companies believed their companies' success was based on novel, unique, or proprietary ideas.	1992, 80% of the CEOs of Inc. 500 companies said that the ideas for their companies were ordinary, and that they owed their success to better business models.
Knows the Trade	Knows the Business
Eastern, one of the first airlines in the United States, was founded by pilot Eddie Rickenbacker.	Federal Express, an overnight delivery service using airplanes, was developed from a business plan written by Fred Smith while he was studying for his MBA at Yale.
Automation	Innovation
Technology lets business automate the work people had always done	Technology lets people do things never done before.

SOURCE: Adapted from Tom Richman, "The Evolution of the Professional Entrepreneur," Inc.'s the State of Small Business Special Issue, l997: 50–53.

DIMENSIONS OF ENTREPRENEURSHIP

New Venture Creation

This book is concerned with entrepreneurship as the formation of a new business enterprise—most often called simply **new venture creation**. It contains theory and research about, and descriptions of, practice and techniques of entrepreneurship. We take an economic and managerial approach to entrepreneurship and new venture creation, although at times we borrow important material from other disciplines. Much has been written about the phenomenon of entrepreneurship and new venture creation from the economic and managerial perspectives. There have been numerous descriptive studies and some valuable empirical research, but no textbook, including this one, can offer prospective entrepreneurs advice that will ensure their success. There is no "rule for riches" as we will see in the next chapter. Not enough is known about entrepreneurship (or business

STREET STORY 1.2

Peace of Mind Goes Digital

Jeremiah Hutchins says he had many ideas for new business ventures while driving his truck along the highways of California. None of his ideas, including one to digitize business cards on miniature CD-ROMs, ever got off the ground.

But a radio alert report about a missing child inspired Hutchins to make the entrepreneurial leap to actually starting a business. Hutchins, the father of two small girls, wondered whether his mini-CD idea might be used to store identification data for children.

Within 24 hours, Hutchins had networked with a local police investigator to get some feedback on his idea. The investigator liked his concept, and supplied Hutchins with a list of the kinds of information, such as a physical description, blood type, scars, and distinctive habits, that the police want to have when a missing-person report is filed. Hutchins also searched the Internet to see if anyone else offered a similar product, and decided he had discovered a niche with an unmet need.

Over the next ten days, Hutchins took a leadership role as he and his partner, a security guard at the trucking firm where Hutchins worked, did more groundwork. They created and registered a Web-site domain name (www.safekidscard.com), and then tested digital cameras, ink, CD burners, and other equipment in preparation for creating a prototype of a digital ID card.

The idea of parents collecting information about their children as a safety measure is certainly not unique to Jeremiah Hutchins. But the technology he used to collect and store that data into a compact database was innovative. When Hutchins showed local police how he could use a computer to collect child identification information and then store it in a convenient form, they were impressed. They invited him to set up a booth at a community safety fair the following week. Just three weeks after he first had this idea, Hutchins and his partner had sold 150 ID cards and grossed $3,000.

Hutchins' primary product today is a do-it-yourself, Windows-compatible CD-ROM that holds three digital color photos and a digital thumbprint, along with personal, medical, and contact information. Slightly larger than a credit card, the mini CD can be carried in a parent's wallet, and can be easily shared with police or hospitals in the event of an emergency. Hutchins' Web site also markets ID cards for adults and pets, along with a variety of related products, including child ID bracelets, dental impression kits, shoe labels, personal safety books, and DVDs.

Hutchins has also been innovative in expanding his company. In 2002, he began selling franchises, and by 2005, he had 43 functioning franchises producing ID CDs on site at schools, day-care centers, and other locations. Several Web sites now recommend Safe Kids Card as a good example for people who want to launch low-cost, home-based businesses.

According to the company Web site, the franchisee fee is less than $20,000, including equipment. Safe Kids Card also sells economical distributorships to people who want to market the do-it-yourself ID kits in their area.

In 2006, Safe Kids Card began a partnership with the National Troopers Coalition in which a portion of the proceeds troopers receive from selling kits benefits state trooper programs. In the future, Hutchins also hopes to works with businesses that will offer customers a discount or gift certificate for the ID kits as a service or appreciation gift.

This entrepreneur has done a good job of using technology to benefit both himself and society.

SOURCE: Adapted in part from Gwendolyn Bounds, "You Have a Great Idea. Now What?" *The Wall Street Journal Online*, May 9, 2005. Retrieved from the Web May 2, 2006. http://www.online.wsj.com.

in general) for the field to be considered a "sure thing." In fact, any guidance obtained from a book is probably of little long-term value to a potential entrepreneur.[41] However, the insights a reader gains by comparing personal experience with the material in this book may be invaluable.

One thing we do know is that ventures that employ resources and capabilities that are valuable, rare, hard to copy, and have no good substitutes, in favorable industry conditions, provide sustainable competitive advantage.[42] Choosing the appropriate resources is ultimately a matter of entrepreneurial vision and intuition. The creative act underlying such vision is a subject that has so far not been a central focus of resource-based theory. This book extends the theory and views of entrepreneurship within the context of the resource-based theory of the firm.[43]

Opportunity Analysis

A second dimension of entrepreneurship focuses on **opportunity analysis**. *Opportunity* is the confluence of personal preparation, external circumstances, and sensitivity to change. Different people may have different opportunity analyses. Some may feel the time window of opportunity is open and that they are ready to begin the new venture creation process. Others may feel they are not yet personally well prepared or that the external circumstance is not yet right or has passed them by. People might well agree on both preparation and circumstances, but have different levels of sensitivity. Some people are first-movers and others are, more cautiously, later movers. Chapters 2, 3, and 4 are devoted to processes and models for venture opportunity analysis. Chapters 6, 7, 8, and 9 will emphasize lower-level opportunity analysis in marketing, finances, and organizations, respectively.

Where do entrepreneurial opportunities come from? How does one get business ideas? One approach to the answer is "change." Changes in the business environment offer opportunities for entrepreneurs. Existing firms have their resources, strategy, and organization structure geared for the past or current environment. When a change occurs, the new firm frequently has an easier time spotting it and configuring a set of resources and an organization to meet the new needs and the new realities than an existing organization. Change can occur from market disequilibrium, factors that enhance production possibilities, and the opportunities created from earlier acts of entrepreneurship. Entrepreneurship builds on itself and is a virtuous[44] cycle of economic activity.[45]

According to the late management guru, Peter Drucker (who firmly believed that entrepreneurship could be taught), there are seven sources of opportunity to look for in the environment.[46]

The Unexpected. When current businesses are surprised by an unanticipated event, they are often unable to adapt quickly enough to take advantage of that event. The event can be an unexpected success (good news) or an unexpected failure (bad news). For example, if war breaks out where it is unexpected, it changes the economics and demand structure of the warring parties and their populations. The war can provide opportunity if it is ethically pursued. Similarly, a breakthrough in a peace negotiation can also provide opportunity, because it can change the economies of the former combatants. For example, if the Israeli and Palestinian conflict can be resolved, the beachfront property in the Gaza strip (now a dormant resource) would become one of the premier vacation resorts in the world.

Sometimes the unexpected happens directly to the company; The shock can be fatal or it can be the source of new opportunities. For example, in August of 2000, the Walt Disney Company released a movie called "Coyote Ugly" about a wild and raucous bar in New York. The movie was not especially believable and the reviews were bad. It faded from mainstream consciousness, but then an unexpected event occurred: the movie became a cult hit. Sudddenly, the real Coyote Ugly bar received a great rush of interest and publicity. The owner, Lilliana Lovell, had a hit business on her hands. "What business ever anticipates getting $40 million in free national advertising? We decided to take advantage of it," she said. So she cleverly imitated all the details of the movie set and now has 13 bars and is a millionaire. "Most people have to build a business to get the brand and name recognition, she did it in reverse. There has never been a woman to build a [national] chain of bars, period," remarked Morris Reid, a branding specialist.[47]

The Incongruous. Incongruity is dissonance, something that "ought to be" but is not. Incongruity creates instability and opportunity. For example, it is incongruous for a growing industry with increasing sales not to be profitable, but such a scenario is possible and is taking place now on the Internet. Some key to the industry's economics has yet to be discovered. When reality and conventional wisdom collide, incongruity exists. Listen for "expert old-timers" who use the words *never* and *always* to explain how things should be. These unexamined assumptions may have once been right, but may now be wrong and therefore may provide opportunities for the responsive entrepreneur.

The Process Need. The process need has its source in technology's inability to provide the "big breakthrough." Technicians often need to work out a way to get from point A to point B using some process. Currently, researchers are making efforts in the areas of superconductivity, fusion, interconnectivity, and the search for a treatment and cure for AIDS. Thomas Edison and others knew that in order to start the electric energy industry, they needed to solve a process need—to develop a light bulb that worked. Process need opportunities are often addressed by program research projects, which are the systematic research and analysis efforts designed to solve a single problem, such as the effort against AIDS.

Industry and Market Structures. Changes in technology, innovation, and invention alter market and industry structures by altering costs, quality requirements, and volume capabilities. This alteration can potentially make existing firms obsolete if they are not attuned to it and are inflexible. Similarly, changes in social values and consumer tastes, as well as demographics, shift the economics of industries to a new equilibrium. The markets of firms that do not adapt to these changes are fair game for the entrepreneur.

Demographics. Demographic changes are changes in the society's population or subpopulations. They can be changes in the size, age, structure, employment status, education, or incomes of these groups. Such changes influence all industries and firms by changing the mix of products and services demanded, the volume of products and services, and the buying power of customers. Some of these changes are predictable, because people who will be older are already alive, and birth and death rates stay fairly stable over time. Other changes are not predictable and are caused by natural disasters, war, social change, and immigration. Population statistics are available for assessment of demographic changes, but opportunities can be found before the data are published if the entrepreneur observes what is happening in the street and being reported in the newspaper.

Changes in Perception. Is the glass half full or half empty? The two perceptions are logically equivalent but reflect significantly different attitudes and behaviors. People hold different perceptions of the same reality, and these differences affect the products and services they demand and the amounts they spend. Some groups feel powerful and rich; others, disenfranchised and poor. Some people think they are thin when they are not; others think they are too fat when they are not. The entrepreneur can sell power and status to the rich and powerful, and sell relief and comfort to the poor and oppressed. Whether people are rich or poor, if they perceive that they are middle class, they will demand education for their children, good housing for their families, and travel for their vacations.

New Knowledge. New knowledge is often seen as the "superstar" of entrepreneurial opportunity. However, it can be "temperamental, capricious, and hard to manage."[48] Having new knowledge is not enough: entrepreneurs must also find a way to make products from this knowledge and to protect the profits of those products from competition as the knowledge is spread to others. In addition, timing is critical. It frequently takes the convergence of many pieces of new knowledge to make a product. For example,

> A number of knowledge bases came together to make possible the computer. The earliest was the binary theorem, a mathematical theory going back to the 17th century that enables all numbers to be expressed by two numbers only: one and zero. It was applied to a calculating machine by Charles Babbage in the first half of the nineteenth century. In 1890, Hermann Hollerith invented the punch card, going back to the invention in the early 19th century by Frenchman J. M. Jacquard. The punch card makes it possible to convert numbers into "instructions." In 1906 an American, Lee de Forest, invented the audion tube, and with it created electronics. Then, between 1910 and 1913, Bertrand Russell and Alfred North Whitehead, in the *Principia Mathematica*, created symbolic logic, which enables us to express all logical concepts as numbers. Finally, during World War I, the concepts of programming and feedback were developed, primarily for the purposes of anti-aircraft gunnery. By 1918, in other words, all the knowledge needed to develop the computer was available. The first computer became operational in 1946. (P. Drucker, *Innovation and Entrepreneurship*. NY: Harper and Row, 1985)

Three additional dimensions or lenses are used to study entrepreneurship: individuals, environments, and organizations. These are required to flesh out the arguments and examples.[49] The interactions among individuals, environments, and organizations make each new venture unique and must be considered.

The Individual

The role that individuals play in entrepreneurship is undeniable. Each person's psychological, sociological, and demographic characteristics contribute to or detract from his or her abilities to be an entrepreneur. Personal experience, knowledge, education, and training are the accumulated human resources that the founder contributes to the enterprise. The personal integrity of the entrepreneur and the way the entrepreneur and the new venture are viewed by others are captured in the person's reputation. The risk profile of the entrepreneur determines the initial configuration of the venture—for example, financing, product offerings, and staffing. Although it is common to speak of the individual entrepreneur, frequently the entrepreneur is not alone. Entrepreneurs rely on a network of other people, other businesspeople, and other entrepreneurs. These contacts are personal resources that help the entrepreneur to acquire additional resources and start his or her business. It is true that "who you know" and "who knows you" are sometimes very valuable resources in new venture creation.

One of the individual entrepreneur's most important responsibilities is to establish an ethical climate for the new venture. Business **ethics** has been defined in many ways by many people. One definition of ethical behavior is: any business decision that creates value for the customer by matching quality and price. Why is this so? Ethical decisions (1) provide the customer with valid data about the product and service, (2) enable the customer to make a free and informed choice, and (3) generate customer commitment to the product and the organization that provides it. Violations of these three rules produce unethical behavior— invalid and false data, coerced and manipulated decisions, and low integrity and poor reputation for the firm.[50] How important are ethics and a good reputation? According to one advertising executive, "The only sustainable competitive advantage any business has is its reputation."[51]

Entrepreneurs are sometimes placed in situations where ethical decision making appears hard. It is tempting to cut corners, look for the edge by shading the truth, and adopt a *caveat emptor* ("let the buyer beware") attitude. If entrepreneurs see themselves as outsiders, underdogs, overworked, and underappreciated, they may make decisions based on the premise that the ends justify the means. Caution is advised. The means will become known, and if the means fail the tests for ethical conduct, the fine reputation of the product and the entrepreneurial team will be irreparably tarnished.

The role of the individual founder or team changes over time. We can imagine that at the founding of the business, the imprinting of the individual/team characteristics on the business represents the primary way of identifying the firm. The venture is made in the image of its makers. But over time the importance that this initial imprinting has on the firm decreases. While the imprinting is always present in some form, the business develops its own personality and characteristics. New leaders and managers come aboard. Product and service mixes change and new management makes organizational changes. Eventually the business develops its own identity, although the ethos and the values of the original entrepreneurs may remain.

The Environment

The environment poses both opportunities (see above) and threats for new venture creation. The opportunities come in the form of change and resources—money, people, technology. The entrepreneurial challenge is to acquire resources from the environment, combine them with other resources already possessed, and configure the new venture into a successful organization. The threats, or constraints, imposed by the environment

STREET STORY 1.3

Sam Walton's 10 Best Rules

Sam Walton was born in 1918 and died in 1992. In his lifetime, he built the largest, most successful retail organization in the world and became America's richest person. His chosen path to empire was either "overlooked or underestimated by his rivals."

After graduating from the University of Missouri, Walton went right to work for J.C. Penney in 1940 for $75 per month. He loved retailing and its competitiveness. He bought his own store, a Ben Franklin, when he was mustered out of the Army in 1945. However, he did not open the first Wal-Mart until 1962.

Between 1940 and 1962, "Mr. Sam" developed many of the habits and garnered the experience that was to serve him so well later. He says his big lesson came early when he found that if he "bought an item for 80 cents . . . and priced it at a dollar, [he] could sell three times more of it than by pricing it at $1.20. I might have made only half the profit per item but because I was selling three times as many, the overall profit was much greater."

In the early 1960s, Mr. Sam discovered others were beginning to develop large discount stores and chains. He did his homework and spent many nights on the road visiting these other merchants' stores. He admits that he "borrowed" quite a bit from Sol Price, founder of Fedmart. He finally decided that the future was in discounting, and proceeded to open the first Wal-Mart. In 1962, Wal-Mart's first year, the first Kmart, Target, and Woolco stores were also opened.

Ten years after the opening of the first Wal-Mart, the scoreboard read: Kmart, 500 stores and $3 billion sales; Wal-Mart, 50 stores and $80 million sales. In addition, the four leading retailers of the first half of the century—Sears, J.C. Penney, Woolworth, and Montgomery Ward— were still flourishing, and every urban area had a regional department store or chain with which to compete. Many had resources far in excess of Walton's. So how did Mr. Sam become number one?

In a book written shortly before his death in 1992, Mr. Sam was asked about his rise to prominence. He said that the keys were (1) going head to head with Kmart, because the pressure of the competition made everyone a better retailer and encouraged innovation and change; (2) going small town (under 50,000 people), because this was an underserved niche; (3) employee profit sharing, because everyone was then an owner directed toward the same goal; and (4) communication and sharing information with all people inside the organization, because doing so empowered people and pushed responsibility for decision making down. Sam wouldn't say this, but a fifth factor was his tireless and unceasing dedication to keeping costs down and spirits up. His leadership was unparalleled by any of his competitors.

Clearly, Mr. Sam possessed personal that experience, values, vision, and dedication in heroic proportions; he was unequaled by any of his rivals. But were his business decisions so unique that they cannot or could not be duplicated by another firm? When asked this question, Mr. Sam came up with his 10 rules to follow, rules that worked for him. If you follow these rules, can you be the next Sam Walton?

Rule 1: Commit to your business and believe in it.
Rule 2: Share your profits with your partners (employees).
Rule 3: Motivate your partners, challenge them, and keep score.
Rule 4: Communicate everything.

Rule 5: Appreciate your associates with well-chosen words.
Rule 6: Celebrate your successes.
Rule 7: Listen to everyone and get them talking.
Rule 8: Exceed your customers' expectations.
Rule 9: Control your expenses.
Rule 10: **BREAK ALL THE RULES**. Swim upstream. Go the other way.

Rule 10 is a doozy (as well as a paradox). It suggests that rules 1 through 9 may not be for everyone. It also suggests that Mr. Sam himself knew that by following everyone's advice on everything, you could never achieve much more than everyone else. Just as Mr. Sam visited as many Kmarts as he could, everyone who paid attention could have visited all the Wal-Marts and copied what they did. You could easily duplicate rules 1 through 9, but you could never duplicate precisely the decisions that were made following rule 10. This is the unique and idiosyncratic aspect of Mr. Sam that made him the world's greatest merchant.

SOURCE: *Fortune*, March 23, 1992:113–l14, and June 29, 1992:98–106.

are those inherent in any competitive marketplace. The entrepreneur can overcome these constraints, or protect against their worst effects, by developing strategies that exploit the firm's resources. The key elements of the environment are the government and politics, the economy, technology (i.e., innovation and invention), sociodemographics, and the ecosystem. Because the environment is characterized by change, uncertainty, and complexity, entrepreneurs must continually monitor events and trends and make adjustments to their organizations and strategies.

The Organization

The result of nearly all entrepreneurial start-ups is the creation of a new organization. This organization has a form and structure. It has a strategy that enables it to penetrate or create a market (entry wedges) and protect its position (isolating mechanisms). It possesses resources that it transforms into value for its customers.

However, an organization can be even more than this. An organization is made up of people who have skills and talents, values and beliefs, and maybe the recognition that by working together they can create something special. For example, the organization can have a culture that supports high performance and high quality. We will take a few minutes to look more closely at the concept of quality.

Quality is a difficult concept to grasp, yet it is critical to success. It is a way to differentiate the firm and provide it with a degree of protection from competitors. Quality is part of the entrepreneur's strategy. We will address strategy again in Chapter 4, but it is important to get a handle on this issue early.

Garvin identified five different approaches to the concept of **quality**: transcendent, product based, user based, manufacturing based, and value based.[52]

The Transcendent Approach. The transcendent approach to quality is philosophical and asks questions about the nature of things. With this approach, quality is considered "innate excellence."[53] Some experts dismiss this approach as being of little practical value for the businessperson, but we believe it can offer some guidance. A product's or service's quality concerns the function that it is intended to serve. Anything that inhibits that function detracts from quality. For example, consider quality in terms of a restaurant meal. Its quality includes its nutritional value, premium ingredients, taste, aroma, presentation, and timeliness. A poor-quality meal lacks what is necessary and also has other qualities attached, such as slow service, foreign ingredients, poor presentation, and careless preparation. The high-quality meal is distinguished from the poor-quality meal because it has only the elements it should and none of the detracting elements.

Product-Based Approach. The product-based concept of quality focuses on an attribute of the product that is held in high regard—for example, the high butterfat content in ice cream, the tightness and intensity of evenness (consistency) of stitches in a garment, or the durability of a washing machine. Quality of this sort can be ranked because it lends itself to quantitative measurement. Because the assessment of these attributes can be made independently of the user, product-based quality is sometimes referred to as "objective" quality.[54]

User-Based Approach. User-based quality is "subjective"—it exists in the eye of the beholder. Customers have different preferences, wants, and needs and therefore judge a product's quality by its usefulness to them. Are firms who meet these needs, but do so in nonquantitative ways (perhaps through advertising or superior product distribution), producing quality products? And when "subjective" quality competes with "objective" quality, is "good enough" really enough? For example, Toyota continues to have among the highest customer ratings for its automobiles despite the objective fact that many of Detroit's slow-selling cars are every bit as good. The car-buying public makes Toyota the higher quality product by how it perceives the brand.

Manufacturing-Based Approach. Manufacturing-based quality, or process quality, concerns the attention to detail in the construction and delivery of the product or service. It is linked to customer wants and needs and to objective quality because it presumes that someone defined *conformance standards* for the product or service. *Quality* is defined as the degree to which the product conforms to a set standard or the service to set levels and times. In other words, high reliability and zero manufacturing defects are important. The problem with this definition is that the link between standards and customer preferences was established in the past, perhaps long ago, and is not responsive to changes in the environment. Manufacturing-based quality shifts attention internally to how things are done. At its worst, it leads to taking the wrong steps but taking them very well.

Garvin's last category of quality is value based. This approach takes the concept of quality farther than the previous definitions. **Value** looks at quality in terms of price, and price is what customers consider when they decide whether to buy a product or service. If money were not scarce, nothing would be valuable, not even quality, because everyone could buy anything—but this is, of course, not true. Therefore, in business where prices are signals and money is scarce, value, not pure quality, is critical.

Which is the correct perspective on quality and value for the entrepreneur? We believe that entrepreneurs should understand all these perspectives and be able to make decisions based on their current situations. The ability to understand many facets of quality improves the entrepreneur's decision making. It enables an entrepreneur to meet the challenges posed by complex problems. It highlights the importance of the individual in new venture creation.

Figure 1.1 illustrates the dimensions of entrepreneurship and new venture creation.

PARADOXES OF ENTREPRENEURSHIP

The resource-based theory of entrepreneurship also helps explain two of the paradoxes of entrepreneurship in ways that other theories cannot.

Intelligence Paradox

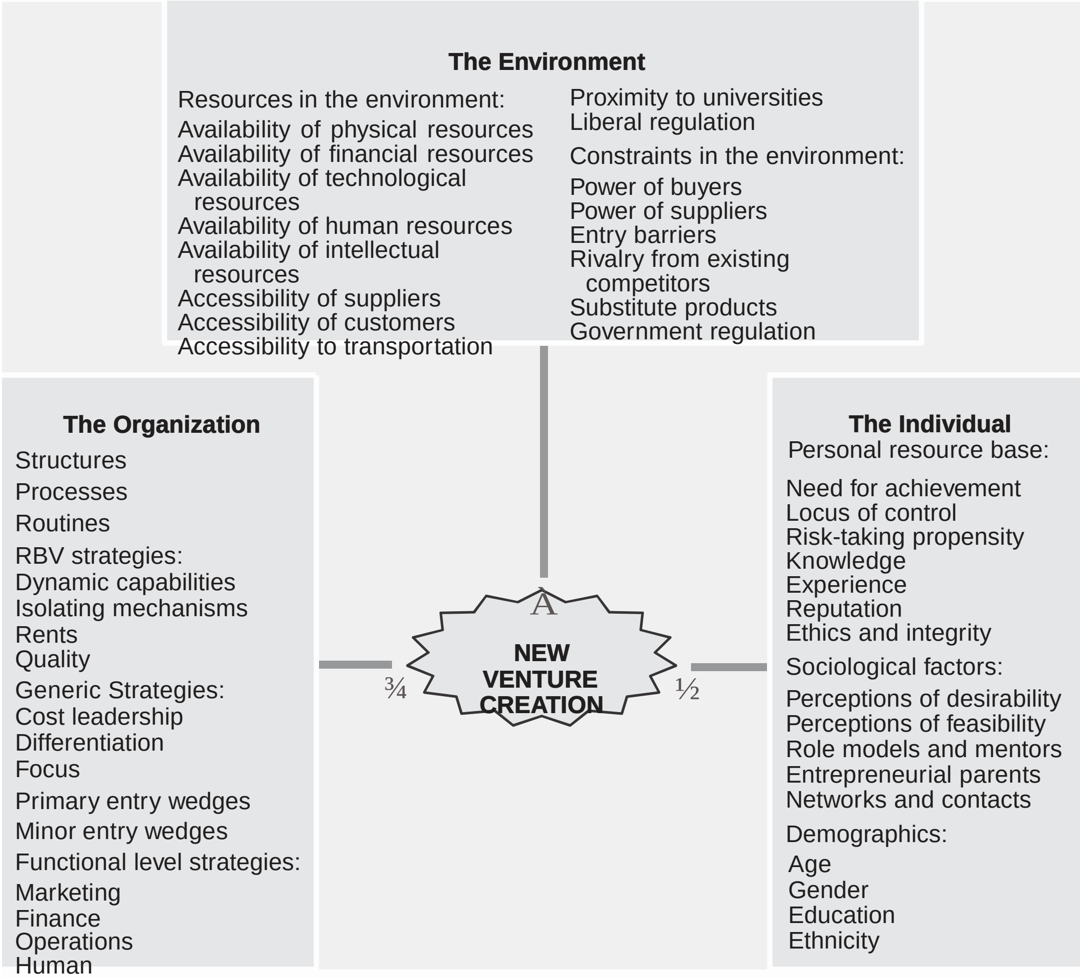
The first paradox is often stated as, "If you are so smart, why aren't you rich?" Certainly professors and researchers can testify that there are a great many more smart people than rich people. A good theory of entrepreneurship needs to explain why intelligence does not always lead to success in business. Common logic seems to dictate that the better we understand a phenomenon such as new venture creation, the more likely we are to be successful in its practice. Textbook presentations of entrepreneurship that provide facts without examining cause and effect may make the student smarter (in some narrow sense), but these approaches are unlikely to make anyone (except the authors) richer.

The resource-based approach acknowledges that keen analysis (strategy formulation) and fact accumulation are necessary but insufficient tasks for entrepreneurs. Also, the resource-based theory holds that some aspects of entrepreneurship cannot be analyzed; they are hard to copy because no one, including the founders, quite understands how or why they work. This inability to be duplicated or explained is actually a business advantage because competitors cannot copy the entrepreneur's strategy if they can't understand it. In simple language, what is known (or knowable) to all is an advantage to none. We can get smarter without getting richer if the knowledge we possess lacks any of the four characteristics (valuable, rare, hard to copy, or no substitutes).[55]

Entry Barrier Paradox

The second paradox is summed up by the old line, "You wouldn't want to belong to any club that would have you as a member."[56] The parallel application of this adage to new venture creation is that "you wouldn't want to enter any industry that would have you" (low-entry barriers) because if you could get in, then anyone could. Therefore, the opportunity will appear unattractive. This is the traditional economic analysis that examines the height of the entry barriers and weighs the cost of entry against the profit potential (margins) of firms in the industry, and the probability of retaliation by incumbents.[57] One implication of this analysis is that, for the vast majority of economic organizations, existing firms have the edge. Yet, experience indicates that certain individuals create businesses in industries with seemingly insurmountable barriers, and these individuals achieve superior and sometimes spectacular results. Analysis of industry structure fails to explain this phenomenon because it cannot explain why everyone cannot follow suit. The resource-based theory can explain the likes of Sam Walton, founder of Wal-Mart (see Street Story 1.3), Ted Turner of Turner Broadcasting, and Dave Thomas of Wendy's

FIGURE 1.1 Dimensions of New Venture Creation



SOURCE: Adapted from W. Gartner, "The Conceptual Framework for Describing the Phenomenon of New Venture Creation," Academy of Management Review 10, 1985: 696–706.

as individuals with unique personal resources. They were able to enter industries that appeared to have powerful predatory competitors and go against the odds to build major influential organizations.

ORGANIZATION OF THE BOOK

Chapter 1 provides the framework for the study of entrepreneurship, beginning with the theme that entrepreneurs succeed because of the resources that they possess and acquire and the strategies they employ. This resource-based theory is described in greater detail in Chapter 2, where we also examine different types of resources and capabilities, and explore the relative importance of each.

Chapter 3 explains the environment for entrepreneurship as having two interrelated components: (1) a remote environment that cannot be controlled by the entrepreneur, and (2) a competitive environment in which the entrepreneur executes his or her strategies and plans. The importance of environmental scanning and a model for scanning are also presented in this chapter. Chapter 4 details exactly how entrepreneurs go into business by looking at the strategies they pursue. We will also introduce the Information Rules strategies that are critical to the success of ventures based on information. Chapter 5 explains the basics of writing the business plan. The plan is required for all new ventures and it signifies the transition from planning to implementation. We offer an example of a business plan as the appendix to Chapter 5.

After Chapter 5, we make the transition from the formulation of venture strategy to the implementation phase. Chapter 6 examines the marketing-entrepreneurship interface. We examine how the success of the venture is enhanced with effective marketing. We also cover many of the marketing, sales, and pricing strategies that are critical for the new venture. The advent of electronic commerce and the Internet has changed forever the nature of starting a business for those who incorporate technology into their operations and products. We will focus on information-related businesses and see how the combination of having rare, valuable, and hard-to-copy information and the Internet provide new opportunities for entrepreneurs.

Chapter 7 describes the foundations of entrepreneurial financing, including debt, equity, and cash flow. Chapter 8 continues the discussion of financial issues by looking at how investors and entrepreneurs view each other, and describes how they are likely to want to structure a financial deal. The chapter also covers legal and taxation issues.

Chapter 9 explores the new venture's organization. We will look at how some organizations are strong from the start and have characteristics that enable them to persevere through many business cycles. Our discussion is based on Collins and Porras's book, *Built to Last*. Chapter 10 describes corporate venturing and intrapreneurship. We see how large organizations try to keep fresh so they can remain innovative and entrepreneurial. In this final chapter, we introduce the *Balanced Scorecard* concepts.

The 10 chapters are followed by a selection of cases drawn from real situations and business plans. These cases illustrate the possibilities and opportunities facing entrepreneurs.

A FINAL WORD

Not everyone will succeed as an entrepreneur, and sometimes the people who do succeed do so only after a number of painful attempts. As the introductory quote illustrates, studying entrepreneurship and being an entrepreneur are two different things. The odds of success are quite different in these two endeavors, and the outcomes are evaluated by different criteria. However, the student of entrepreneurship should realize that he or she can be a successful entrepreneur. Previous academic achievement is not a requirement.

Many of the students who excel in accounting, marketing, or finance will spend most of their careers working for entrepreneurs—people who were better at seizing opportunity than taking classroom examinations.

Entrepreneurship students should try not to be too concerned about their grades. Consider the story of Fred Smith, founder of Federal Express. It is said that when he took the entrepreneurship course in which he proposed a nationwide delivery system for packages that would compete with the U.S. Post Office, he received a grade of "C" for his efforts, suggesting that at times teachers of entrepreneurship have limits to their vision as well. The true test of entrepreneurial potential is in the marketplace, not in the classroom.

SUMMARY

The future is full of entrepreneurial opportunities, and new venture creation and entrepreneurship are changing the face of the world's businesses and economies. Historically, entrepreneurship has taken many different turns. In today's market-based economies, new venture creation is the key to technological and economic progress. Through entrepreneurship, people will continue to live better, longer, and more rewarding lives.

We have defined *entrepreneurship* as the creation of an innovative economic organization (or network of organizations) for the purpose of gain or growth under conditions of risk and uncertainty. This definition enables us to make distinctions between entrepreneurship and other wealth- and income-generating activities.

Although entrepreneurs and entrepreneurship have been studied from many different perspectives, we take an economic and managerial perspective in this book. The guiding framework for our discussion and analysis of entrepreneurial opportunities is the resource-based theory of sustainable competitive advantage. This theory enables us to understand what is unique about the new venture and how the new enterprise will create value for its customers and subsequently its founders. The managerial dimensions of entrepreneurship are individuals, environments, and organizations. These dimensions provide us with a useful organizing framework with which to view the complex forces and interactions that produce entrepreneurial activity.

DISCUSSION QUESTIONS

1. What would it be like to work for an entrepreneurial firm? Compare this to working for a *Fortune* 500 firm. Give examples from your own experience.
2. What are Schumpeter's definitions of an entrepreneurial new venture? Give examples of businesses you know that meet these criteria. How are these firms regarded in our society? By the media?
3. What kinds of uncertainty do you have in your life? Are these uncertainties comparable to the types faced by entrepreneurial firms? What are your coping strategies?
4. What kinds of changes might have to occur in countries like North Korea or Cuba to make them more accessible to entrepreneurs?

5. What kind of American-style ventures do you think would prosper abroad, especially in those countries with a low level of economic freedom? Provide examples.
6. What are Drucker's seven sources of opportunity? Provide examples of each. Which seem to be the easiest, hardest to find?
7. Why doesn't being smart easily translate into being rich?
8. How do entrepreneurial dimensions of individuals, environments, and organizations interact to produce new ventures?
9. Discuss the different forms of quality. Why is quality important for an entrepreneur?
10. What is value? How is it created? Provide examples of value products that you use and enjoy. What makes these special to you?

KEY TERMS

Creation
Economic organization
Entrepreneurship
Ethics
Gazelles
New venture creation
Opportunity analysis
Quality
Resource-based theory
Risk
Uncertainty
Value
Virtual organization