

# ***Entrepreneurship***

***Third Edition***

**William D. Bygrave**

Babson College

**Andrew Zacharakis**

Babson College

**WILEY**

# CONTENTS

i.

Preface vii

## 1. The Power of Entrepreneurship<sup>1</sup> 1:

- Entrepreneurship and Small Business in the United States 2
  - Entrepreneurial Revolution 4
  - 'Web: Three Revolutions Converge 8
  - Entrepreneurship Revolution Strikes Gold 9
  - Creative Destruction 11
- Causes of the Entrepreneurial Revolution 12
  - Changes in the Entrepreneurial Framework Conditions 14
  - Churning and Economic Growth 17
- Global Entrepreneurship Monitor 19
- Principal Findings from GEM 19
  - Activity 20
  - Necessity- and Opportunity-Driven Entrepreneurs 20
  - Age Distribution 23
  - Gender Differences 23
  - Growth Expectations and Job Creation 24
- 21st-century Economies: Anglo-Saxon or Social Models? 26
  - Conclusion 28
  - Your Opportunity Journal 29
  - Web Exercise 29
  - Notes 29
- A CASE: ALISON BARNARD 35

## 2 The Entrepreneurial Process 47

- Critical Factors for Starting a New Enterprise 48
  - Personal Attributes 50
  - Environmental Factors 50
  - Other Sociological Factors 52
- Evaluating Opportunities for New Businesses 54
  - The Opportunity 55
  - The Customer 56
  - The Timing 56
  - The Entrepreneur and the Management Team 58
  - Resources 58
- Determining Resource Needs and Acquiring Resources 59
  - Startup Capital 61
- Profit Potential 63
- Ingredients for a Successful New Business 65 **j**
  - Conclusion 67
  - Your Opportunity Journal 67
  - Notes 67 **k**
- Ⓜ CASE: VERA BRADLEY 69

## 3 Opportunity Recognition/Shaping, and Reshaping 79

- From Glimmer to Action: How Do I Come Up with a Good Idea? 80
  - Finding Your Passion 80
  - Idea Multiplication 82
- Is Your Idea an Opportunity? 86
  - The Customer 86
  - The Competition 97
  - Suppliers and Vendors 100
  - The Government 101
  - The Global Environment 101
  - The Opportunity Checklist 101
- "I Don't Have an Opportunity" 101
  - Conclusion 103
  - Your Opportunity Journal 104
- HI Web Exercise 104
  - Notes 104
- 3 CASE: JIM POSS 107

## 4 Understanding Your Business Model and Developing Your Strategy 121

- The Business Model 121
  - The Revenue Model 122
  - The Cost Model 125
- The First-Mover Myth 127
- Formulating a Winning Strategy 129
  - The People Are What Matters 130
  - Entry Strategy 132
  - Growth Strategy 135
- Conclusion 143
- Your Opportunity Journal 143
- Web Exercise 143
- Notes 144
- Ⓜ CASE: ZUMBA FITNESS 146

## 5<sup>1</sup> Entrepreneurial Marketing -157

- Why Marketing Is Critical for Entrepreneurs 158
- Entrepreneurs Face Unique Marketing Challenges 158
- Acquiring Market Information 159
- Marketing Strategy for Entrepreneurs 161
  - Segmentation, Targeting, and Positioning 161
  - The Marketing Mix 162
- Guerrilla Marketing 175
- Marketing Skills for Managing Growth 176
  - Understanding and Listening to the Customer 176
  - Building the Brand 177 **'**
- Conclusion 178

## iv | Contents

- Your Opportunity Journal 178
- Web Exercise 179
- Appendix: Customer Interview 179
  - General Outline: It Needs to Be Tailored to Meet Your Research Needs 179
- Notes 180
- A CASE: Eu YAN SANG INTERNATIONAL, LTD. 182

## 6 Building the Founding Team 197

- Power of the Team 198
- Where Do You Fit? 199
- How to Build a Powerful Team 203
- Bootstrapping: Building the Team Based on - Stage-of-Venture Life 205
- Compensation 206
  - Equity 206
  - Salary 211
  - Other Compensation Considerations 211
- External Team Members 212
  - Outside Investors 212
  - Lawyers 212
  - Accountants 213
  - Board of Advisors 214
  - Board of Directors 214
- Keeping the Team Together 215
  - Burnout 216
  - Family Pressure 217
  - Interpersonal Conflicts 217
- Conclusion 217
- Your Opportunity Journal 218
- Web Exercise 218
- Notes 218
- a** CASE: ZEO, INC. 221

## 7 The Business Planning Process 235

- The Planning Process 237
- The Story Model 239
- The Business Plan 240
  - The Cover 240
  - Executive Summary 241
  - Table of Contents 241
  - Industry, Customer, and Competitor Analysis 242
  - Company and Product Description 246
  - Marketing Plan 247
  - Operations Plan 251
  - Development Plan 252
  - Team 253
  - Critical Risks 255
  - Offering 257
  - Financial Plan 257
  - Appendices 257
- Types of Plans 257
- Style Pointers for the Written Plan and Oral Presentation 258
- Conclusion 259
- Your Opportunity Journal 260
- Web Exercise 260

- Notes 260
- A CASE: P'KOLINO 261

## 8 Building Your Pro-Forma Financial Statements 305

- Common Mistakes 306
- Financial Statement Overview 307
- Building Your Pro-Forma Financial Statements 308
  - Build-Up Method 308
  - Revenue Projections 309
  - Cost of Goods Sold 311
  - Operating Expenses 312
  - Preliminary Income Statement 314
- Comparable Method 315
- Building Integrated Financial Statements 317
  - Income Statement 318
  - Balance Sheet 320
  - Cash-Flow Statement 321
- Putting It All Together 321
  - Conclusion 323
  - Your Opportunity Journal 323
  - Web Exercise 324
  - Notes 324
- a** CASE: P'KOLINO FINANCIALS 325

## 9 Financing Entrepreneurial Ventures Worldwide 337

- Entrepreneurial Financing for the World's Poorest 338
  - Microfinancing 338
  - Microcredit for the Poorest of the Poor 339
- Entrepreneurs and Informal Investors 339
  - Amount of Capital Needed to Start a Business 341
  - Characteristics of Informal Investors 344
  - Financial Returns on Informal Investment 344
  - Supply and Demand for Startup Financing. 345
- Venture Capital 346
  - Classic Venture Capital 347
  - Importance of Venture Capital in the U.S. Economy 349
  - Mechanism of Venture Capital Investing 351
  - Financial Returns on Venture Capital 353
  - Venture Capital in Europe 355
- Factors Affecting Availability of Financing 356
  - Total Entrepreneurial Activity and Informal Investing 356
  - Factors Affecting Informal Investing 356
  - Factors Affecting Classic Venture Capital 356
- Conclusion 357
- Your Opportunity Journal 357
- Web Exercise 358
- Notes 358
- A CASE: DAYONE 360

## 10 Raising Money for Starting and Growing Businesses 379

- 5 Jim Poss, BigBelly Solar 379
- Bootstrapping New Ventures 380
- Valuation 381
  - Earnings Capitalization Valuation 381
  - Present Value of Future Cash Flows 382

Market-Comparable Valuation (Multiple of Earnings) 382	Obtaining Bank Loans Through Accounts Receivable Financing 436
Asset-Based Valuation 383	Pledging 436
Example of Market-Comparable Valuation 383	Pledging with Notification 436
Asset-Based Valuation Example 385	Factoring 436
Financing a New Venture 386	Recourse 437
Informal Investors 387	Obtaining Loans against Inventory 437
Business Angels 389	Obtaining "Financing" from Customer Prepayments 438
Searching for Business Angels 391	Choosing the Right Mix of Short-Term Financing 438
Types of Business Angels - 391	Traditional Bank Lending: Short-Term Bank Loans 438
Putting Together a Round of Angel Investment 392	Maturity of Loans 439
Venture Capital 394	Interest Rates 439
Candidates for Venture Capital 394	Collateral 440
Ideal Candidates for Venture Capital, 395	Applying for a Bank Loan 441
Actual Venture-Capital-Backed Companies 395	Restrictive Covenants 441
Dealing with Venture Capitalists 397	General Provisions 442
Negotiating the Deal 398	Routine Provisions 442
Follow-On Rounds of Venture Capital 399	Specific Provisions 443
Harvesting Investments 400	Equipment Financing 443
Initial Public Offering 400	Obtaining Early Financing from External Sources 443
Pros and Cons of an IPO 401	SBA-Guaranteed Loans 444
The Process of Going Public 403	Applying for an SBA Loan 444
BFWS Goes Public 405,	Planning Cash Flow and Planning Profits 445
Selling the Company" 405	H Conclusion 446
A Strategic Acquisition: LowerMyBills.com 405	<b>B Your Opportunity Journal 447.</b>
Why Be Acquired? ' 407	- Web Exercise 447
- Conclusion 408	- Notes 447
- Your Opportunity Journal 409	A CASE: FEED RESOURCE RECOVERY 449
- Web Exercise 409	
- Notes 410	
<b>a CASE: METACARTA: GROWING A COMPANY, DO WE TAKE THE VC MONEY? 413</b>	
<b>11 Debt and Other Forms of Financing 423- &gt;</b>	<b>112 Legal Issues,' Including Intellectual Property,* 463'</b>
Getting Access to Funds—Start with Internal Sources 423	Why, When, and How to Choose an Attorney 463
Start with Credit Cards and Home Equity Lines 424	Leaving Your Present Position 464
Cash Conversion Cycle 425	Corporate Opportunity 464
Working Capital: Getting Cash from Receivables and Inventories 426	Recruitment of Fellow Employees 464
Using Accounts Receivable as Working Capital 427	Noncompetition 465
The Sales Pattern 428	Intellectual Property 466
Cash versus Credit Sales 428	The Basics: What Is Protectable and How Should It Be Protected? 467
Credit Policies 428	Patents 467
Setting Credit Terms 429	Trade Secrets 472
Collection Policies 430	Trademarks 474
Setting Credit Limits for Individual Accounts 431	Copyright 476
Inventory 432	International Protection for Intellectual Property 477
Sources of Short-Term Cash: More Payables, Less Receivables 433	Choice of Legal Form 479
Cash from Short-Term Bank Loans 433	Control 480
Cash from Trade Credit 434	Personal Liability 481
Cash Obtained by Negotiating with Suppliers 434	Taxation 482
Cash Available Because of Seasonal Business Credit Terms 434	Initial Investment of the Founders 483
Advantages of Trade Credit 435	Administrative Obligations 484
Cash Obtained by Tightening Up Accounts Receivable Collections 435	Choosing a Name 484
	Stockholders' and Operating Agreements 485
	Negotiating Employment Terms 485
	Disposition of Equity Interests 485
	Legal and Tax Issues in Hiring Employees 488
	Employees as Agents of the Company 488
	Employment Discrimination 489
	Employment Agreements 489

## vi | Contents

- Raising Money 489
  - Conclusion 491
  - Your Opportunity Journal 491
  - Web Exercise 492
  - Notes 492
- a** CASE: TESSERA 493.

### 13 Entrepreneurial Growth 501

- Making the Transition from Startup to Growth 502
  - Looking Forward: The Choice to Grow, or Not,...or Sell 502
- A Model of Driving Forces of Growth 504
- The Growth Process 505
- Execution 505
  - Instituting Controls 507
  - Tracking Performance 508
  - Managing the Cash Cycle 510
  - Leveraging the Value Chain 512
  - Maintaining the Entrepreneurial Organization 513
- Opportunity Domain 513
- Organizational Resources and Capabilities 516
  - Obtaining Financial Resources for the Growing Company 517
  - Intangible Resources and Capabilities 517
- Leadership 519
  - Starting the Delegation Process 519
  - First-Level Management 520
  - From Delegation to Decentralization 521
  - Professional Management and Boards 521

- Coordinating the Driving Forces 522
  - Leading People; Developing Entrepreneurs 522
- Conclusion 523
- Your Opportunity Journal 524
- Web Exercise 524
- Notes 525
- a** CASE: LAZYBONES 526

### 14 Social Entrepreneurship 535

- Introduction 535
- The Rise in Social Entrepreneurship 536
- Social Entrepreneurship Defined 538
- A Social Entrepreneurship Typology 538
  - 1. Traditional Venture 540
  - 2. Social Consequence 540
  - 3. Social Purpose Venture 540
  - 4. Enterprising Nonprofit. 541
- Hybrid Ventures 542
  - Choosing Your Venture Type 545
- Measuring Impact 547
  - Conclusion 548
  - Your Opportunity Journal 549
  - Web Exercise 549
  - Notes 550
- a** CASE: YEAR UP: WORKFORCE TRAINING FOR URBAN YOUTH 552
- Glossary 569
- Index 579