

GEMBA

November 16, 2011

Entrepreneurship Workshop

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Objectives for the Day

Conversation about:

- What constitutes an entrepreneurial opportunity?
- How do you formulate a plan for a new venture?
- What does good execution look like in a start up?
- Maybe a discussion of some new ideas

Plan for the Day

- Entrepreneurship framework
- Starbucks
- Entrepreneurial opportunity
- Planning: strategy and operating plan
- Zaplet
 - (Execution discussion)
- New business ideas

Format: Team discussion & presentations

Resources

Guidelines for the entrepreneur:

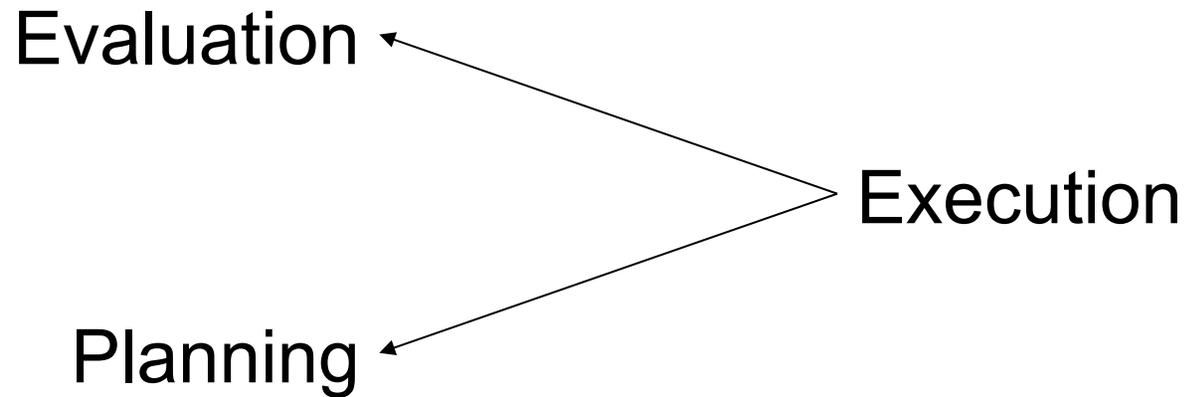
<http://www.dukeven.com/>

Program for Entrepreneurs:

<http://www.dukep4e.org>

(find a link to the EMBA concentration process here)

The Basics



Framework for Analysis

Investment prospectus:

- Team
- Need/problem
- Solution
- Competitive advantage
- Risk / return

Company's plan:

- Strategy:
 - Target customers
 - Business model
 - Position
 - Milestones
- Operating plan:
 - Plan for each functional area
 - Budget

Execution:

- Market Research
- Strategy development
- Marketing
- Business development
- Sales planning
- R&D Management
- Operations management
- Process and infrastructure management
- Budgeting
- Financing
- People management

Teams

Team 1

Chandra

Nak. Rao

Periyadan

Romanov

Saginov

Scherb

Toxe

Team 2

Adams

Andreykin

Cheung

Coleman

Falbo

Karabulut

Maragos

Rajagopalan

Team 3

Ayala

Bhandare

Chew

Huber

Kurdziel

Qayed

Strappa

Team 4

Aspero

Bell

Curry

Estrada

Glushakov

Hesler

Li

Taylor

Questions

Starbucks

- How would you pitch the 1985 ask for \$400,000 (p. 9)?
- What was Starbucks strategy and why was it successful?

Zaplet

- Why did it fail?
(No opportunity, bad strategy/plan, bad execution?)
- Could anything have been done to make Zaplet succeed?

OPPORTUNITY EVALUATION

The Team

“This story illustrates my thesis that strategy is easy, execution is hard.” (Arthur Rock, 1987)

Therefore, invest in people.

Team capabilities

- Careful observers
- Creative
- Disciplined doers
- Team players

Individual capabilities

- Competence (technical & managerial)
- Experience / network
- “Brutally honest”
- Question / listen / accept criticism
- **Driving energy**

Entrepreneurial Opportunity

- Problem currently not solved
- Potential for change in consumption

Requires:

- Innovation
- Capability to exploit the innovation

Not every idea is an opportunity

Sources of Opportunity

Society

- Changing demographics
- Changing tastes & interests
- Fears & hopes
- Regulation

Technology

- Innovation: new combinations
- New technologies
- New knowledge

Markets

- Change in regulation
- Supply chain disruption
- Inefficiencies

Order Effects

First order: Substitution - faster, better cheaper

Second order: More of the underlying task or capability

Third order: Creation of new structure, institutions, organizations, etc.

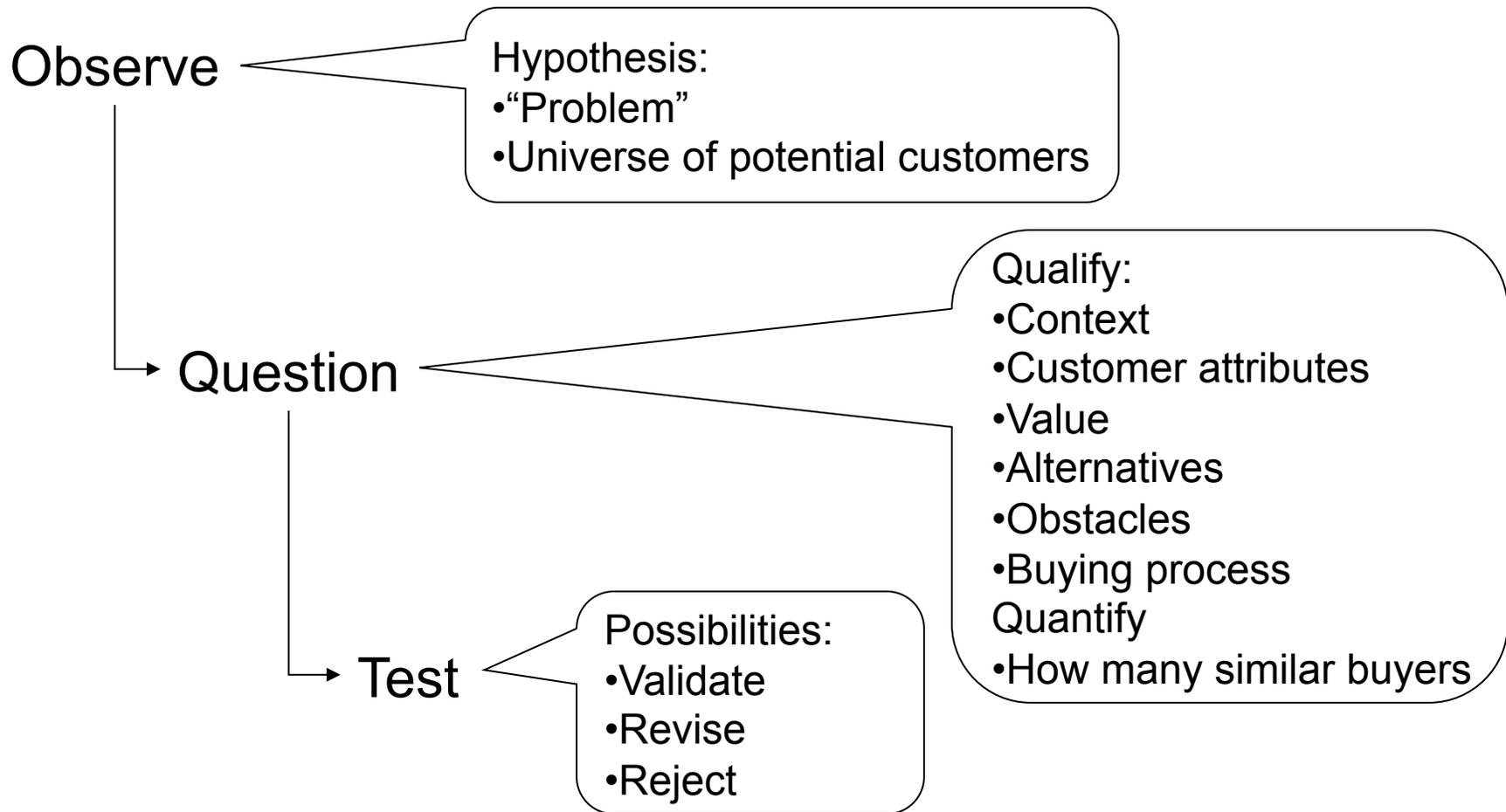
Entrepreneurial opportunities exist at all levels and for those who can solve new problems created by new structures, etc.

How Do you Start?

“You can observe a lot by just watching.”

(Paraphrase of a famous philosopher)

How to Conduct Primary Market Research



Evaluation of an Opportunity

1. Is there a sufficiently attractive market opportunity (need or problem)?
2. Is the proposed solution feasible, both from a market perspective and a technology perspective?
3. Do we have an team that can effectively capitalize of this opportunity?
4. Can we compete (over a sufficiently interesting time horizon)?
5. What is the profile risk and return of this opportunity?

Core Elements of a Business Plan Document

Investment prospectus:

- Team
- Need/problem
- Solution
- Competitive advantage
- Risk / return

NEW VENTURE PLANNING

Planning

1. Strategy

- Target customers
- Business model
- Position / competitive advantage
- Objectives

2. Operating plan

- Plan for each functional area
- Budget

Business Plan Document

Investment

prospectus:

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- People management

Strategy in a New Venture

- Similar but different
- More and less freedom

Compared to corporate strategy

New Venture Strategy

1. Target customers

- Who are the candidates?

2. Business model

- What are the options?

3. Sustainable competitive advantage

- How can you compete over the long term?
- What investments should you make?

4. Objectives / milestones

- What is the order of execution?
- How do you structure financing?

These questions are all linked.

The process is iterative and piecemeal, not sequential

Target Customers

Start with formulating a choice:

- Who are potential targets?
 - XYZ corp. & ABC corp.
- What do they represent?

Considerations:

- What is the required solution? Can we deliver?
Does it strengthen us?
- Ease of implementation for the customer
- Decision process
- Size of opportunity represented

A Conceptualization

Value/
Differentiation

Good

Bad

Difficulty / cost to
the company

Size of market also a consideration

Understanding the Market

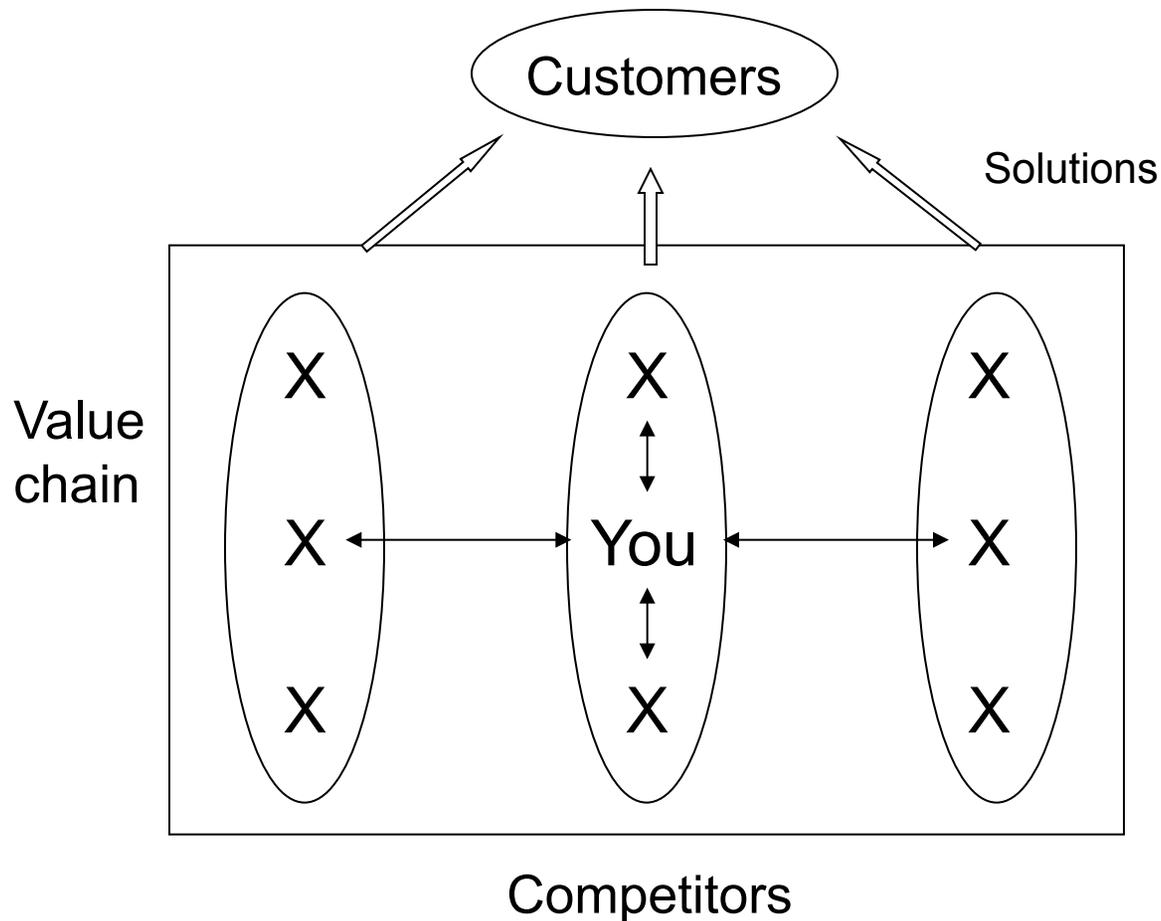
What are you trying to achieve?

- What is the pain and how severe is it?
- What are the customers' alternatives?
- How many customers?
- How much will they pay you?
- For exactly what product?
- How will you convince them to buy?

Business Model

- What is the “whole product”?
 - How will it get to the customer?
 - What will your role be?
- What is the perceived value?
- What will customers pay for?
- How do they want to pay?

Position



How much and what part of the solution will you provide?

- Core competencies
- Business relationships

How are you uniquely identified?

What is defensible?

- Core competencies
- Messaging
- Plans

Competitive Position

Objective: Sustainable competitive advantage

What is competitive advantage?

- Something that allows the firm to deliver value to the customer profitably
- (implies that the firm does it better than competitors)

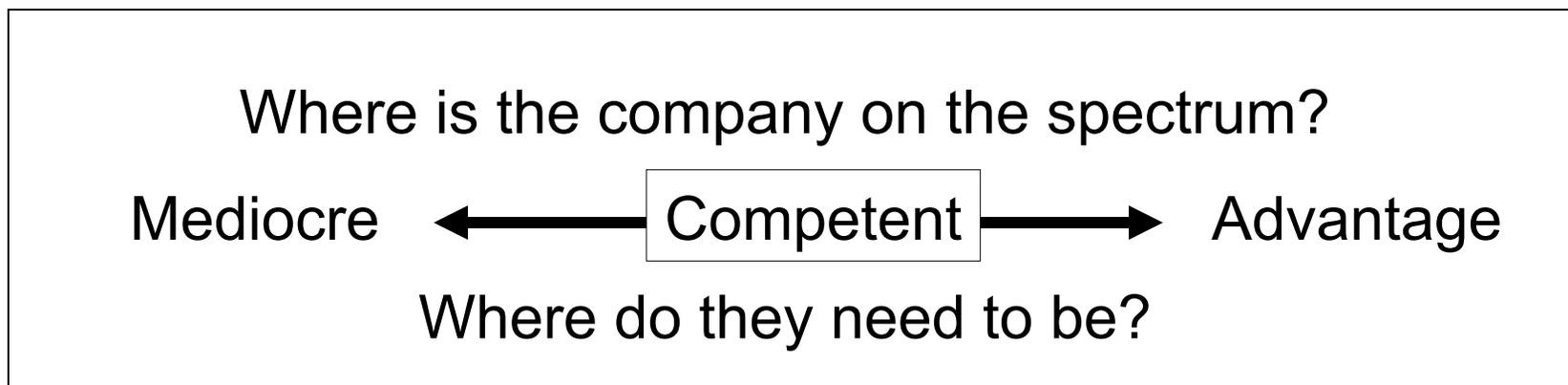
What is *sustainable* competitive advantage?

- A competitive advantage that is hard to imitate or innovate around

Competencies

Firms do many things

- Design / develop
- Manufacture
- Market
- Sell
- Service
- Hire
- Innovate
- Strategize
- Plan
- Respond to changes



Innovation

Sustaining:

- Make a product or service perform better in ways that customers in mainstream market value
- Always introduced by incumbents

Disruptive:

- Create an entirely new market
- Perform worse on some dimension important to mainstream
- Lower margin

Objectives

Basic question: Will your venture succeed?

Imagine a series of big steps that increase your confidence

- E.g.: a customer, validation of technology, selling model

These steps can constitute a series of objectives for the venture:

- And become the milestones in your financing plan

Digression: What Can Go Wrong?

1. Nobody wants what you are selling.
2. Somebody wants it, but they don't represent a real market.
3. People want it, but for some reason they can't buy it or can't use it.
4. People want it, but you can't get it to them (economically).
5. The technology doesn't work.
6. The technology works but you can't protect it.
7. The technology works but you can't get it into a reasonable product.
8. You build a bad product.
9. You can't build your product for a low enough cost.
10. Somebody introduces a better product.
11. Somebody has the power to stop you and exercises it.
12. You need somebody else in the value chain to do something and they don't.
13. You can't find the right people.
14. You just don't execute on something important.
15. Etc.

Risk

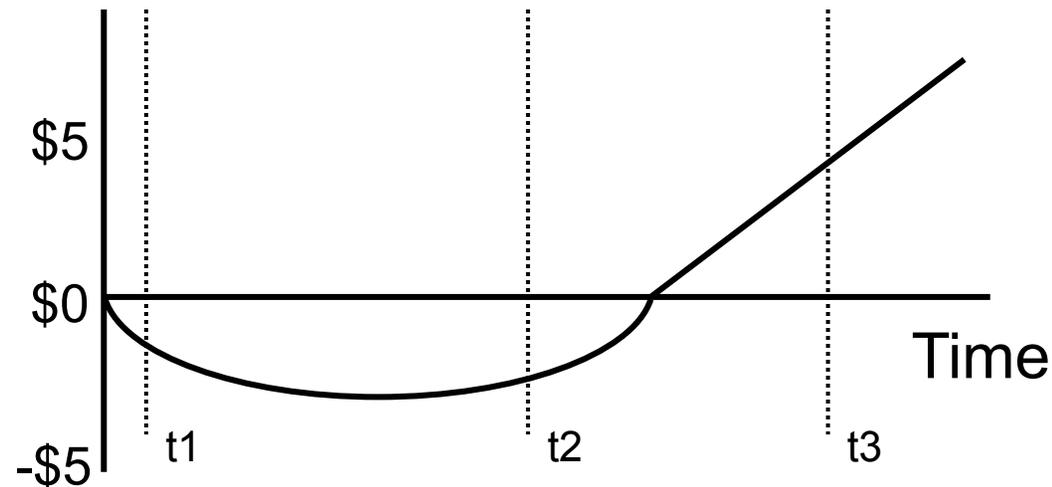
- Risk derives from one of these bad things happening.
- Not all bad things have the same negative impact.
 - Some are life threatening.
 - Some just reduce the likely return.
- The relevant operating notion is:
Probability of adverse event
X Negative impact

Lowest Cost Resolution of Uncertainty

Theoretically, you could:

1. Rank order the points of uncertainty in decreasing order of risk to the venture.
2. Conceive a plan that resolves each point of uncertainty for the lowest cost (time and money) – think of this as performing an experiment.
3. Factor in any issues of overall timeliness and interdependencies.
4. Use this outline as a framework for your plan.
5. Make corrections as you learn.

How much Money Do You Need?



- Should you raise the total amount of cash needed (according to projections) in a single investment?
Usually not
- How much is the business worth?
- What increases the value of the company?
Reduction of uncertainty

How Much Money Should You Raise or Invest?

1. Establish a plan (which you will end up revising):
2. Determine a milestone that produces a step up in valuation - what will remove the (a?) main source of uncertainty?
 - (Keep in mind that investment may be tranced)
3. Determine cash needs
 - Including asset based financing to reduce requirement for equity based financing
4. Raise enough to get you to the next milestone that would cause step up in valuation (+ small cushion, if possible)

OPERATING PLAN & FORECASTING

What is a Forecast?

Projection of future revenue

Revenue = # of customers X ave. revenue/customer

**Revenue = # of prospects X probability of success
X ave. revenue/customer**

**Revenue = # of prospects at time t (months before rev.)
X probability of success
X ave. revenue/customer**

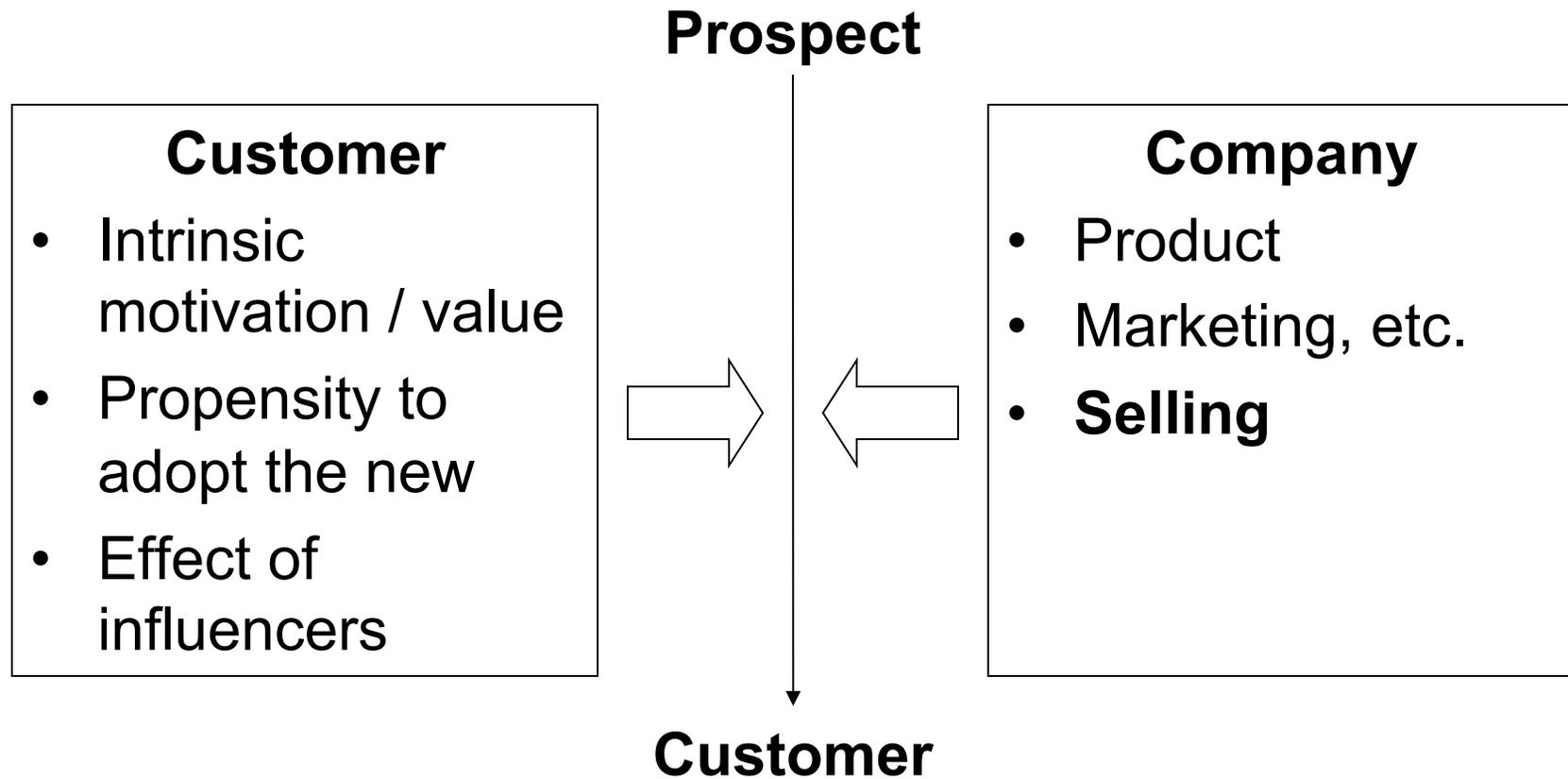
The Basic Questions

1. How many prospects?
 - Changes over time
2. What is the probability of conversion?
3. How long does the conversion take?
4. What is the average revenue per customer?

What Is a Prospect?

- A prospect (or 'lead') is a customer who fits a profile that you have created.
- Your business may have different profiles, so different classes of prospects.

What Determines Probability?



Length of Time

- This is primarily determined by the customer's
 - Buying process / cycle
 - Degree of urgency / strategic alignment
- (The length of time will be influenced by your selling effort.)
- In the case of a corporate customer, the decision process involves a set of discrete steps.

Average Revenue

- Easiest of many hard things to estimate, but still not easy
- If not a single discrete decision,
 - Value
 - Pace of adoption
 - Organizational issues

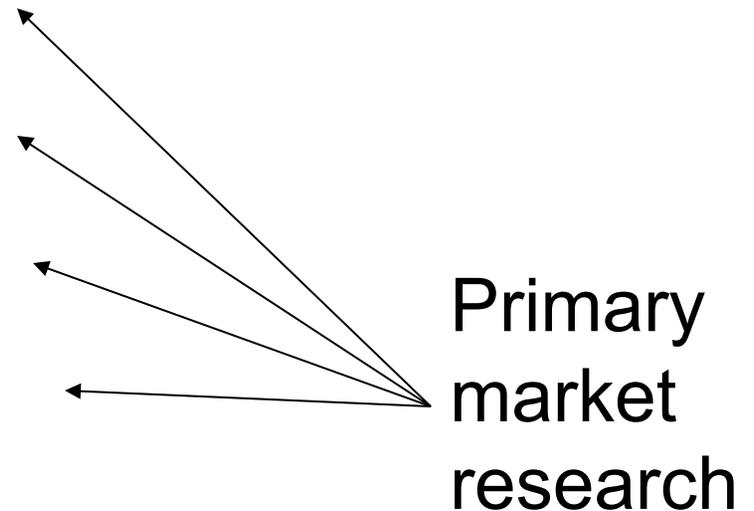
Role of Market Research

Revenue =

**# of prospects at time t
(months before rev.)**

X probability of success

X ave. revenue/customer

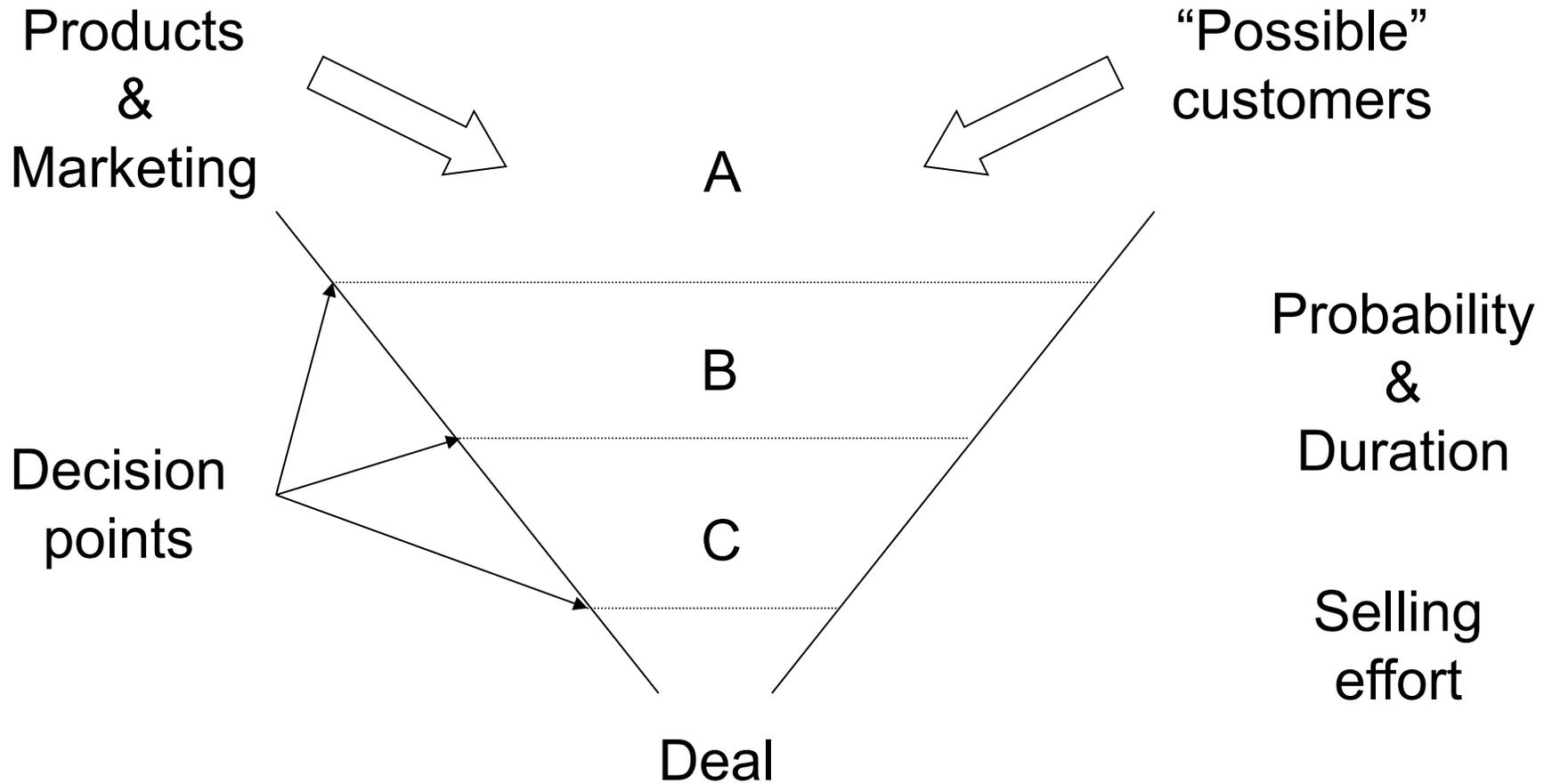


Selling Process

1. Establish a customer profile
2. Identify leads (as economically as possible)
3. Qualify leads (as economically as possible)
4. Move the potential customer through the process in a structured fashion

This is best managed by a professional.

A Model

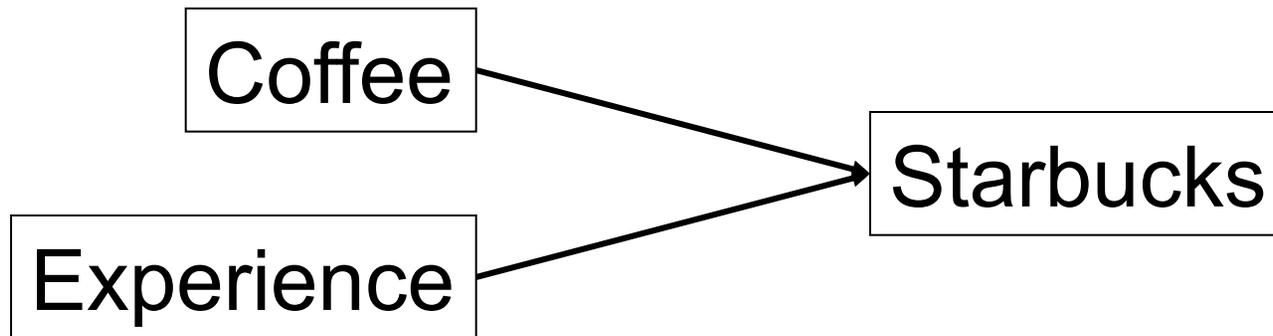


A Couple of Principles

- Build a model
- This drives your budget.
- Measure and revise!!

CASES

The Starbucks Opportunity



Supported by demographics:

- Income growth
- Financial security
- Focus on gratification

Is this a Business?

- Key driver: economics of one coffee shop
- Raised seed funding to prove the concept
- If valid, the rest was all about growth
 - More stores
 - More products

Key Insights

- Opportunity itself
 - Validated by market growth
- People - critical in service business
- Importance of brand
- Quality
- Demand creation: “word of mouth”
- Infrastructure & processes to support growth

Engine of Success

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Sustainable competitive advantage

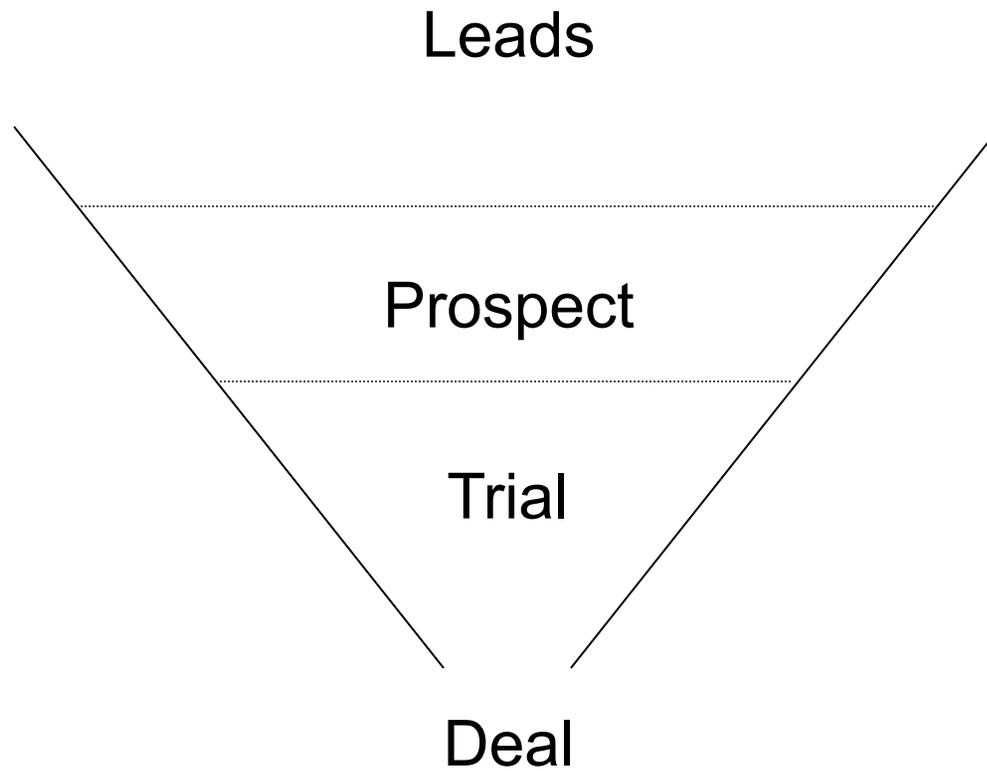
Zaplet

- Sales
- Financing
- People
- Competition
- Strategy

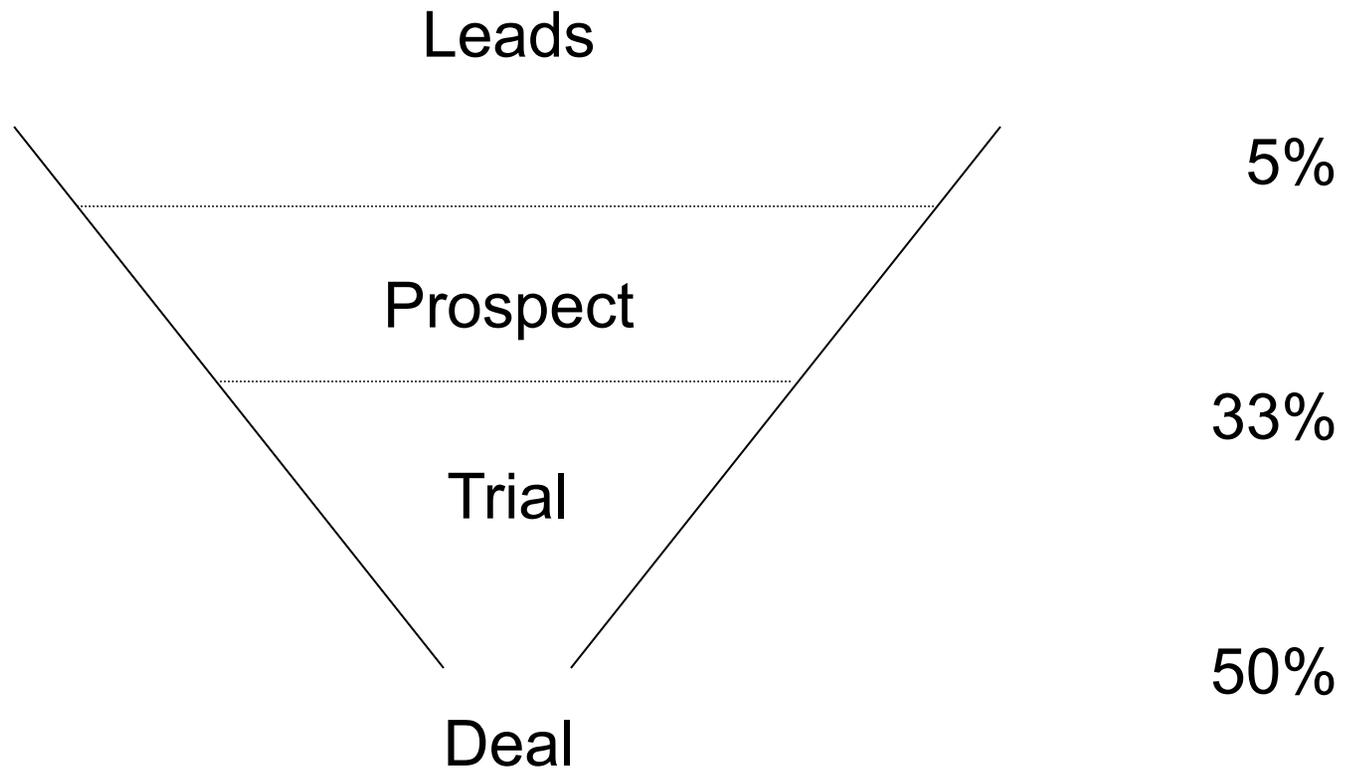
Zaplet Questions

- What mistakes did Zaplet make?
- What would you recommend to Alan Baratz?
- Could Zaplet have succeeded?

Sales Process



Conversion



Key Questions that Drive Sales Productivity

- Deal size
- Sales cycle (length of time the process takes to conclude)
- Sales effort (actual time engaged with the customer)
- Percentage promotion (from one stage to the next)

Sales Force Productivity

- Quota: \$1.2M
- 3 quarters ramp up to full productivity
- Activity per quarter:
 - 1 deal
 - 2 trials
 - 6 prospects
 - 120 leads

Are the assumptions reasonable?

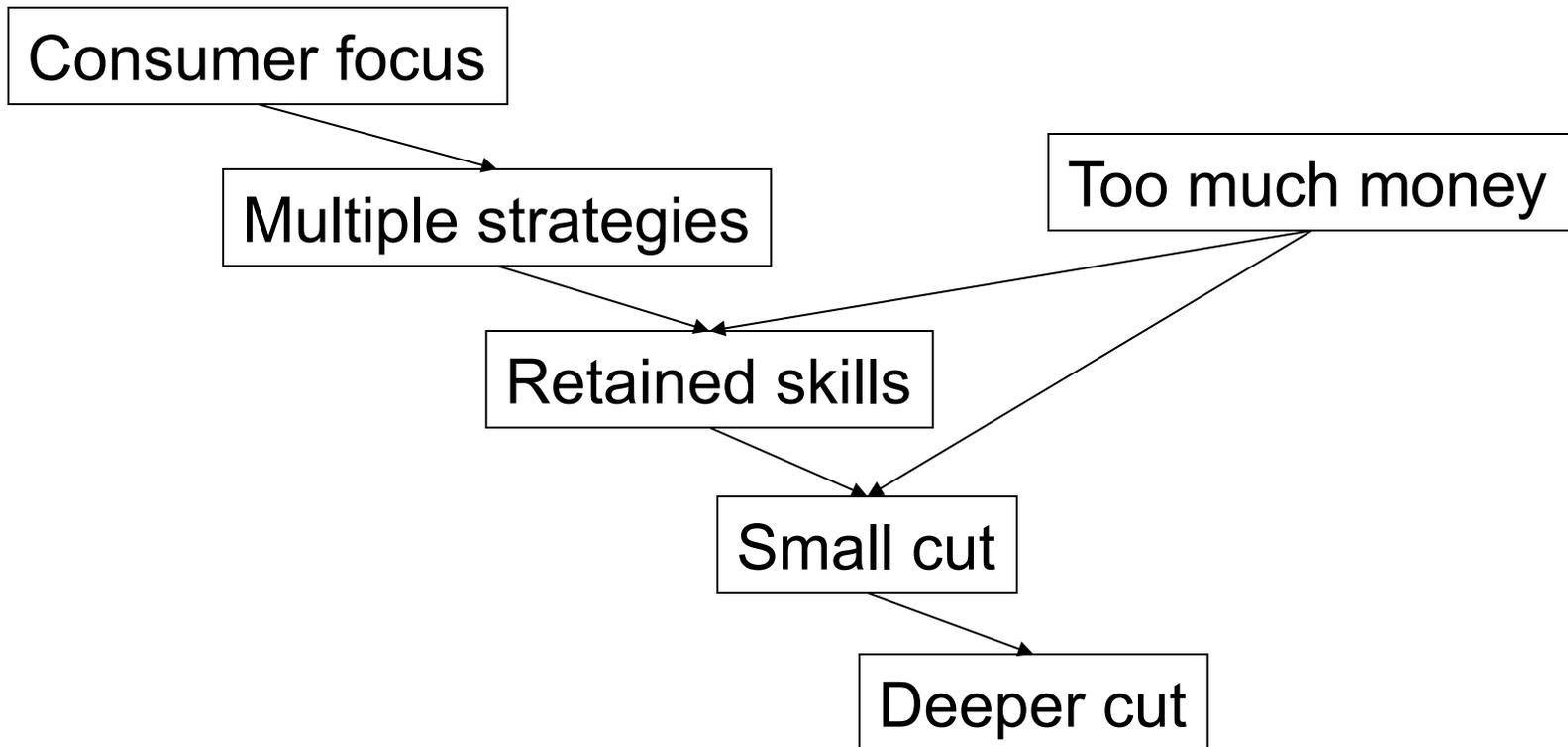
Zaplet Sales Productivity Assumptions

- Deal size:
 - Take average of department / division / enterprise
 - unrealistic and oversimplified
- Sales cycle:
 - Did not consider customer budgeting cycle
- Sales effort:
 - Aggressive / no effort to verify
- Percentage promotion:
 - Aggressive / no effort to verify

Financing

- The next big thing
 - KP then the rest of Sand Hill Rd.
 - 11/99: 1st round:
 - \$5M
 - 10/00: 2nd round:
 - \$90M & it could easily have been more
-
- Zaplet could afford a \$14M per quarter run rate - was this justified & was it good for the company?

People Management



People Questions

- What were the people related consequences of the multiple strategies & strategy shifts?
- How were the downsizings managed?
- What were the consequences of the downsizings?

Managing a Restructuring

- Two approaches
 - What can I cut? (Current budget is baseline)
 - What do I need? (Baseline is 0)
- Can downsizings be avoided?
 - Validate idea before staffing to implement
 - Assess people impact of change in strategy (and hire people who are flexible)
 - But the future is still unknown!

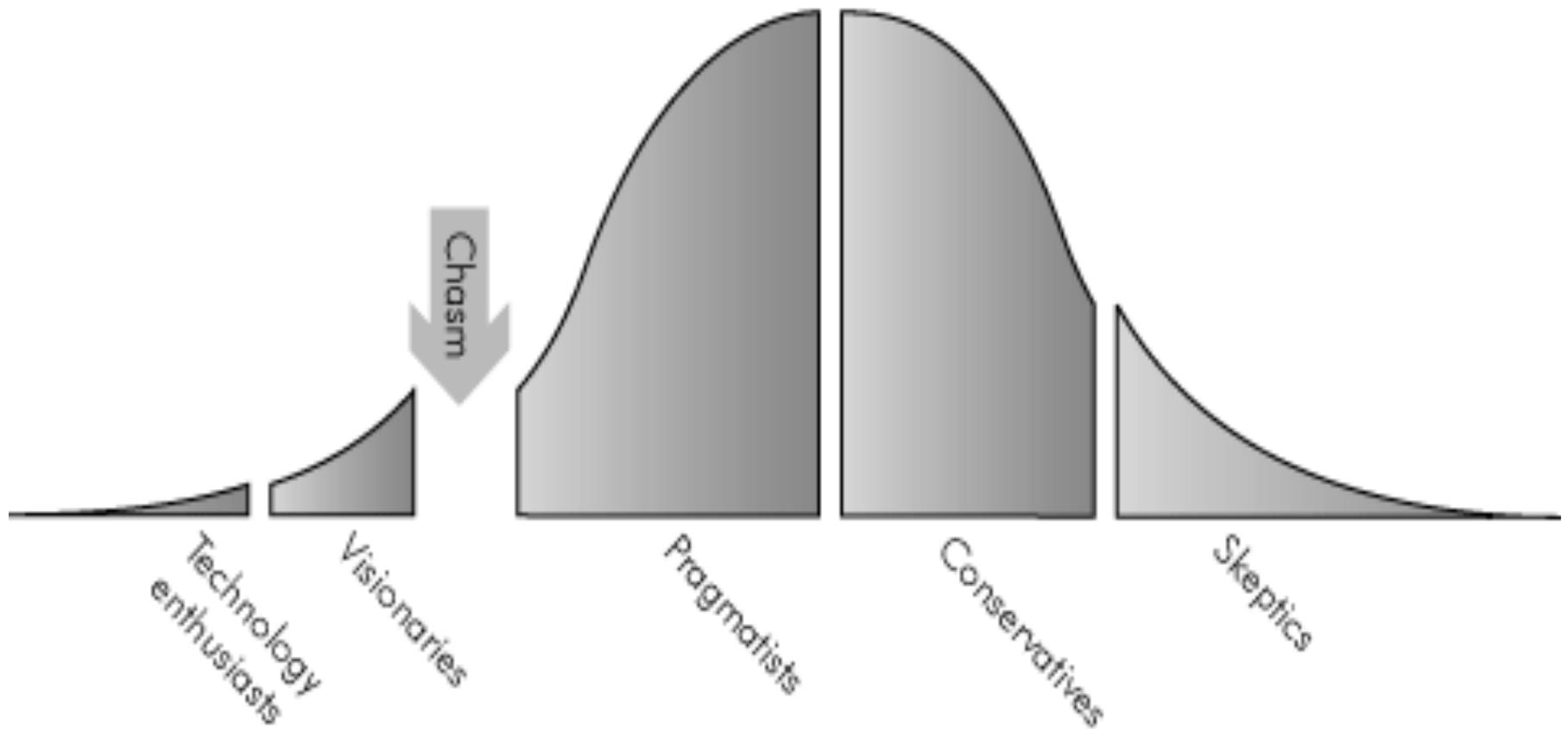
Zaplet: The Idea

- Cool?
- Useful?
- Usable?
- Valuable?

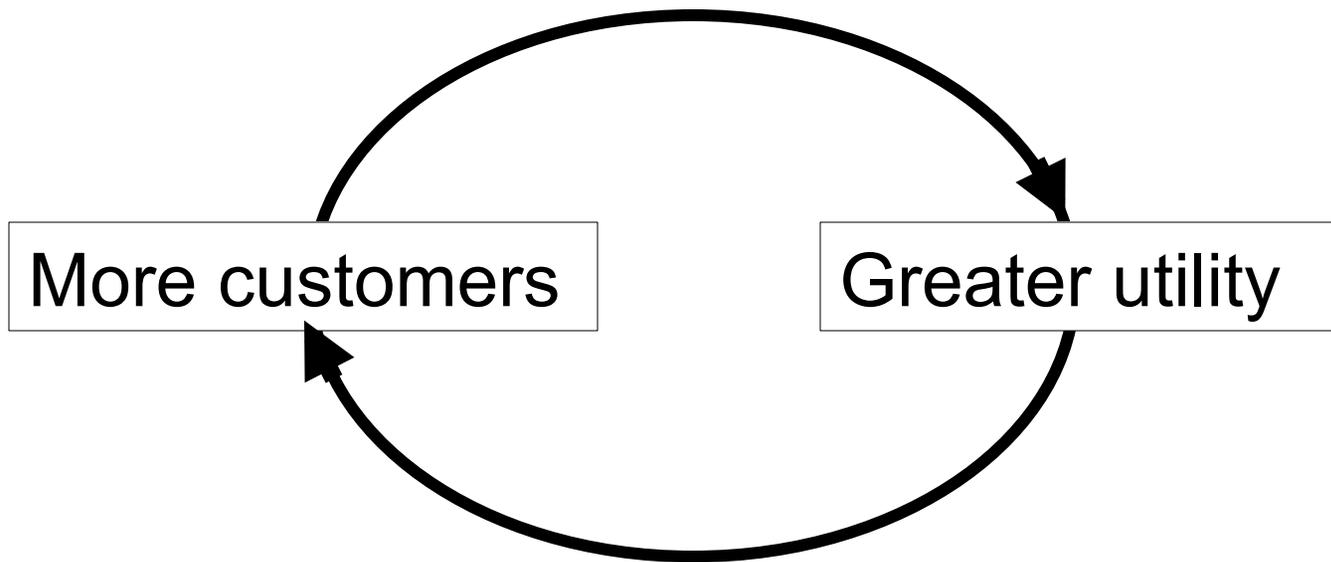
Customer

- Robert & Brian
- Consumer
- Larry Purpuro (RNC) “Dynamite in a box”
- Enterprise, but who?

Where Were Zaplet's Customers?



Network Effects



Did this apply to Zaplet?

Competition

- They didn't think they had any direct competition.
 - Was this good or bad for them?
- The closest competitors (“peripheral”) were CRM and SFA vendors.
 - Was there something they might have learned from this?

Strategy

Looking for focus:

1. Consumer
2. 5 business units
3. The enterprise

Positioning:

- Interactive email application
- “Collaboration for the unstructured portion of the day”
- “Collaborative business process management”

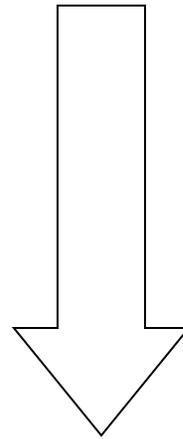
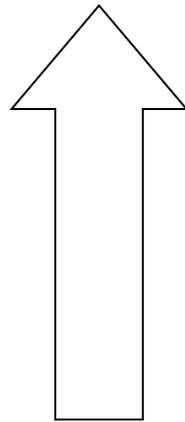
Why was this so hard?

Could the process have been better managed?

Horizontal vs Vertical

Infrastructure:

- OS
- Networking
- DB
-



Applications:

- Financial
- Engineering
-

Where do collaboration
tools fit?

Horizontal vs Vertical

	Horizontal	Vertical
Early buyer	<ul style="list-style-type: none">• Technologist	<ul style="list-style-type: none">• Business manager
Value proposition	<ul style="list-style-type: none">• General	<ul style="list-style-type: none">• Specific
Integrator	<ul style="list-style-type: none">• Customers	<ul style="list-style-type: none">• Vendor
Risks	<ul style="list-style-type: none">• No business case• Technology hurdles	<ul style="list-style-type: none">• Low return on engineering• Miss broader market

The Excuses

- Product “didn’t have all of the features it needed to have.”
- Market downturn
- Product becomes a “nice-to-have” rather than a “must-have.”
- Positioning:
 - “collaboration for the unstructured portion of the day”

Could a vertical strategy have succeeded for Zaplet?

Lessons

- No true focus on the customer
- No solution
- Did not raise hard questions & think through the consequences if things didn't work out

Summary & Discussion

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