**Chapter Outline**

**Spotlight: Shorts International**

**(http://www.shortsinternational.com)**

1. **Coming Up With Startup Ideas**

*Distinguish among the different types and sources of startup ideas* **Types of Startup Ideas**

* + - Exhibit 3-1 Types of Ideas That Develop into Startups
    - Type A ideas – Startup ideas centered around providing customers with an existing product not available in their market.
    - Type B ideas – Startup ideas, involving new technology, centered around providing customers with a new product.
    - Type C ideas – Startup ideas centered on providing customers with an improved product.

*Ask students if they know of examples of a startup (created from scratch). Ask students for businesses that fit each of these types of ideas.*

* + **Common Sources of Startup Ideas**

*Discuss circumstances that lead to ideas for starting a new business.*

* + - Exhibit 3-2 Common Sources of Startup Ideas (with percentages)

*Ask students if they have individual ideas for possible business startups.*

* + - Accidental Discovery such as Serendipity – A gift for making desirable discoveries by accident
    - Hobbies and Personal Interests – grow beyond leisure into business
    - Keeping An Eye On Change
      * Exhibit 3-3 (Drucker) Change-Based Sources of Entrepreneurial Opportunities
        + Industry or Enterprise Factors – The unexpected, the incongruous, process needs, structural change
        + External Factors – Demographics, Changes in perception, New knowledge
      * Change inspires innovation
    - Other Idea Leads
      * Personal contacts with potential customers and suppliers, professors, patent attorneys, former or current employees or co-workers, venture capitalists, and chambers of commerce
      * Visiting trade shows, production facilities, universities, and research institutes
      * Observing trends everywhere
      * Reading widely even though the materials doesn’t seem related can spark ideas
      * Reading articles on the creativity of entrepreneurs
      * Visiting the library and looking through Yellow Pages in other cities
      * Traveling to other states to visit entrepreneurs in your area of interest.
      * Searching the Internet for information.

1. **Using Innovative Thinking to Generate Business Ideas**

*Use innovative thinking to generate ideas for high-potential startups*.

* + **Suggestions for Search**
    - When it comes to ideas, borrow heavily from existing products and services or other industries
    - Combine two businesses into one to create a market opening
    - Begin with a problem in mind, or think of a “pain” that you can relieve.
    - Recognize a hot trend and ride the wave
    - Study an existing product or service and explore ways to improve its function
    - Think of possibilities that would streamline a customer’s activities
    - Consider ways to adapt a product or service to meet customer needs in a different way
    - Imagine how the market for a product or service could be expanded
    - Study a product or service to see if you can make it “green.
    - Keep an eye on new technologies
  + **Be open at all times for new ways to do business and new services and products**

1. **Using Internal and External Analyses to Identify Business Ideas**

*Describe external and internal analyses that might shape the selection of opportunities.*

* + **Outside-In Analysis**
    - General environment – the broad environment, encompassing factors that influence most businesses in a society
      * Economic trends - changes in the rate of inflation, interest rates, and even currency exchange rates which promote or discourage business growth
      * Sociocultural trends – societal currents that may affect consumer demand, opening up new markets and forcing others into decline
      * Political/legal trends – changes in tax law and government regulation that may pose a threat to existing companies or devastate an inventive business concept
      * Global trends – reflect international developments that create new opportunities to expand markets, outsource, and invest abroad
      * Technological trends – may spawn or wipe out new ventures
      * Demographic trends- population size, age structure, ethnic mix, and wage distribution
    - Industry environment – the combined forces that directly impact a given firm and its competitors
      * New competitors
      * Substitute products/services
      * Rivalry
      * Suppliers
      * Buyers
    - Competitive environment – the environment that focuses on the strength, position, and likely moves and counter-moves of competitors in an industry
      * Who would be the new venture’s current competitors?
      * What unique resources do they control?
      * What are their strengths and weaknesses?
      * How will they respond to the new venture’s decision to enter the industry?
      * How can the new venture respond?
      * Who else might see and exploit the same opportunity?
      * Are there ways to co-opt potential or actual competitors by forming alliances?
  + **Inside-Out Analysis**
    - Resources and Capabilities
      * Resources - The basic inputs that a firm uses to conduct its business
      * Tangible resources – Those organizational resources that are visible and easy to measure
      * Intangible resources – Those organizational resources that are invisible and difficult to assess
      * Capabilities – The integration of various organizational resources that are deployed together to the firm’s advantage
      * Competitive advantage – A benefit that exists when a firm has a product or service that is seen by its target market as better than those of competitors
    - Core Competencies
      * Core competencies – Those capabilities that provide a firm with a competitive edge and reflect its personality
      * Determining the core competencies is possible once there is an accurate view of their resources and capabilities
  + **Integrating Internal and External Analyses**
    - SWOT analysis – An assessment that provides a concise overview of a firm’s strategic situation that deals with Strengths, Weaknesses, Opportunities, and Threats

*Have students enter “SWOT Analysis” into Google and see the many possible formats SWOT analysis can take. Have them choose a format and use that format for the Case at the end of the chapter.*

* + - Provides a succinct view of current conditions – must be repeated periodically to check conditions

1. **Selecting Strategies That Capture Opportunities (Strategy – A plan of action that coordinates the resources and commitments of an organization to achieve superior performance)**

*Explain broad-based strategy options and focus strategies. Have students define strategy.*

* + **Broad-Based Strategy Options**
    - Cost-Based Strategy – A plan of action that requires a firm to be the lowest-cost producer within its market
    - Differentiation-Based Strategy – A plan of action designed to provide a product or service with unique attributes that are valued by consumers
  + **Focus Strategies**
    - A plan of action that isolates an enterprise from competitors and other market forces by targeting a restricted market segment
    - Focus Strategy Selection and Implementation
      * A decision regarding the direction a firm will take in relating to its customers and competitors
      * Implemented by
        + Restricting focus to a single subset of customers
        + Emphasizing a single product or service
        + Limiting the market to a single geographical region
        + Concentrating on superiority of the product or service
    - Drawbacks of Focus Strategies
      * A firm may become too specialized
      * Strategy guru Michael Porter) indicates four conditions that may cause a segmented market to erode
        + The focus strategy is imitated
        + Target segment becomes structurally unattractive because the structure erodes or because demand simply disappears
        + Target segment’s differences from other segments narrow
        + New firms sub segment the industry

1. **Is Your Startup Idea Feasible?**

*Assess the feasibility of a startup idea before writing a business plan.*

* + Feasibility analysis – A preliminary assessment of a business idea that gauges whether or not the venture envisioned is likely to succeed
  + Fatal flaw – A circumstance or development that alone could render a new business unsuccessful (see Exhibit 3-9 A Feasibility Analysis Framework)
  + **Market Potential** 
    - Includes buyers (current or potential customers) who have the ability to pay for the product or service and sellers who compete with one another by offering identical or similar products or services to the same general group of buyers
    - Feasibility analysis helps identify a potential trend that can support promising startup ideas
      * Macro-market analysis establishes boundaries including the number of customers target for study and their overall purchasing power and habits
      * Micro-market analysis ties idea to market niche that appears to offer acceptable prospects for growth and a path to market entry that seems to be protected from existing competition
  + **Industry Attractiveness**
    - Macro-level industry analysis used to establish overall attractiveness of the industry in which the startup will be established (see questions presented in the appendix to this chapter)
    - Micro-level industry assessment focused more on the probability of a startup’s success over the long term
  + **New Venture Leadership** – A new business will only be as strong as its leader which means it is important to assess whether the entrepreneur or the entrepreneurial team can handle the job

1. **Looking Forward** – discussion of chapter topics for Chapters 4-13

**Answers to end-of-chapter discussion questions**

* + - 1. **Why might an entrepreneur prefer to launch an entirely new venture rather than buy an existing firm?**

There are several reasons. The entrepreneur may have a new product or service that necessitates a new business. Also, those businesses that are available for sale may be handicapped by poor locations or undesirable facilities that the entrepreneur wishes to avoid.

* + - 1. **What are the three basic types of startup ideas? What are the most common sources of inspiration for startup ideas?**

T*ype A* ideas are those concerned with providing customers with a product or service that does not exist in a particular market but that exists somewhere else. *Type B* ideas are those that involve new or relatively new technology. *Type C* ideas are those based on offering customers benefits from new and improved ways of performing old functions. Type C ideas account for the largest number of startups.

1. ***List the six most important trends of the general environment. Give a hypothetical example of a way in which each trend might affect a small business.***

The six general trends are economic trends, sociocultural trends, political/legal trends, global trends, and technological trends. Students may indicate hypothetical examples such as a business may be affected by political trends as governmental changes occur which may cause such things as tax law to change. These affect entrepreneurial activity because they generate the discontinuities that open the doors to new business opportunities. For example, the Internet (an innovation from the technological segment) has spawned countless new small firms that offer products and services to Internet users. Hypothetical examples of trends from each segment will vary, of course, but these should illustrate the potential of discontinuities (or radical shifts) that put existing firms at a disadvantage to new rivals that see the opportunities present in that trend.

1. **What are the primary factors shaping competition in an industry, according to Porter’s model? In your opinion, which of these forces will have the greatest impact on industry prices and profits?**

The following five forces determine the nature and degree of competition in an industry:

• The threat of new competitors

• The threat of substitutes

• The bargaining power of buyers

• The bargaining power of suppliers

• The rivalry among existing competitors

Different forces dominate industry competition depending on the particular circumstances. The entry of new competitors places a limit on prices. The threat of substitutes and buyer power also influence the prices that can be charged. The bargaining power of suppliers determines the cost of raw materials. Rivalry among existing competitors influences prices and costs of competing in areas such as product development, advertising, and sales force.

The relationship between the strength of industry forces and prices/profits in the industry represents an inverse function. That is, stronger forces generally lead to lower prices/profits, while weaker forces yield higher prices/profits. Experts disagree about which force has the greatest impact on prices and profits. For example, some empirical evidence suggests that the threat of new competitors has the strongest effect, while others contend that rivalry among existing competitors is most important. Student responses to this will vary, but it is important that they understand the dynamics of the five forces well enough to see how the impact might vary.

1. **How are capabilities related to tangible and intangible resources? How are these related to core competencies?**

Organizational capabilities result from the useful integration of tangible and intangible resources of the firm. Resources contribute little to the competitive advantage of the firm unless they are configured in some way that helps the firm to compete. The chapter illustrates this concept by describing a computer system as functional only when it integrates a CPU with a keyboard, a monitor, etc. A keyboard by itself is of little use, and the same is true of resources in isolation. Once entrepreneurs have an accurate view of the their resources and capabilities, they are ready to identify core competencies. Core competencies are those resources and capabilities that provide an enterprise with a competitive advantage over its rivals, such as the combining of a wide selection of gourmet coffees with the “Starbucks experience” a customer has when visiting the coffeehouse icon. Core competencies emerge when a company learns over time to use its resources and capabilities in unique ways that reflect the “personality” of the enterprise. Entrepreneurs who can identify core competencies and apply them effectively are in the best position to help their ventures achieve a competitive advantage and superior performance.

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1. ***What is a SWOT analysis? How can a SWOT analysis help the entrepreneur match opportunities in the external environment with organizational capabilities?***

An environmental assessment examines the general environment and the industry environment with the goal of finding opportunities that can be pursued while uncovering threats against which the firm should provide some sort of defense. The organizational assessment, on the other hand, looks inside the firm to inventory both strengths and weaknesses in the firm’s arsenal of resources, capabilities, and core competencies. However, a solid advantage foundation can be established only when the strengths and weaknesses of the organization are appropriately matched with a current or probable profile of opportunities and threats. This integration is best mapped out using what is commonly known as SWOT analysis, which provides a concise overview of the firm’s strategic situation.

1. **What are the two basic strategy options for creating a competitive advantage*?***

## One option involves creating a cost advantage by producing a product at the lowest cost within the market. The second option is achieving a marketing advantage by creating a product or service that can be differentiated in the marketplace.

1. **Explain what is meant by the term focus strategy?**

A focus strategy attempts to position the firm to successfully exploit a narrow market segment in which there is little or no competition.

1. **What are the advantages and disadvantages of a focus strategy? What must an entrepreneur know and do to maintain the potential of a focus strategy?**

Focus strategies can be effective in both domestic and international markets. Small firms are predicted to see rich opportunities in the future, at home and abroad. However, new ventures in general often fail because of poor market positioning or lack of a perceived advantage by customers in their target market. To minimize this chance of failure, an entrepreneur should consider the benefits of exploiting gaps in a market rather than going head-to-head with competition. Many entrepreneurs have focused on market niches, and their creative efforts illustrate just how well these strategies can work. Selection of a very specialized market is, of course, not the only possible strategy for a small firm. Nevertheless, focus strategies are very popular among this category of enterprises. It allows a small firm to operate in the gap that exists between larger competitors. If a small firm chooses to compete head-to-head with other businesses, particularly large corporations, it must be prepared to distinguish itself in some way—for example, by attention to detail, highly personal service, or speed of service—in order to make itself a viable competitor.

Those firms that adopt a focus strategy tread a narrow line between maintaining a protected market and attracting competition. Entrepreneurs must be prepared to face competition if their ventures are profitable. Michael Porter cautions that a segmented market can erode under any of four conditions: (1) the focus strategy is imitated, (2) the target segment becomes structurally unattractive because of erosion of the structure, or because demand simply disappears, (3) the target segment’s differences from other segments narrow, or (4) new firms sub segment the industry. Entrepreneurs must guard against these risks.

1. **Name and describe the major features of a feasibility analysis. Why is feasibility analysis important?**

A feasibility analysis assesses a business idea to determine whether or not the venture in mind is likely to succeed. The major features of a feasibility analysis should consider aspects of market potential, industry attractiveness, and new venture leadership while avoiding a fatal flaw that could cause the new business to be unsuccessful. Exhibit 3-9 provides a Feasibility Analysis Framework that includes an understanding of success factors, micro level aspects such as niche and competition, and macro level aspects such as market and industry to consider before writing a business plan. A feasibility analysis is important because it identifies possible flaws in a business idea that could cause a business to fail.

# COMMENTS ON CHAPTER “YOU MAKE THE CALL” SITUATIONS

**Situation 1**

* + 1. **How would you classify Lugar’s startup idea? Is it a Type A, Type B, or Type C idea?**

Lugar’s idea is a Type A idea – a New Market. Garage sales have occurred for many years, however, Lugar determined that people ran garage sales on a limited basis and would benefit from help on pricing and advertising as well as set up.

* + 1. **What was the source of Lugar’s startup idea?**

Lugar helped his mother with a garage sale and saw that she needed help in order to be successful.

* + 1. **Would you recommend that he give this startup concept a try? Explain your reasoning.**

This concept could be very successful. Since it would be inexpensive to try the idea he should do some market research to determine feasibility of the idea. He needs to determine whether his pricing scheme would be acceptable to the individuals needing his services. He needs to come up with ideas for advertising – for example, he may want to charge differently for people who want him to handle the advertising (charge more) than for people who want to do it on their own (charge less). If he feels that advertising is a vital service, he should develop a sales approach that indicates to people the advantage of that portion of his business.

**Situation 2**

1. ***Based on the frameworks introduced in this chapter, what kind of strategy is Anglada following in his new venture?***

Anglada is utilizing a Type A idea by tapping into a new market for his business venture. His business is centered around providing his customers product/service that is not available in their market. There are companies that will customize a motorcycle chopper but not companies that will provide a custom paint design on a low-profile high speed motorcycle.

1. ***Identify the strengths upon which this business is built. Do you see any weaknesses that may be of concern to the company?***

Clearly Anglada’s biggest strength is being the first company to provide this type of service/product in this motorcycle community. He has a love, passion, and talent for this work. He also has developed a respectable customer base which gives credibility to the work he is doing. A weakness to his business might be a Type C company challenging his territory. Someone else may find a way of providing a similar service for less money, faster service, or improved quality. Anglada will have to stay focused on his core competencies and continue to promote his strengths.

1. ***Are there any particular threats that will put Nick Anglada Originals at risk as time goes on? Can you see any opportunities that may allow the company to expand in the future?***

Anglada will need to remain open to changes in his business industry and seek ways of improving his product/service. Threats to his business may included changes to his demographics (shifts in size, age, ethnicity, and income distribution) and perception. Anglada also needs to determine if this is a fad-market (also known as a hot-trend) and if so, he may want to ride this wave until it ends then embark on a new venture. Clearly Anglada has a differentiation-based strategy in that he is providing a product/service that has unique attributes and is valued highly by his customer. Expansion opportunities may come from competitive threats. That is, he may want to buy-out a competitor that infringes on his customer base. And/or he may acquire a company that provides some innovative technology that may enhance his business.

1. ***What resources and capabilities form the foundation for the business? Do you think these will be sufficient to create a sustainable competitive advantage for the company? Why or why not?***

Anglada’s primary resource is his talent and skill with painting. Being able to conceptualize a customer’s vision and transform that vision onto the motorcycle itself. This could be enough to sustain Anglada as his unique perspective and style of art his is “signature”. These types of customers are enthusiasts of the product and are able to identify a particular artist. In other words, Anglada has the opportunity of positioning himself to the point that customers can identify an Anglada bike. They may also like to own an Anglada bike. This is his competitive advantage. These types of customers aren’t particularly price-sensitive and therefore, Anglada could have a long and lucrative business venture.

**Situation 3**

**1. Will the market for Sorenson’s product continue to grow in the years ahead?**

With the escalating consumption of coffee in the United States and abroad, it would seem that the potential for market growth for Sorensen’s product is likely to grow. However, the greater concern is with the probability of larger competitors coming into the market and taking business away from Sorenson, which is the focus of question 2 below.

2. **Given the company’s success, what sources of competition should he expect?**

There are two general sources of competition on which Sorenson should keep an eye. The first of these is large competitors that have the resources to develop a similar product and use their market power to pry sales away from Sorenson. Their advantages from scale economies could be substantial and make it hard for Sorenson to maintain his position. Since the product is likely to become commodity-like in the future, he may also see competition from overseas manufacturers that can easily tap into low-cost labor and drive prices down to the point that Sorenson will find it difficult to make a profit.

1. **What steps would you recommend that he take to protect his company from the onslaught of competition that is likely to come?**

There are several steps that Sorenson can take to maintain/grow his position in the market. For example, he could find an advantage that customers will notice and value (e.g., superior design or function), come up with a clever name that people find easy to remember, and/or promote brand identity vigorously. He could also be constantly on the lookout for ways to drive down his costs (e.g., expand sales to increase economies of scale, keep overhead low) and search relentlessly for ways to reach new customers.

**SUGGESTED SOLUTION TO CASE 3: FIREWIRE SURFBOARDS, LLC**

1. ***Identify and describe Firewire Surfboard’s major competitors. How are these rivals positioned in the marketplace?***

Three major competitors were names in the case: Channel Islands (located in Santa Barbara, California; the gold standard in surfboards according to the case), Surftech (located in Santa Cruz, California), and Lost Surfboards (located in San Clemente, California). Additional surfboard manufacturers include Becker and Santa Cruz who are apparently not considered major competitors.

The competitors as the case begins have existing market share and also have been providing the custom made surfboards that surfers in the target market expect. Firewire, on the other hand, has entered the market with an off-the-rack type of product with the advantage of being lighter and allowing a skateboard technique in the water.

1. ***Put yourself in the role of Firewire’s entrepreneurial team at the time of the company’s founding. What should they have anticipated in the way of competitor reaction and the response of prospective customers?***

Since custom boards are expected in this industry, Firewire represented a threat to established businesses in the industry. In addition, Firewire represents a change in surfing technique. People don’t like change! Therefore, prospective customers would need to be sold on these differences.

1. ***What is Firewire’s core competence? Is it sustainable?***

The core competency is innovative technology that changes in surfing and mimics skateboarding actions. It is computer-aided and but continually be up-dated and upgraded. With new surfers starting out on skateboards, this could be a gold mine if those young people can be switched to surfing from skateboards.

1. ***Conduct a SWOT analysis on the company. Does this analysis reveal any promising future opportunities for Firewire? Will pursuit of those opportunities lead to competitive response by current or potential rivals?***

Most significant **strengths**:

The company’s unique technology

Rapidly developing brand recognition

Boards lighter, stronger, more flexible

Most significant **weaknesses**:

The company’s dependence on off-the-rack products

Need to change how surfers handle surfing

Negative perception of product

Most significant **opportunities**:

Skateboarders who can switch their technique to surfing

Professionals using the boards to win competition

The development of new/related products such as custom boards and new transportation devices for cars (because there are no fins on these boards)

Most significant **threats**:

Competition from larger, more established rivals

Displacement from newer technologies

Competition “borrowing” their technology

Economic downturn

Switching skateboarders to using Firewire products and becoming involved in surfing is a definite opportunity. Many young people learn to skateboard and enjoy it. This may represent a big market for surfboarding. Market research should be established to determine the worthiness of this market for Firewire.

All competitors who see Firewire as a threat to their businesses will definitely respond to the growth of Firewire. Firewire must be aware of such a threat and be prepared to respond.

1. ***What broad-based strategy is Firewire following? Is this the best way to position the company? Why or why not?***

First, to create a solid brand, they are developing an off-the-rack basis to establish their brand and then move into custom-shaped boards. Positioning the company using this strategy is contrary to the “normal” way boards are sold. However it appears to be working. They have competitors using the boards, which will get the boards promoted in surfing magazines and on Internet sites. This establishes credibility with the surfing community around the world.

1. ***Given the company’s recent shift in strategy, what do you think its major challenges will be?***

With the shift to custom boards, a major challenge will be the established board manufacturers who will see this change as a test of their brands. Once a company establishes a reputation as an off-the-rack manufacturer, it may be difficult to reposition as a custom manufacturer. Apparently things have moved swiftly in this industry in the past with the change to foam boards occurring in 12 months. Changing to custom boards may be easier than establishing Firewire as an off-the-rack manufacturer.

1. ***What recommendations would you make to Mark Price, Firewire’s CEO, as he thinks about the company and its future?***

The company should continue to field surfers using its boards to get recognition via competition. Serious surfers as well as others probably keep up with competition to see who won and what boards were used. Firewire should continue to improve technology through R&D. Firewire should establish connections with the organizations that operate the competition in places such as Oahu and other surfing Mecca’s.