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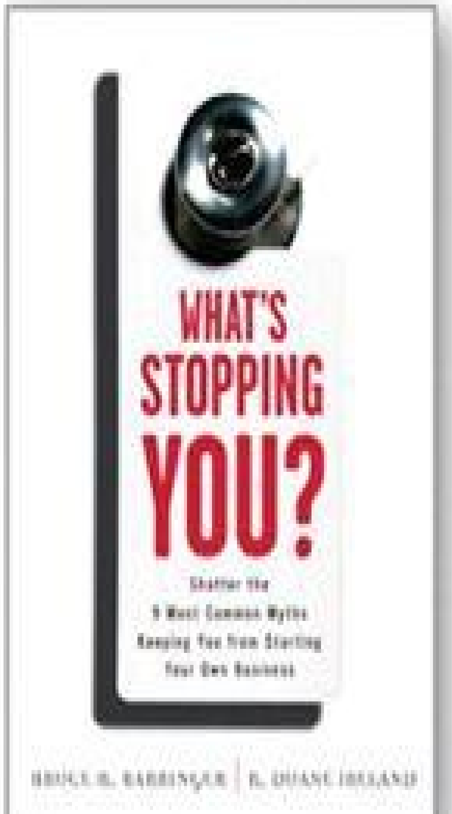

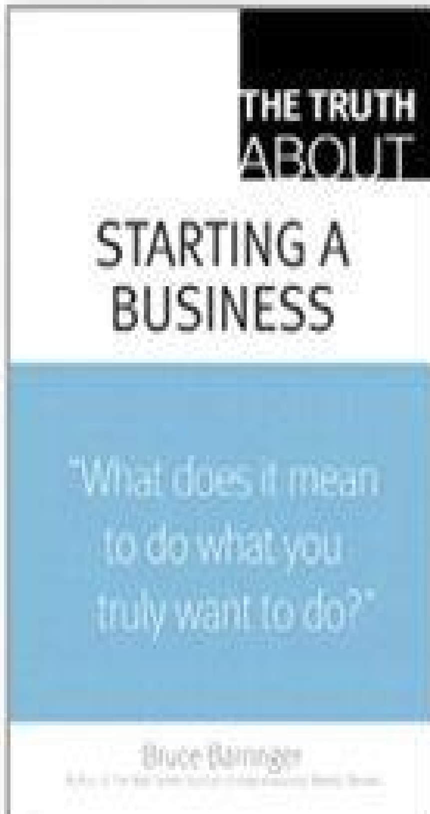

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FINANCIAL TIMES

Entrepreneurship Lessons for Success (Collection)

Bruce Barringer
Edward D. Hess
Charles F. Goetz
R. Duane Ireland

Contents

The Truth About

Starting a Business

Bruce R. Barringer

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For my family, Janet, John, Jennifer, and Emily.

Praise for *The Truth About Starting a Business*

"When thinking about starting a business, have you ever felt discouraged because you did not know somebody or some thing? If that is the case, Barringer can be your wise uncle. In this insightful new book, he shares common-sense advice, based on research that can help to get you started and going in the right direction to launch your own venture."

—**James Fiet, Ph.D.**, Brown Forman Chair in Entrepreneurship, University of Louisville

"Relevant and easily accessible advice on how to start your own business. Barringer's great primer covers it all, from naming your company to handling legalities, from publicity to the psychology of being an entrepreneur."

—**Matt Hedges**, Founder and President, Vino de Sol

"This book is a must read! Barringer has developed an easy-to-follow blueprint on how to start a new business. He takes the complexity of entrepreneurship and streamlines it, providing insight and expertise that is invaluable to those venturing out on their own."

—**Christopher Jones, CAGS**, Licensed Educational Psychologies, NCSP, President & CEO, Dynamic Interventions, Inc.

"I found myself smiling as I read some of the truths because I found it talking about myself and peers who have started numerous companies. This book should be on the seasoned entrepreneur's list of 'what I should have read before I started my business.'"

—**Joe Keeley**, President & CEO, College Nannies & Tutors Development

"This book is the ultimate handbook for starting a business: from coming up with an idea to implementing it with success and vigor. It walks a potential business owner through the steps of writing a business plan, creating an identity, financing a business, hiring personnel, marketing, and creating a work-life balance. It is a tool that no new business owner should be without."

—**Dr. Emily Levy**, Founder & CEO, EBL Coaching

"Barringer cuts to the chase with his simple, relevant, and hard-hitting truths. In practical language and with significant insight about the realities of venture start-up, he speaks on very personal level to the prospective entrepreneur."

—**Michael H. Morris, PhD**, Chris J. Witting Chair and Professor, Whitman School of Management, Syracuse University

"This is one of the best entrepreneurship books I've read. If you're an entrepreneur or are thinking about starting a business, this book is a must read! I wish I had this book when I first started out."

—**Ryan O'Donnell**, Co-Founder and CEO, BullEx Digital Safety

"Barringer reveals many realities about being an entrepreneur and starting a business. Beyond just loving what you do, it is obviously critical to understand as many of the components that go into running your business as possible."

—**Evan Shapiro**, Co-Founder, Blue Maze Entertainment

Part I The Truth About What It Takes to Be a Business Owner

Truth 1. Why people start businesses

You’re flipping through a magazine and come across a test that assesses whether you have the right personality to start a business. You take the test and learn that you’re best suited for a traditional career. Your heart sinks, because you’ve been giving business ownership some thought. But you figure that the people who designed the test know what they’re doing. Right? Wrong!

There’s no scientific evidence that shows that people with certain personalities are more likely to start a business or will be a more successful business owner than anyone else. In fact, the somewhat surprising collection of research results illustrate that there are no meaningful differences between business owners and nonbusiness owners on the most basic human characteristics, behaviors, and desires.[1] Most people, for example, want to make more money and crave independence, not just business owners. People who start their own businesses are just as diverse as people in regular jobs. You don’t have to have a certain personality, behave in a particular way, or have a certain set of desires to be a successful business owner.

> You don’t have to have a certain personality, behave in a particular way, or have a certain set of desires to be a successful business owner.

What, then, motivates people to start their own business? In most instances, it’s riskier and harder to start and run a business than it is to traverse a traditional career. Although there are many reasons that motivate people to start their own business, two reasons are paramount: the presence of aspiration gaps in people’s lives, and passion for a business idea.

Aspiration gaps

All of us have aspirations, which are made up of our most important goals, objectives, ambitions, and longings. Our aspirations vary because they’re influenced by our values, abilities, experiences, families, and individual circumstances. When one or more of our aspirations are unmet, we have aspiration gaps in our lives. Collectively, our aspirations form what researchers call our aspiration vectors. Sometimes our aspirations vectors get complex, like when we’re simultaneously trying to build a career, raise kids, love our spouse, save money, and so on. For people who have strong aspirations and are insistent that certain aspirations are met, their aspirations become the driving force in their lives. For example, a young mother might have the following three aspirations: a job that pays at least $35,000 per year, the ability to be home by 3:00 p.m. on weekdays to meet the school bus, and Sundays free to participate in church and volunteer-related activities. Similarly, the assistant manager for a large retail chain, like Home Depot or Target, might be driven by the single aspiration to have his own store by the time he is 30.

People can become discouraged or distressed when they look at their job or alternative jobs in the traditional labor market and conclude that none of the choices will allow their most important aspirations to be met. In these instances, an alternative is to start a business. Although starting a business isn't easier than a traditional job, business owners usually have more discretion and control over their schedule and career trajectory. This discretion and control helps people better juggle both professional and family-related goals and aspirations and accomplish the things they want the most.[2]

> Small business owners often work long hours and make sacrifices to make their businesses work, but they say it's worth it because they're passionate about the businesses they're running.

Passion for a business idea

A second factor that motivates people to start their own businesses is passion for a business idea. What frequently happens is that a person gets an idea for a new product or service, and there is no practical way to bring the idea to market other than starting a new business. In these instances, a person's passion for the idea is determined by how desirable and feasible the idea seems to be.[3] Many prospective business owners become very passionate about their ideas, particularly if they believe that the resulting business will improve their own circumstances and positively influence other people's lives.

An important result of passion is that it often elicits extraordinary effort on the part of business owners to get their businesses off the ground and to run them successfully. Small business owners often work long hours and make sacrifices to make their businesses work, but they say it's worth it because they're passionate about the businesses they're running.

Truth 2. The right business for you

Business magazines and Web sites regularly publish lists of the best businesses to start. These businesses are usually in rapidly growing industries like health care, senior services, green energy, and specialty stores. The idea is that businesses in these industries satisfy emerging environmental trends and sell products and services that are likely to be in high demand for some time. So if you started a business, would you be foolish *not* to pick a business from one of these lists?

The answer is that it depends. It depends on whether the business is something that you’re passionate about and helps you meet your personal goals and aspirations. The business you select should also be congruent with your skills, abilities, aptitudes, and talents. There’s a theory in organizational behavior referred to as *person-organization fit*, which says that a person’s satisfaction on the job is not a function of the person or the organization but a function of the fit between the two.[1] In a start-up context, this theory is a reminder of how important it is for prospective business owners to have an accurate understanding of their abilities and skills before settling on a specific business opportunity. It’s not a given that we automatically know what our best skills and aptitudes are. If you’re uncertain, ask friends, family members, and coworkers for their input or seek help from a local college or university. The placement centers at public colleges and universities normally have skills assessment tests available that can help you better understand the type of business opportunity that is the best match for you.

> The best business to start is the one that matches who you are, what you know how to do, what you like to do, and what resources you have.

It’s also important to have an intuitive sense of whether a particular opportunity is right for you. Tim Berry, the founder of Palo Alto Software, says that he is frequently asked by prospective business owners “What’s the best business to start?” He tells people to look in the mirror. The best business to start is the one that matches who you are, what you know how to do, what you like to do, and what resources you have. Berry is quick to add that a good business also has to sell a product or service that people want to buy.[2] This is a topic you’ll explore more in Part II, “The Truth About Generating and Testing Business Ideas.”

The business you select should also be consistent with your lifestyle expectations. The old adage “Be careful what you wish for” is as true in business as it is in other areas of life. For example, if you identify a business opportunity that has a large upside potential and obtain funding from a professional investor, you should know what to expect. Most professional investors shoot for a 30-to 40-percent annual return on their investment.[3] This level of expectation will force you into a fast growth mode literally from the start, which typically implies a quick pace of activity, a rapidly raising overhead, and a total commitment in terms of time and attention on your part. The upside is that if the new company is successful, you’ll normally do well financially. If what you’re really after, however, are nonfinancial rewards, such as the ability to work in an area that is personally rewarding to you or the ability to better juggle family and job-related responsibilities, you may not want the pressures associated with investors continually looking over your shoulder. A less ambitious, but perhaps more personally satisfying, business may be a better choice for you.

> The business you select should also be consistent with your lifestyle expectations. The old adage “Be careful what you wish for” is as true in business as it is in other areas of life.

Truth 3. Questions to ask before you quit your job

You've pretty much decided. You've picked a business idea that's a good fit for you, and you're ready to move forward. But you're nervous about quitting your job. You're just not sure when you should quit your job to start your business.

Good! Your sense of unease about quitting your job is a good thing. Making the leap from being an employee to being a business owner is a big step. You should be sure that you have identified a sound business idea and that you're fully prepared before you leave your job. There is no set formula for knowing when the timing is right to leave. But here are some questions to ask yourself as your think through your decision.

> Making the leap from being an employee to being a business owner is a big step. You should be sure that you have identified a sound business idea and that you're fully prepared before you leave your job.

- **What's the real reason you want to quit your job to start a business?** If you're quitting for a positive reason, such as passion for a business idea, you'll have a better chance of succeeding than if the reason is negative, such as you're sick of your boss or you fear you might lose your job.[1] Make sure that after your job is gone and you're working on your business, it's something you really want to do.
- **Do you have a viable business idea?** It's not good enough to simply "think" you have a viable business idea. You need to write a business plan, share it with people who can give you informed feedback, and talk to prospective customers. Don't launch a venture that's hastily conceived. Know what you're doing.
- **Are your finances in order?** You need to know your start-up costs and have sufficient cash on hand or a plan for raising the cash before you launch your business. You should also have sufficient money in the bank (experts recommend up to six months) to cover living expenses while your business gets going. What if you encounter unexpected costs? Are you willing to cut back on expenses or ask your spouse to take on an extra job to make things work?

- **Are you emotionally ready?** Owning and running a business is different from being an employee. You'll have your own money at stake and will normally work longer hours than you did before. It's also harder to simply "leave your work behind" at the end of a day. One thing that surprises many new business owners is that they miss the hectic pace and busyness of the work environment they left, where they had frequent interactions with coworkers and others. Many new business owners work alone, especially if they work out of their homes. This type of lifestyle can be lonely and hard to get used to, particularly if you enjoy frequent interactions with others. The best way to determine what your life will be like is to get to know one or more business owners in the field you'll be entering.
- **Can you start the business part time?** Many business owners start their businesses part time. While this approach isn't possible in all situations, you should give it some thought. By starting a business part time, you can gain valuable experience, tuck away the money you earn, and find out if you really like the business before you quit your job. In some businesses, it takes time to build a productive client list. You may be able to time the departure from your job with the point-in-time where your client list is large enough and profitable enough to justify your full-time attention.

Have lengthy discussions with your spouse before you quit your job. Talk about both the hardships and the rewards that starting your business will entail.

- **Is your spouse supportive?** You know from your life experiences that career-related decisions don't impact just you. If you have a spouse and kids, they'll feel the impact, too. Have lengthy discussions with your spouse before you quit your job. Talk about both the hardships and the rewards that starting your business will entail. Don't make the leap without the most important people in your life on board.

Truth 4. Key characteristics of successful business owners

Although there’s no tried-and-true formula for determining who’s best equipped to become a successful business owner, studies have shown that successful business owners share a set of common personal characteristics. Knowing these characteristics helps prospective business owners assess whether business ownership is a good choice for them and whether steps need to be taken to bolster their capabilities in certain areas.

Passion for their business

Passion is the enthusiasm, joy, and zeal that emerge when business owners are doing something that they feel is important and truly enjoy.[1] As mentioned in Truth 1, “Why people start businesses,” passion is often the reason that people start a business. Passion is needed to infuse a business with excitement and drive and helps the founder or founders persevere through the ups and down of the startup process. It’s also a source of motivation and a reward. The payoff that many business owners receive from their passion and hard work is the extreme satisfaction they experience as they work in their business and watch customers benefit from the products and services they sell. Only you can determine if you’re truly passionate about a particular business idea. Many business experts say, “Don’t start a business you’re not passionate about.” It’s good advice.

> Passion is the enthusiasm, joy, and zeal that emerge when business owners are doing something that they feel is important and truly enjoy.

Tolerance for ambiguity

Tolerance for ambiguity is the ability to deal with ambiguous situations in a sensible and calm way.[2] It’s context-dependent—meaning that the same situation may be ambiguous in one setting and not in another. For example, the manager of an Olive Garden restaurant may know exactly what to do if someone calls and asks if the restaurant can set aside enough tables for a group of 30 people at 7:00 p.m. that evening. The owner-manager of a new restaurant may have never had that request before and may have to stop and think about what to do. The manager might think, “I’d love to seat 30 people at the same time, but what will the people who have already waited 30 minutes for a table think if a large group walks in and is seated right away?” These types of dilemmas face the owners of new businesses frequently because the businesses are new and are still establishing their policies and procedures. Business owners with a high tolerance for ambiguity can normally handle new and uncertain situations with relative ease, while business owners with a low tolerance for ambiguity would handle the same situations with more angst and unease.

> Business owners with a high tolerance for ambiguity can normally handle new and uncertain situations with relative ease.

Self-efficacy

A critical yet not often explained characteristic of successful business owners is self-efficacy. Self-efficacy is similar to self-confidence and refers to a person’s belief in being capable of performing a particular task.[3] Individuals generally avoid tasks where their self-efficacy is low and are drawn to tasks where their self-efficacy is high. As a result, a person with high self-efficacy for a given task, like starting a business, will usually approach it with enthusiasm and drive.[4] This is why some people, even though they often think about starting a business, never do it. Deep down inside, they don’t believe they have the skills and abilities necessary to start and run a successful business. You can heighten your self-efficacy for starting a business by working in a field closely related to the business you’re thinking about starting, becoming acquainted with people who have started successful businesses (and realizing that they are no smarter or more capable than you are), and being encouraged by others.

Truth 5. You may not need “prior business experience”

If you ask 100 people with traditional jobs why they’ve never started their own business, a common response that you’d get would be a lack of business experience. Most people see prior business experience as a necessary prerequisite to starting a business of their own.

In some cases, this sentiment is correct. Some businesses do take a substantial amount of experience to successfully start and run. Most financial services and medical products companies, for example, are started by people with deep industry backgrounds and business expertise. There are also technical aspects of running a business, such as finance and accounting, which take time and effort to learn and perfect, regardless of the type of business. In these instances, people who have business experience have a leg up on those who don’t. It’s also easy to envision the advantage that someone who has managed people and run a successful business before might have over someone who hasn’t.

But there are many examples of people who’ve started successful businesses without prior business experience. Bill Gates of Microsoft and Michael Dell of Dell are two examples. Many people become passionate about a business idea and pursue the idea regardless of their level of prior business experiences. There are a variety of ways that people compensate for their lack of experience. Some start their business part-time and learn as they go. Others take on a partner who has business experience or make key hires early on. Still others take classes through their local Small Business Development Center or rely on SCORE (Service Core of Retired Executives) advisors for help (free, online at www.score.org).

> There are many examples of people who’ve started successful businesses without prior business experience.

There are also alternatives for starting a business that minimize the need for prior business experience. These alternatives allow people to pursue an opportunity in which the fundamentals of the business have already been thought out. The alternatives include franchising, direct sales, and businesses that have wellestablished business models.

> There are also alternatives for starting a business that minimize the need for prior business experience. These include franchising, direct sales, and businesses that have wellestablished business models.

Franchising is a form of business ownership in which a firm that already has a successful product or service (*franchisor*) licenses its trademark and method of doing business to other businesses (franchisees) in exchange for an initial franchise fee and an ongoing royalty. In some industries, such as restaurants, hotels, and automobile service, franchising is the dominant form of business ownership. Franchising provides an individual the opportunity to own a business using a tested and refined business system. The franchisor also typically provides training, technical expertise, and other forms of ongoing support. Many franchise systems are open to people with general skills but no prior "domain-specific" or other business experience. In fact, some franchise systems shy away from people with prior experience in the field the franchise operates in, fearing that they could have too many preconceived notions about how to run the business.

Direct sales is another option. While most people cringe when they hear the words "direct sales" (or multilevel marketing), there are legitimate direct sales opportunities. Currently, there are over 14 million people in the United States involved in direct sales.[1] Well-known direct sales companies include Tupperware, The Pampered Chef, Avon, and Discovery Toys. Although the direct sales industry as a whole suffers because of the high-pressure sales tactics of some of its members, there are an increasing number of highly legitimate opportunities. (More about this in Truth 13, "Believe it or not: There are legitimate opportunities in direct sales.") The majority of direct sales organizations do not require their participants to have prior business experience.

A third option is to start a business in an area where the business's business model is well documented and well understood. A firm's business model describes how it operates and makes money. An example of a business with a wellestablished business model is a bed & breakfast. Dozens of books are available that provide advice about how to open and run a successful bed & breakfast and provide instruction for how to manage day-to-day operations. Workshops are also held periodically across the country about how to open and operate a successful bed & breakfast. There are many similar examples. Following a wellestablished business model negates, at least in part, the prior business experience needed to launch and run one of these businesses.

Part II The Truth About Generating and Testing Business Ideas

Truth 6. The most common sources of new business ideas

In my experience, promising new business ideas emerge from three sources: changing environmental trends, unsolved problems, and gaps in the marketplace. Select an idea that fits one of these sources. Even though you may be passionate about a particular idea or it may be a perfect fit with your skills, it still has to be an idea that people need and are willing to buy.

Changing environmental trends

The first source of business ideas is changing environmental trends. The most essential trends are economic trends, social trends, technological advances, and political action and regulatory changes. Changes in these areas often provide the impetus for new business ideas. For example, an important economic trend is the buying power of baby boomers. As baby boomers reach retirement age, a sizable portion of their spending will be redirected to areas that facilitate their retirement. This trend will invariably spawn new businesses in many areas, largely because baby boomers have greater disposable income relative to previous generations. The most promising areas include finance, travel, housing, recreation, and health care. Social trends are equally critical. Current examples include an increased focus on health and fitness, an emphasis on alternative forms of energy, and the increasing diversity of the workforce. One new company, Greasecar Fuel Systems, makes conversion kits that allow diesel engines to run on vegetable oil. The company is growing largely because its business idea is directly tied to an increased social awareness of the need to find alternatives to fossil fuels.[1]

> Even though you may be passionate about a particular idea or it may be an ideal fit with your interests and skills, it still has to be an idea that people need and are willing to buy.

Technological advances and political and legal changes provide ongoing sources for new business ideas. After a technology is created, products often emerge to advance it. For example, the Apple iPod has created an entire industry that produces iPod accessories. It’s now estimated that for every $3 spent on an iPod, at least $1 is spent on an accessory.[2] Similarly, political and legal changes often provide an opening for new business ideas. An example is the No Child Left Behind Act of 2002. The act requires states to develop assessments in basic skills to be given to all students in certain grades. Shortly after the act was passed, Kim and Jay Kleeman, two high school teachers, started Shakespeare Squared, a company that produces materials that help schools comply with the act.

Unsolved problems

The second approach to identifying business ideas is to recognize problems and find ways to solve them. Problems can be experienced or recognized by people through their jobs, hobbies, or everyday activities. For example, in 1991, Jay Sorensen dropped a cup of coffee in his lap because the paper cup was too hot. This experience led Sorensen to invent an insulating cup sleeve and to start a company to sell it. Since launching his venture, the company, Java Jacket, has sold over 1 billion cup sleeves.

Advances in technology often result in problems for people who can't use the technology in the way it's sold to the masses. For example, some older people find traditional cell phones hard to use—the buttons are small, the text is hard to read, and it's often hard to hear someone on a cell phone in a noisy room. To solve this problem, GreatCall is producing a cell phone called the Jitterbug, which is designed specifically for older users. The Jitterbug features large buttons, easy-to-read text, and a cushion that cups around the ear to improve sound quality. Another company, Firefly Mobile, is now selling a cell phone designed specifically for tweens, ages 8 to 12. The phone weighs only two ounces and is designed to fit into a kid's hand. It includes appropriate limitations for a young child and speed-dial keys for Mom and Dad.

Gaps in the marketplace

The third source of business ideas is gaps in the marketplace. There are many examples of products that consumers need or want that aren't available in a particular location or aren't available at all. Part of the problem is created by large retailers, like Wal-Mart and Costco, which compete primarily on price and offer the most popular items targeted toward mainstream consumers. While this approach allows the retailers to achieve economies of scale, it leaves gaps in the marketplace. This is the reason that clothing boutiques and specialty shops exist.

These businesses are willing to carry merchandise that doesn’t sell in large enough quantity for Wal-Mart or the other big-box retailers to sell.

> There are many examples of products that consumers need or want that aren’t available in a particular location or aren’t available at all.

There are also product gaps in the marketplace, many of which represent potentially viable business opportunities. For example, in 1997, Julie Aigner-Clark realized that there were no videos on the market to expose her one-year old daughter to music, the arts, and science, so to fill the gap she started Baby Einstein, a company that produced uplifting videos for children aged three months to three years. The company did so well it was acquired by Disney in 2001 and is still selling products under the Baby Einstein brand today.

Truth 7. Want several alternatives? Techniques for generating new business ideas

One thing to guard against is settling on a business idea too quickly. Whether you're just starting to look for an idea or have a notion of the business you'd like to start, it's a good idea to identify and think through several alternatives. Two common ways to generate business ideas are brainstorming and library and Internet research.

Brainstorming

Brainstorming is the process of generating several ideas about a specific topic. The approaches range from a person sitting down with a yellow legal pad and jotting down business ideas to formal "brainstorming sessions" that are led by moderators and involve a group of people. In a formal brainstorming session, the leader of the group asks the participants to share their ideas. One person shares an idea, a second person reacts to it, a third person reacts to the reaction, and so on. A flip chart or whiteboard is typically used to record the ideas. A productive brainstorming session is freewheeling and lively and is intended to generate as many substantive ideas as possible.[1]

Brainstorming sessions can also be informal. For example, during the creation of Proactiv, a popular acne treatment product, Dr. Katie Rodan, one of the company's founders, hosted dinner parties at her house and conducted brainstorming sessions with guests. Rodan credits these sessions with helping her and her cofounder develop ideas that shaped Proactiv and moved the process of starting the company along.[2] Another approach to brainstorming is to utilize the three sources for business ideas discussed in Truth 6, "The most common sources of business ideas." Imagine this. Suppose you are part of a small group that is trying to brainstorm ideas for a new type of fitness center. You create three columns on a whiteboard labeled Changing Environmental Trends, Unsolved Problems, and Gaps in the Marketplace. After brainstorming ideas in each category, a pattern jumps out at you: The population is aging, older people are increasingly interested in fitness, and many of the machines and classes taught in traditional fitness centers aren't suitable for the 50+ demographic.

Based on this pattern, your first solid idea is to create a fitness center designed specifically for people 50 years old and older.

Library and Internet research

A second approach to generating business ideas is to conduct library and Internet research. A natural tendency is to think that an idea should be chosen and the process of researching the idea should then begin. The problem is that this approach is too linear. Often the best business ideas emerge when the general notion of an idea, like opening an innovative type of fitness center, is merged with extensive library and Internet research. This combination of activities is likely to provide insights into the best types of fitness centers to start.

> Often the best business ideas emerge when the general notion of an idea is merged with extensive library and internet research.

The best approach to utilizing a library is to discuss your general area of interest with a reference librarian, who can point you to useful resources, such as industry-specific magazines, trade journals, and reports. Simply browsing through several issues of a trade journal on a topic can spark new ideas. Powerful search engines and databases are also available through most university and large public libraries. An example is IBIS World, a company that publishes market research on all industries and subcategories within industries. IBIS World is a fee-based service but is normally free if accessed through a library. IBIS World has literally dozens of pages on the health and fitness club industry alone. Spending time reading this information could spark new ideas for fitness centers or help flesh out an existing idea.

Internet research is also important. If you're starting from scratch, simply type "new business ideas" into Google or Yahoo! to bring up links to newspaper and magazine articles that talk about the latest new business ideas. While these types of articles are general in nature, they provide a starting point. If you have a specific idea in mind, like the fitness center concept we've been discussing, a useful technique is to set up a Google or Yahoo e-mail alert using keywords that pertain to your topic of interest. Google and Yahoo! e-mail alerts are e-mail updates of the latest Google or Yahoo! results (that is, press releases, news articles, blog postings) based on your topic. This technique, which is available for free, will feed you a daily stream of news articles and blog postings about specific topics.

While some people are inclined to select a business idea too quickly, other people have the opposite problem—they have trouble coming up with a sensible business idea. If this happens to you, don’t get discouraged. Business ideas often take time to develop. Many people brainstorm and conduct various forms of library and Internet research for weeks or months before they settle on a specific idea.

Truth 8. A make-it or break-it issue: Selecting an idea that can be sold into a niche market

One rule of thumb that you should adhere to when searching for a business idea is to select an idea that you can sell into a niche market.

A niche market is a place within a larger market segment that represents a narrow group of customers with similar interests and needs. For a new business, selling into a niche market is crucial for at least two reasons. First, it allows a firm to establish itself within an industry without competing against major participants head on. Second, a niche strategy allows a firm to focus on serving a specialized market well instead of trying to be everything to everybody in a broad market, which is nearly impossible for a new entrant. An example of a firm that sells into a niche market is Prometheus Laboratories, a company that sells diagnostic services to the 15,000 doctors in the United States who specialize in gastroenterology and rheumatology. Explaining his firm's strategy of developing world-class expertise in specialized areas, then CEO Michael Walsh said, "We want to be an inch wide and a mile deep."[1]

Another way of thinking about this topic is to distinguish between vertical and horizontal markets. A vertical market, which is analogous to a niche market, focuses on similar consumers or businesses that have specific needs. For instance, a start-up business might focus on providing accounting software designed specifically for specialty eateries, like small coffee and smoothie restaurants. A horizontal market meets the needs of a broad swath of consumers or businesses, rather than a specific one. A start-up that tries to sell an accounting software product to all small businesses would be selling into a horizontal market. It's easy to imagine how much more difficult it would be for a new business to take on industry leaders and try to sell to a broad market rather than limiting itself to a smaller niche. Once a business gains momentum, it can expand into related areas and broaden the scope of its market.

> A niche market is a place within a larger market segment that represents a narrow group of customers with similar interests and needs.

Some new businesses, as a result of the nature of their industry, do compete head-to-head against larger rivals for some of their products but can still benefit by identifying niche markets to specialize in. An example is a new nursery that sells plants and lawn and garden supplies. A portion of what the nursery sells, like its generic plants and its name-brand lawn and garden fertilizer, may complete against larger stores, like Home Depot and Lowe’s, which often have garden centers. If this is the case, it’s important that the nursery seek out niche markets, within the lawn and garden industry, which will set it apart from its larger rivals. For example, it might specialize in providing hedges, shrubbery, and sod for new construction and develop relationships with local builders and contractors. It might also become the “place to go” to purchase outdoor and indoor fountains. Specializing in these areas allows the new nursery to establish a unique identity and offsets, at least in part, the disadvantage of competing head-to-head against larger rivals on some of its products.

> Once a business gains momentum, it can expand into related areas and broaden the scope of its market.

Truth 9. Screening and testing business ideas

After you choose a business idea, test the idea to gain a sense of its feasibility. Some business owners pick an idea and immediately move forward, but it is much better to pause and spend some time scrutinizing the idea.

The proper sequence in thinking through the merits of a business idea and launching a business is as follows:

- Identifying a business idea
- Screening and testing the idea to determine its initial feasibility ■Writing a business plan
- Launching the business

Complete this process to avoid falling into the "everything about my idea is wonderful" trap.[1] All business ideas have strong and weak points, and you should be aware of both before you proceed. In addition, studies have shown that prospective business owners tend to overestimate their chances for success.[2] As a result, you need to gain an objective assessment of its potential. There are four areas to consider in testing the initial feasibility of a business idea.

Product/service feasibility— Determine if the proposed product or service is desirable and serves a need in the marketplace. Prepare a concept statement, a one-page document that includes the following:

- A description of the product or service and its benefits ■The intended target market
- A description of how the product or service will be sold ■A brief description of the company's initial management team

After you develop the statement, you should show it to 10 to 15 people who can provide informed feedback. Attach a short survey to the statement that asks the participants to (1) tell you the things they like about the product or service idea, (2) provide suggestions for making it better, (3) tell you whether they think the product or service idea is feasible, and (4) share additional comments or suggestions. Tally, read, and evaluate all responses.

Instead of developing a formal concept statement, some prospective business owners simply talk through their idea with people and gather informal feedback.

Either approach is valid as long as the feedback you obtain gives you a good sense of the feasibility and desirability of your product or service idea and any areas in which it might need to be tweaked or strengthened.

Industry/niche market feasibility— The second area to explore is the industry your business will be part of and the niche market you plan to go after. The most attractive industries for new businesses have the following characteristics:

- ■ Are large and growing rather than small and shrinking ■Are early rather than late in their life cycles ■Are important to their customers (by selling products or services that people "must have" rather than "would like to have") ■Feature environmental trends moving in favor of the industry ■Have high rather than low operating margins

You should also assess the attractiveness of the specific niche market you plan to target. An ideal market for a startup is one that's large enough for the proposed business but small enough to avoid attracting larger competitors.

Finding good information on your industry and niche market takes a little work. The best place to start is to tap into the resources available at a university or large public library. Industry trade journals and magazines also provide information. Talking to business owners who are part of the industry you plan to enter is another option.

Organizational feasibility— The third area to explore is whether the proposed business has sufficient managerial know-how and expertise to be launched and successfully managed. This task requires the people starting the business to be honest and candid in their self-assessments. The two most important factors are the passion that the individuals have for the business and the extent to which the people involved understand the industry in which the business will compete.

There are other people-related factors that have been linked with startup success:

- ■ Relevant industry experience or prior business startup experience ■Depth of professional and social networks ■Experience and expertise in cash flow management ■Access to mentors or people who can provide startup advice ■ Level of creativity
- ■ Undergraduate or graduate degree

While you don't have to score high on each of these factors to be a successful business owner, looking over this list, combined with how passionate you are about the business and how well you understand the industry in which the business will compete, should give you a general sense of how prepared you are to start the proposed business.

Financial feasibility— The fourth area to consider is the financial feasibility of the proposed business. The two most central areas to consider are the total startup cash needed and the financial performance of similar businesses.

You need to have a sense of how much it will cost to launch the proposed business. Prepare a preliminary budget that lists the operating expenses and capital purchases required to get the business up and running. After you arrive at a total figure, provide an explanation of where the money will come from. If you expect the money to come from a bank loan, from an investor, or from friends and family, step back and consider how realistic those options are.

It's also good to get a sense of a proposed business's financial potential by comparing it to similar, established businesses. Again, you'll have to do some work to find the information you need. If you identify a business that is similar to the one you want to start, and the business isn't likely to be a direct competitor, it's not inappropriate to contact the owner or manager and ask about the business's sales and income. Even if the owner is only willing to talk in general terms ("our annual sales are in the $2 million range, and we're netting between $150,000 and $200,000 per year"), that information is better than nothing. Internet searches are also helpful. If you're interested in starting a fitness center, for example, typing "fitness center sales and earnings" into the Google search bar results in links to articles about fitness centers that discuss sales and earnings data.

Truth 10. Writing a business plan: Still as important as ever

Imagine the following. Two friends of yours are thinking about opening a seafood restaurant. After doing some preliminary analysis, they decide to write a business plan. They spend the next two months meeting five nights a week to hash out every detail of the business. They study the restaurant industry intently, identify their target market, develop a marketing plan, settle on a hiring schedule, plan their facility, determine what their startup expenses will be, and put together three years of pro forma (projected) financial statements. After 40 meetings and several drafts, they produce a 30-page business plan that explains every aspect of the business. They ask you to proofread it, and as you read through the plan, you learn about current trends in the restaurant industry, how your friends' business will take advantage of the trends, what the business will look like, how it will differentiate itself from its competitors, how much it will cost to get started, and much more.

Impressed? You have reason to be. There is convincing evidence that writing a business plan contributes to startup success.[1] It forces the founders of a business to systematically think through every aspect of their business and develop a concrete blueprint to follow. It also creates a mechanism for a business to present itself to outsiders.[2] Most bankers and investors, for example, ask for a business plan when they are approached for funding. If you don't have a business plan, or you have to scramble to put one together, it makes a poor impression. Planning also reduces anxiety and stress. Business owners who become overwhelmed during the startup process rarely have a business plan in place. Starting a business can be a difficult and complicated process. A well-written business plan normally anticipates and provides solutions for handling the hardest and trickiest issues.[3]

> There is convincing evidence that writing a business plan contributes to startup success.

Most business plans are 20 to 35 pages and are divided into sections that represent the major aspects of a new venture's business.

A sample plan is as follows:

I. Executive Summary

II. Company Description

III. Industry Analysis

IV. Market Analysis

V. Marketing Plan

VI. Management Team and Company Structure

VII. Operations Plan

VIII. Product (or Service) Design and Development Plan

IX. Financial Projections

Appendixes

The title of the sections varies from plan to plan, as does the quality of the writing, the substance of the plan, and the degree to which the plan convinces the reader that the business opportunity is exciting, feasible, and within the capabilities of the people launching the business. Writing a business plan that includes all these elements is not an easy task, but it is a fulfilling and useful one. Think back to the vignette that opened this chapter. Although the two individuals sacrificed 40 evenings to write their plan, just think how much they learned through the process and how much more confident and self-assured they'll be when they launch their business. They'll also have a blueprint to follow and will have a plan available to provide to bankers or investors if needed.

> One possible outcome of writing a business plan is that it may show that a particular business isn't feasible.

Publications on how to write a business plan are available at bookstores, and Small Business Development Centers and SCORE chapters often sponsor workshops on how to write a business plan.[4] Some businesses hire consultants or outside advisors to write their business plans. Although there's nothing wrong with getting advice and making sure a plan looks as professional as possible, an outside person shouldn't be the author of the plan. Besides listing facts and figures, a business plan needs to project a sense of anticipation and excitement about the possibilities surrounding a new venture, which is a task best accomplished by the creators of the business. Plus, hiring someone to write the plan denies the prospective business owners the positive benefits of the writing experience.

One possible outcome of writing a business plan is that it may show that a particular business isn't feasible. While reaching that conclusion may be regrettable, it is better to fail on paper than in real life.

Part III The Truth About Entry Strategies

Truth 11. Starting from scratch: Developing your own product or service

There are four common ways to get into business: starting from scratch, buying a franchise, participating in direct sales, and buying an existing business. When most people think of starting a business, they think of starting from scratch. This approach involves developing your own business idea and building the business from the ground up. But there are pluses and minuses to each method of getting into business. This Truth focuses on the advantages and disadvantages of starting a business from scratch.

Advantages of starting a business from scratch

Starting a business from scratch is the ultimate business start-up experience. You start with a clean slate and are able to shape and mold the business as you see fit. You select (or develop) the product or service you will sell, pick the business's name, select a location, and build the business. If you're careful, you can often start and build the business fairly inexpensively. In fact, the average business in the United States is started for about $10,000.[1] Even aggressive growth firms, in most cases, don't take an arm and leg to start. Every year *Inc*. magazine compiles a list of the 500 fastest-growing privately owned businesses in the United States. In 2006, the medium amount it took to start one of the businesses on the list was $75,000.[2] That means that half of them were started for less than $75,000. It's normally more expensive to buy a franchise or purchase an existing business.

> Starting a business from scratch is the ultimate business start-up experience.

Starting a business from scratch, for many people, is also very satisfying. The business is a direct reflection of your efforts, values, work ethic, and skills. It's also the most practical way for a prospective business owner to bring a new product or service idea to market. While there are many advantages to franchising, participating in direct sales, and buying an existing business (as discussed in Truths 12 to 14), these approaches require you to build on someone else's product or service idea. Additionally, if you're starting a business to fill an aspiration gap, such as being home by 3:00 p.m. on workdays to meet the school bus or having Sundays free to participate in volunteer activities, starting a business from scratch may be your best alternative. Many people who buy retail franchises, for example, find the hours of operation and other rules to be so rigid that they have to plan their lives around their business. While starting a business from scratch is in many ways more demanding than other ways of getting into business, the owner has the advantage of setting the hours of operation and the overall tone for the business.

Disadvantages of starting a business from scratch

There are also disadvantages to starting a business from scratch. Starting a new business entails greater risk than buying a franchise, participating in a direct sales organization, or buying an existing business. You must also build your business's brand, develop a marketing campaign, establish relationships with suppliers, and complete the other chores necessary to build a business from its inception. While many people enjoy engaging in these activities, they are time-consuming and require expertise. As mentioned in Truth 5, "You may not need prior business experience," one of the principle advantages of franchising and direct sales, in particular, is that the fundamentals of the business have already been worked out.

It's also more difficult to obtain financing for a new business than it is to buy a franchise or purchase an existing business. There is always a certain degree of skepticism surrounding a brand-new business. The skepticism can be lessened through a well-developed business plan, as discussed in Truth 10, "Writing a business plan: Still as important as ever." A new business doesn't have a track record to rely on. One of the primary advantages of buying a franchise, such as a Subway or a Curves International, is that the business concept is proven, which is reassuring to bankers and investors. The same rationale applies to buying an existing business. As a result of these realities, the same person who is unable to secure a $50,000 loan to start a business from scratch may be able to borrow two to three times that amount to buy a franchise or an existing business. The perceived risk involved with starting a business from scratch is that much higher than the other alternatives.

Making the call—Is starting a business from scratch the right strategy for you?

In general, individuals who have prior business experience are best-suited to start a business from scratch. It also helps to have access to start-up funds through personal savings or via loans from friends and family. These are not hard-and-fast rules, however. Many people have started successful businesses from scratch with no prior business experience and limited start-up funds. The best strategy for making the call is to weigh the advantages and disadvantages of starting a business from scratch against the alternatives for your own circumstances.

> In general, individuals who have prior business experience are best-suited to start a business from scratch.

Truth 12. Franchising: Buying into someone else’s formula for success

Franchising is a form of business ownership in which a firm that already has a successful product or service (franchisor) licenses its trademark and method of doing business to other businesses (franchisees) in exchange for an initial franchise fee and ongoing royalties. The total initial investment includes the franchise fee, the costs associated with getting the franchise up and running (which vary by franchise), and any other fees that are part of the franchise agreement. The ongoing royalty fee, which is usually around 6 percent, is based on a percentage of weekly or monthly gross income.

Advantages of buying a franchise

There are two primary advantages to buying a franchise as opposed to starting a business from scratch. First, franchising provides a small business owner the opportunity to own a business using a tested and refined business system. This attribute reduces the time and the amount of experience needed to get a franchise business going. In addition, the trademark that comes with the franchise provides instant legitimacy for the business. For instance, if you’re interested in opening a fitness center for women, you’ll likely attract more customers by opening a Curves or Lady of America franchise than a new, independently owned business. The second advantage to buying a franchise is that the franchisor typically provides training, technical expertise, and other forms of ongoing support. For example, if you buy a Curves franchise, your initial investment gets you a weeklong training program at Club Camp—which is Curve’s training center in Waco, Texas. Additional training is provided at regional events and at the company’s annual meeting, and any franchisee needing a refresher can return to Club Camp for free. This type of support is what attracts people of all backgrounds to the franchise concept, regardless of their prior work experiences. “We get people from all walks of life, says Cassie Findley, director of continuing education and research at Curves. “We get homemakers who want to become entrepreneurs and run their own businesses. We get retirees who want to help women change their lives, and we get a small percentage of investors. They’re not physical fitness professionals when they come to us.”[1]

> Franchising provides a small business owner the opportunity to own a business using a tested and refined business system.

Disadvantages of buying a franchise

The main disadvantages of buying a franchise are the costs involved and the loss of some of your independence as a business owner. The total initial investment to get a franchise up and running varies from $31,400 to $53,500 for a Curves franchise (depending on the location and other factors) to $74,900 to $222,800 for a Subway. The monthly royalty payments are permanent. While there are similar costs involved with starting a business from scratch, there are no ongoing royalty payments. In regard to independence, many franchise systems are sticklers about doing things in a specific manner. McDonald's and other fast-food retailers, for example, are strict in terms of their restaurants' appearance and how their food is prepared. As a result, franchising is typically not a good fit for people who like to experiment with their own ideas and are independent.

Ultimately, franchising represents an attractive middle ground for many people. So says Joe Cummings, the purchaser of a PostNet franchise. A PostNet franchise is similar to a FedEx Kinko's store. After a 21-year career with Bristol-Myers, Cummings took a buyout and spent a year deciding on what to do next. Commenting on why he settled on a PostNet franchise rather than opening his own business, Cummings said, "I wanted to get what I call the best of both worlds—the support of a proven system in an environment that's really entrepreneurial. I felt a franchise was the best way to do that."[2]

> The main disadvantages of buying a franchise are the costs involved and the loss of some of your independence as a business owner.

Caution

One note of caution: You should be careful if you decide to buy into a franchise system. While there are many excellent franchise systems to choose from, some systems never live up to the level of support promised. The best way to check out the merits of a franchisor is to ask for the names, addresses, and phone numbers of several of the franchisor's current franchisees and then call these individuals and ask them about their experiences. You can also ask for a copy of the franchisor's Franchise Disclosure Document (FDD), which contains detailed information about the background and financial health of the franchisor.

Truth 13. Believe it or not: There are legitimate opportunities in direct sales

While most people wince or cringe when they hear the words “direct sales” (or “multilevel marketing”), there are attractive and legitimate direct sales opportunities. The industry is dominated by women (85.2 percent), who normally enter direct sales part-time as a way of earning extra income.[1] There are over 15.2 million people in the United States involved in direct sales, and the number keeps growing.[2] Well-known companies include Tupperware, The Pampered Chef, Creative Memories, and Mary Kay. Many direct sales organizations are large and growing. The Pampered Chef alone has over 60,000 independent sales consultants. Its consultants conduct over one million in-home demonstrations, called Cooking Shows, every year.[3]

> The Pampered Chef is an example of a direct sales organization that exemplifies the good in the industry.

Many people have negative feelings toward the direct sales industry because they have either personally been subjected to a high-pressure sales pitch or know someone who has. Although the industry as a whole suffers as a result of these types of sales tactics, not all direct sales firms fit this stereotype. The Pampered Chef is an example of a direct sales organization that exemplifies the good in the industry. Started by Doris Christopher in 1980, the integrity and stature of the company is such that it was acquired by Berkshire Hathaway in 2002. Berkshire Hathaway is controlled by Warren Buffett, one of the most respected and well-known investors in the world. In the Foreword to the book, *The Pampered Chef*, in which Christopher chronicles the history of the company, Buffett writes,

> *“The Pampered Chef is truly loved by its customers because it has found a need and filled it exceptionally well, helping everyday home cooks to become masters of their own home kitchens and making mealtime preparations quick, easy, and fun. It also offers its consultants an incomparable business opportunity, allowing men and women to build a home-based business of their own, based on Doris Christopher’s personal blueprint for success. When you read the profiles of The Pampered Chef’s Kitchen Consultants in Chapter*

> *8, you may wonder what you're doing in your nine-to-five cubicle while these folks are happy cooking their way to fame and fortune."*[4]

Most people start with an organization like The Pampered Chef part-time and only make it a full-time job if they do extremely well. The sales typically take place through in-home sales demonstrations or parties, although an increasing percentage of direct sales are taking place online. In addition to selling the product, you recruit others to sell the product for you. You then receive a percentage of your recruits' sales. This facet of direct sales is one of its biggest lures. It allows you to earn income from your efforts along with the efforts of the people you recruit. It also incents the person who signed you up to provide you ongoing mentoring and support, since that person also receives a percentage of your sales.

If you go the direct sales route, make sure you pick a company that sells a product or service that you're passionate about. Since the majority of your sales will come through one-on-one product demonstrations or home parties, you'll need to convey a genuine interest and passion for the product you're selling to be successful. The biggest mistake that people make when they go into direct sales is to become more enamored with the "financial opportunity" than the product or service they sell.

> The biggest mistake that people make when they go into direct sales is to become more enamored with the "financial opportunity" rather than the product or service that they sell.

You should also be careful about the specific direct sales organization that you sign up with. Avoid organizations that require you to buy a ton of product upfront or promise that you'll get rich with little effort. One way to minimize the chances that you'll select a company you'll later regret is to restrict your selection to organizations that are members of the Direct Selling Association (www.dsa.org), a highly respected industry trade group. To become a member of the Direct Selling Association, a firm has to go through a rigorous one-year application process and abide by the organization's Code of Ethics. Currently, only 213 of more than 1,000 direct sales organizations that exist are members. If an organization is not a member of the Direct Sales Association, and you're still interested in joining, you should, at a minimum, check the company's history with your local Better Business Bureau, your state's Attorney General, and the Federal Trade Commission.

Truth 14. Buying a business

If you’re intrigued by the idea of owning and operating a business but don’t want to start a business from scratch or pursue franchising or direct sales, a final option is to buy an existing business. Although there are many rewards associated with building a business from the ground up, there are distinct advantages to buying a business that’s already established. There will also be an increasing number of businesses for sale to choose from. An estimated 65 percent to 75 percent of all small businesses in the United States—some 10 million—will likely go up for sale over the next five to ten years as a result of the retirement of baby boomers.[1]

There are two primary advantages to buying an existing business. First, you avoid the time and expense involved with selecting and testing a business idea. Second, you start, on day one, with a business that has customers and an established cash flow.[2] You’ll also have an easier time obtaining financing or funding. Bankers like to see three to five years of proven performance before they lend money to a business. As mentioned in Truth 11, “Starting from scratch: Developing your own product or service,” this reality works to the advantage of the buyers of existing businesses and to the disadvantage of businesses started from scratch.

> Although there are many rewards associated with starting a business and building it from the ground up, there are distinct advantages to buying a business that’s already established.

All told, there are ten primary advantages to buying a business versus starting one from scratch:

- Established customers
- Established products or services
- No time invested in picking and testing a business idea (at least initially—new products or services may be added later) ■Proven business concept and processes ■Trained employees ■Business generates cash flow from day one ■ Established suppliers
- Easier to obtain financing or funding ■Seller may lend support and assist with financing ■Lower risk of failure

An existing business may also offer amenities, like an ideal location, which you'd never be able to replicate starting a similar business from scratch.

The primary disadvantage to buying an existing business is the cost. The hard work involved with starting and building a business, along with the customers and cash flow that come with it, is built into the purchase price. This intangible is often called *goodwill*, which is the excess of the purchase price over the value of the assets of the business. So it's generally more expensive to buy an existing business than it is to start a similar one from scratch. There is also the possibility of hidden costs. For example, some of a business's best employees may leave once the business changes hands, even if they indicated they would stay. Similarly, receivables that were thought to be collectable may turn out to be uncollectable. You can anticipate these types of complications and build them into your offer price to a degree, but it's hard to anticipate everything, and disappointments often occur.

It's also hard to find a profitable business for sale at a reasonable price. Business owners often have an inflated idea of the market value of their business. In addition, it's not uncommon for the owners of businesses with fading potential to try to unload them, regardless of how good they try to make them appear. Still, thousands of businesses are bought and sold every year with good results. The most common places to look for businesses for sale include

- Newspaper classified advertising under "Business Opportunities"
- Business opportunity magazines, which are available at major bookstores
- Business brokers (identified through yellow pages advertising and Internet searches)
- Word of mouth through friends, family, and business acquaintances
- Internet searches (listed under "business opportunities" or "businesses for sale")

Proceed cautiously and thoroughly check out the businesses that spark your interest. If you get serious about a particular business, hire an attorney to represent you. You may also want to hire an accountant to help you go over the business's books. While you'll have to swallow hard when these professionals quote their fees, it's normally small potatoes compared to making a major mistake in the process of buying a business.

Proceed cautiously and thoroughly check out the businesses that spark your interest.

Truth 15. Internet businesses: The sky does seem to be the limit

Although starting an Internet business isn't a distinct business-entry strategy, like starting a business from scratch or buying a franchise, many people put it in a category of its own. The Internet, as a place to do business, continues to grow, and there are a number of ways that individuals are starting part-time and full-time businesses that are strictly online.

While many Internet businesses simply sell products or services online rather than through brick-and-mortar stores, one of the beauties of the Internet is that you don't have to have a product or service to sell to support an online business. If you know a lot about a particular topic, such as cooking, investments, or home repair, you can launch a Web site, populate it with articles and other useful information, and make money by essentially selling access to the people you attract to your Web site. You do this by selling advertising space on the Web site. This one factor has enabled numerous people to convert hobbies and personal interests into part-time and full-time online businesses.

People make money online in a variety of ways; however, this Truth focuses on how people support part-time and full-time businesses via Web sites. The two most common ways are e-commerce Web sites and advertising-supported special-interest Web sites.

E-commerce Web sites

E-commerce refers to the direct buying and selling of products and services online. Most e-commerce companies sell products, although there are a growing number of online businesses that sell services. People opt to sell products and services online rather than through traditional means for a variety of reasons. Some online stores are set up to sell a product that wouldn't sell in sufficient volume to support a brick-and-mortar store. An example is Oddball Shoe Company (www.oddballshoe.com), a Web that sells a size 16 EEEE athletic shoe for men and similar odd-sized shoes. Another rationale for an online store is to gain a broad audience for a specialty item. An example is Wadee (www.wadee.com), a Web site that sells handmade children's toys.

There are two ways that Web sites that sell products are set up. Some companies make their own products or stock products made by others and then ship them to customers when they receive an order. Other companies utilize a process referred to as *drop shipping*. Drop shippers feature an online storefront but don't have inventory. Instead, when they take an order, they pass it on to a wholesaler or manufacturer, who fills the order and then ships it directly to the customer—usually in a box with the online retailer's name and invoice inside. By utilizing this method, an online merchant earns a lower margin than it would if it controlled the entire process itself, but its costs are lower, too. It also doesn't get stuck with inventory that goes out of style. eBags (www.ebags.com), an e-commerce company that sells luggage, backpacks, and similar items, is an example of a drop shipper.

> Some online stores are set up to sell a product that wouldn't sell in sufficient volume to support a brick-and-mortar store.

Advertising-supported special interest Web sites

The second type of Web site that supports part-time or full-time businesses is an advertising-supported special interest Web site. These sites post articles, tips, and other forms of information about a specific topic or category of topics and make money by attracting visitors to the site and then selling advertising to companies interested in reaching those visitors. There are three ways to sell advertising on a Web site:

- **Pay-per-click programs—** A pay-per-click program places ads on Web sites, and the owner of the site is paid a small commission every time someone clicks on the ad. All the major search engines sponsor pay-per-click ad programs. Examples include Google's AdSense, Yahoo! Search Marketing, and MSN adCenter. The most compelling aspect of pay-per-click programs is that they deliver contextually relevant ads. This means the ads mirror the content of your site, which is good for the advertiser and helps boost your commissions.

> A pay-per-click program places ads on Web sites, and the owner of the site is paid a small commission every time someone clicks on the ad.

- **Affiliate programs—** An affiliate program is a way for online merchants, like 1-800-FLOWERS or Amazon.com, to get more exposure by offering a commission to Web sites that are willing to feature ads for their products or services. In most cases, the ads are small text ads, and the merchant sponsoring the program pays the affiliate a small commission every time someone clicks on the ad and buys one of its products or services.

- **Direct ads—** You can also go directly to advertisers and sell space on your Web site. These ads tend to be banner ads, skyscraper ads (tall ads that run along the side of a Web site), or ads with pictures that are embedded in the content of a Web site. If you run ads like these on your Web site, you're paid a commission based on either the number of times an ad is clicked or the number of times it is seen (that is, the number of *impressions*).

An example of an advertising-supporting Web site that has good content and generates substantial revenue is Ask the Builder (www.askthebuilder.com), which is sponsored by Tim Carter, a well-known columnist on home repair. Information and instructions on all types of home building projects and repair are available on this Web site, as are links to areas that focus on specific topics, like air conditioning, deck construction, and plumbing. Clicking any one of these areas brings up Google AdSense ads that deal with that specific area. All together, the site has hundreds of AdSense ads. Carter can do this and still attract large numbers of visitors because the information he provides is good and helpful.

Part IV The Truth About Getting Up and Running

Truth 16. Choosing a location for your business

As a new business prepares to get up and running, there are a number of decisions that must be made. One of the most significant is where the business will be located. A good choice of location can help a business get off to a solid start, while a poor choice can have the opposite effect. A poor choice can also be difficult to fix, particularly if a business signs a long-term lease or purchases property.

Fortunately, there is a standard set of issues to consider when selecting a business's location.

For some businesses, location is key, while for others it's almost irrelevant. For example, many service businesses—such as painters, electricians, mail-order companies, and Internet businesses—don't interface directly with the public, so their physical location isn't a major issue. In fact, these businesses often seek out nondescript locations to economize on costs. In contrast, location is an extremely crucial issue for retail stores, certain service businesses, and professional practices (like doctor's offices) that deal directly with the public.

> A good choice of location can help get a business get off to a solid start, while a poor choice can have the opposite effect.

If location is important, what type of location will work best for you?

The key consideration here is to pick a location that will increase your flow of customers. Start by asking yourself the following questions:

- Will my customers come on foot, or will they drive and need a place to park?
- Will more customers come if the business is located near other similar businesses?
- Will more customers come if the business is located near complementary businesses?
- Do the demographics of the trade area the business will be located in make a

difference?

Answering these four questions can go a long way in helping a business owner select an appropriate location. For example, if you're opening an urban bagel shop or a similar type of business, you'll want to locate in an area that has a high amount of foot traffic. In contrast, if you're opening an auto parts store or a convenience store, you'll want to be on a busy street where the store can be seen by drivers who can pull into your parking lot. In terms of being near similar businesses, clothing stores and jewelry stores, for example, often benefit by being near similar businesses, since people like to comparison shop. A hair salon or barber shop, where comparison shopping isn't as much of an issue, may do better by itself. Some businesses benefit by locating near a big-box store like Wal-Mart or Target, because their customer bases are similar and they benefit from the increased traffic. An example is Sally's Beauty Supply, which appears in 26 percent of U.S. Wal-Mart-anchored shopping centers.[1] Similarly, some businesses benefit by being located near complementary businesses. Ice cream shops, for example, do better when they're located near movie theaters and restaurants.

An extremely important issue is whether the demographic makeup of a trade area is suitable for a particular business. A high-end clothing boutique, for example, needs to be in an affluent area. Stores that sell children's clothing do better in areas with a high percentage of young families than in areas with a high percentage of retirement-age people. You can obtain the demographic breakdown of most communities in the United States (and even zip codes within communities) via American FactFinder (http://factfinder.census.gov), which is a Census Bureau Web site. Another good source is City-Data.com (www.cita-data.com), which contains similar and often more current demographic information on U.S. cities and towns.

How much can you afford?

A third consideration is how much you can afford. This is a tough issue, because the best locations invariably are the most expensive. Most businesses that aren't home-based businesses rent or lease property rather than build or buy, which reduces the cost some.[2] The best way to determine the rental or lease rates for a particular area is to talk to a real estate broker or agent. Ultimately, a business can only occupy premises that it can afford. There is no practical way around this issue other than to carefully weigh your financial priorities. In some cases, a business, like an urban bagel shop, may be better off spending more than originally budgeted on a premium location and less than originally budgeted on ancillary items like computer equipment or the restaurant's decor. You need to dedicate limited resources to the areas that ultimately will make the largest positive impact on your business.

Is the physical structure you're considering adequate?

Once you locate a property to lease or rent, you should be careful to make sure it is adequate for your business. For example, if you are considering space for an Internet business, it will need to be wired to connect to a fiber-optic network or a T1 line (high-volume Internet connection). If you will be cooking in a building, it may need to be vented in a certain manner and need additional plumbing and electric work. While these issues may seem obvious, it's often a matter of negotiation regarding who will pay for the upgrades that are needed. If you can't convince the landlord to do the necessary work, a seemingly ideal location may be cost-prohibitive. There are other issues that are potentially negotiable, so make sure you think through your circumstances carefully. For example, if you open a retail store in an enclosed mall or strip mall, you can often negotiate what's called a *restrictive covenant* to prevent the landlord from leasing space to one of your direct competitors.

Complying with local zoning laws is another principal issue. Never sign a lease and occupy a property until you're confident it's zoned for your type of business.

Truth 17. Something you'll say a million times: Your business's name

While at first glance naming a business may seem like a minor issue, it is an extremely important one. A company's name is one of the first things people associate with a business. Keep in mind that it is a word or phrase that will be said thousands or hundreds of thousands of times during the life of a business. A company's name is also the most critical aspect of its branding strategy. A business's name must facilitate rather than hinder how the business wants to differentiate itself in the marketplace and how it wants to be viewed by its customers.

The primary consideration in naming a business is that the name should complement the type of business the company plans to be. It is helpful to divide companies into four categories to discuss this issue.

> The primary consideration in naming a business is that the name should complement the type of business the company plans to be.

Consumer-driven companies

If a company plans to focus on a particular type of customer, its name should reflect the attributes of its clientele. For example, a clothing store that specializes in small sizes for women is called La Petite Femme. Similarly, an online store that sells clothing for big and tall men and boys is named Big and Tall Guys. A company that installs cameras in day care centers and allows parents to log on to a password-protected Web site to see their children during the day is called ParentWatch. These companies have names that were chosen to appeal specifically to their target market or clientele.

Product-or service-driven companies

If a company plans to focus on a particular product or service, its name should reflect the advantages that its product or service brings to the marketplace. Examples include 1-800-FLOWERS, Whole Foods Markets, XM Satellite Radio, and Jiffy Print. These names were chosen to reflect the distinctive attributes of the product or service the company offers, regardless of the clientele.

Industry-driven companies

If a company plans to focus on a broad range of product or services in a particular industry, its name should reflect the category it is participating in. Examples include Sports Authority, Bed Bath & Beyond, Toys R Us, and Home Depot. These companies have names that are intentionally broad and are not limiting in regard to target market or product selection.

Personality-or image-driven companies

Some companies are founded by individuals who put such an indelible stamp on the company that it may be smart to name the company after the founder. Examples include Charles Schwab, The Trump Organization, Calvin Klein, and Magic Johnson Enterprises. These companies have names that benefit from a positive association with a particular person or distinctive founder. Of course, this strategy can backfire if the founder falls out of favor in the public's eye.

Other considerations

There are also some general rules of thumb for naming a business. Select a name that is easy to spell, easy to pronounce, and doesn't limit the future expansion of the business. For example, a name like Sally's Sewing Supplies isn't a good choice. It's easy to spell and pronounce, but at some point the business might want to expand beyond sewing supplies. Once you settle on a name, you should contact the Secretary of State's office in the state where you're located to make sure the name is available. If it is, you should reserve it in the manner recommended by the Secretary of State. You should also trademark the name. Information about how to trademark a business's name is discussed in Truth 35, "Trademarks: An essential form of protection."

> Select a name that is easy to spell, easy to pronounce, and doesn't limit the future expansion of the business.

A final factor to consider in selecting a name for a business is whether its Internet domain name is available. This can be a frustrating endeavor, because the majority of the most obvious names have already been taken. If the name you’ve chosen for your business isn’t available, don’t panic. A little ingenuity can go a long way. You can normally either tweak the name of your business or your Internet domain name to make things work. For example, suppose you have decided to open a restaurant that will feature low-fat dishes and have settled on the name Healthy Options. You check and find that the Internet domain name www.healthyoptions.com is taken. You don’t need to give up on the Healthy Options name. You can vary the Internet domain name as long as it makes sense. For example, at the time this book was written, the Internet domain name www.healthyoptionsrestaurant.com was available—a perfectly acceptable Internet domain name for your business.

Truth 18. The paper chase: Obtaining business licenses and permits

If you're anxious to get your business started, the last thing you normally want to do is deal with government paperwork. Do it anyway. It's important to obtain the licenses and permits you need. You can also be subject to stiff penalties if you don't comply in a timely manner.

Most of the licenses and permits you'll need are required to be in place before your business opens. They vary by city, county, and state, as well as by the type of business you plan to start, so study the regulations carefully. Some licenses are difficult to get—such as liquor licenses. For example, in some states, the only way to get a liquor license is to buy a preexisting license. This stipulation often results in a bidding war when someone is willing to give up their liquor license, which increases the price. Enjoy the paper chase.

> Most of the licenses and permits you'll need are required to be in place before your business opens.

Obtaining a business license

Most communities require businesses to obtain a license to operate. Your city clerk should be able to handle this for you. If you plan to operate your business from home, a separate home occupation business license is often required. When you apply for a license, your city planning and zoning department will usually check to make sure your area is zoned for the purpose you want to use it for. If your business is located outside a city or town's jurisdiction, you'll need to go to your county courthouse to obtain your business license.

If you're a sole proprietor, you can usually stop here, as far as your business license goes. If you have employees, or your business is a corporation, a limited liability company, or a limited partnership, you'll need a state business license in addition to your local one. There are additional state provisions that you may need to comply with. If you're starting a retail or service business, you'll need to obtain a sales tax license, which enables you to collect taxes on the state's behalf. You'll need a special license to sell liquor, lottery tickets, gasoline, or firearms. People in certain professions, such as barbers, chiropractors, nurses, and real estate agents, must normally pass a state examination and maintain a professional license to conduct business. This category covers a wide swath of businesses, so check with your state government to see if your profession applies. Certain businesses also require special state licenses. Examples include child care, health care facilities, hotels, and restaurants. Again, check with your state to see if your business is subject to special licensing and inspection requirements.

> If you're starting a retail or service business, you'll need to obtain a sales tax license, which enables you to collect taxes on the state's behalf.

A narrow group of businesses are required to have a federal business license, including investment advising, drug manufacturing, preparation of meat products, broadcasting, interstate trucking, and businesses that manufacture tobacco, alcohol, or firearms, or sell firearms. These licenses are obtained through the Federal Trade Commission.

Nearly all business are required to obtain a federal *employer identification number (EIN)*, also known as a tax identification number, which is used in filing various business tax returns. The only exception is sole proprietors who do not have employees. In this instance, the sole proprietor uses his social security number as the tax identification number. You can obtain a tax identification number free from the Internal Revenue Service by calling 800-829-4933.

Permits

Along with obtaining the appropriate business licenses, you may need to obtain one or more business permits, depending on your location and the nature of your business. The permits regulate how you do business. For example, if you plan to sell food, either as a restaurateur or as a wholesaler to other retailers, you'll need a city or county health department permit. If your business will be open to the public or will use flammable material, you may need a fire department permit. Some communities require businesses to obtain a permit to put up a sign. Because requirements vary from city to city on these and other issues, you'll need to ask around to see if any special permits are required for your business. If you're occupying a building, there will also be building code requirements you'll have to comply with.

All businesses that plan to use a fictitious name, which is any name other than the business owner's name, need a fictitious business name permit (also called a *dba* or *doing business as*). If you're a sole proprietor, you can obtain the permit at the city or county level. For example, if your name is Sarah Ryan and you apply for a business license, your business will be registered as Sarah Ryan. If you want to use another name, like Gulf Coast Fresh Flowers, you must apply for a fictitious name permit. You normally need a fictitious name permit to obtain a checking account in your business's name. It's also important to have a fictitious name permit if you execute any contracts, sign any agreements, or pay bills or accept payments under your business's name.

Sources of assistance

There are a number of resources available to assist business owners in identifying the proper licenses and permits to apply for. The Small Business Administration (SBA) maintains a Web site, at www.sba.gov/hotlist/license.html, that features links that provide information on how to obtain a business license in each state. In addition, most major bookstores, like Borders and Barnes & Noble, carry publications that talk about "doing business in" whatever state you are located in. These publications normally cover business licensing and permit procedures for the applicable state. Many city governments also publish documents that provide guidance for doing business in their city. Good places to look for these publications are the city government's Web site, the city library's Web site, or the Web site for the local Chamber of Commerce. For example, the Dallas Public Library publishes a publication titled "Starting a Small Business in Dallas: A Resource Guide." The guide is available via the Dallas Public Library's Web site at http://dallaslibrary.org/CGI/smallbiz.htm.

Truth 19. Choosing a form of business ownership

When you launch a business, you need to choose a form of legal entity. Sole proprietorship, partnerships, corporations, and limited liability companies are the most common. There is no single form of business ownership that works best in all situations.

Sole proprietorship—The simplest form of business ownership is the sole proprietorship,[1] which involves one person. The person and the business are essentially the same. The biggest advantage of the sole proprietorship is that the owner maintains complete control over the business. The biggest disadvantage is that the sole proprietor is responsible for all the liabilities of the business. If a sole proprietor's business is sued, the owner could theoretically lose all the business's assets along with personal assets. As a result, a sole proprietorship is not a good choice for most new businesses.

Advantages of a sole proprietorship:

- Creating one is easy and inexpensive.
- The owner maintains complete control of the business and profits.
- It is not subject to double taxation (explained later).

Disadvantages of a sole proprietorship:

- Liability on the owner's part is unlimited.
- The business ends at the owner's death or loss of interest in the business.
- The liquidity of the owner's investment is low.

Partnerships—If two or more people start a business, they must organize as a partnership, corporation, or limited liability company. Partnerships are organized as either general or limited partnerships. The primary advantage of a general partnership is that the business isn't dependent on a single person for its success. The primary disadvantage of a general partnership is that the individual partners are liable for all the partnership's obligations. As a result, a general partnership is typically not a good choice for a new business.

Advantages of a general partnership:

- Creating one is easy and inexpensive.
- Business losses can be deducted against the partner's other sources of income.
- It is not subject to double taxation (explained later).

Disadvantages of a general partnership:

- Liability on the part of each general partner is unlimited.
- Disagreements among partners can occur.
- The liquidity of each partner's investment is low.

The second form of partnership is the limited partnership. The primary difference between the two is that a limited partnership includes two classes of owners: general partners and limited partners. The general partners are liable for the obligations of the partnership, but the limited partners are liable only up to the amount of their investment.

Corporations—A corporation is a separate legal entity organized under the authority of a state. Corporations are organized as either C corporations or subchapter S corporations. A C corporation is a legal entity that is separate from its owners. The major advantage of a corporation is that it shields its owners from personal liability for obligations of the business. The major disadvantage is that a corporation is subject to double-taxation—the corporation is taxed on its net income and, when the same income is distributed to shareholders in the form of dividends, it is taxed again on the shareholder's personal income tax returns.

Advantages of a C corporation:

- Owners are liable only for the obligations of the corporation up to the amount of their investment.
- No restrictions on the number of shareholders.
- The ability to share stock with employees through incentive plans can be a powerful form of employee motivation.

Disadvantages of a C corporation:

- Setting up and maintaining one is more difficult and expensive than a sole proprietorship or general partnership.
- Business losses cannot be deducted against the shareholder's other sources of income.
- Income is subject to double taxation.

A subchapter S corporation combines the advantages of a partnership and a C corporation. It is similar to a partnership in that the profits and losses of the business are not subject to double taxation. It is similar to a corporation in that the owners are not subject to personal liability for the behavior of the business. The major disadvantage of the subchapter S corporation is that it is limited to 100 shareholders, which can be a drawback when trying to raise money from a large pool of investors.

Limited liability company—The limited liability company (LLC) is a form of business organization that is gaining popularity in the United States. The main advantages of the LLC are that it is more flexible than a subchapter S corporation in terms of number of owners and tax-related issues, and all members enjoy limited liability. The main disadvantages are that it is relatively complex to set up, and in some states the rules governing the LLC vary.

Advantages of a limited liability company:

- Members are liable for the obligations of the business only up to the amount of their investment.
- The number of shareholders is unlimited.
- There is no double taxation.

Disadvantages of a limited liability company:

- Setting up and maintaining one is more difficult and expensive than the other legal entities.
- Some of the regulations governing LLCs vary by state.
- Some states levy a franchise tax on LLCs, which is essentially a fee the LLC pays the state for the benefit of limited liability.

According to a study published by the Kauffman Foundation, 35.5% of businesses start as sole proprietorships, 30.5% start as LLCs, 20.1% start as subchapter S corporations, 7.9% start as C corporations, and 5.7% start as limited or general partnerships.[2] It is money well spent to consult with a small business accountant or attorney to select the form of business ownership most appropriate for your start-up.

Truth 20. Creating a Web site: An absolute necessity

Imagine the following scenario. Your 10th wedding anniversary is coming up, and you and your spouse have talked about trying a new restaurant, called Helen's Grill, which just opened. You want to make sure the evening is special, so you decide to learn more about the restaurant. You go to Helen's Grill's Web site and view pictures of its interior, look at the menu, read comments from satisfied customers, and click on a link labeled "Reservations for special occasions." You find that the restaurant will set up a table for you and your spouse with fresh flowers, a bottle of wine, and a personalized anniversary greeting. You make the reservation. Helen's Grill acquires a new customer.

If you're starting a business, you need to be like Helen's Grill. You need a Web site to introduce yourself to customers, share information about your business, and conduct e-commerce if appropriate. Although building a Web site takes money and effort, it's a business necessity. A recent study of small businesses that have a Web site found that 78 percent feel their business benefits by being online.[1]

> Although building a Web site takes time, money, and effort, it's a business necessity.

Creating a Web site involves three key steps: determining the objectives of the site, building the site, and monitoring the site to assess and improve its effectiveness.

Determining the objectives of your Web site

There are many options regarding the look and functionality of a Web site, so it's important to determine what you want your Web site to accomplish before you start building it. There are basically three levels of Web sites to choose from[2]:

- **Basic Web site—** A basic Web site introduces your business and consists of a few pages that highlight your product or service, archive news releases and press about your business, and provide contact information. These sites are usually created from a template and cost as little as $200 if you build it yourself or between $1,000 and $3,000 if you hire someone else to do it.

- **Intermediate Web site—** An intermediate site allows you to receive online requests, sell products via a shopping cart, process credit cards, and display more information than a basic site. These sites are customized by a Web site designer and cost between $1,500 and $6,000.
- **Advanced Web site—** An advanced site does everything an intermediate site does along with complex tasks like tracking inventory and maintaining customer databases. These sites involved specialized programming and run $5,000 and up.

Building Your Web Site

If you're content with a basic Web site and have a limited budget, there are do-it-yourself Web site packages available through vendors such as Homestead (www.homestead.com) and Register.com (www.register.com). These companies sell packages that include instructions and tools for building a Web site, along with the services necessary to launch and maintain the site. If you don't want to do the work yourself, or you want an intermediate or advanced site, you'll have to hire a Web design firm.[3] One thing to be careful of is not to totally turn over the design and maintenance of your Web site to someone else. Although you may need a Web design firm to build and host your site, you should learn how to add content to your site and make changes on your own.

Many excellent books and periodicals talk about Web site design. You should consider several questions when building your site and on a periodic basis after it's up and running.

- Is it visually appealing?
- Do the pages load quickly?
- Is the layout well organized?
- Is it easy to navigate?
- Does it answer the most obvious questions that someone coming to the site might have?
- Is the site easy to find?
- Does the site emphasize the points that differentiate my company from my competitors?

Monitoring your Web site to assess and improve its effectiveness

The third step in launching and maintaining a Web site is to monitor its effectiveness and make changes when necessary. This is an activity (called Web analytics) that many small businesses don't engage in. When you launch your site, you have to hire a company to host it. Make sure that your host is set up to give you statistics on the usage of your site, or hire a separate company to give you the information. A sample of the information you can obtain is as follows:

- The number of visitors you have each hour, day, and week of the month
- The number of unique visitors that you receive (on a daily or weekly basis)
- A report on where your visitors come from
- A report on what pages on your Web site are viewed the most frequently
- Statistics that track a sales campaign's effectiveness

By analyzing this type of information, you can see the pages and products that people are most interested in, whether there are a high number of people visiting a particular product page but not buying (indicating that the page needs to be reworked), and how well offline promotional campaigns are working. For example, if Helen's Grill ran a series of ads in a local newspaper, and it prominently displayed its Web site address in the ads, one way it could measure the success of the newspaper campaign is by monitoring the degree to which the ads increased traffic to its Web site.

Part V The Truth About Raising Money

Truth 21. How to think about money as it relates to starting a business

A concern that most prospective business owners have is whether they'll be able to raise sufficient funds to start a business. It's a legitimate concern. It does take money to start and grow a business. But the amount of money needed to start a specific business is not a set amount. The same business might cost one person $10,000 to start and another person $25,000—trust me, this isn't an exaggeration. The amount needed depends on how a person thinks about money as it relates to the start-up process, how frugal a person is, and how resourceful a person is in gaining access to money and other resources.

The following are two categories of insights regarding the role of money in starting a business. As you read through these insights, think about your own attitudes about money. One of the reasons that many businesses are started for as little as they are is that people adjust their attitudes about money as they get acquainted with the start-up process.

> One of the reasons that many businesses are started for as little as they are is that people adjust their attitudes about money as they get acquainted with the start-up process.

Skimpy finances can be a blessing rather than a curse

The first category of insights regarding money and the start-up process is that there is a silver lining to having limited start-up funds. While Truths 23 through 27 focus on how to raise start-up funds, more people finance their start-ups with their own money than from bank loans, money from investors, or some other means.[1] Although this reality leaves many business owners with skimpy start-up funds, there is an upside. Many successful business owners, looking back, feel that having limited funds forced them to focus, become self-reliant, and develop a mindset of frugality—qualities that have served them well as they've grown their firms. This sentiment is affirmed by Caterina Fake, cofounder of Flickr, the popular photo-sharing Web site, which was started in 2002. In reflecting back on the role of money in the early days of her firm, Fake said:

> *"The money was scarce, but I'm a big believer that constraints inspire creativity. The less money you have, the fewer people and resources you have, the more creative you have to become. I think that had a lot to do with why we were able to iterate and innovate so fast."*[2]

There is another silver lining to launching a firm with limited funds. Although in some cases it is necessary to go to a bank or an investor to obtain financing, the problem with obtaining money from these sources is that there are consequences that business owners often don't fully anticipate. While most bankers and investors have good intentions, they assert considerable control over the businesses they provide money to as a means of protecting their investments. So for people leaving traditional jobs to start their own businesses, obtaining money from a banker or investor is often like trading one boss for another. You might free yourself from working for a boss in a traditional sense but could have an equally influential boss in the form of a banker or investor.

Techniques that enable business owners to minimize start-up costs

The second category of insights regarding money and the start-up process is that there are techniques that enable business owners to minimize the costs associated with starting a business. There are three predominant techniques.

The first technique is to select an appropriate business to start. If you have limited start-up funds, you should start a business that requires a small up-front investment. Fortunately, many businesses meet this criterion. Home-based businesses, which now represent more than half of the 26.8 million U.S. small businesses, are popular largely because they take very little capital to start. The second technique is to seek out help. For small business owners, there are many sources of assistance that provide counsel and advice on how to minimize start-up expenses. An example is the Service Corps of Retired Executives (SCORE), which is a nonprofit organization that provides free consulting services to small business. There are also organizations that provide coaching and support to specific groups of business owners and tailor their offerings to fit the groups. An example is Ladies Who Launch, an organization that sponsors workshops and provides materials that encourage and inform female business owners.[3]

The third technique is to cut costs and save money at every opportunity. The most effective way to do this is to develop a mindset of frugality and resourcefulness. While many people aren’t naturally frugal, they foster these qualities to get their businesses off the ground and to minimize the costs of their ongoing operations. Common money-saving techniques include buying used equipment instead of new, obtaining payments in advance from customers, and buying items cheaply but prudently through discount outlets or online auctions such as eBay, rather than at full-price stores.

Truth 22. Calculating your initial startup costs

The first step in determining how much money it will take to start a specific business and whether you'll need to pursue outside financing is to determine your startup costs. A business's startup costs refer to the total cash needed to get the business up and running. All businesses incur expenses before they make their first sale. A common mistake that business owners make is to underestimate their startup costs and get caught short on cash before their business even opens.

> A common mistake that business owners make is to underestimate their startup costs and get caught short on cash before their business even opens.

How to calculate your startup costs

Prepare a budget that lists all the costs that you'll incur to launch your business. You need to consider four categories of costs.

- **Capital costs—** This category includes real estate, buildings, equipment, vehicles, furniture, fixtures (shelves, wall brackets, cabinets), and similar capital purchases. These costs vary considerably depending on the business. A restaurant or retail store may have substantial initial capital costs, while a home-business may have little to no capital expenses.
- **"One-time" expenses—** This category includes legal expenses, fees for businesses licenses and permits, deposits for utilities, Web site design, business logo design, and similar one-time expenses and fees. All businesses incur at least some of these expenses.
- **Provisions for initial operating losses—** Many businesses require a ramp-up period in which they lose money until they are fully up to steam and reach profitability. For example, it usually takes a new fitness center several months to reach its membership goals. It's important to have cash set aside to make it through this period. If you have a business plan, and the plan includes pro forma (or projected) financial statements, you should

have an accurate estimate of your initial losses. If you don't have a business plan, experts recommend that you set aside six months of your business's estimated monthly operating expenses to see you through the ramp-up period. You'll need to estimate your monthly operating expenses to arrive at this figure.

- **Provisions for living expenses—** Experts also recommend that you set aside six months of living expenses for you and your family to see you through the ramp-up period. The need to do this depends on your individual situation. Some business owners have spouses who are working that can cover their living expenses. Other businesses start part-time, and the business owner keeps his or her full-time job until the business is cash-flow positive.

Don't get caught unaware regarding startup expenses. It is better to overestimate rather than underestimate the amount it will cost to launch your business, and adding a cushion is a good idea. Murphy's Law is prevalent in the startup world—things will go wrong. It is a rare startup that doesn't experience some unexpected expenses during the startup phase.

Finding information on startup costs

You need to estimate startup costs as accurately as possible. There are several ways of finding the information you need, all of which involve a little legwork. You can estimate your expenses item by item by contacting the appropriate vendors, government agencies, and people who can provide informed estimates. For example, if you're thinking about leasing space in a strip mall, you can usually obtain data on what strip mall space goes for from a local realtor or property manager. Another way to identify startup costs is to talk to the owners of businesses that are similar to the one that you're planning to start. You should try to find businesses that are outside your trade area so the owners don't see you as a potential competitor. Many first-time business owners are surprised by how cooperative and helpful other business owners are. Another approach is to contact a trade association that represents businesses in the industry you'll be entering. Many trade associations compile statistics on startup costs. There are also online resources that help business owners connect with people who are eager to help. For example, Startup Nation (www.startupnation.com) is an online community that allows business owners to connect with one another and chat about startup costs and other business-related topics.

Determining the financing that you'll need

Once you know what your startup costs will be, you'll be in a position to determine the most appropriate way to finance your business. The five ways to finance a new business include (1) personal funds (including loans from friends and family and bootstrapping), (2) debt financing, (3) equity funding, (4) grants, and (5) other potential sources of financing. These sources are discussed in Truths 23 to 27.

> Once you know what your startup costs will be, you'll be in a position to determine the most appropriate way to finance or fund your business.

Truth 23. Personal funds, loans from friends and family, and bootstrapping

The most common source of start-up funds is the founder's personal savings.[1] This source is closely followed by loans from friends and family and personal sources of debt, such as credit cards and home equity loans. If you're surprised by these statements, you're not alone. There is a prevailing belief that most business owners must appeal to bankers or investors to get their businesses off the ground. Some businesses do require bank loans or money from investors to get started, but the majority of business owners rely on personal funds, loans from friends and family, personal sources of debt, and bootstrapping to get started. This Truth focuses on loans from friends and family and boostrapping as two common ways of raising start-up funds. Both of these choices can be great sources of start-up funds, but you need to utilize them in ways that maintain positive family relationships and allow a business to reach its full potential. Personal sources of debt, such as credit cards and home equity loans, are discussed in Truth 24, "Debt financing."

> The most common source of start-up funds is the founder's personal savings. This source is closely followed by loans from friends and family.

Loans from friends and family

According to the Global Entrepreneurship Monitor, which is a joint research effort by Babson College and the London Business School, millions of businesses are financed each year with money from friends and family, while only a few thousand obtain funds from professional investors. In fact, in the United States, from 2000 to 2003, 5 percent of the adult population invested privately in some else's business. The investment went to close family members (41.8 percent), friends and neighbors (28.5 percent), other relatives (10.5 percent), strangers (9.4 percent), work colleagues (6.1 percent), and other (3.6 percent).[2] Besides offering loans, friends and family often help out new business owners with gifts, forgone or delayed compensation (if a friend or family member works for the new business), or reduced or free rent. For example, Cisco Systems, the giant producer of Internet-related gear, started out in the house of one of its cofounder's parents.

There are three rules of thumb that you should follow when asking friends and family members for start-up funds. First, you should present your request in a businesslike manner, just like you would to a banker or investor. Describe the potential of the business along with the risks involved. Second, if the help you receive is in the form of a loan, a promissory note should be prepared, with a repayment schedule, and the note should be signed by both parties. Stipulating the terms of the loan in writing reduces the potential of a misunderstanding and protects both you and the friend or family member providing the funding. Third, you should be careful to ask only people for help who are in a legitimate position to offer assistance. It's not a good idea to ask certain friends or family members, regardless of how much they may have expressed a willingness to help, for assistance if losing the money would cripple them financially. Remember, there are risks involved with any new business. If you're unable to repay a loan to a friend or family member, you risk not only damaging your business relationship with them but your personal relationship as well.

> You should be careful to ask only people for help who are in a legitimate position to offer assistance.

Bootstrapping

Bootstrapping is finding ways to raise start-up funds without the need for external funds through creativity, ingenuity, thriftiness, or any means necessary.[3] (The term comes from the adage "pull yourself up by the bootstraps.") It is the term attached to the general philosophy of minimizing start-up expenses by aggressively pursuing costs-cutting techniques and money-saving tactics, as discussed in Truth 21, "How to think about money as it relates to business." There are many well-known examples of business owners who bootstrapped to get their companies started. Legend has it that Steve Jobs and partner Steve Wozniak sold a Volkswagen van and a Hewlett-Packard programmable calculator to raise $1,350, which was the initial seed capital for Apple, Inc.

While bootstrapping is highly recommended in almost all start-up situations, there are subtle downsides. Cost-cutting and saving money are admirable practices, but if you push these practices too far, you can hold a business back from reaching its full potential. In addition, business owners who bootstrap by working out of their homes rather than renting office space are often lonely. The price of renting space in an office building or strip mall where there are other businesses present may be worth it if it provides a business owner access to a network of people who can be relied on to provide social support and business advice.

Truth 24. Debt financing

About 48 percent of businesses use some form of debt financing during their initial year of operation. The sources most frequently used are personal credit card debt (30.2 percent), personal bank loans (18 percent), business credit card debt (14.6 percent), and loans from friends and family (10.1 percent).[1] Note that the majority of debt financing is not in the form of a bank loan. Instead, business owners rely on more personal sources of debt financing to supplement their start-up needs.

> The majority of debt financing is not in the form of a bank loan. Instead, business owners must rely on more personal sources of debt financing to supplement their start-up needs.

There are two major advantages to debt financing opposed to equity funding, which will be discussed in Truth 25, "Equity funding." The first is that none of the ownership of the business is surrendered—a major advantage for most business owners. The second is that interest payments on a loan (in most cases) are tax deductible, in contrast to dividend payments made to investors, which aren't. There are two major disadvantages to debt financing. The first is that debt must be repaid. Cash is typically tight during a start-up's first few months and sometimes for a year or more. The second is that lenders often impose strict conditions on loans and insist on ample collateral to fully protect their investment. This often requires that a business owner's personal assets be collateralized as a condition of the loan.

Commercial banks are not a practical source of financing for most new businesses.[2] This sentiment isn't a knock against banks; it's just that banks are risk adverse, and financing start-ups is a risky business. That's not to say that you can't get a home equity loan to fund part or all of your start-up needs. It's just that most banks won't normally assume the risk of loaning money directly to a business with an unproven track record. They would rather loan money to an individual who has equity in a home to pledge as collateral.

When banks do loan money to start-ups, the money is often loaned through the Small Business Administration (SBA) Guaranteed Loan Program. This program is a realistic alternative for many start-ups and offers reduced interest rates and longer repayment terms than conventional loans. The SBA does not have money to lend but makes it easier for business owners to obtain loans from banks by guaranteeing the loans. The most notable SBA program available to small businesses is the 7(A) Loan Guaranty Program. The loans are for small businesses that are not able to obtain loans on reasonable terms through normal lending channels. Almost all small businesses are eligible to apply for an SBA guaranteed loan. The SBA can guarantee as much as 85 percent on loans up to $150,000 and 75 percent on loans over $150,000. In most cases, the maximum guarantee is $1.5 million. A guaranteed loan can be used for working capital to start a new business or expand an existing one. It can also be used for real estate purchases, renovation, construction, or equipment purchases. The best way to learn more about the SBA Guaranteed Loan Program and determine if you are eligible is to meet with a participating lender.

> One channel for borrowing funds that is getting quite a bit of attention is Prosper.com, a peer-to-peer lending network.

There are a variety of other avenues that business owners can pursue to borrow money. Getting loans from friends and family, as discussed in Truth 23, "Personal loans, loans from friends and family, and bootstrapping," is a popular choice. Credit card debt, although easy to obtain, should be used sparingly. One channel for borrowing funds that is getting quite a bit of attention is Prosper.com, a peer-to-peer lending network. Prosper is an online auction Web site that matches people who want to borrow money with people who are willing to make loans. Most of the loans made via Prosper are fairly small ($25,000) but might be sufficient to meet a new business's needs.[3] There are also organizations that lend money to specific demographic groups. For example, Count Me In, an advocacy group for female business owners, provides loans of $500 to $10,000 to women starting or growing a business.[4] An organization that is aligned with Count Me In and American Express, named Make Mine a Million $ Business, lends up to $50,000 to female-owned start-ups that have been in business for at least two years and have $250,000 or more in annual revenue.[5]

Some lenders specialize in *microfinancing*, which are very small loans. For example, Accion USA gives $500 credit-builder loans to people with no credit history.[6] While $500 might not sound like much, it could be enough to open a home-based business such as an eBay Store or to get started in a direct sales organization.

Truth 25. Equity funding

Equity funding is obtaining money from an investor. Investors are typically interested in businesses that plan to grow and can capture fairly large markets. These businesses normally have a unique business idea and a proven management team and are shooting to capture large markets. If your business fits this profile, and you're willing to accept the hectic pace of activity that running a rapid growth business entails, seeking equity funding may be a good option for your business.

The primary advantage of equity funding is access to capital, which is the reason it's often pursued by businesses that have high start-up costs. In addition, because investors become partial owners of the firms they invest in, they often try to help those firms by offering their expertise and assistance. The money received from investors also doesn't have to be paid back. The investor receives a return on the investment through dividend payments and by selling the stock. The primary disadvantage of equity funding is that the firm's owners relinquish part of their ownership interest and may lose some control.

There are two sources of equity funding: business angels and venture capitalists.

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Business angels

Business angels are individuals who directly invest their personal funds into start-ups. They generally invest between $10,000 and $500,000 in a single company and are looking for companies that have the potential to grow 30 to 40 percent per year (which is very aggressive) before they are acquired or go public.[1] Jeffrey Sohl, the director of the University of New Hampshire's Center for Venture Research, estimates that only 10 percent to 15 percent of private companies meet that criterion.[2] The one exception that might help you get your foot in the door with an angel investor, if your business doesn't meet the traditional criteria, is if the purpose of your business is aligned with a personal interest or passion of the investor. For instance, if you're starting a company to make a safer car seat for infant children and meet an angel investor who has an intense interest in child safety products, you could capture the investor's attention even if your firm isn't capable of a 30 to 40 percent per year growth rate.

Most business angels remain fairly anonymous and are matched up with business owners through referrals. If you're interested in pursuing angel funding, you should discretely work your network of acquaintances (bankers, lawyers, accountants, successful entrepreneurs) to see if anyone can make an appropriate introduction.

Venture capitalists

The second type of equity investor is venture capitalists. Venture capital firms are limited partnerships of money managers who raise money in "funds" to invest in start-ups and growing firms. Some of the better-known venture capital firms are Kleiner Perkins, Sequoia Capital, and Redpoint Ventures. Similar to business angels, venture capital firms look for a 30 to 40 percent annual return on their investments and a total return over the life of investments of 5 to 20 times the initial investments. The major difference between venture capital firms and business angels is that venture capital firms lend little money to start-ups (preferring to wait until a firm proves its product and market) and normally don't invest less than $1 million in a single firm. As a result, venture capital funding is only practical for a small number of business start-ups.

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Truth 26. Grants: It takes the right fit

A potential source of small business funding is grants. A grant is a gift of money that does not have to be repaid. While there is no nationwide network for awarding grants to start-up firms, almost every state, city, and local community is trying to find ways to encourage people to start businesses as a way of growing their economies. As a result, there are a growing number of programs available through both the public and the private sectors to provide grant money to promising business start-ups.

Obtaining a grant takes a little detective work. Granting agencies are by nature low-key, so they normally need to be sought out. The best place to inquire about the availability of grants for a particular business is via your local Small Business Development Center, SCORE chapter, and similar organizations. Although these groups rarely have grant money available, they'll be able to direct you to organizations that are awarding grants to small businesses in your area. Most grant programs are competitive, meaning that you have to apply for the grant and compete against other start-ups to receive the funds. One of the keys to obtaining grants is to learn to write effective grant proposals. Many Small Business Development Centers sponsor seminars on how to write successful proposals.

> Obtaining a grant takes a little detective work. Granting agencies are by nature low-key, so they normally need to be sought out.

A typical scenario of a small business that received a grant is provided by Rozalia Williams, the founder of Hidden Curriculum Education, a for-profit company that offers college life skills courses. To kick-start her business, Williams received a $72,500 grant from Miami Dade Empowerment Trust, a granting agency in Dade County, Florida. The purpose of the Miami Dade Empowerment Trust is to encourage the creation of businesses in disadvantaged neighborhoods of Dade County. The key to William's success, which is true in most grant-awarding situations, is that her business fit nicely with the mission of the granting organization, and she was willing to take her business into the areas the granting agency was committed to improving. After being awarded the grant and conducting her college prep courses in four Dade County neighborhoods over a three-year period, Williams received an additional $100,000 loan from the Miami Dade Empowerment Trust to expand her business.[1] There are also private foundations that grant money to both existing and start-up firms. These grants are generally tied to specific objectives or a specific project, such as research and development in a specific industry.

The federal government has a pair of grant programs for technology firms. The Small Business Innovation Research (SBIR) program is an established program that provides over $1 billion in cash grants per year to small businesses that are working on projects in specific areas. Each year, ten federal departments and agencies are required by SBIR to reserve a portion of their research and development funds for awards to small businesses. The second program, Small Business Technology Transfer (STTR), is similar to the SBIR program except it requires the participation of researchers working at universities or other research institutions. A list of the agencies that participate in both programs, along with an explanation of the application processes, is available at www.sba.gov/SBIR.

The full spectrum of grants available through the federal government is listed at www.grants.gov. State and local governments, private foundations, and philanthropic organizations also post grants announcements on their Web sites. Finding a grant that fits your business is the key. This is no small task. It is worth the effort, however, if you can obtain some or all of your start-up costs through a granting agency.

Finding a grant that fits your business is the key. This is no small task.

One thing to be careful of is grant-related scams. As a business owner, you may receive unsolicited e-mail messages from individuals or organizations that assure you that for a fee they can help you gain access to hundreds of business-related grants. The reality is that there aren’t hundreds of grants that fit any one business—so the offer is likely a scam.

Truth 27. Persistence pays off: Finding alternative sources of start-up funds

There are sources of funds for new businesses that aren't as obvious as traditional sources of debt financing, equity funding, and grants. A mistake that people make when looking for start-up funds is not casting their net wide enough. It's also a mistake to place too much reliance on a single source of financing without considering alternatives.

Similar to finding grants, finding obscure sources of financing takes legwork and persistence. In most cases, you must also match your start-up with a program or source of funding that fits the nature of your business. The following is a partial list of sources to consider. The best way to become aware of these and similar sources is to work your network of business acquaintances. Many sources of start-up funds fly just under the radar. The most common way to learn about them is through a tip or a referral from a business associate.

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Business plan competitions and other contests

An increasing number of business plan competitions are held across the United States. Many of these competitions offer cash prizes. The number of small business contests sponsored by companies that sell products to small businesses is also increasing. An example is the VISA Business Breakthrough Contest, a joint venture between VISA and MSN, which in 2007 offered five $10,000 awards to businesses that submitted essays explaining how they became more efficient in one of five categories (finance, marketing, organization, team building, and technology).[1] A simple Google search using the keywords "small business contests" will produce similar examples.

State and community small business loan and assistance programs

Many state and community not-for-profit organizations and governmental agencies sponsor loan programs designed to encourage and support business ownership. An example is the Vermont Community Loan Fund, which is a fund that provides loans to businesses that help revitalize struggling communities in Vermont and provide jobs to low-to-moderate-income Vermonters.[2] A similar example is the First Community Loan Fund in Delaware. The fund is a not-for-profit Community Development Financial Institution (CDFI) that specializes in supporting small businesses, micro-enterprises, and affordable housing in the State of Delaware.[3] The best way to find if there are equivalent programs in your state is to check with your local Small Business Development Center or your state Department of Commerce.

Patriot Express Pilot Loan Initiative

The Patriot Express Pilot Loan Initiative is a program sponsored by the Small Business Administration (SBA) to help veterans and members of the military community gain access to the resources needed to start a business. It's the only program sponsored by the SBA that targets a specific group of people. Similar to the SBA Guaranteed Loan Program discussed in Truth 24, "Persistence pays off: Finding alternative sources of start-up funds," the initiative does not lend money directly to veterans but makes it easier for veterans to obtain financing by guaranteeing loans offered by the SBA's network of participating lenders. It features the SBA's lowest interest rates for guaranteed business loans. The program extends to spouses of active duty military personnel and the widowed spouses of service members who died during service or of a service-connected disability.[4]

Loan and grant programs for women and minority business owners

There are a growing number of business assistance programs that target women and minority business owners. For example, the Minority Business Development Agency (MBDA) is a federal agency created specifically to foster the establishment and growth of minority-owned businesses. MBDA provides funding for Minority Business Development Centers, Native American Business Development Centers, and Business Resource Centers located throughout the United States. While these centers are not a direct source of start-up funds, they provide assistance in many areas and help minority-owned businesses seek financing through a variety of channels.[5] An example of an organization set up to invest money in minority businesses is the Minority Angel Investor Network (MAIN). It is a network of accredited investors with an interest and commitment to invest in high-growth, minority-owned, or minority-led companies. The organization's focus is on businesses in the greater Philadelphia, Pennsylvania area.[6]

Customer and supplier financing

Customers and suppliers are an often-overlooked source of start-up financing. Sometimes suppliers, if they recognize that your business has the potential to become a regular customer, will provide your business financing or funding to help it get off the ground. Similarly, if you feel that your product or service will add considerable value for a particular customer and save the customer money, the customer might be willing to prepurchase a certain amount of the product, which is a way for you to generate start-up funds. If you're buying a franchise, you can typically obtain financing through your franchisor.

Tapping into personal funds

There are also ways that business owners tap into personal funds to raise start-up capital, beyond using savings and cash on hand. Examples include borrowing against the cash value of a life insurance policy and tapping into an IRA, 401K, or similar retirement account. You'll normally need guidance and advice from a tax accountant to draw funds from a tax-deferred retirement account to finance a business venture.

Part VI The Truth About Building a New Business Team

Truth 28. How to approach the task of building a “new business” team

One facet of starting a business that all experts agree on is that the quality of the people who start and build a business is instrumental to its success. As one expert put it, “People are the one factor in production...that animates all the others.[1] Often, several businesses are started at the same time that sell essentially the same product or service. When this happens, the key to success is not the product or service but rather the ability of the initial founder or founders to assemble a team that can execute the idea better than anyone else.

A new business’s “team” is the group of founders, key employees, and advisers that move a new business from an idea to a fully functioning firm. Usually, the team doesn’t come together all at once. Instead, it is built as the new business grows and can afford to hire additional personnel. The team also involves more than paid employees. Many new businesses have a board of directors, a board of advisors, and other professionals they rely on for direction and advice.

> A new business’s “team” is the group of founders, key employees, and advisers that move a new business from an idea to a fully functioning firm.

There are two issues that you should be particularly sensitive to as you build your team. Your sensitivity to these issues and the way you handle them will send important signals to the people who you’ll approach for access to resources (such as bankers and investors) and will be instrumental to the way in which your new business team takes shape.

Being open to advice

First, the way your new business team is put together indicates the extent to which you’re open to advice and are able to generate enthusiasm for your business. If you start a business and are relying strictly on yourself, you run the risk of conveying to others that you are a “one-man show” and have no intentions of building a team or taking advice from others. In contrast, if you start a business and report that you’ve attended a number of small business seminars, have met with counselors from your local Small Business Develop

Center and SCORE chapter, and have a five-member advisory board already in place, you're conveying a very different impression. These efforts show that you're open to advice, are willing to share power, and are able to garner support for your business idea. These initiatives may also cause a banker or investor to think, "Wow, if this person ever gets in a bind, he or she'll have a nice network to lean on for counsel and advice," or "If this person is able to fill a five-member advisory board before his or her business even starts, I bet he or she will have no trouble selling the business concept to paying customers."

> The way your new business team is assembled indicates the extent to which you're open to advice and able to generate enthusiasm for your business.

Having a clear sense of how the business will evolve

The second thing to be sensitive to as you start building your new business team is to have a clear sense of how the team will evolve. Almost all new businesses have gaps in the personnel they need. That's normal. Just make sure you have a plausible explanation for how you're dealing with the gaps until you can permanently fill them. In addition, avoid the impression that you're näive or unsure about the order in which to fill the gaps. For example, if you're developing a new product, such as an accessory for the Apple iPhone, you'll need access to expertise on marketing and sales during the time the product is being developed, to make sure it's saleable after it's produced. For you to say that a marketing and salesperson will be hired after the product is developed shows a lack of understanding of the proper upfront role of marketing input. If you can't afford to hire a marketing person during your product development stage, that's understandable, but evidence should be provided that shows where you'll get access to marketing expertise. This is where aligning yourself with a competent SCORE advisor, establishing a relationship with your local Small Business Development Center, or putting together a board of directors or a board of advisors plays a vital role. You can often mine one or more of these groups, usually for free, to find people with specific expertise who are willing to provide counsel and advice until you can afford to hire full-time expertise.

Truth 29. Starting a business as a team rather than an individual

One of the most significant decisions a prospective business owner makes is whether to launch a business as a sole proprietor or whether to take on one or more partners. There is no best choice that works in all situations. The choice normally boils down to whether the idea for the business was conceived with others and whether the people involved are equally committed to starting a business.

While most businesses are started as sole proprietorships, a growing number of businesses are started by a team of two or more people.[1] Businesses that fit this criterion must organize as a partnership, corporation, or limited liability company. It's normally not a good idea to organize as a general partnership, because the individual partners are liable for all the partnership's obligations. This complication can be overcome by organizing as a corporation or a limited liability company, as described in Truth 19, "Choosing a form of business ownership." It's best to have an attorney involved to help you navigate the legalese of starting a business with two or more people, to make sure you select a form of business ownership that meets your collective goals.

Most founding teams consist of two to four people. A team larger than four people is typically too big to be practical.[2]

Advantages to starting as a team rather than an individual

It's generally believed that new businesses started by a team have an advantage over those started by an individual. A team brings more talent, resources, ideas, and professional contacts to a new business than does a sole proprietor.[3] In addition, the psychological support that cofounders of a new business can offer one another may be an important element in a firm's success.

> It's generally believed that new businesses started by a team have an advantage over those started by an individual.

Several factors affect the value of a team that is starting a new business. First, teams that have worked together before have an advantage. If people have worked together before and have decided to partner to start a business together, it usually means that they get along personally and trust one another.[4] They also tend to communicate with one another more effectively than people who are new to one another.[5] Second, if the members of the team are diverse in terms of their abilities and experiences, they are likely to have different points of view about technology, hiring decisions, and other issues. Typically, these different points of view generate debate among the founders, reducing the likelihood that decisions will be made in haste or without the airing of alternative points of view.

Disadvantages to starting as a team rather than an individual

There are two potential disadvantages associated with starting a business as a team rather than as a sole business owner. First, the team members may not get along. This is why investors and others favor teams consisting of people who have worked together before. Second, if two or more people start a business as "equals," conflicts can arise when the business needs to establish a formal structure and designate one person as the chief executive officer (CEO). If the business has investors, the investors will usually weigh in on who should be appointed CEO. In these instances, it's easy for the founder who wasn't chosen as the CEO to feel slighted. This problem is exacerbated if multiple founders are involved. At some point, a hierarchy will have to be developed, and the founders will have to decide who reports to whom.

Founders' agreement

One of the smartest things a team of founders can do to avoid the pitfalls identified in the previous section is to draft a founders' agreement before the business is started. A founders' agreement is a document that deals with issues such as the relative split of the equity among the founders of the firm and how individual founders will be compensated for the cash or the "sweat equity" they put into the firm.[6] The items typically included in a well-developed founders' agreement are as follows:

- Nature of the prospective business
- A brief business plan

- Proposed titles of the individual founders
- Apportionment of stock (or division of ownership)
- Identification of any intellectual property signed over to the business by any of the founders
- Buyback clause, which explains how a founder's shares will be disposed of if he or she dies, wants to sell, or is forced to sell by court order

Having a founders' agreement ensures that the founders have addressed and hashed out critical issues regarding their respective roles in the business before the business is started.

Truth 30. Recruiting and hiring employees

New businesses vary in terms of how quickly they need to recruit and hire employees. In some instances, the founder or founders work alone until the business generates enough sales to justify hiring the first hourly or salaried employees. In other instances, employees are hired immediately.

Founders differ in their approach to the task of recruiting and selecting employees. Some founders draw on their network of contacts to identify candidates. Others advertise their openings through traditional media such as classified ads and employment Web sites like Monster.com. One thing that surprises many first-time business owners is that finding good employees is not an easy task. In fact, several studies have shown that a difficulty in finding qualified employees is a barrier to growth for many new businesses.[1] As a result, you need to develop a deliberate and determined approach to recruiting and hiring and realize that finding good people takes time and effort.

> One thing that surprises many first-time business owners is that finding good employees is not an easy task.

Hiring your first employee

For many business owners, hiring the first employee is a milestone event. If the decision is prudent, it generally indicates that the business is gaining momentum. There are three rules of thumb for hiring your first employee that you should observe in most instances.

- Formalize the process by preparing a job description and conducting formal interviews for the position that is open. Give the position a title, and make sure you have a clear notion of the employee’s authority and scope of responsibility.
- Comply with all the legal ramifications of becoming an employer by following IRS regulations regarding income tax withholdings from employee paychecks and similar matters. Also check with your state government to determine the documents you must file and whether you are required to pay worker’s compensation insurance.
- Pay a fair wage. Many small business owners are successful because they

are willing to work extremely long hours for relatively low pay. The payoff comes through the increased valuation of the business. Unless you're willing to give your first employee an ownership stake in the business, you must pay a fair wage and set a reasonable work schedule to keep the employee.

For many business owners, hiring the first employee is a milestone event.

Fortunately, there are many sources of assistance to help small business owners' work through the process of hiring their first employee. Small Business Development Centers sponsor workshops to teach strategies for recruiting and hiring employees. In most areas, they also make available "document packets" for employers who are hiring employees. The packets contain everything from tax forms to instructions on how to conduct background checks to drug testing forms. The IRS maintains a Web site to help small businesses understand the regulations they are required to comply with. It even offers online classes to explain the rules.[2] Many state governments maintain Web sites and distribute printed publications to help employers comply with state regulations.

Hiring tips and techniques

One hiring technique that many small businesses find useful is to try people out on a part-time basis or as a freelance employee (or intern) to determine if they are a good fit before offering them a full-time job. Individuals who are willing to work on a freelance basis, some of whom are looking for full-time jobs, can normally be identified through your personal network of acquaintances or through a freelance job-search Web site such as Guru.com or Elance.com.

An important tip for hiring employees is to be cautious about offering employees ownership interest in your business. The rationale for offering employees a piece of the company is to incent them to work hard and act like an owner. It's often not necessary to do this. If you can offer your early employees many of the same benefits you obtain from self-employment—a flexible schedule, the chance to work in an area they are passionate about, and freedom from the pressures associated with "climbing the corporate ladder"—you are in most instances already offering them a better experience than they would find through working for a midsized or large firm. If you do offer your employees an ownership interest in your business, make sure to vest theirs interests gradually. It's fully appropriate to require your employees to "earn" their ownership interest in your business through their performance and their longevity with the company.

Truth 31. Board of directors

The need for a board of directors depends on the type of business you start. If your business starts as a corporation, it is legally required to have a board of directors. A board of directors is a panel of individuals elected by a corporation's shareholders to oversee the management of the firm. In an early-stage firm or a small firm, the board may be restricted to the principles running the firm. In these instances, the board serves little more than a legal function. In other instances, however, the board plays an active role in the management and oversight of the business.

Technically, a board of directors has three responsibilities: (1) appoint the firm's officers, (2) declare dividends, and (3) oversee the affairs of the corporation. The optimal size of a board of directors for a start-up is three to five people.[1] A board is typically made up of both inside directors and outside directors. An inside director is also an officer of the firm. An outside director is someone who is not employed by the firm. A five-member board of directors usually consists of two inside directors and three outside directors. Most boards meet formally three or four times a year. Large firms pay their directors for their service. New businesses are more likely to pay their directors in company stock or ask them to serve without direct compensation—at least until the company is profitable.

If handled properly, a business's board of directors can be a central part of its new business team. An active board provides guidance and lends legitimacy to a firm.

> If handled properly, a business's board of directors can be a central part of its new business team.

Provide guidance

Although a board of directors has formal oversight responsibility, its most useful role is to provide guidance and support to the managers of the firm. Many well-intended business founders and managers simply "don't know what they don't know," which often results in missteps early in the life of a start-up. Experienced board members often see these potential missteps before they occur and help new business teams avoid them. Many business owners interact with their board members frequently and obtain vital input. The key to making this happen is to select board members with needed skills and useful experience who are willing to give advice and ask insightful and probing questions.

> Although a board of directors has formal oversight responsibility, its most useful role is to provide guidance and support to the managers of the firm.

Individual members of a board of directors can also help fill competency gaps when a company is started, as mentioned in Truth 28, "How to approach the task of building a 'new business' team." If a firm gets investment capital, the investor normally occupies a seat on its board of directors. Investors do this not only to protect their investment but also to assume a formal role in lending advice and assistance to the business.

Lend legitimacy

Providing legitimacy for a firm is another main function of a board of directors. Well-known and respected board members bring instant credibility to the firm. For example, just imagine the positive buzz a firm could generate if it could say that a well-known entrepreneur, investor, or banker had agreed to serve on its board of directors. This phenomenon is referred to a signaling. Presumably, a high-quality individual would be reluctant to serve on the board of a low-quality start-up because that would put his or her reputation at risk. So when a high-quality individual does agree to serve on the board of a new firm, the individual is in essence "signaling" that the company has the potential to be successful.[2]

Achieving legitimacy through high-quality board members can result in other positive outcomes. Well-known board members can often help companies get their foot in the door with potential suppliers and customers. Board members are also often instrumental in helping young firms arrange financing or funding.

Truth 32. Board of advisors

A board of advisors is a panel of experts asked by a firm's managers to provide counsel and advice on an ongoing basis. Unlike a board of directors, a board of advisors possesses no legal responsibility for the firm and gives nonbinding advice.[1] A board of advisors can be established for general purposes or can be set up to address a specific issue or need. For example, some start-ups set up customer advisory boards shortly after they are founded to help them fine-tune their initial offerings.

> A board of advisors can be established for general purposes or can be set up to address a specific issue or need.

Similar to a board of directors, the main purposes of a board of advisors is to provide guidance and lend legitimacy to a firm. Both of these attributes are seen in the advisory board set up by Laura Udall, the entrepreneur who started ZUCA, a company that makes backpacks on rollers for school age kids. When asked about the types of advice and support she gets from people outside her immediate management team, Udall said,

> "The company has a board of directors, but I also have created a wonderful board of volunteer advisors that has been very helpful with tactical and strategic decisions. The advisory board has evolved over the years as a result of my network. I asked each of the members to join as a result of their specific expertise. It now includes a CFO/COO of a prominent corporation, an executive in the luggage industry, a mom inventor who has founded several successful companies, a product designer, and a manufacturing expert."[2]

Imagine the type of advice and support Udall gleans from this group of advisors.

Most boards of advisors have between 5 and 15 members and interact with each other and with a firm's managers in several ways. Some advisory boards meet three or four times a year at the company's offices or in another location. Other advisory boards meet in an online environment. In some cases, a firm's board of advisors are scattered across the country, making it more cost-effective for a business's owners to interact with the members of the board on the telephone or via e-mail rather than bring them together physically. In these situations, board members don't interact with each other on a face-to-face basis, yet they still provide high levels of counsel and advice. The fact that a start-up has a board of directors does not preclude it from establishing one or more advisory boards. For example, Coolibar, a maker of sun protective clothing, has a board of directors and a medical advisory board. According to Coolibar, its medical advisory board "provides advice to the company regarding UV radiation, sunburn, and the science of detecting, preventing, and treating skin cancer and other UV-related medical disorders, such as lupus."[3] The board currently consists of six medical doctors, all with impressive credentials. Similarly, Intouch Technologies, a medical robotics companies, has a board of directors along with a business and strategy advisory board, an application and clinical advisory board, and a scientific and technical advisory board.[4]

> The fact that a start-up has a board of directors does not preclude it from establishing one or more advisory boards.

Although having a board of advisors is widely recommended in start-up circles, most start-ups do not have one. As a result, one way you can make your start-up stand out is to have one or more boards of advisors.

Part VII The Truth About Intellectual Property

Truth 33. Intellectual property: What is it, and how is it protected?

Imagine that you have started a business to produce a new type of smoke alarm that is specifically designed for kitchens. It is similar to other smoke alarms but is more capable of detecting a kitchen fire than any alarm on the market. You've named it "Kitchen Sentry." Your tagline is "We Protect Cooks and Kitchens." You just acquired the Internet domain name www.kitchensentryfirmalarm.com.

Fortunately, during the time you were developing your product, you attended a seminar on intellectual property sponsored by your local Small Business Development Center (SBDC). You immediately went to an attorney who specializes in helping small businesses secure their intellectual property to talk about your device. Since that time, you have applied for a patent; trademarked the "Kitchen Sentry" name, your tagline, and your logo; and copyrighted key portions of your printed material. You have also designated certain portions of what you do as trade secrets. For example, the software code that helps the Kitchen Sentry detect a kitchen fire earlier than any other firm alarm is not protected by a patent. It's nearly impossible for a competitor to learn the code by reverse-engineering one of your devices. As a result, rather than disclosing this information, which would be necessary if you patented it, you have decided to keep it secret and protect it internally.

> *Intellectual property* is any product of human intellect that is intangible but has value in the marketplace.

Like Kitchen Sentry, many new businesses have valuable intellectual property. Intellectual property is any product of human intellect that is intangible but has value in the marketplace. Traditionally, businesses have thought of their physical assets—such as land, buildings, and equipment—as their most important assets. Increasingly, however, a business's intellectual assets are the most valuable. Think of the value of the Starbuck's trademark, the Nike "swoosh" logo, or the Microsoft Windows operating system. All of these are examples of intellectual property that provide their respective businesses with a competitive advantage in the marketplace. A business like Nike would be hurt much more by the loss of its "swoosh" logo than by the loss of a physical asset such as a building or piece of equipment.

> A business like Nike would be hurt much more by the loss of its "swoosh" logo than by the loss of a physical asset such as a building or piece of equipment.

The four forms of intellectual property protection are patents, trademarks, copyrights, and trade secrets. They are described in Truths 34 to 37. Intellectual property laws exist to encourage individuals and businesses to be innovative and to take risks by granting them exclusive rights to the fruits of their labors for a period of time. There would be no financial incentive for an individual to invent a device, like the Kitchen Sentry firm alarm, if it could be immediately copied by someone else. Intellectual property laws also help individuals make well-informed choices. For example, when consumers see a Panera Bread restaurant, they know exactly what to expect because only Panera Bread is permitted to use the Panera Bread trademark for soups, signature sandwiches, and bakery products.

One special note about intellectual property laws is that it's up to business owners to take advantage of them and to safeguard their intellectual property once it is legally protected. Police forces and fire departments are available to quickly respond if a business owner's buildings or physical assets are threatened, but there are no intellectual property police forces or fire departments in existence. The courts prosecute individuals and companies that break intellectual property laws. However, it is up to the individual business owner to understand intellectual property laws, safeguard intellectual property assets, and initiate litigation if intellectual property rights are infringed upon or violated.

Truth 34. To patent or not to patent?

When it comes to inventing a product, like the new type of fire alarm described in Truth 33, "Intellectual property: What is it, and how is it protected?" the first thing you should do is get a patent, right? Well, maybe. Getting a patent is an expensive and time-consuming process. As a result, while there are many good reasons for getting a patent, there are several steps you should take before hiring a patent attorney and starting the process.

Steps to take before applying for a patent

First, as discussed in Truth 9, "Screening and testing business ideas," you should test and screen your business idea to make sure it has value in the marketplace. A common mistake that business owners make is to invent a product, spend a considerable amount and money to patent it, and find that the market for the product doesn't exist or is too small to be worthy of pursuit.

Second, you should conduct a preliminary patent search on your own to see if your idea is already patented. You can do this by going to the United States Patent & Trademark Office (USPTO) Web site (www.uspto.gov/) and conducting a preliminary search. Just for fun, try this example. Suppose you invented a toothbrush with a tube of toothpaste attached to the handle. Go to the USPTO Web site, locate the Search text box at the top of the pages, and type "toothbrush + toothpaste." You'll find that 265 patents have already been granted for devices that in various ways combine toothbrushes and toothpaste. While you may find a new way to combine toothbrushes and toothpaste, and be granted a patent, you hardly have a completely original idea. In fact, patent # 6390103 is titled "Toothpaste Dispensing Toothbrush Having Floss Dispenser."[1] This patent, which was granted in 2002, goes one step further than you were thinking.[2]

> You should test and screen your business idea to make sure it has value in the marketplace.

None of this is to suggest that you shouldn't apply for a patent if you've invented a new device, but just be careful. The costs involved, which vary depending on the complexity of the device, range from between $4,500 to $6,500 to patent a relatively simple device, like a new type of paper clip, to between $6,500 and

$9,000 to patent a moderately complex device, like a retractable dog leash. The costs involved include attorney fees and United States Patent & Trademark Office filing fees. Costs go up substantially when trying to patent a highly complex product like a new type of medical device.[3]

> The costs involved include attorney fees and United States Patent & Trademark Office filing fees.

What is a patent, and what's eligible for patent protection?

A patent is a grant from the federal government conferring the rights to exclude others from making, selling, or using an invention for the term of a patent. However, a patent does not give its owner the right to make, use, or sell the invention; it gives the owner only the right to exclude others from doing so. This is a confusing issue for many people. If a business is granted a patent for an item, it is natural to assume that it could start making and selling the item immediately. But it cannot. A patent owner can legally make or sell the invention only if no other patents are infringed on by doing so. For example, if an inventor obtained a patent on a computer chip and the chip needed technology patented earlier by Intel to work, the inventor would need permission from Intel to make and sell the chip. Intel may refuse permission or ask for a licensing fee for the use of its patented technology. Although this system seems odd, it is really the only way the system could work. Many inventions are improvements on existing inventions, and the system allows for improvements to be patented, but only with the permission of the original inventors, who usually benefit by obtaining licensing income in exchange for their consent.

There are three types of patents: utility patents, design patents, and plant patents. Utility patents are the most common type of patent and cover what we generally think of as new inventions. The term of a utility patent is 20 years from the date of the initial application. After 20 years, the patent (which is not renewable) expires, and the invention falls into the public domain. A complete description of the invention for which a utility patent is sought is required, including drawings and technical details. A patent must be applied for within one year of when a product or process was offered for sale, put into public use, or described in any printed publication—or the right to file a patent application is forfeited. There are three basic requirements for a patent to be granted. The subject of the patent application must be (1) useful, (2) novel in relation to prior arts in the field, and

(3) not obvious to a person of ordinary skill in the field.

Provisional patent applications

One provision of patent law that is particularly critical to small business owners is that the U.S. Patent and Trademark Office (USPTO) allows inventors to file a provisional patent application, pending the preparation and filing of a complete application. Filing for a provisional patent allows the term “Patent Pending” to be applied to an invention. Filing for a provisional patent grants “provisional rights” to an inventor for up to one year, pending the filing of a complete and final application.

Truth 35. Trademarks: An essential form of protection

Unlike patents, nearly all small businesses can benefit from trademark protection. Once the name, logo, and other distinguishing marks for a business have been selected, they should be trademarked so they become the sole possession of the business's owner.

What is a trademark?

A trademark is any word, name, symbol, or device used to identify the source or origin of products or services and to distinguish those products or services from others. Archaeologists have found that as far back as 3,500 years ago, potters made distinctive marks on their articles of pottery to distinguish their work from others. As discussed in Truth 17, "Something you'll say a million times: Your business's name," the name (and other marks) a business associates with itself makes a difference in terms of how it's perceived and whether it gets noticed. For example, the original name that Jerry Yang and David Filo, the cofounders of Yahoo!, selected for their business was "Jerry's Guide to the World Wide Web." Not too catchy, is it? The name was later changed to Yahoo!, which caught on with early adopters of the Internet and is now one of the most recognizable trademarks in the world.

Nearly all small businesses can benefit from trademark protection.

There are four types of trademarks: trademarks, service marks, collective marks, and certification marks. Trademarks and service marks are of the greatest interest to business owners. Service marks are similar to trademarks, but they are used to identify the services or intangible activities of a business rather than a business's physical product. Travelocity, eBay, and Google are examples of service marks.

How a trademark is obtained

Trademarks are obtained through the United States Patent & Trademark Office (USPTO) and are renewable every ten years, as long as the mark remains in use. Once you've selected a trademark, you should conduct a trademark search to determine if the trademark is available. If someone else has already established rights to the proposed mark, you can't use it. You also can't choose a trademark that is confusingly similar to someone else's trademark. For example, if you tried to trademark the name Apple Core for a computer company, Apple Inc. would undoubtedly argue that your name is confusingly similar to its name.

Technically, a trademark does not have to be registered to receive protection and to prevent other companies from using confusingly similar marks. Once a mark is used in commerce, such as in an advertisement, it is protected. There are distinct advantages, however, to registering the mark through the USPTO. Registered marks are allowed nationwide priority for use of the mark, are permitted to use the federal trademark registration symbol (®), and carry with them the right to block the importation of infringing goods into the United States. The right to use the registered trademark symbol is particularly important. Attaching a trademark symbol to a product (for example, My Yahoo! ®) provides notice of a trademark owner's registration. This posting allows an owner to recover damages in an infringement action and reduces an offender's claim that it didn't know that a particular name or logo was trademarked.

You can register a trademark on your own. In fact, there are a number of Web sites, including the USPTO site, that provide step-by-step instructions for how to register a trademark. There are gray areas in trademark law, however, and you want to get it right. You also don't want to infringe on someone else's trademark. Accordingly, in most cases, it's advisable to retain an attorney to help you secure your trademarks.

What can be trademarked?

The following items are eligible for trademark protection:

- Words, such as Yahoo! and Microsoft
- Numbers and letters, such as 3M, CNN, and 1-800-CONTACTS
- Designs and logos, such as the Nike swoosh logo
- Sounds, such as the familiar four-tone sound that accompanies "Intel Inside" commercials
- Fragrances, such as the special scent on certain brands of stationary
- Shapes, such as the distinctive shape of the Apple iPod
- Colors, such as the distinctive purple color of Nexium, a pill that treats acid

reflux disease (advertised as the “purple pill”)

- Trade Dress, such as the distinctive appearance of the inside of a Panera Bread restaurant

Trademark protection is broad and provides many opportunities for businesses to differentiate themselves from one another. The key for a new business is to trademark its products and services in ways that draw positive attention to them.

Rules of thumb for selecting appropriate trademarks

There are two rules of thumb to help businesses owners select appropriate trademarks. First, a mark, whether it is a name, logo, or design, should display creativity and strength. Marks that are inherently distinctive, such as the McDonald’s Golden Arches; made-up words, such as Google and eBay; and words that evoke particular images, such as Double Delight Ice Cream; are strong trademarks.

Second, words that create favorable impressions about a product or service are helpful. A name such as Safe and Secure Childcare for a day care center positively resonates with parents.

Truth 36. Copyrights laws: A surprising breadth of protection

Of all the forms of intellectual property protection, the copyright laws are possibly the least understood. Most of us think of books, newspaper articles, and musical scores as needing copyright protection. But copyright law extends much further. Nearly anything that a business creates that is in written or digital form is eligible for copyright protection.

A copyright is a form of intellectual property protection that grants to the owner of a work of authorship the legal right to determine how the work is used and to obtain the economic benefits from it.[1] The work must be in tangible form, such as a book or computer software program. Businesses typically possess a treasure trove of copyrightable material. A work does not have to have artistic merit to be eligible for copyright protection. As a result, things such as operating manuals and advertising brochures qualify for protection.

> Businesses typically possess a treasure trove of copyrightable material.

What is protected by a copyright?

Copyright law protects "original works of authorship." The primary categories of material that can be copyrighted are as follows:

- Literary works
- Musical compositions
- Computer software
- Dramatic works
- Sound recordings
- Architectural works
- Motion pictures and other audiovisual works
- Pictorial, graphic, and sculptural works

Anything that is written down is a *literary work*. Characters that are associated with a company qualify for protection. A character that looks like the Aflac duck or the GEICO gecko would infringe on the copyright that protects those characters. *Derivative works*, which are works that are new renditions of something that is already copyrighted, are also copyrightable. As a result of this provision, a musician who performs a rendition of a song copyrighted by Aerosmith can obtain a copyright on his or her effort. Of course, Aerosmith would have to consent to the infringement on its copyright of the original song before the new song could be used commercially, which is a common way that composers and bands earn an extra income.

The main exclusion from copyright law is that a copyright cannot protect an idea. For example, a business owner may have the idea to open a soccer-themed restaurant. The idea itself is not eligible for copyright protection. However, if the business owner writes down what the soccer-themed restaurant will look like and how it will operate, that description is copyrightable.

> The main exclusion from copyright law is that copyrights cannot protect ideas.

How to obtain a copyright

Technically, a copyright exists the moment a work of authorship assumes a tangible form. You have to register the copyright with the U.S. Copyright Office (www.copyright.gov), however, if you want to bring a lawsuit for infringement. There are two steps that are normally taken to solidify a copyright, cumulating with registering a work with the copyright office.

First, you can enhance copyright protection for anything in written form by attaching the copyright notice, or *copyright bug* as it is sometimes called. The bug—a C inside a circle—typically appears in the following form: © 2008 Kitchen Sentry Inc. By placing this notice at the bottom of a document, an author (or company) can prevent people from copying the work without permission and claiming that they did not know that the work was copyrighted. Substitutions for the copyright bug include the word Copyright and the abbreviation *Copr*.

Second, you can obtain further protection by registering the work with the U.S. Copyright Office. Filing a simple form and depositing one or two samples of the work with the office completes the registration process. The need to supply a sample obviously depends on the nature of the item involved. Obviously, you could not supply one or two copies of an original painting. Filing promptly is recommended and makes it easier to sue for copyright infringement if necessary.

Copyrights last for a long time. Any work created on or after January 1, 1978, is protected for the life of the author plus 70 years.

Copyright infringement

Copyright infringement occurs when one work derives from another or is an exact copy or shows substantial similarity to the original work. It is a growing problem in the United States and in other countries. For example, less than a week after the original *Harry Potter* movie was released in the United States, bootleg video discs were reported for sale in at least two Asian countries.[2] To prove infringement, a copyright owner is required to show that the alleged infringer had prior access to the copyrighted work, and the work is substantially similar to the owner's.

There are many ways to prevent infringement. For example, a technique frequently used to guard against the illegal copying of software code is to embed and hide in the code useless information, such as the birth dates of the authors. It's hard for infringers to spot useless information if they are simply cutting and pasting large amounts of code from one program to another. If software code is illegally copied and an infringement suit is filed, it's difficult for the accused party to explain why (supposedly original) code includes the birth dates of its accusers. Similarly, some publishers of maps and other reference works deliberately include bits of phony information in their products, such as fake streets and nonexistent railroad crossings, to try to capture copiers. Again, it would be pretty hard for someone who copied someone else's copyrighted street guide to explain why the name of a fake street was included.[3]

Truth 37. Trade secrets: Guard them carefully

Most businesses, including start-ups, have a wealth of information that is critical to their success but does not qualify for patent, trademark, or copyright protection. Some of this information needs to be kept secret to help a business maintain its competitive advantage. An example is a business's customer list. A business may have been extremely diligent over time tracking the preferences of its customers, helping it fine-tune its marketing message and target past customers for future business. If this list fell into the hands of one or more of the company's competitors, its value would be diminished, and it would no longer provide the company a unique competitive advantage.

A trade secret is any formula, pattern, physical device, idea, process, or other information that provides the owner of the information with a competitive advantage in the marketplace. Trade secrets include marketing plans, product formulas, financial forecasts, employee rosters, logs of sales calls, and similar material. Unlike patents, trademarks, and copyrights, there is no single government agency that regulates trade secret law. Instead, the theft of trade secrets is made illegal by a patchwork of state and federal economic espionage laws.

> Trade secrets include marketing plans, product formulas, financial forecasts, employee rosters, logs of sales calls, and similar material.

What qualifies for trade secret protection?

Not all information qualifies for trade secret protection. In general, information that is known to the public or that competitors can discover through legal means doesn't qualify for trade secret protection. If a company passes out brochures at a trade show that are available to anyone in attendance, nothing in the brochure can typically qualify as a trade secret. Similarly, if a secret is disclosed by mistake, it typically loses its trade secret status. For example, if an employee of a business is talking on a cell phone in a public place and is overheard by a competitor, anything the employee says is generally exempt from trade secret protection. Simply stated, the general philosophy of trade secret legislation is that the law does not protect a trade secret unless the owner has protected it first.

Businesses can maintain protection for their trade secrets if they take reasonable steps to keep the information confidential. The strongest case for trade secret protection is information that is characterized by the following:

- Is not known outside the company
- Is known only inside the company on a "need-to-know" basis
- Is safeguarded by stringent efforts to keep the information secret
- Is valuable and provides the company a competitive advantage
- Was developed at considerable cost, time, and effort
- Cannot be easily duplicated, reverse-engineered, or discovered

Trade secret disputes

Trade secret disputes arise most frequently when an employee leaves a business to join a competitor and is accused of taking confidential information along. For example, a marketing manager for one business may take a job with a competitor and create a marketing plan for the new employer that is nearly identical to the plan being worked on at the previous job. The original employer could argue that the marketing plan that the departed employee was working on was a company trade secret and that the employee essentially stole the plan and took it to the new job. The key factor in winning a trade secret dispute is that some type of theft must have taken place. Trade secrets can be lawfully discovered. For example, it's not illegal for one company to buy another company's products and take them apart to see how they're assembled.

> Trade secret disputes arise most frequently when an employee leaves a business to join a competitor and is accused of taking confidential information along.

A company damaged by trade secret theft can initiate a civil action for damages in court. In denying the allegation, the defendant typically argues that the information in question was independently developed (meaning that no theft took place), was obtained by proper means (such as with the permission of the owner), or was innocently received (such as through a casual conversation at a business meeting). Memorization is not a defense. An employee from one business can't say, "All I took from my old job was what's in my head" and claim that just because the information conveyed wasn't in written form, it's not subject to trade secret protection. If the courts rule in favor of the business that feels one of its trade secrets has been stolen, the firm can stop the offender from using the trade secret and obtain substantial financial damages.

The best way to protect trade secrets is through physical measures and written agreements. Physical measures range from placing security fences around buildings to restricting access to sensitive files like customer lists. Written agreements are also key. For the best protection, a business should ask its employees to a sign a nondisclosure agreement at the time of original employment. A *nondisclosure agreement* is a promise by an employee or another party (such as a supplier) not to disclose a company's trade secrets.

Part VIII The Truth About Marketing

Truth 38. How to approach marketing in a new business

Marketing refers to all the activities that a business engages in to be successful in selling a product or service that people not only desire but are willing to buy.[1] Most of a business's marketing activities are executed through one of the four Ps of the marketing mix—product, price, promotion, and place (or distribution). Most new business owners see the development of an effective marketing program as a key factor to their ultimate success.

Be careful, however, of how you think about marketing and the financial resources that you dedicate to it. Marketing is one area where hard work and ingenuity can make up for a lack of funds. It's also an area where money can be easily wasted if a business doesn't have a well-thought-out marketing plan. There are three things to be mindful of as you approach the topic of marketing and promotions in a new business.

Make your marketing efforts consistent with your mission

First, a business's marketing efforts should be consistent with its overall mission and values. For example, Kitchen Sentry, the fictitious firm introduced in Truth 33, "Intellectual property: What is it, and how is it protected?", has the mission of protecting individuals and families against kitchen fires. The company believes that people fear kitchen fires as much as any calamity that might befall themselves or their families, and that having a high-quality smoke alarm in the kitchen will provide people peace of mind. Kitchen Sentry's marketing efforts should reflect and reinforce these core beliefs. A common mistake that new businesses make is that their marketing efforts are poorly focused. Stay on script. If the people behind Kitchen Sentry care deeply about protecting families from kitchen fires and their product is sound, those attributes should be the focal points of the company's marketing efforts.

Know your customers

Second, a business needs to have a clear sense of who its customers are and how they behave. A well-managed start-up uses a two-step approach for selecting its market: segmenting the market and selecting or developing a target market. This process is explained in Truth 39, "Segmenting the market and selecting a target market." A business must complete these steps and clearly define who its customers are, because all of its marketing decisions hinge on these initial critical choices. If other marketing decisions are made first, such as choosing an advertising campaign, there is a danger the firm will not send a clear message to its target customers. For example, if a jewelry store that features high-end merchandise advertised in a local shopper alongside discount merchants, it would risk sending confusing signals to its intended market. It's more affluent clientele might wonder, "Is this a high-end store, or isn't it?"

It's also important that a business knows as much about its customers as possible, from knowing the amount of disposable income they have, to the periodicals they read, to the media they watch. Knowledge of these and similar factors helps you fine-tune your marketing strategy and lower expenses.

Learn about the full array of marketing techniques that are available

Third, a business needs to learn about the full array of marketing techniques that are available. The majority of business owners are familiar with the most expensive ways to run a marketing campaign, such as buying print and media advertising, but they are less familiar with more cost-efficient alternatives. Many of the most cost-effective ways for a business to get noticed, from passing out brochures to speaking to civic groups, are inexpensive but take time and effort. The best approaches to learning about the methods available are to look through books and magazines on marketing and promotions and take a class from your local Small Business Development Center (SBDC).

An example of an inexpensive way for a business to get noticed is to write a blog. Blogs familiarize people with a business and help build an emotional bond between a business and its customers. A case in point is a blog written by Mary Baker, the co-owner of Dover Canyon Winery. Baker started her blog in April 2006 using a software package called TypePad Pro that costs her $149.50 a year to maintain. She uses the blog to give her readers periodic updates on what's happening at the winery and how she feels about her life and her business. She also posts pictures of herself, her pets, her family, and daily life at the winery. To make her customers aware of her blog, she drops a postcard with the blog's address into bags with customer purchases. There is also a link to the blog on the Dover Canyon Winery's Web site. Mail order sales for the winery almost doubled from 2006 to 2007.[2]

While writing a blog may not be appropriate for all businesses, the overarching point is that Mary Baker found an inexpensive and novel way to promote her business, rather than relying on more traditional and expensive forms of promotion. In a midsized city, a large newspaper ad can run as high as $5,000.

Truth 39. Segmenting the market and selecting a target market

A new business must address this critical question: Who are our customers, and how will we appeal to them? A well-managed start-up uses a two-step approach to answer the first of these questions: segmenting the market, and selecting or developing a specific target market.

Segmenting the market

The first step in selecting a target market is to study the industry in which your firm intends to compete and determine the different potential target markets in that industry. This process is called market segmentation. Market segmentation is important because a new business generally has only enough resources to target one market segment, at least initially.[1] Markets can be segmented in many ways, such as by geography (city, state, country), demographic variables (age, gender, family income), psychographic variables (personality, lifestyle, values), and benefits sought (quality, ease of use, prestige). Sometimes a business segments its market on more than one dimension to drill down to a specific market segment that the business thinks it is uniquely capable of serving. For example, GreatCall, the company that makes Jitterbug, a cell phone designed specifically for older people, segmented the cell phone market by age and by benefits sought. The Jitterbug, which targets older users, features large buttons, easy-to-read text, and a cushion that cups around the ear to improve sound quality. Similarly, PopCap games, an electronics games company, segmented its industry by gender and benefits sought. It targets women and makes electronic games that are casual and relaxing. This is an entirely different segment from the segment targeted by Electronic Arts, the largest company in the electronic games industry. Electronic Arts targets young males and produces games that are flashy and action-packed.

> Market segmentation is important because a new business generally has only enough resources to target one market segment, at least initially.

To test whether you have segmented your market successfully, the requirements for successful market segmentation are as follows:

- Uniformity of needs and wants appears within the segment.
- Diversity of needs and wants exists between the segments.
- Differences within the segment should be small compared to differences across segments.
- The segment should be distinct enough so that its members can be easily identified.
- It should be possible to determine the size of the segment.
- The segment should be large enough to be profitable.

Despite the importance of market segmentation, it is a process that new businesses often overlook. Overlooking this activity can result in a business that hasn't carefully studied the possibilities in the industry it plans to enter before selecting its target market. One opportunity that new businesses have is to segment their markets in new ways. Before Great Call and PopCap Games came along, no one had segmented the cell phone market by age and benefits sought or segmented the electronic games industry by gender and type of game. Both of these companies now have growing businesses, largely because they are servicing distinct and growing segments within their broader industries.

Selecting a target market

Once a firm has determined the different markets that exist within an industry, the next step is to select a target market. Typically, a new business doesn't target an entire segment of a market, because many market segments are too large to target successfully. Instead, most businesses target a smaller niche or vertical market within the segment (as discussed in Truth 8, "A make-it or break-it issue: Selecting an idea that can be sold into a niche market"). For example, one segment of the fitness industry is fitness centers that sell monthly memberships. (Another segment would be companies that sell exercise equipment to be used in the home.) Within the segment that sells monthly membership are several smaller niche markets that are targeted by different companies. For example, Curves targets women, Cuts targets men, My Gym is just for children, and Club 50 targets people 50 years old and older.

In most cases, the secret to appealing to a smaller niche market is to understand the market and meet its needs better than those needs can be met by businesses targeting an entire market segment. This is the secret behind the phenomenal success of Curves, which grew from one fitness center for women in 1992 to over 10,000 today.[2] By focusing on a clearly defined target market, a business can become an expert in that market and then provide customers with high levels of value and service. This advantage is one of the reasons that Philip Kotler, a world-renowned marketing expert, says, “There are riches in niches.”[3]

> By focusing on a clearly defined target market, a business can become an expert in that market and then be able to provide customers with high levels of value and service.

Truth 40. Establishing a brand

A brand is a set of attributes that people associate with a business. These attributes can be positive, such as trustworthy, innovative, dependable, or easy to deal with, or they can be negative, such as cheap, unreliable, sloppy, or difficult to deal with.

The customer loyalty a company creates through its brand is one of its most valuable assets. This sentiment is affirmed by Russell Hanlin, the CEO of Sunkist Growers, who said, "An orange is an orange...is an orange. Unless...that orange happens to be a Sunkist, a name 80 percent of consumers know and trust."[1] By putting its name on an orange, Sunkist is making a promise to its customers that the orange will be wholesome and fresh. Other ways of thinking about the meaning of a brand are as follows:

- A brand is a guarantee.
- A brand is a pledge.
- A brand is a reputation.
- A brand is an unwritten warrantee.
- A brand is an expectation of performance.
- A brand is a presentation of credentials.
- A brand is a collection of memories.
- A brand is a handshake between a company and its customers.

Start-ups must build a brand from scratch, which starts with selecting the company's name. One of the keys to effective branding is to create a strong personality for a business, designed to appeal to the chosen target market.[2] Southwest Airlines, for example, has created a brand that denotes fun. This is a good fit for its target market: people traveling for pleasure rather than for business. Similarly, Starbucks has created a brand that denotes an experience framed around warmth and hospitality, encouraging people to linger and buy additional products. A business ultimately wants its customers to strongly identify with it—to see themselves as "Southwest Airlines flyers" or "Starbucks coffee drinkers." People won't do this, however, unless they see a company as being different from competitors in ways that are significant to them.

> The customer loyalty a company creates through its brand is one of its most valuable assets.

So how does a new business develop a brand? On a philosophical level, a business must have meaning in its customers' lives. It must create value—something that customers are willing to pay for. Imagine a father shopping for airline tickets so that he can take his three kids to see their grandparents for Christmas. If Southwest Airlines can get his family to their destination for $75 per ticket cheaper than its competitors, Southwest has real meaning in the father's life. Similarly, if a young couple buys a Cranium board game, and playing the game with other couples results in lasting friendships, Cranium will have a special place in their hearts. Businesses that create meaning in their customers' lives stand for something in terms of benefits, whether it is low prices, fun, fashion, improved health, or something else.

On a more practical level, brands are built through a number of techniques, including advertising, public relations, sponsorships, support of social causes, and good performance. A business's name, logo, Web site design, and even its letterhead are part of its brand. A new business needs to think about the brand it plans to develop before it picks its logo and initiates other marketing-related activities. The first impression a business makes with its potential customers should convey the essence of how it wants to be viewed and seen.

> A business's name, logo, Web site design, and even its letterhead are part of its brand.

Affirming all these points, Dan Byrne, the CEO of Byrne Specialty Gases, a company that provides specialized gases to laboratories, sums up what his company has done to build a strong brand during its 20 years of existence:

> "It is all based on trust, reliability, responsiveness, quality, *etc.* It is all these infinitesimal details that drive a company's brand. We have the attitude that everything matters. We lost a large customer once that went to a discount provider. Three months later the customer called back almost hat in hand. Our level of service reinforces our brand and keeps customers coming back to us."[3]

Truth 41. Selling benefits rather than features

In their attempts to gain visibility, many new businesses make the mistake of promoting the features rather than the benefits of their products or services.

A promotional strategy that focuses on the features of a product, such as its technical merits, is almost always less effective than a strategy that focuses on what a product can do for the person buying it. For example, one of the most successful advertising campaigns ever launched by McDonald's featured the jingle, "You deserve a break today—at McDonald's." McDonald's could have stressed the cleanliness of its stores or the uniformity of its French fries, which are features. Instead, it struck a chord with people by focusing on one of the biggest benefits of eating at McDonald's—not having to cook. Although not as obvious in today's society, not having to cook a meal at home was a rare treat when McDonald's started using this tagline.

The same rationale can be applied to any product or service. Consider the ZUCA rolling backpack (introduced in Truth 32). In her initial attempts to get the ZUCA noticed, Laura Udall, the company's founder, could have talked about the ZUCA's durable aluminum frame, its oversized silent wheels, its washable nature, and its number of available colors. All these are features. But it's more likely that she focused on the benefits of the product—the fact that it relieves back pain and is durable enough that a child can sit on it while waiting for the school bus. (The ZUCA includes a fold-out seat.) These are the benefits or the value that the ZUCA delivers to its users.

Sometimes it's hard to resist the temptation to focus on features rather than benefits. For instance, it's easy to imagine why an engineer who has just invented a new product wants to talk about the product's technical specifications. Similarly, it's natural for a company that has just developed an improved digital camera to want to point out all the bells and whistles that its camera has that other cameras don't. However, one of the most fundamental precepts of marketing is that "customers don't buy features; they buy benefits."[1] The first thing that customers want to know is how the product or service will help them accomplish their goals and improve their lives.

Truth 42. Pricing: The most dicey element in the marketing mix

Of the four elements of a business's marketing mix—product, price, promotion, and place (or distribution), price is often the toughest. A business doesn't want to undercharge for its products and services and leave money on the table, nor does it want to overcharge and drive business away.

The price a company charges for its products and services also sends a clear message to its target market. For example, Oakley positions its sunglasses as innovative, state-of-the art products that are both high quality and visually appealing. This position in the market suggests the premium price that Oakley charges. If Oakley advertised innovative, state-of-the art products but charged a bargain basement price, it would send confusing signals to its customers. Its customers would wonder, "Are Oakley sunglasses high quality, or aren't they?" In addition, the lower price wouldn't generate the sales revenue Oakley needs to continuously differentiate its sunglasses from competitors' products in ways that are meaningful to its customers.

> The price a company charges for its products and services sends a clear message to its target market.

Most business owners use one of two methods to set the price for their products: cost-based pricing and value-based pricing.

Cost-based pricing

In cost-based pricing, the list price is determined by adding a markup percentage to a product's cost. The markup percentage may be standard for the industry or may be arbitrarily determined by the business owner. The advantage of this method is that it is straightforward, and it is relatively easy to justify the price of a product or service. The disadvantage is that it's not always easy to estimate what the costs of a product will be, particularly for a start-up. Once a price is set, it is difficult to raise it, even if a company's costs increase. In addition, cost-based pricing is based on what a company thinks it should receive rather than on what the market thinks a product or service is worth. It is becoming increasingly difficult for businesses to dictate prices to their customers, given customers' ability to comparison-shop on the Internet and find what they believe is the best bargain for a product.[1]

Value-based pricing

In value-based pricing, the list price is determined by estimating what customers are willing to pay for a product and then backing off a bit to provide a cushion. What a customer is willing to pay is determined by the perceived value of the product and by the number of choices available in the marketplace. Sometimes, to make this determination, a business has to conduct focus groups or try different pricing options to test markets. A business influences its customer's perception of value through branding, promotions, and the other elements of its marketing mix.

Whether you choose cost-based pricing or value-based pricing is an important call. Most experts recommend value-based pricing because it hinges on the perceived value of a product or service rather than a cost plus markup, which is a formula that ignores the customer.[2] Most experts also warn new business owners to resist the temptation to charge a low price for their products in the hopes of capturing market share. This approach can win a sale but generates little profit. In addition, most consumers make what's called a price-quality attribution when looking at the price of a product. This means that consumers naturally assume that the higher-priced product is also the better-quality product.[3] If a business charges a low price for its products, it sends a signal to its customers that the product is low quality regardless of whether it really is.

> Most experts recommend value-based pricing because it hinges on the perceived value of a product or service rather than a cost plus markup, which is a formula that ignores the customer.

Of course, regardless of whether a business chooses cost-based or value-based pricing, its price must make sense given the realities of the marketplace. Some businesses are able to charge a premium price for their product or service. To charge a premium price, one or more of the following characteristics must generally be present:

- Demand for the product is strong relative to supply.
- Demand for the product is inelastic. (People will buy at almost any price.)
- The product is patent protected and has a clearly defined target market.
- The product offers additional features that produce tangible benefits (for

example, a strong warranty that protects against having to prematurely replace the product).

- A new technology is being introduced.
- The product serves a compelling need (like a pharmaceutical product that relieves pain).
- The product is a luxury item and targets an affluent clientele.

Truth 43. It’s okay to advertise, but think through your choices carefully

There are many ways that businesses advertise. While it’s normally cost-prohibitive for new businesses to advertise on television and in major newspapers and magazines, there are alternatives that are less expensive or free. Pick and choose carefully. Advertising is an area where a business can spend a lot of money to produce meager results, or spend very little and achieve impressive outcomes.

The two major categories of advertising include print and media advertising and Internet advertising.

> Advertising is an area where a business can spend a lot of money to produce meager results, or spend very little and achieve impressive outcomes.

Print and media advertising

Print and media advertising runs the gamut from television ads to posting flyers on grocery store bulletin boards. The type of advertising a business selects hinges largely on whether it’s targeting a national audience or a local clientele. There are some advertising-related initiatives that all new businesses should take advantage of. For example, the major search engines, like Google and Yahoo!, have business directories that list local businesses and, in some cases, even provide a map to show where they are located. You can get your business listed but have to go to the Web sites and sign up. The listings are either free or subject to a small yearly fee. If you want to see how this works, type “sporting goods stores in Tulsa, Oklahoma” into the Google search bar and see what happens. The names of the “local businesses” that appear have registered their businesses in the Google business directory.

Radio advertising is effective for many businesses that have a local station with a listening audience that reflects the demographic they’re trying to reach. Classified ads, either in local newspapers or online, remain effective in many instances. Direct mail, placing an ad in a local business directory, and advertising in publications such as local homeowners’ association newsletters are additional choices. A business's own signage and visibility can be its most effective form of advertising. Some home remodeling businesses, for example, report that their top source for getting new business is people who see their trucks parked in neighborhoods and call the phone number displayed on the side of the trucks.

Another option is to advertise in an industry trade journal. A trade journal is a periodical, magazine, or publication that focuses on a specific industry, trade, or type of business. A directory of trade associations (which publish trade journals) is available through Weddle's.[1] Many trade associations also sponsor trade shows and conferences where new businesses can gain visibility and display their products.

Internet advertising

An increasingly effective way for new businesses to get noticed and sell their products is via pay-per-click Internet advertising, as discussed in Truth 15, "Internet businesses: The sky does seem to be the limit." This type of advertising is provided by the major search engines, such as Google, Yahoo!, and MSN. Google has two pay-per-click programs—AdWords and AdSense. AdWords allows an advertiser to buy keywords on Google's home page, which triggers text-based ads to the side (and sometimes above) the search results when the keyword is used. If you type "watches" into the Google search bar, you see ads from businesses that sell watches. Many companies report impressive results utilizing this approach, presumably because they are able to place their ads in front of people who are already searching for information about their products. Google's other pay-per-click program is called AdSense. It is similar to AdWords, except the advertiser's ads appear on other Web sites or blogs instead of Google's home page. You've seen AdSense ads many times as you've looked at Web sites and blogs. They are easy to spot because they have a small emblem underneath the ads that says, "Ads by Google."

> An increasingly effective way for new businesses to get noticed and sell their products is via pay-per-click Internet advertising.

Truth 44. Public relations: More important than ever

One of the most cost-effective ways for a new business to get noticed and to promote its product or service is through public relations. Public relations refer to efforts to establish and maintain a positive image for a company with the public.

The major difference between public relations and advertising is that public relations efforts are not paid for—directly. The cost of public relations to a business is whatever it takes to network with journalists and other people to try to interest them in saying and writing good things about a company and its products. While there is nothing inherently wrong with advertising and similar forms of promotion, people know that ads and promotions are paid for, so they discount them to a certain degree. It's normally more persuasive when an unbiased third party talks about the merits of your product or service.[1] The key to getting good public relations, such as a newspaper or magazine article written about your company, is to create a human interest story that's associated with your business. It also helps to be proactive in regard to speaking out on behalf of your industry and talking to trade groups and civic groups about your area of expertise.

> The key to getting good public relations, such as a newspaper or magazine article written about your company, is to create a human interest story that's associated with your business.

There are other ways in which a business can enhance its chances of getting public relationship via the press. One technique is to prepare a press kit, which is a folder that contains background information about the company and includes a list of its most recent accomplishments. The kit is normally distributed to journalists and is placed on the business's Web site. In fact, if you've ever picked up a national magazine and read an article about a business in a small town and wondered how the magazine knew about the business, it's typically because the business sent the magazine a press kit and the business's story (or product or service) fit the article the magazine was interested in writing about.

Another way to generate public relations is to win an award or be recognized in some positive manner. For example, in 2007, WhiteWave's Silk Soymilk won the American Culinary ChefsBest Award for the Best Taste. WhiteWave can now refer to the award in its promotions and has earned the right to display the ChefsBest seal of approval on its products.[2] Businesses also generate public relations by attending trade shows and similar events. For example, the largest trade show for consumer electronics is International CES, which is held in Las Vegas every January. Many new technology firms use this show to present their products to the public for the first time. They do this in part because they have a captive media audience that is eager to find interesting stories to write about.

> Another way to generate public relations is to win an award or be recognized in some positive manner.

There are also community-and industry-related activities that a business owner can engage in to generate positive public relations for the firm. Examples include writing a column in a local newspaper, publishing a company newsletter, and speaking to civic groups. These activities cost little or no money but can enhance the image of a business.

A representative list of public relations activities include

- Press releases ■Media coverage ■Articles about the business in local newspapers, national magazines, or industry press ■Blogging
- Monthly newsletter ■Sponsoring free seminars ■Contributing expert how-to or advice articles in your local newspaper ■Civic, social, and community involvement

Truth 45. Distribution and sales: More choices than ever

Distribution encompasses all the activities that move a business's products from its place of origin to the consumer. For some businesses, like restaurants and fitness centers, distribution is not a major issue because they service their customers directly. But for many companies, like Kitchen Sentry, the smoke detector company introduced in Truth 38, "How to approach marketing in a new business," the landscape is much different. Kitchen Sentry will have key decisions to make regarding how its products will be distributed and sold.

Distribution and sales alternatives

The first step in determining a distribution and sales strategy is to sort through the choices. For example, imagine you are starting a business that sells hardware products to consumers. You could opt to field a sales force that approaches retail chains like Home Depot and Lowe's to persuade them to carry your products. You could sell directly to consumers without the need for salespeople, through catalog or Internet sales. Another option is to sell through an intermediary, such as a distributor, wholesaler, or manufacturer's representative. If you decided to go this route, your intermediary would call on Home Depot and Lowe's on your behalf. Intermediaries are sometimes difficult to find and attract. It's not uncommon for a firm to have to "prove" that its product will sell, by selling it itself, before a high-quality distributor or wholesaler will sign on.

> The first step in determining a distribution and sales strategy is to sort through the choices.

Similar choices apply for some service businesses. Hotels, for example, sell their services (typically rooms) directly through their Web sites and telephone reservation services and through intermediaries, such as travel agents, tour operators, and airlines. For example, if you were planning a trip to Walt Disney World in Orlando, Florida, you could book your flight, rental car, and hotel through Orbitz, Expedia, or many similar services. In these cases, Orbitz and the others are acting as intermediaries for the service providers.

The key to making the right choices among these alternatives is to think carefully first about where people in your target market shop, and then about the most effective and economical way to get your products some shelf space in those outlets. You also need to think about the operational ramifications of your choices. Although it might sound good to get your product placed in Wal-Mart or Costco from the outset, few new businesses are prepared to ramp up production fast enough or offer the huge volume of product needed to satisfy these types of retailers. In addition, you need to carefully weigh the choice of retail outlets and other resellers with your brand and the image you want to convey to your target market. Coach, for example, is a billion-dollar company that sells stylish handbags, footwear, and accessories. It's built its business by selling through specialty stores rather than mass merchandisers. Specialty stores are more consistent with Coach's upscale image than mass merchandisers; they appeal to consumers who prioritize quality and brand image over price.

Sales strategy and related issues

If you decide to employ your own sales force, you'll need to decide how many salespeople will be needed, how the numbers will be ramped up as the company grows, and how the salespeople will be compensated. These factors vary by industry, so you'll probably need to talk to industry experts and study industry trade journals to make these calls.

If you decide to distribute your products through intermediaries, you'll have to decide how the intermediaries will be chosen and the ways in which the intermediaries will interface with the sales outlets in your industry. In most cases, you'll have to support your distributors and wholesalers with training, technical support, shipping, point-of-sale advertising material, and other forms of sales support.

An exciting element of distribution and sales strategy for new businesses is that you don't always have to follow the conventional forms of distribution and sales. One way a business can innovate and provide unique value in the marketplace is through distribution and sales. For example, Dell revolutionized the computer industry by deciding to sell directly to consumers rather than through retail stores. Similarly, ProFlowers is making noise in the flower industry by changing the number of hands that flowers pass through before they are sold to consumers. Flowers are raised by growers and then typically pass through the hands of an importer (or distributor), wholesaler, and retailer before they are sold to the customer. This process typically takes between 7 and 12 days. As a flower passes through the process, temperature and humidity often change, which degrades the flower’s appearance and shortens its vase life. ProFlowers, which sells online, has sharply reduced the number of steps a flower must go through as it travels from the grower to the customer. When an order is placed via its Web site, ProFlowers routes the order to a grower that it has contracted with. The grower fills the order and ships it directly to the customer via UPS or FedEx utilizing proprietary technology provided by ProFlowers. The intermediaries are eliminated, saving ProFlowers money and allowing the customer to receive flowers that are fresher and last longer than flowers purchased through a traditional outlet.

> An exciting element of distribution and sales strategy for new businesses is that you don’t always have to follow the conventional forms of distribution and sales.

Part IX The Truth About Financial Management

Truth 46. Managing a business's finances

A business owner's ability to get a business up and running and to keep the business operating smoothly hinges largely on prudent financial management. Regardless of the quality of a product or service or how compelling of a need it fills, a company can't be viable in the long run unless it is successful financially.

There are many practical issues involved in the prudent financial management of a business. A business owner must be aware of how much money the business has in the bank and if that amount is sufficient to satisfy the business's financial obligations. Just because a business is successful doesn't mean that it doesn't face financial challenges. For example, many small businesses that sell their products to larger companies, such as Motorola, 3M, and Home Depot, don't get paid for 30 to 60 days from the time they make a sale. Think about the difficulty this scenario creates. The small firm must buy parts, pay its employees, pay its routine bills, ship its products, and wait for one to two months for payment. Unless a business manages its money extremely carefully, it is easy to run out of cash, even if its products or services are selling like hotcakes. Similarly, as a company grows, its cash demands often increase to service a growing clientele. A business needs to accurately anticipate whether it will be able to fund its growth through earnings or if it will need to establish a line of credit at a bank or look for investment capital.

> Just because a business is successful doesn't mean that it doesn't face financial challenges.

The financial management of a business deals with questions such as the following on an ongoing basis:

- How are we doing? Are we making or losing money?
- How much cash do we have on hand?
- Do we have enough cash to meet our short-term obligations?
- How efficiently are we utilizing our assets?
- How do our growth and net profits compare to those of our industry peers?
- Where will the funds we need for capital improvements come from?
- Are there ways we can partner with other firms to share risk and reduce the

amount of cash we need?

- Overall, are we in good shape financially?

A properly managed business stays on top of the issues suggested by these questions through the tools and techniques discussed in Truth 47, "Managing a business's finances," and Truth 48, "The nitty-gritty: Forecasts, budgets, and financial statements".

Particularly important issues for first-time business owners

First-time business owners need to be aware of two additional issues that play a role in financial management.

First, many businesses are viable and ongoing once they get started. The trick is to get them started. Unless your business is cash flow positive from the beginning, which is rare, there will be a period when you'll lose money while you're ramping up the business. For example, you may be planning to open a fitness center and have determined that you'll make money if you can sign up 1,200 or more members. But you won't have 1,200 members the day you open. It may take you six months to a year to reach your membership goal. In the meantime, all your fixed expenses (and most of your variable expenses) will march on. Most businesses do experience a start-up period during which they lose money (or make little money) until they are fully up to speed and reach profitability. Businesses need to be fully aware that this period will take place and to plan for it. The worst time to go to a bank, family member, or investor to help meet a cash shortfall is when you're facing a cash crisis.

> Many businesses are viable and ongoing once they get started. The trick is to get them started.

The second thing to be mindful of if you are a first-time business owner is that most people are not familiar with how to complete the types of forecasts, budgets, and financial statements that are needed to prudently manage the finances of a growing business. If you fall into this category (as most people do), don't wing it. Get help. The financial management of a business is too imperative not to take it seriously. A good source for one-on-one help is SCORE, an organization mentioned several times in this book. Small Business Develop Centers (SBDCs) frequently hold workshops on how to complete financial statements and learn accounting and budgeting software programs.

Truth 47. Financial objectives of a business

Before a business develops the types of forecasts, budgets, and financial statements that it needs to manage its finances, it must have a firm grasp of its financial objectives. Nearly all businesses have three main financial objectives: profitability, liquidity, and overall financial stability. Understanding these objectives sets a business on the right financial course and helps explain the need for forecasts, budgets, and financial statements, which will be discussed in Truth 48, "The nitty-gritty: Forecasts, budgets, and financial statements."

> Nearly all businesses have three main financial objectives: profitability, liquidity, and overall financial stability.

Profitability

Profitability is the ability to earn a profit. Many start-ups are not profitable their first several months of operations, as discussed in Truth 47, "Financial objectives of a business," but they must become profitable to create a sustainable business and provide a return to their owners.

A business also must know if its profits are increasing or declining and whether they are leading or lagging industry averages. The first question, whether a business's profits are increasing or declining, can be answered through the maintenance of accurate financial records. The second question, whether a business's profits are leading or lagging industry averages, is tougher. Normally, businesses collect this information through informal conversations with industry peers or by joining an industry trade group, which typically collects information about the average profitability for businesses in the industry.

Obviously, if a business's profits are declining (or are nonexistent) or if the business is lagging industry averages, corrective action is necessary. One thing that continually surprises small business counselors is the number of small business people who don't have a good grasp on whether their profits are increasing or declining and how they stack up against their industry peers. Don't fall into that group. Stay on top of these issues so you can take corrective action immediately if necessary.

Liquidity

Liquidity is a company’s ability to meet its short-term financial obligations. As indicated in Truth 46, “Managing a business’s finances,” a business must carefully manage its cash to make sure it has enough money in the bank to meet its payroll and cover its short-term obligations.

Normally, the biggest culprits in straining a business’s liquidity are letting its accounts receivables or its inventory levels get too high. There are many colorful anecdotes about business owners who have had to rush to a bank and get a second mortgage on their houses to cover their business’s payroll. This set of events usually occurs when a business takes on too much work and its customers are slow to pay. A business can literally have a million dollars in accounts receivable but not be able to meet a $25,000 payroll. This is why almost any book you pick up about growing a business stresses the importance of properly managing your cash flow.

Some businesses deal with potential cash flow shortfalls by establishing a line of credit at a bank or by maintaining a healthy cash reserve. Other businesses are careful not to take on too much work, so their accounts receivable and inventory levels remain manageable.

Overall financial stability

Stability is the strength and vigor of the business’s overall financial posture. For a business to be stable, it must not only earn a profit and remain liquid but also keep its debt in check. If a firm continues to borrow from its lenders and its debt-to-asset ratio (which is calculated by dividing its total debt by its total assets) gets too high, it may have trouble meeting its obligations and securing the level of financing needed to fuel its growth.

Many business owners are caught off guard by the continuing need to remain vigilant regarding the overall financial stability of their business. You would think that if a business got off to a good start, increased its sales, and started making money, things would get progressively more stable. In many instances, however, just the opposite happens. Imagine the following scenario. A business gets off to a fast start and projects that its sales will double in the next two to three years. To make this happen, the business needs more people and additional equipment to handle the increased workload. The new equipment needs to be purchased, and the new people need to be hired and trained before the increased business generates additional income. Even though the business might be better off in the long run as a result of the increased business, it’s easy to see the strain that’s placed on the business in the short run to get there.

> Many business owners are caught off guard by the continuing need to remain vigilant regarding the overall financial stability of their business.

Truth 48. The nitty-gritty: Forecasts, budgets, and financial statements

To assess whether its financial objectives are being met, businesses rely heavily on the preparation and the ongoing analysis of forecasts, budgets, and financial statements. In addition, it's necessary for business owners to learn basic bookkeeping, to keep their records straight for tax and other reporting purposes.

Forecasts

A forecast is an estimate of a business's future income and expenses. It's the first step in completing a budget and a set of projected (or pro-forma) financial statements. A business that is already up and running bases its forecasts on its past performance, its current circumstances, and its future plans. So a business that grossed $250,000 last year would use that figure as a starting point for projecting next year's sales and would then adjust the figure upward or downward based on current circumstances (that is, state of the economy, entrance of new competitors, buying mood of customers) and future plans. The same rationale applies for forecasting expenses.

It's harder to forecast the initial sales and expenses for a start-up. There are four common ways to go about it:

- Contact the trade associations in your industry to ask if they track the annual sales and expense numbers for businesses that are similar to the one you plan to start.
- Find a comparable business and ask the owner if he or she would help you predict your initial sales and expenses.
- Conduct Internet searches to see if you can find articles about businesses that are similar to the one you plan to start. Occasionally, the articles will include sales and expense figures.
- Utilize the multiplication method to project sales. If you're planning to sell a product on a national basis, like the Kitchen Sentry Smoke Detector, utilize a top-down approach: You estimate the total number of people who buy smoke detectors, estimate the average price they pay, and then

estimate the percentage of the market you believe you will get. If you have a business that will sell on a local basis, like a restaurant or a clothing boutique, you utilize a bottom-up approach: You determine how many customers to expect and the average amount each one will spend.

Most experts feel that finding a business comparable to the one you plan to start and asking the owner for input is the most effective method for forecasting the initial sales and expenses for a new business.

> Most experts feel that finding a business comparable to the one you plan to start and asking the owner for input is the most effective method for forecasting the initial sales and expenses for a new business.

Budgets

Budgets utilize the information generated by forecasts and organize a business's income and expenses into specific categories. In most cases, a business completes its forecasts and budgets simultaneously. Organizing a business's income and expenses into specific categories provides a practical way of tracking those numbers on an ongoing basis and helps a business answer the question, "Are we on track financially?"

Budgets also help a business in day-to-day decision making. For example, if a business budgets $10,000 a year for marketing, and midyear it has spent $5,000 of its budget, it knows that it can't say yes to an advertising company that is trying to persuade it to buy a $7,500 marketing campaign for the remainder of the year without exceeding its budget.

Financial statements

To further understand, track, and document their financial performance, businesses should also complete historical and projected financial statements on a regular basis. The statements include the income statement, balance sheet, and cash flow.

The historical income statement reflects the results of the operators for a business for a given period. It records all the projected sales and expenses and shows whether the business is making a profit or is experiencing a loss. The balance sheet is a snapshot of a business's assets, liabilities, and owner's equity at a specific point in time. It is an important tool for measuring a business's overall financial stability. The cash flow shows the money that is flowing into and the money that is flowing out of a business on an ongoing basis; it provides a real-time picture of a business's cash position. Projected financial statements are similar to historical statements except they look forward rather than backward.

Completing both historical and projected financial statements takes some practice, and most business owners buy books, attend workshops, or work with their accountants to learn how to prepare the statements. If you aspire to obtain a bank loan, seek investment capital, or sell your business at some point, you need to maintain accurate financial statements. It's difficult for a banker, investor, or potential buyer to analyze your business without historical and projected incomes statements, balance sheets, and cash flows to go by.

Part X The Truth About Growing a Business

Truth 49. Preparing for growth

Most businesses want to grow. Even businesses that are started to accommodate a certain lifestyle or allow their owner to meet a personal goal or aspiration normally want to expand their sales and profits over time.

Growth doesn't happen by chance, however. Growing a business successfully takes preparation, good management, and an awareness of the challenges involved. Growing a business can be a joy or a nightmare—trust me, I've seen both. There are many businesses that have started, grown prudently, and are thriving, returning to their owners just the sort of lives they had hoped for. Sadly, there are also many businesses that have done just the opposite—they've started, grown either too slowly or too quickly, and have failed, leaving their owners financially and emotionally drained.

> Growing a business successfully takes preparation, good management, and an awareness of the challenges involved.

The key to properly preparing for growth involves appreciating the nature of growth and planning for it in a conscientious and purposeful manner.

Appreciating the nature of business growth

There are two central things to appreciate about the nature of business growth. First, not all businesses have the potential to be aggressive growth firms. The businesses that have the potential to grow the fastest over a sustained period of time are ones that solve a significant problem or have a major impact on their customers' productivity or lives. This is why the lists of fast-growing businesses are often dominated by technology and health-care companies. These companies have the potential to make the biggest impact on their customer's lives. This point is affirmed by comparing the frozen food industry to medical products and biotechnology. In 2007, the frozen food industry grew by 0.6 percent, while the medical products industry grew by 3.2 percent and biotechnology grew by 9.5 percent.[1] While there is nothing wrong with starting a business in frozen foods, you need to have a realistic outlook on how fast the business will likely grow. Even though an individual frozen food company may get off to a fast start, as it gets larger, its annual growth will normally start to reflect its industry's norms.

The second thing that a business owner needs to appreciate about growth is that a business can grow too fast. Many businesses start fast and never let up, which is stressful for everyone involved. Other businesses start, grow at a measurable pace, and then experience a sudden upswing in orders and have difficulty keeping up. This scenario can transform a business with satisfied customers and employees into a chaotic workplace with people working 50+ hours a week scrabbling to push the business's product out the door as quickly as possible. Here are some indicators that a business is growing too fast:

- You have to borrow money to pay for routine operating expenses.
- You have extremely tight profit margins.
- You have an overstretched staff.
- Your quality is slipping.
- Customer complaints are up.
- Your productivity is falling.
- The work environment is stressful and frantic.

The way to prevent these and similar outcomes from happening is to recognize when to put the brakes on and have the courage to do it. Sometimes this means actually turning down business, which can be a hard thing to do for a business that is committed to servicing its customers in the best manner possible.

Planning for growth

You also should plan for growth. The process of writing a business plan, discussed in Truth 10, "Writing a business plan: Still as important as ever," greatly assists in this effort. A business plan normally includes a detailed forecast of a business's first three to five years of sales along with an operations plan that describes how the business will meet its forecasts. Even though the business will invariably change during the first three to five years, it's good to have a plan. Many businesses periodically revise their business plans and allow them to help guide their growth-related decisions.

A business owner should also step back and measure the business's growth plans against his or her personal goals and expectations. As mentioned in Truth 2, "The right business for you," a decision to grow quickly will necessitate a quick pace of activity and a hectic lifestyle. Although the upside may be a more financially successful business, sacrifices will have to be made in terms of the number of hours worked and the pressures that accompany a more hectic lifestyle.

A business owner should also step back and measure the business's growth plans against his or her personal goals and expectations.

Truth 50. Stages of growth: More opportunities, more challenges

The majority of businesses go through a discernible set of stages referred to as the organizational life cycle. These stages include introduction, early growth, continuous growth, maturity, and decline. Each stage must be managed differently. Business owners need to be familiar with these stages, along with the unique opportunities and challenges that each stage entails.

The introduction, early growth, and continuous growth stages are focused on here.

Introduction

This is the start-up phase where a business determines what its core strengths and capabilities are and starts selling its initial products or services. It's a hands-on phase for the owner, who is normally involved in every aspect of the day-to-day operations of the business. The business is typically nonbureaucratic, with no (or few) written rules or procedures. The main goal of the business is to get off to a good start and to try to gain momentum in the marketplace.

The primary challenges for a business in the introduction stage are to make sure the initial product or service is right and to start laying the groundwork for building a larger and busier organization. Don't rush things. For instance, if you start a Web site to sell shoes, it's normally best to make sure your approach to selling shoes works and resonates in the marketplace before adding handbags, sunglasses, and other items.

> The primary challenges for a business in the introduction stage are to make sure the initial product or service is right and to start laying the groundwork for building a larger and busier organization.

In regard to laying the groundwork to build a larger organization, many businesses use the introduction stage to try different concepts to see what works and what doesn't, recognizing that trial and error gets harder as the business grows. It's good to document what works and start thinking about how the business's success can be replicated when the owner isn't present or when the business expands beyond its original location.

Early growth

A business's early growth stage is characterized by increasing sales and heightened complexity. The business is normally still focused on its initial product or service but is trying to increase its market share and might have related products in the works. The initial formation of policies and procedures takes place, and the process of running the business starts to consume more of the owner's time and attention.

For a business to be successful in this stage, two things must take place. First, the owner of the business must start transitioning from his or her role as the hands-on-supervisor of every aspect of the business to a more managerial role. As articulated by Michael E. Gerber in his excellent book *The E-Myth Revisited*, the owner must start working "on the business" rather than "in the business."[1] The basic idea is that early in the life of the business, the owner is typically directly involved in building the product or delivering the service that the business provides. As the business moves into the early growth stage, the owner must let go of that role and spend more time learning how to manage and build the business. If the owner isn't willing to make this transition or doesn't know that it needs to be made, the business will never grow beyond the owner's ability to directly supervise everything that takes place, and the business's growth will eventually stall.

The second thing that must take place for a business to be successful in the early growth stage is that increased formalization must take place. The business has to start developing policies and procedures that tell employees how to run it when the owner or other top managers aren't present. This is how a McDonald's restaurant runs so well when it's staffed by what appears to be a group of teenagers. The employees are simply following the policies and procedures that were originally written down by Ray Kroc, McDonald's founder, and have been added to and improved over the years. An early growth stage business will not develop policies and procedures as elaborate as McDonald's, but it must start formalizing how it achieves its success.

Continuous growth stage

As a business moves beyond its early growth stage and its pace of growth accelerates, the need for structure and formalization increases. The resource requirements of the business are usually a major concern, along with the ability of the owner and manager to take the firm to the next level. Often, the business will start developing new products and services and will expand to new markets. Smaller firms may be acquired, and the business might start partnering with other firms.

The importance of developing policies and procedures increases during the continuous growth stage. A business also needs to develop a formal organizational structure and determine clear lines of delegation throughout the business. Although *formalization* is a term that is often frowned upon by business owners who want to free themselves from the trappings of Corporate America, well-developed policies and procedures lead to order, which typically makes the process of growing a business more organized, enjoyable, and successful.

> The importance of developing policies and procedures increases during the continuous growth stage.

Truth 51. Strategies for growth

The practical side of growth is the actual strategies that businesses employ to grow their organizations. It's helpful for business owners to be acquainted with the breadth of growth-related strategies that are available so they can select the strategy or strategies that make the most sense at a certain point in time in light of their individual situations.

The strategies for growth are divided into internal growth strategies and external growth strategies.

Internal growth strategies

Internal growth strategies involve efforts taken within the business, such as new product development, other product-related strategies, and international expansion. Almost all businesses start by featuring internal growth, and many businesses stick with this strategy as they grow. Here are the most common internal growth strategies:

- New product development
- Improving an existing product or service
- Increasing the market penetration of an existing product or service
- Extending product lines
- Geographic expansion
- International expansion

Many businesses prefer internal growth because it typically leads to an incremental, even-paced approach to growth. For example, many retailers start with one store and then grow by opening additional stores or by selling their products through distributors. By growing in this manner, the company can control its pace of growth and time its store openings and new distribution agreements to coincide with the resources it has available. It's also easier for a business to control its culture by growing through internal means. If a business grows by adding employees as new products (or stores) come online, it can socialize the employees into its culture. Conversely, if a firm grows via an external strategy, such as an acquisition, it will have employees who have been raised in different corporate cultures and will normally have a more difficult time creating cohesion among its employees.

> Almost all businesses start by featuring internal growth, and many businesses stick with this strategy as they grow.

The primary downside of internal growth is that it tends to be a slow form of business growth. While a slow, deliberate approach to growth has many advantages, in some industries relying strictly on internal growth does not permit a business to develop sufficient economies of scale or broaden its product offerings fast enough to remain competitive.

External growth strategies

External growth strategies rely on establishing relationships with other firms, such as mergers, acquisitions, strategic alliances, and franchising. It is increasingly common for businesses to utilize one or more external growth strategies as soon as the early growth stage of its organizational life cycle. Here are the most common external growth strategies:

- Merger
- Acquisition
- Licensing agreement
- Strategic alliance
- Joint venture
- Franchising

A business can normally grow faster through external growth than internal growth because it immediately adds a product or capability that might have taken months or years to develop internally. For example, when eBay acquired PayPal, it acquired PayPal’s proprietary electronic payments system, something PayPal worked diligently to perfect over a period of several years. Similarly, by forming a strategic alliance or joint venture, a firm can tap into the resources of its partner and reach new markets without having to build out its own infrastructure. For example, many American food companies have strategic alliances with large European food companies to gain access to their European distribution networks.

> A business can normally grow faster through external growth than internal growth because it immediately adds a product or capability that

might have taken months or years to develop internally.

The primary downside of external growth is that by relying on other firms to help develop its growth, a business loses some of its flexibility and decision autonomy. It also complicates its business and runs the risk of joining with a partner that is either unreliable or doesn't share its core values. The net result of engaging in external growth is usually to speed up a business's pace of growth. As a business's pace of growth increases, the challenges of growth, such as cash flow management, are usually exacerbated.

Many businesses blend internal and external strategies for growth as they pass through the stages of growth and expand their businesses. The important thing to remember as a business owner is that you should select the means of growth that is best for you and your company, given the conditions you face and the lifestyle decisions you've made.

Part XI The Truth About Starting a Business and Maintaining a Healthy Personal Life

Truth 52. Work life balance: Practical tips

Most people start businesses to improve their lives—whether the goal is to make more money, have a more flexible lifestyle, or pursue a particular passion. But business ownership can also be all-consuming. It can easily consume the majority of a person's time and attention and negatively affect an individual's marriage, family life, and physical and emotional well-being.

Fortunately, there are steps that business owners can take to strike a healthy balance between their business and their personal lives, but there is a catch. The catch is that the steps must actually be taken—they can't just be thought about or put on a to-do list. The following is a list of three practical tips for starting a business and maintaining a healthy personal life. Candidly, it's been my observation that people who start businesses and end up with miserable personal lives don't do any of these things. Don't let this happen to you. Take these tips to heart, and search for additional tips and advice.

Establish a routine

Many business owners suffer because they don't place boundaries on their business life. The enviable result is working long hours because there is always something that needs to be done. The way to solve this problem is to set a routine and stick to it. Depending on the nature of your business, you could set your hours for 8:00 a.m. to 5:00 p.m. on weekdays. If that isn't a realistic approach, you could commit to being home every evening by 6:00 p.m. or commit to not working on Saturdays and Sundays.

> Many business owners suffer because they don't place boundaries on their business life.

While you'll have to find a schedule that works for you, the overarching point is to establish a routine and stick to it. This approach will provide you time to unwind and will allow your family to reliably schedule activities during your free time.

Get help

There is no reason to "go it alone" as a business owner. Virtually every city and midsized town has an active SCORE chapter, and access to Small Business Development Centers and other sources of counseling and advice are either available or just a stone's throw away. You should also align yourself with mentors and set up a board of advisors, as suggested in Truth 32, "Board of advisors." The ability to share the pressures of your business with others relieves burnout and typically leads to a brighter and healthier disposition. As your business grows, you may also be able to shift some of the pressure to partners or employees.

An example of the positive influence that a mentor or advisor can have is provided by Oron Strauss, a business owner who received funding from a business angel. Recalling an experience with his angel investor, Strauss said,

> "About a year ago, when I was having a particularly bad week, I fired off a long, heartfelt e-mail message to my angel. I explained, in great detail, the difficulties I faced and my thoughts about them. His response was succinct: 'All sounds normal. You're handling it well. Keep up the good work.' My first response was disappointment over what struck me as a curt response. Then I realized that the angel had given me the best possible response. He understood what I was going through was normal and that I would make it."[1]

Imagine how advice like this positively affects a person's personality disposition and self-esteem. One of the best ways to maintain a successful business and a healthy personal life is to remain emotionally healthy yourself.

One of the best ways to maintain a successful business and a healthy personal life is to remain emotionally healthy yourself.

Set up systems and procedures

A third way to find the right balance between your business and your personal life is to put in place systems and procedures that help the business run without your being physically present. This is a step that takes time and experience to implement but is vital. One of the worst predicaments to get into, as a business owner, is to open a restaurant, store, or similar business and base so much of the success of the business on your physical presence that you feel you can't leave while the business is open. This type of setup traps a business owner into a life of long hours, week after week, with no end in sight. It's hard for anyone to run a successful business and maintain a healthy personal life under these types of circumstances.

A much better approach is to carefully document every aspect of how the business is run and then develop systems, policies, and procedures that others can follow while you aren't physically present. This scenario is what allows a business to run smoothly and reflect all the positive attributes of the owner, even when the owner isn't physically present. It's also the only way a business owner can maintain a normal life, especially if the business is open 70 to 80 hours a week, which is normal for a restaurant or retail store.

Truth 53. Starting a business as a means of achieving a healthy personal life

While many business owners start businesses and then struggle to find the right balance between their business and their personal life, others approach the process in the opposite manner. They begin with a desire to achieve a properly balanced life and then start a business as a means of achieving it.

There are three distinct advantages that business ownership offers in regard to achieving a healthy personal life. These advantages are available in varying degrees, depending on the nature of the business. In some cases, they represent the very reason that people choose business ownership over a traditional career.

Flexibility

Although most business owners work just as hard or harder than people in traditional jobs, they normally have more flexibility in their schedules. This facet of business ownership appeals to people who feel strongly about goals that they have outside of work, like being home when their kids get off the school bus or doing volunteer work. Some people value this facet of business ownership so much that they're willing to sacrifice some level of income for self-employment. This sentiment is affirmed by Margot James, a business owner who wrote,

> "One of the reasons I enjoy what I do is the flexibility. I have other interests besides paid work. I do a lot of volunteer community work...I have decided that whatever needs I have, I could sacrifice some level of income for flexibility. I made that conscious decision."[1]

Being your own boss also provides you the flexibility to build a business that is consistent with your personal values and ideas. For example, Chick-fil-A, a $2 billion chain of chicken restaurants, isn't open on Sundays and places books and other "values-based" messages in its kids meals. These practices are a direct reflection of founder Truett Cathy's personal values.

Achieving a personal goal or aspiration

As indicated in Truth 1, “Why people start businesses,” sometimes starting a business is the only way people can fulfill their most important goals and aspirations. For example, there are heartfelt stories of people who have faced challenges in their lives, such as a child with a debilitating medical issue, who have had to create businesses to find a solution for their child’s problem because no other solution was available. In these instances, a person’s goals and aspirations quickly shift to finding relief for a loved one’s suffering or affliction.

> Although most business owners work just as hard as or harder than people in traditional jobs, they normally have more flexibility in their schedules.

Other examples are less extreme but demonstrate a similar point. One example is Sue Schwaderer and Bill Lawrence. In the late 1990s, Schwaderer was making a six-figure income working for Oracle Software, and Lawrence was successful managing three apartment buildings they owned in Evanston, Illinois, a Chicago suburb. Although they were making good money, they didn’t enjoy their everyday life. “We were tired of never seeing each other and of too much business travel...too much traffic, too many people, too much noise,” Schwaderer recalls.[2] The two left their life in Chicago behind and opened a 14-room bed and breakfast in picturesque Saugatuck, Michigan, a town of 1,000. Although the income from the bed and breakfast doesn’t match what they were making in Chicago, they are happier and enjoy the less hectic pace of a smaller town.

The ability to pursue a passion

Finally, as expressed throughout this book, the ability to pursue a personal passion is the instrumental reason that many people start their own business. In many instances, the business returns to the owner a sense of fulfillment and satisfaction that has a positive impact on his or her personal life.

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About the Author

Bruce Barringer, a renowned expert on entrepreneurship, is Professor of Management at University of Central Florida. His books include *Entrepreneurship: Successfully Launching New Ventures, 2nd Edition, Preparing Effective Business Plans: An Entrepreneurial Approach, and What's Stopping You?: Shatter the 9 Most Common Myths Keeping You from Starting Your Own Business.*

So, You Want to Start a Business?

8 Steps to Take Before Making the Leap

Edward D. Hess
Charles F. Goetz

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Dedication

To all the entrepreneurs who have taught me that business is much more than just making money; it is the primary means through which most people achieve their dreams for a better life for themselves and their families. To that end business is a noble profession.

—Ed Hess I dedicate this book to everyone who dreams of a better life and who is willing to accept some risk so that they can see their dreams come true. And to my family, who has made it possible for me to achieve my dreams. Thank you—I love you all.

—Charlie Goetz

Praise for *So, You Want to Start a Business?*

"I used *So, You Want To Start a Business?* to restructure my furniture hardware company. The book was full of applicable information that I have used and will continue to incorporate into my company. I couldn't ask for a better resource."

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"Practical, sensible advice to anyone starting a business. A great short course in entrepreneurship."

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"This is exactly the kind of book first time entrepreneurs always needed but was never available. Everyone who is thinking about becoming an entrepreneur must read this book."

—Dr. E.W. Leonard, Associate Dean, Executive MBA Program, Goizueta Business School, Emory University "Here is the straight story about being a successful entrepreneur from people who have been one and taught many. Clear, practical, and concise, this book delivers the goods."

—Andy Fleming, Principal, Core Growth Partners, Atlanta, GA "Solid advice for building and growing a sustainable business."

—Andrew Bourne, CEO, WayPoint Technologies, Phoenix, AZ

"Professor Hess's book has helped me improve my services and make clients feel appreciated, respected, and most of all, like they're getting a great service at a fair price."

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—Derica Justice, Owner, Bon Bini Print & Design

"This is a great practical guide with lessons and insights for anyone who wants to start a business. You will go back to it again and again."

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"Whether you are a striving young entrepreneur or a middle-aged person with the courage to trust your wits, this book is indispensable."

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—Philippe Sommer, Director of Entrepreneurship Programs, Batten Institute, Darden School of Business, Charlottesville, VA "This book is a great primer and an excellent reference book for an entrepreneur."

—Walter Negley, CEO, TSP, Houston, TX

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—Ed Hess

First off, I would like to apologize for those who I might have inadvertently left out. If your name is not on this list and it should have been, unfortunately you are one of them—my sincere apology.

There have been many people who have directly and indirectly helped me in the writing of this book. In many cases, they don’t even know they helped, including some of my colleagues and students at Emory and the entrepreneurs and board members that I work closely with every day.

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Most importantly, though, I want to give special thanks to Ed Hess. To his credit,

he recognized before anyone else that there is a large market of want-to-be entrepreneurs who have had little business training and that they deserved a tool of their very own they could use to achieve the type of business success they too have been dreaming of.

So, You Want to Start a Business? was his dream and a worthy endeavor. I very much appreciate that he allowed me to come along.

—Charlie Goetz

About the Authors

Edward D. Hess is a Professor of Business Administration and Batten Executive-in-Residence at the Darden School of Business at the University of Virginia. Prior to joining Darden, he was Adjunct Professor of Business, Founder and Executive Director of both the Center for Entrepreneurship & Corporate Growth and the Values-Based Leadership Institute at the Goizueta Business School, Emory University.

Professor Hess is the author/editor of five other books and over 40 articles on business strategy, finance, growth, and family businesses. He is a magna cum laude graduate of the University of Florida and received a J.D. degree from the University of Virginia and an LL.M degree from New York University.

He is a frequent speaker, and his work has appeared in the *Financial Times*, *Fortune* magazine, and on CNBC.

Prior to joining academia, Professor Hess spent 30 years in the business world as a lawyer, investment banker, strategy consultant, and entrepreneur with Atlantic Richfield Company, Warburg Paribas Becker, Boettcher & Company, The Robert M. Bass Group, and Andersen Corporate Finance. His primary business focus has been private entrepreneurial businesses, and he has built three successful service businesses. He has taught courses on Entrepreneurship, Entrepreneurial Leadership, Organic Growth, and Managing Small Businesses. His writings and books can be found at www.EDHLTD.com.

Charles F. Goetz is the Distinguished Lecturer in Entrepreneurship at the Goizueta Business School at Emory University. Prior to joining Emory, Mr. Goetz was a successful serial entrepreneur. He built nine businesses, which in total employed over 1,500 people. He was successful in selling a number of these businesses while also experiencing some failures. Combined, these businesses gave him a valuable insight into understanding what it truly takes to build a successful business.

Professor Goetz serves on the Boards of Directors of several entrepreneurial venture and not-for-profit organizations. He is also an Angel investor in several businesses and is a frequent speaker on Entrepreneurship and Business Development. He recently published his first book, *The Great Entrepreneurial Divide: The Winning Tactics of Successful Entrepreneurs and Why Everyone Else Fails!* In addition, he has been recognized by Emory students as an Outstanding Lecturer in the MBA and Executive MBA Programs. Prior to becoming an entrepreneur, Professor Goetz was a senior executive at Citicorp. He has a BA in Economics from Emory University and an MBA from the University of Texas at Austin.

Introduction

Welcome to our book! In this introduction, we want to answer a few questions that many of you may have:

- Should you buy this book?
- Why is this book important?
- What topics are covered?
- Why are the authors qualified to write this book?

Who Should Buy This Book?

This book was written to help anyone starting a business—whether he or she is a business person or not. This book also should be helpful for anyone who has started a business and is not making enough money. Lastly, this book should help anyone investing in a start-up because most start-ups face the same challenges.

Why Is This Book Important?

Over 5,000,000 new businesses are started each year, but millions will fail, and most new businesses fail for the same sets of reasons. Our experience has taught us that there are 8 common reasons why start-ups fail, and with our combined 50 years building, financing, and teaching others how to build successful businesses behind us, in this book we offer ways to avoid making those 8 common mistakes.

What Topics Are Covered?

Our goal is simple and focused: to teach you how to avoid the 8 common mistakes many start-ups make.

Ask ten people why so many new business ventures fail, and many will answer, "Because the new business was undercapitalized." Undercapitalized means the business runs out of money before it makes enough profit to survive. We disagree with that conclusion. Running out of money is the result or consequence of more fundamental, underlying failures—the 8 common mistakes—which we teach you how to avoid.

People run out of money because they make one or more of the following 8 common mistakes:

1. Choosing a bad business opportunity (Chapter 3)
2. Choosing the wrong customers (Chapter 4)
3. Trying to sell the wrong product (Chapter 5)
4. Selling for the wrong price (Chapter 6)
5. Overestimating the number of and the speed of customer purchases (Chapter 7)
6. Mismanaging the business (Chapter 8)
7. Failing to hire and retain the right people (Chapter 9)
8. Being unable to grow or scale the business to accommodate growth (Chapter 10)

This book will direct your focus to the 3 Ws:

1. **W**hat will you sell?
2. **W**ho will buy?
3. **W**hy will they buy?

Why Are We Qualified to Write This Book?

Ed Hess lives in Charlottesville, Virginia, and spent most of his business life advising entrepreneurs and financing their business ventures. He went to college at the University of Florida and to law school at the University of Virginia and graduate law school at New York University. Ed's professional career was spent with firms like Atlantic Richfield Company, Warburg Paribus Becker, Boettcher and Company, The Robert M. Bass Group, and Andersen Corporate Finance, and he has built three service businesses.

In 1999, Ed began teaching business students part-time at Goizueta Business School, Emory University, during which time he created and taught the entrepreneurship course. In 2002, Ed joined the faculty at Goizueta full-time as an Adjunct Professor where he became the Founder and Executive Director of both the Center for Entrepreneurship and Corporate Growth and the Values-Based Leadership Institute.

Ed has written five other books:

- Hess, Edward D. *Make It Happen! 6 Tools for Success* (EDHLTD, 2001).
- Hess, Edward. *The Successful Family Business: Proactively Managing Both the Family and the Business* (Praeger: Westport, Connecticut, 2005).
- Hess and Kazanjian, eds. *The Search for Organic Growth* (Cambridge University Press: New York, 2006).

- Hess and Cameron, eds. *Leading with Values: Positivity, Virtue and High Performance* (Cambridge University Press: New York, 2006).
- Hess, Edward. *The Road to Organic Growth: How Great Companies Consistently Grow Marketshare from Within* (McGraw-Hill: New York, 2007).

In July 2007, Ed joined the Faculty of the Darden School of Business at the University of Virginia as a Professor of Business Administration and Batten Executive-in-Residence where he teaches courses on building small businesses and organic growth.

Charlie Goetz earned his college degree at Emory University and holds an MBA from the University of Texas. Charlie is a successful serial entrepreneur. He built several successful businesses, which in total employed over 1,500 people. He sold most of his businesses and made substantial amounts of money their sales. Charlie then began teaching entrepreneurship at Emory University in the Goizueta Business School where he was again successful. His courses are always oversubscribed, and he has earned multiple teaching awards.

Today, Charlie lives in Atlanta, Georgia, and is an investor in several new businesses and consults with people starting businesses. His specialties are marketing, customer acquisition, and product development.

How to Use This Book

There are two ways to use this book:

1. Read it from start to finish. It was written in a specific order—tracing a business idea from the idea stage through the steps of building a business.
2. If you want to focus on a specific question, issue, or problem, go to that chapter. Each chapter will stand by itself.

This book will not guarantee that you will be successful, but it should help you avoid the 8 common mistakes made by start-up businesses.

Chapter One. Can You Be a Successful Entrepreneur?

Chapter Topics

- ***What do successful entrepreneurs do?***
- ***Who are successful entrepreneurs?***
- ***Two common paths to entrepreneurial success***

You have decided to open a business. Now what? What product or service do you want to sell? Who needs that product or service? As you explore the pages that follow, you must consider every aspect of what you need to know to succeed and avoid the common pitfalls.

Business Rule #1

The Jerry McGuire Rule: Follow the Money—Cash is King.

What Do Successful Entrepreneurs Do?

> Successful entrepreneurs satisfy **CUSTOMERS' NEEDS** better, faster, and/or cheaper than someone else (the competition).

Business is a game—a serious game. It is a competition. You keep score by adding up sales (cash received from customers), and you make sales by meeting or satisfying customer needs.

Business Rule #2

The Peter Drucker Rule: "The sole purpose of business is to serve customers."

Peter Drucker was one of the leading business management thinkers of the last decade. He understood that every business is a service business regardless of what product it sells because the primary purpose of a business is to serve customers. To serve customers you must satisfy their needs at a better price or with better service than your competition does.

Who Are Successful Entrepreneurs?

Many people think that to be a successful entrepreneur, you need to be smart, have money, have a college degree, be an inventor, do something which never has been done before, and/or be willing to risk all your savings and your family's money.

Wrong, Wrong, Wrong, *WRONG*

To be a successful entrepreneur:

You do <u>NOT</u> have to be an "A" student.

You do <u>NOT</u> have to have a college degree.

You do <u>NOT</u> need to have a lot of money.

You do <u>NOT</u> have to be an inventor.

You do <u>NOT</u> have to take big risks.

Howard Schultz, who built Starbucks, came from poverty. Bill Gates, who built Microsoft, dropped out of college. Sam Walton did not invent a new business. Ross Perot did not take big risks when he built EDS.

Academic research has shown that there is no correlation between personality, intelligence, book learning, or family pedigree and entrepreneurial success. Moreover, research has taught us that successful entrepreneurs do not have to take big risks and "bet the ranch"; but rather, they test ideas quickly while risking small amounts. Entrepreneurs test their ideas and test the key assumptions that are necessary for business success. They get in the field with potential customers and learn from doing.

So anyone who has the right skills and right temperament and who can sell his or her skills can be an entrepreneur. Age, gender, nationality, country of origin, race, religion, and schooling are not predictive of success or failure.

Successful entrepreneurs are action-oriented—they try their ideas with customers and learn how to improve their products or services. Entrepreneurs are tinkerers. They keep working at it until they get it right for customers.

Customers determine success. To be successful, you need to produce a good product that delivers value to the customer for a fair price. Value means meeting customer needs.

We also know that to be successful you do not need a unique product or service, nor do you need to be smarter than your competition. What you have to do better is (1) listen to your customer and help your customer meet their needs, (2) give your customer great service, and (3) deliver a good product—all for a fair price, fair to the customer and to you.

What have we learned from successful entrepreneurs?

Many successful entrepreneurs came from humble backgrounds and were raised by ambitious parents. Many worked for years in a business before leaving to start their own businesses. And most were not inventors. Most successful entrepreneurs are able to find good opportunities. They find needs that many customers have and then have the courage to take the leap to try to meet those needs on their own.

Good entrepreneurs understand that the customer is always right—so they listen to customers and try to improve their products. They are not stubborn, defensive, or rigid.

Business Rule #3

Customers know best what they need.

Good entrepreneurs are also generally good with people. People like doing business with nice people, and employees like working for nice people.

Key Definitions

First, let's agree on some key definitions used throughout the book.

- An ***entrepreneur*** is anyone who actually starts a new business. Note we said start—not think about, not consider—but actually do it.

Entrepreneurs are doers.
"To do is to be."—Socrates
"To be is to do."—Plato

- ***Entrepreneurship*** is the process of building a business. This process is an "act–learn–do it better" process. Entrepreneurs learn as they go. This learning is iterative and incremental.
- A ***customer*** is anyone with unmet needs who has enough money to pay someone else to meet those needs.
- ***Price*** is the amount of money you get paid to do something for a customer—or the amount of money a customer is willing to pay you to meet their need.
- ***Cost*** is the amount of money it costs you to meet the customer's need. Costs include materials, overhead, labor, delivery, billing, installation, heat, lights, rent, taxes, and so on.
- ***Profit*** equals cash received from a customer less your costs to produce the product or service.
- ***Your profit*** is what you live on—what you have to spend for rent, mortgage, car, food, lights, clothes, kids, and so on.

Two Common Paths to Entrepreneurial Success

Basically, there are two ways to increase your chances of entrepreneurial success:

1. ***Learn the business:*** Work in and learn a business before starting a similar business. Learn about the suppliers, the customers, how to operate the business for some years and then go out and start a similar business. Examples: Wal-Mart, Home Depot, Chilis, Starbucks, EDS, Outback Steakhouse, and Intel.
2. ***Start your part-time business:*** Keep your day job and begin your business at nights and on the weekends and build it up before quitting your day job. Example: Ford Motor Company.

Do people "risk it all" and start businesses with little business experience and no customers? Yes. But these occurrences are rarer than you think. Many people lower the risk of starting a business because they begin a business with a customer or customers.

Let’s stop here. You should ask yourself these questions:

- What business do I know?
- What am I good at doing?
- What am I not good at doing?
- Do I know any potential customers?
- What do they really need/want?
- Can I give them what they need/want?

Remember the business rules:

Business Rule #1:
The Jerry McGuire Rule: Follow the Money—Cash is King.

Business Rule #2:
The Peter Drucker Rule: "The sole purpose of business is to serve customers."

Business Rule #3:
Customers know best what they need.

Chapter One: Lessons Learned

1. Businesses succeed only by meeting customer needs.
2. Businesses succeed because they make profits.
3. Business profit equals cash in from customer minus cash out for costs.
4. Successful entrepreneurs meet customers’ needs better, faster, or cheaper than someone else.
5. IQ, education, family background, race, religion, and ethnic origin are not predictive of entrepreneurial success.
6. Successful serial entrepreneurs are not big risk takers—they take small-measured risks.
7. Most successful entrepreneurs are not inventors or discoverers or geniuses.
8. Business is about people. You need people to buy your product, people to work hard for you, and people to finance your business.
9. Many successful entrepreneurs had previous work experience in the same types of business they started.
10. Many successful entrepreneurs developed their businesses part-time before quitting their paying jobs.

11. Entrepreneurs are *doers*.
12. Entrepreneurs test an idea—they do trials.
13. Entrepreneurs learn and iterate, tinker and get better.
14. Entrepreneurs listen to customers.
15. Entrepreneurs constantly get better and improve their products or services.

Chapter Two. Basic Rules of Business Success

Chapter Topics

- ***The 8 common start–up mistakes***
  1. ***Choosing a bad business opportunity***
  2. ***Choosing the wrong customers***
  3. ***Choosing the wrong products or services***
  4. ***Pricing products or services improperly***
  5. ***Not selling to enough customers fast enough***
  6. ***Not executing well***
  7. ***People problems***
  8. ***Mismanaging growth***
- ***Basic rules of business success***
- ***The 7 Ws***

The 8 Common Start–Up Mistakes

In the following sections, we discuss the 8 common mistakes start-up companies make and use them as a teaching tool to set forth the basic rules of business that successful entrepreneurs use.

Common Mistake #1: Choosing a Bad Business Opportunity

There is a BIG difference between a good *business idea* and a good *business opportunity.*

Ideas are as plentiful as sand on a beach. The entrepreneurial trash cans are full of good ideas—ones for products that work and that make sense. The problem is that customers did not need them badly enough to pay for them.

The difference between a business idea and a business opportunity is two–fold:

1. Good business opportunities satisfy existing customer needs.
2. Customers are willing to now pay for satisfying those needs.

Customers might consider an idea "nice–to–have" but do not see it as necessary.

The second big difference between a good idea and a good business opportunity is that a good idea may not "pencil"—that is, the economics might not work. By that we mean it is unlikely that enough product will sell at a profit large enough for you to earn a living. A good business opportunity pencils—you should be able to make a good profit.

Another reason your good idea may be a bad business opportunity is execution. It may be something hard for you to do or to produce for any number of reasons, or it may be outside your skill level. Or the product may be too complex to be made in bulk with consistent high quality by employees.

Your business idea may not be a good opportunity because you cannot find customers or because there is good competition that you cannot beat either because of cost or quality level issues. Good business opportunities are ones that meet customer "must–haves." There is a specific customer need or "pain" that is met or reduced because of your product or service.

We meet many hopeful entrepreneurs who tell us they have created a new product or they have developed something that is completely new.

Unlikely.

Trust us, in the year 2008, there are very, very few things that you can think of that someone somewhere has not already thought of and tried. That is okay. Uniqueness is not necessary.

Business Rule #4

You are looking for a good business opportunity—not a good idea.

So what is a good business opportunity? A good business opportunity

1. Has many potential customers with real needs (a large market).
2. Has customers who you can find (customer access).
3. Has customers who have money to buy your product (qualified prospects).
4. Allows you to make and sell your product at a profit (good profit margin).
5. Can result in enough sales to enough customers fast enough (conversion rate).
6. Allows you to earn your needed income level.
7. Is something you are qualified to do.
8. Requires that you do something that someone else is not doing well enough (beatable competition).

Another way to describe a good business opportunity is

- A large potential market, with…
- …Customer access with…
- …Many qualified prospects, with…
- …The potential for a good profit margin, with…
- …The potential for fast enough customer adoption; so…
- …You can earn enough money by…
- …Doing something that you are qualified to do by…
- …Beating the competition.

In Chapter 3, "What Is a Good Business Opportunity?" we will use an approach that is adapted from the brilliant work Discovery Driven Planning did in 1995 by Professors Ian MacMillan of Wharton Business School and Rita McGrath of Columbia University Business School. We can use it to evaluate business ideas and test whether a given idea is a good business opportunity.

Success in the business world is measured by positive cash flow. Positive cash flow results from customers paying you enough for your product that you can cover all your costs plus make a large enough profit that you can make a living.

Common Mistake #2: Choosing the Wrong Customers

To be successful in starting a business, you have to have a match; that is, you have to align the right customers with the right products or services, which then results in the customers' needs being met—which is a large part of the foundation of a successful business. Mistakes can occur by trying to force a "fit" between who you might see as a customer and your product as you produce it. Customers know what they need, and not all potential customers will be real customers. You have to find those customers. *Customer segmentation,* which is discussed in subsequent chapters, is a good tool to use in choosing which customers to go after. *Qualified prospects* will be your goal—those high-priority prospects who have the specific needs you can fulfill and the money to pay you for meeting their needs.

Mismatches occur when you try to sell a potential customer something he or she truly does not need resulting in you having chosen the wrong customer.

Common Mistake #3: The Wrong Product

What is the right product? The right product is that product which gives the customer what he or she needs, no more, at a price they can afford and which allows you to make a fair profit.

Delivery channels will be the means through which you reach and get the most attention from the largest number of qualified potential customers. It could be a retail store, the newspaper, the Internet, a wholesaler, or radio advertising. You will also learn on what basis to make your sales pitch: your Product *Differentiation Story*. How will your product or service be better? Will you compete on price, features, reliability, service, or quality?

Creating a sales pitch as to how your product is different and better requires you to understand your competitors' products. This book shows you how to use a competitor product analysis template, looking at the features, performance, cost, reliability, desirability, style, quality, ease of service, ease of repair, and ease of use of your competitors' product(s).

You will also learn how to choose your "battlefield"—the basis on which you can beat your competition. This entails deciding what your differentiators will be.

Selling the right product is giving the customer enough of what he or she needs but not too much, cost–wise. Customers are willing to pay for what they need—not for what they do not need.

Many entrepreneurs fail the product test because

- They love their product more than they love the customer.
- They want to make the world's best product with all the bells and whistles.
- The customer either does not need or is not willing to pay for all the bells or whistles.

Common Mistake #4: Pricing Products or Services Improperly

- How much will someone pay for your product?
- What price do you need to charge to make a profit?
- How do you determine your costs before you start the business?
- How do customers view pricing?
- What are the two best ways to set your price as a start-up?

Pricing is simple: If you get it wrong, two things can happen, and they both are bad. First, no one will buy your product, or second, you make sales but lose money because your costs exceed your price.

There are three key parts involved in determining your price:

1. Figuring out your product cost—fully loaded. Remember:

Price - Cost = Positive Cash Flow

2. Knowing what your competitor’s price is and knowing your potential customers’ buying choices.
3. Value–pricing, which is truly understanding what your potential customer is willing to pay for.

In reading about Common Mistake #4, you will learn when your price has to be lower than the competition’s, when it is okay to be on par or the same as your competitor, and when you can charge a higher price than your competition.

Common Mistake #5: Not Selling to Enough Customers Fast Enough

Chapter 7, "How Can You Overcome Customer Inertia?" deals with the customer buying process, overcoming customer inertia, and the velocity (speed) of purchase and volume (number) of purchases you need to make to be successful.

We are going to make a bold statement, a true one, but for you probably a shocking one:

Business Rule #5
Every entrepreneur over–estimates the number of customers that will buy and the speed at which they will buy.

Why? Because entrepreneurs love their products, and they think everyone will love them as much as they do.

Wrong.

Customer inertia is strong, and people do not like to change their behavior, including their buying habits. Why should your customer change? Why should he or she do something new like buy from you? Chapter 7 discusses how you overcome customer inertia and how you create a sense of urgency to buy.

The second issue we discuss in both Chapters 2 and 7 is the concept of Customer Conversion Rates. You need to accept the fact that all customer prospects will *not* buy your product. How many prospects must you have to convince just *one* of them to buy?

Number of Buyers ÷ Number of Prospects = Customer Conversion Rate

The next variable is how long of a time is the buyer decision process? How long will it take for your prospective buyer to make his decision?

10 minutes?

1 day?

1 week?

1 month?

3 months?

6 months?

1 year?

Wow—big differences.

You will learn that the time to make a sale depends on the magnitude of the price and whether your product has a short lifespan or will last for years. Selling someone a bagel that will last a day is very different from selling someone a car, which will last years. This also impacts the number of customers you will need to be successful—and it impacts the length of time it will take to make a sale.

All of this will teach you a big difference between a high–volume business and low–volume business, which impacts the number of sales you need to make. And you will also learn the difference between low–profit products and high–profit products.

Simply put, you have to sell a lot of low–price, low–margin products to succeed.

Remember: *You will overestimate you number of buyers, AND you will underestimate the length of the buying time.* This combination means that you will not earn as much money as fast as you think.

Common Mistake #6: Not Executing Well

Great—you have customers. Now you have to deliver a quality product on time, every time, defect–free at a profit.

You have to *execute* and *operate* a business, and you probably have never done so.

Chapter 8, "How to Manage Your Business," teaches you some basic management principles—how to understand your *value chain*; how to create *processes*; how to *prioritize* daily tasks and *manage by objectives*; and how to *manage by exceptions* or variances. You will also learn about the *power of simplicity*, the rule of 3s, and the rule of 7s.

Do not be overwhelmed. Most businesses are not rocket science. Running a business is a lot like baking a cake—you need the right ingredients. You need to do steps in the right order. You have to use measured amounts—and you do it the same way every time.

Running a business is "sweating the details" and loving the everyday challenge. But businesses are also composed of people, and people make mistakes. It's is the job of a manager to make good stuff, limit the bad stuff, and fix the mistakes.

Common Mistake #7: People Problems

Business is about *people*. You do business with people: customers, and you do your business in most cases through people: your employees. Your success depends on how your employees treat customers and how your employees do their jobs.

Without good employees doing good work, you will fail—pure and simple.

In Chapter 9, "How Do You Find and Keep Good Employees?" we focus on how to hire, train, and retain good employees and the best practices on how to manage people based on the work done by researchers at the University of Michigan, Harvard, Stanford, Case Western, and at Gallup.

Business Rule #6

Happy employees create happy customers, which creates profits for you!

And who creates happy employees? You! As the owner, manager, or boss, *you* create happy employees by the way you treat them.

Do you treat your employees fairly, with respect, give them a sense of doing something important and meaningful, praise them, teach them, help them accomplish their dreams while they help you accomplish yours?

We discuss two fundamental management rules in the People Problems topic:

1. Employees will do what you measure.
2. They will do it even better if you reward what you measure.

Our goal in Chapters 8 and 9 is to teach you how to create a *high performance business*—how to create an environment that promotes high performance. This will help direct your focus on the "why" of your business—so employees can find meaning and pride in being on your team.

And last, we introduce the concept of creating a "family" at work. The second part of the chapter will focus on you—your people skills and how you need to manage not only your employees but also yourself.

Common Mistake #8: Mismanaging Growth

Congratulations—you have customers. Congratulations—you have more customers than you expected.

Success creates challenges. How do you manage your growth so that you do not implode? Success is good. But too much success too fast can overcome the best new business. By overcoming, we mean that big mistakes happen. Common big mistakes are

- Poor quality products
- Missing customer delivery times
- Poor financial controls
- Employee theft
- Employee defection to a competitor
- Employee illegality or misrepresentations
- Hiring too many new employees too fast
- Improper training of employees due to time pressure
- Promoting people before they are ready for the next job

How do you simultaneously, on a daily basis, service existing customers; produce more products and services on a high quality basis for new customers; hire, train, and motivate new employees; all the while managing cash flow? How do you expand when there is a limit to what you can personally do? Do you need to put into place processes, quality controls, financial controls, and technology? How and in what order? Do you need to make investments in computers, people, and software? And yes, we discuss the unthinkable: Are you the right person to manage the business as it grows?

Basic Rules of Business Success

Let us review some of the key business rules that are the foundation of building a successful business.

Business Rule #1:
The Jerry McGuire Rule: Follow the Money—Cash is King.

Business Rule #2:
The Peter Drucker Rule: "The sole purpose of business is to serve customers."

Business Rule #3:
Customers know best what they need.

Business Rule #4:
You are looking for a good business opportunity—*not* a good idea.

Business Rule #5:
Every entrepreneur overestimates the number of customers that will buy and the speed at which they will buy.

Business Rule #6:
Happy employees create happy customers, which creates profits for you!

Business Rule #7: The 7 Ws
A good business opportunity should answer the 7 Ws.

1. **W**hat can I sell?
2. To **W**hom can I sell?
3. **W**hy will customers buy from me?
4. At **W**hat price?
5. **W**hat are my costs?
6. **W**hen will customers buy?
7. **W**hat will the competition do?

Chapter Two: Lessons Learned

Businesses generally fail for 8 fundamental reasons:

1. People choose a bad business opportunity.
2. People try to sell to the wrong customers.
3. People try to sell the wrong products or services.
4. People price their products improperly.
5. People overestimate the number and the speed at which people will buy.
6. People cannot manage the business so as to consistently produce high quality products on time at a profit.
7. Employee problems.
8. People cannot scale their businesses to accommodate customer demand.

Let’s move on to Chapter 3, and learn some techniques to evaluate business ideas.

Chapter Three. What Is a Good Business Opportunity?

Chapter Topics

This chapter uses two examples, a sandwich shop and a children's clothing store, to explore the majority of the following topics:

- ***Net profit margin and customer conversion rates***
- ***Does your business idea "pencil" (make economic sense)?***
- ***Determining pricing***
- ***Analyzing and learning from your competition***
- ***High margin business versus low margin business***
- ***Estimating your costs and nailing down the details***
- ***Burn rate and breaking even***

This is a chapter you will be able to use over and over until you find the *right* business for *you*. We are going to explore a way of thinking—a template to be used in evaluating business ideas. This method of thinking requires you to understand and keep in mind two key business concepts:

1. **Net Profit Margin**
   Net profit margin is the profit from the sale of a product divided by the sales price of the product. That percentage is a short-hand measure of profitability. Your profit from the *sale of a product* is your sales price minus all the costs to make, sell, and deliver the product.
   If your net profit margin is 20% and you sell a product for $10, then at the end of the day you should make $2.00 profit per sale. However, if your net profit margin is only 5%, then you would only make $.50 profit per sale. This being said, you would have to sell a lot more products with a 5% net profit margin than with a 20% profit margin to earn a $1000 per week profit.
   How many products would you have to sell for $10 with a 20% net profit margin to earn $1000 per week? The answer is 500. But what would be the answer if your net profit margin were 5% instead of 20%?
   That answer is 2,000 products—a *big* difference.
2. **Customer Conversion Ratio**
   Customer conversion ratio is the percentage of customer prospects who

actually buy your product. The goal is to make sales pitches to enough prospects so that you make the required number of sales. Prospects become customers when they buy.

Taking our example in the first point, with a product price of $10 and a net profit margin of %5, you needed to make 2000 sales per week to generate $1000 weekly profit. Well, if your customer conversion ratio is 10%, that means you would have to make 20,000 sales pitches a week—*wow.*

So conversion ratios help you determine the number of sales pitches you need to make and thus the number of sales people you will need—and the number of customer prospects you need weekly and daily.

The higher the conversion ratio, the lower the number of sales pitches you will need to make. As you will learn later, the best way to increase your customer conversion ratio is to focus on high probability prospects—that is, learn how to determine a prospect's likelihood of becoming a real buyer.

Number of Buying Customers ÷ Number of Attempted Sales = Customer Conversion Ratio

Pencil It

We want to stress the importance of "penciling" your business. Do some preliminary research, and put it all down on paper to the best of your knowledge. Use the tools provided in this chapter. Understanding net profit margin, customer conversion rates, costs, and customer traffic will help you do a back-of-the-envelope mathematical analysis. Think about the following:

- Do you have the expertise or knowledge to produce the product?
- How will you make the product?
- What equipment will you need?
- How can you get customers quickly?
- How will prospects know you are in business?
- Who is your competition, and how will they respond?
- Why will your product sell, and what is your value proposition?
- Will your product be cheaper?
- Will your product be better?
- Will your product be different?
- And so on…

If your business idea pencils, it is worth seriously exploring. You can then do more research and homework, and you’re on your way. If your business idea does *not* pencil, find another idea.

Ok, let’s explore an example: Let’s assume you want to open a sandwich shop that sells sandwiches for lunch, and let’s call your new business "The Best Sandwich Shop." What questions do you need to answer to figure out whether this business idea is a good business opportunity?

1. How much money do you need to earn weekly for you and your family?
2. What will be the average sales price for your sandwiches?
3. What will be your fully loaded costs to operate your business?
4. What will be your per sandwich net profit margin?
5. How much profit will that produce per sandwich?
6. How many sandwiches do you need to sell everyday to make a living?
7. How often will customers come into your shop and buy?
8. How many total different customers will you need each week to make your livelihood?

For purposes of this example, we are assuming that

- You know how to make a good sandwich.
- You can get good sandwich meats, produce, and breads.
- You can find a good and affordable location for your shop.
- You can get the necessary state and local food establishment licenses to operate.

Example 1: The Best Sandwich Shop

The first question you have to ask is: "How much money do you need to earn before income taxes on an annual basis?"

$10,000?

$20,000?

$30,000?

$40,000?

$50,000?

$100,000?

What is your goal? What is the minimum you need? What would be *nice* to earn?

Let's assume (only as an example) that your answer is $40,000 per year before taxes or $800 per week *net profit*, assuming two weeks of vacation and holidays. Ok, how do you make $800 net profit per week?

You sell sandwiches.

How many sandwiches do you need to sell each week? The answer to that question depends on the answers to the following questions:

1. What will be the average sales price for your sandwiches?
2. What will it cost you to make a sandwich, including all your costs for rent, heat, lights, water, insurance, labor, and so on. (This is your total cost to open and run your business weekly divided by the number of sandwich sales per week.)
3. What is your average profit per sandwich: your average sales price minus your average costs per sandwich?
4. Divide $800 by that average profit number. For example, if your average net profit per sandwich is $1.00, you need to sell 800 sandwiches per week or 160 per day.

Now comes the researching and digging for information part. How do you find out what your average sales price per sandwich should be? How do you estimate your operating costs?

What Is the Average Price You Can Sell Your Sandwiches For?

First, think about the kind of sandwiches you want to sell. How many different kinds can there be? Where do people buy those sandwiches now? At what prices do those places sell their sandwiches?

Do your research. Do a survey; visit the competition. Visit sandwich places that have been in business longer than a year. Why? Because if they have lasted for a year or more, they are likely to be profitable. And that means their prices for sandwiches exceed their costs. Good information for you. See if they will give you a copy of their menu or at least their take-out menu. What prices are they asking? Do this for several good sandwich places.

Okay, this is a good start. You have learned two key pieces of information: The competition seems to be making a profit at a certain price point, and it is unlikely you can charge more than they are charging unless you are doing something very different from them.

Let's assume that after all this thinking and research, you determine that you can sell good sandwiches at an average price of $5 per sandwich. So if you need to earn $800 each week, and your sandwiches sell on average for $5 each, how many sandwiches do you need to sell each week?

160?

No!

What common mistake did you make? You forgot the difference between sales price and profit. If you guessed 160 sandwiches, that only meant you would have received $800 dollars from customers. Out of that $800, you have to pay all your operating costs. How much of the $5 sales price will be profit? What will it cost you to make a sandwich ("all-in costs")? All-in costs means your cost of food, employee costs, rent, heat, lights, wrapping paper, paper plates, salt, pepper, cleaning supplies, bathroom supplies, employee taxes, insurance, licenses, and so on.

So, what amount do you *really* need? What will be your profit margin?

Competitors

Competitors are a fact of life. You will have them.

This research should start you thinking about how you can attract customers. For example, if you visit your potential competition, why will their customers change and buy from you? Better quality? Better price? Better location? Will you give customers free potato chips or a free drink? Will your shop be more fun to visit?

Learn from competitors. Visit many, many sandwich shops. Write down what you like about each. Sam Walton built Wal-Mart by visiting competitors and copying good ideas. Take the best ideas from your competitors and make a "better sandwich shop."

But do not forget that your competition will respond. You are attacking their livelihood in building your own, and they will protect their turf either by lowering their prices or improving their product or both. This introduces the concept of sustainable advantage. What, if anything, can you do that will help you keep your customers long-term?

Wow, there are so many things to think about. At this point, there are a couple of shortcuts to finding the answers you need. The first way is public information—looking at sandwich companies that have sold stock to the public such as McDonald's, Burger King, and so on.

Comparables

In most cases, there are big companies (like McDonald's, Burger King, Subway, Quinzos, and Chick-Fil-A) who are already in the sandwich business. Some of them are *public* companies. Public companies must disclose their profit margins.

Using the Internet you can look up those companies and find their websites. Go to McDonald's website and look under Company Information. Then click Investor Relations or Investor Information. Then click on Financials or SEC filings. Under SEC filings, you will link to annual reports, which will contain the company financial statements.

Companies disclose their operating margins—gross and net. You will want to look at *net profit margins*. Look at two or three companies and use the average net profit margin. Understand this is just a guideline and that your profit margin will be different. It may be higher because you will be a smaller business (especially in the sandwich shop business), and you should have fewer costs.

Internet Research

Another research tool is to go on the Internet and search sandwich shops and sandwich shop profits. Almost every type of business has a trade association or cooperative that provides a newsletter. These are a great source of information. Today with the Internet, information is out there if you just look hard enough in enough different places. Be a good detective.

Speak with Other Entrepreneurs

Another way to do research is to go visit some sandwich shops in locations that will not be competitors of yours and speak with the owners. Tell them about your dream and ask for their help. Someone will say, "How can I help you?" Then, you should learn about their operating costs and ask them to share with you the big mistakes they made in starting their businesses. In addition, ask their advice about suppliers, how they advertised, how they were successful.

Entrepreneurs generally want to help other entrepreneurs—especially if they are not future competitors.

Back to the Math

Let's assume for our example that the net profit per sandwich is 18% (or 90¢) a sandwich. That is, you can estimate making 90¢ profit on every sandwich you sell. *How many sandwiches must you sell each day to make $800 per week?*

> Profit per week = $800
>
> Profit per sandwich = $.90
>
> Number of sandwiches needed to sell each week = 800/$.90 = 888
>
> Number of sandwiches needed to sell every day on average = **178** (888/5 days per week = 178) Is this realistic?

Is this likely?

Let's factor in some more considerations:

1. Yes, there are eight hours in a workday, but lunchtime is not eight hours long. You have a finite timeframe in which to sell 178 sandwiches.
2. Workers only have one hour max to drive, park, come in, order, eat, and go back to work. The location of your shop is critical. Parking is critical. How you design your shop to move people through quickly is critical.

This raises even more questions for you:

- What time will your lunch business begin?
- What time will your lunch business end?
- How many sandwiches can you make per hour? Or will you pre-make them?
- How many times a week will your customers buy from you?
- How many *different* customers will you need a week?
- How far will customers drive for a good sandwich?
- Do enough people work within a reasonable drive time?

Now think how different your answers would be if the business is a low margin business—say, 5% (see Table 3.1).

Table 3.1. *Number of Sandwiches Per Day*

At a 20% profit margin, you have to sell 160 sandwiches a day. At a 5% profit margin you have to sell 640 a day—*A BIG DIFFERENCE.*

Net Profit Margin	# Sandwiches Per Day
5%	640
10%	320
15%	213
20%	160

Now, if a customer comes in twice a week, every week, you will need at least the ratio shown in Table 3.2.

Table 3.2. *Number of Different Customers Per Week*

Net Profit Margin	# Different Customers Per Week
5%	1600
10%	800
15%	533
20%	400

You should now understand why net profit margins are so important. They determine your volume—*the number of customers you need* to be successful. Your conclusion: You will need *533* different customers if the average customer comes in twice a week.

Remember, you will not attract or get all the lunch business in your area. So how many potential lunch customers need to exist? 2000? 4000? 5000? Again, this raises the issue of location. Opening a shop near your apartment in a residential neighborhood is very different than opening a shop in a high employment location. Remember Willy Sutton—when asked why he robbed banks he said, "Because that is where the money is." Where are your customers? Go where your potential customers are.

The problem with that easy answer is what? You guessed it. Landlords know this. Your rent will be higher in a location near large numbers of workers. So your costs will be higher. This is the *trade-off*. Will the increased rent, though, be offset by more sales, and will the increased rent make it more likely you will succeed? Will the increased rent lower your profit margin from 15% to 12%, or will it lower it from 15% to 5%? That allows you to figure out the impact on the number of sales.

Now let's review. We have gone through a process of figuring out average sales price; figuring out our estimated net profit margin; and figuring out the estimated number of sales we need to make a day, and we have looked at how many repeat customers we may have, which helps us understand the number of potential or prospective customers we may need.

This is the *pencil process*, a method of analysis that gives us a snapshot picture of how much volume we need to do. And we have learned that net profit margin has big consequences in that it dictates the number of customers we need each day.

Let’s look at another example—a children’s clothing store.

Example 2: Children’s Clothing Shop

Now instead of a sandwich shop, assume you want to open a shop that sells children’s clothes. (Ed’s parents’ first entrepreneurial venture was a children’s clothing store.) Assume the average sale is $10.00 per customer with a 15% net profit margin. And let’s assume you still want to take home $800 a week before taxes. So how many sales per week do you have to make?

$10 x 15%	= 1.50	Net profit per sale
$800/$1.50	= 534	Sales per week
Average sales per day/6 days	89	

Table 3.3. *Sales Needed Per Day*

Let’s now learn about customer conversion ratio.

Customer Conversion Ratio

So you need to make 89 sales per day. Will everyone who comes into your store buy? Of course not. Lots of people will be looking, learning, planning ahead, shopping prices, exploring, or just wasting time. Some people call these non-buying people "tire kickers." So what percentage of people who come into your store will make a purchase on any given day?

Table 3.4. *Results of Different Customer Conversion Ratios*

What % of Prospects Will Buy?	# Sales Per Day	Per Day # Total People Needed	Per Week # Total People Needed
10%	89	890	5340
20%	89	445	2670
50%	89	178	1068

Wow, what a difference! Customer conversion rates have a dramatic impact on determining the likelihood you can achieve your goal of $800 net profit per week.

Customer conversion rates will help you understand the *customer traffic* you need—the number (volume) of potential prospects you need daily to sell the amount you need.

Customer traffic will depend on your location and how easy it is for you to let people know you are in business. The goal of a business location and advertising is to increase customer traffic. The more customer traffic, the more likely you will make sales, assuming your traffic consists of potential buyers. Let's review.

The lower the profit margin, the larger the number of paying customers you will need.

Business Rule #8

Low Profit Margin = High Volume

High Profit Margin = Lower Volume

Customer Conversion Rates

Customer conversion rates will tell you how many total prospects you will need to make a sale.

10% conversion = 10 prospects for 1 sale

20% conversion = 5 prospects for 1 sale How often your customers need to buy your product will give you an estimate of how big your customer base needs to be. Will your customers buy from you weekly, monthly, or only on special occasions?

So in a low profit margin business, you need a lot of customers buying from you. Low customer conversion rates indicate you need numerous customer prospects to come into your business—customer traffic. If customers will need your product or service infrequently, this requires even more customer traffic.

Business Rule #9

Profits are your goal—sooner rather than later.

Business Rule #10

Cash flow is your business's lifeblood—it is how you pay your bills.

Two Different Types of Businesses

1. Low Profit Margin
   Or

   Infrequent Buys ⟶ You need lots of customers.
   Or
   Low Customer Conversion Rate
2. High Profit Margin
   Or

   Frequent Customer Purchases ⟶ You need a smaller number of customers.
   Or
   High Customer Conversion Rate

The tools you learned in this chapter allow you to discover the number of potential customers and the number of sales you need every day, which gives you a basis from which to make a judgment as to whether an idea is a good opportunity.

Generally, your net profit margin or allowable profit margin range is limited or determined by the type of business you are in. Most businesses selling similar products will make similar or close to the same margins. What does this mean? Your choice of business— the type of business it is—will greatly influence how much money you can or will make.

Because public companies (companies whose stock is sold publicly) have to disclose their numbers, it is possible to compute average net profit margins by type of business (see Table 3.5).

Table 3.5. *Margins by Sector*

Industry Name	After-tax Operating Margin
Apparel	8.49%
Auto Parts	5.47%
Building Materials	9.45%
Computers/Peripherals	7.66%
E-Commerce	7.95%
Educational Services	10.67%
Electronics	5.05%
Environmental	13.15%
Food Processing	7.64%
Food Wholesalers	3.03%
Furniture/Home Furnishings	7.34%
Grocery	3.38%
Healthcare	12.14%
Heavy Construction	2.91%
Home Appliance	6.98%
Homebuilding	5.01%
Household Products	15.12%
Human Resources	3.33%
Information Services	15.49%
Machinery	9.62%
Medical Services	7.79%
Medical Supplies	8.98%
Metal Fabricating	10.41%
Office Equip/Supplies	7.06%
Packaging & Container	9.46%
Paper/Forest	11.12%
Pharmacy Services	1.64%
Restaurant	12.05%
Retail (Special Lines)	6.10%
Retail Automotive	4.69%
Retail Building	7.66%
Retail Store	4.71%
Shoe	8.70%
Toiletries/Cosmetics	8.76%
Wireless Networking	10.67%

Data Used: Value Line database, of 7364 firms
Date of Analysis: Data used is as of January 2008
Source: http://pages.Stern.nyu.edu/~adamodar/New_Home_Page/datafile/margin.html

So what good are these numbers? They may help you choose a business. For over 7000 big businesses in 2005, the average after-tax operating margin was 11.98%. Assuming a 30% average tax rate, the average pre-tax profit margin was around 17%.

Now, your immediate reaction might be that this is simple—choose a higher margin business…

NO! NO! NO!

You should choose the best margin business in which you would have the highest probability of succeeding at. That means: *A business you can do because of expertise, experience, knowledge, and which you would enjoy doing and A business for which you have or can get customers.*

You have to be able to produce and deliver high-quality products or services on time, defect-free, and for a profit. And because this business will consume most of your waking hours, you should enjoy doing it.

Estimating Your Costs

Business Rule #11

Control your costs—spend wisely on the right stuff.

The next step in thinking in more detail about your business idea is drilling down to estimate your total costs to make, sell, and deliver your product or service.

What happens if you overestimate cash coming in and underestimate your costs?

YOU CAN LOSE MONEY!

And you will have to make up that difference (loss) from your savings, a home equity loan, family loans, or selling property.

THIS IS SERIOUS!

That is why we stress: Please, please, do your homework. There is a wealth of information out there, and there's so much available right at your fingertips on the Internet.

What Does Net Profit Margin Tell You About Costs?

> 100% – Net profit margin = Your projected costs percentage It gives you the answer! For example, if you are in a 10% net profit margin business, your projected costs are 90% of your *sales price* (assuming you sell enough stuff). So your total cost estimates should add up to 90% of your average sales price.

Example:

1. Sales Price = $10 per transaction
   Net Profit Margin = 10%
   Your Profit = $1
   Your Costs = $9
   All of your costs added up should approximate $9 per sale, assuming you sell enough to cover all of your costs.
2. Sales Price = $15 per transaction
   Net Profit Margin = 20%
   Your Profit = $3
   Your Costs = $12
   All of your costs added up should approximate $12, assuming you sell enough to cover all of your costs.

You need to do research and talk to other business people and accountants and create an estimated weekly cost chart (see Table 3.6).

Table 3.6. *Sample Cost Chart*

Expense	Per Monthly Cost	Expense	Per Monthly Cost
Accounting		Inventory	
Advertising		Legal	
Business Supplies		Licenses	
Cost of Supplies		Lights	
Cost to Deliver		Marketing	
Employee Costs		Phone	
Equipment		Rent	
Furniture		Repairs & Maintenance	
Heat		Taxes	
Insurance		Water	

Why Do You Need to Know Your Costs?

There are two main reasons:

1. You will not usually make sales the first day you are in business because there is a *start-up time*—a time in which you are paying expenses without receiving cash from customers.
2. It will take you time to reach *break-even*—that month when your cash in

from customers equals your costs for the month.

Business Rule #12

Know your burn rate—how soon will you run out of money?

Knowing your costs allows you to plan for your *burn rate*—how fast will you burn through the money you have available from yourself and family and friends to start your business.

To emphasize the importance of choosing a good business opportunity before you start your business, remember these basic business rules: **Business Rule #8:**
Low Profit Margin = High Volume
High Profit Margin = Lower Volume

Business Rule #9:
Profits are your goal—sooner rather than later.

Business Rule #10:
Cash flow is your business's lifeblood—it is how you pay your bills.

Business Rule #11:
Control your costs—spend wisely on the right stuff.

Business Rule #12:
Know your burn rate—how soon will you run out of money?

7 Ws

The 7 Ws are a good shortcut way to think about business opportunities. Use them as a tool to evaluate whether a business idea is worth exploring seriously:

- **W**hat can I sell?
- To **W**hom can I sell?
- **W**hy will customers buy from me?
- At **W**hat price?
- **W**hat are my costs?
- **W**hen will customers buy?
- **W**hat will the competition do?

Chapter Three: Lessons Learned

1. Business ideas are like sand at the beach—plentiful, but there are few new or unique business ideas.
2. Not every business *idea* will make a good business *opportunity*.
3. Your idea needs to "pencil"—that is, make economic sense.
4. The key "pencil" drivers are:
    - The amount of money you need to make
    - Net profit margin
    - Customer conversion rate
    - Customer traffic volume
    - Speed of sales
    - Customer buying frequency
    - Burn rate and staying power—how much time (money) can you invest until you make a profit?
5. Remember the 7 Ws:
    - **W**hat can I sell?
    - To **W**hom can I sell?
    - **W**hy will customers buy from me?
    - At **W**hat price?
    - **W**hat are my costs?
    - **W**hen will customers buy?
    - **W**hat will the competition do?
6. Common mistakes business starters make:
    - Overestimating the number of customer sales
    - Overestimating how fast people will buy
    - Underestimating their costs
    - Underestimating the competition
7. Owning a low margin business means:
    - You need a lot of customers.
    - Customers need to buy frequently.
    - You will have to operate very efficiently.

- Your room for financial mistakes or errors will be small.
- Volume of customer traffic, customer conversion rates, and knowing the competition is very important.

8. Owning a higher margin business generally means:
    - You need fewer customers.
    - Your customers probably will not be frequent buyers.
    - You will need to consistently generate new customer prospects.
    - Customer conversion rates could be low.
    - You need a constant flow of good customer prospects.
9. Your estimated weekly costs help you predict your *burn rate*: the speed at which you will burn through your money. Burn rate tells you how long you can stay in business until you hit break-even.
10. *Break-even* is the point at which your weekly incoming cash equals your costs going out.

Chapter Four. How Do You Choose the Right Customers?

Chapter Topics

- ***Who are your right customers?***
- ***Why do customers buy?***
- ***How do you find high-probability prospects?***
- ***Doing a market survey***
- ***Who is your competition?***
- ***How do you do a competitor analysis?***

This chapter, as well as Chapter 5, "How Do You Design Your Product or Service?" will help you answer the 3 Ws:

- ***What will I sell?***
- ***Who will buy?***
- ***Why will they buy?***

The Right Customers

You already know that customers are the lifeblood of every business. And you have learned that most businesses overestimate the speed of finding customers and the number of people who will buy their products or services.

So who are customers? Customers are high-probability prospects who actually buy your product.

Business Rule #13

Customers are high-probability prospects who actually buy your product.

Who Is a Prospect?

A prospect is anyone who has a need or a want that is motivating him or her to consider buying a product or service. Customers buy to meet needs or to solve a problem—or they buy to satisfy their wants or desires.

You'll remember from our sandwich shop example in Chapter 3, "What Is a Good Business Opportunity?" a prospect will buy a sandwich because he or she is hungry (need) or because they are thinking about the joy of eating that sandwich (want or desire).

All entrepreneurs have restraints such as limited time, money, and people. Because of these restraints, you have to be careful in how you spend your time and money. You need to spend your time and money finding and selling to high-probability prospects who can become your customers.

Business Rule #14

Focus on high-probability prospects—*not* just anyone willing to listen.

Who Are High-Probability Prospects?

As we stated, customers buy to solve needs or satisfy desires. Customers' needs come from problems, and the importance of any problem is measured by the amount of "pain" associated with it. The greater the pain, the more likely the customer will buy something to relieve the pain.

High-probability prospects have serious needs or desires.

Needs or desires can be categorized by intensity or degree: top priority, high priority, or medium priority:

- **Top Priority—**Those prospects with needs and desires that are top priority have the following traits:
  - Timing of purchase is critical—the sooner the better.
  - Price is not as important of a factor.
    An example of a top priority would be if you are bleeding so badly that you could die if you do not get immediate attention. In that case, you are not likely to take the time to shop hospitals for the best price or for even the best doctors. You need help now!
- **High Priority—**Prospects who have a high priority for specific solutions to a problem or desire are likely to make their purchase decisions in the near future. In most cases, a decision to purchase a solution has been made; the only thing left is to decide which solution to chose. High-priority prospects are likely buyers.
- **Medium Priority—**Prospects who have medium priority needs and wants

tend to be price-sensitive and are slow to make a purchase decision.

The greater the need or desire, the more likely you will be able to convert a prospect into a customer. The lower the need or want, the less likely you can convert the prospect into a customer. Therefore, you want to find and focus on high-probability prospects: those with top priority or high priority needs or desires.

Business Rule #15 It is easier to convert top and high-priority prospects to customers than other prospects.

How Do You Find High-Probability Prospects?

The answer is simple: Ask people what they need and want.

The best way to get the information you need is through research. There are two ways to do research. The first way is called primary research, and the second is secondary research.

Primary research is research where you or the people you hire talk *directly* with potential customers. Primary research is asking people questions to learn about their needs or wants and is a great tool—talk to people and learn what they like, dislike, and so on.

Examples of primary research are

- **Market surveys** are surveys that can be performed in person, on the phone, or by mail. They usually include 15 questions or less and provide more accurate information when a large number of people are questioned. Surveys are good tools for determining who are the best prospects for your product or service and how many of these prospects are in your area.
- **Focus groups** are small groups of people who you get together and who are asked specific questions about their needs, wants, and your product.

Secondary research is defined as getting the information you need from sources that have done their own research and either offer it to you for a fee or for free (for example, census information from the government). Consequently, you're getting the answers *indirectly* from the market. The negatives of getting secondary information from the market are that the questions asked may not be the best questions nor asked of the best people. The benefits of secondary information are its lower cost, and you usually can get the information faster. *Because secondary information is either free or low cost and already exists, you should start here.*

Where can you find good secondary research?

The two best avenues of secondary research are to search the Internet for information and to find a trade association that represents either sellers of the product you want to sell or buyers of that product.

Business Rule #16

Learn about your industry. Search the Internet and find a relevant trade association.

What are trade associations? *Trade associations* are organizations made up of members—people like you—who are in the same type of business you want to start or people who sell the same product you want to sell.

There are over 20,000 trade associations in the United States. To see if there is an association for you, usually all you have to do is go to the Internet and do a quick search. The overwhelming majority of these associations have their own websites so you can review what they have to offer. To get the research and business information you may find helpful, you might have to join the association, which in most cases is a minimal cost.

So first do your research on the Internet. Find a relevant trade association and then consider doing your primary research.

Primary Research—Doing a Market Survey

There are two ways to do a survey: Do it yourself or hire a market research firm to do it. Whether you do your own survey or you pay a company to do it for you, you will need to determine the questions you want to ask.

Creating Market Survey Questions

What are the best practices for creating your own market survey? First, you need to focus on the goals of your survey. The most common purposes of market surveys are

1. Identifying high priority market needs and wants
2. Determining your target prospects
3. Designing your product or service
4. Identifying the best communication channels to use for marketing

After you define your goals, you should draft questions you think would be valuable to know about your prospects. Do not forget that you will need to include a couple of demographic questions to help you identify the best prospect base.

For example, if your customers are businesses, you might ask their industry, sales volume, number of employees, and so on, and if they are consumers, you might ask questions related to age, income, marital status, and so on.

When developing your questions, try to word them so the customer can answer them with a yes or no or so that the responder can rank the answers on a scale of 1 to 5.

You can use a scale such as

1 = very unimportant

2 = unimportant

3 = neither important or unimportant

4 = important

5 = very important

Prioritize the questions you think are the most valuable or that you consider must-haves. Delete any question that you can find the answer to from another source such as through secondary research sources. Make sure that no two questions are really asking the same thing.

Last, since most people are, at most, willing to spend no more than four minutes answering your questions, we recommend that you do not ask more than 15 questions. After you have developed your survey, test it on a number of people you know to see how long it takes to answer. If it takes more than four minutes, you will need to shorten it.

To help you design your survey questions, we have developed the following example.

Example Survey Questions

Let’s assume you’re thinking about opening a car repair shop. Because there is a lot of competition in the market for repairing cars including car dealers or specialty repair shops like transmissions or brake shops, you want to make sure that there is enough potential customer interest to warrant opening your shop.

In addition to determining if there is enough demand in the market to open your shop, you want to know what types of repairs car owners are most looking for, where the best location would be for your business, and what the best way would be to market to your prospects.

Here are some examples of the type of questions you might want to consider:

Need/Want Questions

- Which of the following choices most closely represents how often you have to bring your car in for repair*:*
  Never ____
  Rarely ____
  About once every 6 months _____
  Once every 3 months ____
  Almost once a month or more _____
- When you have a problem with you car, do you usually go to the same place to have it repaired?
  Yes ___
  No ____
- Where would that be? ____________________________________
- On a scale of 1-5 (with 1 being very unsatisfied to 5 being very satisfied), please answer the following questions:
  - How satisfied are you with your present car repair places? ____
  - How satisfied are you with their prices? _____
- How interested would you be in finding another place that can do all your repairs at a reasonable price?

  Not interested _____
  Somewhat interested _____

Very interested _____

- What kind of car problems do you experience most?
  ____

Demographic Questions

- How many cars do you own?
  0 ____
  1 ____
  2 ____
  3 or more _____
- What kind of car(s) are they, and how old are they?
  1 _______________________ Age: ________
  2 _______________________ Age: ________
  3 _______________________ Age: ________
  4 _______________________ Age: ________
- What is your marital status?
  Single ____
  Divorced ____
  Married ____
- Who at your house is responsible for making the decision where to get the car repaired?
  You _____
  Spouse/Significant Other _____
  Whoever has the problem _____
- What is your zip code? _____________
- Which of the following categories most closely represents your annual household income?
  Less than $25,000 _____
  $25,000-$50,000 _____
  $50,000-$75,000 _____
  Over $75,000 _____

Product Questions

- Would you be likely to try a new repair place for your car if:
  - They guaranteed the lowest price:
    Yes _____
    No _____

Don’t Know ______

- They guaranteed their work for one year:
  Yes ______
  No ______
  Don’t Know ______
- If you could win a free trip to Disney World for a week:
  Yes ______
  No ______
  Don’t Know ______
- Someone you trusted recommended it:
  Yes ______
  No ______
  Don’t Know ______
- If they gave you a rental car if your car repair will take over 3 hours to fix:
  Yes ______
  No ______
  Don’t Know ______

Marketing/Advertising Questions

- On a scale of 1-5 (with 1 = never; 3 = sometimes; and 5 = always), how likely are you to read the following:

  Major Area Newspaper ______
  Community Newspaper ______
  Direct Mail ______
  Unsolicited Email ______

Tracking Survey Answers

Before you start asking people your survey questions, you will need a way to track the answers. We recommend that you use an Internet survey tool. There are many you can choose from online (the following are for example only): www.surveymonkey.com, www.zoomerang.com, or www.zapsurvey.com.

These tools are invaluable whether you are planning on doing your survey online, by phone, or in person. They are relatively inexpensive to use, normally less than $100. When you sign up, just follow the directions they give to enter your questions.

Now that you have determined the questions you're going to ask and you have selected a survey tool to record the answers, the next thing you have to do is to determine the following:

1. The number of surveys you will need to complete
2. How many people you will have to contact to make sure you get the number of survey answers you need
3. Where you are going to find the people or get the names of people to contact
4. The most effective way to implement your survey

Let's review each of these items:

1. **How many surveys do you need to complete?**
   Obviously, the larger the sample you use, the more likely your results will be reliable. That said, we recommend as a rule of thumb, that you take the question from your survey that has the most answer choices (taking the questions from the example we just presented, 5 was the largest number of answer options of any question) and multiply that by 20. Given the questions we presented, you would need to receive at least 100 competed surveys (see equation below):

   (5 [largest number of answer alternatives] x 20) = 100

   This should provide you with a large enough sample to generate a reasonable level of accuracy. In no case should you have less than 40 completed surveys.
2. **How many people will you have to contact to get the number of completed surveys you require?**
   On average you can assume that only a small percentage of the people you contact will be willing to answer your questions. The actual number depends on how you contact them. If it's in person, on average you will need to talk to 10 to 20 people for everyone that's willing to answer. If the contact is made by phone, you will need to plan on calling—on average—40 to 60 people for every completed survey. If the contact is made by mail or email, you should plan on 100 to 300 per completed survey.
3. **Where do you find the people or get the names of people to contact?**

The key is to find the right people to ask. The people you are interested in are people who are likely to be prospects. For example, if you're looking to sell car repair services like the example given, you only want to talk to people who own cars. The best way to find the right people to answer your survey is to buy a list of either phone numbers, mailing addresses, or email addresses (if available) of people or businesses that meet your criteria.

You can purchase a list relatively inexpensively from list companies online (usually around $0.05 to $0.10 per name). The following three are examples of list companies: www.turbo.marketing.info/index.html, www.w3data.com, and www.engmarketingsolutions.com.

In buying a mailing list, make sure you give the company you are buying your list from as much information as you can about the people or businesses you're trying to contact. Doing so will ensure that you get the best list available.

4. **What's the most effective way to implement your survey?**

   Your choice of how to best implement your survey will depend on a number of factors. They include cost, time, size of list, and so on.

   The key to keeping the cost low and the timing short is to offer an incentive for people to complete your survey. Examples of incentives include entering their names into a contest where they can win something they would find valuable or paying them to complete the survey (usually five to ten dollars) or donating money to the charity of their choice in place of direct payment.

   For planning purposes, you should estimate the average cost per completed consumer survey to run from a low of $10 to over $50 depending on length of survey, target market, and respondent incentive offered. The average cost per business survey can run from a low of $25 to over $100 depending on the job level of person you want to talk, the effectiveness of your telemarketer or marketing piece, among other factors.

   If you choose to do a survey, try to avoid the months of July, August, November, and December as the response rates tend to be much lower during those months.

The Competition

What do you have to know about your competitors?

Competitors are those people selling products or services that are the same or similar to your offerings. Competitors want the same thing you want: customers.

You are in a race, a competition, with your competitors to get customers who usually only buy a product or service from one place.

Business Rule #17

If someone buys from one of your competitors, *you lose*, and the competitor wins.

Secondly, to compete and *beat* your competitors, you have to understand what your competitor is selling so you can offer a better product—one that meets customer needs *better*.

So how can you beat the competition?

- Offer the same product at a lower price
- Offer the customer more benefits for the same price
- Perform faster
- Provide higher quality
- Provide better reliability
- Give better service
- Make it easier for the customer to buy

You also need to specifically identify your competitors. Who is selling the same thing you want to sell? Here it gets tricky. You can define your competition broadly or narrowly. If you want to open a bowling alley, what are you selling? Bowling or entertainment? If you think you are only selling bowling, you will look at only bowling alleys as your competition. This is a narrow definition.

However, if you think you are selling entertainment, you will look more broadly at your customers' choices in your geography including miniature golf, games, arcades, movies, and so on.

Business Rule #18

When in doubt, always define your competition broadly, not narrowly.

To get the kind of information you need about your potential competitors, we recommend you do the following:

- **Search the Internet—**If your competitor is a public company, you can get detailed financial and marketing information by going to its website and downloading an annual report. In addition, whether it's a public company or not, you can search the website for product and company information, product pricing, marketing strategy, payment terms, and selection.
- **Shop your competitors—**To get a good understanding of the strengths and weaknesses of your competitors, try posing as one of their customers. If it makes sense and fits into your budget, buy their products or services so that you get in-depth information about them and see how they work and what's good or bad about them.
- **Ask your competitors for information—**Believe it or not, the best place to get good information about your competitors is from your competitors themselves. That's right, ask them. Start off by asking their salespeople. Their salespeople are trained to answer questions, and they are likely to provide you with the detailed information you request. At minimum, they usually will send you literature on their products and company. If the competitor has a customer service department, call them. They are usually a good place to find out about any new products or services that are likely to be introduced in the future.
- **Analyze the competition's strengths and weaknesses—**After you have gathered information on your competitors, it's time to *analyze it*. Your primary objectives in analyzing the information are to determine the strengths and weaknesses of their product or service offerings and to identify if and where they are not satisfying customers' needs and wants that you have identified.

Business Rule #19

Attack competitors' weaknesses.

The best way to analyze the information is to develop a competitive analysis, which is simple to build. First, make a list of the top and high priority customer needs and wants that you have identified from your primary and secondary market research. On a piece of paper, list those customer needs and wants in a column one below the other on the left side of the chart.

Second, on the top, list your major competitors by name horizontally one after the other (see Table 4.1).

Table 4.1. *Competitive Analysis*

Customer Needs/Wants	Competitors						
	A	B	C	D	E	F	G
List 1st Need/Want							
List 2nd Need/Want							
List 3rd Need/Want							

Third, starting with the first need/want on your list, look at each competitor separately and determine if that competitor presently offers any kind of solution for it. If they do not have a solution that addresses that need/want, put a "0″ in the box under that competitor's name.

If a competitor has a product or service that addresses that need/want, you will need to enter in that box a number on a scale from 1 to 5 (1 means the product does a very poor job solving that need/want, and 5 means that the product does an excellent job solving that need/want). After you have done this for each competitor, continue the same process for the second need/want until you have either entered a zero or a numerical answer in each box on the page.

Fourth, once you have completed filling in the all the boxes, it is easy to see which needs/wants are not being addressed effectively. To determine this, add up the numbers in the boxes from left to right for each need/want separately. If you do this correctly, you will have a total number for each need/want in your list.

See Table 4.2 for two of the numerical values of the needs/wants.

Table 4.2. *Competitive Analysis with Data*

Customer Needs/Wants	Competitors							
	A	B	C	D	E	F	G	Total
1st Need/Want	4	1	3	5	2	4	5	24
2nd Need/Want	1	3	3	2	4	2	3	18

The needs/wants with the *lowest* number are the needs/wants that are *not* being addressed well by your competitors—in Table 4.2, this would be the "2nd Need/Want."

If you make sure your product meets the same needs met by your competitors

***and** that your product meets the unmet need or want, you have a good chance of out-competing your competition*.

This competitor analysis is not a one-time event. Remember you are in a race with competitors for every customer, and there will only be one winner. If you win enough, your competitors will do something to respond to you so they can win. They may lower their prices; they may add or improve their offerings. So you need to reassess their offerings often enough to stay abreast of what your competitor is selling so you can stay competitive. Competitors *will* respond, and you will have to respond to their response and so on. That is the beauty of business. It is not a static game.

Business Rule #20

Competitors will respond. Business is like a baseball game—there is always another inning.

In this chapter, we have tried to help you understand why customers buy and have given you tools to find high-quality prospects and to understand your competition. Remember:

Business Rule #13:
Customers are high-probability prospects who actually buy your product.

Business Rule #14:
Focus on high-probability prospects—*not* just anyone willing to listen.

Business Rule #15:
It is easier to convert top-and high-priority prospects to customers than other prospects.

Business Rule #16:
Learn about your industry. Search the Internet and find a relevant trade association.

Business Rule #17:
If someone buys from one of your competitors, *you lose*, and the competitor wins.

Business Rule #18:
When in doubt, always define your competition broadly, not narrowly.

Business Rule #19:
Attack competitors' weaknesses.

Business Rule #20:
Competitors will respond. Business is like a baseball game—there is always another inning.

Chapter Four: Lessons Learned

1. Your company's likelihood for success is directly tied to identifying your prospects' most important needs and wants and then providing a solution that best meets their objectives.
2. Because not all prospects are equally as likely to buy your product or service, it's important that you determine which specific prospects are most interested in buying your product or service and what's different about them from the rest of the market.
   Prospects who are the most likely to buy your product or service are your target market.
3. The benefits of identifying targeted prospects include marketing and advertising savings, more enhanced product or service design, and increased sales.
4. Doing your homework is critical to your success.
5. Talk to people—learn firsthand people's needs/wants.
6. Constantly survey prospects, customers, and the competition.
7. Know your competitors' strengths and weaknesses so that you can take advantage of their limitations and better serve your targeted customers.
8. Your goal is to spend your time on high-probability prospects.
9. You have limited time and money. Do your research, focus, and be disciplined.

Chapter Five. How Do You Design Your Product or Service?

Chapter Topics

- ***Why should you design your product or service?***
- ***Give customers what they need—not what you think they need***
- ***What is the difference between product features and product benefits?***
- ***What does "value" mean to a customer?***
- ***The Value Proposition Ratio***
- ***A Value Proposition example***
- ***Your reason for being***
- ***Your competitive advantage***
- ***Low innovation***
- ***Product design chart***
- ***Prototyping your product—doing a test***

Give Customers Only What They Truly Need

Now that you have identified your most likely buyers and their needs or desires, the next step is to create, structure, or design your product or service offering to meet those needs or desires. You have choices in what to offer for sale.

Remember your goal is to offer customers solutions—to solve customer problems or meet customer needs. That is your *value proposition*—the "why" people will buy from you.

Business Rule #21

> Customers buy solutions, so you must constantly assess what customers really want or need and make sure you give them that—*not* what you think they need, nor more than they need because they will not want to pay for anything they do not need.

Features or Benefits

Products and services are composed of both features and benefits.

Features are the ingredients of a product. They can usually be added or subtracted from a product or service much like different spices can be added to a meal to vary its taste. Features are generally added to a product or service to *enhance it*—to make it better for the customer. *Features are options—not necessities*. Features are add-ons and can be differentiators.

Benefits, on the other hand, are the reason for the product or service to exist in the first place. Benefits are *necessities*. Benefits are your solution to the customer's problems or desires. And benefits solve a problem, reduce "pain," or satisfy a desire.

So you have to offer benefits; features are optional. What features should you offer, if any? In designing your offering, you have to be concerned about *value*.

What Is Value?

If benefits were the only thing that mattered to people, customers would naturally buy products and services that deliver the greatest amount of benefits over those that offer less. For example, the top-of-the line Mercedes (S Class) has a more attractive list of benefits to the vast majority of consumers than does the Honda Civic. Why then did the Honda Civic outsell Mercedes S Class in 2006 in the United States many times over?

The answer is simple; benefits by themselves are not the only variable in a customer's purchase decision. The other equally as important factor is *price*. The price customers are willing to pay acts as a counterbalance to value. Customers want the best value they can afford.

Business Rule #22

The goal is to deliver the most value to your customer at a price that is both affordable for your customer and profitable for you.

To help you measure your product or service's value, the following formula was developed. It is called the *Value Proposition Ratio* (see below):

Value = Benefits ÷ Cost

Because value is a function of both benefits and cost, they both have to be taken into account when measuring a product or service's value to customers.

The value proposition gives you an effective way to compare your product or service to those of your competitors. The larger the Value Proposition Ratio is, the greater the value.

Why is it necessary to compare products or services to one another? The reason is simple: You need to do this so you can determine how attractive your product or service is relative to your competitors'. The greater your perceived value, the more attractive your product or service will be and the more likely customers will buy it.

Business Rule #23

The key is the value perceived by the customer.

To be successful, your product or service has to be the most attractive alternative to a large enough number of customers so that you can make a profit. Because this concept can be a little confusing, we have developed the following example to show you how to use the Value Proposition Ratio to increase the attractiveness of a product or service.

Example: Enhancing Your Product/Service Value

For this example, we're going to assume that a new company (we will call it NewCo) is going to build brick homes in the $250,000 price range. NewCo will be building its homes in the same subdivision as two other well-known and highly respected builders in the market, who are also going to sell their brick homes for $250,000.

All three companies are building 2,000 square foot houses with similar floor plans that include 3 bedrooms and 2 bathrooms. NewCo and its two competitors have all allocated an identical $50,000 per house for amenities, and all three builders have a 10% profit margin built into their house pricing.

If NewCo does not do anything differently, it is less likely to sell homes than either of its competitors because NewCo has no reputation in the market, while its competitors are proven and well respected—which customers value. NewCo's challenge raises these questions:

- What could NewCo do to make its product more attractive to buyers than its two competitors?
- How can NewCo design its offering to provide more value without increasing the cost to the customer?
- How can NewCo give customers more of what they want at the same price as the competition and still make a fair profit?

NewCo has three primary options for increasing its product's value to make it more competitive. It can

1. Lower its price.
2. Increase the money it spends on amenities, which will reduce its profit.
3. Offer a more attractive set of amenities than its competitors for the same $50,000 cost.

If NewCo chooses to either lower its price or increase its costs, its profit will decline. If it has to increase its costs or lower its price by more than 10% to be competitive, the company will not be able to make a profit or stay in business. So alternatives (1) and (2) are not viable.

Therefore NewCo's best alternative is to identify a more attractive set of amenities that the company can deliver at the same cost to the customer. That is the essence of product design. Offer more of what the customer truly needs or wants at the same costs and get rid of features or amenities that customers do not perceive as high value-add.

How can NewCo do this?

It has to ask its customers, "What do you really want or need, and what do you value the most?" NewCo (and you) have to do your homework—do your research and get customers to focus on what they truly want and need. NewCo did this by utilizing a combination of focus groups and a market survey. They used the focus groups to help them develop the best questions for their survey, and they used the survey to get an accurate picture of what amenities customers really wanted.

The two most important set of questions in the NewCo survey were

1. How much were customers willing to pay for each of eighteen different amenity options? The amenities they presented included but were not limited to: wood floors, stainless steel appliances, granite countertops, and stone fireplaces.

2. How much were people willing to pay extra for a house if it was built by Competitor A, Competitor B, or NewCo? They asked this question to measure the value of the competitors' reputations and track records versus NewCo being a new company with an unproven track record.

With the results obtained from the survey, it calculated the value people attributed to each of seven different amenity package offerings. Two of these packages represented what their competitors were offering in their houses, and five were new amenity package options NewCo had created using input from their focus groups.

Table 5.1 shows the results of the research. Keep in mind each amenity package actually costs the same—$50,000. The numbers that follow represent the perceived value in the minds of potential buyers.

Amenity Packages	Perceived Value by Customers	Cost
Package 1 (New Amenity Package 1)	$52,222	$50,000
Package 2 (New Amenity Package 2)	$65,556	$50,000
Package 3 (New Amenity Package 3)	$87,778	$50,000
Package 4 (New Amenity Package 4)	$46,678	$50,000
Package 5 (New Amenity Package 5)	$81,111	$50,000
Package 6 (Competitor A)	$58,889	$50,000
Package 7 (Competitor B)	$62,778	$50,000

Table 5.1. *Perceived Value*

Notice the differences in perceived value by the potential customers. Keep in mind all the amenity offerings cost the same $50,000 to build or install. But they have very different perceived values: from a low perceived value of $46,678 to the high of $87,778.

BINGO. You have solved the value proposition.

Because Amenity Package 3 delivers the most perceived value ($87,778), and it costs the same $50,000 to build, NewCo chose it to include in its houses. To determine if this was going to be enough to make its houses the most attractive in its market, it used the Value Proposition Ratio to calculate the relative value of all three builders' homes and then compared them (see Table 5.2).

Benefits	Competitor A	Competitor B	Competitor C
2,000 Square Feet	$208,500	$208,500	$208,500
Perceived Value of Amenities	$58,889	$62,778	$87,778
Perceived Value of Reputation	$3,850*	$2,050*	$168*
Total Benefits	$271,239	$273,328	$296,446
Customer Cost	$250,000	$250,000	$250,000
Value Proposition Ratio	**1.085**	**1.093**	**1.186**

* Determined using NewCo market survey.

Table 5.2. *Comparison of Value Proposition Ratios*

Remember in evaluating the Value Proposition Ratio, the largest number wins. The NewCo home should win because it will deliver more perceived value ($296,446 for the $250,000 purchase price) than the competition delivers.

NewCo in this example was able to offer a better product at the same cost as the competition.

However, there is nothing to stop either of NewCo's competitors from either copying NewCo's amenity package in the future or even doing more detailed research to develop their own more attractive amenity packages. NewCo's lead over its competitors, therefore, is not one they will likely be able to defend long-term and as a result, is likely to be short-lived. To survive and thrive in the future, they will have to find another reason for customers to choose them over their competitors.

To win in the marketplace, you have to constantly improve your service or product offering to stay ahead of the competition.

Business Rule #24

Avoid the Winner's Curse: Do not think you will continue winning forever. Do not become complacent or overconfident.

How do you stay ahead of the competition and avoid the Winner's Curse?

What is the reason your company should exist in the market in the first place? What is it that you can do better than your competitors? If you cannot find a way to do something better than your competitors do it—bringing something to the table that your customers will value long-term—you will likely fail.

Your "Reason for Being"

Your business must have a purpose for existing in customers' minds. This "reason for being" is your *differentiato*r. It is what makes you valuable to the customer and how you differ from your competition.

To help you determine your company's reason for being, we have listed some of the more common reasons for being that companies use to be successful:

- Offering the lowest prices in the market
- Making the product/service the easiest to use
- Providing the best guarantee in the market
- Delivering the best service
- Offering the most attractive financing options
- Providing the largest selection of products/services
- Offering the longest business hours in the market
- Offering to deliver when competitors do not
- Offering the highest quality
- Being the most reliable—doing what you say

So in thinking about your product offering, not only should you focus on the *benefits* you will offer to customers, you also need to think about how you will offer them—with what services or guarantees or with what delivery options that will make you different from the competition.

What will be your reason for being? What will your name or brand mean or stand for? Will you stand for quality, reliability, being the lowest cost alternative, being the fastest, being the easiest to deal with, being the best? WHAT WILL YOUR BUSINESS STAND FOR?

Good businesses design or create a total offering that they execute 99% of the time on time and defect-free. They focus on doing what they are good at, and they execute better than the competition.

Business Rule #25

This is the competitive advantage you are seeking: to offer more value at an affordable price and do it defect-free, on time, and with good service every time.

The goal is to create that image of who you are in your customer's mind through your product or service offering and how you do business.

Here are some examples of some well-known companies and their competitive designs:

- **Wal-Mart's** competitive advantage is its lower prices and large selection. It has a competitive advantage because it is the largest buyer of products in the world, and it does everything it can to keep its prices the lowest in the industry. As such, Wal-Mart can sell its products for lower than anyone else and still make a good profit.
- **Pfizer Pharmaceutical Company's** competitive advantage is its exclusive rights to certain medicines and its ability to get physicians to prescribe it. It is able to sell a medicine like Celebrex at a substantial margin because of the patents it has. Legally, this constrains its competitors from competing directly against it. In addition, Pfizer has thousands of pharmaceutical representatives who market Celebrex to physicians every day.
- **Google's** competitive advantages are its top-of-the-mind name recognition and its proprietary Internet search capabilities. In addition, Google's highly attractive and high-priced stock enables it to quickly and easily purchase add-on businesses that leverage its position in the market and its long-term profitability. Given all these strengths it would be extremely difficult for a competitor to beat it.

Now, just because we showed some of the most successful companies in the world, do not assume that only large companies can have competitive advantages. After all, competitive advantages are the reason why small companies get big.

Low Innovation

There is one more very important point that we need to make before you start designing your company's products or services, and that is the following:

A new or small business is much more likely to be successful if it takes a *proven product in the market and makes small changes to it that customers say they want. This product design process is called*low innovation.

Many great businesses have been built taking things competitors do plus putting them together in a new offering. Learn from your competitors and your customers. You can even design a business by taking good ideas from several competitors. Improvements are easier to do than creating wholly new products for which there is no proven market demand.

In contrast, new or small businesses that offer high innovation products or services that are totally new and unique to their market are much more likely to fail. The key to making the right changes to products/services in the market are

- To first make sure your customer will truly value the changes you are considering
- To be certain that the changes you make are affordable for the customer AND allow you to make a fair profit.

Table 5.3 shows examples of three well-known products and successful product enhancements that have been made to these popular products along with examples of enhancements that could still be made.

Table 5.3. *Product Enhancements*

Product	Enhancements Already Made	Possible New Enhancements
Soft Drinks	Caffeine Free	Vitamin Enhanced
	Extra Caffeine	Dessert Drinks
	No Calories	You Heat It Up
Sofa/Couches	Turns into a Bed	Expands to Increase Seating
	Stain Guard	Push-of-a-Button Pattern Changes
	Same Day Delivery	Built-in Seat Warmers
Televisions	Surround Sound	Smell-A-Vision
	Digital	Channels Change Using Voice Command
	Hangs on Wall	Waterproof—Can Be Watched in the Shower

It's Now Time to Build Your Product/Service

Now that you know the basics for building a product or service, it's time for you to design yours. To help you with this process, we have developed the following Product/Service Design Chart (see Table 5.4).

Table 5.4. *Product/Service Design Chart*

Product or Service Name	Customer Needs/Wants	Reasons for Being	Your Product Benefits	Your Product Features
Your Product or Service				

To increase your likelihood for building a successful product or service, it's necessary to complete the following product design steps in the following order:

1. First, list the highest priority customer needs and/or wants that you have identified from your market research and from your experience in the market in the Customer Needs/Wants column.
2. Second, list all the reasons why your business should exist in the market relative to the needs and wants you just listed and relative to what your competitors are presently offering in the Reason for Being column. What will your business stand for or represent?
3. Next, in the Product Benefits column list all the major benefits your product or service is going to offer that satisfy customers' needs and wants.
4. Finally, list all the features that you will include in your product or service offering in the Product Features column.

Can You Build or Produce It?

Now that you know what the design of your product/service will look like, it's time to turn your attention to how your company is going to build it. To help you do this, we have developed the following set of questions for you to consider prior to building your product/service:

1. Can you build it?
    - What expertise do you need that you do not have?
    - If you need outside assistance, do you know where to get it?
2. How much will it cost, and how long will it take you to build?
3. Is it better to build it yourself or to buy it from someone else who can do it better?
    - If you're going to buy it from someone else, who?
    - How much will they charge?

- What kind of capacity do they have?

After you have answered these questions to your satisfaction, you are ready to build your company’s "first" version of your product or service. Why a "first" version? The next section answers this question.

The Prototype—The Test

The reason for a "first version" is so you can test your product/service in the market with actual customers to make sure you have exactly what they want. If you do not test your product/service before you start spending money on marketing and selling it, you are likely to waste valuable time and money by offering a less attractive product or services than what the market really wants.

The process of testing a new product or service is called a *prototype* or *beta test*.

What Is a Prototype and How Does It Work?

A prototype is a company’s first real-world trial of its product(s) or service(s) by a set of customers who have agreed to use the product/service to identify issues and make recommendations.

While it will delay your market introduction somewhat, it is well worth it. Once completed, your final product will be more marketable, and you will be less likely to waste valuable time and money trying to sell a product/service that does not exactly meet the market needs.

The benefits of a prototype include learning and getting feedback from customers, which can lead to:

- Product improvements
- Customer references

Other Tips

While there have been whole books written on product design, we are only able to allocate one chapter to this subject. As such, we have developed the following list of other tips that you should consider when building your product or service:

Business Rule #26

Don’t fall in love with your product or service. Be willing to listen to negative feedback and change.

- When you fall in love with your product or service, you lose perspective. You find reasons and/or excuses not to listen to your customers' feedback.

Business Rule #27

Rarely is it the product or service that is the reason for success in a new business. In reality, it is the execution of the business that is the primary driver of a new venture's success.

- Get your product or service out into your market as soon as possible. It is better to come out with a product or service that does not have all of its benefits in place and get market feedback than it is to wait to make your product or service perfect.
    - The longer it takes you to get your product/service to the market, the less likely you will be successful.
    - After you get your product or service into the market, you will start getting valuable feedback.
    - Feedback can be used if needed to modify your product or service to better meet the customers' needs and wants.
    - The longer you take to get your product or service out into the market, the more money you will have spent, and the less you will have available if you should need to change it relative to market response.
    - Rarely do the overwhelming majority of products or services come out perfect when they are first introduced.

Business Rule #28

Get good customer references as soon as you can. Use them to sell to other customers.

- New and small companies rarely have the dollars to spend on advertising required to build a brand.
- A brand effectively gives a company a seal of approval and, consequently, an advantage over nonbranded or unknown companies

in selling their products.

- Quality customer references reduce the risk of buying from an unknown company. Therefore, they are the first step in building a company's brand without having to spend millions in marketing in the process.

This chapter is chock full of good rules to remember about how to design your product or service to create the best differentiating value proposition for your customers. What you want to do is offer more value than your competition or the same value at a lower price. Remember:

Business Rule #21:
Customers buy solutions, so you must constantly assess what customers really want or need and make sure you give them that—*not* what you think they need, nor more than they need because they will not want to pay for anything they do not need.

Business Rule #22:
The goal is to deliver the most value to your customer at a price that is both affordable for your customer and profitable for you.

Business Rule #23:
The key is the value perceived by the customer.

Business Rule #24:
Avoid the Winner's Curse: Do not think you will continue winning forever. Do not become complacent or overconfident.

Business Rule #25:
This is the competitive advantage you are seeking: to offer more value at an affordable price and do it defect-free, on time, and with good service every time.

Business Rule #26:
Don't fall in love with your product or service. Be willing to listen to negative feedback and change.

Business Rule #27:
Rarely is it the product or service that is the reason for success in a new

business. In reality, it is the execution of the business that is the primary driver of a new venture's success.

Business Rule #28:
Get good customer references as soon as you can. Use them to sell to other customers.

3 Ws

The 3 Ws are a shorthand strategy. They keep you focused on what really is important and, hopefully, you will stay focused on the essence of business: meeting customer needs. Remember:

- **W**hat will I sell?
- **W**ho will buy?
- **W**hy will they buy?

Chapter Five: Lessons Learned

1. Customers buy solutions, so you must constantly assess what customers really want or need and make sure you give them that—*not* what you think they need nor more than they need because they will not want to pay for anything they do not need.
2. The goal is to deliver the most value to your customer at a cost that is both affordable for your customer and profitable for you.
3. Avoid the Winner's Curse—overconfidence and complacency.
4. The competitive advantage you are seeking is to offer more value at an affordable price and do it defect-free, on time, and with good service every time.
5. Don't fall in love with your product or service—that is the job of your customers.
6. Go to market as fast as possible—learn from your customers.
7. Get customer references as soon as you can—they will help you make more sales.
8. Product benefits are necessities. Product features are options.
9. The Value Proposition Ratio is Value = Benefits ÷ Costs.
10. Value is what the customer perceives it to be—not what you think it is.
11. Your "reason for being" is your essence, your differentiator, and what your business stands for in the minds of customers.

12. Low innovation product design is less risky than a developing a totally new product.
13. Remember you have to be able to build or produce your product reliably and 99% defect-free, on time, and at a profit.
14. Develop a prototype and get in the market quickly and learn from your customers. Test and learn, and adapt and improve. Constant improvement is key.

Chapter Six. What Is the Right Price for Your Product or Service?

Chapter Topics

- ***Why is price important?***
- ***Profit = Sales Price – Costs***
- ***Variable costs and fixed costs***
- ***Cost plus pricing or competitive pricing***
- ***Break-even: How do you cover your costs?***
- ***The use of payment terms, discounts, guarantees, and sales***

The price you pick for your product and/or service is one of the most important factors in building a successful business. The price you pick impacts

- Whether customers will buy your product
- The positioning of your product against your competition
- Your business's profitability

First things first: When setting your product/service's price, there are certain rules you have to understand. The most important one is that you need to have a good idea of what your costs are before you can even begin considering setting your price. If you do not know your estimated costs, you will not be able to determine a price that should produce a profit. Remember:

> Profit = Sales Price - Costs

How do you determine your costs? There are two types of costs, variable and fixed. All costs are either variable or fixed in all businesses. *Variable costs* are those costs that vary in amount depending on how much you sell or produce. Variable costs depend on your volume. In the case of our sandwich shop from Chapter 3, "What Is a Good Business Opportunity?" variable costs include food supplies, paper plates, napkins, trash bags, and so on, which will vary with the volume of sandwiches made. *Fixed costs*, on the other hand, are costs that are fixed and do not fluctuate regardless of how much product/service you sell. Examples of fixed costs are rent, management fixed salaries, marketing, salespeople base salaries, phone, and so on.

To estimate your costs, you need to first add up all your fixed costs. These are costs that are not going to change for at least one year no matter how much you sell. The following is a list of the most common fixed costs a new business may have (remember your business might not have all of them, or you could have others specific to your business):

- Monthly rent
- Monthly fixed salaries and employee benefits and taxes
- Monthly phone/cable/DSL costs
- Average monthly business property and casualty insurances
- Monthly lease amounts for furniture, equipment, and/or autos

After you have determined how much your fixed costs are per month, you need to turn your attention to your variable costs. As we just discussed, variable costs fluctuate with your sales volume and tend to change as frequently as monthly. The following is a list of common variable costs in a business. Variable costs tend to differ widely by type of business, and as such these are only examples:

- Product costs
    - Cost of goods you purchased and resold that month or the direct cost of making the product you sold
- Utility costs
- Sales commissions
- Bonuses
- Travel and entertainment costs
- Office supplies
- Miscellaneous expenses that vary monthly

Your monthly costs equal your monthly fixed costs plus your monthly variable costs.

So, now how do you determine your sales price? Basically, for a new start-up, there are two basic ways: cost plus pricing or competition pricing.

Cost plus pricing is one of the two most common pricing strategies used today by new businesses. It is done by first determining what it really costs your company to produce or make your product/service. This is known as your *fully loaded cost*.

To calculate fully loaded cost for your product/service, you add the variable costs you paid for the product/service plus a proportional fixed overhead cost. To determine a proportional fixed overhead cost per product/service, you add up all your fixed costs for the year and divide it by the number of products/services you hope to sell that year. If, for example, your total fixed cost for the year is $180,000 and you're planning on selling 3,000 products, your proportional fixed overhead cost per product would be $60 ($180,000/3,000 = $60).

Then you need to add that $60 to your variable costs, the costs associated with making the product: materials, purchased components, wrapping, shipping, delivery, installation, and so on. After you have determined that fully loaded cost, you add to it a profit margin. If, for example, you want to make $45,000 in profit for the year, you would add $15 for your profit ($45,000/3,000 = $15).

Assuming your variable cost per product is $40, your total product price would be

Variable Cost:	$ 40
Proportional Fixed Cost:	$ 60
Profit Margin:	$ 15
Total Product/Service Price:	$115

You are rightfully asking, "How do I estimate my costs when I do not know how much I am going to sell?" Therefore, how do I set my price?

Well, you make your best guess and as you get experience you learn and reset your price as needed. Or you get your customer to agree to pay a price equal to your actual cost plus a negotiated profit. This is hard to do in a retail environment but easier to do in a service environment. As an example, Ed just had some bookcases built in his house. His carpenter wanted to do it on a cost plus basis. Ed paid for the cost of the materials—lumber, finish, hooks, and so on, and the carpenter charged $35 an hour as his profit.

If you adopt the cost plus pricing method, the first thing the customer will want is an estimate of the final price, and then in some cases he or she will ask you to guarantee that price. That is, if you underestimate your costs, you are responsible for the cost overrun. Both are fair requests, and they put the responsibility upon you to know your costs and your business.

Our experience is that this is very hard to get right in the beginning. Most people make their best estimate and learn as they go from their first sales. Then with better information, they are able to set better prices because they then have real information on costs.

Competitive Pricing

The other most common pricing strategy used by new and small businesses is competitive pricing. Without a doubt, this is the easiest pricing strategy to use. Competitive pricing means you determine your price based on what your competitors charge.

To do this, first you have to identify your most likely competitors. Then you need to find out what they charge for their products/services that are the most like yours. You need to compare your product/service as honestly as possible to theirs. If your product is better—includes more features or better materials or delivers more benefits, you may be able to charge more. But when your product is less competitive, you probably will want to charge less than what that competitor is charging.

The theory behind competition pricing is that if the competitor is still in business, he or she must be making a profit at the prices he or she is charging, and so should you.

Break-even Formula

The break-even formula is an extremely valuable tool. With it you will be able to determine how much you will have to sell to cover all your costs (no profit), given the price you plan on charging. After you have calculated the number of units you need to sell to break even, you need to determine if you reasonably think you can sell at least that amount. If you're not comfortable that you can sell at least that much, you have three choices:

1. You can raise your price. This will lower the total number of units you will need to sell. However, a note of caution: Increasing price may negatively impact the attractiveness of your product/service to your customers and reduce your ability to make sales.
2. You will need to lower your fixed costs. The more fixed costs you can cut out of the business, the fewer units you will need to sell. Be careful here; you should only cut costs that won't negatively impact your business.
3. Find another business opportunity.

To determine how much you need to sell to break even, you need to know

- Your fixed costs per year
- The price you're planning on charging for your product/service

- The variable costs for your product/service

Number of Products Required to Be Sold to Break Even

Assumptions:

- Your company's fixed costs are $200,000 per year.
- The price you are planning to charge is $128.50 per product.
- Your variable cost per product is $23.50.

$128.50 (price) – $23.50 (variable cost) = $200,000 ÷ $105.00

= 1,905 units

In this example, your company would need to sell 1,905 units just to break even per year given the price you're charging. That is a gut check for you.

Additional Pricing Factors

One of the most important keys to an effective pricing strategy and business success is making it as easy as possible for your customers to purchase your product or service. To that end, there are a number of other pricing-related factors that you can use to influence customers purchasing besides just price.

The answer to choosing the right factor(s) to use for your business is in understanding what really drives your customers' purchase decisions. The following are just some examples of what drives different customer purchasing decisions:

- Because many customers use financing these days instead of purchasing products/services for cash, there is a segment of customers that are more concerned about how much their monthly payment is going to be than the actual price of the product/service. We call this segment *Monthly Payment Customers*.
- There are other potential customers who do not have the money now in their budget to purchase the product/service. They are more concerned about the timing of when they have to pay than they are with the price. We call this segment *Timing of Payment Customers*.
- There is also a different customer segment in the market who are more concerned about minimizing the risks associated with purchasing a new product/service than they are with price. We call this segment *Risk-Adverse*

Customers.

After you have identified what's important to your customers in making their purchase decisions, you're ready to start developing your pricing strategy. The following are some real-world examples of companies that have developed pricing strategies to meet their specific customer requirements. These specific pricing strategies are credited with helping maximize each of the following companies' sales and profitability:

Monthly Payment Amount Driven:

- Below market or no interest rate financing
  - Automobile companies
  - Furniture stores
  - Appliance stores

Pricing Tied to Actual Usage (companies offering price discounts for high-volume users):

- AT&T volume discounts.
- Comcast gives discounts to customers who use more than two of their available services.

Timing or Payment Driven:

- First payments delayed six months or more
  - Rooms To Go
  - New office/apartment leases with long-term contracts

Risk-Adverse Driven:

- Free trial periods
  - Salesforce.com
  - Norton.com
- Fixed fee pricing (get all you use for one set monthly fee):
  - Metro PCS—cellular phone company
  - Vonage
  - Gas Utility Companies—SCANA Energy
- Money-back guarantees
  - Mail order diet products/specialty vitamins

- Infomercials
- Software—PeopleSoft

Now before you start thinking about different payment option alternatives, you need to remember Business Rule #1:

Business Rule #1

The Jerry McGuire Rule: Follow the Money—Cash is King.

When considering offering extended payment options, do not forget that you still have fixed and variable costs to pay. **If you do not pay them, you will not be able to stay in business long.** The only way you may be able to take advantage of one or more of these payment options is to identify a company that would be willing to finance your customers' deferred payments, assuming your customers have good credit. There are companies that will pay you upfront and offer financing to your customers, but it will cost you money. Whether this makes sense or not depends on the incremental sales you're able to make. In other words, if you use these techniques to generate sales, your profit will be less. To earn what you need to earn, you will need to sell more. Therefore, these techniques only work if they will help you sell more products.

Chapter Six: Lessons Learned

1. Price impacts your volume of sales and your profit.
2. Profit = Sales Price – Costs
3. There are two types of costs: fixed and variable.
4. Variable costs vary with your volume of product sold.
5. Review your costs monthly.
6. Price also determines your break-even volume—the amount you need to sell to earn enough profit to cover your costs.
7. Cost plus pricing and competitive pricing are two good pricing strategies.
8. You may have to offer guarantees or payment terms to certain customers.
9. Remember—to you, cash is king.

Chapter Seven. How Can You Overcome Customer Inertia?

Chapter Topics

- ***Customer inertia—the fear of change***
- ***Selling is overcoming the obstacles to a sale***
- ***Nine common reasons people do not buy***
- ***Seven techniques to get a customer to try your product***
- ***The key to selling is listening***
- ***The psychology of selling***
- ***The customer-buying timeline***
- ***Selling is like fishing***
- ***Reward customer referrals and loyalty***

By now you have learned that when starting a business you need paying customers fast—to cover your costs. You only have so much money to invest in your business, and you have to pay your fixed costs whether you make sales or not.

So you need customers *yesterday*. But you will learn that most customers do not have the same urgency to act as you do.

Most likely, a sale of your product requires people to change because it is unlikely that you will be selling something that no one else sells. Change is hard for most people; change takes time, and people have to get comfortable. People have to work through their hesitance and fear of change. But you do not have a great deal of time—you have expenses every day. So how do you get people to change and buy your product or service *quickly*?

You have to create a sense of urgency.

Yes, people are hesitant to change and are scared that change may be bad for them. This is your challenge to overcome.

Business Rule #29

Selling is overcoming obstacles to a sale.

Obstacles to a Sale

Making a sale is a process of overcoming obstacles. People generally will not tell you they are afraid to change—no one admits that to strangers. No, they will give you reasons or excuses why they will not buy. These are the *obstacles* or hurdles that you have to overcome to make a sale. What do you have to do to overcome these obstacles?

- First you have to ask your customers questions about what their problems, needs, or goals are. You have to understand their needs and understand why their current solutions are or are not working. Are they satisfied or not? If not, why? Poor quality? Unreliable delivery? Poor service? Invoice mistakes? Too expensive?
- You have to ask them what it would take for them to change. What does your product have to do?
- Then you have to shape your sales pitch into solving the customers' needs, stressing the benefit of your product—what it will allow your customers to do better, faster, or cheaper.
- Then you have to ask for feedback—ask questions to draw out the obstacles to sale.
- Then you have to drill down with questions to try to understand the *real* obstacles to sale.
- Then you have to overcome them by explaining how buying your product accomplishes customers' objectives, meets their needs, and is not a big risk to try.

The sales process should be an interactive *conversation* with the customer—not a speech by you, and it takes two key skills:

1. Listening
2. Being a good detective

Business Rule #30

You cannot listen when you are talking.

Business Rule #31

You will make few sales convincing buyers you are smarter than they are or that you know their businesses better than they do.

The Risks of Buying from You

To address and overcome the obstacles to sale, you need to understand them. The obstacles to sale are often one or more of the following:

- Your product is unproven—how do your customers know it will work?
- You do not have a pool of satisfied customers who can vouch for your product.
- Your business is small—you may not be in business in six months—then how can customers depend on you?
- You have few employees. How can a customer get quick service if he or she has a problem with your product?
- To change to your product means a customer has to change to other products as well—why should they?
- They are not that unhappy with their current vendors.
- You are too expensive.
- Their current vendors are relatives.
- Your product does not improve their situations that much.

You need answers to their concerns, and you have to answer them directly and honestly.

Over time, you will build a "tool box" of ways to sell. You will enjoy the challenge, and you will become comfortable with the fact that you will not be successful every time. You will understand that it takes different approaches with different prospects—that people make sales decisions at different paces—and that some people just are not ready to buy.

The key is to learn as quickly as possible what the obstacles to sale are for you.

When someone gives you reasons why they do not want to buy, be sure to get all the reasons out on the table before you really start selling. Do not let the prospect "faucet" you—do not let the prospect keep dripping obstacles after you solve some by asking them:

- "Are these *all* of your concerns?"
- "Before I address your concerns, are there any others?"

- "Do I understand that the key reasons you have concern are 1, 2, and 3?"

One sure way *not* to overcome the obstacles to sale is to minimize or dismiss customers' inertia or fear. No. You have to acknowledge it and convince them that buying from you is not as risky as they think. How do you do that?

1. **Try It—You Will Like It.** Let prospects sample the product for free. By sampling it and testing it, they do not have to decide to change until after they know, use, and see the benefits of the product.
2. **Give Away Free Samples.** Have you ever gone in a grocery store or a bakery and tasted a sample of a muffin, cookie, a cooked dish, some cheese, and so on? You were trying a free sample to see if you liked it. Did you ever buy that product? Yes—you did.
3. **Give Demonstrations.** Sometimes it helps to get the buyer and his or her boss together for lunch or after work and give a demonstration of your product—along with a free lunch or snack.
4. **Absolute Happiness Guarantee.** Sometime it takes the "absolute happiness" offer: "If at any time, for any reason you are unhappy, I will give you a 100% money-back guarantee (or even a 105% money-back guarantee)."
5. **Free Repairs/Service for Six Months.** To encourage people to buy, you can offer free repairs or free service for a time period.
6. **Deferred Payment Plans.** Make it easy for your first customers. If applicable, let them pay over time.
7. **References/Testimonials.** The main purpose of your first sales is not money—it is to get good references—testimonials that you can use to make other sales. Remember, no one wants to be the first buyer. The best advertising, the best way to make people comfortable, is to have happy, satisfied customers willing to recommend your business to others.

Business Rule #32

You need satisfied customers quickly. It is okay to reduce your price to get your first customers.

Business Rule #33

The hardest sale is the first sale. The second hardest sale is the second sale.

Making Sales Takes Practice

The key to making sales is getting the customer to talk, to tell you his or her needs and to voice concerns and objections. To know or be able to make an educated guess about the selling objections, you have to listen. The hardest thing for enthusiastic sales people to do is to **know when to shut up and listen**. Make the pitch, and if the prospective buyer does not respond, ask him or her questions:

1. Do you think my product will meet your needs?
2. Why not?
3. If not, what are *your* needs?

The Psychology of Sales

There are hundreds of books, courses, seminars, and DVDs on selling techniques. But selling is pretty simple:

- Not all prospects are buyers.
- People buy from nice people—people they can trust.
- It takes time—visits, calls, meetings, and so on to build trust.
- Trust is established by honesty, telling the truth about your product about what it can do and what it cannot do.
- Trust is established because you want to build relationships. The buyer represents more to you than just money.
- Trust is established by admitting mistakes when you make them, fixing them quickly, saying you are sorry, and making the customer happy.
- People want to do business with people they can rely on and who show up on time, do the job well, and are pleasant to be around. These types of relationships take time to build.
- *Never, never* bad-mouth the competition. Win on the merits of your own product or service.

The Customer Buying Timeline

Understanding the customer buying timeline is really about understanding a few things:

- What is the number of people who have to approve the sale?

- When and how often do they meet to make the decisions? Daily, weekly, monthly?
- How badly do they need your product?

Time Is Your Enemy—Your Money Is Burning

Remember that when starting out, you have time pressures. You need to make enough sales right away to stay in business.

Be smart.

Learn to qualify your sales prospects. You need to spend your time on those prospects that appear to be easier to sell. Remember your goal is *quick sales*—sales that will generate references, satisfied customers, and cash.

Selling Is Like Fishing

Every sale requires a hook—just like fishing. What do fly fishers do? Well, they study the facts: water flow, rocks, insects, and temperature and make a choice as to the right fly to throw in the water to catch a fish. They try a fly. If the fish does not bite after three or four passes, what do they do? Well, they try another fly and another fly until they get a strike.

In selling you need different "flies," too. Different flies for you are different reasons for a potential customer to buy your product. If the customer does not strike at your first pitch, change and make another one.

With experience, you will learn that there are two or three key common reasons why people will buy your product.

Keep listening and trying ideas until the prospect bites, and when he or she bites, set the hook. Focus on that point and close the sale by asking him or her to buy for that reason. When you have made the sale, **stop selling and start papering**.

Get the buyer’s signature, check, money, and get out of there fast before he changes his mind. Too many people keep talking after they have made the sale. Nothing better can happen. Stop talking, get the money, and leave.

Customer Referral Programs and Customer Loyalty Programs

If you are selling products or services that allow you to do this, select happy customers and make it beneficial for them to refer customers to you and make it beneficial for them to buy more from you.

Reward customers for sending you buyers, not prospects. Reward customers for buying more.

The easiest sale to make is one to a satisfied customer. The second easiest sale to make is to a satisfied customer's family, friend, or business associate. You can reward customer referrals and customer loyalty by gifts or discounts, such as coupons, free dinners, free movie tickets, and so on.

Business Rule #34

Selling can be learned—it takes practice.

Business Rule #35

Selling is showing people how your product meets their needs.

Start with a Customer

If at all possible, the best way to start a business is to have customers from the very beginning. How do you do this? This is more likely to occur if you are working in a particular type of business and want to start a similar one because you see an opportunity your current boss does not care about or want to address. Working for someone else lets you learn the business, understand the suppliers, and learn on someone else's money how to sell those products and services. That is how Wal-Mart, Home Depot, and Starbucks were all started. The founders learned the business as employees first.

Remember the business rules:

Business Rule #29:
Selling is overcoming obstacles to a sale.

Business Rule #30:
You cannot listen when you are talking.

Business Rule #31:
You will make few sales convincing buyers you are smarter than they are or that you know their businesses better than they do.

Business Rule #32:

You need satisfied customers quickly. It is okay to reduce your price to get your first customers.

Business Rule #33:
The hardest sale is the first sale. The second hardest sale is the second sale.

Business Rule #34:
Selling can be learned—it takes practice.

Business Rule #35:
Selling is showing people how your product meets their needs.

Chapter Seven: Lessons Learned

1. Customer inertia is real and serious.
2. To make a sale, you need to overcome obstacles to sale.
3. You cannot overcome what you do not understand. You have to ask questions and listen.
4. The sale starts when you understand the reasons why the prospect does not want to buy.
5. There are 9 common reasons people do not buy.
6. There are 7 techniques to get people to try your product.
7. Selling is like fishing—find the right hook.
8. Understand the customer timeline to buy.
9. Reward customer referrals and loyalty.

Chapter Eight. How to Manage Your Business

Chapter Topics

- ***Management and start-up overload***
- ***Flow charting your value chain, supply chain, and manufacturing chain***
- ***Creating processes for quality control and efficiency***
- ***Customers' desire for quality on-time delivery and kind service***
- ***Management by objectives***
- ***Management by exceptions***
- ***The power of prioritization and simplicity***
- ***The Rule of 3s and the Rule of 7s***
- ***Measuring and rewarding employees' performance***
- ***Management from the front lines***
- ***Iteration—the necessity of improving every day***
- ***Creating a positive working atmosphere for employees***

Business Rule #36

> Management is teaching, motivating, and rewarding others for doing their jobs how you want, when you want, and at the speed you want.

Management is also the coordination of people, supplies, and other inputs that together allow you to make your product *on time* and *defect-free*—***every time***.

Start-Up Overload

Let's assume you have started a business and you have made some sales and you have satisfied customers—congratulations! What now?

You are responsible for everything from turning on the lights, ordering supplies, making product, seeking new customers, hiring help, sweeping the floor, and paying the bills to being a good family person and getting enough sleep. Welcome to *start-up overload*. But, surprisingly, you are energized, motivated, and having fun.

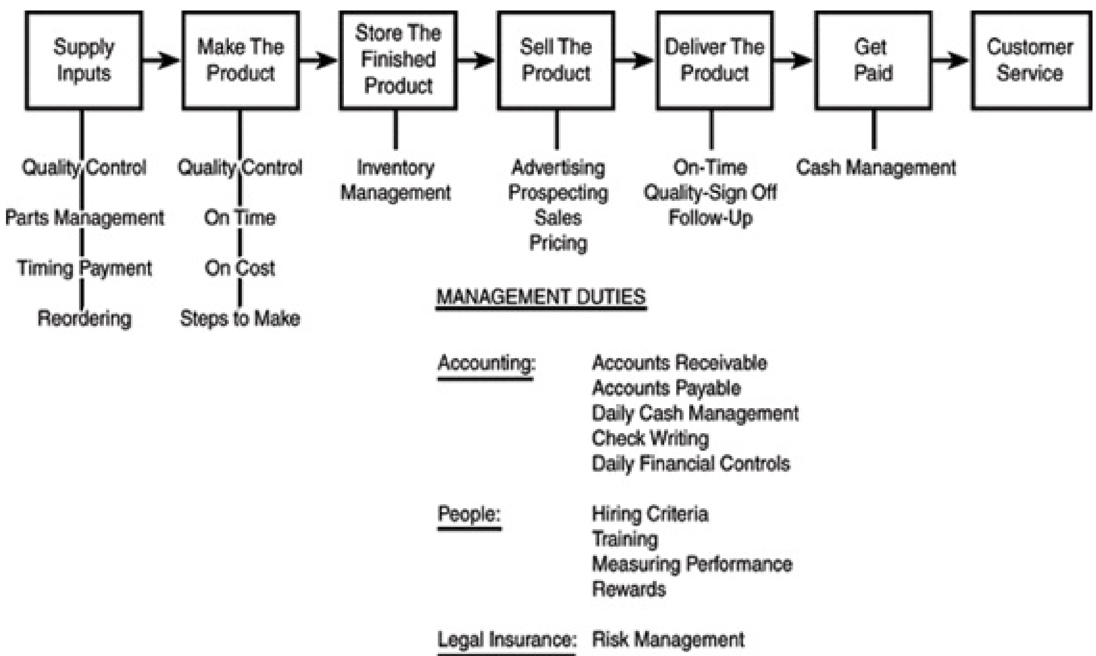
What we want to focus on in this chapter is how you keep control of all the moving parts and in essence manage yourself, prioritizing your time so that you can take care of the critical tasks necessary for your success every day.

You will learn that feeling overwhelmed, having too much to do, and never catching up is normal and does not go away. You will also learn to tell the difference between must-dos and nice-to-dos *real* fast. To do this you need a way of understanding your business as a linked chain of processes. This linked chain is your *value chain*.

Your Value Chain

Your value chain is composed of all the components, the parts, and the building blocks of your business. A value chain represents each step necessary to make and sell your product or service (see Figure 8.1).

Figure 8.1. *Value chain*



Flow charting your value chain is important for two reasons:

1. It makes you more aware of all the steps necessary to make and deliver your product or service.
2. It shows you how many different instructional manuals (your processes) you ultimately need to create— in other words, your cookbook or instruction manual so that others (employees) can do the steps as you would do them, consistently and at a high quality.
   The key parts of your value chain are
   - Your *inputs* (supplies-ingredients) that go into the product or service

creation or manufacturing process.

- What you do with the inputs to make the product.
- How do you deliver the product to the customer?
- How you service customers (help them)?
- How do you keep count of your costs and revenue—your accounting, billing, and collection process?
- How do you know that your customer is happy or satisfied?
- How do you find new customers?
- How do you keep up with what your competition is doing?
- How do you control and manage your cash flow?
- How do you know you are producing quality, defect-free products on time?

Your Supply Chain

One of your greatest challenges is that you must manage and work on different parts of the chain every day—and you have to deal with some of them simultaneously. As you grow, you'll see that all of this stuff happens every day.

Your supply chain includes all the ingredients that you need to deliver a finished, high-quality product to your customer.

- What are the key parts, supplies, or components that you will need to make your product?
- Where can you buy them?
- At what price?
- When and on what basis do you have to pay for those supplies?

Key Point

Will your inputs supplier allow you to pay him after your customer pays you?

Your Manufacturing (Assembling) Chain

Your manufacturing, assembling, or creation process is composed of each step-by-step item you need to do with or to your inputs (raw materials) to make what you are selling. Let's take an example: baking a cake (see Table 8.1).

Table 8.1. *Manufacturing Chain Example: Baking a Cake*

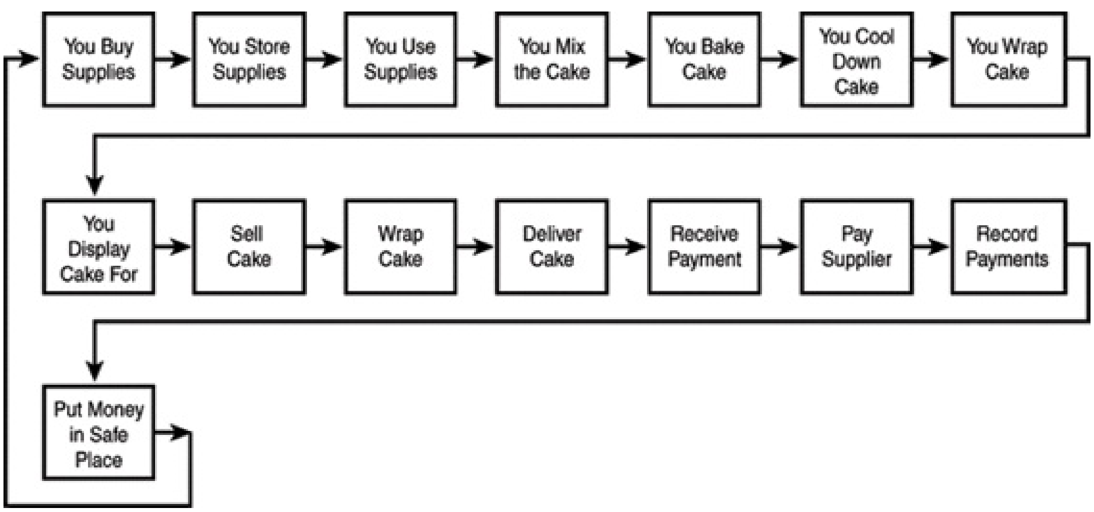
Inputs/Supplies +	Equipment/Utensils +	Delivery Material	
Butter	Spatulas	Box	
Flour	Mixer	Wrapping	
Flavoring	Bowls	Ribbon	
Yeast	Baking Pans	Logo	= Cake
Baking Soda	Soap and Water	Carrying Bag	
Nuts	Brushes	Customer Instructions	
Chocolate	Oven	Freshness Protection	
Cherries	Electricity or Gas		
	Oven Mittens		

The purpose of the manufacturing chain is to illuminate all the details—the steps you need to undertake and all the parts and supplies you need to do the job. Managing the business is the process of *"changing inputs into outputs."*

We left out a key component in our cake example—didn't we?

Yes, we also must include the step-by-step instructions for *how to make the cake* (see Figure 8.2). These instructions have to be written down clearly enough that an employee who does not know how to make a cake could understand and follow them. This will be your manual, so you have to write it in a simple form so that anyone can follow it.

Figure 8.2. *Baking a cake: key processes*



Each of the steps in Figure 8.2 must be drilled down into to create granular cookbook processes detailing how to do each step. That is *Execution Process*.

Remember, you cannot get too granular.

Why Do You Flow Chart Your Business?

Each step along the value chain is something you have to

- Focus on daily
- Manage daily
- Improve daily

Value chains help you drill down to the details of execution—the *how* you will get it done.

Horst Schulte, the former CEO of Ritz Carlton Hotels, used to teach Ed's entrepreneurship classes for one hour. Horst told the students he could teach them in that hour everything they needed to know about building a successful business, as shown in Business Rule #37.

Business Rule #37

The Horst Schulte Rule: No matter what the business is, customers want the same three things:

1. A defect-free, quality product
2. On-time delivery
3. To be treated nicely

Defect-free and on-time delivery requires you to create *processes* (ways of doing things that produce good, quality results every time).

Processes are the steps or the instructions you write out, which any employee can use to do the job like you would do it. These steps or instructions should be improved upon by employees and updated as your business grows and develops. Your employees ultimately should take on the ownership of their jobs and their processes and become better and faster each day.

So you have to focus first on the key steps and then write down instructions to be followed by others. By doing this first, you are creating a process:

Process = Standardization

= Details of Execution

= Quality

Management by Objectives

You are starting a business. Every day there are hundreds of things you need to do—find customers, serve customers, make products, buy supplies, keep customers happy, keep up with the money, train employees, oversee employees, motivate employees, and so on. How do you manage? How do you keep control and prioritize your tasks?

You manage by objectives. Objectives are goals—"to-dos." You will have long-term, short-term, and daily goals and objectives.

Each day before the start of the day you should write down your objectives for that day. Then at lunchtime, you should evaluate them based on your morning experience and then write down your afternoon objectives. Management by objectives helps you *prioritize and focus* your time on the most critical important tasks. It helps you spend your time on the important stuff and helps you not be overwhelmed everyday by minutia. Management is a daily prioritization and focus exercise. What are your most important goals?

- Making high-quality products
- Supplying products on time
- Producing satisfied customers
- Managing cash and expenses

You manage by objectives or goals day-in, day-out, no excuses, no exceptions. You set goals, and you achieve them. Then you set new goals.

Business Rule #38

Business is like farming: You get up every day, you till some soil, you plant, you water, you fertilize, you pull weeds, you harvest, and you get up and do it again tomorrow and the next day, and the next day….

Business Rule #39

Business is not complex; it is pretty simple. Make and sell something that someone needs. And do it defect-free, on time, with great service. Business is the details—the little things all added together that drive success. You need to focus on the details of execution.

Business Rule #40

You are only as good as your last sale. Complacency will kill you.

Business Rule #41

You build your business one customer at a time.

Management by objectives teaches you to prioritize because all problems and issues do not have equal weight. This is a hard thing for most people to learn. Many people start businesses and fail, unfortunately. All of these people probably worked very hard. But hard work is not enough. You have to work hard on the key stuff—the right stuff. But what is the right stuff?

1. *Finding and serving customers:* Without customers, you are out of business!
2. *Quality and customer satisfaction:* Unless you meet customer needs and deliver a quality product, you're out of business!
3. *Cash flow:* If you do not produce cash in excess of your costs in a reasonable amount of time, you are broke and out of business!

So setting objectives can be as simple as

- Making five calls today on new, qualified sales prospects
- Calling three customers, thanking them, and asking them for more business
- Focusing on getting the two last customer orders shipped ahead of time

You have to follow up and make sure the right things are getting done the right way. Is this hard? Yes. Can you do it? Yes. Why do we say that? Because millions of people—no smarter than you—are doing it every day.

- You manage by doing.
- You manage by knowing what is going on.
- You manage by making sure the priorities are getting done the right way and on time.

Management by objectives is a *prioritization* process that will teach you to automatically focus your limited time on those tasks most important to your business success.

Most people who start their own businesses will tell you they worked harder in it than they did on a job. But most will also tell you they loved it. They were the bosses. They had the power and worked to do the job right and to make the customers happy as they saw fit.

You, as an owner/manager of a small business, can learn a lot from how the military trains its squad leaders. They are taught to

- Assess the situation.
- Determine what needs to be done.
- Ask how they can have the impact.
- Do it.
- Evaluate/Learn/Improve.
- Move on to the next problem.

Management by Exceptions

You go to your business today. A lot is going on. You have your daily objectives, which are prioritized to make you and your employees focus on what is really important. You have had your daily morning team-teaching meeting.

Guess what? Stuff happens.

Something will always go wrong. Managing by exceptions is managing and fixing what goes wrong.

Business Rule #42

All businesses will make mistakes. Mistakes are a given.

Your objectives in managing by exception should be to

- Know or find out about the mistakes quickly
- Fix the mistakes
- Learn and do not make the same mistakes again

Employees are human beings. Human beings make mistakes. Accept that.

Outback Steakhouse Rule:
Teach; don't punish.

How can you find out about the mistakes? You might see it, your customer could complain, or your employees can catch the mistakes for you.

Business Rule #43
You cannot fix mistakes, and you cannot limit the damage unless you know about mistakes. Reward mistake illumination and do not "shoot" the messenger.

Common mistakes are

- *Waste*: Supplies are wasted, stolen, or lost, resulting in higher costs and lowering profits.
- *Theft*: Cash is stolen because someone other than the owner can write checks or count the cash daily.
- *Poor quality:*Sloppiness.
- *Late deliveries*
- *Treating customers badly*: Being short, rude, uncaring, or not giving them all your attention.
- *Poor cash management*: Not managing costs, receivables, and the checkbook.
- *Over-promising to customers*: Only promise what you can do.
- *Lying about what you sell and what you can deliver*: The truth always

comes out.
- *Trying to cover up mistakes*: Mistakes will happen—admit them and make them right.
- *Violating the Golden Rule*: The essence of dealing with employees and customers.

The Power of Simplicity

The military's "KISS" principle works: **K**eep **I**t **S**imple, **S**tupid.

It is far better to do a few things excellently than to be a master of none.

Businesses are built like houses. First, you need the right foundation. Then you add the sides and roof. All of these basics are time-consuming. But you have to get the basics right, or the house will fall down. Only after you have a firm foundation do you worry about the bells and whistles (curtains and furnishings). You want to build a business in the same way.

You have a dream. You can see the end game—a thriving business with 25 employees and two locations, you making good money, and even driving a new company car every three years. Dreams are good. They are your long-term goals. But what do you have to do first today to achieve your dreams?

Meet a Customer's Need Better, Faster, or Cheaper Than the Competition.

Each day is a new game. What counts is your performance today—not yesterday. Go in each day with the right attitude.

Business Rule #44

Every day is *Show Time!*

And to stay a winner, you have to get better. Getting better means improving, and you improve in small steps (incrementally).

Do not try to make big changes all the time—make small steps. Why? Eventually, you will have employees, and employees as people can only learn so fast and can only accommodate or accept so much change. Keeping it simple has many positive results:

- You focus on what is important.
- You can teach people in a digestible fashion.

- You can drill down to processes more easily and then work daily to *tweak* and incrementally improve how you do the key stuff.

"Keep it simple, stupid" also teaches us the *Rule of 3s* and the *Rule of 7s*.

Rule of 3s

Most people can focus on no more than three key things at any one time. Do not overwhelm employees or customers with long lists. What are the three key things people need to learn or do today?

- Can you, in a short, concise, and clear sentence or two, explain to someone what your business is?
- Can you explain how you are different or better than the competition in a short sentence?
- Can you explain to every employee why his or her specific job is important?
- Can you explain to every employee the three things he or she must do everyday?
- Can you explain to each employee how he will be graded and rewarded?
- Can you explain in a short sentence to each employee what three things are *not* under any circumstances allowable behavior?

Business Rule #45

The George Bernard Shaw Rule:

- Tell them what you are going to tell them.
- Tell them.
- Tell them what you just told them.

Business Rule #46

Jack Welch, former GE CEO: "You cannot communicate too much."

Rule of 7s

Most people can only manage seven or fewer people at a given time. So as you grow your business and increase the number of employees, you will need to add *structure*—a shift manager or an assistant manager who has responsibility to help manage employees. The Rule of 7 comes from the military, as did KISS.

Measurements and Rewards

If you will have other people (employees) working for you, there are two fundamental management principles you must understand, as listed in Business Rule #47.

Business Rule #47

1. People are likely to do what you want when you *measure* that performance.
2. People are more likely to do what you want if you measure it *and* reward those behaviors.

Measurements are how you keep score. For example, you have started a new business, and like all new businesses, you need paying customers to make profits. So you hire a salesperson. How will you measure her performance?

- Number of sales calls each day?
- Number of sales calls on qualified prospects?
- Number of sales made per week?
- Number of satisfied customers?
- Number of profitable sales?
- Number of profitable cash sales?

You can see that you have many alternatives, and you should choose the key measures. Measure the desired behaviors and think about the results you want. Many people fail to *drill down* to think about what is really important.

- Is it the number of sales calls, or is it the number of sales calls on *qualified (likely)* buyers?
- Is it the number of sales made, or is it the number of *profitable* sales made?
- Is it sales made or satisfied customers?

People will do what you measure.

Now you have to be fair. You should measure what employees are responsible for and what they can "control." If you measure number of sales, and you created a product no one wants—that is your fault, not theirs.

If you want 25 sales calls a day by phone or 5 sales visits a day, you will get that. But you may find a low percentage hit rate or conversion rate. That is, someone may have to make many, many calls before you get a sale.

Okay, so you decide to measure qualified sales calls—calling on five solid, prequalified prospects (likely buyers) a day. Better. But are you paying them to generate prospects or sales? If prospects, then who closes the sale? You? What do you truly want?

Profitable Sales
with
Satisfied Customers
who
Pay on Time

If a salesperson promises extras to make a sale, will the sale still be profitable? If to beat the competition, the salesperson over-promises or represents the product inaccurately, will you have a very satisfied customer? **NO**.

So as you can see, we are pushing you to think through what you measure and how you reward it. When should you reward the salesperson?

Time of Sale?

Time of Delivery?

Time of Payment?

It depends on your view of his job. Will he be responsible for the customer in after-sale service and customer satisfaction? Will the salesperson be the lead contact with the customer, or will you?

What if the salesperson leaves? If you do not know the customer well, is the customer going to stay with you or follow the salesperson?

Tip

All salespeople should sign an agreement stating all customers are owned by the business and they agree not to solicit or take customers to a competitor for a set time period and within a set geographical area.

The other thing we know about motivation and reward is that *rewards closely linked in time to good behaviors produce more good behaviors*.So bonuses or sales commissions need to be paid often in close time proximity to the behavior. The same rule applies for "penalties" regarding bad behavior.

Measurements also work better if they are

- Transparent
- Objective
- Fairly applied
- Rarely changed

We cannot tell you the absurd number of business owners who change sales compensation programs because salespeople are making too much money. Huh?

If you are measuring the right stuff, you should be making a lot of money if a salesperson is making a lot of money. Why would you reduce or change the compensation plan or cut geography down so salespeople will make less? Excuse me. Why not just put a gun to your head?

The other thing we know about high performance businesses is that they keep "the rules of the game" (how employees are measured and rewarded) relatively stable over a long period of time. This builds trust with employees that if they play by your rules and perform, they will be treated fairly, consistently, and have the opportunity to advance.

Never Change:

Your values

Your standards

Your key policies

Always Change:

Job execution to be better and faster

Stay on the Front Lines

Sam Walton used to say he followed the "management by walking around" principle. He was right. Good managers are on the front lines with employees and customers. And good managers do not hide in their offices or yearn for a nice office with a secretary guarding the door. Good managers are on the front lines seeing, learning, motivating, and leading by example.

Because we know that the goal in any business is to constantly improve and be better each day, you as the owner have to know what is going on and constantly teach and inspire.

Business Rule #48

Employees will act toward customers as you act toward employees. *Employees will imitate you.*

Employees in this regard are like young people. They model themselves after role models. If you want employees to be nice to your customers and say thank you, you have to treat your employees with respect, dignity, and say thank you to them.

Constant, be-better environments are created by engaged, involved managers (leaders) who follow the Golden Rule, lead by example, and who do what is right.

By definition, this kind of constant improvement environment requires an atmosphere where mistakes are accepted so they are corrected and learned from. Mistakes are teaching opportunities, not punishment opportunities.

Iteration

Iteration is the taking of small steps to be better. Many small improvements add up to a competitive advantage. In fact, what makes great companies better than the competition is the fact that they constantly improve. Iteration is the process of becoming better and faster. Your customers and employees will tell you what to improve if you ask and listen.

Make Work Fun

Your goal is to do a lot of business and to generate sizable income. To do this you will likely need employees, and you are dependent on them for your income. Like it or not—you need them.

To make money, you need to sell a lot of products that are high quality. High quality comes from processes that produce standardization, which comes from repetition: doing the task the same way every day. Repetition becomes boring. That is why you have to throw in some fun sometime. Some breaks, some ice cream, some pizza. Give people some paid time off and play games, hold contests, celebrate birthdays, and so on. You want to create an atmosphere in which making you money is more than a job for your employees.

Remember: You started your own business because you did not like being an employee. So manage your work environment to have fun sometimes. Make being your employee fun and meaningful.

And remember the business rules:

> **Business Rule #36:**
> Management is teaching, motivating, and rewarding others for doing their jobs how you want, when you want, and at the speed you want.

> **Business Rule #37:**
> The Horst Schulte Rule: No matter what the business is, customers want the same three things:

1. A defect-free, quality product
2. On-time delivery
3. To be treated nicely

> **Business Rule #38:**
> Business is like farming: You get up every day, you till some soil, you plant, you water, you fertilize, you pull weeds, you harvest, and you get up and do it again tomorrow, and the next day, and the next day….

> **Business Rule #39:**
> Business is not complex; it is pretty simple. Make and sell something that someone needs. And do it defect-free, on time, with great service. Business is the details—the little things all added together that drive success. You need to focus on the details of execution.

Business Rule #40:
You are only as good as your last sale. Complacency will kill you.

Business Rule #41:
You build your business one customer at a time.

Business Rule #42:
All businesses will make mistakes. Mistakes are a given.

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You cannot fix mistakes, and you cannot limit the damage unless you know about mistakes. Reward mistake illumination and do not "shoot" the messenger.

Business Rule #44:
Every day is Show Time!

Business Rule #45:
The George Bernard Shaw Rule:

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- Tell them.
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Business Rule #47:

1. People are likely to do what you want when you *measure* that performance.
2. People are more likely to do what you want if you measure it *and* reward those behaviors.

Business Rule #48:
Employees will act toward customers as you act toward employees. Employees will imitate you.

Chapter Eight: Lessons Learned

1. Management is the daily focus on producing high-quality products on time that meet customer needs, and it is the coordination of supplies, parts, processes, and people to get that desired result.
2. Every business has a value chain that should focus you on the parts of the business you need to manage.
3. You need to develop value chain as well as supply chain and manufacturing chain flow charts.
4. Management’s goal is to get the same high-quality result 99% of the time.
5. Management achieves 99% high-quality results through processes—drilling each job down to each step needed to complete it well.
6. Employees not only have to learn the job but also have to get better and faster; they have to constantly improve.
7. Good managers manage daily by objectives—the prioritized to-dos.
8. Good managers teach at least 15 minutes everyday to all employees the key objectives, the "have-to-dos" to be successful and the "cannot-dos."
9. Managing by exception is how you focus on the mistakes and problems.
10. Mistakes are a given. The key is to find them out quickly and fix them before they become big mistakes.
11. KISS: Keep It Simple, Stupid.
12. Learn to communicate clearly, concisely, and compellingly.
13. Constant improvement is far more important than doing it right the first time.
14. Structure becomes necessary when you have more than seven employees.
15. Measuring employees’ performance is critical.
16. Measure the right things. Measure behaviors that create the right results.
17. Measure frequently and give results to all employees.
18. Reward what you measure.
19. Make work fun; make work a game to learn.
20. Create a constant improvement business, a high-performance environment.
21. High-performance environments are positive, energetic places to work and are based on the Golden Rule.
22. You need the committed hearts and minds of your employees to make money.

Chapter Nine. How Do You Find and Keep Good Employees?

Chapter Topics

- ***People will be a big challenge.***
- ***What employees want.***
- ***Hiring for fit: focusing on values, drive, and motivation. Hire people who want to work hard to get ahead.***
- ***Doing your research when hiring—asking questions, checking references, and hiring everyone on a trial basis.***
- ***Creating a positive atmosphere for your employees.***
- ***The importance of employee buy-in and playing to people's strengths.***
- ***Instructing and training your employees and promoting from within.***
- ***Setting clear expectations of both desirable and undesirable behaviors.***
- ***Managing best practices:***
  - ***Treating your employees well and creating a "family" atmosphere.***
  - ***Hiring people like your customers.***
  - ***Creating meaning for your employees.***
  - ***Leading by example.***
- ***Managing you!***

We truly hope you need to read this chapter because it means that either you can afford employees or your business has more work than you and your family can do alone.

This People Stuff Is Hard

This people stuff is hard because people are human beings with faults and emotions. It takes hard work to learn how to hire, how to train, and how to inspire and motivate people to work hard to make *your* business a success.

High-performance organizations have learned that people will work harder if they feel part of something that they can be proud of. Create an environment where your employees feel part of a team and a "family" at work.

A "family-at-work" feeling comes about because the leaders care about their employees as people, not just as "horses pulling a wagon" or a "cog in the wheel."

The #1 challenge to growing a business is—**people**.

Business Rule #49

Happy Employees + Happy Customers = You make money

And

Happy Employees = Higher Productivity, Higher Quality, and Higher Loyalty

Business Rule #50

Boss + Happy Employee = Happy Customer

Or

Boss + Unhappy Employee = Unhappy Customer

How you treat your employees will determine whether or not they will help you make money.

What Do Employees Want?

Employees want the same things you want. They want to be treated

- With respect
- With dignity
- Honestly
- Fairly

Employees also want to have the opportunity to learn and advance and as the U.S. Army says, "Be all you can be." And being listened to and having some say over their lives is necessary for employees to fully buy-in to your program.

Why Is High Employee Turnover Bad?

Neither you nor we are good enough or smart enough to hire the right people all the time. But employee turnover is costly, disruptive, and takes your eye "off the ball"—satisfied, paying customers. It is frustrating and time-consuming hiring people, getting them trained correctly, and then having to start all over with a new employee after the experienced good employee leaves. Quality and efficiency suffers with constant employee turnover.

Ed, at one point, built a business with 25 employees, and he thought he was good at recognizing "winners"—but numbers do not lie. His hiring success rate was only 50%: Half of the time he was right, and the other half of the time he was wrong.

So he decided he needed to learn hiring best practices—and he did.

So, to avoid the costs, inefficiencies, and resulting customer unhappiness from constant employee turnover, you need to focus on how to avoid the problem—that starts with hiring the right people.

Hire for Fit

Most successful business builders have learned that it is better to hire for cultural fit—focusing on values fit over just hiring for skills.

Hire people with the right attitude and a track record of success. Hire people with high standards with integrity. Hire people with the drive to work hard and the drive to succeed to make a better life for themselves and their families.

One big company that Ed researched learned after 15 years of hiring that they simply should hire the "glass is half full" people and not "the glass is half empty" people.

That is a pretty good summary because how one approaches life or the day is really critical. Customers and other employees want to be around positive people—people who cast light, not darkness.

Other lessons to be learned about hiring are

1. Men and women with military service or training have been taught the value of rules, hard work, teamwork, process and thus can make good employees.
2. People who have experienced and rebounded successfully from adversity have character. Look for someone wanting to make his or her life better. Think about it—work is the means or avenue through which most people try to achieve their dreams for themselves and their families. Find people who want to join your journey and when you find them, take care of them.
3. Hire people like your customers. Sam Walton built Wal-Mart by hiring people just like his customers—people from small towns who understood

the value of a dollar and who came from humble backgrounds. Employees who are like your customers can relate easier to and better understand your customers.

Hiring Tools

To increase your chances of success, interview people two or three times. Check their backgrounds and work references. Ask references direct, blunt questions and listen to how they answer. Listen to the tone or how fast or slowly they answer. Listen for them hedging their answers or being hesitant.

Ask job applicants if they have anything embarrassing in their backgrounds. Everyone does, so listen to how they respond. Then decide whether it is important or not to your decision. Ask them if they have ever been charged with a crime and follow up with a background check.

In today’s world of lawsuits, references rarely speak directly about negative stuff—they speak indirectly. Ask those providing references if they would have any reservations about hiring the person again. Ask them if they would recommend the person without qualifications, and ask them what the person’s weaknesses are. You might not get as detailed information as you would like, but you should always ask.

Probationary Hiring

Hire everybody on a one-month probationary basis. That means you will determine in one month or less whether they have a job. This gives you time to evaluate and test them out. It generally will not take you a month to decide, but it does help protect you if you have made a wrong choice.

Buy-In

The ultimate question is: Will the employee "buy-in" and find meaning in working for your business? Will doing a good job be meaningful? Do they see the purpose of what you are trying to do? If you are starting a bakery that offers cakes and cookies, for example, you should not hire someone who does not like sweets. How can someone who does not eat dessert passionately make or sell desserts?

If you are doing shoe repair, look at the interviewee’s shoes—are they shined? Cared for? Clean?

If you are going to open a home cleaning service, is the interviewee wearing clean, pressed clothes? Do they take pride in their appearance?

So you should

- Hire for fit and willingness to work hard to succeed.
- Hire based on track record.
- Hire ex-military people.
- Hire people who are like your customers.
- Hire people who can relate to your business.
- Hire "the glass is half full" people.
- Hire people who need (not just want) a job.

The Rules of the Game

Employees will need to be taught what to do and how to do it, but they will make mistakes. That is your job is to train them. No one in the beginning is going to do the job as well as you can or would. But your goal is to move employees in that direction.

Teaching and training requires you to take the time to

- Point out mistakes.
- Teach people what to do.
- Give them the opportunity to do it.

If you have hired people of honesty, drive, and willingness to work hard to be successful, find them the right job that plays to their strengths.

Business Rule #51

> Play to people's strengths. You do not have the time or money to correct people's weaknesses.

Nonetheless, if a person steals, comes to work habitually late or drunk, or becomes physically or verbally abusive with a customer or fellow worker, fire them quickly and on the spot. You and your business must have a ***zero tolerance*** for behavior that is unethical, dishonest, or abusive.

Tell your employees not only what behaviors are good but equally as important, tell people directly and in writing what behaviors will not be tolerated and are grounds for instant dismissal.

Best Practices of Managing Employees

Constant communication and feedback are critical. Here are some keys:

- Explain the job.
- Teach the job.
- Give people the tools to do the job.
- Evaluate often and give feedback frequently.
- Document the feedback.
- If someone is doing something wrong, show him how to do it right.
- Reward good behavior with emotional rewards, too—praise, recognition, and so on.

Elementary grade school teachers are smarter than most managers. They understand the power of "stars"—giving out stars for good performance. You can create a great working atmosphere by

- Saying "thank you."
- Getting to know your people and their lives. In times of personal stress, cut people some slack.
- Asking them monthly whether they are happy in their jobs. If they're not, find out why. Decide whether you can make their jobs better.
- Making work fun and celebrating successes with pizza, ice cream, or a small gift.
- Thinking about work uniforms being a source of pride—shirts and blouses, hats, and bags that builds spirit de corps.

Learn and teach that the most important

- Business *word* is: Improvement.
- Business *phrase* is: Thank you.
- Business *objective* is: Serve your customer.
- Business *question to customers* is: How may I help you?

Promote from Within

As much as you can, promote from within. People want the chance for advancement and "to be all they can be." Great companies such as UPS, SYSCO, Best Buy, Walgreens, and Southwest Airlines have found success in doing this.

The Meaning of Work

Are your employees only a means to your end? Or are your employees the end?

What do we mean by that? If you focus on what your *duty* is to your employees—what you owe them for helping make you successful—you will have a higher chance of success than if you treat your employees like fungible commodities to be used like work horses.

People want and need more than a paycheck. Money by itself is not enough for consistent high performance. People spend a lot of time at work. Create an environment that enables high performance, enthusiasm, and positivity. Emotional recognition and praise are important to people.

Create an environment in which people are proud to work. Constantly explain how your business is helping people or is doing something good.

Also create an atmosphere of being the best at what you do and out-competing the competition. Teach the value and inner joy of excellence and the joy of satisfaction knowing you did your best.

Jimmy Blanchard, the former CEO of Synovus Financial, said he spent a million dollars on consultants trying to learn how to create a high-performance company, and he found out the simple truth:

"Just take care of your people."

Read about great teams like the San Antonio Spurs, the United States Marine Corps, Starbucks, Walgreens, Southwest Airlines, Synovus Financial, UPS, and Best Buy, where employees have become a key driver of success. These companies became great because of their people.

Remember: Happy Employees + Happy Customers = You make money.

The people stuff is all about leadership. There are thousands of leadership books you could read, but leadership is really pretty simple:

1. Take care of your people.
2. Live the Golden Rule.
3. Lead by example.
4. Never ask anyone to do anything you are not willing to do.

Business Rule #52

Before you can manage others, you need to *manage yourself*.

What do we mean? Each day before you go to work, you have to get yourself ready to be enthusiastic and engaged about your business—it is show time. Every day is game day in our world. Go into work with the right attitude—be up, be positive, be prepared.

Your emotional attitude (good or bad) will infect your workplace and your employees. Prepare yourself to lead by example.

Mental Rehearsal

Each day work out on paper what you want to focus on—what points to teach and what objectives you want to accomplish.

Think ahead of time what you need to do, how you want to do it, and how you will handle surprises, mistakes, or problems. Think about your employees—who needs encouragement or who needs teaching. Think about your customers—who needs to hear from you. Think about all aspects of your business before the day starts.

Prepare, prepare, prepare.

Mental Replay

After each day replay in your head the events of the day—what went right? What went wrong? What could you have done better? What process needs to be improved? What mistakes need to be corrected?

Mental replay is how you learn. Each day you should be determined to do at least one thing better than you did yesterday. Infuse your employees with that goal:

"Let's be better today than we were yesterday."

And remember:

Business Rule #49:
Happy Employees + Happy Customers = You make money
And
Happy Employees = Higher Productivity, Higher Quality, and Higher Loyalty

Business Rule #50:

Boss + Happy Employee = Happy Customer
Or
Boss + Unhappy Employee = Unhappy Customer

Business Rule #51:
Play to people's strengths. You do not have the time or money to correct people's weaknesses.

Business Rule #52:
Before you can manage others, you need to manage yourself.

Chapter Nine: Lessons Learned

1. Employees are people, too. They want the same exact things you want—dignity, respect, and the opportunity to be all they can be.
2. Hire for *fit*; focus on values and character. You can teach skills—you cannot teach character and drive.
3. Become good at hiring. Hire only after a thorough investigation and a probationary period. Hire people with a track record of success.
4. Hire employees who are like your customers. They will understand and relate to your customers better.
5. Play to people's strengths. You do not have enough time to fix people's weaknesses.
6. Be clear about what the job is. Be truthful and manage expectations.
7. Teach—Teach—Teach.
8. Inform your employees often what behaviors are *not* tolerated. Give daily/weekly feedback and keep records.
9. Be fair, consistent, and honest. Lead by example.
10. Ask your employees monthly if they are happy. If they aren't, why not? Happy employees result in happy customers. How you treat your employees is the critical determination of whether they are happy and how they will perform.
11. Make work fun and meaningful, and when you can, always promote from within.
12. High-performance organizations create a "family."
13. Remember: Happy Employees + Happy Customers = You make money.
14. Take care of your people.
15. Manage yourself as thoroughly as you manage your employees. Mentally

rehearse the day to come and mentally replay the previous day to see where you can make improvement.

Chapter Ten. How Do You Manage Growth?

Chapter Topics

- ***Growth can be good or bad***
- ***Growth will stretch your resources***
- ***Growth requires more employees and more cash***
- ***To manage growth you have to maintain high quality standards***
- ***To maintain high quality you will need a hiring and training process***
- ***Manage the unexpected***
- ***Use of outsourcing or part-timers***
- ***Legal contracts and structure***
- ***Upgrading employees***
- ***Customer diversification***
- ***Growth changes your job***

Most businesses face the same two major inflection points at which failure rates can be high:

1. Start-up survival—getting past break-even to making money
2. Managing growth

Building a successful business is challenging, fun, rewarding, scary, and just plain hard work, and you must be vigilant at these two points to overcome the potential for failure.

We have spent the first nine chapters focusing on how to avoid the common mistakes start-ups make, which is the main focus of this book. We now want to introduce you to the challenges that you will face when you enter a high-growth phase.

Growth Can Be Good or Bad

High growth requires you to manage more business under strong restraints. Those restraints are your limited time and limited money to invest in the business, and too few people to handle the growth. Growth stretches you, your people, and your capabilities. Too much growth too fast makes it hard to maintain quality and timeliness, which every customer wants.

Growth presents you with three big challenges:

1. People
2. Quality
3. Cash

On the people side, you will need more people quickly to serve more customers. Hiring people takes time. Training people takes time. Time is in short supply because you want the new business, need the new business, and are afraid to turn new business away.

So what do you do? First, you have to maintain high quality. That is non-negotiable. ***It is better to turn away work than to produce bad work.***

Secondly, you have to ask more of your employees. They will need to work overtime and weekends while you hire and train new employees. Involve your employees in finding new employees and training them.

Likewise with quality. Quality requires more process (instruction manuals) and more checks. You will need to choose your best employees and ask them to help write process instructions, and you will have to create a new structure giving those employees responsibility for oversight, quality control, and checking the work of new employees. This also means that you have to give them a pay raise to reward them for taking on this important role.

Growth will require you to prioritize what you do everyday and will require you to spend more time managing and less time "doing." This is a hard transition for many people because by definition entrepreneurs are doers, not managers.

And let's not forget about ole number one: CASH FLOW. Growth will require you to hire more people, which will increase your weekly payroll. Growth will cause you to have to buy more supplies and raw materials, which are needed by the increasing number of customers, all of which increases your cash payments to others ahead of your receipt of cash from customers.

Managing cash flow becomes even more paramount in a high growth situation because you may have a month lag between increased costs and receipt of cash from customers. How will you manage this?

The first source of that additional cash is you. The second source is a loan from family or friends. The next source of cash is getting your suppliers to finance your purchases of supplies until you deliver the product and collect the cash from customers. Unlikely sources of cash are your new customers and a bank, but it does not hurt to ask. Somehow you have to work through this cash flow timing issue.

Let's make this real. Using our sandwich shop example from Chapter 3, "What Is a Good Business Opportunity?"—you are selling regularly to 50 customers a day at lunch. Because your satisfied customers are spreading the word, all of a sudden you have 100 customers on a Tuesday. Your first thought is "Eureka!" Your second thought is that it is a fluke. But on Wednesday, Thursday, and Friday, you also have in excess of 100 customers.

Thank goodness for the weekend. What do you do? You need more people, more supplies, faster sandwich making, more space, another cash register, and so on because everyone wants high-quality, fast, good service during their lunch hour.

You are now facing the paradox of growth in Business Rule #53.

Business Rule #53

Growth can be good if managed well

Or

Growth can destroy your business if managed poorly.

The Two Absolutes

When you run the risk of being overrun by growth, what do you do?

First, you have to set your *priorities*:

1. You have to maintain high quality and produce satisfied customers.
2. You have to focus on the money.

Secondly, you "chunk." You break the challenge down into digestible chunks by what is most important, and you do those things first. What do you need to do?

You need more employees. How many? Where can you find them?

Can you or should you bootstrap employees? That is, fill in on a temporary basis with whomever you can lay hands on? Do you have friends, family, or employees' family members that can help out until you hire and train more employees?

Be careful and hire slowly. Remember—quality is #1. New people need to be trained and supervised. It is far better to tell potential customers, "Right now we are at full capacity, but we are expanding—please come back. Give us another chance, and here is a gift card for a free sandwich next week."

So what are your priorities?

- Quality
- Financial controls
- Good people

Process

Every part of your business has a process. Process is the *how* of what you do. It is the granular details of: buying supplies, storing supplies, preparing the sandwich ingredients, having a clean shop, having an attractive place to come and eat, ensuring good sandwiches, having sanitary restrooms, and keeping your sandwich line moving.

Drilling down more, process is about

- Cutting tomatoes
- Washing lettuce
- Spreading mustard
- Wrapping sandwiches
- Making coffee
- Restocking supplies
- Controlling costs, waste
- Greeting customers
- Keeping records of what types of sandwiches are selling
- Preventing spoilage

Processes yield checklists. Checklists are teaching tools. The more process you create early on, the easier it is to teach others when growth occurs.

With your checklists, you can give experienced employees the job of teaching new employees. You need short, one-page checklists for your key processes, which are to be filled out and signed each day (see Table 10.1).

Table 10.1. *Checklists*

Employee Checklist		Public Restroom	
Time Checked In	___	Paper Towels	___
Hands Washed	___	Toilet Paper	___
Hair Net On	___	Door Locks Work	___
Clean Appearance	___	Soap Dispenser	___
No exposed scrapes	___	Mirrors Cleaned	___
Gloves Used	___	Sink Cleaned	___
		Floor Cleaned	___
		Toilet Cleaned	___
		Toilet Sanitizer	___

Perishable Food		Checked At	
Refrigerator Temperature	___	10 A.M.	___
Food Checked	___	12 P.M.	___
Food Expiration Dates Checked	___	2 P.M.	___

How you ever seen an experienced airline pilot go through his or her checklist before a flight? It is done each and every time, no matter how much experience the pilot has. Checklists are key.

Financing Growth

What happened today? You sold 100 sandwiches, and you exhausted your supplies of tomatoes, lettuce, turkey, and roast beef. What do you do? You need the ingredients for tomorrow. You must replenish—but how much? Was today a fluke? Or should you buy 200 sandwiches worth of supplies? Or should you buy larger quantities and get a discount?

Be conservative: Do not end up with perishables over the weekend. Make sure you control waste.

Growth requires investment—more machinery, another cash register, more tables, more plates, bigger refrigerators. What do you buy first? Where do you find the money? Do you borrow from family? Do you finance with your seller? Do you go to a bank? Do you put the purchases on your credit card?

You do whatever is *easy*, *quick*, and *cheap*.

Financial Controls

Unfortunately, too many businesses get hurt by embezzlement and theft. You have to control the cash. You must control ordering supplies, and you count the money and make the bank deposit. And until you get much bigger, you should be the only person allowed to sign checks or spend money.

You also need a process to know each day where you stand financially. What did you sell today by type? Total dollars? What did you spend today? Month to date? As you operate the business, adjust your budget so it is realistic as to your costs.

Managing the Unexpected

You need a contingency plan for major risks. For example, with our sandwich shop, what do you do if

- You do not receive delivery one morning of your food supplies?
- Your refrigerator breaks down?
- You have a fire?
- Half of your employees stay home sick?
- A customer finds a hair in his sandwich?
- Your toilet overruns?
- You are very sick with the flu?
- Your child has an emergency at school?
- The electricity in your store goes out?
- A customer faints?
- An employee cuts himself?

For your contingency plan, you need to have thought through what you would do in each case if one of the listed events occurred. You need emergency phone numbers posted for cases of fire, health emergencies, and accidents. If one of these events happens, you need to be prepared ahead of time.

People

You will also need people processes and people controls as you grow.

First, as you gain experience with employees, pick your best two and do a profile of the perfect employee including background, experience, personality, and attitude. What experiences do you think have contributed to their success?

If you wanted to hire more employees like them, what major things would you look for? Create a checklist of what to look for when you hire. Prioritize what has worked so far and what is important to you.

Second, take those key employees and ask them to write out two checklists for you:

1. Instructions to new employees on what it takes to be successful working at your store, rules of conduct (how to treat customers), and rules of appearance.
2. A step-by-step guide to how to do a particular job right each and every time. Assign new employees the simplest, easiest, non-customer interaction jobs. Do this to test them out. Put your best employees "up front," dealing with customers and ensuring the sandwiches are made correctly.

Third, start keeping records of people interviewed and why they were rejected and also keep performance and attendance records for your current employees. You have to hire and fire for specific reasons, and they cannot be based on race, gender, or age—and you need to be able to prove you are doing this.

Fourth, you need to test employees often for drugs.

Fifth, keep records of hours worked and payroll and all applicable federal and state withholdings. Hire a payroll service to process all this for you.

Sixth, as you grow, you will decide whether you will add employee benefits or bonuses to your program. These programs can be costly. Shop wisely. See if there is a small business co-op in your hometown that you could join that would offer you health insurance on a group basis—cheaper than what you can buy on your own.

Small Business Services

As you grow, you will have to decide when and if to hire a part-time bookkeeper, hire an outside accountant to do your taxes, outsource your payroll, or buy computers for your business.

As you grow, you will need timely, quality information to keep control.

Table 10.2 is a checklist of things to consider:

Table 10.2. *Managing a Small Business*

Payroll	Hire payroll service.
Accounting	Hire a part-time accountant.
Accounts Receivable and Payable	Manage yourself daily and weekly.
Inventory Management	Count and order weekly.
HR Records	You update and document weekly.
Legal and Insurance	Start looking for a good business lawyer. Insurance is critical to your business.

As you grow, you will progress as shown in Table 10.3.

Table 10.3. *Other Controls*

Accounting	Move to part-time CPA, then to CPA doing your taxes, then to CPA doing an annual audit.
Accounts Receivable and Payable	Move from you paying bills and collecting money to your part-time controller doing those tasks, to a full-time controller.
HR Records	You do this in the beginning and then move to a part-time HR assistant helping in this area.
Inventory Management	You do this and then you move to a part-time controller and then to a full-time controller.

You will progress from outsourcing to part-time help to full-time help. As you hire accounting and quality control help, you will want to hire people with experience—people who have experience in business growth.

This point bears repeating: As you grow, hire people who have worked in high-growth businesses and who have made the common mistakes and have already learned how to manage and work in the crazy high-growth environment.

The challenges that high growth will present to you are *not* unique to you. Every business faces similar challenges. So when you hire people, hire those who have already learned how to succeed in this environment. Pay for experience. There is no reason you have to make the same mistakes others have made.

Check-Off

Always have two people sign off on any report—have someone periodically check the report to prevent mistakes, theft, and fraud.

Legal

You will move from using a lawyer to form your business to having legal contracts: better forms for invoices, purchase forms and orders, HR forms, confidentiality agreements, non-compete agreements, lease negotiations, and so on.

As you grow, you will step up the quality of your risk management and spend wisely for protection through insurance.

Legal Structure

When you start a business, you should use a legal form of business that protects your personal assets and home and family from liabilities such as a LLC (limited liability company) or a LLP (limited partnership). You can do this yourself by finding the form under your state government website under the Secretary of State or Corporation and Business Department.

Many small businesses start as sole proprietorships—the entrepreneur is the owner. If the business is doing business under a name like "The Sandwich Shoppe," many states require you to register that name as a "doing business as" name. Also many states will require you to get a business license and pay a business tax or property tax.

Business Rule #54

Growth requires more

- Processes
- Quality Controls
- Financial Controls
- Risk Management
- Real-Time Information

Let’s summarize what we have discussed so far:

- Growth will require you to move from doing everything yourself to hiring others to help you.
- Growth requires more checklists, that is, more "recipes" and lists of how to do things.

- Growth requires you to manage cash flow. When you grow, you will incur more costs—money for people, supplies, and products before you receive customer cash.
- Growth will require you to invest more money or to borrow more money unless you can get financing from your suppliers or cash earlier from customers.

As an example, in the sandwich shop, you could sell a weekly discount card enticing the buyer to purchase five sandwiches for $27 instead of the usual price of $30. If they pay in advance, this will decrease your profits, but it will also quickly provide you cash to buy supplies.

Small Business Networks

Growth will be challenging. But you can learn from other entrepreneurs. Most towns have a Chamber of Commerce or Entrepreneurs Network or a Business Club. Go once a month and meet people and ask their advice (make sure to ask *successful* entrepreneurs).

Always remember that every challenge you will face, someone else has faced that same situation, too.

Upgrading People

The toughest part of growth is the people part. You will need employees with skills and experience working for bigger businesses, and you may have to terminate people who have been with you from the start.

You have to upgrade to more skilled and experienced people. Hopefully, you can manage this by keeping loyal employees, but if not, you have to terminate them honestly and fairly.

This is difficult and hard. But many entrepreneurs will tell you their biggest mistake was not doing this fast enough.

Customer Diversification

As you grow, mostly likely your business will grow with some existing customers. *Beware* if any one customer becomes a big part of your business (20% or more). Understand that this customer is not usually making a long-term commitment to you. Always think about what would happen if you lost that customer. Would you have to terminate good employees? Would you have to lease a smaller space?

Ultimately, you would like for no customer to account for more than 10% of your business. You want to be diversified. In business, stuff happens. Customers can be bought, they can move, and they can go out of business.

Growth Changes Your Job

As you grow, you will not be able to do everything yourself. You will have to move from being a full-time "doer" to managing others and overseeing process and controls as well as *some* doing.

Managers are *teachers*. They create checklists for employees. Managers each day check all the important parts of the business. Managers look at the big picture and allocate their time accordingly among customers, production, teaching, quality control, cash management, and getting more business. You have to think about all these responsibilities and do something each day in each area.

You have to *plan* your day, *prioritize* your work, and *focus* on the key parts to make your business successful. You need your daily checklist. You need to think and plan more—***not*** just react.

As you grow, you will add levels of sophistication, and you will start to ask harder questions such as

1. ***Is my growth profitable?***
   Not all customers are profitable. Most businesses will tell you that about 80% of the profits come from 20% of the customers. So understand who they are and serve them well. Also understand which 10% to 20% of your customers are unprofitable or painful to serve. Slowly, replace them.
2. ***Am I the right person to grow the business?***
   Some entrepreneurs do not have the skills or personality to manage a larger business and need help—an experienced operations or financial person. First, you have to be careful and hire someone with a great track record with impeccable integrity and honesty.
   And you have to protect yourself legally with contracts and agreements that he or she will not leave you for a competitor or start a competing business and will not hire or steal employees or customers.
   And never, never—without experience and controls—give those people unilateral power over money or ordering or spending your money.

Business Rule #55 You and ONLY YOU control the money.

Hire these people first on a trial basis. Check them out with past employers. It is better to hire someone you know in your community. Be wary of people with many jobs in many different cities.

3. ***How big do I want to become? How big do I need to be?***
   Some people get caught up in the "high" of growth and continue to grow until their businesses are so big they become something different than what they originally wanted.
   Always remember growth can be good, and growth can be bad. You should decide how much growth is good for you.
   Every level of growth requires more people, more process, more controls, and more cash management. We are not saying that growth is bad for you. We are saying to approach growth and the size of your business realistically and understand that many businesses fail when they expand geographically to more locations or when they diversify into new products or when owners lose control of the money.
   Always be wary of the downside—what can go wrong—and have contingency plans and manage for both success and risk management.
   Lastly, growth will change your competition. By that we mean you will face bigger competition that may have more money than you and thus can afford to lower their prices to take away your customers. As you grow and expand, that competition will likely view you as a competitive threat. Before growing, you were too small for them to care or worry about.

Remember:

Business Rule #53:
Growth can be good if managed well
Or
Growth can destroy your business if managed poorly.

Business Rule #54:
Growth requires more

- Processes

- Quality Controls
- Financial Controls
- Risk Management
- Real-Time Information

Business Rule #55:
You and ONLY YOU control the money.

Chapter Ten: Lessons Learned

1. Growth can be good or bad.
2. Growth creates people, quality, and financial issues.
3. Growth requires more controls and processes.
4. Growth requires the entrepreneur to become a manager.
5. Managing is different than doing.
6. Every financial area of your business (supplies, inventory, accounting, cash management, HR, and training employees) will need more process and controls.
7. Controls and processes have to be created real-time as you operate the business.
8. Growth will require you to upgrade your employees.
9. Growth will require you to manage customer concentration risk.
10. Growth will require more legal and insurance costs.
11. Growth will stretch you and will require you to operate differently.
12. Growth will require you to manage more proactively than reactively.
13. Growth will change your competition.

Conclusion

Well, what have we learned? Let's review the Business Rules and Lessons Learned from each chapter in this conclusion.
We hope you have learned valuable tools and concepts that you can use to pursue your dream. Best wishes and enjoy your journey.

—Ed and Charlie

Business Rules

Business Rule #1

The Jerry McGuire Rule: Follow the Money—Cash is King.

Business Rule #2

The Peter Drucker Rule: "The sole purpose of business is to serve customers."

Business Rule #3

Customers know best what they need.

Business Rule #4

You are looking for a good business opportunity—*not* a good idea.

Business Rule #5

Every entrepreneur overestimates the number of customers that will buy and the speed at which they will buy.

Business Rule #6

Happy employees create happy customers, which creates profits for you!

Business Rule #7: The 7 Ws

1. What can I sell?
2. To Whom can I sell?
3. Why will customers buy from me?
4. At What price?
5. What are my costs?
6. When will customers buy?
7. What will the competition do?

Business Rule #8

Low Profit Margin = High Volume

High Profit Margin = Lower Volume

Business Rule #9

Profits are your goal—sooner rather than later.

Business Rule #10

Cash flow is your business’s lifeblood—it is how you pay your bills.

Business Rule #11

Control your costs—spend wisely on the right stuff.

Business Rule #12

Know your burn rate—how soon will you run out of money?

Business Rule #13

Customers are high-probability prospects who actually buy your product.

Business Rule #14

Focus on high-probability prospects—*not* just anyone willing to listen.

Business Rule #15

It is easier to convert top-and high-priority prospects to customers than other prospects.

Business Rule #16

Learn about your industry. Search the Internet and find a relevant trade association.

Business Rule #17

If someone buys from one of your competitors, *you lose*, and the competitor wins.

Business Rule #18

When in doubt, always define your competition broadly, not narrowly.

Business Rule #19

Attack competitors' weaknesses.

Business Rule #20

Competitors will respond. Business is like a baseball game—there is always another inning.

Business Rule #21

Customers buy solutions, so you must constantly assess what customers really want or need and make sure you give them that—*not* what you think they need, nor more than they need because they will not want to pay for anything they do not need.

Business Rule #22

The goal is to deliver the most value to your customer at a price that is both affordable for your customer and profitable for you.

Business Rule #23

The key is the value perceived by the customer.

Business Rule #24

Avoid the Winner's Curse: Do not think you will continue winning forever. Do not become complacent or overconfident.

Business Rule #25

This is the competitive advantage you are seeking: to offer more value at an affordable price and do it defect-free, on time, and with good service every time.

Business Rule #26

Don’t fall in love with your product or service. Be willing to listen to negative feedback and change.

Business Rule #27

Rarely is it the product or service that is the reason for success in a new business. In reality, it is the execution of the business that is the primary driver of a new venture’s success.

Business Rule #28

Get good customer references as soon as you can. Use them to sell to other customers.

Business Rule #29

Selling is overcoming obstacles to a sale.

Business Rule #30

You cannot listen when you are talking.

Business Rule #31

You will make few sales convincing buyers you are smarter than they are or that you know their businesses better than they do.

Business Rule #32

You need satisfied customers quickly. It is okay to reduce your price to get your first customers.

Business Rule #33

The hardest sale is the first sale. The second hardest sale is the second sale.

Business Rule #34

Selling can be learned—it takes practice.

Business Rule #35

Selling is showing people how your product meets their needs.

Business Rule #36

Management is teaching, motivating, and rewarding others for doing their jobs how you want, when you want, and at the speed you want.

Business Rule #37

The Horst Schulte Rule: No matter what the business is, customers want the same three things:

1. A defect-free, quality product
2. On-time delivery
3. To be treated nicely

Business Rule #38

Business is like farming: You get up every day, you till some soil, you plant, you water, you fertilize, you pull weeds, you harvest, and you get up and do it again tomorrow, and the next day, and the next day….

Business Rule #39

Business is not complex; it is pretty simple. Make and sell something that someone needs. And do it defect-free, on time, with great service. Business is the details—the little things all added together that drive success. You need to focus on the details of execution.

Business Rule #40

You are only as good as your last sale. Complacency will kill you.

Business Rule #41

You build your business one customer at a time.

Business Rule #42

All businesses will make mistakes. Mistakes are a given.

Business Rule #43

You cannot fix mistakes, and you cannot limit the damage unless you know about mistakes. Reward mistake illumination and do not "shoot" the messenger.

Business Rule #44

Every day is *Show Time!*

Business Rule #45

The George Bernard Shaw Rule:

- Tell them what you are going to tell them.
- Tell them.
- Tell them what you just told them.

Business Rule #46

Jack Welch, former GE CEO: "You cannot communicate too much."

Business Rule #47

1. People are likely to do what you want when you *measure* that performance.
2. People are more likely to do what you want if you measure it *and* reward those behaviors.

Business Rule #48

Employees will act toward customers as you act toward employees. *Employees will imitate you.*

Business Rule #49

Happy Employees + Happy Customers = You make money And

Happy Employees = Higher Productivity, Higher Quality, and Higher Loyalty

Business Rule #50

Boss + Happy Employee = Happy Customer

Or

Boss + Unhappy Employee = Unhappy Customer

Business Rule #51

Play to people's strengths. You do not have the time or money to correct people's weaknesses.

Business Rule #52

Before you can manage others, you need to *manage yourself*.

Business Rule #53

Growth can be good if managed well

Or

Growth can destroy your business if managed poorly.

Business Rule #54

Growth requires more

- Processes
- Quality Controls
- Financial Controls
- Risk Management

- Real-Time Information

Business Rule #55

You and ONLY YOU control the money.

Lessons Learned

Chapter One

1. Businesses succeed only by meeting customer needs.
2. Businesses succeed because they make profits.
3. Business profit equals cash in from customer minus cash out for costs.
4. Successful entrepreneurs meet customers' needs better, faster, or cheaper than someone else.
5. IQ, education, family background, race, religion, and ethnic origin are not predictive of entrepreneurial success.
6. Successful serial entrepreneurs are not big risk takers—they take small-measured risks.
7. Most successful entrepreneurs are not inventors or discoverers or geniuses.
8. Business is about people. You need people to buy your product, people to work hard for you, and people to finance your business.
9. Many successful entrepreneurs had previous work experience in the same types of business they started.
10. Many successful entrepreneurs developed their businesses part-time before quitting their paying jobs.
11. Entrepreneurs are *doers*.
12. Entrepreneurs test an idea—they do trials.
13. Entrepreneurs learn and iterate, tinker and get better.
14. Entrepreneurs listen to customers.
15. Entrepreneurs constantly get better and improve their products or services.

Chapter Two

Businesses generally fail for 8 fundamental reasons:

1. People choose a bad business opportunity.

2. People try to sell to the wrong customers.
3. People try to sell the wrong products or services.
4. People price their products improperly.
5. People overestimate the number and the speed at which people will buy.
6. People cannot manage the business so as to consistently produce high quality products on time at a profit.
7. Employee problems.
8. People cannot scale their businesses to accommodate customer demand.

Chapter Three

1. Business ideas are like sand at the beach—plentiful, but there are few new or unique business ideas.
2. Not every business *idea* will make a good business *opportunity*.
3. Your idea needs to "pencil"—that is, make economic sense.
4. The key "pencil" drivers are:
    - The amount of money you need to make
    - Net profit margin
    - Customer conversion rate
    - Customer traffic volume
    - Speed of sales
    - Customer buying frequency
    - Burn rate and staying power—how much time (money) can you invest until you make a profit?
5. Remember the 7 Ws:
    - **W**hat can I sell?
    - To **W**hom can I sell?
    - **W**hy will customers buy from me?
    - At **W**hat price?
    - **W**hat are my costs?
    - **W**hen will customers buy?
    - **W**hat will the competition do?
6. Common mistakes business starters make:
    - Overestimating the number of customer sales • Overestimating how

fast people will buy
    - Underestimating their costs
    - Underestimating the competition
7. Owning a low margin business means:
    - You need a lot of customers.
    - Customers need to buy frequently.
    - You will have to operate very efficiently.
    - Your room for financial mistakes or errors will be small.
    - Volume of customer traffic, customer conversion rates, and knowing the competition is very important.
8. Owning a higher margin business generally means:
    - You need fewer customers.
    - Your customers probably will not be frequent buyers.
    - You will need to consistently generate new customer prospects.
    - Customer conversion rates could be low.
    - You need a constant flow of good customer prospects.
9. Your estimated weekly costs help you predict your *burn rate*: the speed at which you will burn through your money. Burn rate tells you how long you can stay in business until you hit break-even.
10. *Break-even* is the point at which your weekly incoming cash equals your costs going out.

"The sole purpose of business is to serve customers."

—*Peter Drucker*

"If you do not make a profit in your business, you are a charity—a not-for-profit."

—*Ed Hess*

Chapter Four

1. Your company's likelihood for success is directly tied to identifying your prospects' most important needs and wants and then providing a solution

that best meets their objectives.

2. Because not all prospects are equally as likely to buy your product or service, it's important that you determine which specific prospects are most interested in buying your product or service and what's different about them from the rest of the market.
   Prospects who are the most likely to buy your product or service are your target market.
3. The benefits of identifying targeted prospects include marketing and advertising savings, more enhanced product or service design, and increased sales.
4. Doing your homework is critical to your success.
5. Talk to people—learn firsthand people's needs/wants.
6. Constantly survey prospects, customers, and the competition.
7. Know your competitors' strengths and weaknesses so that you can take advantage of their limitations and better serve your targeted customers.
8. Your goal is to spend your time on high-probability prospects.
9. You have limited time and money. Do your research, focus, and be disciplined.

Chapter Five

1. Customers buy solutions, so you must constantly assess what customers really want or need and make sure you give them that—*not* what you think they need nor more than they need because they will not want to pay for anything they do not need.
2. The goal is to deliver the most value to your customer at a cost that is both affordable for your customer and profitable for you.
3. Avoid the Winner's Curse—overconfidence and complacency.
4. The competitive advantage you are seeking is to offer more value at an affordable price and do it defect-free, on time, and with good service every time.
5. Don't fall in love with your product or service—that is the job of your customers.
6. Go to market as fast as possible—learn from your customers.
7. Get customer references as soon as you can—they will help you make more sales.
8. Product benefits are necessities. Product features are options.
9. The Value Proposition Ratio is Value = Benefits ÷ Costs.
10. Value is what the customer perceives it to be—not what you think it is.

11. Your "reason for being" is your essence, your differentiator, and what your business stands for in the minds of customers.
12. Low innovation product design is less risky than developing a totally new product.
13. Remember you have to be able to build or produce your product reliably and 99% defect-free, on time, and at a profit.
14. Develop a prototype and get in the market quickly and learn from your customers. Test and learn and adapt and improve. Constant improvement is key.

Chapter Six

1. Price impacts your volume of sales and your profit.
2. Profit = Sales Price – Costs
3. There are two types of costs: fixed and variable.
4. Variable costs vary with your volume of product sold.
5. Review your costs monthly.
6. Price also determines your break-even volume—the amount you need to sell to earn enough profit to cover your costs.
7. Cost plus pricing and competitive pricing are two good pricing strategies.
8. You may have to offer guarantees or payment terms to certain customers.
9. Remember—to you, cash is king.

Chapter Seven

1. Customer inertia is real and serious.
2. To make a sale, you need to overcome obstacles to sale.
3. You cannot overcome what you do not understand. You have to ask questions and listen.
4. The sale starts when you understand the reasons why the prospect does not want to buy.
5. There are 9 common reasons people do not buy.
6. There are 7 techniques to get people to try your product.
7. Selling is like fishing—find the right hook.
8. Understand the customer timeline to buy.
9. Reward customer referrals and loyalty.

Chapter Eight

1. Management is the daily focus on producing high-quality products on time that meet customer needs, and it is the coordination of supplies, parts, processes, and people to get that desired result.
2. Every business has a value chain that should focus on the parts of the business you need to manage.
3. You need to develop value chain as well as supply chain and manufacturing chain flow charts.
4. Management's goal is to get the same high-quality result 99% of the time.
5. Management achieves 99% high-quality results through processes—drilling each job down to each step needed to complete it well.
6. Employees not only have to learn the job but also have to get better and faster; they have to constantly improve.
7. Good managers manage daily by objectives—the prioritized to-dos.
8. Good managers teach at least 15 minutes everyday to all employees the key objectives, the "have-to-dos" to be successful and the "cannot-dos."
9. Managing by exception is how you focus on the mistakes and problems.
10. Mistakes are a given. The key is to find them out quickly and fix them before they become big mistakes.
11. KISS: Keep It Simple, Stupid.
12. Learn to communicate clearly, concisely, and compellingly.
13. Constant improvement is far more important than doing it right the first time.
14. Structure becomes necessary when you have more than seven employees.
15. Measuring employees' performance is critical.
16. Measure the right things. Measure behaviors that create the right results.
17. Measure frequently and give results to all employees.
18. Reward what you measure.
19. Make work fun; make work a game to learn.
20. Create a constant improvement business, a high-performance environment.
21. High-performance environments are positive, energetic places to work and are based on the Golden Rule.
22. You need the committed hearts and minds of your employees to make money.

Chapter Nine

1. Employees are people, too. They want the same exact things you want—dignity, respect, and the opportunity to be all they can be.
2. Hire for *fit*; focus on values and character. You can teach skills—you cannot

teach character and drive.

3. Become good at hiring. Hire only after a thorough investigation and a probationary period. Hire people with a track record of success.
4. Hire employees who are like your customers. They will understand and relate to your customers better.
5. Play to people’s strengths. You do not have enough time to fix people’s weaknesses.
6. Be clear about what the job is. Be truthful and manage expectations.
7. Teach—Teach—Teach.
8. Inform your employees often what behaviors are *not* tolerated. Give daily/weekly feedback and keep records.
9. Be fair, consistent, and honest. Lead by example.
10. Ask your employees monthly if they are happy. If they aren’t, why not? Happy employees result in happy customers. How you treat your employees is the critical determination of whether they are happy and how they will perform.
11. Make work fun and meaningful, and when you can, always promote from within.
12. High-performance organizations create a "family."
13. Remember: Happy Employees + Happy Customers = You make money.
14. Take care of your people.
15. Manage yourself as thoroughly as you manage your employees. Mentally rehearse the day to come and mentally replay the previous day to see where you can make improvement.

Chapter Ten

1. Growth can be good or bad.
2. Growth creates people, quality, and financial issues.
3. Growth requires more controls and processes.
4. Growth requires the entrepreneur to become a manager.
5. Managing is different than doing.
6. Every financial area of your business (supplies, inventory, accounting, cash management, HR, and training employees) will need more process and controls.
7. Controls and processes have to be created real-time as you operate the business.
8. Growth will require you to upgrade your employees.
9. Growth will require you to manage customer concentration risk.

10. Growth will require more legal and insurance costs.
11. Growth will stretch you and will require you to operate differently.
12. Growth will require you to manage more proactively than reactively.
13. Growth will change your competition.

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Two academics and two consultants collaborate to put forth a model for how family businesses evolve and the different roles family members can play as family members, employees, and owners. (ISBN 0-87584-555-4)

Hess, Edward D. *The Successful Family Business: A Proactive Plan for Managing the Family and the Business*. Westport, CT: Praeger Publishers, 2006.

Ed's practical guide to common family issues that arise in a family business. (ISBN 0-275-98887-2)

Lansberg, Ivan. *Succeeding Generations: Realizing the Dream of Families in Business*. Boston: HBS Press, 1999.

This book focuses on succession and the complex issues involved in managing a succession. A good but long read on marshalling a family's dream, the selection process, the governance issues, and about letting go. (ISBN 0-87584-742-0)

Ward, John L. *Keeping the Family Business Healthy*. Business Owner Resources, 1997.

Fundamentally, a strategy book for managing and perpetuating a family business. A good basic primer. (ISBN 1-55542-026-5)

Ward, John L. *Perpetuating the Family Business*. New York: Palgrave Macmillan, 2004.

This, in my opinion, is John Ward's best book—what he has learned in his 25 years teaching, researching, and consulting. This book will reinforce many of the lessons you learned in Ed's book. (ISBN 1-4039-3397-9)

Finance, Accounting, and Measurement Books

Bruner, Robert F. *Deals From Hell: M&A Lessons that Rise Above the Ashes*. Hoboken, NJ: Wiley, 2005.

Bob Bruner is the dean at the University of Virginia Darden School of Business and is one of the leading authorities on mergers. Do they work? Under what conditions? And what are the common pitfalls? A must-read for anyone thinking of merging their business or selling for stock. (ISBN 978-0-471-39595-9)

Copeland, Thomas E., Tim Koller, and Jack Murrin. *Valuation: Measuring and*

Managing the Value of Companies. 2nd ed. New York: Wiley, 1994.

The bible of valuation written by three McKinsey & Company professionals. This book should answer your questions on discounted cash flow projections, EBITDA versus accounting net income, the real cost of financing or capital, values-based management, and finding the value drivers of your business. (ISBN 0-471-36190-9)

Fridson, Martin, and Fernando Alvarez. *Financial Statement Analysis: A Practitioner's Guide*. 3rd ed. New York: John Wiley & Sons, 2002.

An outstanding book for those with a basic understanding of accounting. A compendium of common issues in understanding securities offerings and evaluating competitors' or targets' financial statements. The ways numbers can be massaged or manipulated. (ISBN 0-471-40915-4)

Kaplan, Robert S., and David P. Norton. *The Balanced Scorecard: Translating Strategy into Action*. Boston: HBS Press, 1996.

How do you measure results? How do you measure employee or business unit results? Many businesses today utilize some form of balanced scorecard to link measurements and strategy and to achieve strategic alignment of their different business units, departments, or functions. This book makes it possible for every business, regardless of size, to measure better and hold people accountable. (ISBN 0-87584-651-3)

Schilit, Howard. *Financial Shenanigans: How to Detect Accounting Gimmicks and Fraud in Financial Reports*. 2nd ed. New York: McGraw-Hill, 2002.

From the pioneer of accounting sleuthdom, the common accounting gimmicks and ways to manipulate the financial picture of a company. Use this checklist to evaluate the financial statements of the business you may want to buy. (ISBN 0-07-138626-2)

Stern, Joel M. and Donald H. Chew, editors. *The Revolution in Corporate Finance*. 2nd ed. Cambridge, MA: Blackwell Finance, 1992.

A compendium of fine articles on the topics of capital budgeting, cost of capital, capital structures, raising capital, interest rate swaps, and spin-offs, carve-outs, and divestitures. (ISBN 0-631-18554-2)

Leadership Books

Badaracco, Joseph. *Leading Quietly*. Boston: HBS Press, 2002.

Joe Badaracco is a wonderful, humble leader and professor at Harvard Business School. He graciously helped Ed when he was beginning his teaching career with no motivation other than kindness. He, in this book, dispels the myths of leadership and asserts that leadership is patient, careful, and incremental. He lays out a framework or template for leadership analysis and action. (ISBN 1-57851-487-8)

Behar, Howard. *It's Not About the Coffee*. Portfolio, 2007.

A good book on leadership and people-centric policies at Starbucks. (ISBN 9781591841920)

Bennis, Warren G. and Robert J. Thomas. *Geeks & Geezers*. Boston: HBS Press, 2002.

The authors look at the role of adversity in a leader's life. They correctly focus on the fact that in extremely difficult times, character, confidence, and values are solidified and that adversity prepares one to deal with life's challenges. (ISBN 1-57851-582-3)

George, Bill. *Authentic Leadership*. San Francisco: Jossey-Bass, 2003.

Bill George is the former chairman and CEO of Medtronic. His book is an illuminating story about the authentic leadership model. He focuses on purposes, values, and self-discipline and gives one hope in this era of corporate scandals that one can lead with values and morals and create shareholder value, too. (ISBN 0-7879-6913-3)

Gergen, David R. *Eyewitness to Power*. New York: Simon & Schuster, 2000.

The subtitle of David Gergen's book is *The Essence of Leadership: Nixon to Clinton*, and he does not disappoint. A thoughtful work focusing on style, checks, and balances, character, and power. The pros and cons of each president's leadership are here for all to learn from. (ISBN 0-684-82663-1)

Goleman, Daniel, Richard E. Boyatzis, and Annie McKee. *Primal Leadership: Realizing the Power of Emotional Intelligence*. Boston: HBS Press, 2002.

Goleman and his colleagues at Rutgers and Case Western University have put the leadership onus right back where it belongs—on you. Our effectiveness as

leaders is dependent on our emotional intelligence. Our ability to manage our emotions, understand others' motions, and to relate and connect to people emotionally. A must-read for every male. (ISBN 1-57851-486-X)

Greenleaf, Robert K. *Servant Leadership*. New York: Paulist Press, 2002.

Robert Greenleaf, a former AT&T executive, in 1977 espoused that service to others was the essence of leadership. Servant leadership is growing in popularity and is also known as values-based leadership. (ISBN 0-8091-0554-3)

Books on Lessons to Learn from Bad Leadership

Eichenwald, Kurt. *Conspiracy of Fools: A True Story*. New York: Broadway Books, 2005.

A spell-binding account of the inner working of Enron from a corporate finance viewpoint primarily. Reads like a mystery thriller. It tells the story of when management loses touch with the details, condones inappropriate behavior, and compensates people for the wrong results. Wall Street's role in this disaster is not pretty. And Arthur Andersen's overriding of its quality control people in order to satisfy Enron is shameful. (ISBN 0-7679-1178-4)

McLean, Bethany, and Peter Elkind. *The Smartest Guys in the Room: The Amazing Rise and Scandalous Fall of Enron*. New York: Portfolio, 2003.

The story of the Enron Company—its culture, value, and leadership. How the greed of the 1990s impacted the ability of accountants, lawyers, and Wall Street to render their duties to the investing public. The story of arrogance, hubris, greed without values, and form over substance. How smart, "normal" people got caught up in peer pressure and lost their anchors or moral compasses for what is right and wrong. (ISBN 1-59184-008-2)

Stewart, James B. *Disney War*. New York: Simon & Schuster, 2005.

The excruciating details of an autocratic, insecure CEO who packed his board with those beholden to him. The pettiness, the duplicity, and the failure of core values are mind-boggling. The story is like a soap opera, and much can be learned about the CEO's decision-making processes. (ISBN 0-684-80993-1)

Management Books

Bossidy, Larry, and Ram Charan with Charles Burck. *Execution: The Discipline of Getting Things Done*. New York: Crown Business, 2002.

Bossidy and Charan refocused U.S. business leadership on the key role of execution. The best strategy in the world is not worth much if you cannot execute it. Bossidy's mantra is a culture of critical inquiry that produces reality for management. His views on constructive debate, measurement, and rewards are spot on. He sets forth the GE model of aligning strategy and action. (ISBN 0-609-61057-0)

Buckingham, Marcus, and Curt Coffman. *First, Break All the Rules*. New York: Simon and Schuster, 1999.

This book would have sold even more copies with a representative title. Ed uses it in his classes. It is the best book to teach you how to manage people—how to communicate, set objectives, and hold people accountable, and it is a primer for managing people best practices—based on years of research by Gallup. (ISBN 0-684-85285-1)

Collins, James C. *Good to Great*. New York: HarperBusiness, 2001.

Jim Collins produced the best-selling business book since *Search For Excellence*. (ISBN 0-06-662099-6)

Finkelstein, Sydney. *Why Smart Executives Fail and What You Can Learn from Their Mistakes*. New York: Portfolio, 2003.

Professor Finkelstein's book is a welcomed addition. His research shows that most major business failures occur in big transactions: mergers, change initiatives, new competition, and they occur because of leadership's arrogance, hubris, insularity, and from flawed cognition—the failure to see and process reality. If you are successful, a must-read to stay successful. (ISBN 1-59184-010-4)

Hamel, Gary. *The Future of Management*. Boston: HBS Press, 2007.

A thought-provoking read on how to build a modern business where all stakeholders win. (ISBN 1-4221-0250-5)

Magretta, Joan. *What Management Is*. New York: Free Press, 2002.

This book brings all of us back to the basics of what is management. Anytime you get caught up in either management hype or think you have figured the management game out—you should pull this book off the shelf and read it. (ISBN 0-7432-0318-6)

Sullivan, Gordon R., and Michael V. Harper. *Hope Is Not a Method*. New York: Broadway Books, 1997.

If you need to change something major in your business, read this book about the U.S. Army's massive change initiative in the early 1990s. One of the best books on the execution of change. (ISBN 0-7679-0060-4)

Marketing and Sales Books

Bedbury, Scott with Stephen Fenichell. *A New Brand World: 8 Principles for Achieving Brand Leadership in the 21st Century*. New York: Viking, 2002.

From 1995 to 1998 Scott Bedbury was senior vice president of marketing at Starbucks and prior to that, the head of advertising at Nike. Need I say more? A thought-provoking book on the power of brand—what your company represents. Just maybe your most important product is your brand. (ISBN 0-670-03076-7)

Heskitt, James L., W. Earl Sasser, and Leonard A. Schlesinger. *The Service Profit Chain*. New York: Free Press, 1997.

Using Southwest Airlines, Ritz-Carlton, Taco Bell, and others, these three Harvard Business School professors irrefutably establish the link between employee satisfaction and customer satisfaction and loyalty and profits. This book from the logistics and marketing worlds confirms the role of values, people-centric cultures, and employee satisfaction in driving business results. (ISBN 0-684-83256-9)

Kotler, Philip. *Kotler on Marketing*. New York: Free Press, 1999.

Northwestern University's dean of marketing with over 15 books to his credit. He views marketing as a competitive advantage and a disciplined strategy. Thought-provoking and it will change your view. (ISBN 0-68-85033-8)

Sheth, Jagdish N., and Rajendra S. Sisodia. *The Rule of Three: Surviving and Thriving in Competitive Markets*. New York: Free Press, 2002.

Ed's friend, Jag Sheth, has produced the theory that in every industry, three companies will dominate a market. The authors give hope to small firms who specialize and who do not get too big to become a target of the Big 3. (ISBN 0-7432-0560-X)

Articles

The most consistent source of high-quality business articles written for the business person is the *Harvard Business Review*. Some favorites follow:

Collins, Jim, "Level 5 Leadership: The Triumph of Humility and Fierce Resolve," *HBR*, January 2001, 66–76.

Good to Great, the # 1 best selling business book of the last ten years busted the myth about leaders of great businesses. No, they are generally not charismatic larger-than-life heroes. They are humble, passionately-focused people.

Collis and Montgomery, "Creating Corporate Advantage," *HBR*, May/June 1998, 70–83.

How do you align your strategy, structure, control processes, and human resources to maximize your chances of success? Three different models are discussed based on Tyco, Sharp Electronics, and Newell Rubbermaid.

Couter, Diane L., "Sense and Reliability—A Conversation with Celebrated Psychologist Karl E. Werck," *HBR*, April 2003, 84–90.

Ed heard Karl Werck talk in February 2005 at one of my conferences about high reliability organizations, and in 30 minutes he added a whole new dimension to his thought process. Successful organizations not only reward values they cherish, they also focus on non-desired behaviors. This article discusses high reliability organizations like air traffic controller teams, fire fighters, and emergency room personnel.

Drucker, Peter F., "Managing Oneself," *HBR*, March/April 1999, 64–74.

A wonderful article about the toughest management job in the world—managing yourself. Most people do not spend the time to assess themselves and put themselves into position to play to their strengths. Drucker's "mirror" test is a good one for any leader, parent, or partner.

Magretta, Joan, "Governing the Family-Owned Enterprise: An Interview with Finland's Krister Ahlstrom," *HBR*, Jan-Feb 1998, 112–123.

A thought-provoking interview with the non-family CEO of a large multi-

generational family business dealing with issues of governance, the different roles family members play, how to keep the family connected to the business, the roles of Family Councils, and a Family Values Statement.

Miller, Warren D., "Siblings and Succession in the Family Business," *HBR* Jan-Feb 1998, 22–36.

Three family members vying to be the successor CEO is the recipe for disaster. This Harvard case study is illustrative of the problems of having too many family members working in the business. Four outside experts present their advice. Some practical, some not.

Pearson, Andrall E., "Tough-Minded Ways to Get Innovative," *HBR*, August 2002, 117–124.

The former President of Pepsi Co. has more good advice in these seven pages than most books have. He demystifies innovation and growth.

Porter, Lorsch, Norhia, "Seven Surprises for New CEOs," *HBR*, October 2004, 62–72.

A good article for new CEOs of both public and private companies—and yes, family businesses. Generally, CEOs overestimate how fast and how much they can impact an organization. Lessons to be learned—do not think it is about you, and do not lose touch with the line employees and customers.

Rogers, Holland, and Haas, "Value Acceleration: Lessons from Private Equity Masters," *HBR*, June 2002, 94–101.

Private equity firms have an expertise in buying firms, operating them for a few years, and either doing an IPO or selling the business at a very good return. Why can these financial engineers run businesses better than management? The authors of the consulting firm, Bain & Company, studied 2,000 private equity transactions and came away with four key managerial principles that can apply to your business, too.

Slywotzky, Adrian J., and Richard Wise, "The Growth Crisis and How to Escape It," *HBR*, July 2002, 72–83.

In the decade of the 1990s, less than 10% of the public companies grew their revenues 10% or more in eight or more years. Consistent top-line growth is hard. What works? Geographical expansion, acquisitions, price increases, innovation? Their answer lies in your existing customer relationships.

Special Issue: "Inside the Mind of the Leader," *HBR*, January 2004.

Buy this whole journal. It contains good articles by Warren Bennis (*Geeks and Geezers*), Daniel Goleman (*Primal Leadership*), Colleen Barrett of Southwest Airlines, and David Gergen.

Ed uses "When Followers Become Toxic" by Lynn R. Offerman in his leadership classes to discuss "Yes People" and "Corporate Suck-Ups."

Information Portals

1. *Entreworld.org* is the information portal of the Kauffman Foundation. Its content is broken down into three parts: starting your business, growing your business, and supporting entrepreneurship. Starting your business has nine subtitles:

    - You, the Entrepreneur
    - Market Evaluation
    - Product/Service Development
    - The Right People
    - Finances
    - Marketing and Sales
    - Legal and Taxes
    - Technology
    - Special Interest Groups

    Under each subtitle are 3 to 7 content areas.

    Likewise, growing your business has nine subtitles with 3 to 10 content areas. Critical new ones are accessing capital and growth strategies.

    The Entrepreneur Search Engine has a wealth of information listed under:

Academic Materials, Organizations, Publications, Research, Center for Entrepreneurship, Distance Learning, and Family Business.

The Family Business section lists 32 Family Business Centers at universities with links to their sites.

2. *Fambiz.com* is the family business portal of Northeastern University. It has a good article search feature.
3. *Ffi.org*, Family Firm Institute, is a consultant organization that publishes *The Family Business Review*.
4. www.kennesaw.edu/fec (Cox Family Enterprise Center) is run by Ed's friend, Joe Astraclan. He is the editor of *The Family Business Review* and Cox published family business cases.
5. www.knowledge.wharton.upenn.edu is a good, free information source from top-ranked Wharton Graduate Business School.
6. www.gsb.stanford.edu is the Stanford Knowledgebase and a good, free information source about business thought leadership. Stanford's Executive Education site has an outstanding catalog of speeches on CDE for reasonable prices.

Author's Commentaries

These commentaries were written by Ed Hess for private company CEOs and owners, and the content is explained in the titles. These commentaries can be found on his web site: www.EDHLTD.com.

"10 Keys to Raising Growth Capital," *The Catalyst*, April 2004.

"Are Your Employees a Means to Your End?" *The Catalyst*, May 2004.

"Blocking and Tackling," *The Catalyst*, December 2003.

"Corporate Social Responsibility: The Value of Business Stewardship," *The Catalyst*, October 2004.

"Do You Have a Broken Arrow Plan?" *The Catalyst*, August 2003.

"Entrepreneurial Leadership: Why Should Anyone Follow You?" *The Catalyst*, June 2003

"Entrepreneurs: Reality vs. Myth," *The Catalyst*, July 2004.

"Going Public to Get Rich: Reality Therapy," *The Catalyst*, April 2003.

"Independent Directors: Private Companies Need Them," *The Catalyst*, March 2003.

"Managing Execution," *The Catalyst*, January 2003.

"Managing the Family Business: The Golden Goose and the Sandbox," *The Catalyst*, May 2003.

"Managing VUCA," *The Catalyst*, June 2004.

"Rapid Growth: Be Careful What You Ask For," *The Catalyst*, July 2003.

"The Family Business Succession: The Duality Principle," *The Catalyst*, February 2004.

"The Family Business: The Unintended Consequences of Gifts of Stock," *The Catalyst*, January 2004.

"The ’Perfect’ Investment," *The Catalyst*, September 2004.

"The Silver Bullet of Leadership," *The Catalyst*, November 2004.

"What Do Good Leaders Actually Do? (Part I)," *The Catalyst*, September 2003.

"What Do Good Leaders Actually Do? (Part II)," *The Catalyst*, November 2003.

"What Is the Meaning of Business?" *The Catalyst*, October 2003.

"When Should Your Business Stop Growing," *The Catalyst*, March 2004.

"Why Successful Companies Often Fail," *The Catalyst*, February 2003.

Financial Times Press

Inside Front Cover

More than 5,000,000 new businesses are started each year…but 70% of them will fail. Now, two renowned experts on entrepreneurship identify the 8 "killer mistakes" that cause most business failures—and give you the knowledge, tools, and hands-on advice to avoid them, so you can build a business that *thrives*.

Unlike other books on entrepreneurship, this book focuses on the crucial operational issues associated with consistent pro.tability. You'll learn how to identify the right opportunities and customers; design winning products and services; set the right prices; overcome customer inertia; avoid common day-to-day management mistakes; .nd and keep good employees; and finally, smoothly manage growth.

Throughout, the authors draw on real life entrepreneurial experiences, case studies, and leading-edge research. There's nothing theoretical here: This is fast-paced, 100% practical advice you can use to make your business dreams and goals come true—starting *right now*.

What really makes a successful entrepreneur?
What they do, how they act…and how to .nd your best path to business success

Get the 3 "Ws" right from the start
What will you sell, who will buy it—and why will they buy it?

55 simple, indispensable rules for success
What you must know about customers, competitors, and your employees

The art and science of managing people, operations, and growth
Create processes, set priorities, maximize quality, measure people—and improve every day

Inside Back Cover

Edward D. Hess, JD, LLM, has spent most of his business life advising entrepreneurs and .nancing their business ventures. He is currently Professor of Business Administration and Batten Executive-in-Residence at the Darden School of Business, University of Virginia. He founded and led the Center for Entrepreneurship and Corporate Growth and the Values-Based Leadership Institute at the Goizueta Business School, Emory University. His books include *The Successful Family Business*, *The Search For Organic Growth*, and *The Road To Organic Growth*. He has personally built three successful service businesses. His website is www.EDHLTD.com.

Charles F. Goetz, MBA, Distinguished Lecturer in Entrepreneurship at Emory's Goizueta Business School, has built nine successful businesses in six industries. He serves on the boards of several entrepreneurial ventures and not-for-pro.ts. He recently published *The Great Entrepreneurial Divide*. His specialties are marketing, customer acquisition, and product development.

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What's Stopping You?

Shatter the 9 Most Common Myths Keeping You from Starting Your Own Business

Bruce R. Barringer, PhD
R. Duane Ireland, PhD

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To Janet, John, Jennifer, and Emily: The love and support of a family is a wonderful thing.
—Bruce Barringer

To Mary Ann: Thank you for your never-ending support, love, and nurturing for all of these years. I love you.
—R. Duane Ireland

Praise for *What's Stopping You?*

"Bruce Barringer and Duane Ireland's new book, *What's Stopping You?* is an insightful and thought-provoking examination of nine common myths that discourage individuals from starting new businesses. ... This book is much-needed and long overdue.... The value of *What's Stopping You?* is that it effectively debunks the false premises that too often preclude acts of business start up. *What's Stopping You?* is an encouraging, instructive, and eloquently written book that would be a valuable addition to any aspiring entrepreneur's bookshelf."

Jeffrey G. Covin, Samuel and Pauline Glaubinger Professor of Entrepreneurship, Kelley School of Business, Indiana University, Bloomington, Indiana

"Over the years I have observed many seemingly great business opportunities never get off the ground. Quite often, what holds these aspiring entrepreneurs back are common misconceptions about the difficulties and risks of starting a new business. In *What's Stopping You?*, Professors Barringer and Ireland systematically break down the myths that hold many entrepreneurs back from pursuing their dreams."

Jeffrey R. Cornwall, The Jack C. Massey Chair in Entrepreneurship, Belmont University, Nashville, Tennessee

"Barringer and Ireland simultaneously demystify start-up misconceptions and empower readers to explore their own opportunity with renewed passion. Many prospective entrepreneurs feel trapped by myths, the authors carefully detail the myth's fallacies and encourage the reader to see beyond start-up stereotypes. Future and experienced entrepreneurs have much to learn from *What's Stopping You?*"

Sarah Schupp, Founder/CEO, University Parent Media, Boulder, Colorado

"Creating your own business from scratch can be a mental, emotional, and financial roller coaster ride. Bruce Barringer and Duane Ireland's book provides a 'voice of reason' and helps give you the confidence to realize you can do it. They recognize that starting a business is hard work, but that it is attainable—and that you should celebrate your accomplishments every step of the way."

Jan Stephenson Kelly, Cofounder/CEO, Spark Craft Studios, Cambridge, MA

About the Authors

Bruce R. Barringer, PhD is an Associate Professor at the University of Central Florida. The author of two small business/entrepreneurship textbooks, Barringer's work is read worldwide. He is also the author of the *Wall Street Journal's Entrepreneurship Weekly Review*, which is distributed to small business and entrepreneurship teachers and students across the United States.

R. Duane Ireland, PhD is Professor of Management and holds the Foreman R. and Ruby S. Bennett Chair in Business in the Mays Business School at Texas A&M University. He is the author of entrepreneurship and strategic management textbooks that are widely sold throughout the world. He teaches entrepreneurship to executive MBA students and has consulted with a variety of small and large organizations.

Preface

Have you ever caught yourself daydreaming while at work and wondering if what you’re doing is all you’ll achieve in your career? Or has your heart ever ached to meet a certain desire, like completing work that you truly enjoy, being your own boss, making more money, or being home when your kids get out of school?

These types of thoughts and desires confront people every day—even those with seemingly perfect jobs. In response, most people just sigh or shrug and accept life as it is. But not always. A growing number of people from all walks of life are starting their own businesses as a way of improving their lives. In fact, there are roughly 15 million self-employed people in the United States today. But there is a problem. The problem is that because some business owners have hit it rich and made a large impact on society, there is a growing tendency to view business owners as bigger-than-life and place them in the same category as professional athletics and rock stars. This tendency has led to the prevailing wisdom that starting a business is an extremely difficult task and that a person must have "loads of money" and "tons of talent" to get a new business off the ground.

While it’s true that some businesses are difficult to start and that talent and money are needed to get a business off the ground, many of the tales and perceptions about the enormous difficulties associated with starting a business are just myths. The truth is that the ability to start a successful business is much more within the average person’s reach than the myths allow us to believe. If you have the interest it took to pick up this book, chances are you have the talent, the money, and the character needed to start and run a business of your own.

Who Is This Book Written For?

This book is for anyone who has thought about starting his own business but has been reluctant to try. This group covers a wide spectrum, from people who have an idea for a new business but are uneasy about leaving their current jobs to people who are dissatisfied with their jobs or careers but feel trapped. It also includes people who have a goal or want to live a particular lifestyle and see starting a business as the most reasonable way to make it happen.

Although some people do start businesses, most of the people in these categories think about it occasionally but set their thoughts aside because of the anxiety and worry caused by the nine myths that we discuss in the book. It's hard to blame them. Listen to the first three myths and ask yourself if they would discourage you from starting a business: Myth 1: It takes an extraordinary person to start a business; Myth 2: Starting a business involves lots of risk; Myth 3: It takes a lot of money to start a business. Pretty daunting list, isn't it? And there are six myths to go!

A potentially rewarding part of reading this book are the many people you meet that objectively aren't any smarter, richer, or more gifted than you. What they do have that you probably don't is a successful business startup. As we progress together through the chapters of the book, we knock off the myths one by one by showing how ordinary people prove that they simply aren't true. But there are exceptions. In most cases, it does take an extraordinary person and lots of money to launch a biotechnology, a medical products, or a semiconductor firm. But these cases, by far, are the exception rather than the rule. You'll be amazed what people are able to accomplish with very little money and the simple common sense that is the foundation on which many of the business startups described in this book were built.

What Will You Learn by Reading This Book?

Next time you go to a bookstore or are in an airport gift shop, try this little experiment: Spend a few minutes watching people browse through the business magazines or books. Watch their faces and try to guess what their circumstances are. If you're like us, in the majority of instances, you'll get the feeling that they're looking for answers. There is some problem or unmet need in their personal or professional lives that they'd like to resolve but can't figure out how to on their own. So they're scanning the books for potential answers. If you conduct this experiment long enough, we can almost guarantee you that you'll see the ultimate example of this scenario play out. Someone will be scanning the shelves of business books and will come across a book that immediately catches her attention. The person will then intently page through the book for a few minutes, in a state of total concentration, and a slight sign of hope or relief will gradually start to cross his or her face. As the person proceeds to the checkout counter, he or she will be clutching the book as if it were a $1,000 bill. You can't help but hope, for that person's sake, that his or her question has just been answered.

This experiment is a reminder of how desperate people are for answers to the problems or challenges in their lives and how much hope, information, and potential help books can offer. If you're reading this preface, you're probably tired of your job, want to make more money, desire to pursue the career you have always wanted, or are thinking about starting your own business for a reason equally important to you. What's stopping you, if you're similar to most of the people we talk to, is a lack of knowledge about the business startup process and nervousness about one or more of the topics covered by our nine myths. This set of circumstances leads to a lack of self-confidence, which researchers believe is the number one reason that people hesitate to start their own firms.

What you will learn by reading this book is the truth about many of the most important aspects of starting a business. Our goals are to educate you and stir your emotions. We hope that as you read the book, you'll pause from time to time and think to yourself, "That's interesting—perhaps I have been too quick to dismiss the idea of starting my own business." We also pledge that the stories will be compelling enough that you'll stop occasionally to excitedly tell a coworker or friend things like, "Do you know it's not true that nine out of ten new businesses fail?" (In truth, 66% of new businesses are still operating after two years, and 50% survive four years or more.) Or you'll want to share stories such as, "You won't believe how this woman I just read about quit her job as a general partner in an investment firm to buy an adventure travel company. She didn't do it because she could make more money—she did it to lead a more satisfying and enjoyable life."

How Is This Book Organized?

The book is organized into nine chapters—one chapter for each of the nine myths. Each chapter starts by stating the myth and the corresponding truth and is followed by a complete discussion of the chapter's topic. Each chapter contains two to three special features that add to the material in the chapter. Although the book is admittedly upbeat, we paint a realistic job preview for those who are thinking about becoming a business owner. We want people to be realistic about their prospects, but we also want them to be confident and to think, "I can do this. It's not beyond my reach."

We now invite you to enjoy learning about the myths associated with starting your own business and to learn from the lessons in this book. If you are inspired by a particular story in the book, if you would like to tell us your startup story, or if you are impacted by this book in any way, please feel free to e-mail us your story at story@mythsbook.com. We would love to hear from you. Much of what we know we learn from people just like you. We’d love to consider including your story in future books as we work together to dispel the myths and reveal the truth about the business startup process.

Part I: *Getting Started—It May Not Be as Hard as You Think*

Chapter 1. Myth No. 1: It Takes an Extraordinary Person to Start a Business: Truth No. 1: You Can Do It!

Introduction

The notion that it takes an extraordinary person to start a business is the most damaging myth that we discuss in this book. In most cases, it simply isn't true. There are two ways to think about this myth. First, ordinary people, no richer or smarter than you, start new businesses every day. To convince you of this, we'll introduce you to some of these people in this chapter and throughout the book. Second, even if the myth were true, who's to say that you're not extraordinary? No one has the exact same set of abilities, skills, values, experiences, past accomplishments, and personal aspirations that you do. As a result, you could be more uniquely qualified or have a more compelling reason to start a specific business than someone with a PhD from an Ivy League school or 20 years of executive work experience.

If you accept that these sentiments are true, it can totally transform your attitude about whether you're capable of starting a business. It can free you to start thinking about whether specific business opportunities are right for you rather than whether you're capable of starting a business at all. It can also boost your morale and sense of self-esteem. Starting a business isn't easy, but neither are many things in life that are worth pursuing. The brutal reality of life is that in most instances what we're able to accomplish boils down to whether we believe we can do it or not, the amount of encouragement and support we get, and the degree to which we're willing to work hard and get help. As you'll see throughout this chapter, there is no aspect of life in which this set of realities is truer than in the case of starting your own business.

The differences between people who start their own businesses from those who don't has been studied for years. The somewhat surprising collection of results illustrate that there are no meaningful differences between business owners and nonbusiness owners in the most basic human characteristics, behaviors, attitudes, and desires.[1] Most people, for example, want to make more money and crave independence, not just people who start their own businesses. Similarly, in regard to personality traits, people who start their own businesses are just as diverse as people who work in traditional jobs. You don’t have to have a certain personality, behave in a particular way, or have a certain set of motives or desires to be a successful business owner.

What type of person, then, do you have to be to start and run your own successful business? Say you’re a 50-year-old male whose career has plateaued, and you see no chance for advancement, or you’re a 28-year-old female with two small children, and it literally breaks your heart to drop them off at daycare five mornings a week. What type of people are able to say, "Stop, I’m not doing this anymore. There is another option—I’m starting my own business to take control of my life, set my priorities straight, and do something that makes sense for me and that I’ll be able to thoroughly enjoy."

The myth that "it takes an extraordinary person to start a business" is damaging in part because it focuses strictly on the individual. If you believe it, it puts the entire burden on you, rather than the broader set of circumstances and issues involved. It causes you to think, either consciously or subconsciously, "Am I good enough?" or "Do I have what it takes?" Thinking this way invariably leads to an up or down vote in your mind—you decide, once and for all, whether you’re good enough or not good enough to start a business based on your notion of what an "extraordinary person" is. This type of thinking is fundamentally flawed. Objectively, most of us don’t know if we have the skills, abilities, aptitude, and experience necessary to tackle a specific task or do a particular job unless we learn more about it (or have done it or something similar to it before). In addition, nearly all of us would seek the advice of others and ask their opinions about our suitability for a particular business or career before making the final decision to start our own businesses. In some cases, we may even decide to go back to school or get additional training if we’re interested in a particular area but don’t think our skills are sufficient. So in reality, the issue of whether you’re good enough to start a business doesn’t depend just on *you* at a fixed point in time. It depends on a lot of things. Primarily, it depends on the *fit* between your skills, abilities, experiences, and aspirations and the demands of the particular business you have in mind. It also depends on whether you really *want* to start a business or not.

There are basically four types of businesses, as shown in Table 1.1.

Table 1.1. Types of Businesses

Type of Business	Explanation	Examples
Survival	A business that provides its owner just enough money to put food on the table	Handyman, lawn service, part-time childcare and pay bills
Lifestyle	A business that provides its owner the opportunity to pursue a certain lifestyle and make a living at it	Home-based eBay business, sub-shop, single-unit franchise, clothing boutique, personal trainer
Managed Growth	A business that employs 10 or more people, may have several outlets, and may be introducing new products or services to the market	Multi-unit franchise, regional restaurant chain, Web retailer (modest scale)
Aggressive Growth	A business that is bringing new products and services to the market and has aggressive growth plans	Computer software, medical equipment, Web retailer (large scale), national restaurant chain

All these types of businesses are acceptable—there is no value judgment made here. This book, however, focuses on the last three: lifestyle, managed growth, and aggressive growth firms. A natural outcome of the myth that it takes an extraordinary person to start a business is the mistaken belief that every business should grow rapidly and make a lot of money. There are many small businesses that provide their owners financial security and satisfying lives and never grow or make tons of money. This book equally targets this type of business along with more aggressive growth firms.

In our experience, at least four primary factors prompt and motivate people to start their own business. As you read through these factors, tip your chair back from time to time and think about your own life and the degree to which each of these factors might play a role in your own decision to start a business. Pay particular attention to the examples of people who left traditional jobs to start their own businesses and the reasons they made the decisions they did.

Factors That Prompt and Motivate a Person to Start His or Her Own Business

The factors that prompt and motivate people to start their own businesses are shown in Figure 1.1. A person's decision to start a business is both practical and personal. It's practical in that the decision is based partly on a simple calculation of whether a person can better manage her life and meet her aspirations and goals through a traditional job or by owning a business. It's personal in that the decision also hinges on whether a person believes she is capable of owning a business or not, whether she has the support of the most important people in her life, and the degree of passion she has for a particular business idea.

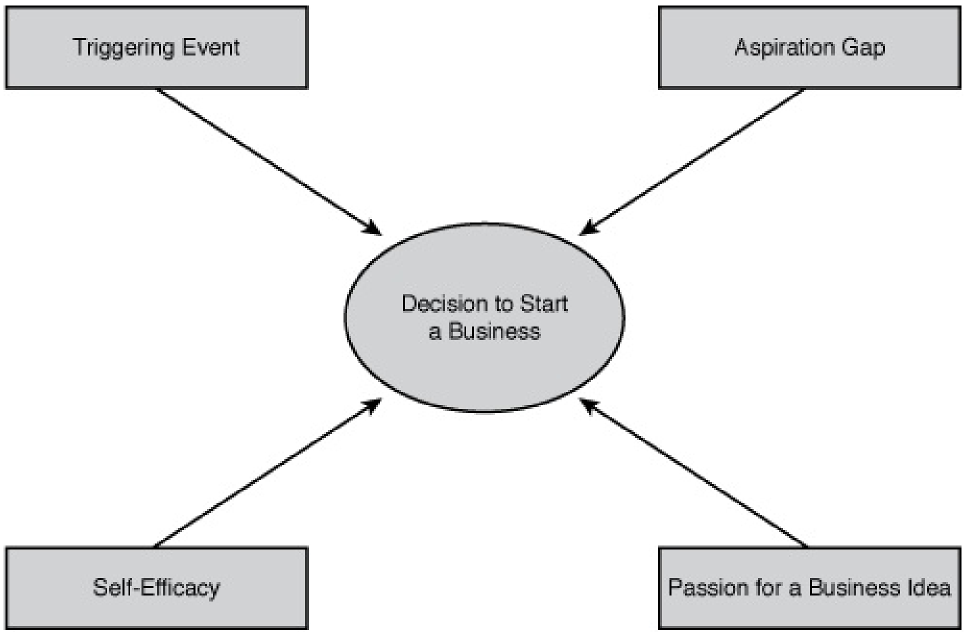

Figure 1.1. *Factors That Prompt and Motivate a Person to Start His or Her Own Business*

Let's look at the four factors that prompt and motivate someone to start a business.

Triggering Event

There is almost always a triggering event that starts someone thinking about starting a business. A triggering event can be getting a business idea, either by deliberate search or chance encounter, or it can be any incident or occurrence that has an impact on a person and causes him to think about making a major life change—like changing a job or career. Examples of triggering events, which can be either positive or negative, are shown in Table 1.2.

Table 1.2. Triggering Events

Positive	Negative
New business idea	Job loss
Birth of first child	Passed up for a promotion at work
All children are now in school	Need to transfer to a less desirable location
Last child has left home (empty nest)	Undesirable changes at work
Inheritance	Serious health issue
Personal milestone (40th birthday)	Death in family
Retirement	Major national trauma (9/11)

For many people, the types of events shown in Table 1.2 have little impact, at least as far as their jobs or careers are concerned, and don't trigger any reaction. For others, one or more of these events might be deeply impacting and cause them to seriously consider making changes in their lifestyles and careers.

An example of how an event can trigger a major change in a person's life, which leads to the decision to start a business, is provided by Sean Tennant, a middle-aged male. After a 20-year career with Delta Airlines, Tennant had to decide whether to take a pay cut to stay in Boston or transfer to Atlanta, a Delta hub. "I had to make a decision whether to go and get a cheap buyout (equivalent to three months' salary) or stay with a sinking Titanic and get nothing," Tennant recalls.[2] He decided to leave Delta and buy a Cartridge World franchise. Cartridge World is a rapidly growing franchise organization that refills ink cartridges for about half the price a new cartridge costs. An added benefit of owning a Cartridge World franchise, from Tennant's perspective, is that it encourages people to recycle ink cartridges rather than replace them, a practice that appeals to his sense of environmental stewardship. Tennant now owns and runs a busy Cartridge World franchise and indicated that his business started breaking after only four months.

Sometimes a Trigger Event Must Wait Until the "Timing Is Right" for a New Business to Be Launched

Although the term "triggering event" implies that an event immediately triggers a person's interest in starting a business, that doesn't mean the business starts right away. Sometimes people mull over the impact of an event for some time, or there are other reasons why the business might not start immediately. This happened to Dave Long, one of the cofounders of Screen Life, the company that makes the popular DVD board game, Scene It?, a game in which players answer trivia questions about films or pop culture.

In 1992, Long and his wife, Kelly, hosted a Halloween party in their San Diego home. To do something different, Long came up with the idea of putting together a videotape that featured scenes from various Halloween-themed moves. Short scenes played until someone shouted out the title of the film. The game was a hit. The next day Long and his wife got together with two of their guests from the night before to talk about converting the idea into a commercial product. Unfortunately, they quickly discovered an insurmountable obstacle—the linear nature of the VHS format. It's not possible on a video tape to quickly jump from scene to scene or to stop a scene (when someone gets the right answer) and quickly move to the next scene. They decided to shelve the idea until technology provided a better solution.

In October 2000, Long bought a DVD player, and all of a sudden his idea of eight years prior didn't seem so far-fetched anymore. The DVD format allows for much more flexibility than video tapes by allowing users to jump from scene to scene quickly and conveniently. Long partnered with Craig Kinzer, a game enthusiast, and after some experimentation and lots of help from others, Scene It? was born. They formed their new company and introduced the game to the marketplace in 2002, 10 years after the Halloween party where the whole idea began.[3]

Aspiration Gap

The second factor that prompts people to begin thinking about starting a business is the presence of one or more aspiration gaps in their lives. All of us have aspirations, which are made up of our most important goals, objectives, ambitions, desires, and longings. Our aspirations vary because they are influenced by our values, abilities, experiences, families, jobs, and individual circumstances. When one or more of our aspirations are unmet, we have *aspiration gaps* in our lives. The extent to which an aspiration gap prompts someone to take action, to try to eliminate or narrow the gap, varies based on the importance of the aspiration and the individual involved.

Collectively, our aspirations form what researchers call our *aspiration vector*, which is the sum total of all of our aspirations. Sometimes, our aspiration vectors can get complex, particularly during busy times in our lives, like when we're simultaneously trying to build a career, love our spouse, raise kids, save money, stay fit, and so forth. For people who have strong aspirations and are insistent that certain aspirations are met, their aspirations become the motivating or driving factors in their lives. For example, a young mother might have the following three aspirations regarding a job that are particularly important to her: pays at least $40,000 per year, has her home by 3:00 pm on weekdays to meet the school bus, and allows her Sundays to be free to participate in church and volunteer-related activities. Similarly, an Assistant Manager for a large retail chain, like Target or Lowe's, might be driven primarily by the single aspiration of having his own store to manage and run by the time he is 35.

A person can become discouraged or upset when he or she looks at his or her job or alternative jobs in the traditional labor market and concludes that none of the choices will allow his or her most important aspirations to be met. In these instances, a logical alternative is to start a business. Although starting a business isn't easier than a traditional job, a business owner often has more discretion and control over his or her time and schedule. This rationale explains in part the recent jump in the number of home-based businesses. Home-based businesses often help people better juggle both professional and family-related goals and aspirations.

Daryn Kagan, a former reporter for CNN, become discouraged with her career trajectory and decided to leave the cable network to do something she had thought about for a long time, create a Web cast (a streaming video on a Web site) that features good news.

> *"After 12 years at CNN, it became clear that I wasn't going to have the kind of opportunities that I wanted. I see that as the nudge I needed to move on. I had been thinking of some version of this (business) for a long time. These are the kind of stories I have been drawn to—the kind that make your heart go zing. It was one of those moments in your life where you have a chance to sit back and think, 'If I could do anything in my life, what would it be?'"*[4]

After leaving CNN, Kagan eliminated her aspiration gap and fulfilled her ambition by launching darynkagan.com. If you'd like to see the fruits of her efforts, you can go to her Web site and view her daily "good news" Web cast. The stories she posts are both heartfelt and inspiring.

An example of three people who shared an aspiration gap and eliminated it by starting a business together is the story of Christopher Jones, David LaBat, and Mary McGrath. The three, who are educational psychologists, had secure jobs at a public school in the Santa Clarita Valley, north of Los Angeles. Over time, they felt inhibited by the limited range of services they were able to provide students in a school setting; so they left their jobs to start Dynamic Interventions, a more full-service educational psychology and counseling center:

> *"The idea came from some general frustrations with not being able to practice the breadth of service that [we wanted to]," Jones said. "And instead of going to work and being angry about it for the next 30 years, we decided to do something about it. With Dynamic Interventions, our service doesn't stop at the end of the school day. We can go more in-depth and be more beneficial to the whole family."*[5]

Dynamic Interventions now offers a full range of educational and counseling services for school-aged children and their families.

A final example is Kristina O'Connell, who experienced a triggering event and an aspiration gap at the same time, which led her to start Wadee, an online company that sells handmade children's toys and gift items. A former high-tech marketing executive, O'Connell comments on the set of circumstances that motivated her to start her own business:

> *"In 2000, I lost both my parents. That, on top of the fact that I started having children, changed my perspective. It made me realize how short life is, so you've got to do what you love. I had run out of gas with high-tech and was burnt out, so at the end of 2002, I decided to take a couple of years off and start Wadee. I wanted to be home with my family, so I built my business around my family. My husband has been tremendously supportive, and that has allowed me the freedom to follow my passion."*[6]

Even though she was a successful high-tech executive, O'Connell had a long-time interest in starting a company to make children's toys. That interest, or aspiration, coupled with the loss of her parents and the start of her own family, provided her the necessary motivation to set her high-tech career aside and fulfill her aspiration to launch her business.

Self-Efficacy

A third factor that prompts people to start their own businesses is *self-efficacy.* Self-efficacy is similar to self-confidence and refers to the strength of a person's belief that he or she is capable of successfully completing a task.[7] A person generally avoids tasks where his sense of self-efficacy is low and engages in tasks where self-efficacy is high. It’s important to understand the distinction between self-efficacy and self-esteem. Self-esteem refers to a person’s overall sense of self-worth, whereas self-efficacy refers to a person’s ability to complete a specific task. As a result, a person could have a very poor self-efficacy for performing a specific task, like playing golf, but still have a very high self-esteem, if playing golf isn’t an activity that’s very important to the person’s overall sense of self-worth.

The result of this rationale is that a perfectly normal person with a healthy sense of self-esteem could have very low self-efficacy for starting a business. Low self-efficacy often leads people to believe that a task is harder than it is. It also affects how a person deals with a task. Individuals with high self-efficacy for a given task, like starting a business, usually approach it with enthusiasm and drive, while people with a low self-efficacy for the same task approach it with skepticism and dread.[8] This is why some people, even though they often think about starting their own businesses, have never done it. Deep down inside, they believe that they don’t have the skills and abilities to start and run a successful business.

Four factors that affect a person’s self-efficacy for starting a business (or performing any task) are explained in Table 1.3: experience, modeling, social persuasions, and physiological factors. A person can increase his or her self-efficacy for starting a business by strengthening themselves in one or more of these areas. Simply reading the stories of ordinary people who start and run successful businesses is one form of modeling (or vicarious learning) and can provide you with the sense that "If they can do it, I can do it, too!" Similarly, participating in small business workshops and events where you get encouragement from successful business owners, who are no smarter or more capable than you, can boost your self-efficacy for starting a business of your own.

Table 1.3. Factors Affecting Your Self-Efficacy in Starting a Business

Factor	Explanation
Experience	Experience starting a business or working in a field closely related to the business that you are interested in starting boosts your self-efficacy.
Modeling	Also called vicarious learning. Refers to the extent to which you are acquainted with people who have started successful businesses—either by reading about them or observing them directly. The more you see yourself as similar to these people, the more positive impact knowing them has.
Social Persuasions	The degree to which people encourage or discourage your interest in starting a business directly affects your confidence regarding whether you can do it.
Physiological Factors	How you feel physically when you think about starting your own business. Anxiety and stress lower self-efficacy; excitement and enthusiasm increase it.

J.J. Matis, a successful business owner, affirms the importance of vicarious learning through reading about others. Matis started a company called J.J. Creations which designs, manufactures, and sells a line of backpacks, travel bags, book bags, and similar items primarily for sports fans. In 1999, she looked for something that she could use to carry her water bottle, peanuts, binoculars, and radio when going to a Los Angeles Dodgers game. When she couldn't find anything out of the ordinary, she created a bag herself (she had been sewing since she was a teenager) that looked like a baseball. At the game, she was inundated by people asking her where she got her bag, which prompted her to think that she might be onto a business idea. She took her idea to Mike Nygren, the merchandising manager for the Dodgers. Nygren encouraged her to make some additional samples and incorporate the project into her MBA program at California Lutheran University. After receiving her MBA, Matis started her business, which took considerable persistence and will. The business now sells bags for a variety of sports teams, politicians, and rock groups. Her "flag-bags" are even featured in the Senate Gift Shop on Capitol Hill in Washington, D.C.

Matis later wrote:

> *"After being a Featured Lady on LadiesWhoLaunch.com in April 2004, I received numerous emails from readers who felt inspired by my story of turning my graduate project into a business. Mostly, their emails expressed how they're planning on starting a business and by reading my story of perseverance and tenacity, they're going ahead with pursuing their ideas for starting a business. It inspires me when people express that I've inspired them!"*[9], [10]

Dealing with Loneliness by Creating a Support Network and Having Faith in Yourself

One thing that surprises many new business owners is that they miss the hectic pace and the busyness of the work environment that they left, where they had frequent interactions with coworkers and others. Many new business owners work alone, especially if they work out of their homes or garages. This type of lifestyle can be lonely, and can be hard to get used to, particularly if you’re a "people person" and enjoy frequent interaction with others.

There are at least a couple ways to overcome this challenge. The first is to create a support structure, not just to get business advice, but to have people to interact with and talk to on a regular basis. Brian Magierski, the founder of Kalivo, a company that helps other companies engage with their customers using the latest Internet technologies, said to new business owners:

> *"It’s tremendously rewarding and difficult. You really have to have a sense of purpose about it if you’re going to buy into it, because you are generally out on your own. That’s part of the appeal of it, but it’s also part of what makes it difficult to do as well as frightening to do in some respects. Be prepared for that and create a great support structure behind you whether that’s your spouse or your network of friends, because you’re going to need it to get through the tough early days."*

A second way that business owners can overcome loneliness and prop themselves up is through simple patience, self-confidence, and faith in themselves. These attributes come with maturity and belief in a business idea and are particularly important when not only loneliness, but the exact path the new business will take, is still unclear. Jeff Reifman, the founder of NewsCloud, a social networking site for people interested in news, says:

> *"I primarily work alone. I have a couple of people I work with, but they’re more hourly. These days, I work out of a coffee shop. It’s a tough lifestyle. And I think most entrepreneurs who work out of their homes or their garages, they sort of know that early stage.*

What's hard about this is when you don't have a model that is ready where you see that there's a plan in front of you, and you're sort of meandering towards experimenting. It's harder to know when that cycle ends. And so, you have to have a lot of faith in yourself, a lot of patience. I say that, as an entrepreneur now as opposed to 10 years ago, I think patience and self-confidence are the qualities that really help me now."[11]

Passion for a Business Idea

A fourth factor that prompts people to start their own businesses is passion for a business idea. What often happens is that a person gets an idea for a new product or service, and there is no practical way to bring the idea to market other than starting a new business. In these instances, a person's willingness to quit her job or start the business part-time often hinges on how passionate he or she is about the product or service idea.

In many cases, a person's passion for a business idea stems from the belief that the idea will positively influence people's lives. This sentiment guided Benjamin Troget, cofounder of Kepner-Tregoe, a management consulting firm. He said:

> *"Tremendously important to me was the feeling that we were doing something that had a significance far beyond building a company or what the financial rewards could be. I was convinced we were doing something that had tremendous importance in the world."*[12]

This level of passion explains why billionaires like Bill Gates of Microsoft, Steven Jobs of Apple, and Larry Page and Sergei Brin of Google continue working after they are financially secure. They strongly believe that the product or service they are selling makes a difference in people's lives and makes the world a better place to live. It also explains why many owner-operated businesses do well in spite of stiff competition. If a business owner is willing to work long hours and commit himself or herself passionately to see a business succeed, that's a combination that's hard to replicate in a regular firm.

An example of the pervasive role of passion in conceiving and launching a new business is provided by John Plaza, the founder of Seattle Biodiesel, a company that makes biodiesel, an environmentally friendly substitute for regular diesel fuel. Plaza, a former airline pilot, quit his job flying commercial airplanes to pursue an interest in alternative fuels. A single flight sparked his passion for environmental stewardship and caused him to decide to make a career change:

"I was flying a 747 from Anchorage to Tokyo, and I started thinking about how much fuel that flight used. I figured out that in a 6 hour flight, we used enough fuel to power my personal vehicle for 42 years. I had to make a change."[13]

The change Plaza made was to start Seattle Biodiesel. To get the business off the ground, Plaza mortgaged his home, sold his boats and cars, and borrowed money against his 401(k). Taking financial actions such as these are common for entrepreneurs who are passionate about their ideas.

How a Father's Attempt to Help His Infant Daughter Through a Health Crisis Ignited Passion for a Business Idea

In 1992, Kenny Kramm's second daughter, Hadley, was born premature. As an infant, she developed a medical disorder that required her to take medicine four times a day. The medicine tasted awful, and Kramm and his wife had a hard time helping Hadley keep it down. The Kramms grew increasingly concerned. Every time Hadley didn't keep down a full dose of the medication, her condition worsened. "We were ending up in the emergency room on a weekly basis," Kramm recalls. While her situation grew more desperate, Hadley's doctors and nurses could do little more than urge the Kramms to help Hadley keep her medicine down—in any way they could.

Kenny Kramm, who worked in his parents' pharmacy, started experimenting with concentrated flavors that could be mixed with Hadley's medicine to mask its bitter taste. Eventually, he and his father produced a banana flavor concentrate that they were able to safely mix with the medicine, and were elated when Hadley started accepting the flavored medicine. Almost immediately, her condition stabilized, both medically and emotionally.

Over the next three years, Kramm and his father continued to experiment with adding flavors to Hadley's various medicines. Gradually, Kramm started seeing his pursuit as a business idea. Surely many other parents faced the same challenge that he and his wife had faced with Hadley, he thought. In 1995, he decided to incorporate and named the business Flavorx. To move the business forward, he partnered with one of the largest flavoring companies in the world to help develop custom flavors that could be safely mixed with medicines. After months of testing, Flavorx’s first additives were formally approved.

Flavorx’s additives are now available in most pharmacies in the United States and are frequently used to improve the taste of both child and adult medicines. As for Hadley, her father’s solution was just what she needed. From the time she took her first dose of banana-flavored medicine, she has never had another medicine-related hospital visit.[14]

The payoff that many business owners receive from their hard work and passion is the level of extreme satisfaction they experience as they work in their businesses every day and watch customers benefit from the products or services they sell. Joy Pierson, the founder of Candle Café and Candle 79, two restaurants in New York City, is such a person. Her restaurants serve organic and vegan food, which provide options to people who not only prefer a certain diet, but have strict dietary restrictions because of allergies or other health concerns. Pierson said her greatest success is...

> *"...the opportunity to touch people’s lives in a profound way through feeding them. We offer menus for people with Celiac disease, who cannot tolerate wheat. One day a child with Celiac disease dined in our restaurant. She was about nine years old and had never been to a restaurant before...she couldn’t risk the possibility of cross-contamination from wheat products. She and her family were thrilled that they were able to experience being in a restaurant together to celebrate a special occasion."*[15]

A similar example is Lubna Khalid, the founder of Real Cosmetics, a company that creates make-up and skin-care products for women of all nationalities and ethnicities. Khalid started Real Cosmetics as a result of her own personal frustration in not being able to find products and colors for her skin tone. Khalid said:

> *"What I love about this business is the opportunity to create something new, different, and innovative and the chance to create images and colors that work on a range of skin tones. The other day, we did a photo shoot using seven different models who were women of all different backgrounds. It was incredibly satisfying to produce this shoot and experience the culmination of all my ideas."*[16]

One aspect of passion is that it is often used as a proxy by others to determine how committed an individual is to starting a firm and seeing it through. Tom Simpson, an investor who passed on the opportunity to get in on the ground floor of Starbucks because he couldn't see how anyone could make much money selling coffee said, "I missed and completely discounted all the passion that Howard Schultz had and what he was going to set up (and how he planned) to accomplish his goals."[17] Simpson now says that when he meets a team (of prospective business owners), he watches to see if their eyes light up when they make their presentation for funding.

Additional examples of how business owners view passion are shown in Table 1.4.

Individual and Business Started	View on the Importance of Passion
Jared Ross VENA-Fine Italian Takeout Italian Food Toronto, Canada	My MBA has been invaluable in so many ways. However, one thing business school doesn't teach is how to prepare for the less glamorous, humbling jobs like scrubbing the bathroom floors and driving around the city making deliveries. But it's worth it because I'm **passionate** about my business. For as long as I can remember, I dreamed of being an entrepreneur. Now my dream is a reality, and the risks are mitigated knowing that I reap all the rewards of my hard work. I love every grueling minute of it and can't wait to go to work tomorrow.
Matthew Dunn MusicIP Digital Music Monrovia, California	If you don't have a fundamental "can't walk away from it" **passion** for what you're going to do, you're probably going to have a hard time making it unless you're lucky and even if you do, you'll be tired. I'm never tired of this; I wish there were more hours in the day so that we could do this better and do it faster and do more of it.
Peter Flint Trulia.com Residential Search Engine San Francisco, California	The key is to have a **passion** and to never give up. This is imperative because it creates a drive to solve business problems.
Judi Sheppard Missett Jazzercise Fitness Franchiser Fitness and Exercise Classes Carlsbad, California	First and foremost, you must be **passionate** about what you're doing—whether you're leading a large group of people through a step class or massaging the kinks out of an individual's body. Out of **passion** develops a strong work ethic, and without it you won't succeed. Some people go into fitness careers thinking, "Oh, it will be a nice thing to do and it will keep me fit." These people don't survive because they don't have enough dedication.
Laura Gasparis Vonfrolio Educational Enterprises Educational Services Richmond, Virginia	The only entrepreneurial trait that is universal, in my view, is **passion**. I've met smart entrepreneurs, stupid entrepreneurs, but they all had **passion**. Some go into it for the fun, some to make money, some to prove a point, some because they don't want to work for anybody else, but the successful ones all have **passion**.
Ross Levin Accredited Investor Edina, Minnesota	You could build a business with anything, as long as you can find something that you can be **passionate** about. If I could have been a minister, I bet I would have built a thriving congregation.

Table 1.4. The Importance of Passion in Starting New Businesses

Summary

Ordinary people, just like you, can and do start successful businesses every day.

The irony is that many people never get the chance because they think they can't do it or they believe that only extraordinary people start their own businesses. If one or more of the factors that prompt or motivate people to start their own businesses applies to you, you may want to give business ownership more serious consideration.

The next chapter deals with the myth that starting a business involves lots of risk. While there is a measure of risk involved with any endeavor in life, it's important to think about risk holistically. If this chapter has caused you to stop and think, "Boy, maybe I should do something different with my life. I have unfilled aspirations and passions, too," your biggest risk might be to maintain the status quo, rather than to make the change that will lead to a more satisfying and fulfilling life.

One final note of inspiration. Muhammad Yunus is a Bangladeshi banker who won the Nobel Peace Prize for inventing the concept of microcredit. Microcredit is the extension of small loans to people who can't qualify for traditional financing. Yunus recently wrote a brilliant and heartfelt book titled *Banker to the Poor*. In the book, Yunus took on the myth that it takes an extraordinary person to start a business and also talked about the role of small business (or entrepreneurship) in building economic systems around the world. Yunus wrote:

> *"To me, an entrepreneur (small business person) is not an especially gifted person. I rather take the reverse view. I believe that all human beings are potential entrepreneurs. Some of us get the opportunity to express this talent, but many of us never get the chance because we were made to imagine that an entrepreneur is someone enormously gifted and different from ourselves. If all of us started to view every single human being, even the barefooted one begging in the street, as a potential entrepreneur, then we could build an economic system that would allow each man or woman to explore his or her economic potential. The old wall between entrepreneurs and laborers would disappear. It could become a matter of personal choice whether an individual wanted to become an entrepreneur or a wage earner."*[18]

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Chapter 2. Myth No. 2: Starting a Business Involves Lots of Risk: Truth No. 2: It May Not Be as Risky as You Think

Introduction

If you ask people with traditional jobs why they have never started their own businesses, a very common response you'll get is that starting a business involves too much risk. It's a natural response. In general, people are risk-averse, particularly when it comes to losing something they own or possess. For most of us, there are few things that are more important to our security and sense of self-worth than our jobs. As a result, it's not surprising that people are protective of their jobs and almost instinctively see leaving their jobs to start their own businesses as a risky proposition.

The problem with these sentiments is that they are overly protective and unnecessarily deter people from starting their own businesses. There are many people, some of whom you met in Chapter 1, who have successfully transitioned from traditional jobs to self-employment. The general notion that starting a business involves a great deal of risk is simply not true. The often battered about figure that 9 out of 10 business fail in their first few years is an exaggeration. According to Brian Headd, an economist for the U.S. Small Business Administration, 66% of new businesses are still operating after two years, 50% survive four years or more, and 40% survive six years or more. Additionally, about one-third of all businesses that close or are sold are considered to be successful by their owners.[1]

It's also important to place starting a business as an alternative to traditional employment in its proper perspective. While starting a business involves risk, working for a traditional employer is not risk-free. Between 70,000 and 80,000 corporate employees are laid-off every month, about 30,000 more per month than in the early 2000s. In addition, in many industries, pension funds, health insurance, and other benefits are being trimmed or eliminated at a rapid pace. This is a trend that is occurring in many countries around the world.

A misconception related to the myth that starting a business involves lots of risk is the often expressed sentiment that business owners themselves are risk-seekers. This idea stems largely from the impression that people who start their own businesses are willing to risk their careers, life savings, family relationships, friendships, and emotional well-being on chancy new businesses that might or might not succeed. While starting a business does entail risk, researchers have found that business owners are "moderate" rather than high-risk takers.[2] There are two explanations for this finding. First, rather than plunge blindly into a new venture, business owners tend to take well-informed calculated risks. They also try to accurately discern the degree of risk involved through the techniques we talk about in this chapter. As a result, most business owners don't tend to perceive starting a business as being as risky as you and we might see it. Second, in many cases, business owners redefine the meaning of risk and see their businesses as secondary or acceptable risks in their lives. This scenario played out for Kenny Kramm, the business owner introduced in Chapter 1. Recall, Kramm worked feverishly to find a way to help his infant daughter, Hadley, take her medicine, and as a result, started Flavorx, a company that makes additives that help medicines taste better. For Kramm, the biggest risk in his life was his daughter's health, not the business he was starting. Similar examples include mothers or fathers who start home-based businesses so they can be home with their kids and people who start businesses to pursue passions that are particularly important to them. It's not that these people are reckless or are predisposed to accept higher risks than nonbusiness owners. It's just that they don't see their businesses as high-risk or are willing to accept some additional level of risk, given the other opportunities their businesses allow them to pursue.

If people are in general risk-averse, what type of people, then, are able to set aside the natural tendency to protect their jobs and maintain the status quo and start their own businesses? What set of attributes motivate someone to learn enough about a business opportunity to make a well-informed decision about whether it's a good opportunity or not? Or what set of qualities gives a person sufficient drive to quit her job or work hard enough in her spare time to start a business to accommodate a higher goal, like Kenny Kramm did when he started Flavorx?

Before addressing these issues, we'd like to briefly explain the nature of risk and why it's difficult for people to quit a job to start a business. The very nature of risk inclines people to protect what they have, whether it's a job or another asset, rather than make a dramatic life change like starting a business. After looking at these issues, we'll articulate the attributes that allow people to set aside their aversion to risk and start their own businesses.

Why It’s Difficult for People to Quit Their Jobs and Start Their Own Businesses

Risk is a concept that signifies a potential negative impact or outcome that results from a process or future event.[3] In everyday language, we use the term "risk" to indicate the probability of a loss. Two terms that are associated with the study of risk are the *endowment effect* and *loss aversion*. An understanding of both these terms and the concepts behind them provide insight into why it’s difficult for people to quit their jobs and start their own businesses.

The endowment effect refers to the fact that people value a good, service, or anything of value more once they posses it.[4] In other words, people place a higher value on things they own opposed to equivalent or even superior items they don’t own. In one famous study depicting this effect, college students placed a high value on a coffee mug that had been given to them but put a lower price on a near equivalent mug they did not yet own. There is a very powerful urge among people to protect what they already own or possess, even though something of greater value may be within their reach. It’s easy to see how this applies to people and their jobs. When an individual already has a job, his tendency is to protect it, imperfect as it might be, rather than quit that job to start a business. The problem with this tendency is that people often exaggerate the desirability and future potential of a job simply because they have it.

The second dimension of risk that helps explain why it’s hard for people to quit their jobs to pursue self-employment is loss aversion, which refers to the tendency for people to strongly prefer avoiding losses rather than acquiring gains.[5] In fact, some studies have shown that losses are as much as twice as psychologically powerful as gains. The way this applies to people and their jobs is similar to the endowment effect. People are reluctant to lose or give up something, like their jobs, even if the possibility exists that they could exchange them for something much better, like different jobs or starting their own businesses. Ironically, what this means is that people often achieve the worst of both worlds without even realizing it. They’ll fight hard to keep jobs that are mediocre or poor, simply to avoid losing them, while they are psychologically less inclined to fight hard to gain something that might improve their situations, like different jobs or starting their own businesses.

What "Who Wants to Be a Millionaire?"

Teaches Us About Why People Are Reluctant to Start Their Own Businesses

The game show "Who Wants to Be a Millionaire?" is the ideal setting for illustrating the endowment effect and loss aversion. The endowment effect refers to the fact that people value something more once they possess it, while loss aversion refers to the tendency for people to strongly prefer avoiding losses over acquiring gains. Collectively, the two theories help explain why people tend to cling to their present jobs, even if they are sub-par, rather than try to find different jobs or start their own businesses in an effort to improve their situations. It also explains why people on games shows like "Who Wants to Be a Millionaire?" often take the money rather than try for a higher amount.

The way the show works is simple. On a particular show, the host asks a contestant a series of up to 15 questions, each worth a monetary value starting at $100 and moving up to $1 million. For each question the contestant answers correctly, the contestant can either take the money that has been won or risk the money to try to advance to the next level. (The rules varied some during the years of the show.) The game is fun to watch, partly because when a contestant reaches a certain level, like $64,000, either Regis or Meredith (the show’s two hosts) shows the contestant a signed check for that amount. This is when the endowment effect and loss aversion often kick in. Once the contestant sees the $64,000 in tangible form, there is a powerful urge to protect and hold onto it, even though much more could be potentially won if the game continues. The effect is even clearer when people preprogram themselves to try to avoid it. This intention is apparent when people say, often with their voices trembling, something like, "I promised myself I would not drop out until I reached the $125,000 question." The reason their voices tremble is because they are fighting a natural urge. Their natural urge is to take the $64,000 and run.

The endowment effect and loss aversion, as they play out in games shows and in everyday life, speak to something that is a deep part of human nature. People are more inclined to go with a sure bet, like taking the $64,000 instead of risking it for a higher amount, or keeping their jobs rather than starting their own businesses, even when they are within an arm’s length of significantly more money or a potentially more satisfying career.

In our experience, there are three activities in which people engage to overcome the natural tendency to succumb to the endowment effect and loss aversion and objectively assess whether starting a business is right for them. As you read through and think about these activities, pay particular attention to how each activity can bring clarity and a sense of purposefulness to your life. The problem with succumbing to natural tendencies, like loss aversion and the endowment effect, is that they in effect place a person on autopilot rather than equip them to make more personal and deliberate choices. This outcome can be a good thing when someone reflexively withdraws his or her hand from a hot stove. But it can be a bad thing if it keeps a person in an unsatisfying job when other alternatives, like starting a business, are readily available.

Make an Objective Decision About Starting a Business by Setting Aside Anxieties About Risk

Three activities that can help people transcend loss aversion and the endowment effect to determine whether starting a business is right for them are shown in Figure 2.1. The first two activities, "Determining what you want out of life" and "Having a good sense of what's the 'worst thing that can happen' if your business fails," are usually needed to get a person to the point where he is open to even considering starting his own business. You'll see this reality reflected in several of the examples that follow. The third activity, "Researching the business opportunity," is needed to help a person assess the attractiveness of a particular business opportunity.

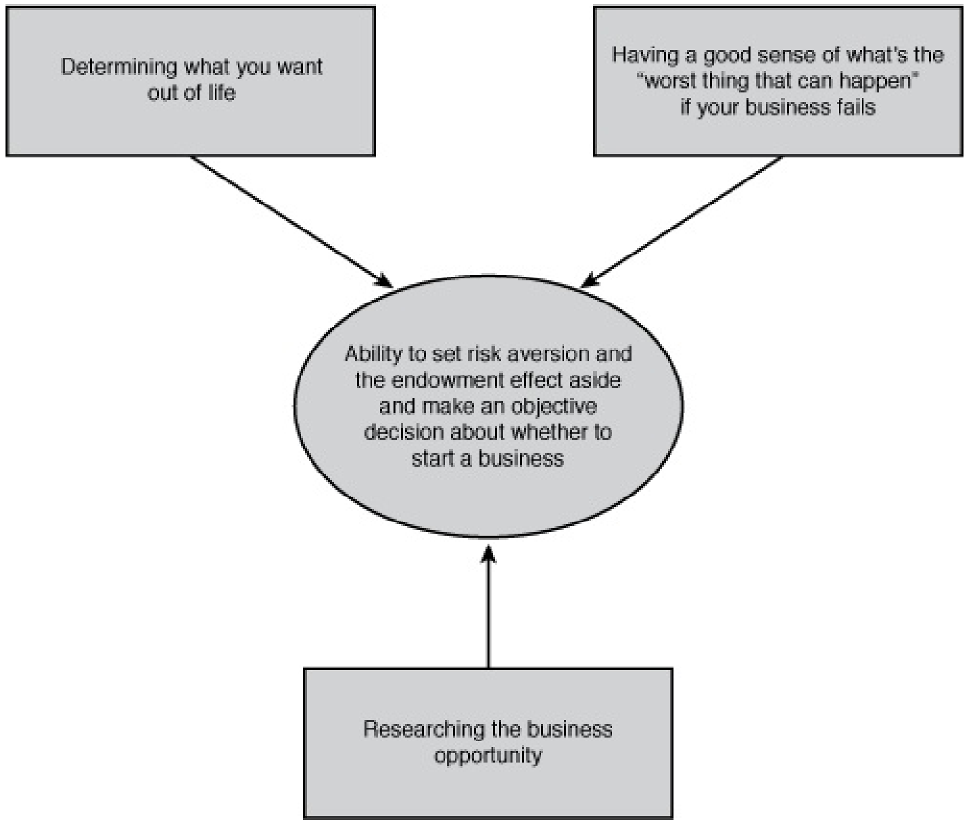

Figure 2.1. *Activities that enable an individual to set aside risk aversion and the endowment effect and make an objective decision regarding whether starting a business is right for him or her*

An awareness of these activities can be very helpful for two reasons. First, if you're thinking about starting your own business, the activities can be used as a literal checklist to help you overcome the natural tendency to yield to loss aversion and the endowment effect in your own life. These are powerful effects, and they typically can't simply be willed away. You have to first convince yourself that starting a business is the right thing to do before you can convince others. Second, an awareness of the activities is helpful because, collectively, they are holistic and deal with both the personal and the business side of starting a business.

Let's now take a closer look at these three activities.

Determining What You Want Out of Life

The first activity people need to carry out is determining what they want out of life. This is a subjective task that is frequently more difficult than it seems. It is also something people must do for themselves. A mentor, spouse, parent, or book might help a person determine alternatives for her life, but ultimately a person's awareness of what she wants out of her life and career must come from within. Sadly, most people are not vigilant enough about determining what they really want and, as a result, spend precious years in so-so jobs and mediocre lifestyles. An important way of reducing risk in all aspects of life is for a person to determine his most important goals, passions, and aspirations and then focus his valuable time and resources in those areas.

There are many ways to go about gaining an appreciation for what's most important in life. Some people write a personal mission statement or values statement. Others acquire a sense of their most important aspirations and goals more gradually or subtly. Many people also reevaluate what's most important to them as the result of a significant life event, such as the birth of a first child, a health scare, the loss of a job, or a national tragedy like the terrorist attacks on September 11, 2001. These types of events jolt people into thinking through their most important personal goals and priorities.

There are at least two ways that determining what you want out of life can help you set aside risk anxieties and decide whether starting a business is right for you. First, people who have a good sense of what they want out of life tend to look at life holistically and are more likely to select careers or occupations that facilitate the entirety of their lives and aspirations, rather than settling for something that just earns them a paycheck. This is the reason that the vast majority of small businesses are classified as "lifestyle" firms (see Table 1.1). Rather than starting a business to accumulate wealth or gain prestige, the majority of people start businesses to pursue certain lifestyles and make a living at it.

An example of a married couple who started their own business for exactly this reason is Sue Schwaderer and Bill Lawrence. In the late 1990s, Schwaderer was making a six-figure income working for Oracle Software, and Lawrence was successfully managing three apartment buildings they owned in Evanston, Illinois, a Chicago suburb. Although they were making good money, they didn't enjoy their everyday life. "We were tired of never seeing each other and of too much business travel...too much traffic, too many people, too much noise," Schwaderer recalls.[6] The two left their life in Chicago behind and opened up a 14-room bed and breakfast in picturesque Saugatuck, Michigan, a town of 1,000. Although the income from the bed and breakfast doesn't match what they were making in Chicago, they are happier and enjoy the less hectic pace of a smaller town. The desire to pursue what was most important in their life was stronger than the tug of loss aversion and the endowment effect, and they were able to meet their aspirations through business ownership.

Why Two People with Successful Careers Left Their Jobs to Start Their Own Businesses

There is no more vivid an illustration of how having a good sense of what you want out of life can change how you view jobs and careers than when people give up lucrative careers to start businesses that seemingly have much less income potential than the careers they left behind. This is exactly what happened in the cases of Hannah Sullivan and Emily Levy.

Hannah Sullivan spent the majority of her career in high-powered jobs in the investment world. Most recently, she was a general partner at San Francisco-based Fremont Ventures, a part of the Fremont Group, a private investment company that manages more than $10 billion in assets. But her passions have always been hiking, canoeing, and other outdoor activities. In 2001, Sullivan was ready for a break from the investment world. Ironically, about the same time, she met Katie, the owner of Tahoe Trips & Trails (an adventure and travel company), who was ready for a break from her industry. Despite her prestigious career, Sullivan admits that she had been looking into the possibility of either buying or starting an adventure travel company for the previous 10 years. Sullivan quit her job and purchased Tahoe Trips & Trails. She left the investment world and her promising career behind and is now expanding the operations of her new endeavor.

Emily Levy grew up in South Florida helping her mother run a school for students with learning disabilities. She developed an alternative strategy for teaching reading comprehension to dyslexic students, but when it was time for college, she decided to pursue other interests and was accepted into an eight-year medical program at Brown University. Ultimately, Levy deferred medical school to pursue a career in investment banking and money management in New York City.

About a year after she moved to New York, Levy realized that finance wasn't for her but stopped short of quitting her job or going back to medical school. Returning to her true interest and roots, she started tutoring students with learning disabilities part-time.

> *"Soon my entire after-work schedule was full! I had never worked so hard in my life—doing finance all day and helping kids late into the night," Levy recalls. "I knew I had to make a decision: Stick with a secure job in finance or jump into my real passion."*[7]

Levy took the leap and started EBL Coaching, a tutoring service for kids who are struggling in school or trying to overcome learning disabilities.

The second way that determining what you want out of life can help you set aside risk considerations and decide whether starting a business is right for you is if an important aspect of what you want can only be satisfied by starting your own business. This scenario played out for Kimberly Wilson, the founder of Tranquil Space, a yoga studio located in Washington, D.C. Wilson had a successful career as a paralegal but did a lot of yoga in her spare time. She had trouble finding yoga classes that she liked, so she started inviting people to her home to do yoga and provide her own instruction. As her interest in yoga grew, she attended a 200-hour yoga training course in California and made the decision to start her own yoga studio. The transition from working for a company to self-employment was tough, however, and the silent pull of loss aversion and the endowment effect can be felt in Wilson's remembrance of how she felt when she completed her yoga training and returned home to quit her job and start her studio:

> *"I came back from the training and cried. I knew I had to take the plunge, but it was tough to summon the courage. I am thrilled that I did not stick with my comfort zone."*[8]

Another example of how loss aversion and the endowment effect can be overcome if an important aspect of what someone wants can only be satisfied by starting a business is provided by Doug and Lisa Powell. Doug and Lisa, who are both graphic designers, live in the Minneapolis area with their two children. The Powells were a typical family until 2004, when their daughter Maya, who was seven at the time, got sick. It turned out that Maya had type 1 diabetes, a disease that develops in a small percentage of children and young adults. A person with type 1 diabetes has a pancreas that does not produce insulin, a hormone necessary to sustain life. To treat her condition, little Maya would have to prick her finger to test her blood and take insulin one or more times a day for the rest of her life.

As you can imagine, Doug and Lisa Powell initially felt overwhelmed. As the parents of a seven-year-old type 1 diabetic, they needed to quickly learn how to help Maya manage her disease. To accomplish this goal, the Powells set out to try every device available to help Maya understand her condition and to help her cope with her daily regimen. They tried books, alarms, toys, games, medical alert bracelets, and other devices. After trying all these items, they were struck by two things. First, almost everything they found related to type 2 rather than type 1 diabetes. Although "type 1 diabetes" and "type 2 diabetes" sound similar, they are distinctly different diseases. Many of the tools and instructional aids available for type 2 diabetics don’t work for people with type 1. The second thing that the Powells noticed was that the vast majority of the material and devices they tried were emotionally cold and intimidating—particularly for a young child. They didn’t see how using any of these items could uplift Maya’s spirits while teaching her about her disease.

Given what they had discovered, they decided to use their skills as graphic designers to develop their own materials to educate and encourage Maya and help her manage her daily regime. They started sharing the materials with other parents whose children had type 1 diabetes and were surprised by how positive the feedback was. As a result, they decided to start a business, named Type 1 Tools, to share their material and their passion for helping children with type 1 diabetes with other parents and caregivers. Word quickly spread about how effective the Powells’ Type 1 Tools are, and people with type 2 diabetes started asking for similar material. The couple obliged and refocused their company, renaming it Type 1 and Type 2 Tools, to help children and adults with both types of diabetes.[9]

Kimberly Wilson and Doug and Lisa Powell all had good jobs and promising careers but developed a keen sense of what was critically important to them in their lives. For Wilson it was starting a yoga studio, and for the Powells it was helping children with type 1 diabetes cope with their disease. In both cases, they couldn’t fulfill their most important ambitions through traditional employment or by passing their ideas along to someone else. Starting a business was the only way they could accomplish what was most important to them. They, like other business owners, were able to overcome the natural tendency to avoid risk and start their own businesses by focusing on the more important things in their lives.

Having a Good Sense of What’s the "Worst Thing

That Can Happen" if Your Business Fails

The second activity or task that helps people set aside loss aversion and the endowment effect and objectively assess whether starting a business is right for them is having a sense of "what’s the worst thing that can happen" if the business they’re contemplating fails. This activity is not meant to encourage people to be fatalistic, but to develop a reasoned notion of the actual "life risk" involved with starting a particular business. Even if a business endeavor itself is risky, the broader question is how much risk starting the business actually has in the broader scope of a person’s life. For example, Michael Dell, who dropped out of college to start Dell Inc., explained, "The opportunity looked so attractive, I couldn’t stay in school. The risk was so small. I could lose a year of college."[10]

There are two ways that people frame the issue of "what’s the worst thing that can happen if my business fails." The first is to objectively assess the risk of starting the business within the context of their lives. For example, many people start a business part-time before committing to it full-time. In these instances, if the initial results of the business are disappointing, a person can drop the business before she gives up her job. Similarly, in a two-wage-earner household, one spouse can keep his or her job while the other starts a business, and if the spouse that remains in a traditional job is able to cover the family’s living expenses, collectively the couple has less risk. This sentiment is affirmed by Manoj Saxena, the founder of Exterprise, a company that helps others build online marketplaces. In response to a question pertaining to the risk involved with starting his business, Saxena said:

> *"Second, I had the financial backing in the form of my wife who was working at IBM and had the ability to support our family. I knew I wouldn’t be forced to eat Ramen noodles to survive; we had income coming in that allowed me to focus on Exterprise."*[11]

There are other types of businesses that objectively have little risk. Examples include home-based eBay businesses and direct-sales businesses, like Tupperware and May Kay, where the upfront investment is relatively low. Many people who are otherwise risk-averse have no problem starting these types of businesses because the business can essentially be suspended at any time with little or no cost. Other people lower the risk associated with their businesses by relying strictly on their own funds and operating in a very frugal manner.

The second way people frame the issue of "what’s the worse thing that can happen if my business fails" is to fix in their minds a fall-back position if their businesses fail. This sentiment is often prevalent in people who have skills that are in high demand, like engineering or computer programming, and intuitively know that if they leave their employer on good terms to start a business, and the business fails, they will have little trouble reentering the workforce. This type of outlook is also prevalent among younger people who see their whole lives ahead of them and aren't afraid of starting over if a business endeavor fails. This view is expressed by Joyce Rita Hazan, the founder of Rita Hazan Salon. When asked about the risk involved with her business, Hazan said:

> *"I didn't think about it [being a risk]. I thought, 'What's the worse thing that can happen?' So I lose everything, and I can move in with my mom. What do I have to lose? Money? Big deal. I can make that again. I'll still have a roof over my head and people who love me."*[12]

Researching the Business Opportunity

The third activity or task that helps people set loss aversion and the endowment effect aside and objectively assess whether starting a business is right for them is researching the specific business opportunities they are considering. Taking time to learn the ins and outs of an opportunity is largely what makes business owners moderate rather than high-risk takers. The most common way to reduce anxiety in any facet of life is to collect information and become well-informed. It is also one of the most common forms of advice given to prospective business owners. "If you're ready to take the risk of starting a new enterprise, research your business carefully before taking the plunge," says Tony Lee, an editor for StartupJournal, the *Wall Street Journal*'s Web site for small business. "Even though business failure rates aren't as high as we think, aspiring entrepreneurs need to do their homework."[13] Similar words of advice are provided by Stephen Light, the founder of Flow Corp, a company that makes high pressure water cutting machines. "Before you launch a new service, you do everything you can to understand it and try to mitigate the risk surrounding it."[14]

In our experience, there are three primary ways that prospective business owners successfully approach the task of researching a particular business opportunity:

1. Get advice from experts and informed people.
2. Gather general information about an opportunity.
3. Write a business plan.

Candidly, our experience has taught us that people who frequently kick around the idea of starting their own businesses but never actually do are often guilty of engaging in none of these activities. Again, one of the primary reasons that business owners don’t tend to perceive starting a business as being as risky as the general public might see it is that they have studied the process and have an informed awareness of the potential risks and rewards involved.

The first approach that prospective business owners often take to research an opportunity is to talk to informed people about the opportunity/industry they are thinking about entering. People often surprise themselves by the quality of feedback and advice they are able to obtain from industry leaders and other informed individuals simply by asking for help. This point is affirmed by Larry Smith, the founder of *SMITH* magazine, which features amazing stories about ordinary people. When asked what advice he would give to aspiring business owners, Smith replied:

> *"Don’t be afraid to ask for help. I learned that 9 times out of 10 people are usually nice. I just went to people and said, ’Hey, I’m working on this new magazine, and could I speak with you about it.’ People are amazing! I went to the editors of* ReadyMade *(a magazine for people who like to make things), and they could’ve easily looked at me as a competitor. Instead, they just laid it out for me. I wasn’t afraid to cold call anybody, and it just amazed me how fantastic and helpful people can be. What’s the worst they can do? Say no!"*[15]

Another approach prospective business owners use to collect information and reduce their anxieties about a particular opportunity is to ask people who are in the business or industry about their experiences. This approach was pursued by Carleen Peaper, the owner of a Cruise Planners franchise. Prior to buying the franchise, Peaper contacted a number of current Cruise Planner franchisees to see what their experiences had been:

> *"I was really apprehensive about making an investment of my time and money into a franchise, so I e-mailed 50 Cruise Planner agents with a set of questions, asking for honest feedback. Everyone responded. That was a big thing that helped me determine that I wanted to join them. I also liked the way the company runs. They give us support, training, and tools but let us run with it. You can work with big groups, luxury travel, or whatever fits you."*[16]

This type of feedback is invaluable. It not only provided Peaper a sense of the level of satisfaction that Cruise Planner franchisees have, but provided her additional information about the way the company operates.

The second way that prospective business owners conduct research is to study industry (or business-specific) books, magazines, Web sites, and databases. If you don't know where to start this type of pursuit, a good place to begin is by visiting a college, university, or large public library. Simply approach a reference librarian and say, "I am thinking about starting a business in the cruise industry (or whatever industry you are interested in), can you direct me to information that might be helpful to me?" Often, a wealth of insightful information will flow from this type of inquiry.

Starting to Research a Business Idea: Begin Your Search at a College, University, or Public Library

In the age of Google and Yahoo!, it's easy to confine the research we complete on a topic to Internet searches. But one of the most frequently overlooked and valuable places to start investigating the merits of a business opportunity is at a library. Large public or university libraries have accesses to magazines, trade journals, and databases, which would cost hundreds if not thousands of dollars to access from home. A skilled librarian can use a database like ReferenceUSA, for example, to find the number of pet stores in Lincoln, Nebraska, where the stores are located in the city, and what the average income is in the neighborhoods surrounding each of the stores. Imagine how useful this type of information would be to someone putting together a business plan on opening a pet store in Lincoln. Along with providing access to the information, the typical reference librarians will also spend time with individuals to show them how the databases work and how queries are conducted. Some librarians will even put together a market research study on behalf of a prospective business owner for a nominal or very reasonable fee.

To promote business startups in a city or region, many libraries now offer expanded services to people thinking about starting their own businesses. The services often include classes, networking opportunities, and access to business professionals to solicit advice from. In fact, since it opened 10 years ago, the Science, Industry and Business Library, which is part of the New York Public Library in Manhattan, says it has trained 64,000 people through its 20 free classes. Examples of courses offered in a recent session included the following:

- Introduction to Patents
- Companies & Contacts: Creating Customized Lists
- Research 101: The Basics
- Research 102: Getting the Most out of Online Databases

Another common service offered by libraries is to provide office space for SCORE (Service Corp of Retired Executives) volunteers to meet with prospective business owners. SCORE volunteers provide free advice to prospective business owners on a wide range of business topics, including how to identify a target market, how to put together a marketing plan, how to set up an accounting system, and how to obtain a business license.

Other strategies for conducting business research include reading industry trade journals (which can be easily identified through an Internet search) and industry-specific magazines and by studying the Web sites of potential competitors. Attending industry trade shows is also a good strategy. Also reading business magazines geared toward small businesses, like *Fortune Small Business*, *Inc.*, and *Entrepreneur*, can provide invaluable insight and information. Reading these types of publications is also a confidence builder. As shared in Chapter 1, the more people in traditional jobs read and learn about business owners, the more they come to realize that owning and running a business is well within the reach of most individuals.

The third way that prospective business owners conduct research in an effort to learn more about a business opportunity and overcome risk anxieties is to write a *business plan*. A business plan is a written document that carefully explains every aspect of a new business venture. In many instances, having a business plan is a sheer necessity. Most bankers and investors, for example, won't consider financing a business that doesn't have a formal business plan.

Publications on how to write a business plan are available at bookstores like Borders and Barnes & Noble and local Small Business Development Centers, and SCORE chapters often sponsor workshops on how to write a business plan.

Most business plan are between 20 and 30 pages long and follow a conventional format outlined in the books and taught through the workshops. Although writing a business plan may appear at first glance to be a tedious process, a properly prepared business plan can save a business owner a tremendous amount of time, money, and heartache by working out the kinks in a business idea and by providing a firm understanding of the risk involved before rather than after the business is started.

Writing a business plan is not a trivial event. A well-conceived plan normally takes several days or weeks to prepare. The upside is that for someone who is serious about a particular business opportunity, writing a business plan will reveal more about the potential risks and rewards involved than any other single activity. If the plan reveals to a prospective business owner that there is too much risk surrounding a particular business opportunity, reaching that conclusion should be considered to be a successful outcome of the business planning process. It is better to fail on paper than for real. Conversely, the plan might reassure a prospective business owner that the business idea is viable and has a high probability of succeeding. This type of conclusion would help a prospective owner set aside loss aversion and the endowment effect and move forward in pursuing the business opportunity.

Summary

The primary message of this chapter is that people are in general risk-averse and must take purposeful steps to overcome their natural tendency toward loss aversion before they are able to quit their jobs and start their own businesses. This set of circumstances is not necessarily a bad thing. You should feel good about the risks involved with a particular business opportunity and your ability to manage the risks before you leave a stable job to start your own business. But an equally important message conveyed by the chapter is that people often exaggerate how good their present jobs or careers are simply because they have them. This tendency causes people to unnecessarily limit themselves in visualizing the options possible for their lives.

The next chapter deals with the amount of money it takes to start a successful business. We hope you find the chapter to be a breath of fresh air. Many businesses are started for much less money than you might think. We'll help you organize your thinking about the role of money in the startup process.

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Chapter 3. Myth No. 3: It Takes a Lot of Money to Start a Business: Truth No. 3: It Might Not Cost as Much as You Think

How much do you think it costs to start a business? If you're thinking about a biotechnology, semiconductor, or medical product firm, you'd probably say a lot, and you'd be right. But how much do you think it costs to start an average business, like the privately owned businesses you deal with every day? And where do you think the majority of the startup capital for these businesses comes from? According to the *Wells Fargo/Gallup Small Business Index*, the average small business is started for about $10,000, with the majority of the money coming from the owners' personal savings.[1]

If this figure strikes you as low, you're in good company; it strikes most people as low. That's because when most people think of businesses, they think of the types of businesses that they interact with the most frequently, like grocery stores, restaurants, gas stations, and large retail stores. These types of business do take a lot of money to start and run. But chances are if you start a business, it won't be like these businesses—at least initially. It will be more like the businesses highlighted so far in this book. Most of these businesses didn't take a tremendous amount of money to start. Even aggressive growth firms, in most cases, don't take an arm and a leg to get started. Each year *Inc*. magazine compiles a list of the 5,000 fastest-growing privately owned firms in the United States. In 2006, the medium amount it took to start one of the businesses on the list was $75,000.[2] That means that half of them were started for less than $75,000. And these firms cover a wide swath of businesses, from building contractors to advertising agencies to retail stores.

There is somewhat of a catch, however, involved with starting a business with limited funds. The catch is that most people simply don't have any experience or insight when it comes to determining how much it will cost to start a business, how to economize on startup expenses, or how to raise money if needed. These are topics that there is no reason to think about until you start seriously thinking about starting a business. To provide insight regarding these issues and to further dispel the myth that it takes a lot of money to start a business, this chapter is divided into three sections. The first section provides insights into how to think about money as it relates to starting a business. The second section focuses on the techniques that enable business owners to minimize the costs associated with starting a business. The third section focuses on the choices that small business owners have for raising startup funds if needed.

Insights Into How to Think About Money as It Relates to Starting a Business

For most people, the topic that consumes the majority of their thinking as it relates to money and starting a specific business is "How much money will it take to get the business off the ground?" While this question makes perfect sense, there is no concrete answer. The same exact business might cost one person $10,000 to start and another person $25,000—trust us, this isn't an exaggeration. The amount needed typically depends on how a person thinks about money as it relates to starting a business, how frugal a person is, and how resourceful a person is in gaining access to money and other resources.

While money is obviously needed to start even the most basic business, many of the observations that successful business owners make about money are surprising. While you'd think money would be held in high esteem, many business owners discount the importance of having plentiful funds as a key to new business success. Instead, they tend to see the absence of money as a motivator for developing qualities such as resourcefulness, creativity, focus, frugality, and drive.

The following are three insights about the role of money in the startup process. As you read through each insight, think carefully about how each topic relates to your own attitudes about money. One of the reasons that many businesses are started for as little money as they are is that people adjust their attitudes about money as they become more acquainted with the startup process.

Now let's look at three insights regarding the role of money in the startup process.

Skimpy Finances Can Be a Blessing Rather Than a Curse

The first insight regarding money and the startup process is that there is a silver lining to having limited startup funds. Many successful business owners, when they reflect back on their startup years, feel that having limited funds forced them to focus, become self-reliant, and develop a mindset of frugality—qualities that have served them well as they've grown their firms.

The importance of focus is affirmed by Caterina Fake, cofounder of Flickr, the popular photo-sharing Web site, which was started in 2002. In reflecting back on the role of money in the early days of her firm, Fake said:

> *"The money was scarce, but I'm a big believer that constraints inspire creativity. The less money you have, the fewer people and resources you have, the more creative you have to become. I think that had a lot to do with why we were able to iterate and innovate so fast."*[3]

Flickr's first product was a multiplayer online game called Game Neverending. At one point mid-way through the development of the game, the programmers, on a lark, added an instant messenger application to the game's environment, which allowed users to form communities to share photos. Surprisingly, the photo-sharing feature quickly passed the game itself in terms of popularity. As the photo-sharing feature continued to gain momentum, the game itself was dropped because the company couldn't afford to work on both projects simultaneously. Flickr (www.flickr.com), as a photo-sharing Web site, became extremely popular and was acquired by Yahoo! in 2005 for somewhere between 20 and 30 million dollars. Ironically, it was the lack of money, rather than the abundance of it, that caused the founders of Flickr to drop the game and focus on the photo-sharing site, a decision that turned out to be very profitable for the company.

In regard to developing a culture of self-reliance, having limited startup funds often instills discipline in a firm and forces the founders to substitute ingenuity and hard work for financial resources. An example of how this played out in one firm is provided by Doris Christopher, the founder of The Pampered Chef. Christopher started The Pampered Chef in 1980 and ran the company out of her home well beyond its startup years. Explaining how having limited startup funds helped set her on a lifelong track of financial discipline, Christopher wrote:

> *"With a bankroll of only $3,000 to start my business, I didn't have any choice; I had to watch my overhead. It taught me discipline, which I have been mindful of throughout my business career."*[4]

The Pampered Chef, which was started in 1980, has been an enormously successful company. It sells kitchen utensils through home parties, utilizing a direct sales approach (like Tupperware). At last count, the company had nearly 70,000 Pampered Chef consultants and 12 million people attending its home parties each year. To this day, the main theme of Christopher's speaking and writing is to caution business owners to avoid debt, minimize overhead, and remain self-reliant.

Finally, limited funds at the outset often help a firm develop a mindset of frugality—a quality that is often very helpful as a firm grows and expands. For example, many businesses that are started on a shoestring learn to function very inexpensively and continue to watch their money very carefully, even after they become successful.

How Not Having Much Money Helped One Founding Team Learn to Be Self-Reliant and Receive a Nice Payoff When Its Business Was Acquired

In the early 1990s, Ron Gruner, a serial entrepreneur, launched Shareholder.com, a company that helped large firms better communicate with their shareholders. The company started with no investment capital and funded its growth entirely through earnings. There were times, Gruner readily admits, when having more money would have been nice and would have enabled the firm to grow much faster. But the benefit of having limited funds was that the company became self-reliant, and its employees learned how to substitute ingenuity and hard work for money. In an interview Gruner gave to Jessica Livingston, the author of *Founders at Work*, he recalled a specific example that makes this point:

> *"Here's an example: Back when the whole Internet thing was getting started, I hired a computer consultant to come in and advise us about what our Internet infrastructure should be. He was a well-credentialed, Microsoft-accredited engineer, etc. He came in and said, 'You need to buy x number of servers and this kind of software and all that, and it's a quarter of million dollars to do it right.' We said we couldn't even come close to doing that. So I went down to Barnes & Noble, bought several books, including some of the Dummy series. And we built our first Internet servers, which lasted us several years, on Gateway desktop computers, using Microsoft Access as our database system and using basically off-the-shelf server software. We did that for $3 [thousand] or 4,000, and it worked great."*[5]

This type of behavior—doing things yourself rather than spending a lot of money—is referred to as bootstrapping, a practice we'll talk about later in the chapter. In Shareholder.com's case, an added benefit of learning to be self-reliant was that it motivated the company to remain independent during the heady dot-com era of the late 1990s and early 2000s, when money from investors was readily available. By not taking money, the company was able to remain nimble and react quickly to competitive challenges because it didn't have to consult with bankers or investors before it made a decision.

Shareholder.com grew steadily through the years, and the payoff came in 2006 when the firm was acquired by NASDAQ. Because Gruner and his team learned to be self-reliant and live with limited funds, they didn't have anyone to split the proceeds with when the firm was sold.

Raising or Borrowing Money Is Trading One Boss for Another

The second insight regarding the role of money and the startup process has to do with raising equity capital or borrowing to fund a business. One of the first things that many people do when they decide to start a business is to try to raise money through a bank or an investor. There are several choices that business owners have for raising money, including commercial banks, SBA guaranteed loans, investors, grants, supplier financing, and several others. Of these choices, many people automatically assume that the only way they'll raise the amount of money they need is via a commercial bank or an equity investor. While the other choices might hold promise, most people's initial reactions are that the alternatives pale in comparison to the amount of money that can be raised from a bank or through an investor.

While in some cases it is necessary to go the bank or investor route, the problem with obtaining money from these sources is that there are consequences that business owners often don't fully anticipate. Bankers and investors typically assert considerable control over the businesses they provide money to as a means of protecting their investments. While the majority of bankers and investors have good intentions, the level of scrutiny and control their investments allow them often has an impact on the firms they fund. For example, banks are inherently conservative and often caution their clients to grow slowly, while investors are the opposite and regularly pressure the companies they invest in to grow quickly to increase their valuations. What’s missing here is what the business owner wants. So for people leaving traditional jobs to start their own businesses, obtaining money from bankers or investors is often like trading one boss for another. You might be freeing yourself from working for a boss in a traditional sense but could have an equally influential boss in the form of a banker or an investor.

An additional consideration when taking money from an investor is that you exchange partial ownership in your business for funding. This aspect of the small business owner–investor relationship can also be problematic. Unlike the business owners introduced in this book, who started their businesses to fulfill personal aspirations or follow their passions, the majority of investors are not in it for the long term—they want their money back in three to five years along with a sizeable return. This means that a business owner like Daryn Kagan, the former CNN reporter who started a "good news" Web cast, will probably have to sell her business in three to five years from the time it was started if she accepted investment capital. Although this scenario will undoubtedly net Ms. Kagan a handsome financial return, assuming her business is gaining traction and is profitable, she’ll lose direct control of the business she was so excited to create.

The solution to avoid these potential problems is steering clear of bank financing or equity funding or, at the minimum, having a clear understanding of the nature of the relationship you’ll have with your banker or investors. It’s possible for a small business owner to have a healthy relationship with a banker or an investor. The overarching point, however, is that small business owners should go into these relationships with their eyes wide open, fully understanding the parameters of the relationships they’re developing.

Excess Funds Can Enable a startup to Operate Unprofitably for Too Long

The third insight regarding money and the startup process is that having excess funds often masks problems and enables a firm to operate unprofitably for too long. Many businesses lose money their first several months while they ramp up and gain customers. That’s normal. But at some point, a business has to operate profitably to prove that it is a viable, ongoing pursuit. People who start businesses with limited funds typically find out quickly if their businesses are capable of turning a profit. Because they don’t have excess funds to rely on, they must make adjustments quickly, like cutting expenses or increasing sales, to turn a profit. Ultimately, if the business doesn’t work, it is shut down. In contrast, if a person starts a business with abundant funds, the business can operate for months at a loss and stay open if the owner relies on excess funds to keep the business afloat. The owner may never feel pressured to cut costs or generate additional sales, thinking that the business simply needs more time to prove itself. If the business ultimately fails, it will normally lose more money and more of its owner's time and prestige than the less well funded startup.

A related complication associated with having abundant funds is that a business's cost structure and clientele is often determined by the amount of money it has initially. For example, if you decided to open a clothing store and were offered $200,000 by an investor to start the business, you might rent space in an upscale mall, hire experienced salespeople, buy the latest computer equipment, and launch an expensive advertising campaign. While this sounds good, once the business is started and the $200,000 is gone, you might be locked into a high overhead business that has to sell high margin products to an affluent clientele to make the business work. Conversely, if you had started with less money, you might have signed a shorter tem lease in a more modest facility, hired your initial salespeople part-time to see which ones worked out the best, bought used computer equipment, and found inexpensive ways to spread the word about your store. Utilizing this approach, you'd actually have more flexibility and room to maneuver than the better funded scenario.

Collectively, the purpose of these three insights is to put the importance of money in starting a business in its proper perspective. While many people think, "If I only had the money, I'd start my own business," the insights provided here show that having money isn't a panacea. In fact, the discipline imposed by having limited funds is often an advantage and creates a healthier business in the long run.

The next section of this chapter focuses on techniques that enable business owners to minimize the costs associated with starting up. While many businesses ultimately do need to raise some money to get started, the amount needed can be greatly reduced through creative and novel cost-cutting techniques.

Techniques That Enable Business Owners to Minimize the Costs Associated with Starting a Business

As mentioned earlier in the chapter, the numbers reported for the average cost of starting a business strike most people as low. When you think about the cost of buying a car or even a major household appliance, it's easy to question whether the average business is really started for around $10,000. The answer is that while it might cost $10,000 to start the average business, that figure doesn't tell the whole story. Many business owners put a tremendous amount of free labor into starting their firms and become experts at scraping and scrounging to gain access to resources at reduced cost. In fact, many observers believe that a business owner's ability to "bootstrap" all or part of its resource needs is a key to business success. The term *bootstrap* comes from the German legend of Baron Munchausen pulling himself out of the sea by pulling on his own bootstraps. In startup circles, bootstrapping means finding ways to avoid the need for bank financing or investor funding through creativity, ingenuity, thriftiness, cost-cutting, or any means necessary.[6]

This section of the chapter focuses on three techniques that enable business owners to minimize the costs associated with starting a business. The techniques include selecting an appropriate business to start, seeking help, and cutting costs and saving money at every available opportunity.

Selecting an Appropriate Business to Start

The first step involved in minimizing the costs associated with starting a business is to select an appropriate business. If you have limited funds, you should start a business that requires a small up-front investment, has a short sales cycle (meaning the customer decides quickly whether to buy), has short repayment terms (30 days or less), and has a high degree of recurring revenue. Businesses with the opposite characteristics generally take too much money for a business owner with limited resources to start and run.

Fortunately, there are many businesses that meet the criteria described. Home-based businesses, which now represent more than half of the 26.8 million U.S. small businesses, are popular largely because they take very little capital to start and have low overhead. The cost savings that are realized by operating a home-based business often help these businesses earn profits from the start, which helps them accumulate the funds necessary to move into larger quarters when needed. This is exactly what happened in the case of Emily Levy, the founder of EBL Coaching, the tutoring service for children introduced in Chapter 2. Commenting on her startup experience, Levy wrote:

> *"My startup costs were minimal since I was working out of my apartment. Now that the business has grown, however, I have to pay for office space, insurance, advertising and tutors, but EBL Coaching has been profitable*

from the start. There are many businesses that you can start with minimal capital, especially if you start small and grow organically as demand increases."[7]

Service businesses are also fairly inexpensive to start depending on the nature of the business. Though not exhaustive, a list of service businesses that typically meet the criteria discussed above are shown in Table 3.1. An example from the table is a home inspector. Nearly every real estate transaction requires a home inspection, making it a fairly lucrative business. The up-front costs of becoming a home inspector are fairly modest, which include training and certification and a basic set of home inspection tools. The sales cycle is short, considering that once an inspection is ordered, it is normally completed within a few days. The repayment term is also short because the inspector usually requires payment the day of the inspection. And there is normally a high degree of recurring revenue. Even though the same people don't normally require repeat inspections, the vast majority of a home inspector's business comes from referrals from builders and real estate agents.

Table 3.1. Examples of Service Businesses That Are Attractive Alternatives for Prospective Business Owners with Limited Funds

Automotive Detailing	Massage Therapist
Bookkeeper	Messenger Service
Bridal Consultant	Nanny Service
Career Counselor	Online Retailer
Counselor/Psychologist	Photographer
Daycare Service	Property Management Service
eBay Store	Public Relations Consultant
Executive Search Firm	Tax Preparation Service
Financial Planner	Transcription Service
Home Inspector	Travel Agent
Interior Designer	Tutoring Service

The types of businesses that aren't good choices for prospective business owners with limited funds are businesses that bring new products to market, businesses that are capital-intensive like manufacturing firms, and businesses that require a lot of employees like a call center. While these businesses might have more potential profitability than home-based businesses and service firms, they simply take too much money to start for someone with limited startup funds.

Seek Out Help

The second technique that helps business owners minimize the costs associated with starting a business is to seek out coaching and assistance. There are many ways for new businesses to get this type of help. The Small Business Development Center (SBDC), for example, is a government agency that provides free management assistance and coaching to small business owners. Your local SBDC can be identified at www.sba.gov/sbdc. Another good choice is the Service Corps of Retired Executives (SCORE), which is a nonprofit organization that provides free consulting services to small businesses. SCORE's 10,000+ volunteers are retired business owners who counsel in areas as diverse as finance, operations, ecommerce, and sales. You can find your local SCORE chapter at www.score.org. Both of these organizations can provide business owners concrete advice and suggestions for how to minimize the costs of starting a specific business.

Prospective business owners should also identify local small business and entrepreneurship organizations to plug into. These organizations offer seminars, sponsor networking events, hold business plan competitions, and introduce their members to service providers and potential sources of financing or funding. An example is the Oregon Entrepreneurs Network (www.oen.org), an organization that services prospective business owners in Oregon and southwest Washington. The organization, which charges a nominal membership fee, provides its members a full slate of programs and services. A similar example is the Venture Lab at the University of Central Florida in Orlando, Florida (www.venturelab.ucf.edu). The Venture Lab provides coaching and advice to anyone in Central Florida who has a business idea and needs help assessing the merits of the idea and shaping it into a viable business. There are similar organizations in almost every city in the United States.

Finally, there are organizations that provide coaching, advice, and support to specific groups of business owners and tailor their offerings to fit the groups. An example is Ladies Who Launch (www.ladieswholaunch.com), an organization that sponsors workshops and provides materials that encourage and support female business owners. The workshops include discussions, case studies, stories, and anecdotes that help women leverage their unique abilities to launch businesses efficiently and effectively. Similar organizations and support groups are available for veterans, members of minority groups, college students, senior adults, and other demographic groups.

Cut Costs and Save Money at Every Opportunity

The most obvious way to minimize the costs associated with launching a business is to cut costs and save money at every opportunity. The most effective way to do this is to develop a mindset of frugality and resourcefulness. While these attributes might seem obvious, in many cases, frugality and resourcefulness are learned skills. Many people aren't naturally frugal or resourceful, but as a result of an intensive desire to make their businesses work, they foster these qualities to help get their businesses off the ground and to minimize the costs of their ongoing operations.

A list of common cost-cutting and cost-saving techniques is provided below. While the techniques are well known, the trick is to put them into action. An example of a business owner who put the third item on the list, "Look for opportunities to barter," is provided by Clara Rankin Williams, the founder of Clara Belle Collections, a jewelry design business. When asked for words of advice regarding how to start and run a business, Williams said:

> *"Take advantage of random situations. I was at a truck show and I heard a friend talking with a marketing consultant. I asked the consultant whether there was any chance she might be interested in helping me with my marketing and swapping jewelry for services. She was. As an entrepreneur, you have to think out of the box, especially if you want to survive in an increasingly crowded marketplace."*[8]

This type of behavior exemplifies a mindset of frugality and resourcefulness. There are other cost-cutting and cost-saving techniques that aren't as well known as those shown in the following bulleted list. A sample of these techniques includes employing open source software instead of more expensive proprietary software packages, writing or participating in blogs as an alternative to buying advertising, utilizing online tools such as Skype instead of paying for long distance, and eliminating the cost of buying a fax machine by utilizing an online fax forwarding service such as eFax.

- Buy used instead of new equipment.
- Coordinate purchases with other businesses.
- Barter.
- Lease equipment rather than buying.
- Obtain payments in advance from customers.
- Minimize personal expenses.
- Avoid unnecessary expenses, such as lavish office space or furniture.

- Buy items cheaply but prudently through discount outlets or online auctions such as eBay, rather than at full-price stores.

There are many examples of business owners who dramatically reduced the cost of launching their businesses by utilizing combinations of the techniques described here. One example is provided by Michelle Madhok, the founder of SheFinds (www.shefinds.com), a company that helps people find bargains on the Internet:

> *"I financed SheFinds myself and have spent about $5,000 of my own money to get the business off the ground. The most expensive items were forming the LLC [which is a form of business ownership], legal costs, and public relations. My [Web] site was built for about $250 by a guy in the Ukraine who I found on Craig's List (www.craigslist.com). My photos were done for barter, and I got a good deal on the illustrations on my site because the artist had downtime. I worked with many independents—my lawyer was an independent, because I [didn't] see the value in paying for a big, fancy firm. And I looked for discount resources on the Internet—if you search around, you can find companies that will make quality color copies for about 20 cents a copy."*[9]

Madhok's experience is a clear example of a firm that cost $5,000 to start but could easily have cost $25,000 absent her frugal mindset and deliberate attempts to cut costs.

Choices That Small Business Owners Have for Raising StartUp Funds if Needed

Some startups do need to raise money to get their businesses off the ground. In these instances, it's been our experience that the most knowledgeable and well-informed business owners have the most success. The most common mistake that prospective business owners make is not having a business plan. Although some books and magazine articles suggest that a business plan isn't necessary, our experience has taught us that this advice is dead wrong. It's almost inconceivable that a business would be successful obtaining money from a bank, an investor, a granting agency, a supplier, or future customer without a business plan that describes the business and validates its financial potential. Help for writing a business plan can be obtained from the SBDC, SCORE, or other small business support groups. There are also books detailing how to write a business plan available at Borders, Barnes & Noble, and Amazon.com. The first author of this book has a business plan book titled *Preparing Effective Business Plans: An Entrepreneurial Approach*, which can be obtained via Amazon.com or a similar online bookstore.

A second mistake people often make when looking for financing or funding is that they don't cast their nets wide enough. There are many sources of financing and funding available for small businesses. As a result, it is poor strategy to place too much reliance on some sources of funding and not enough on others.

This section of the chapter outlines the choices that small business owners have for raising startup funds if needed. The alternatives include bank financing, equity funding, grants, and a few others.

Bank Financing

Historically, commercial banks have not been a practical source of financing for startup firms. Most banks are relatively conservative and won't loan money to a business that doesn't have a proven track record and some type of collateral. That's not to say that you can't get a home equity loan to fund part or all of the money you need. It's just that most banks won't assume the risk of loaning money directly to a business with an unproven track record. They would rather loan money to an individual who has equity in a home to pledge as collateral.

The Small Business Administration (SBA) Guaranteed Loan Program is a realistic alternative for many business startups. The SBA does not have money to lend but makes it easier for business owners to obtain loans from banks by guaranteeing the loans. Approximately 50% of the 9,000 commercial banks in the United States participate in the Guaranteed Loan Program. The most notable SBA program available to small businesses is the 7(A) Loan Guaranty Program. The loans are for small businesses that are not able to obtain loans on reasonable terms through normal lending channels. Almost all small businesses are eligible to apply for an SBA guaranteed loan. The SBA can guarantee as much as 85% (debt to equity) on loans up to $150,000 and 75% on loans over $150,000. In most cases, the maximum guarantee is $1.5 million. A guaranteed loan can be used for working capital to start a new business or expand an existing one. It can also be used for real estate purchases, renovation, construction, or equipment purchases. The best way to learn more about the SBA Guaranteed Loan Program and determine if you are eligible is to meet with a participating lender.

There are a variety of other avenues that business owners can pursue to borrow money. Credit cards should be used with extreme caution. One channel for borrowing funds that is getting quite a bit of attention is Prosper (www.prosper.com), a peer-to-peer lending network. Prosper is an online auction Web site that matches people who want to borrow money with people who are willing to make loans. Most of the loans made via Prosper are fairly small ($25,000 or less) but might be sufficient to meet a new business's needs. There are also organizations that lend money to specific demographic groups. For example, Count Me In (www.countmein.org), an advocacy group for female business owners, provides loans of $500 to $10,000 to women starting or growing a business. An organization that is aligned with Count Me In and American Express, named Make Mine a Million $ Business (www.makemineamillion.org), lends up to $45,000 strictly to female-owned startups.

There are also lenders who specialize in "microfinancing" which are very small loans. For example, Accion USA (www.accionusa.org) gives $500 credit-builder loans to people with no credit history. While $500 might not sound like much, it could be enough to start a home-based business such as an eBay store.

John and Caprial Pence: How the SBA Guaranteed Loan Program Helped Two Business Owners Get the Financing They Needed

John and Caprial Pence are two of Portland, Oregon's finest cooks and busiest business owners. The two run a growing number of businesses in the Portland area, all focused around fine food. A distinctive aspect of their story is the role that the SBA Guaranteed Loan Program played in their success. The Pences have utilized the SBA loan program twice, and it has been instrumental in helping them build their businesses.

John and Caprial met at the Culinary Institute of America in Hyde Park, New York, where they were both attending school to become chefs. In the mid-1980s, following graduation, they moved to Seattle where they launched their careers. In 1990, Caprial won the James Beard Award for the best chef in the Pacific Northwest. At the same time, she was working on her first cookbook, teaching classes, and appearing on local TV.

In 1992, the Pences decided to move to Portland and bought the old Westmoreland Bistro with private financing. In 1998, they decided to remodel and expand the Bistro when space became available next door.

The Pences considered several options for financing. The most realistic alternative, based on the advice of their banker, was an SBA guaranteed loan. The Pences agreed, and the bank facilitated a $260,000 seven-year SBA guaranteed loan. The loan enabled the couple to expand the seating capacity of their restaurant from 26 to 70 tables.

Following the expansion of the restaurant, the Pences decided to diversify and leverage their cooking expertise by opening a cooking school and a cookware shop. A second SBA guaranteed loan, for an identical amount as the first one, made these objectives a reality. The addition of the cooking school and the cookware shop has tripled the Pence's annual revenue.

The future for the Pences and their businesses looks bright. The restaurant initially brought in around $1,000 a day but now brings in $4,000 to $5,000 on an average weekday. The cooking school offers classes and demonstrations nearly every evening, where participants pay from $35 to $135 for hands-on classes or to view special cooking demonstrations. Just recently, the Pences started to bootstrap a television show from the cooking school, and Caprial celebrated the publication of her eighth cookbook.[10]

Equity Funding

Equity funding is obtaining money from an investor. Investors are typically interested in businesses that plan to grow rapidly and can capture fairly large markets. These businesses normally have a unique business idea, a proven management team, and are shooting to capture large markets.

There are two types of equity investors. The first are referred to as *business angels*. Business angels are individuals who invest their personal funds directly into startups. They generally invest between $10,000 and $500,000 in a single company and are looking for companies that have the potential to grow 30–40% per year before they are acquired or go public.[11] Jeffrey Sohl, the director of the University of New Hampshire's Center for Venture Research, estimates that only 10–15% of private companies meet that criterion.[12] The one exception that might help you get your foot in the door with an angel investor, if your business doesn't meet the traditional criteria, is if the purpose of your business is aligned with a personal interest or passion of the investor. For instance, if you're starting a company to make a safer car seat for infant children and meet an angel investor who has an intense interest in child safety products, you could capture the investor's attention even if your firm isn't capable of a 30–40% per year growth rate.

Most business angels remain fairly anonymous and are matched up with business owners through referrals. If you're interested in pursuing angel funding, you should discreetly work your network of acquaintances (bankers, lawyers, accountants, successful entrepreneurs) to see if anyone can make an appropriate introduction.

The second type of equity investor are *venture capitalists*. Venture capital firms are limited partnerships of money managers who raise money in "funds" to invest in startups and growing firms. Some of the better known venture capital firms are Kleiner Perkins, Sequoia Capital, and Redpoint Ventures. Similar to business angels, venture capital firms look for a 30–40% annual return on their investments and a total return over the life of investments of 5 to 20 times the initial investments.[13] The major difference between venture capital firms and business angels is that venture capital firms lend very little money to startups (preferring to wait until a firm proves its product and market) and normally don't invest less than $1 million in a single firm. As a result, venture capital funding is only practical for a very small number of business startups.

Grants

A potential source of small business funding that does not get enough attention are *grants*. A grant is a gift of money that does not have to be repaid. While there is no nationwide network for awarding grants to startup firms, almost every state, city, and local community is trying to find ways to encourage people to start businesses as a means of growing their economies. As a result, there are a growing number of programs available at all levels of government, through the private sector and via foundations, to provide grant money to promising business startups.

Obtaining a grant takes a little detective work. Granting agencies are by nature low-key, so they normally need to be sought out. The best place to inquire about the availability of grants for a particular business is via the SBDC, SCORE, small business incubators, and similar organizations. Although these groups might not have grant money available, they might be able to direct you to organizations that are awarding grants to small businesses in your area.

A typical scenario of a small business that received a grant is provided by Rozalia Williams, the founder of Hidden Curriculum Education (www.hiddencurriculum.com), a for-profit company that offers college life skills courses. To kick-start her business, Williams received a $72,500 grant from Miami Dade Empowerment Trust, a granting agency in Dade County, Florida. The purpose of the Miami Dade Empowerment Trust is to encourage the creation of businesses in disadvantaged neighborhoods of Dade County. The key to William's success, which is true in most grant awarding situations, is that her business fit nicely with the mission of the granting organization, and she was willing to take her business into the areas the granting agency was committed to improving. After being awarded the grant and conducting her college prep courses in four Dade County neighborhoods over a three-year period, Williams received an additional $100,000 loan from the Miami Dade Empowerment Trust to expand her business. There are also private foundations that grant money to both existing and startup firms. The MacArthur Foundation, for example, is a private grant awarding agency which recently dedicated $2 million to fund projects dealing with digital media and learning.

The federal government has a pair of grant programs for technology firms. The Small Business Innovation Research (SBIR) program is an established program that provides over $1 billion in cash grants per year to small businesses that are working on projects in specific areas. Each year, 10 federal departments and agencies are required by SBIR to reserve a portion of their research and development funds for awards to small businesses. A list of the agencies that participate, along with an explanation of the application process, is available at www.sba.gov/sbir. A privately owned Web site, SBIRworld (www.sbirworld.org), provides useful tips and advice on how to apply for SBIR grants.

The second program, the Small Business Technology Transfer (STTR) program is similar to the SBIR program except it requires the participation of researchers working at universities or other research institutions. Information about the STTR program can be obtained from the Web sites just identified.

Other Potential Sources of Funding

There are other potential sources of funds available for business startups. Similar to locating grants, finding the money takes a little detective work but could be time well spent. For example, there are an increasing number of business plan competitions held across the United States. Many of the competitions offer cash prizes. There are also an increasing number of small business contests sponsored by companies that sell products to small businesses. An example is the Visa

Business Breakthrough Contest, which offers five $10,000 awards to businesses that submit essays explaining how they can become more efficient in one of five categories (finance, marketing, organization, team building, and technology). A simple Google search using the keywords "small business contests" will produce similar examples.

More sophisticated ways of obtaining startup funds involve asking for cash advances from suppliers or potential customers. Some suppliers, if they recognize that your business has the potential to become a regular customer, will invest in your business or provide your business financing to help it get off the ground. Similarly, if you feel that your product or service will add considerable value for a particular customer and save the customer money, the customer might be willing to prepurchase a certain amount of product, which is a way for you to generate startup funds. If you're buying a franchise, you can typically obtain financing through your franchisor. These alternatives need to be investigated on a case-by-case basis.

There are also ways that business owners tap into personal funds, beyond using savings and cash-on-hand. Examples include borrowing against the cash value of a life insurance policy and tapping into a retirement account. You'll normally need advice from a tax accountant to draw funds from a tax deferred retirement account to finance a business venture.

Summary

It's important to have the right frame of mind regarding money and the startup process. Often having abundant funds isn't necessarily the best thing. Many business owners look back on their startup years and recall that it was the lack of money that caused them to get creative and develop sound financial habits—attributes that are still serving them well today. Money is also a topic where it pays to be somewhat of a sleuth. There are many sources of startup funds available, such as grants, business plan competitions, and SBDC guaranteed loans. These sources of funds, however, have to be sought out and tracked down to make an impact on a new company.

The next chapter focuses on the myth that it takes a lot of business experience to start a successful firm. Because most of the businesses we deal with are established companies, it's easy to believe that they were started by experienced business people and have always run as smoothly as they do. In reality, most businesses were started by people just like you. There are also many forms of experience that are helpful in the business startup process. You might have vastly underestimated the value of the skills and experiences that you presently have.

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Chapter 4. Myth No. 4: It Takes a Great Deal of Business Experience to Start a Successful Business: Truth No. 4: Successful Businesses Are Started by People with All Levels of Business Experience

Introduction

One of the most pervasive myths that inhibit people from starting their own businesses is the notion that it takes a great deal of business experience to start a successful business. It's easy to understand where this notion comes from. Most of the businesses we deal with are established companies with employees, customers, well-established processes, and track records of success. Because we didn't see these businesses when they were young, it's easy to believe that they've always run as smoothly as they do today. In addition, most of the business founders we know about, such as Bill Gates (Microsoft) and Michael Dell (Dell), seem to have done everything right in building their businesses. If someone told you that each of these individuals had substantial business experience before they started their companies, there would be no reason to disbelieve them.

The problem with these depictions is that they create misconceptions about the way businesses start and evolve and the amount of expertise it takes to start them. Most businesses start small and grow over time—it's just that we rarely see them when they're first getting started. Wal-Mart, for example, started with a single store in Bentonville, Arkansas. And there are many examples of firms, including Microsoft and Dell, which were started by people with no business experience at all. In fact, most of the businesses we profile in this book were started by people with little or no prior business experience. Examples include darynkagen.com (started by a former CNN reporter), Dynamic Interventions (started by three school psychologists), Flavorx (started by a man working in his parents' pharmacy), and The Pampered Chef (started by a homemaker).

There are businesses that do take a substantial amount of experience to successfully start and run. Most financial services and medical product companies, for example, are started by people with deep industry backgrounds and business expertise.

There are also technical aspects of starting a business such as finance and accounting, which take time and effort to learn and perfect, regardless of the type of business. In these instances, people who have business experience have a leg-up on those who don't. It's also easy to envision the advantage that someone who has managed people and run a successful business before might have over someone who hasn't.

Still, there are many examples of people who have started successful businesses without prior business experience. In the absence of knowing their individual stories, however, it's easy to believe the myth. Regrettably, this misconception causes capable people to never seriously investigate starting their own businesses. Without having information to the contrary, however, it's easy for people to assume that their lack of business experience is too difficult an obstacle to overcome.

To further dispel the myth that it takes a great deal of business experience to start a successful business and to provide suggestions to people who remain uneasy about their lack of business experience, this chapter is divided into three sections. The first section provides insight into the role that prior business experience plays in the business startup process. The second section focuses on business opportunities that minimize the need for substantial business experience. The third section focuses on techniques that help people overcome the lack of prior business experience as they launch their own businesses.

Insights Into the Role That Prior Business Experience Plays in the Business StartUp Process

In most startup situations, there are two benefits to having prior business experience. The first is the acquisition of specific skills. If you are proficient at accounting or know the ins and outs of hiring and managing people, those skills are helpful in starting and growing a business. The second benefit is a simple assimilation of how businesses run and what makes them successful. Simply by being part of the business world, people gain a sense of what works and what doesn't work in particular business situations.

The question then becomes how valuable is prior business experience in a startup setting and how much of an obstacle is not having this experience. Would Dell, darynkagen.com, and the other companies we've highlighted that were started by people with no business experience be stronger today if they had been started by experienced businesspeople? In addition, are there forms of business experience that might be a detriment rather than an advantage in a startup setting? And how much does practical experience count? If I've worked as an auto mechanic all my life and would like to open a store that sells customized auto accessories, am I capable of starting that business, or do I need to get some business experience first?

The sections that follow provide three insights about the role of prior business experience in the startup process. As you read through each, give careful thought to how the insight affects your own views on the topic. Many people overcome the fear that a lack of business experience is too large an obstacle by becoming more familiar with the startup process and by gaining a better appreciation of the value of the other skills and capabilities they possess.

Nearly Everyone Feels Inadequate on Some Level

The first insight regarding the role of prior business experience in the startup process is to keep the role of business experience in perspective. It's only one type of experience. There are many forms of experience that potentially affect the success of a new business, including business experience, practical experience in the specific area the business will operate in, sales experience, and leadership experience. Virtually no one has an ideal set of experiences as a foundation for starting a new business. Because of this, nearly everyone feels inadequate on some level. While the auto mechanic who wants to open a store to sell customized auto parts might feel inadequate because he doesn't have business experience, a seasoned business person with the same idea could feel inadequate because he doesn't know as much about repairing or modifying cars.

Feelings of inadequacy are also prompted by the sheer number of tasks people realize they'll be responsible for if they start their own businesses. This facet of business ownership causes people with business backgrounds to question whether their range of experience is adequate. For example, you might be a graphic artist who wants to open your own shop and have experience managing a staff and overseeing a budget, but might still feel uneasy because you have no experience in marketing or sales.

The overarching point of these observations is that nearly everyone feels inadequate in some aspect of starting a business. This emotion is so strong that some business owners say that their innermost fear is that their customers or employees will discover how much they really "don't know" about the business they've started. The first step to overcoming fear of inadequacy is to give yourself credit for the experiences you've had. If you think about the jobs you've had, the volunteer work you've done, the work you did in school, your family experiences, and so forth, your breadth of experience is probably more expansive than you first imagined. The second step is to boost your own self-efficacy for starting a business. Self-efficacy refers to your belief that you can perform a specific task (like starting a business). Several steps for boosting your self-efficacy for starting a business were discussed in Chapter 1, including reading books and articles about ordinary people who started successful businesses and participating in small business workshops and events where you get encouragement from business owners.

Certain Types of Business Experience Might Actually Hurt Rather Than Help You

The second insight is that there are certain types of business experiences that might actually hurt rather than help in your efforts to start a business. This heads-up refers to the difficulties some people have transitioning from a corporate environment to a small business, so these circumstances might not apply to you. Still, for those fitting this profile, it is important information to have.

The primary complication that occurs when people from corporate backgrounds try to start their own businesses is they have trouble adjusting to the constraints inherent to the startup setting. It's easy to envision the frustrations that someone might experience coming from a resource-rich large firm to trying to launch a business on a razor-thin budget. In addition, the skills that a person develops in a corporate setting are often not a good fit for a small firm. This point is made by Guy Kawasaki, a well-known investor and entrepreneur:

> *"Success in a big organization doesn't guarantee success in a startup. The skills needed in each context are different. A vice president of Microsoft (with its established brand, infinite resources, and 100 percent market share) may not be the right person for a 'two guys in a garage operation.'"*[1]

This mismatch of skills can also extend to management techniques and business processes. A person who has worked for IBM, Hewlett-Packard, and Motorola might have an impressive resume, but there is no guarantee that the IBM, Hewlett-Packard, or Motorola ways of doing things is appropriate for a specific small business. One silver lining to having limited or no business experience is that you're able to approach the challenge of starting a business with fresh eyes and no preconceptions. In some instances, simple commonsense management, applied by someone with limited or no business experience, might be more effective than the more sophisticated techniques that would be applied by someone with more business experience.

Domain-Specific Experience Is Often as Important as Business Experience

The third insight regarding the role of business experience in the startup process is that *domain-specific experience* is often as important as business experience. Domain-specific experience is experience in the specific area in which your startup will compete.

There are many companies that are started by people with unique insights into specific areas as a result of their jobs, hobbies, family responsibilities, or intense interest in particular areas. These people may or may not have business experience, but it's their domain-specific experience that is the motivating factor for starting the business.

An example of a business that was launched and is now being successfully run largely as a result of domain-specific experience is provided by Tish Ciravolo, the founder of Daisy Rock Guitars, a company that makes guitars just for women. Daisy Rock guitars are stylish, have feminine names (e.g., Atomic Pink, Power Pink, and Rainbow Sparkle), and incorporate design features that accommodate a woman's smaller hands and build. Ciravolo started playing the guitar when she was in high school and has devoted a large portion of her life to playing in bands and helping girls and women become acquainted with the guitar. The motivation for Daisy Rock grew from Ciravolo's desire to provide her own daughters and other females with something she didn't have when she was growing up—a guitar designed specifically for women. Commenting on this desire, Ciravolo said:

> *"When the time comes, I want their experience [referring to her daughters Nicole and Sophia] as musicians to be different from when I was growing up, when every guitar available was designed with men in mind. I want them to be able to walk into a music store anywhere and be able to find something made with them in mind. Daisy Rock is not about making me rich and famous or being a hero to anyone. It's simply an opportunity to leave a legacy for my kids and provide females with great instruments designed with them in mind."*[2]

This exemplifies how domain-specific knowledge, like Ciravolo's familiarity with the difficulties women face in playing guitars designed for men, provides insights that can lead to business ideas and actual products. No amount of business experience would have provided Ciravolo the insight she gleaned about guitars through her actual experiences. Founded in 2000, Daisy Rock's annual sales are now in excess of $2 million.

There are many other examples, some of which have been highlighted in this book, of people who have drawn upon domain-specific experience to get their businesses off the ground. An example is Doug and Lisa Powell, the business owners introduced in Chapter 2 who started Type 1 and Type 2 Tools, the company that provides age-appropriate motivational and educational material for child diabetics. It was Doug and Lisa Powell's familiarity with their daughter's disease and their skills as graphic designers that provided them the insights and capabilities needed to start the company.

Obtaining Domain-Specific Experience Over Time

One thing people thinking about starting their own businesses should consider, particularly if they are uneasy about the amount of business experience they have, is to start their businesses part-time and accumulate experience as they go. While this approach isn't possible in all situations, it can apply in more circumstances than you might think. By starting a business part-time, you can gain valuable experience, tuck away the money you earn, and find out if you really like the business before you quit your current job.

What's needed to start a business part-time is a little creativity regarding how to do it and a commitment to learn as much as possible along the way. For example, if your dream is to open a barbeque restaurant, you could start by catering barbeque on weekends as a way of learning the business and experimenting with recipes. If you'd like to open your own Web site design business, you could start on a freelance basis and obtain jobs through venues such as Elance (www.elance.com) and Craigslist (www.craigslist.com). If you make crafts and envision opening a craft store someday, you could start by selling your products at craft shows and through local stores on a consignment basis. That way you'll learn what sells and what doesn't sell and get a sense of whether you really want to operate a craft store full-time.

Opportunities That Minimize the Need for Substantial

Business Experience

One approach that people utilize to compensate for a lack of business experience is to pursue a business opportunity that minimizes the need for business experience. Many businesses require their founders to basically develop the businesses from scratch. In these instances, if the founders do not have prior business experience, they have to quickly get up-to-speed and learn the basics of starting a business. While business owners are often able to accomplish these objectives, there is an alternative. The alternative is to pursue a business opportunity in which the fundamentals of the business have already been thought out, and the business owner's responsibility is to run the business. Some approaches that fit this profile are franchising, direct sales, and businesses that have well-established business models.

Franchising

Franchising is a form of business ownership in which a firm that already has a successful product or service (franchisor) licenses its trademark and method of doing business to other businesses (franchisees) in exchange for an initial franchise fee and an ongoing royalty. The cost of buying into a franchise system varies, as shown in Table 4.1. The total initial investment includes the franchise fee, the costs associated with getting the franchise up and running (which vary by franchise), and any other fees that are part of the franchise agreement. The ongoing royalty fee, which is usually around 6%, is based on a percentage of weekly or monthly gross income.

Table 4.1. Initial Cost to the Franchisee of Opening a Franchise

Franchise Organization	One-Time Franchise Fee	Ongoing Royalty	Total Initial Investment
Subway	$15,000	8%	$74,900 to $222,800
Curves	$24,900 to $39,900	5% to 6%	$31,400 to $53,500
Great Clips	$25,000	6%	$98,900 to $184,700
CruiseOne Inc.	$9,800	3%	$9,800 to $25,400
WIN Home Inspection	$25,000	7%	$45,600 to $57,600
1-800-GOT-JUNK?	$20,000+	8%	$73,500 to $98,900
Cold Stone Creamery	$42,000	6%	$294,300 to $438,900

There are two primary advantages to buying a franchise as opposed to opening a business of your own. First, franchising provides a small business owner the opportunity to own a business using a tested and refined business system. This attribute reduces the amount of prior business experience needed to participate in most franchises. In addition, the trademark that comes with the franchise proves instant legitimacy for the business. For instance, if you're interested in opening a fitness center for women, you'll likely attract more customers by opening a Curves or Contours Express franchise than a new, independently owned business. The second advantage to buying a franchise is that the franchisor typically provides training, technical expertise, and other forms of ongoing support. For example, if you buy into a Contours Express franchise, your initial investment gets you Contours Express's exclusive 16-piece line of fitness equipment, cue tapes, wall charts, training on all business systems, and the support of a fitness professional who will help you open your center and run it for the first few days. Moving forward, you have access to a quarterly marketing package, an annual convention, and periodic training seminars. This type of training and support is what attracts people that lack business experience to the franchise option. According to Daren Carter, Contours Express's founder, 99% of the company's franchisees had no formal fitness training before they purchased a Contours Express franchise.[3] This level of inexperience is typical for a franchise system. In fact, some systems shy away from people with prior experience in the field the franchise operates in, fearing that they could have too many preconceived notions about how to run the business.

The main disadvantages of buying a franchise are the costs involved and the loss of some of your independence as a business owner. As shown in Table 4.1, there are substantial costs involved with buying into most franchise systems, and the royalties are permanent. While there are costs associated with opening an independent business, you get to keep 100% of your profits. In regard to independence, many franchise systems are sticklers about doing things in a very specific manner. McDonald's and other fast-food franchises, for example, are very strict in terms of their restaurants' appearance and how their food is prepared. As a result, franchising is typically not a good fit for people who like to experiment with their own ideas and are independently minded.

Ultimately, franchising represents an attractive middle ground for many people. So says John Cummings, the purchaser of a PostNet franchise. A PostNet franchise is similar to a FedEx Kinko's store. After a 21-year career with Bristol-Myers, Cummings took a buyout and spent a year deciding on what to do next. Commenting on why he settled on a PostNet franchise rather than opening his own business, Cummings said:

> *"I wanted to get what I call the best of both worlds—the support of a proven system in an environment that's really entrepreneurial. I felt a franchise was the best way to do that."*[4]

One note of caution—you should be careful if you decide to buy into a franchise system. While there are many excellent franchise systems to choose from, some systems never live up to the level of support promised. The best way to check out the merits of a franchisor is to ask for the names, addresses, and phone numbers of several of the franchisor's current franchisees and then call these individuals and ask them about their experiences. You can also ask for a copy of the franchisor's Uniform Franchise Offering Circular (UFOC), which is a document that contains 23 categories of information about the background and financial health of the franchisor. Section 20 of the document contains contact information for all of the system's current franchisees.

Direct Sales

The second type of business opportunity that minimizes the amount of prior business experience that's needed is *direct sales*. While most people cringe when they hear the words "direct sales" (or multi-level marketing), there are legitimate direct sales opportunities. Currently, there are over 14 million people in the United States involved in direct sales (full-time and part-time), and the industry generates roughly $30.5 billion in annual sales.[5] Well-known companies in the industry include Tupperware, The Pampered Chef, Avon, Mary Kay, World Book, and Discovery Toys.

Many people have negative feelings toward the direct sales industry because they have either personally been subjected to a high pressure sales pitch or know someone who has. Although the industry as a whole suffers as a result of these types of sales tactics, not all direct sales firms fit this stereotype, and there is an increasing number of highly legitimate opportunities. An example of a direct sales organization that exemplifies the good in the industry is The Pampered Chef, discussed in Chapter 2. The integrity and stature of the company is such that it was acquired by Berkshire Hathaway in 2002. Berkshire Hathaway is controlled by Warren Buffett, one of the most respected and well-known investors in the world. In the foreword to the book, *The Pampered Chef*, in which Christopher chronicles the history of the company, Buffett writes:

> *"The Pampered Chef is truly loved by its customers because it has found a need and filled it exceptionally well, helping everyday home cooks to become masters of their own home kitchens and making mealtime*

preparation quick, easy, and fun. It also offers its consultants an incomparable business opportunity, allowing men and women to build a home-based business of their own, based on Doris Christopher's personal blueprint for success. When you read the profiles of The Pampered Chef's Kitchen Consultants in Chapter 8, you may wonder what you're doing in your nine-to-five cubicle while these folks are happy cooking their way to fame and fortune."[6]

Most people start with an organization like The Pampered Chef part-time and only make it a full-time job if they do extremely well. The sales typically take place through in-home sales demonstrations or parties, although an increasing percentage of direct sales is taking place online. In addition to selling the product, you'll also recruit others to sell the product for you. You then receive a percentage of your recruits' sales, just like the person that recruited you receives a percentage of your sales. One of the lures of direct sales is that you can usually get started for a few hundred dollars, which gets you your initial inventory and sales material. Most direct sales organizations provide you with training, marketing material, and ongoing support. You also get a mentor and champion in the person that recruited you. The person that recruited you has a vested interest in your success, since he or she receives a commission on your sales.

If you go the direct sales route, make sure you associate with a reputable organization. One way to minimize the chances that you'll select a company you will later regret is to restrict your selection to organizations that are members of the Direct Selling Association (www.dsa.org), a highly respected industry trade group. To become a member of the Direct Selling Association, a firm has to go through a rigorous one-year application process and abide by the organization's Code of Ethics. Only 216 of more than 1,000 direct sales organizations that exist are currently members. If an organization is not a member of the Direct Sales Association, and you are still interested in joining, you should, at a minimum, check the company's history with your local Better Business Bureau, your state's Attorney General, and the Federal Trade Commission.

Azante Jewelry: How One Direct Sales System Got Started

Azante Jewelry was started by Cheri Larson in 2003. The original idea for the business was to sell jewelry through boutiques in Door County, Wisconsin. Shortly before the business was launched, a friend asked

Larson if she'd be willing to show her jewelry to a group of her friends. Larson agreed, and that gathering turned into $1,400 in sales. It also got Larson thinking that maybe a direct sales model was better than selling her jewelry through boutiques.

After a few similar outings, Larson decided to commit to the direct sales approach and spent the next year and a half researching the direct sales industry and the competition in her area. She also attended several small business seminars hosted by the Urban Hope Entrepreneurial Center in Green Bay, Wisconsin. The seminars focused on topics such as writing a business plan, researching markets, and understanding financial issues.

Larson formally rolled out her business in 2003 with two sales consultants. Her role was to design and oversee the manufacturing of the jewelry and encourage and motivate her independent sales force. Today, Larson employs five people at her Green Bay office and has 75 independent sales consultants. The thing that differentiates Azante Jewelry from jewelry that can be bought in stores is its quality and workmanship. Each piece is hand crafted and consists of a unique design.

Larson has no desire to grow Azante Jewelry quickly. Although she'd like to reach the heights of The Pampered Chef someday, that goal won't come soon. Still, Larson has high hopes for both the size of the business and her ability to grow her ranks of independent sales consultants. Commenting on the holistic nature of her business, Larson said:

> *"There's an opportunity to get quite large. The important thing is to offer an employment opportunity to women who might be stay-at-home moms or just want to work part-time."*[7]

Businesses That Have Well-Established Business Models

The third type of business opportunity that minimizes the amount of prior business experience that's needed is starting a business that has a well-established business model. A firm's business model describes how it operates and makes money. There are a number of businesses that have a fairly standard business model. Following these models negates, in part, the prior business experience needed to launch and run one of these businesses.

An example of a business with a well-established business model is a bed & breakfast. There are literally dozens of books available that provide advice about how to open and run a successful bed & breakfast. These books are very hands-on and contain worksheets and formulas that help estimate the cost of opening a bed & breakfast and provide instruction for how to manage day-to-day operations. To illustrate the strength and diversity of books that are available, a sample is provided in Table 4.2. There are also workshops held periodically across the country about how to open and operate a successful bed & breakfast. Several trade associations support the industry. An example is the Professional Association of Innkeepers (www.paii.org), which was founded in 1988 and now has over 3,000 members.[8] There are also bed & breakfast organizations that service smaller areas. Examples include the Wisconsin Bed and Breakfast Association (www.wbba.com) and Inn Virginia, the Bed & Breakfast Association of Virginia (http://innvirginia.org). Both organizations offer seminars for people thinking about opening their own bed & breakfast. A similar assortment of books, workshops, seminars, and trade associations is available for other businesses.

Table 4.2. Books That Provide Instruction for How to Open a Bed & Breakfast

Title and Author	Publisher and Year Published
How to Open a Financially Successful Bed & Breakfast or Small Hotel by Laura Arduser and Douglas R. Brown	Atlantic Publishing Company (2004)
Complete Idiot's Guide to Running a Bed and Breakfast by Susannah Craig and Park Davis	Alpha (2001)
How to Open and Operate a Bed & Breakfast (8th Edition) by Jan Stankus	Globe Pequot (2007)
How to Start and Operate Your Own Bed-and-Breakfast: Down-To-Earth Advice from an Award-Winning B&B Owner by Martha W. Murphy and Amelia R. Seton	Owl Books (1994)
So—You Want to Be an Innkeeper by Jo Ann M. Bell, Susan Brown, Mary Davis, and Pat Hardy	Chronicle Books (2004)

Another example of a business that someone with minimal prior business experience could open is an eBay store because there is an established method for opening one. eBay has a physical location on the eBay Web site (www.ebay.com) that a person can utilize to list the things he or she has for sale and to interact with customers. While you don't need an eBay store to sell items on eBay, most serious eBay sellers have one. eBay makes it extremely easy to set up a store. An easy-to-follow set of instructions is available on the eBay Web site, and the company offers a complementary selling consultation to anyone in the form of a one-on-one phone conversation with an eBay consultant. In addition, eBay makes forums available for eBay sellers to ask questions and discuss ideas with one another, and eBay University (www.ebayuniversity.com) provides access to training material and lists the itinerary for eBay seminars that are held in over 30 cities each year. There are also a large number of books that have been written by independent authors that provide instructions and tips for how to open an eBay store. The net result is that there are now reportedly over one million people worldwide making their living selling merchandise on eBay.

The overall point of this discussion isn't to draw attention to bed & breakfast businesses and eBay stores. The larger message is that there are many business opportunities, aside from franchising and direct sales, where the nuts-and-bolts of the business have been carefully thought out and are documented in easily accessible forms. This set of factors lessens the need for prior business experience in launching and running these businesses.

Techniques That Help People Overcome the Lack of Business Experience

Another approach that people take to compensate for a lack of business experience is to partner with someone who has business experience or join a support group. In fact, one of the most common reasons business partnerships form is that the individuals involved realize that they don't have sufficient experience and skill to launch businesses on their own. In addition, there are a growing number of social networks and forums that business owners can join to get support and advice from more experienced business people.

The two techniques covered in this section that help people overcome their lack of business experience are forming business partnerships and joining support groups/participating in online forums.

Forming Partnerships

An important decision a business owner faces is whether to start a business alone or whether to include a partner. A total of 56% of the firms included in the 2007 *Inc.* 5,000, which is the 5,000 fastest-growing private companies in the United States, were started by two or more people.[9] In general, it's believed that new ventures started by two or more people have an advantage over those started by an individual, because a team brings more talent, resources, ideas, and professional contacts to a new venture than does a sole business owner. In addition, the emotional and psychological support that the partners in a new business can offer one another can be an important element in a firm's success.

The ideal partnership brings together people with complementary experiences and skills. For example, an individual with technical skills, like a computer programmer, might want to seek out a partner who has business experience to create a more well-rounded team. This scenario played out for Kabir Shahani and Chris Hahn, the cofounders of Appature, a software company that targets the healthcare industry. In this instance, Hahn sought out Shahani to create a partnership in which their respective skills complement each other's. Shahani recalls:

> *"He [Hahn] had a lot of faith in my skills, and I feel really fortunate that he did. I'll never forget that conversation. We were sitting in a Thai restaurant in the International district [of Seattle], and he said, 'Look, I can build anything, and I think you can sell anything, so let's do it.'"*[10]

The biggest mistake people make in forming partnerships is partnering with others who have the same skills and same deficiencies that they have. The reason this happens is that people tend to draw from their circles of acquaintances when selecting a partner. Engineers know other engineers, physical therapists know other physical therapists, cooks know other cooks, and so forth. Try to resist the temptation of partnering with one of your peers. The best partnerships are the ones that bring together people with complementary skills.

You should be careful when selecting a partner because starting a business with another person is a major undertaking and places a strain on the best of relationships. This is why picking a business partner is often compared to selecting a spouse—it's a long-term relationship that is painful to terminate. One necessity in forming a business partnership is to create a written partnership agreement. You can get help doing this through your local Small Business Development Center, SCORE chapter, or an attorney.

There is also a full complement of small business legal forms, including a standard partnership agreement, available at www.findlaw.com. If you don't have a formal partnership agreement, you leave yourself open to the possibilities of serious disagreements down the road.

Joining Support Groups and Participating in Online Forums

Another technique business owners use to compensate for a lack of business experience is to join support groups and participate in online forums. All business owners need periodic advice and support. In addition, the simple act of hanging out with other business owners, whether in person or online, can be extremely helpful. A theme repeated throughout this book is that knowing the stories of other business owners can boost your own self-efficacy or belief that you can start and run a successful business. Joining a support group and/or regularly participating in online forums are ways of guaranteeing yourself that you will regularly interact with other business owners.

There is an increasing number of support groups available for business owners. Most of them target a specific demographic or focus on a particular industry. For example, there are several support groups for women business owners. An example is the National Association for Women Business Owners (www.nawbo.org), which provides services on a national level and supports 90 local chapters across the United States. The local chapters sponsor dinner meetings, lunch meetings, and other events where women business owners listen to speakers, participate in business-related workshops, and network with one another. Most of the local chapters host their own Web sites to highlight their events. An example is the Web site of the Orlando Chapter of the National Association for Women Business Owners, which is available at www.nawboorlando.org.

If you're looking for a support group in your area and can't find one, check the Meetup Web site. Meetup (www.meetup.com) is an online platform that allows individuals to organize local groups via the Web. Once a group is formed, its members "meet up" on a regular basis offline. The service, which was launched in 2002, has struck a chord, and there are currently over 13,000 Meetup groups worldwide, which focus on topics as diverse as cooking and flying kites. A growing number of these groups focus on some aspect of small business or entrepreneurship. To find out if there is a small business Meetup group in your area, simply type "small business" in the search box on the Meetup front page and enter your zip code. A sample of small business Meetup groups that were meeting when this chapter was written is included below. If there isn't a Meetup group in your area, you can start one.

- The Metro Detroit Small Business Meetup Group
- The Cincinnati Small Business Help Group
- Arizona & Easy Valley eBay Seller's Meetup Group
- Small Business Strategies for Success (Stone Mountain, GA)

- The San Diego E-Business Owner’s Meetup Group
- The Overland Park (Kansas) Work At Home Meetup Group

There are also a growing number of online forums that have been developed to provide small business owners support and advice. An example is StartupNation (www.startupnation.com).

The StartupNation Web site sponsors online forums for small business owners that cover topics such as selecting a business for yourself, business planning, developing your invention, and accounting and financial management. It also features open-ended forums such as "coffee talk," where small business owners can chat with one another about any topic that is on their minds. The general tone of the forums tends to be supportive and upbeat, which is exactly what many small business owners need. A small business forum that is more specific is the Small Business Computing and E-Commerce Forum (www.smallbusinesscomputing.com). This forum is similar to the one just described but focuses strictly on technology issues.

Summary

In the vast majority of cases, a lack of business experience isn’t a reason to stop someone from starting a business. No one starts a business with the ideal set of experiences and skills. The collection of experiences and skills that you presently have, along with a willingness to choose the business you start carefully and learn as you go, will serve you well if you decide to start a business of your own.

The next chapter focuses on the myth that the best business ideas are already taken. By looking around, it’s easy to see why this myth is so prevalent—there are literally thousands of products to choose from. But in reality, people come up with new business ideas everyday—many of which make a real difference in people’s lives. In Chapter 5, we show you how to identify and generate new business ideas.

Endnotes

1. Guy Kawasaki, *The Art of the Start* (New York: Portfolio, 2004), 102.
2. Daisy Rock home page, http://www.daisyrock.com (accessed September 20, 2007).

3. Franchise Gator home page, http://www.franchisegator.com (accessed September 20, 2007).

4. CJ Prince, "Buying Balance by Finding a Franchise," *Success Magazine*, http://www.successmagazine.com/article.php?article_id=195 (accessed September 20, 2007).

5. Direct Sales Association home page, http://www.dsa.org (accessed September 21, 2007).

6. Doris Christopher, *The Pampered Chef* (New York: Doubleday, 2005), ix.

7. Leah Call, "Direct Sales Success," *Wisconsin Entrepreneur's Network*, http://www.wenportal.org (accessed September 20, 2007).

8. Professional Association of Innkeepers home page, http://www.paii.org (accessed September 21, 2007).

9. *Inc.*, November 20, 2007.

10. nPost, accessed September 22, 2007 (see chap. 1, n. 11).

Chapter 5. Myth No. 5: The Best Business Ideas Are Already Taken:
Truth No. 5: There Are an Infinite Number of Possibilities for Good Business Ideas

Introduction

Of all the myths surrounding business ownership, the notion that the best business ideas are already taken is the most exaggerated. It simply isn't true. New businesses based on new ideas are started everyday. In addition, there is nothing wrong with starting a business that's a slight variation of something that already exists. In fact, most new businesses do not launch revolutionary new products or services—they are just too expensive to bring to market. Though there are exceptions. FedEx, for example, was started in the 1970s on the revolutionary idea of creating a system to facilitate the overnight delivery of packages. Far more common are businesses such as The Pampered Chef, which sells unique but not revolutionary kitchen products, and Daisy Rock, which sells guitars that are designed specifically for women but are otherwise regular guitars.

The reason it's easy to believe the myth that the best business ideas are already taken is that it seems as if the marketplace as crowded and full of products that meet every conceivable need. In many instances, this perception is correct. Think of how many different choices we all have for car insurance, credit cards, house paint, and tires. These are products in mature industries where it is difficult to think of new business ideas. But for someone who's thinking about starting a business, there are ample opportunities elsewhere. For example, think about how society is changing. The aging of the population alone is spawning new business ideas almost daily—from fitness centers designed specifically for older people to cell phones that have large buttons and bright screens to make them easier for older people to use and see. There are also many problems that remain unsolved. This sentiment is captured by Philip Kotler, a marketing expert, who said:

> *"Think about problems. People complain about it being hard to sleep through the night, get rid of clutter in their homes, find an affordable vacation, trace their family origins, get rid of garden weeds, and so on. As*

the late John Gardner, founder of Common Cause, observed: 'Every problem is a brilliantly disguised opportunity.'"[1]

The gist of Kotler's point is that potential business owners have fertile ground in which to discern new business ideas. If you agree with this sentiment, it makes more sense to believe that the best business ideas have yet to be discovered rather than the best business ideas are already taken.

How, then, are new business ideas discovered? And what are the attributes of effective versus ineffective ideas? Even if we've convinced you by now that the best business ideas aren't already taken, you're still left with the task of coming up with a business idea as the foundation for starting your own business. To address these issues and further dispel the myth that the best business ideas are already taken, this chapter is divided into two sections. The first section focuses on the three most common sources of new business ideas. The second section focuses on techniques that potential business owners use to explore these sources and generate business ideas.

Three Most Common Sources of New Business Ideas

The first step in discerning new business ideas is to understand where business ideas come from. In our experience, business ideas emerge from three sources: changing environmental trends, unsolved problems, and gaps in the marketplace. A recognition and understanding of these sources is helpful to people who are trying to identify business ideas for themselves. Once you understand the importance of each of these sources, you'll be much more likely to look for opportunities and ideas that fit each profile. One thing to be careful about as you read through each source is immediately thinking of an idea and quickly moving forward with it. Business owners often think of many ideas before they settle on the idea that becomes their business—so don't rush the process. It's also important not to select an idea simply because it is appealing. Although the conviction and passion for an idea is vitally important, the key to the selection process is to identify a product or service that people need and are willing to buy, not one that seems fun or attractive to sell.

Now let's look at the three most common sources of business ideas, as reflected in Figure 5.1.

Figure 5.1. *Three sources of new business ideas*

A Critical Issue When Searching for a Business Idea: Selecting an Idea That Can be Sold Into a Niche Market

One rule-of-thumb that you should adhere to when searching for a business idea is to select an idea that can be sold into a niche market.

A *niche market* is a place within a larger market segment that represents a narrower group of customers with similar needs. Starting by selling to a niche market allows a firm to focus on serving a specialized market very well instead of trying to be everything to everyone in a broad market, which is nearly impossible for a new firm. The challenge in identifying an attractive niche market is to find a market that's large enough for the proposed business but is yet small enough to avoid attracting larger competitors, at least during the time it takes for the new business to successfully get off the ground. An example of a company that has selected a niche market that meets these criteria is Dogster (www.dogster.com), a social networking site for dog owners. The site allows its users to create profiles for their dogs, participate in dog-related forums, post photos and video clips of their dogs, and perform a number of other activities. The site, which was started from scratch in 2004 with its sister site, Catster (www.catster.com), now has over 275,000 human members, 340,000 photos of dogs and cats, and a collection of blue-chip advertisers, including Disney and Target. Although the firm operates in the $36 billion pet industry, it has carved out a specialized niche market for itself and is reported to be operating in the black and generating more than a million dollars a year in advertising revenue.

As Dogster gains momentum and financial resources, it may grow beyond this specialized market but has gotten off to a good start largely because it has remained laser-focused on a clearly defined niche market (social networking for dog and cat owners) rather than spreading itself too thin in the larger pet industry.

Changing Environmental Trends

The first source of new business ideas is changing environmental trends. The most important trends for people to follow in thinking of starting their own business are economic trends, social trends, technological advances, and political action and regulatory changes. Changes in these areas often provide the impetus for new business ideas. When looking at environmental trends to discern new business ideas, there are two caveats to keep in mind. First, it's important to distinguish between trends and fads. New businesses typically do not have the resources to ramp up quickly enough to take advantage of a fad. Second, even though we discuss each trend individually, they are interconnected and should be considered simultaneously when brainstorming new business ideas. For example, one reason the Apple iPod is so popular is because it benefits from several trends converging at the same time, including teenagers and young adults with increased disposable income (economic trend), an increasingly mobile population (social trend), and the continual miniaturization of electronics (technological trend). If any of these trends weren't present, the iPod wouldn't be as successful as it is.

Table 5.1 provides examples of how changes in environmental trends have provided the impetus for new business ideas and new businesses. The following is a discussion of each trend and how changes in a trend provide openings for new business and product ideas.

Table 5.1. Companies Started to Take Advantage of Changes in Environmental Trends

Changing Environmental Trend	Resulting New Business Opportunities	Companies That Resulted
Economic Trends		
Search for alternatives to traditional fossil fuels like gasoline and diesel fuel	Ethanol, biodiesel, solar power, wind-generated power	SolFocus, Seattle Biodiesel, Misole
Teenagers with more cash and disposable income	Designer clothes, compact discs, MP3 players, game consoles	Hot Topic, Karma Loop, SanDisk
Social Trends		
Increased interest in different, tastier, and healthier food	Healthy-fare restaurants, organic foods, healthy-focused grocery stores	Chipotle, White Wave, Whole Foods
Increased interest in fitness as the results of new medical information warns of the hazards of being overweight	Fitness centers, in-house exercise equipment, health food stores	Curves, Espresso Fitness, GNC Nutrition Center
Technological Advances		
Development of the Internet	E-commerce, improved supply chain management, improved communication, social networking	Google, Amazon.com, Travelocity, MySpace.com
Miniaturization of electronics	Laptop computers, MP3 players, PDAs	Digital Lifestyle Outfitters, Palm, Research In Motion
Political and Regulatory Changes		
Increased EPA and OSHA standards	Consulting companies, software to monitor compliance	ESS, PrimaTech, Compliance Consulting Services, Inc.
Sarbanes Oxley Act of 2002	Software vendors, consulting companies	CEBOS, OiWare, Nexum

Economic Trends

An understanding of economic trends is helpful in determining areas that are ripe for new business ideas as well as areas to avoid. When the economy is strong, people are more willing to buy discretionary products and services that enhance their lives. Individual sectors of the economy have a direct impact on consumer buying patterns. For example, a drop in interest rates typically leads to an increase in new home construction, furniture sales, and appliance sales. Conversely, a string of corporate layoffs or a rapid decline in the stock market normally leads to a reduction in the demand for luxury goods such as expensive clothing and cars.

When studying how economic trends affect opportunities, it is important to evaluate who has money to spend and what they spend it on. For example, an increase in the number of women in the workforce and their related increase in disposable income is largely responsible for the number of clothing stores targeting professional women that have opened in the past several years. Some of the boutiques, like Ellen Tracey and Tory Burch, compete on a national scale, while others, like Olivine, in Seattle, are single-store boutiques that have been opened by an individual entrepreneur. There are also an increasing number of online stores that serve specific niche markets. For example, Shade Clothing is a realitvely new online store that designs and sells clothing for women who want apparel that is stylish yet not too revealing.

Similarly, as baby boomers reach retirement age, a sizeable portion of their spending will be redirected toward areas that make their retirment more comfortable, enjoyable, and secure. This trend will invariably spawn new businesses in many areas, largely because baby boomers have greater disposable income relative to previous generations. The most promising areas include finance, travel, housing, recreation, entertainment, and health care.

An understanding of economic trends can also help identify areas to avoid. For example, this is not a good time to start a company that relies on fossil fuels, such as airlines or trucking, because of high fuel prices. There are also certain product categories that suffer as a result of economic circumstances. This is not a good time to start a company that sells musical instruments, for example, such as violins, trumpets, and tubas. Domestic production of musical instruments has declined 3% annually over the past four years, and U.S. imports of musical instruments were down 7% from 2005 to 2006.[2] A major reason for this decline is that middle schools and high schools, which have historically been major buyers of musical instruments, have reduced their purchases due to budget cuts. In addition, the advent of online auction sites like eBay has made it easy for people to sell used musical instruments, which has cut into the market for new musical instrument sales.

Social Trends

An understanding of the impact of social trends on the way people live their lives and the products and services they need provides fertile ground for new business ideas. Often, the reason that a product or service exists has more to do with satisfying a social need than the more transparent need the product fills. For example, the proliferation of fast-food restaurants isn't due primarily to people's love for fast food but rather to the fact that people are busy and often don't have time to cook their own meals. Similarly, social networking sites such as MySpace and Facebook aren't popular because they can be used to post music and pictures on a Web site. They're popular because they allow people to connect and communicate with each other, which is a natural human tendency.

Changes in social trends alter how people and businesses behave and how they set their priorities. These changes affect how products and services are built and sold. A sample of the social trends that are currently affecting how individuals behave and set their priorities is provided here:

- Retirement of baby boomers
- The increasing diversity of the workforce
- Increasing interest in healthy foods and "green" products
- New forms of music and other types of entertainment
- The increasing focus on health care, fitness, and wellness
- Emphasis on alternative forms of energy
- Increasing globalization of business
- Increased purchasing power of women
- Increased purchasing power of teenagers and preteens
- Increased availability of inexpensive yet relatively powerful personal computers

Each of these trends is providing the impetus for new business ideas and will continue to do so. For example, the increasing emphasis on alternative forms of energy is spawning business ideas ranging from solar power, to wind-generated electricity, to alternatives for fossil fuels. One new company, Greasecar Vegetable Fuel Systems, makes conversion kits that allow diesel engines to run on vegetable oil. Justin Carvan, the company's founder, got interested in alternative fuels while at Hampshire College. The company is now growing at a rate of more than 200% per year and is projected to reach $2.5 million in annual sales shortly.[3] The increasing emphasis on green products is another social trend that is spawning interesting new business ideas. An example of a recent startup in this area is South West Trading Co., a business that specializes in earth-friendly, alternative fibers and textiles such as yarns made from bamboo, corn, and even recycled crab shells.

Technological Advances

Technological advances provide an ongoing source of new business ideas. In most cases, the technology itself isn't the key to recognizing business opportunities. Instead, the key is to recognize how technologies can be used and harnessed to help satisfy basic or changing human needs. For example, the creation of the cell phone is a technological achievement, but it was motivated by an increasingly mobile population that finds many advantages to having the ability to communicate with coworkers, customers, friends, and families from anywhere and everywhere.

Technological advancements also provide opportunities to help people perform everyday tasks in better or more convenient ways. For example, OpenTable.com is a Web site that allows users to make restaurant reservations online and now covers most of the United States. If you're planning a trip to San Francisco, for example, you can access OpenTable.com, select the area of the city you'll be visiting, and view descriptions, reviews, customer ratings, and in most cases the menus of the restaurants in the area. You can then make a reservation at the restaurant and print a map of directions. The basic tasks that OpenTable.com helps people perform have always been done—looking for a restaurant, comparing prices and menus, soliciting feedback from people who are familiar with competing restaurants, and getting directions. What OpenTable.com does is help people perform these takes in a more convenient and expedient manner.

Another aspect of technological advances is that once a technology is created, products often emerge to advance it. For example, the creation of the Apple iPod has created an entire industry that produces iPod accessories. An example is H2OAudio, a company that was started by four former San Diego State University students that makes waterproof housings for the iPod and the iPod nano. The waterproof housing permits iPod users to listen to their iPods while swimming, surfing, snowboarding, or engaging in any activity where the iPod is likely to get wet. There is a wide variety of other accessories available for the iPod, from designer cases to car rechargers. It is now estimated that for every $3 spent on an iPod, at least $1 is spent on an accessory.[4] Technology advances also give us new platforms to sell everyday products and services more efficiently and effectively. For example, at least four companies on the 2007 *Inc.* 500 started by selling their products on eBay.[5]

Political Action and Regulatory Changes

Political and regulatory changes also provide the basis for new business ideas. For example, new laws create opportunities for business owners to start firms to help companies, individuals, and governmental agencies comply with the laws. A case in point is the No Child Left Behind Act of 2002. The act, which is based on the notion of outcome-based education, requires states to develop criterion-based assessments in basic skills to be periodically given to all students in certain grades. Shortly after the act was passed, Kim and Jay Kleeman, two high school teachers, started Shakespeare Squared, a company that produces materials that help schools comply with the act. On some occasions, changes in government regulations motivate business owners to start firms that differentiate themselves by "exceeding" the regulation. For example, several years ago, the Federal Trade Commission changed the regulation about how far apart the wood or metal bars in an infant crib can be. If the bars are too far apart, a baby can get an arm or leg caught between the bars, causing an injury. A obvious business idea that might be spawned by this type of change is to produce a crib that is advertised and positioned as "exceeding" the new standard for width between bars and is "extra safe" for babies and young children. The change in regulation brings attention to the issue and provides ideal timing for a new company to reassure parents by providing a product that not only meets but exceeds the new regulation.

Political change also engenders new business and product opportunities. For example, global political instability and the threat of terrorism have resulted in many firms becoming more security conscious. These companies need new products and services to protect their physical assets and intellectual property as well as protect their customers and employees.

How Changing Environmental Trends Has Caused an Upswing in (of All Things) Mattress Sales

Some industries experience slow or no growth for years and experience sudden upswings in growth and popularity as the result of savvy industry incumbents or new business founders who realize that environmental change has turned in favor of the industry. In these instances, the businesses that pick up on these changes first and get out in front of the competition have an advantage. A recent example is the mattress industry. In *Business Week's* 2007 list of The Best (100) Small Companies to Watch, two of the companies, Select Comfort and Tempur-Pedic International, are mattress companies. Seriously, with all the high-tech and other interesting companies in the United States, would you have guessed that two mattress companies would have made the list? Probably not. But if you study the mattress industry, your sentiments will change. There are a number of significant environmental trends working in favor of the industry. These trends include:

- Rising incomes and a positive economic environment have led to increased mattress sales at the high end of the market.
- High shipping costs have limited imports from China and elsewhere (imports represent only 2.9% of U.S. mattress sales).
- The recent upswing in hotel and motel construction has resulted in a spike in mattress demand.
- There are roughly 2.7 million hospital and nursing home beds in the United States. These facilities typically purchase high-end mattresses with enhancements that allow them to be electronically adjusted. As the population ages, the healthcare market for mattresses will continue to grow.
- An increased emphasis on fitness and wellness has created new markets for mattresses that improve sleep quality and provide better neck and back support.

On Select Comfort and Tempur-Pedic's Web sites, you'll see that they're tapping into these exact trends. The broader U.S. mattress industry grew by 8.8% in 2004 and 6.9% in 2005, which are both impressive growth rates.

Unsolved Problems

The second approach to new business ideas is unsolved problems. Problems can be experienced or recognized by people through their jobs, hobbies, or everyday activities. Consistent with this observation, many companies have been started by people who have experienced a problem in their own lives, and in the process of solving the problem realized that they were on to a business idea. For example, in 2006 Christine Ingemi, a mother of four children under 11, became concerned by how loud her children were playing their MP3 players. She said she could hear music coming through her children's MP3 players' earphones when she was driving her van with the music on. To prevent her children from playing their MP3 players too loud, she and her husband, Rick, did some research, interviewed several audiologists, and invented a set of earbuds that limit the volume entering the user's ears. After her kids started using the earbuds, Ingemi began getting inquires from other parents asking where they could get a similar device. To make the device available to others, Ingemi started a business, called Ingemi Corp., to sell her IHearSafe earbuds.[6] Similarly, Laura Udall, another mother, invented an alternative to traditional backpacks when her fourth-grade daughter complained daily that her back hurt from carrying her backpack. After conducting research, obtaining feedback from student focus groups, and building several prototypes, Udall invented the ZUCA, a backpack on rollers that strikes the ideal balance between functionality and "cool" for kids. ZUCA is now a successful company, and its rolling backpacks can be purchased online or through a number of retailers.

Advances in technology often result in problems for people who can't use the technology in the way it is sold to the masses. For example, some older people find traditional cell phones hard to use—the buttons are small, the text is hard to read, and it's often difficult to hear someone on a cell phone in a noisy room. To solve these problems, GreatCall Inc., a recent startup, is producing a cell phone called the Jitterbug, which is designed specifically for older users. The Jitterbug features large buttons, easy-to ready text, and a cushion that cups around the ear to improve sound quality. The phone also includes a button that connects the user directly with an operator who can assist in completing a call. Another company, Firefly Mobile, has created a cell phone designed specifically for tweens, ages 8 to 12. The phone only weighs two ounces and is designed to fit a kid's hand. The phone includes appropriate limitations for a young child and speed-dial keys for Mom and Dad.

A useful technique to use when confronted with a difficult problem is to find an instance where a similar issue was solved and then apply that solution to your problem. An example is provided by Susan Nichols, the founder of Yogitoes (www.yogitoes.com), a company that makes nonslip rugs for Yoga enthusiasts. Several Yoga positions require participants to strike poses where they balance their weight on their feet at an angle. In this position, it is easy to fall or slip when using a regular rug or mat. Nichols looked for a Yoga mat that would prevent her from slipping but found out that no one knew how to make one. So she started looking for an example of a product that was designed specifically to prevent it from slipping on a hard floor, to study how it functioned. Eventually, she stumbled upon a dog bowl with rubber nubs on the bottom to prevent it from sliding when a large dog ate or drank from it. Using the dog bowl (of all things) as a model, Nichols found a manufacturer who helped her develop a rug with small PVC nubs that prevent yoga participants from slipping when they perform Yoga moves. Nichols started Yogitoes to sell the rugs, and sales were on track to hit $3 million in 2006.[7]

Many other colorful examples of people who launched businesses to solve problems are included in Table 5.2.

Table 5.2. Companies Started to Solve a Problem

Business Founder	Year	Problem	Solution	Company That Resulted
Arlene Harris	2006	Many cell phones are too complicated, and the buttons are too small for seniors to use easily.	Designed a cell phone for seniors that is easy to use, has large buttons, and has a single button that when pushed connects to an operator who can assist with a call.	GreatCall
Scott Kliger	2006	411 directory assistance calls are expensive, costing from $1.25 to $3.75 per call, depending on the cellular provider.	Created a free, nation-wide, advertiser-supported, directory assistance service.	Jingle Networks
David Bateman	2002	No way for apartment renters to pay their monthly rent online.	Created a software product that allows apartment complexes to enable their tenants to pay online.	Property Solutions
Lisa Druxman	2002	No fitness routine available to help new mothers stay fit and be with their newborns at the same time.	Created a franchise organization that promotes a workout routine (which involves a 45-minute power walk with strollers) that mothers and their babies can do together.	Stroller Stride
Richard Cole	1999	No service available to help people with computer problems at home.	Created an organization that makes "house calls" and helps people solve computer problems in their homes.	Geeks On Call

Gaps in the Marketplace

The third source of business ideas is gaps in the marketplace. There are many examples of products that consumers need or want, that aren't available in a particular location or aren't available at all. Part of the problem is created by large retailers, like Wal-Mart and Costco, which compete primarily on price and offer the most popular items targeted toward mainstream consumers. While this approach allows the large retailers to achieve economies of scale, it leaves gaps in the marketplace. This is the reason that clothing boutiques and specialty shops exist. These businesses are willing to carry merchandise that doesn’t sell in large enough quantities for Wal-Mart or Costco to carry.

There are also product gaps in the marketplace, many of which represent potentially viable business opportunities. For example, in 1997, Julie Aigner-Clark realized that there were no videos on the market to expose her one-year old daughter to music, the arts, and science. To fill this gap, she started Baby Einstein, a company that produced uplifting videos for children aged three months to three years. The company did so well that it was acquired by Disney in 2001. A more common example of a company that filled a gap in the marketplace is provided by p.45 (www.p45.com), a women’s clothing boutique in Chicago. The store carries innovative collections from young fashion designers, original pieces of jewlery made by Chicago area residents, unique shoes, and accessories that complement the clothing in the store. p.45 fills a gap in the marketplace by offering people with particular tastes a line of clothing and accessories that they couldn’t find in mainstream stores. It is also located in an area of Chicago that has a sufficient critical mass of upscale shoppers to support the store.

A common way that gaps in the marketplace are recognized is when people become frustrated because they can’t find a product or service that they need and recognize that other people feel the same frustration. This scenerio played out for Lorna Ketler and Barb Wilkins, who became frustrated when they couldn’t find stylish "plus-sized" clothing that fit. In response to their frustration, they started Bodacious (www.bodacious.ca), a store that sells fun and stylish clothing for hard-to-fit women. Ketler and Wilkins’ experience illustrates how compelling a business idea can be when it strikes just the right cord by filling a gap that deeply resonates with a specific clientele. Reflecting on the success of Bodacious, Wilkins said:

> *"It’s so rewarding when you take a risk and it pays off for you and people are telling you every single day, ’I’m so glad you’re here.’ We’ve had people cry in our store. It happens a lot. They’re crying because they’re so happy (that they’re finding clothes that fit). One woman put on a pair of jeans that fit her, and she called me an hour later and said, ’They still look good, even at home!’ Sometimes people have a body change that happens, whether they*

have been ill or had a baby, and there's lots of emotion involved in it. If you can go out and buy clothes that fit, that helps people feel good about themselves."[8]

A related technique for generating new business ideas is to take an existing product or service and create a new category by targeting a completely different target market. This approach essentially involves creating a gap and filling it. An example is PopCap games (www.popcap.com), a company that was started to create a new category in the electronic games industry called "casual games." The games are casual and relaxing rather than flashy and action-packed and are made for people who want to wind down after a busy day. Currently, 90% of the company's customers are women 25 years old or older, which is a completely different demographic than the young males that the mainstream game manufacturers target.[9] Another approach to filling gaps in the marketplace is to service an area that is lacking a particular product or service. For example, SPC Office Products (www.spcop.com) is a company that sells the same products as Staples and Office Depot but focuses on towns under 20,000 in population. As a rule of thumb, SPC doesn't like to open a store that's within 120 miles of a Staples or Office Depot.[10]

Other examples of companies that were launched to fill gaps in the marketplace are included in Table 5.3.

Table 5.3. Companies Started to Fill a Gap in the Marketplace

Gap in the Marketplace	Resulting New Business Opportunity	Companies That Resulted
No fitness centers designed specifically for women.	Created a fitness center that is just for women, features workouts and exercise machines designed specifically for women, and fits the time and budgetary constraints of its female clientele.	Curves, Contours Express, Lady of America
Lack of toys that focus on the intellectual development of a child.	Toy stores, direct-sales organizations (like Tupperware), and Web sites that sell educational toys.	Discovery Toys, Kazoo & Company
No hair care, skin care, and body care stores that are fresher and more sophisticated than standard Bath and Body outlets but less upscale than high-end stores like Nordstrom's and Sacks.	Specialty boutiques that offer fresh, new, natural, and organic hair care, skin care, and body care products.	Aveda, Origins, Sephora
Restaurants that are both fast and serve good food.	Fast-casual restaurants that combine the advantages of fast-food (fast service) and casual dining (good food).	Panera Bread, Chipotle, Cosi
Shortage of clothing stores that sell fashionable clothing for hard-to-fit people.	Boutiques that sell fashionable clothing for hard-to-fit people—which may include plus-sized clothes, maternity clothes, or clothing for tall or short people.	Casual Male, Ashley Stewart, Casual Plus

Techniques for Generating Ideas

Most businesses are started in one of two ways. Some businesses are internally stimulated. An individual, who hadn't necessarily been thinking about starting a business, sees a problem or recognizes a gap in the marketplace and creates a business to fill it. This was the case with Laura Udall of ZUCA as well as Julie Aigner-Clark of Baby Einstein, who were discussed earlier. Other businesses are externally stimulated. In this instance, an individual has a strong interest in starting a business and then starts looking for ideas for businesses to start. This was the case with Jeff Bezos, the founder of Amazon.com. In 1994, Bezos quit his lucrative job at a New York City investment firm and headed for Seattle with a plan to find an attractive opportunity and launch an e-commerce firm. After kicking around a number of different ideas, he settled on books and started Amazon.com.

This section of the chapter focuses on two techniques that people use to try to explicitly generate new business ideas. These techniques are most commonly used by people searching for business ideas but are also used by people who spot an opportunity (like Laura Udall did when she realized that her daughter needed a different kind of backpack) and want to flesh-out their ideas. Having knowledge about each of the three most common sources of business ideas, articulated here, enhances each of these techniques.

One point to remain mindful of while considering these techniques is that business ideas take time to develop, so it’s important not to become discouraged if an idea doesn’t surface quickly. It’s also important to realize that the best ideas aren’t necessarily the most original—as long as the idea is "different" enough that it adds unique value for the consumer. As mentioned earlier in the chapter, it normally exceeds the budget of a new firm to educate the public about a revolutionary or completely original idea.

Why the Most Original Ideas Aren’t Always the Best Ideas

When considering business ideas, it’s important to realize that the best ideas aren’t always the most original ones, as indicated at the beginning of the chapter. New firms don’t often have the capital to effectively get their names and products or services quickly recognizable.

The diagram pictured here provides a quick visual depiction of the four categories of new business ideas and the most realistic categories for new firms. The simplest ideas (existing products in existing markets) are located in Box 1 and are generally undesirable because they are in crowded fields with stiff competition. The trickiest and most expensive to implement ideas are in Box 4 (new products in new markets) and are usually avoided because they put a new firm too far out on a limb. The most practical ideas for most new businesses are located in either Box 2 or Box 3. The vast majority of new businesses referred to in this book are Box 2 or Box 3 startups.[11]

	Existing Products	New Products
Existing Markets	1	2
New Markets	3	4

Brainstorming

The term *brainstorming* is a catch phrase that means different things to different people. In general, brainstorming is simply the process of generating several ideas about a specific topic. It can easily be used to generate business ideas. The approaches range from a person sitting down with a yellow legal pad and jotting down interesting business ideas to formal "brainstorming sessions" led by moderators that involve a group of people.

In a formal brainstorming session, the leader of the group asks the participants to share their ideas. One person shares an idea, another person reacts to it, another person reacts to the reaction, and so on. A flip chart or whiteboard is typically used to record the ideas. A productive brainstorming session is freewheeling and lively. The session is not used for analysis or decision-making—the ideas generated during a brainstorming session need to be filtered and analyzed, but this is done later. The number one rule of a brainstorming session is that no criticism is allowed, including chuckles, raised eyebrows, or facial expressions that express skepticism or doubt. Criticism stymies creativity and inhibits the free flow of ideas.

Brainstorming sessions dedicated to generating new business ideas are often less formal. For example, during the creation of Proactiv, a popular acne treatment product, Dr. Katie Rodan, one of the company's founders, hosted dinner parties at her house and conducted brainstorming sessions with guests. The guests included business executives, market researchers, marketing consultants, the chief financial officer of a major company, an FDA regulatory attorney, and others. Rodan credits this group with helping her and her cofounder brainstorm a number of ideas that helped shape the company and move the process of starting the company along.[12] Similarly, Sharelle Klause, the founder of Dry Soda, a company that makes an all-natural soda that's paired with food the way wine is in upscale restaurants, tested her idea by first talking to her husband's colleagues, who were in the food industry, and then tapped into the professional network of a friend who owned a bottled water company. Through this process she met a chemist, who was instrumental in helping her develop the initial recipes for her beverage. Klause also went directly to restaurant owners and chefs to ask them to sample early versions of her product.[13] While this approach only loosely fits the definition of brainstorming, the spirit is the same. Klause was bouncing ideas and early prototypes of her product off others to get their reactions and generate additional ideas.

Approaches to brainstorming are only limited by your imagination. For example, to teach her students an approach to utilizing brainstorming to generate business ideas, Marcene Sonneborn, an adjunct professor in the Whitman School of Management at Syracuse University, uses a tool she developed called the "bug report" to help her students brainstorm business ideas. She instructs her students to list 75 things that "bug" them in their everyday lives. The number 75 was chosen because it forces students to go beyond thinking about obvious things that bug them (campus parking, roommates, scraping snow off their windshields in the winter), and think more deeply. On occasion, students actually hold focus groups with their friends to brainstorm ideas and fill out their lists. Another particularly effective approach to brainstorming is to utilize the three sources for new business ideas as a way of organizing the discussion. Imagine this: Suppose you are part of a small group that is trying to brainstorm ideas for a new type of fitness center. You know the market is too crowded to support another generic center, so you’re looking for novel ideas. You create three columns on a whiteboard labeled Changing Environmental Trends, Unsolved Problems, and Gaps in the Marketplace. You then start brainstorming specific ideas, looking at each category individually, and then at how the categories interact with each other. After brainstorming dozens of ideas in each category, you start grouping the ideas into themes or patterns to create more solid ideas. One pattern jumps out at you: The population is aging, older people are increasingly interested in fitness, many of the exercise machines and classes taught in traditional fitness centers aren’t suitable for older people, and there are no fitness centers designed specifically for the 50+ demographic. Based on this pattern, your first solid idea is to create a fitness center designed specifically for people 50 years old and older.

Library and Internet Research

A second approach people can use to generate new business ideas is to conduct library and Internet research, as discussed briefly in Chapter 2. A natural tendency is to think that an idea should be chosen, and the process of researching the idea should then begin. This approach is too linear. Often, the best ideas emerge when the general notion of an idea, like opening an innovative type of fitness center, is merged with extensive library and Internet research, which might provide insights into the best type of innovative fitness center to pursue.

Libraries are often an underutilized source of information for generating business ideas, as mentioned earlier in the book. The best approach to utilizing a library is to discuss your general area of interest with a reference librarian, who can point out useful resources, such as powerful online resources that libraries often have access to. An example is Mintel, an online resource that publishes market research on all major industries and subcategories within industries. Mintel has literally dozens of pages of information on the "Health and Fitness Club" industry alone. Spending time reading through the information could spark new ideas for fitness centers or help affirm an existing idea. Just a few minutes reading Mintel’s report bodes well for the idea of opening a fitness center for the 50+ demographic. According to the report, while 45% of people say they exercise regularly, only 22% belong to fitness clubs, which suggests there are opportunities for membership growth. Households with higher incomes are more likely to belong to fitness clubs, which fits the 50+ demographic. Individuals who are 35 to 54 are the most likely candidates to join health clubs. Interestingly, 67% of the people who currently don’t belong to a fitness club said they would join if they knew the activities would keep them motivated. Mintel’s summary of the fitness club industry concluded by stating, "It is important for health clubs to tailor their offerings to their target market."[14] This is exactly what a fitness center for the 50+ demographic would do. Equally insightful information is available for all industries, so it might be a good use of your time to visit a university or large city library to access the Mintel report on your area of interest.

Internet research is also important. If you’re starting from scratch, simply type "new business ideas" into Google or Yahoo!, and it will produce links to newspaper and magazine articles about the "hottest" and "latest" new business ideas. While these types of articles are general in nature, they provide a starting point if you’re trying to generate new business ideas from scratch. If you have a specific idea in mind, like the fitness center concept we’ve been discussing, a useful technique is to set up a Google or Yahoo "email alert" using keywords that pertain to your topic of interest. Google and Yahoo! alerts are email updates of the latest Google or Yahoo! results (i.e., Web site updates, press releases, news articles, blog postings) based on your topic. This technique, which is available for free, will feed you a daily stream of news articles and blog postings about specific topics.

Summary

The ability to generate a good business idea is a key ingredient to launching a successful startup. Many businesses fail not because the people involved weren’t committed or didn’t work hard; they fail because the businesses weren’t good ideas to start with. Don’t let this happen to you. Following the frameworks and suggestions provided in this chapter can help you enhance your chances of coming up with a business idea that is successful.

The next chapter deals with the myth that no one can compete against Wal-Mart and the other big-box retailers. This myth is true in part—virtually no one can compete against big-box retailers at their own game. New businesses can compete if they understand what the big-boxes’ strengths and vulnerabilities are and adjust their strategies accordingly.

Endnotes

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Part II: *Running and Growing a Business—Don’t Underestimate Your Chances*

Chapter 6. Myth No. 6: No One Can Compete Against Wal-Mart and the Other Big-Box Retailers: Truth No. 6: You Can Compete Against the Big-Box Retailers if You Have the Right Plan

Introduction

One of the main fears that many prospective business owners have is whether they'll be able to compete against Wal-Mart, Home Depot, Best Buy, and the other big-box retailers. It's a legitimate fear. The big-box stores continue to grow, not only in terms of size but in terms of geographic breadth and product line. There are now big-box stores in towns as small as 10,000 people. And the stores don't just sell goods; they sell services, too. For example, Home Depot sells installation services for the carpet it carries, and Best Buy offers at-home computer training and repair. There are also anecdotes, which all of us have heard, of big-box stores moving into towns and driving local merchants out of business. If established businesses can't compete against Wal-Mart or Home Depot, it's hard to blame a prospective business owner for worrying about whether his or her business will have any chance at all.

The reality, though, is that despite these obstacles, many small businesses do compete successfully against big-box retailers. Their success, however, is not by chance. While it's nearly impossible to compete against Wal-Mart and the others on price, price isn't everything. There are many other forms of competition including product quality, customer service, product knowledge, convenience, ties to the local community, and so on. The businesses that compete successfully against the big-box retailers compete on one or more of these variables and avoid head-to-head competition on price. They also manage their businesses prudently and employ steps to keep their costs in check and to get the word out about the points of differentiation between their businesses and the big guys.

The purpose of this chapter is to more fully explore this important topic. In our view, the notion that no one can compete against Wal-Mart and the other big-box retailers is a myth—but there is a caveat attached. In general, no one can compete against the big-box retailers at their own game. So, if you're thinking about starting a business that will compete against a big-box retailer (and most businesses do at some level), you have to first understand their game and then develop a strategy and set of tactics that gives people reason to do business with you. In our experience, the big-box retailers are vulnerable but only to businesses that have a firm sense of how to compete against them.

This chapter proceeds in the following manner. First, we describe how the big-box retailers compete and what their vulnerabilities are. Although Wal-Mart, Home Depot, Costco, and the others are different in many ways, their overall strategies and vulnerabilities are similar. Second, we describe the three most common approaches employed by businesses that compete successfully against the big-box stores. Third, we lay out two specific tactics that new businesses use to make these approaches successful.

How Big-Box Retailers Compete and What Their Vulnerabilities Are

There are two categories of big-box retailers. The first are the general merchandise stores, such as Wal-Mart, Kmart, Costco, and BJ's Wholesale Club. These are the biggest stores, ranging from 50,000 to 225,000 square feet. The second are the category killers, such as Home Depot, Best Buy, PetSmart, Dick's Sporting Goods, and Bed Bath & Beyond. These stores focus on a single category and offer a wide selection of merchandise in that category. The name "big-box" comes from the physical appearance of the stores. They are normally large, free-standing, rectangular, single-floor stores on a concrete slab.

How the Big-Box Retailers Compete

The general merchandise stores, such as Wal-Mart and Target, compete primarily on price and selection. Although they attract people from all income levels, their most frequent customers are people in middle-and lower-income categories. The stores advertise "everyday low prices" and "one-stop shopping" and carry a wide selection of merchandise, from clothing and electronics to prescription drugs, food, toys, and automotive supplies. A Wal-Mart SuperCenter features up to 142,000 items. The approaches of the stores vary some. Costco and Sam's Club, for example, target small business owners along with the general public. Costco features a smattering of high quality products, such as Godiva chocolate and Waterford crystal, at bargain prices. Target has differentiated itself within the general merchandise big-box category by featuring more attractive stores with a slightly higher quality mix of merchandise.

The category killers follow much the same strategy but focus on a single category, such as electronics, pet supplies, sporting goods, or toys. While a category killer store, such as Best Buy or PetSmart, is not as large as a Wal-Mart or Costco, the advantage they have is an ability to zero in on a single category and provide better product knowledge. By focusing on a single category, the category killers are also able to generate more passion among their customers than the general merchandise stores.

Behind the scenes, the lower prices the big-box stores offer are made possible by volume sales, supply chain efficiencies, aggressive negotiations with vendors, and low overhead. The big-box concept also relies on Wal-Mart's original notion of "value loop" retailing as shown in Figure 6.1. The basic idea behind value loop retailing is that low prices generate healthy sales and profits. If a portion of the profits are reinvested in still lower prices, the prices will generate still higher sales and profits. If a portion of these profits are reinvested in still lower prices, sales and profits will continue to rise and so on and so on.[1] There is, of course, a limit to how much sales can go up and prices can go down, but it's easy to see the gist of the strategy.

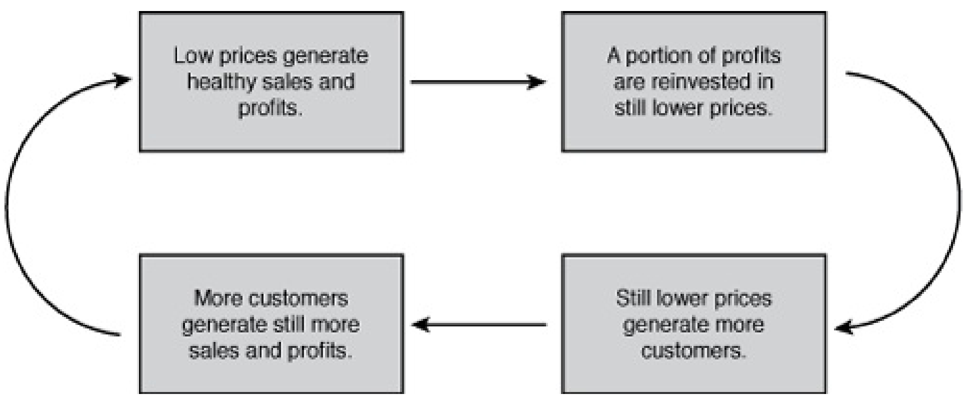

Figure 6.1. *Key to big-box retailers' success: Value loop pricing*

Along with low prices and a broad selection, the big-box stores also pursue a saturation strategy. Wal-Mart has literally blanketed the country with over 1,075 Wal-Mart discount stores, 2,250 Wal-Mart SuperCenter's, 580 Sam's Clubs, and a growing number of Wal-Mart Neighborhood Markets. Target now has over 1,500 stores, and Costco has 490. In the category killer group, Home Depot has 1,900 stores, Best Buy has 820, PetSmart has 900, and Beth Bath & Beyond has 815. These stores are not confined to urban areas. As mentioned earlier, Wal-Mart now has SuperCenters in towns as small as 10,000 in population, and the other big-box retailers are following suit. In most parts of the country, consumers have several big-box stores in their immediate shopping areas.

Vulnerabilities of the Big-Box Stores

The big-box stores have several vulnerabilities. The general merchandisers feature a product strategy that is a mile wide and an inch deep, which limits their ability to provide a wide selection of products or superior product knowledge in any one area. The basic idea is to sell the most popular products in as many categories as possible to value-minded consumers. While this approach allows the general merchandisers to achieve economies of scale (think of how many bottles of Tide Wal-Mart sells in a day), it leaves gaps in the marketplace, as explained in Chapter 5. The general merchandise stores are also vulnerable in regard to customer service, product knowledge, and their ability to develop one-on-one relationships with customers. The very nature of Wal-Mart, Kmart, and Costco's low-cost approach limits the amount they're willing to invest in customer service, and the sheer number of products they sell makes an intimate knowledge of each product impossible. The large size of their stores is also wearisome for many shoppers, who tire of crowded aisles, long checkout lines, an inability to find what they're looking for, and the lack of assistance when needed.

The same vulnerabilities that apply to the general merchandise stores apply to the category killers to a slightly lesser degree. Although the category killers, like Home Depot and PetSmart, are generally better at customer service and product knowledge than the general merchandise stores, they're still trying to sell the most popular products to mainstream consumers, which leaves gaps in the marketplace for others to fill. For example, Dick's Sporting Goods offers an impressive selection of sporting goods and apparel, but it can't offer everything. This reality provides an opening for a company like Just For Girls Sports, which is an online store that specializes in products that are especially designed for athletic girls, teens, and women. The category killer stores are also subject to the same criticism that general merchandise stores experience as a result of their size. While some people enjoy browsing around a large store like a Best Buy or a Dick's Sporting Goods, other people find the experience irritating and tiring.

A vulnerability that applies to both categories of big-box stores, which is most pronounced when a Wal-Mart or a Home Depot enters a smaller town, is a lack of ties to the local community and a perception that the larger store is a threat to local merchants. This issue has resulted in town meetings across the country as local communities have wrestled with the pluses and minuses of allowing big-box retailers to locate in their towns. While big-box stores provide employment and offer consumers access to lower-priced products, they also impact local businesses and take money out of a community. Both of these latter points have been affirmed by careful studies. A study conducted by Kenneth Stone, an Iowa State University economist, found that in the 10 years after a Wal-Mart opened, general-merchandise sales in Iowa towns with a Wal-Mart rose by 25% (mostly from Wal-Mart), while general-merchandise sales in surrounding towns dropped by 34%. During the same period, sales for both clothing stores and specialty stores dropped by 15% to 28% in both Wal-Mart towns and surrounding communities.[2] Similarly, economic impact studies have found that a much lower percentage of money spent at a chain store stays in the local community opposed to money spent at a locally owned business. A study conducted in the Andersonville district of North Chicago found that $68 of every $100 spent at a local firm stayed in the Chicago area while only $43 of every $100 spent in a chain store stayed in the community.[3]

The upshot of this discussion is potentially heartening for prospective business owners. While the big-box retailers clearly win on price, and to lesser degree on selection, they are vulnerable on product quality, product knowledge, customer service, convenience, ties to the local community, and other variables. Because they can't carry everything, they also leave gaps in the marketplace, providing the opportunity for other businesses to fill them. Luckily for new businesses, because the big-box retailers compete primarily at the low end of the market on price, the gaps they leave are generally at the high end of the market where profit margins are larger. Several of the businesses discussed in this book fit this description, including Wadee (handmade children's toys), J.J. Creations (designer bags and backpacks), and Real Cosmetics (skin care products for women of all nationalities). These businesses sell higher-margin products that don't fit the traditional product mix of a big-box retailer.

Table 6.1 illustrates the impact of this collection of insights on a potential new business. Imagine you are thinking about opening a nursery to sell plants, shrubs, trees, and lawn and garden supplies, but are hesitant to move forward because Wal-Mart and Home Depot are in your area and are selling similar products. Assuming that you're knowledgeable, willing to provide a high level of customer service, willing to promote the idea that you're a locally owned company, and otherwise capable of running a sound business, the checklist here shows the areas in which you can win and the areas that you'll most likely lose in competition with Wal-Mart and Home Depot. As shown in the table, while Wal-Mart and Home Depot will invariably win on price and selection might be a draw, you can potentially win every other category (and serve customers that find these categories important). This is the general circumstance in which new firms and existing businesses compete successfully against big-box retailers.

Table 6.1. Garden Nursery Versus Wal-Mart and Home Depot

Point of Competition	Advantage—Wal-Mart and Home Depot	Advantage—Small/ New Business
Price	X	
Selection	draw	draw
Product quality		X
Product knowledge		X
Customer service		X
Convenience		X
Ties to local community		X

The next section of this chapter talks about the three most common approaches employed by small businesses to compete successfully against big-box retailers.

Approaches for Competing Successfully Against Big-Box Retailers

There are many lessons those wanting to start their own businesses can learn from existing firms about competing successfully against big-box retailers. The primary lesson is to take the threat seriously and not leave things to chance. If you plan to open a store or sell products or services that will compete directly against a big-box retailer, you should have an explicit strategy for dealing with the big-box threat. Small businesses don't always do this. A pattern researchers have noticed in retailers that go out of business when a Wal-Mart or other big-box store comes to town is they don't adjust their strategies. In fact, one study of 62 small retailers in southwestern Virginia found that 52% of store keepers didn't adjust their product lineup, 42% didn't adjust their pricing, and 21% didn't adjust their service levels when a Wal-Mart opened in their area.

Another way of looking at the big-box phenomenon is that there are many businesses that it benefits. Local businesses often supply products and services to help the big-boxes operate. In addition, if your business offers a product line that complements rather than competes against a big-box retailer you might actually benefit by locating it in close proximity to the larger store. This strategy is pursued by Sally Beauty Supply, which appears in 26% of U.S. Wal-Mart anchored shopping centers. Explaining the rationale behind this strategy, Sally

Beauty Supply spokeswoman Jan Roberts said:

> *"Wal-Mart generates an enormous amount of traffic, and we like to feed off that. We do have a few similar products, but we offer much more selection. If someone is looking for specific beauty items, we are more likely to have them...like the 400 (personal) appliances we carry, such as blow-dryers and curling irons."*[4]

Now let's look at the three most common approaches that small businesses utilize to compete against big-box retailers.

Operate in a Niche Market

As mentioned in Chapter 5, a niche market is a place within a larger market segment that represents a narrower group of customers with similar needs. It's normally smart for a business that will compete against a big-box retailer to operate in a niche market so it can position itself as a "specialist" and provide a compelling reason for customers to shop at its store. This is what Sally Beauty Supply has done. It offers a very deep line of one product—beauty supplies. As a result of this singular focus, it can position itself as the "place to shop" for beauty supplies in a local community.

This same philosophy can be pursued in virtually any product category, as long as there are enough potential customers to support the business. An example is Paige's Music in Indianapolis. The company, which has been in business since 1871, sells musical instruments to school bands and orchestras. The musical instrument industry is a tough industry, as mentioned in Chapter 5, and sales are down nationwide for a variety of reasons. Competition is also intense. Wal-Mart and Costco sell musical instruments, and there are several national musical instrument chains, including Guitar Center and Sam Ash Music. Despite these threats, Paige's Music continues to grow, largely because of its laser focus on selling to school bands and orchestras, which is a niche market. "There are plenty of opportunities for the small local store to succeed against the big boys," says Mark Goff, owner and president of Paige's Music, "but you've got to hit 'em where they ain't."[5] Paige's primary market is the 400 school bands and orchestras in Indiana, along with the 36,000 students who are enrolled in music classes in Indiana schools. The store's salespeople regularly call on the band and orchestra directors they sell to. This is a tactic that will most likely never be matched by Wal-Mart, Costco, or one of the national musical instrument chains.

If the business or store you're contemplating will have some of the characteristics of a general merchandiser or category killer, you can still benefit by serving niche markets within the context of a larger business. For instance, in the example of the prospective nursery provided earlier, along with competing against Wal-Mart and Home Depot on factors other than price, the nursery could also become a specialist in one or more areas. For example, it might "specialize" in providing hedges, shrubbery, and sod for new construction and try to develop relationships with local builders and contractors. This is a niche market within the larger lawn and garden supply industry. It might also become the "place to go to" to purchase outdoor or indoor fountains. The overall point is that if the nursery couples its focus on the potential points of advantage along with becoming a specialist in one or two areas (while still selling its entire line of products), it will enhance its chances of success.

Differentiate

Once a business selects a niche market, it must differentiate itself from larger stores that sell similar products. Selecting a niche market, such as indoor and outdoor fountains or beauty supplies, is only the first step in separating your business from your larger rivals. The second step is to create meaningful forms of differentiation. Sally Beauty Supply relies on depth of product line and product knowledge as its forms of differentiation. Anyone who has shopped at Wal-Mart and Sally's knows that Sally's has a much broader and deeper line of beauty supplies. This doesn't mean that everyone will buy their beauty supplies from Sally's. But Sally's provides people who want a larger selection of beauty supplies to choose from, a clear alternative to Wal-Mart. The biggest mistake that new firms and existing businesses make when trying to compete against big-box retailers is not drawing a sharp enough contrast between what they have to offer and what the big-box stores have. This notion is affirmed by Kenneth Stone, the Iowa State University economist mentioned earlier in the chapter. After spending 12 years studying the impact of the entry of Wal-Mart stores on small communities in Iowa, Stone concluded that businesses that adjusted and offered something different than Wal-Mart actually benefited from the spillover of additional traffic, while businesses that sold items similar to Wal-Mart lost sales unless they repositioned themselves.[6]

The primary thing to be mindful of in planning a differentiation strategy is the need to differentiate along lines that are important to customers. Apparently, depth of product line and product knowledge are important to Sally's Beauty Supply customers, as evidenced by Sally's success. Another example is Sam's Wine & Spirits, a wine and liquor store that is sandwiched among a Costco, Cost

Plus, Trader Joe’s, and Whole Foods in Chicago. To compete against its big-box rivals, Sam’s Wine & Spirits stresses customer service, product selection, product knowledge, and education. The education piece is the most interesting. To deepen its relationship with its customers, the company has created Sam’s Academy, which offers adult education classes (on wine and liquor), wine tasting experiences, and reward programs for repeat customers. Explaining the rationale for these initiatives, Brian Rosen, one of the business’s owners said, "(Wine) is a knowledge-driven subject, and people want to be educated." Again, the beauty of this form of differentiation is that it’s unlikely to be mimicked by one of Sam’s Wine & Spirit’s big-box rivals.

There are many other ways to differentiate a small business from larger rivals. Some businesses seek out employees who speak the language of their customers—literally. For example, Wheelworks, a large bicycle store in Belmont, Massachusetts (which is near Boston), employs people who speak Spanish, French, Italian, Chinese, and several other languages. This aspect of Wheelwork’s business fits the ethnically diverse nature of its community and provides it an advantage over stores that aren’t as sensitive to this issue. Other companies, like locally owned office supply stores, offer free delivery, day or night, which is something that a Costco, Office Max, or Staples is unlikely to do. Probably the most important form of differentiation is customer service. While almost all companies tout customer service as a point of differentiation, small businesses are able to deliver it in unique ways. For example, remembering the names of frequent customers, writing thank you notes for large orders, and knowing customers’ buying habits is something that small businesses are uniquely capable of doing.

One final note that is particularly encouraging for new or small businesses is that there is growing evidence that price, the factor the big-box retailers rely on the most, might be a fairly fragile form of differentiation. According to the *Harvard Business Review*, two-thirds of shoppers find the entire Wal-Mart shopping experience not worth the savings.[7] A recent *Wall Street Journal* article affirmed this sentiment by reporting that specialty retailers across all segments are gaining on Wal-Mart despite Wal-Mart’s price advantages.[8]

Kazoo & Company: You Can Compete Against the Big Guys—If You Have the Right Plan

There is no denying it. There are many challenges in competing against big-box retailers. So how is it that Kazoo & Company, an independent toy store in Denver, Colorado, is thriving? It’s thriving because of two things—the business has a doggedly determined owner at the helm, and it has a good plan. After you read this short account, you’ll nod you head and think to yourself, yup—that’s a good plan.

Diana Nelson bought Kazoo & Company in 1998. From the outset, she had no illusions that owing a toy store would be easy. When she bought Kazoo, independent toy stores were being tattered to pieces by Wal-Mart, Toys "R" Us, and other large retailers. So she knew the only way to beat them was to outthink them. This is how she did it.

Nelson decided to differentiate Kazoo & Company from Wal-Mart, Toys "R" Us, and other large toy retailers on five specific dimensions.

First, the store changed its merchandise mix. Nelson replaced the Mattel, Crayola, and Fisher-Price toys (which could be bought anywhere) with unique items such as Gotz Dolls from Germany and a wide range of educational toys.

Second, the store welcomes professionals, like speech therapists, to bring their patients into the store to play with them and identify specific toys that might help them progress in their treatments. Observing professionals work with their patients (that is, young children who have some type of disability) also helps Kazoo & Company’s staff know what to recommend when a parent comes in looking for a similar solution.

Third, Kazoo’s store design is unique. While the store itself is still fairly small, it is further broken down into smaller, more intimate departments.

Fourth, the company focuses intently on customer service. This facet of Kazoo’s operation is particularly apparent in its e-commerce site, which was initiated in 1999. As evidence of this, the following comment was posted recently on a Yahoo! bulletin board site, where a consumer wrote a comment about his experience shopping at Kazoo.com:

> *"Old-fashioned friendly service. When I called to check on the delivery date of a little piano I had ordered for my grandson, I was actually speaking to a person that was friendly, polite, courteous, and just delightful. I will continue to buy from this company. They have a real interest in giving top-quality service. It has been a most enjoyable experience."*

Fifth, the inventory in the store is freshened up frequently, so regular customers see different toys each time they come into the store.

Kazoo's plan and its sharp execution have paid off. Business is growing, and the company has been selected by the Toy Industry Association as one of the Top 5 Specialty Retail Toy Stores in North America several times since it was purchased by Diana Nelson.[9]

Stress "Locally Owned"

A third approach that businesses use to compete successfully against big-box retailers is to stress the locally owned facet of their businesses (if they are locally-owned). This approach tugs at the heart strings of people who are loyal to their local communities and have a natural inclination to want to see local businesses succeed. The strategy is evident in signs that are placed in store windows or in ads that read "Locally Owned Business," "We Sell Locally Made Jewelry," or other similar comments. In fact, this type of strategy is much more than an advertising gimmick. One study of residents in Maine, New Hampshire, and Vermont found that 17% to 40% of consumers in each state were willing to pay two dollars more to buy a locally produced $5.00 food item.[10] Similarly, a study by the Leopold Center for Sustainable Agriculture found that "grown locally" ranked significantly higher than "organic" in regard to consumer preferences for fresh produce and meats.[11]

Stressing the local nature of a business can also be helpful in building its brand. Many states and regions of the country have placed labels on products originating from their geographic areas to draw attention to their wholesomeness and freshness. Examples include "Tennessee Pride," "Jersey Fresh," and "Iowa Beef." The subtle message conveyed by these labels is not only where the products come from but where they don't come from. For example, most consumers would probably prefer "Alaskan Wild Salmon" to salmon advertised as coming from a densely populated fish farm in Chile (which is where most salmon in the United States comes from). While the Chilean salmon might be perfectly fine, the freshness factor and the U.S. roots of the Alaskan salmon are likely to give it a leg up for most American consumers.

The same philosophy can be applied at an individual business level. A locally owned business can tout the wholesomeness and freshness of its products (if applicable) as effectively as a region or state. It can also draw attention to the positive economic impact that locally owned businesses have on a community or local economy.

Specific Tactics That Local Businesses Use to Support Their Independent Status

There are a number of tactics that new and small businesses use to support the general approaches described here and to maintain their independently owned status. A tactic is a method employed to help achieve a certain goal. While most companies have similar broad strategic goals (increasing sales, increasing profits, producing quality products, behaving in an ethical manner, and so on), the ways in which they achieve their goals vary widely. The two tactics shown in the following sections are most applicable to businesses that plan to remain independently owned and are particularly concerned about competing against big-box retailers.

Partner with Other Small Businesses

A common tactic new businesses employ is to partner with other new or small businesses to increase their clout and buying power. Making this happen takes initiative and pre-planning on the part of a prospective business owner. He or she must get to know other business owners and establish relationships before the business is started.

There are several ways that small businesses can partner with one another in an effort to be as competitive in the marketplace as possible. One way is by joining or organizing buying groups or co-ops, where small businesses band together to attain volume discounts on products and services. An example is Intercounty Appliance, a buying co-op for 85 independent appliance stores in the Northeast. The co-op aggregates the purchasing power of its members to get volume discounts on appliances and other items such as flat-screen plasma TVs. An example of a much larger buying co-op is the Independent Pharmacy Cooperative, which was founded in Madison, Wisconsin in 1984. It has since grown into the nation’s largest purchase organization for independent pharmacies with over 3,200 member stores and is one of the major reasons that independent pharmacies are able to compete against Walgreens and CVS. There are similar buying co-ops in other industries. In many cases, the co-ops can get the same pricing on merchandise from a vendor as a big-box retailer. While belonging to a buying co-op doesn’t mean an independent firm will be able to compete against a big-box retailer on price, cutting costs on inventory provides the smaller firm with additional resources that can be used to invest in customer service and other forms of differentiation.

There are many other ways that small businesses partner with one another, from splitting the cost of a booth at a trade show to developing a joint advertising campaign. Many local businesses purchase their supplies and services from other local businesses rather than on the open market. This approach helps build camaraderie among locally owned firms and often encourages reciprocal buying and selling among locally owned companies. Big-box stores, which take their marching orders from corporate headquarters, are much less likely to engage in these types of activities.

Looking to Band Together with Other Local Businesses: Join or Start an Independent Business Alliance

An option that locally owned businesses have, that is becoming increasingly common across the country, is to form an *independent business alliance*. An independent business alliance is a nonprofit organization that is committed to nourishing and supporting locally owned firms. Examples include the Boulder Independent Business Alliance (Boulder, Colorado), the Austin Independent Business Alliance (Austin, Texas), and the Portland Independent Business & Community Alliance (Portland, Maine). A sample of the types of activities that independent business alliances perform follows:

- Sponsoring "buy local" campaigns
- Increasing public awareness of the positive economic benefits of shopping locally through feature articles, opinion editorials, local media coverage, and ongoing advocacy campaigns
- Providing locally owned businesses insignias that they can place in their store windows, on their menus or brochures, or in their advertising that designates them as a locally owned firm
- Facilitating networking events for locally owned business owners to get to know one another
- Printing and distributing directories of locally owned businesses

The networking events are particularly important and often lead to independent business owners forming partnerships, swapping business advice, and offering one another emotional support.

If you live in a community that doesn't have an independent business alliance and you're interested in starting one, you can obtain assistance from the American Independent Business Alliance (AMIBA) at www.amiba.net or the Business Alliance for Local Living Economics (BALLE) at www.livingeconomics.org.

Shop the Competition

A second tactic that new businesses utilize, particularly in the context of competing effectively against big-box retailers, is to shop the competition. The basic idea is that once a firm determines how it plans to compete against a larger rival, whether it is on product selection, product knowledge, or some other variable, it should continually assess whether it is maintaining the competitive edge it needs. In many instances, the only practical way to do this is to literally shop at the rival store.

Many business owners are transparent about how they go about this and will literally walk through a nearby Wal-Mart or Home Depot with a pad and pencil in hand. There are normally two objectives in mind when a person shops the competition. The first objective is to check on specific things like a competitor's product selection and prices. The second objective is to view the competitor's merchandise, get a sense of the general nature of the store, and get ideas that you might incorporate into your own store. There is nothing inherently unethical or improper about shopping at a rival's store as long as you are honest and are observing things that are in the open. There are also less intrusive ways to shop the competition, such as looking at its Web site and monitoring its print and media ads.

Business owners vary regarding how bold they are when shopping the competition. Sam Walton was known for frequently visiting Kmart and Target stores during the years he was building Wal-Mart and was reportedly often seen making notes in a spiral notebook or talking into a tape recorder while in a competitor's store.[12] It occasionally irks the manager of a store to see a competitor walking his or her aisle, knowing that comparison shopping is taking place. Some managers see comparison shopping as snooping and actually ask competitors to leave their stores. More often than not, however, it's a routine practice that doesn't raise any eyebrows.

One particular advantage of shopping the competition is that it allows you and your employees to speak more authoritatively to your own customers. Imagine the following scenario: You are the owner of an independent appliance store that sells big screen TVs, which is a product that is one of your biggest money makers. A customer comes into your store with an ad for a 56-inch plasma TV for $2,200 from a big-box store. You sell flat-panel LCD TVs (which use a different technology) and have a 56-inch model for $2,500. Your exchange with the customer might go like this:

Customer:

"How does your 56-inch LCD TV compare to the 56-inch plasma TV I can buy down the street? Your TV is $300 higher."

You:

"Our TV is better," you say without hesitation.

Customer:

"How do you know it's better? Have you seen the 56-inch plasma TV?"

You:

"No, I've never seen the 56-inch plasma TV, but I just know our LCD TV is better. Its brightness and sound quality are rated higher."

Customer:

"But you've never seen the difference with your own eyes? I don't want to pay $300 more for the LCD TV unless it's really better. It's hard for me to see a difference."

You:

"Sorry, I've never actually seen the 56-inch plasma TV."

Not very impressive is it? It would have been much better if you could have said that you've seen the 56-inch plasma TV and then talk about your impressions of the differences between the two TVs. In addition, if you had shopped the competition thoroughly, there would probably be other things you could talk about. For example, if you know you have a cost and convenience advantage over your competitor in regard to delivery and installation, you might say, "Another thing to keep in mind is that the store that carries the plasma TV charges $200 for delivery and installation. We only charge $100. We also deliver and install on weekends and holidays."

Summary

Many small businesses compete effectively against big-box stores, primarily by operating in niche markets and differentiating themselves from what the big-boxes have to offer. There is no denying that the big-box stores are formidable. Stores like Wal-Mart and Target serve hundreds of thousands of customers daily and are growing in stature. But small businesses have an important role to play in the marketplace, too. The most important thing for a new business to understand is how to position itself in a way that avoids direct competition with big-box retailers.

The next chapter focuses on the myth that it's almost impossible for a new business to get noticed. There are actually many ways for a new business to get noticed, but it takes some familiarity with the options and a willingness to persevere. Many business owners enjoy the process of spreading the word about the products or services they have to sell once they catch on to the most effective ways of going about it.

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Chapter 7. Myth No. 7: It's Almost Impossible for a New Business to Get Noticed: Truth No. 7: There Are Many Ways for New Businesses to Get Noticed and Recognized

Introduction

A deep-seated fear that many potential business owners have is that they will start their businesses, and no one will notice. Most of the time, the fear doesn't originate from a lack of confidence in the product or service the business will sell. Business owners normally go to great lengths to make sure their initial products or services are right. Instead, the fear originates from a lack of knowledge about how to make people aware of their businesses and how to market the products. The fear is heightened the first time a prospective business owner checks into the cost of print and media advertising. In a mid-sized city, a large newspaper ad can run as high as $15,000. That's more than the total startup cost of many businesses! Another obstacle is the sheer tempo of ads in the marketplace. The average person is exposed to about 2,000 marketing messages a day.[1] It's no wonder that prospective business owners are fearful about their businesses not getting noticed.

Fortunately, there are inexpensive ways for businesses to get noticed and for their messages to reach their target markets. But there is a problem. The problem is that the majority of business owners are familiar with the most expensive ways to get a business noticed—print and media advertising—and are less familiar with more cost-efficient alternatives. As a result, many businesses struggle to get noticed because they can't afford to do a lot of advertising, and they either don't know about or don't take the time to pursue less expensive alternatives.

The truth is that it is possible for a new company to get noticed, but it takes three things to make it happen. First, it takes a business owner who is willing to learn about the full array of marketing-related techniques that are available. Second, it takes persistence and hard work. Many of the most cost-effective ways for a business to get noticed, from passing out brochures to writing a blog, are inexpensive, but they take time and effort. Third, it takes a focused and sensible marketing strategy.

To address these issues and further dispel the myth that it's almost impossible for a new business to get noticed, this chapter is divided into three sections. The first section provides three rules-of-thumb for approaching the challenge of getting noticed. It's important for a new business to approach this challenge carefully because an ill-advised approach to trying to get noticed can be costly and ineffective. The second section describes how a business establishes a brand. A brand is the set of attributes that people associate with a company. It's important for a business to think about its brand as part of its strategy for getting noticed because it wants to be thought of in a certain way. The third section describes the most common tactics and techniques that businesses use to get recognized or get noticed.

Rules-of-Thumb for How to Approach the Challenge of Getting Noticed

As discussed, increasing the visibility of a new business takes three things—familiarity with the alternatives, hard work, and a sensible strategy. Ironically, once you start investigating the various alternatives, the task becomes harder rather than easier. There are dozens of alternatives for marketing and promoting a business, from traditional print advertising, to attending trade shows, to posting a video on YouTube.com. There are also thousands of books and Web sites dedicated to marketing, advertising, public relations, and other forms of promotions. While these resources are helpful, the advice they provide is so plentiful and varied that it's hard for a new business owner to know where to start.

This section provides three rules-of-thumb for initiating the process of getting your business noticed.

Focus on a Niche Market and the Benefits Offered to Customers

The first rule-of-thumb is to focus singularly on your niche market and the benefits your business offers the targeted customers. While this advice sounds straightforward, not all businesses are clear regarding what their markets are and who they are trying to appeal to. As mentioned in previous chapters, a niche market is a place within a larger market segment that represents a narrow group of customers with similar needs. The reason it's important to know your niche market is that it's premature for a business to select, or even talk about, specific marketing techniques until it has a clear picture of who its customers will be. If a firm starts advertising or promoting its business before it's sure who its customers are, it will not only waste money but can confuse people who are unsure whether the product is intended for them.

It’s also important for a business, as part of its initial efforts to get noticed, to draw attention to the factors that differentiate it from its competitors. This is a potentially make-it or break-it issue for many businesses. It’s hard to get people to try something new or change their habits and behaviors and switch from a product they’re currently using to a new one. As a result, you have to clearly explain how your a product is better or cheaper to get people to try it. It’s typically best to limit the points you focus on to two or three points to make them memorable and distinct.

For example, ZUCA, the backpack on rollers introduced in Chapter 5, has two distinct points of differentiation: It relieves back pain by putting the backpack on rollers, and it is sturdy enough for either a child or an adult to sit on. At the time the ZUCA was introduced, these attributes were different enough from anything else on the market that the company got noticed, and its product took off.

Another activity that’s important for a new business is to learn as much as it can about the people in its niche market, from how much disposable income they have to the periodicals they read and the Web sites they visit. This task can be completed by following prescriptions already discussed in this book. Laura Udall, the founder of ZUCA, conducted focus groups to learn about her target market.[2] She was also a mother, and her original insight for the ZUCA backpack came from watching her own daughter struggle with the backpacks she carried to school every day. Other methods, such as reading industry trade journals and surveying potential clients, are also good ideas.

The steps described here, which should precede your selection of specific tactics and techniques to get your business noticed, are shown in Figure 7.1.

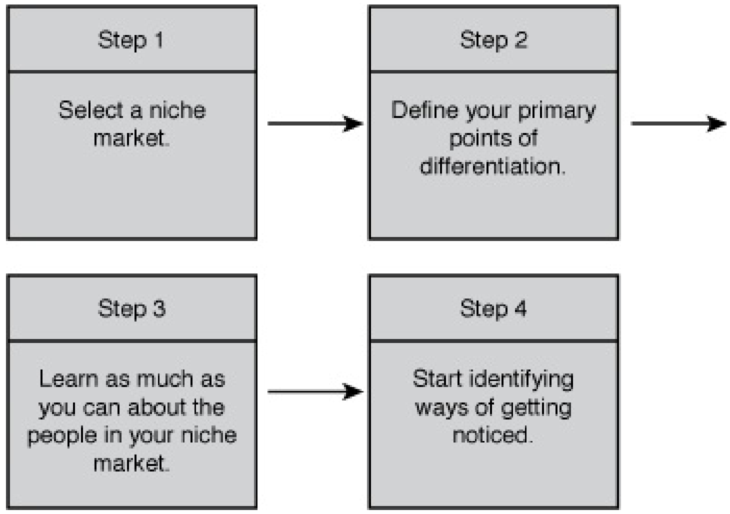

Figure 7.1. *Steps involved in initiating the process of getting a business noticed*

Selling Benefits Rather Than Features

In their attempts to gain visibility, many new businesses make the mistake of promoting the features rather than the benefits of their products or services. A promotional strategy that focuses on the features of a product, such as its technical merits, is almost always less effective than a strategy that focuses on the merits of what a product can *do* for the person buying it. For example, one of the most successful advertising campaigns ever launched by McDonald’s contained ads that featured the jingle, "You deserve a break today—at McDonald’s." McDonald’s could have stressed the cleanliness of its stores or the uniformity of its french fries, both of which are features. Instead, it struck a chord with people by focusing on one of the biggest benefits of eating at McDonald’s—not having to cook. Although not as obvious in today’s society, not having to cook a meal at home was a major advantage when McDonald’s started using this tagline.

The same rationale can be applied to any product or service. Consider the ZUCA rolling backpack. In her initial attempts to get the ZUCA noticed, Laura Udall could have talked about the ZUCA’s durable aluminum frame, its oversized silent wheels, the washable nature of the bag, and the number of colors that were available. These are all features. It’s much more likely that she focused on the benefits of the product—the fact that it relieves back pain and is durable enough that a child can sit on it while waiting for the school bus. (The ZUCA includes a fold out seat.) These are the benefits or the value that the ZUCA delivers to its users.

Consider Diverse Marketing Methods

The second rule-of-thumb pertaining to the challenge of getting a business noticed is to consider diverse marketing methods. The best approaches for learning about the methods that are available are to look through books and magazines on marketing and promotions and take a class from your local Small Business Development Center. Also, study companies that are selling products in the same market you will be targeting to see how they are gaining visibility and how they are marketing their products.

It is advisable to consider as many alternatives as possible before settling on the techniques you'll use to try to increase visibility. In some cases, the choices will be clear. For example, if you plan to launch a Web site to sell plus-sized clothing for children, the only way to reach your audience might be through pay-per-click Internet advertising (more about this option later). In other instances, the best choice or choices may be unclear, and it could take some guidance to find the best alternative. This scenario played out for Proactiv, the #1 seller of acne products in the United States, mentioned in Chapter 5. At one point early in the life of the company, it was suggested to Dr. Katie Rodan and Dr. Kathy Fields, the company's founders, that the best way to get the word out about Proactiv was via infomercials. Initially, the two were shocked because they had a low opinion of infomercials. But they got to thinking that an infomercial might be the best way to educate people about their products. Proactiv was revolutionary in that it was designed to prevent rather than simply treat acne. As a result, the product needed more explaining than could be accomplished in a 30-second television spot or a print ad. Acne is also an embarrassing problem, which made it unlikely that people would go into a store and ask for a detailed explanation of how Proactiv should be used. The following bulleted list lays out the points in favor of using infomercials to sell Proactiv.

- People need to be reeducated about how to treat acne.
- The reeducation can't be done in a 30-second or 60-second television commercial, or in a print ad.
- Acne is an embarrassing problem, so people will be most open to learning about it in the privacy of their homes.
- The demographic group that spends the most time watching infomercials,

women in their 20s, 30s, and 40s, are Proactiv’s market.

- Infomercials provide Proactiv the opportunity to show heartfelt testimonials of people who have used the product. Showing "before" and "after" pictures of people who have used the product and have experienced dramatic results has been a particularly persuasive tactic.

Proactiv launched its first infomercial in 1994, and the vast majority of its customers have been introduced to its products through this medium. Ironically, Rodan and Fields would have never come up with the idea of using infomercials on their own. It took a suggestion from an outside party to alert the two founders to this possibility.[3]

An additional piece of advice that’s provided to business owners when they’re looking for ways to stand out is to think creatively and try new tactics and techniques. The rationale behind this advice is that a new business has to find a way to stand out. There are many examples of businesses that have followed this advice and have created original and fun ideas to draw attention to themselves. For example, to generate interest in Cranium, a board game for adults, the founder borrowed a trick learned from the makers of Trivial Pursuit. For $15,000, they recruited 100 radio stations around the country to have their DJs read Cranium questions over the air. The callers who phoned in the correct answers got a copy of the game as a prize (and everyone listening got introduced to the company). A similarly creative technique was utilized by Zach Nelson, the founder of MyCIO.com (now called McAfee ASaP), to get his business noticed:

> *"One of the great things we did when we first launched MyCIO.com is that we draped our entire eleven-story building on Highway 101 with the MyCIO.com logo. It was the world’s largest billboard. The city of San Jose wasn’t very happy with us for doing it, but they let us keep it up for a month. Everyone that I called after we ran that giant billboard I received a return call back from."*[4]

One pleasant surprise that many business owners experience when they start looking at the options for gaining visibility is that many of the alternatives are inexpensive. For example, 400,000 small businesses reportedly have blogs, which are inexpensive to create and maintain.[5] Similarly, it costs a business owner nothing to speak to a community group or to give an interview to a business magazine. These approaches can be effective ways to get the word out about a new company.

Find Ways to Build Credibility and Support

The third rule-of-thumb pertaining to the challenge of getting your business noticed is to build credibility and support for your company from the beginning. This is most effectively done by finding ways to get others to talk about or validate the merits of your business. While there is nothing inherently wrong with advertising and similar forms of promotion, people know that ads and promotions are paid for, so they discount them to a certain degree. It's normally much more persuasive when an unbiased third party talks about the merits of your product or service.

There are several ways to garner this type of support. Many businesses cultivate reference accounts. A reference account is an early user of a firm's product who is willing to give a testimonial regarding his or her experience with the product. To obtain reference accounts, new firms must often offer their products to a group of customers for free or at a reduced price in exchange for their willingness to try the product and for their feedback. There is nothing improper about this process as long as everything is kept aboveboard and the business is not indirectly "paying" someone to offer a positive endorsement. Once the testimonials are collected, they are used in company brochures, advertisements, and by salespeople who are able to tell potential customers about the positive experiences that other customers have had.

There are more formal ways to build credibility and support. Some businesses sell products that can be certified by an agency and can then place the agency's certification mark on their products. The most familiar certification mark is the UL mark, which certifies that a product meets the safety standards of Underwriters Laboratories. A similar example is the Good Housekeeping Seal of Approval. There are also industry-specific seals of authenticity or approval. An example is the "100 Percent Napa Valley" certification mark, which can only go on bottles of wine where 100% of the grapes used to produce the wine were grown in the Napa Valley of Northern California. If similar certifications are available for the product or service your business plans to offer, it is well worth your time to try to obtain the certification.

There are also occasions when a business benefits when a core aspect of what it's doing meets a standard that is viewed favorably by the pubic. An example of this is provided by White Wave, a company that makes soy milk. In 1996, White Wave came up with a new idea for selling soymilk. It would produce a dry soy mixture, ship it to dairies, pay the dairies to add water, package the resulting soymilk in milk-like containers, and distribute the product. Initially, the going was slow. Then the company caught a big break. In October 1999, the FDA announced that soy was considered a heart-healthy substance that could lower cholesterol. This announcement provided the legitimacy White Wave needed to take its soymilk mainstream, which was its goal from the beginning. White Wave Silk Soymilk is now found in the dairy section of almost every grocery store in the United States.[6]

One additional way businesses build credibility and support, which is talked about in more depth later, is by having favorable articles written about them in newspapers, magazines, and trade journals.[7] It also helps a business to win an award.

For example, in 2007 White Wave's Silk Soymilk won the American Culinary ChefsBest Award for Best Taste. White Wave can now refer to the award in its advertising and has earned the right to display the ChefsBest seal of approval on its products.[8]

Establishing a Brand

A brand is a set of attributes—positive or negative—that people associate with a business. These attributes can be positive, such as trustworthy, innovative, dependable, or easy to deal with, or they can be negative, such as poor-quality, unreliable, sloppy, or difficult to deal with. In our experience, it's important that a new business give thought to the brand it plans to develop before it initiates any marketing or promotional activities. The first impression that a business makes with its potential customers should convey the essence of how it wants to be viewed and seen.

New businesses must build a brand from scratch, which starts with selecting the company's name. One of the keys to effective branding is to create a strong personality for a firm, designed to appeal to its target market. Southwest Airlines, for example, has created a brand that denotes fun. This is a good fit for its target market: people traveling for pleasure rather than business. Similarly, Starbucks has created a brand that denotes an experience framed around warmth and hospitality, encouraging people to linger and buy additional products. A business ultimately wants its customers to strongly identify with it—to see themselves as "Southwest Airlines flyers" or "Starbucks coffee drinkers." People won't do this, however, unless they see a business as being different from its competitors in ways that create a special and valuable experience for them.

The First Step in a Company’s Branding Strategy: Selecting Its Name

While at first glance naming a business might seem like a minor issue, it is an extremely important one. A company’s name is one of the first things people associate with a business, and it is a word or phrase that will be said thousands or hundreds of thousands of times during the life of a business. A company’s name is also the most critical aspect of its branding strategy. It’s important that a business’s name facilitate rather than hinder how the business wants to differentiate itself in the marketplace and how it wants to be viewed by its customers.

A useful way to discuss this issue is to divide companies into four categories:

Consumer-Driven Companies

If a company plans to focus on a particular type of customer, its name should reflect the attributes of its clientele. For example, a high-end clothing store that specializes in small sizes for women is called La Petite Femme. Similarly, a company introduced in Chapter 1, Type 1 and Type 2 Tools, helps children with diabetes cope with their disease. These names were chosen to appeal specifically to their target markets or clientele.

Product-or Service-Driven Companies

If a company plans to focus on a particular product or service, its name should reflect the advantages that its product or service brings to the marketplace. Examples include Jiffy Print, ServiceMaster, Daisy Rock Guitars, and 1-800-CONTACTS. These names were chosen to reflect the distinctive attributes of the product or service the company offers, regardless of the clientele.

Industry-Driven Companies

If a company plans to focus on a broad range of product or services in a particular industry, its name should reflect the category it is participating in. Examples include General Motors, Bed Bath & Beyond, and Home Depot. These companies have names that are intentionally broad and are not limiting in regard to target market or product selection.

Personality-or Image-Driven Companies

Some companies are founded by individuals who put such as indelible stamp on the company that it might be smart to name the company after the founder. Examples include DarynKagan.com, Charles Schwab, The Trump Organization, and Magic Johnson Enterprises. These companies have names that benefit from a positive association with a particular person or distinctive founder. Of course, this strategy can backfire if the founder falls out of favor in the public's eye.

So how does a new business develop a brand? On a philosophical level, a business must have meaning in its customers' lives. It must create value—something for which customers are willing to pay. Imagine a father shopping for airline tickets so that he can take his two children to see their grandparents for Christmas. If Southwest Airlines can get his family to their destination for $75 per ticket cheaper than its competitors, Southwest has real meaning in the father's life. Similarly, if a young couple buys a Cranium board game, and playing the game with other couples results in lasting friendships, then Cranium will have a special place in their hearts. Firms that create meaning in their customers' lives stand for something in terms of benefits, whether it is low prices, fun, fashion, quality, friendliness, improved health, or something else. This means creating a bond between a company and its customers.

On a more practical level, brands are built through the techniques we talked about in the third section of this chapter, which include advertising, public relations, media interviews, and other techniques. A firm's name, logo, Web site design, and even its letterhead are part of its brand. The most powerful metaphor that can be used to describe a brand is that it's a promise that a business makes to its customers. Other ways of thinking about the meaning of a brand are included in the following bulleted list.[9]

- A brand is a promise.
- A brand is a guarantee.
- A brand is a pledge.
- A brand is a reputation.
- A brand is an unwritten warrantee.
- A brand is an expectation of performance.
- A brand is a presentation of credentials.
- A brand is a mark of trust and reduced risk.
- A brand is a collection of memories.

- A brand is a handshake between a company and its customers.

The Most Common Tactics and Techniques for Getting a New Business Noticed

There are a number of tactics and techniques available to business owners to get their businesses noticed. Because most businesses are started with limited funds, as many alternatives as possible should be considered. In the majority of cases, a business will use a combination of techniques rather than rely on one or two. Serendipity and luck also play a role. Once the word gets out about a new product, like the ZUCA rolling backpack, the company is often contacted and asked for interviews and similar opportunities. It is normally to a business owner's advantage to pursue as many of these opportunities as possible, as long as the end-result positively reflects on the business and its brand.

This section discusses the most commonly used techniques for getting a business noticed. The section is divided into four categories: advertising, public relations, Internet-related methods (other than pay-per-click advertising), and word-of-mouth marketing.

Want to Save Time When an Advertising Salesperson Calls on You? Use These Three Criteria

One thing that happens to new businesses is that they are generally inundated by other businesses that want to sell them advertising or some other form of promotion. The challenge for a new business is to sort out the possibilities that make sense from those that don't. There are three criteria that a business can use to quickly make decisions in this area, and utilizing them can help save time and heartache in dealing with advertising salespeople.

Criterion #1: Will my target market see the ad? The first question to consider is whether your target market will even see the proposed ad. For example, if your target market is teenage boys, it's unlikely that they'd see an ad in a local classified magazine—the type that is distributed at grocery stores and gas stations. Because teenagers spend so much time online, a better choice might be placing an ad on Craigslist or a similar

Web site. As a side benefit, advertising on Craigslist is usually free.

Criterion #2: Is the ad or promotion consistent with my brand? Certain types of ads and promotions will be consistent with your brand, and others won't. For example, if you're opening a sporting goods store, buying billboard space at a local high school football stadium might be fully appropriate. It would be silly for someone with an upscale clothing boutique to pursue the same type of promotion—it just doesn't fit.

Criterion #3: Is the ad or promotion within my budget? Be leery of expensive advertising and promotions alternatives. Stay within a reasonable budget. There are so many inexpensive alternatives available that you should exhaust your investigation of these options before you spend a lot of money.

Advertising

There are many different ways that businesses advertise. While it's normally cost-prohibitive for a new business to advertise on television and in major newspapers and magazines, there are other alternatives that are less expensive or free. The two major categories of advertising include print and media advertising and Internet advertising. The following is a discussion of each category with an emphasis on the alternatives most suitable for new businesses.

Print and Media Advertising

Print and media advertising runs the gamut from television ads to posting flyers on grocery store bulletin boards. The type of advertising a firm selects hinges largely on whether it is targeting a national audience, like an e-commerce site that plans to sell hunting and fishing gear, or a local clientele, like a single-store woman's clothing boutique. There are some advertising-related initiatives that all new businesses should take advantage of. For example, the major Internet search engines, like Google and Yahoo!, have business directories that list local businesses and in some cases even provide a map to show where they are located. You can get your business listed but have to go to the Web sites and sign up. The listings are either free or are subject to a small yearly charge. If you want to see how this works, type "hardware stores in Wichita, Kansas" into the Google search engine and see what happens. The names of the "local businesses" that appear have registered their businesses in the Google business directory.

New businesses that plan to target a local clientele typically avoid television, newspaper, and magazine advertising because of the costs involved. As mentioned earlier, a large ad in the newspaper of a mid-sized city can cost as much as $15,000. Radio advertising is effective for many businesses that have a local station with a listening audience that reflects the demographic they're trying to reach. Classified ads, either in local newspapers or online, remain effective in many instances. Direct mail, placing an ad in a local business directory, and advertising in publications such as local homeowners' association newsletters are additional choices. A business's own signage and visibility can be its most important form of advertising. Some home remodeling businesses, for example, report that their #1 source for getting new business is people who see their trucks parked in neighborhoods and call the phone number displayed on the sides of the trucks.

Television, newspaper, and mainstream magazine advertising is also avoided by businesses that plan to target a national clientele. The challenges these businesses have is how to reach their specific niche market. There are several ways to do this. There are literally thousands of magazines that target narrow niches. In some cases, a magazine might even help finance a company's initial ads if it thinks the company looks promising and could become a regular advertiser. Another option is to advertise in industry trade journals, if that's a good fit. A trade journal is a periodical, magazine, or publication that focuses on a specific industry, trade, or type of business. A directory of trade associations (which publish trade journals) is available through Weddle's at www.weddles.com/associations/index.cfm. Many trade associations also sponsor trade shows and conferences where new businesses can gain visibility and display their products.

Internet Advertising

An increasingly effective way for all new businesses to get noticed and sell their products is via pay-per-click Internet advertising. This type of advertising is provided by the major search engines, such as Google, Yahoo!, and MSN. Google has two pay-per-click programs—AdWords and AdSense. AdWords allows an advertiser to buy keywords on Google's home page, which triggers text-based ads to the side (and sometimes above) the search results when the keyword is used. So if you type "fishing equipment" into the Google search bar, you will see ads from Bass Pro Shop, Cabela's, and other companies that have fishing equipment to sell. Many businesses report impressive results utilizing this approach, presumably because they are able to place their ads in front of people who are already searching for information about their products. Google's other pay-per-click program is called AdSense. It is similar to AdWords, except the advertiser's ads appear on other Web sites instead of Google's home page. A full explanation of how AdSense works is provided in Chapter 8.

There are businesses that have relied almost exclusively on pay-per-click advertising to get noticed and to sell their products. These businesses often sell a product that wouldn't sell in sufficient volume to support a brick-and-mortar store. For example, Oddball Shoe Company (www.oddballshoe.com), an online shoe store, sells a size 16 EEEE athletic shoe for men and similar odd sized shoes. People find out about Oddball Shoe when they search for unusual sized shoes on Google and see the company's ad alongside their search results. Pay-per-click advertising has also allowed some people to turn their hobbies into businesses. For example, a Web site named SeatGuru (www.seatguru.com) was started by a flying enthusiast and lists the best seats and the worst seats (in terms of comfort) for each airline by type of aircraft. Prior to the advent of the Google AdSense program, the site had no practical way of making money. Now the site is viable as a for-profit business as a result of participating in the Google AdSense program. If you look at the site, you'll see a number of targeted ads sponsored by the Google AdSense program.

Public Relations

One of the most cost-effective ways for a new business to get noticed and to continually promote its products is through public relations. Public relations refers to efforts to establish and maintain a company's brand and the image associated with the brand to the public. The major difference between public relations and advertising is that public relations is not paid for—directly. The cost of public relations to a business is the effort it takes to network with journalists and other people to try to interest them in saying or writing good things about a company and its products. Examples of public relations techniques include:

- Press releases
- Media coverage
- Articles about the business in local newspapers, national magazines, or industry press
- Monthly newsletter
- Sponsor free seminars
- Contribute expert "how-to" or advice articles in your local newspaper
- Civic, social, and community involvement

In most cases, public relations is better than advertising because it is more grass roots and isn't seen as self-serving as advertising. The key to getting good public relations, such as a newspaper or magazine article written about your company, is to create a human-interest story that's associated with your firm. It also helps to be proactive in regard to speaking out on behalf of your industry and talking to trade groups and civic groups about your industry or area of expertise.

An example of how these efforts come together to create positive public relations and help a business get noticed is provided by Lisa Druxman, the founder of Stroller Strides (www.strollerstrides.com), a franchise organization for new mothers. Stroller Strides is a concept that Druxman developed to get herself back in shape after her first baby was born. It is an organized workout class where women push strollers, power-walk, and exercise outdoors to meet their fitness goals and socialize with other mothers. Prior to starting Stroller Strides, Druxman was the general manager of a health club. Druxman's story is a classic illustration of how public relations works and the potential payoffs involved:

> *"When I (was) the general manager at the health club, I would regularly go on the news promoting new workouts. One day the TV station called me and asked, 'Would you mind coming in with your baby and give (some) tips on how to get back in shape?' So I did, and I promoted my class as if it were this big business—I gave out my home e-mail and personal cell phone number. By the time I got home from the station, I had 75 calls and emails from all over San Diego from people who were interested in taking my class. I had my grand opening class three weeks after that, with 40 people there and more news coverage."*[10]

The key to Druxman's success, in this instance, was that she was able to tell her story through an unbiased third party, the TV program. Her story was compelling enough that it drew more free publicity in the form of news coverage of her grand opening. Many startups seek similar types of public relations through stories in local newspapers or business journals or through a national publication like *Fortune Small Business* or *Entrepreneur*. The key to getting this type of coverage is to have an interesting story to tell rather than simply extolling the value of your product or service.

There are many other ways in which a new business can enhance its chances of getting recognized by the press. One technique is to prepare a press kit, which is a folder that contains background information about the company and includes a list of its most recent accomplishments. The kit is normally distributed to journalists and is placed on the business's Web site. In fact, if you've ever picked up a national magazine and read an article about a business in a small town and wondered how the magazine knew about the business, it's typically because the business sent the magazine a press kit and the business's story (or product or service) fit the article the magazine was interested in writing. Another technique is to attend industry trade shows. Members of the media often attend trade shows to get the latest industry news. For example, the largest trade show for consumer electronics is International CES, which is held in Las Vegas every January. Many new technology firms use this show to present their products to the public for the first time. They do this in part because they have a captive media audience that is eager to find interesting stories to write about.

Internet-Related Methods (Other Than Pay-Per-Click Advertising)

Business owners are increasing utilizing the Internet as a medium for increasing their visibility. Two techniques, other than pay-per-click advertising, are blogging and social networking.

Blogging

As mentioned earlier, approximately 400,000 businesses now maintain blogs. A blog is a Web site where entries are written in chronological order (similar to a diary). A typical blog contains text entries, images, links to other blogs, and space for readers to leave comments in an interactive format.

The idea behind blogs, in regard to helping a business get noticed, is they familiarize people with a business and help build an emotional bond between a business and its customers. An example is a blog written by Mary Baker, the co-owner of Dover Canyon Winery (http://dovercanyon.typepad.com/dover_canyon). Baker started her blog in April, 2006, using a software package called TypePad Pro that costs her $149.50 a year to maintain. She uses the blog to give her readers periodic updates on what's happening at the winery and how she feels about her life and her business. She also posts pictures of herself, her pets, her family, and daily life at the winery. To make her customers aware of the blog, she drops a postcard with the blog's address into bags with customer purchases. There is also a link to the blog on Dover Canyon Winery's Web site. Mail-order sales for the winery almost doubled from 2006 to 2007.[11]

An example of a business owner who credits his blog for the success of his business is Steve Spangler, the owner of Steve Spangler Science. Spangler's Web site sells science kits and experiments for children and adults. In his blog, titled Steve Spangler's Secrets (www.stevespangler.com), he talks about science and describes experiments that can be done safely with common everyday household items. Spangler gained national attention after a video of him demonstrating the explosive effects of dropping Mentos into two liter bottles of soda spread across the Internet. If you haven't seen the video, it is really fun. Just go to YouTube.com and type in "the original mentos geyser video." The spread of the video and the recognition it has brought him sold Spangler on the value of the Internet for getting the word out about a company. Steve Spangler Science is reportedly generating more than $5 million in annual sales.[12]

Social Networking

Social Networking Web sites are ones that bring together people with common interests to share those interests and interact with one another. Most sites provide a variety of ways for users to interact and get to know one another including chat, messaging, e-mail, video, voice chat, file sharing, and discussion groups. Users are generally permitted to build their own profile pages where they can post information about themselves. Most social networking sites are free and have a directory that makes it easy for a user to zero-in on a specific area of interest.

An example of a social networking site is CraftBuddy.com, a site specifically designed for people who make, enjoy, and sell crafts. On the site, users can easily identify crafters with similar interests, view their profiles to learn more about them, and look at photos of their crafts. As a result, it's a good place for anyone starting a craft or craft-related business to showcase his or her company and get feedback on products. Social networking sites vary in terms of whether they allow advertising and e-commerce to take place. Some sites do not allow their users to advertise, overtly promote their products, or conduct e-commerce on their sites. Others sites, like CraftBuddy.com, have a business directory where members can post links to their commercial Web sites.

There are also more broad-based social networking sites like MySpace.com and Facebook (www.facebook.com). These sites are multifunctional platforms that allow their users to collect friends, build professional networks, and create or join groups of similarly minded people. MySpace has approximately 200 million users worldwide. While MySpace is technically intended for noncommercial use, many businesses post pictures of their products and subtly advertise on their MySpace profiles. MySpace has a feature called "Bulletin" that allows you to post messages which are broadcast to every person on your friends list. You can also set up a blog. Many people that write about MySpace warn against building a large network of friends and then spamming them with subtle advertisements and product promotions. Starbuck's MySpace profile is an example of a well-done business profile. You can view it by going to MySpace.com and typing Starbucks in the search engine. Creating a Facebook profile is similar to MySpace and provides many of the same advantages.

The key to determining whether it's worth your effort to set up a MySpace or Facebook profile is whether you think people in your niche market would find you on the site and participate in your network.

Word-of-Mouth Marketing

The fourth category of techniques that business owners use to get their businesses noticed is word-of-mouth marketing. This technique, which is also called buzz or viral marketing, involves getting people to spread the word about a new product or service via face-to-face conversations, e-mail, text messaging, or through other means. Word-of-mouth marketing is effective in part because people are more inclined to follow-up on a product recommendation from a friend or acquaintance than a paid advertisement.

Most word-of-mouth campaigns are initiated through some form of "seeding" in which key individuals or groups of individuals are utilized to get the initiative going. Seeding typically involves giving away samples of products or allowing people to preview a product before it is available to the general public. It also involves steps that reinforce or encourage the word-of-mouth once it's started.

An example of a successful word-of-mouth campaign is provided by PowerBar, the first energy bar on the market. PowerBar's founder, Brian Maxwell, couldn't afford to advertise his product, so he launched what he referred to as a "grass roots seeding" effort to get the company noticed. The first thing Maxwell did, with the help of his girlfriend (and later wife) Jennifer Biddulph, was to go to every sporting event in the San Francisco area (which is where they lived) and talk to people about the product. Between the two of them, they spoke to over 1,200 people. Once the product was ready, Maxwell sent the people they talked to a little box containing five PowerBars and a follow-up survey. This got people talking about PowerBar and sharing the product with their friends. The next move is legendary. To stimulate word-of-mouth in other areas of the country, Maxwell sent a letter to his existing customers offering to send five PowerBars on their behalf to anyone in the United States for just a $3.00 shipping fee. He even put a note in every box that said "To Brian from Sarah in San Francisco" (or whatever the applicable names were). This effort jump-started word-of-mouth about PowerBar in different parts of the country.

As the word-of-mouth surrounding PowerBar grew, Maxwell turned his focus to "seeding" various sports. He identified influential people in each sport and hired them to be PowerBar spokespersons and gave them a certain number of PowerBars to give away. This effort stimulated word-of-mouth surrounding PowerBar in multiple sports. At one point early in the life of PowerBar, Maxwell was approached by the captain of the U.S. Cycling Team that was preparing to represent the United States in the Tour de France. The person asked Maxwell to donate 1,000 PowerBars to the team. Maxwell hesitated but agreed. On a Saturday, three weeks later, right in the middle of the Tour de France, CBS, which was covering the event, did a three-minute segment on PowerBar, a new "energy bar" the U.S. team was eating. Maxwell couldn't believe his good fortune. That single broadcast created word-of-mouth discussions about PowerBar in thousands of different places.[13]

While not all word-of-mouth campaigns will contain the same elements as the PowerBar campaign, the gist of what Maxwell did is reflective of successful word-of-mouth campaigns. He "seeded" initial users of his product and then created incentives to encourage them to talk up the product among their friends and acquaintances.

Summary

This chapter illustrates the importance of being familiar with the startup process. A simple awareness of the most cost-effective ways to getting noticed and how to go about implementing them can save a business owner a substantial amount of money and produce better results in the long run. It's simply no longer necessary for a new business to rely strictly on print and media advertising to gain visibility. Many of the methods discussed in this chapter, some of which are virtually free, are equally effective in increasing the visibility and legitimacy of a new business.

The next chapter focuses on the myth that the Internet isn't all it was hyped up to be. Actually, we think you'll come away from reading the chapter with just the opposite impression—that the Internet is a marvelous tool. In the chapter, we discuss the factors that facilitate Internet business success along with the most common ways that businesses and individuals make money online.

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Chapter 8. Myth No. 8: The Internet Isn't What It Was All Hyped Up to Be: Truth No. 8: There Are Many Legitimate and Enjoyable Ways to Make Money Online

Introduction

An unfortunate myth that discourages people who otherwise could make a good living as business owners is the belief that the Internet isn't all it was hyped up to be. It's not difficult to understand where this sentiment comes from. During the Internet bubble, which lasted from 1995 to early 2001, there were predictions that the Internet would change everything and that brick-and-mortar stores were doomed. After the bubble burst, and thousands of Internet companies went out of business, it became clear that there had been some over-exuberance involved. It's hard to forget the spectacle of companies like Pets.com, with its playful sock puppet, losing its investors' millions of dollars and the sharp decline in the stock market. One Internet stock, Yahoo!, declined from $118.75 a share on January 3, 2000, to $4.06 on September 26, 2001.

Fortunately, the stock market recovered, and the Internet has proven to be resilient.

In fact, the number of Internet users worldwide has almost tripled since early 2001.[1] The number of businesses, shoppers, and people making a living online is also sharply up. It is estimated that United States online sales will increase 17.5% a year from 2007 until 2011.[2] Other activities online are also growing. For example, as mentioned in Chapter 7, approximately 400,000 businesses now maintain blogs, up from near zero in 2004 when business people started blogging.[3]

The truth is that the Internet has turned out to be a remarkable tool and platform. There are a growing number of ways that individuals and businesses are making money online. In fact, one of the beauties of the Internet is that people don't necessarily have to have products or services to sell to make money.

If someone knows a great deal about a particular topic, such as cooking or home repair, she can launch a Web site, populate it with articles, tips, and other useful information and make money online by essentially selling access to the people she attracts to her Web site. This is done primarily by selling advertising space on the Web site, as will be discussed throughout the chapter, to companies who sell products or services of interest to the visitors to the site. This one factor alone has enabled numerous people to convert hobbies and personal interests into part-time and full-time businesses.

To more fully discuss these topics and further dispel the myth that the Internet isn't all it was hyped up to be, this chapter proceeds in the following manner. First, we describe three factors that facilitate Internet-related business success. Second, we describe the most common ways that individuals and businesses make money online. Third, we describe the manner in which the Internet provides a platform for the sale of products and services produced by people working on a freelance basis.

Factors That Facilitate Internet-Related Business Success

Of the many factors contributing to Internet-related business success, three stand out—acquiring Internet-related knowledge and expertise, attracting users, and patience. Many people are not successful making money online primarily because they fall short on one or more of these important factors. Let's learn more about each factor.

Acquiring Internet-Related Knowledge and Expertise

The first factor that contributes to Internet-related success is acquiring Internet-related knowledge and expertise. While you don't have to be a computer geek to launch and run a successful Web site or other Internet application, you do need a certain level of expertise. For example, even if you hire someone to build your Web site or blog, you will normally maintain it and update it yourself. If you decide to monetize the site by participating in an affiliate or pay-per-click program, you'll need to know how to set these programs up. For example, if a business is approved by Google to display AdSense ads, you'll be provided some JavaScript code to paste into the html document that underlies your Web site. While this task isn't difficult you have to know what you're doing. In addition, the more you know about html (the main language for Web sites) and Web site design, the better you'll be at moving the ads around your site to see where they perform the best.

It's also important to know the basics of how the Internet works, particularly as it relates to how to obtain an Internet domain name, how to find a company to host your Web site, how to set up an e-mail account that corresponds to your Internet address, and so on. It's also helpful to know as much as possible about your options before you settle on how to utilize the Internet. For example, if you make crafts at home and plan to sell them online, you might not need your own Web site. You could sell them on eBay or another auction Web site. You could also utilize a service like Etsy (www.etsy.com), which is an online marketplace for the buying and selling of handmade products. If you become an Etsy member, the company will set up an online storefront for you.

The best way to get up-to-speed on these and similar topics is to read Internet-related books and magazines and find help through other reliable sources. Small Business Development Centers often host seminars and workshops on how to start an Internet business. There are also companies that specialize in helping people design Web sites and set up Internet businesses. While many of these companies are legitimate, be careful. There are companies that prey on people who hope to "get rich quick" on the Internet and insist on being paid upfront. Make sure to check out any company before doing any business with them and ask for the names and phone numbers of people who they've helped before. If they won't provide names and phone numbers, look elsewhere.

Attracting Users

Regardless of the type of Internet business you start, one of your main goals will be to attract users or visitors to your site. A large measure of a Web site or blog's value is the total number of unique visitors it attracts on a weekly or monthly basis and the match between the demographic makeup of the visitors (that is, gender, age, occupation, interests, and income level) and the product or topic the site is promoting. The money a Web site or blog can generate is also roughly proportional to the amount of traffic it can produce.

As a result of these realities, it's important to take steps to attract people to your Web site or blog and to increase your traffic over time. There are several ways to do this. It's important to launch a site that satisfies its visitors. This means good quality products and services and a pleasant shopping experience for e-commerce sites, and rich content for blogs and special interest Web sites. These positive attributes keep people coming back and engender word-of-mouth referrals. The degree to which the people who launch a Web site or blog are passionate about their businesses also shows. It takes a lot of work to launch a well-designed, fully functional, and content-rich Web site or blog. If you throw something up quickly primarily to try to make money, it normally won't fly.

There are also specific steps that can be taken to drive traffic to your Web site. One step is to become an expert in your field and write articles and columns and frequently post comments on the blogs of others. Work should always be signed, and the business's Web site address should be listed. When you do this, you are giving people who have an interest in what you have to sell a way to "reach you" through your Web site.

There are also online article directories, such as Free Article Depot (http://free-article-depot.com), which people contribute to for free, hoping that a Web site will pick up the article and post it on its site. These articles have a signature box at the end, which provides you space to tell the reader about yourself, list keywords that pertain to the article, and provide your Web site address. Doing this directs people to your Web site, which is then picked up by the major search engines. As a result, the more articles posted, and the more Web sites that publish them, the earlier your business will appear in Google and Yahoo! search results. Some people claim that the best articles they've posted on Free Article Depot or Ezine Article (another directory) have spread to over 10,000 Web sites within a week. The key is to write articles that Web site owners see as valuable or interesting.

There is also an entire science referred to as Search Engine Optimization (SEO), which suggests additional techniques to get a business's name moved up in search engine results. The idea is that the earlier your business's name appears in search engine listings, the more people will click the link and visit your site. There are many resources, including books, magazine articles, and Web sites, that provide information on this topic.

Patience

Patience is a third factor that contributes to Internet-related success. It takes time and effort to successfully launch an Internet business and build traffic. Because of this, many Internet companies start as part-time businesses, adding content and visitors over time, before they're able to make much money. Top-tier companies only advertise on Web sites and blogs once they've reached a certain threshold of traffic. As a result, if you started a blog that focused on running marathons, you might need to post entries on your blog two or three times a week, write articles to draw attention to your blog, and promote your blog in other ways for several months or longer before you have enough traffic to attract good quality advertisers. People who don't understand this can become easily frustrated. Unless you have a generous advertising budget to promote your site, it will take time for users to find you regardless of how good you are.

It also takes patience and restraint, after you launch your Web site or blog, to resist the temptation to try to do too much too fast. As just mentioned, the primary way to build a successful Internet business is to satisfy users. For e-commerce sites, this means targeting a specialized niche market first rather than trying to tackle broad markets. In the case of a specialty Web site or blog, it means adding advertising slowly rather than quickly to avoid irritating early users. The cardinal rule in building an Internet business is to focus on quality first, and the money will follow.

The Most Common Ways That Individuals and Businesses Make Money Online

There are a growing number of ways that individuals and businesses are making money online. In fact, when the dot-com bubble burst in early 2001, most of the money-making tactics and techniques described here didn't exist. The Internet is a much healthier marketplace today, with multiple legitimate ways for individuals and businesses to sell products and services online and to monetize other types of Internet applications.

The following is a discussion of the six most common ways individuals and businesses make money online. An overview of the most familiar ways the Internet is used, along with an identification of money-making techniques that are most commonly utilized in those areas, is included in Table 8.1.

Table 8.1. How Businesses Make Money with Internet-Related Activities

Internet-Related Activities	Money-Making Techniques	Representative Businesses
E-commerce Web site	Direct sales, subscription fees, commissions	Amazon.com, SmugMug, Redfin
Business Web site (that supports a primarily off-line business)	Direct sales	Screenlife, Real Cosmetics, Yogitoes
Informative Special Interest Web site (often operated by hobbyists and enthusiasts)	AdSense, affiliate programs, direct sales, subscription fees	Zillow.com, SeatGuru.com, Askthebuilder.com
Social networking Web site	AdSense, affiliate programs, subscription fees	Facebook, Dogster.com, Quentin's Friends
Blog	Adsense, affiliate programs, direct sales	JoelComm.com, TechCrunch, TheMommyBlog
Auction Web site	Commissions, AdSense	eBay, StubHub, uBid.com

Affiliate Programs

An *affiliate program* is a way for online merchants, like 1-800-Flowers or Amazon.com, to get more exposure by offering a commission to Web sites and blogs that are willing to feature ads for their products or services. In most cases, the ads are small text ads, and the merchant sponsoring the program pays the affiliate a small commission every time someone clicks the ads and buys one of its products or services. eBay and similar membership sites have a slightly different type of program. If you're an eBay affiliate, you get paid \$25 to \$35 every time someone clicks the eBay ad on your site, creates an eBay account, and places a bid within 30 days. You also get between 50% and 75% of eBay's revenue on all winning bids or Buy It Nows (BINs) within seven days of the click.[4] Some online merchants have extensive affiliate programs. 1-800-Flowers, for example, has more than 40,000 affiliates.

The beauty of participating in an affiliate program, from the perspective of the owner of a Web site or a blog, is that you can make money on your site without incurring the costs involved with creating your own product or service and providing customer support. Your job is to attract people to your Web site or blog, and every time they click on your affiliate marketer's link, you get paid. This approach allows people who are experts in certain areas, like fitness, health care, or investments, to put up Web sites and seemingly give away vast amounts of information. The way they typically make money is by participating in affiliate programs and/or pay-per-click programs, which are described next.

There are two ways to get involved in affiliate programs. Many online merchants place information about how to sign up for their affiliate programs on their Web sites. For example, on Overstock.com, toward the bottom of its home page, there is a link that reads "Become an Affiliate." This link describes Overstock.com's affiliate program, including the commission rate they're currently paying. At the time this book was written, Overstock.com was offering an 8% commission. That means that if you created a Web site and became an Overstock.com affiliate, every time someone clicked through to Overstock.com's Web site from your Web site and spent $1,000, you'd get paid $80. Some affiliate programs are even more lucrative. Amazon.com has offered up to a 20% commission on MP3 downloads that originate through one of its affiliate's sites.

You can also work through a company that manages affiliate programs for others. Examples of companies that do this are Commission Junction (www.cj.com), Link Share (www.linkshare.com), and ShareASale (www.shareasale.com). These companies have access to thousands of online merchants that have affiliate programs. Their job is to find the best match between firms that sponsor affiliate programs and the Web sites and blogs that have the most potential to generate click-throughs to their sites.

Pay-Per-Click Programs

The second way that individuals and businesses make money online is through pay-per-click programs. The basic idea behind these programs is similar to an affiliate program. A Web site or blog allows an advertiser's link to be placed on its site and gets paid a small commission every time someone clicks the ad.

All of the major search engines sponsor pay-per-click programs. Examples include Google AdSense, Yahoo! Search Marketing, and MSN Adcenter. Google's AdSense program is by far the best-known and the largest. You've seen AdSense ads many times as you've looked at Web sites and blogs. They are easy to spot because they have a small emblem underneath the ads that says "Ads by Google."

Anyone with a Web site, blog, or other Internet application that has content can apply to participate in a pay-per-click program. Most Web sites and blogs, if they have reasonably good content and meet the search engine's terms of condition, are approved. As mentioned earlier in the chapter, there is a little work involved with setting up a pay-per-click program, but once things are setup, AdSense or any of the other programs do the rest. The most compelling aspect of pay-per-click programs is that they deliver contextually relevant ads. So if you start a blog about fitness, AdSense will place ads related to fitness on your blog. It's actually fun to watch because the ads will change based on the specific topic you're blogging about. If you write about running on one day, the ads will be for running related products, like treadmills, running shoes, and running apparel. If the topic is swimming two days later, the ads will change and focus on products like swimsuits, goggles, cruises, and sunscreen. AdSense does this by continually scanning blog entries and matching ads with keywords it finds.

Similar to affiliate programs, pay-per-click programs help people who put up special interest Web sites and blogs make money by selling access to the people they attract. Content-rich Web sites often place AdSense ads in multiple locations on their sites. For example, Tim Carter, a well-know columnist on home repair, has a Web site named Ask the Builder (www.askthebuilder.com). Information and instructions on all types of home building projects and repair are available on this Web site, as are links to areas that focus on specific topics, like air conditioning, cabinets, deck construction, lighting, and plumbing. Clicking any one of these areas brings up AdSense ads that deal with that specific area. All together, the site has hundreds of AdSense ads. Carter is able to do this and still attract large numbers of visitors because the information he provides is good and helpful. He might also believe that his ads, in a certain respect, add valuable content to the site. If someone is looking at the portion of his site that deals with how to construct a deck, he or she might actually appreciate seeing ads that point to Web sites where books and blueprints for building decks are available.

The one thing people should strictly avoid in participating in pay-per-click programs is trying to game the system by clicking ads on your own Web sites (to make yourself money) or asking your friends to click the ads. Google, Yahoo!, and the other providers of pay-per-click programs consider this to be "click-fraud" and have extremely sophisticated systems for detecting when this is happening. If you get caught doing this, you can be kicked out of a pay-per-click program, and once you get kicked out it is reportedly very difficult to be readmitted.

Direct Ads

The third way individuals and businesses make money online is through direct advertising programs. These ads tend to be banner ads, skyscraper ads (tall ads that run along the side of a Web page), or ads with pictures that are embedded in the content of a Web site or blog. If you run ads like these on your Web site or blog, you're paid a commission based on either the number of times an ad is clicked or the number of times it's seen (that is, the number of "impressions"). This type of advertising was more popular before affiliate programs and pay-per-click advertising caught on. Many Web site and blog owners shy away from banner ads in particular because they tend to be seen as more intrusive than text ads.

Similar to hooking up with an affiliate program, you can get involved with direct advertising in one of two ways. The first way is to contact an advertiser directly and negotiate the placement of ads. The advantage of doing this is that you eliminate the cut that AdSense or one of the facilitators of an affiliate program takes to deliver you ads. Many Web sites have links that say "Advertise Here" to encourage people to contact them directly. For example, on Ask the Builder's Web site, there is a link on the toolbar at the top of the site labeled "Advertise." This link provides detailed information about Ask the Builder's direct advertising program.

The second way to get involved in direct advertising is to work through a company that arranges direct advertising for online merchants. There are many companies that do this, including BurstMedia (www.burstmedia.com), DoubleClick (www.doubleclick.com), and Tribal Fusion (www.tribalfusion.com). An example of a Web site that is almost always displaying direct ads is Deal of the Day (www.dealoftheday.com).

The judgment call that Web site and blog owners have to make, as it pertains to affiliate programs, pay-per-click ads, and direct ads, is how much is enough. It's a delicate balancing act. As a Web site or blog owner, you want to maximize the earning potential of your site without driving away visitors. One of the nice things about the Internet is that the owner of a Web site or blog can track the traffic on the sites on a real-time basis. As a result, many people are constantly experimenting with the amount of advertising that's displayed on their sites and carefully monitoring how changes in the amount and types of advertising affect the number of visitors they attract.

Why "Free" Web Sites Are Popular

An understanding of how Internet advertising works answers a question that many people ask about the Internet. Why do so many Web sites provide the services they do for free? Blue Mountain (www.bluemountain.com), for example, is a Web site that allows its users to send free e-Cards, create and print cards to be delivered in person, and do all kinds of other fun stuff for free. They don't even sell upgrades or premium products. There is no where on the Blue Mountain Web site where you can spend money.

So why does Blue Mountain do all of this for free? The reason is that free sites tend to attract users faster than sites that charge for their services, and the more visitors that Blue Mountain can get to its site, the more it can charge for advertising. Many of the Web's most popular companies, including MySpace and Facebook, are based largely on this model. By boosting its number of visitors, Blue Mountain can also attract higher-quality advertisers. The company currently displays ads for blue chip advertisers such as MetLife, Circuit City, PetSmart, and Disney.

E-Commerce

A fourth way that individuals and small businesses make money online is through e-commerce. E-commerce refers to the direct buying and selling of products and services online. Several of the Internet businesses we've highlighted in this book, including Wadee (children's toys and gift items) and Odd Ball Shoe Company (odd sized shoes), are e-commerce companies. They have Web sites that are online storefronts and utilize the Internet to sell their products.

There are various types of e-commerce companies. Some companies sell services. An example is onlc (www.onlc.com), a company that sells access to online training videos that help people learn computer software products like Microsoft Access and Excel. Other companies sell matchmaking services. TechStudents.com, for example, sells a service that matches people who need Web sites designed and similar services with technology-oriented college students who are looking for part-time work.

For e-commerce companies that sell products, there are two primary ways they go about it. Some companies, like Wadee, make their own products, warehouse them, and ship them to customers when they receive an order. Other companies utilize a process referred to as *drop-shipping*. Drop-shippers feature an online storefront but do not have any inventory. Instead, when they take an order, they pass it on to a wholesaler or manufacturer who fills the order and then ships it directly to the customer. The product is normally shipped in a box with the online retailer's name on it and the retailer's invoice inside, so it looks like it came directly from the online retailer. By utilizing this method, an online merchant earns a lower margin than it would if it controlled the entire process itself, but its costs are lower, too. It also doesn't get stuck with inventory that goes out of style or doesn't sell for some other reason. The system is not completely friction-free. The online retailer still has to offer customer support and deal with shipping complaints and returned items.

eBags (www.ebags.com), an e-commerce company that sells luggage, handbags, backpacks, and similar items, is an example of a drop-shipper. One of the most attractive aspects of eBag's online store is the sheer number of bags it has for sale—over 8,000. It's unlikely that eBags would carry so many bags if it had to maintain its own inventory and take the risk of getting caught with outdated products.

Most e-commerce companies do not participate in affiliate, pay-per-click programs, or direct advertising programs, opting instead to feature clean-looking Web sites that focus strictly on the products or services they have for sale. This isn't always the case, however. Buy.com, for example, is primarily an e-commerce Web site but almost always has other types of advertising prominently displayed on its site. The reverse also occurs. Some special interest Web sites and blogs that make most of their money on online advertising will have some e-commerce. Ask the Builder, for example, has an online store along with the content and advertising described earlier.

Subscription Services

A fifth way that individuals and businesses make money online is through subscription or monthly access services. These sites typically have specific services that they provide that have sufficient value that people in their niche markets are willing to pay for. Examples are companies that provide "members only" access to online games, music downloads, newsletters, and streaming video coverage of sporting events. For example, Rhapsody is an online music download site. For $14.99 per month, you can download an unlimited number of songs from Rhapsody's two million song library. The songs only remain available, however, while your subscription is current.

A common strategy among firms that charge subscription or access fees is to give away a basic version of whatever they offer for free, to attract visitors, and then sell access to upgraded versions of the service. An example is Box.net, a relatively new online company. Box.net provides online storage for documents, photos, video files, media clips, and any other type of digital file. There are three levels of participation in the company's business: Lite, Individual, and Business. The Lite service, which includes one gigabyte of storage, is free. The Individual service includes five gigabytes of storage for $7.95 per month. The Business service includes 15 gigabytes of storage for $19.85 per month.[5]

Interestingly, some of the subscription-based sites are very resilient in direct competition with sites that offer a similar service for free but include ads on their sites. An example is SmugMug (www.smugmug.com), an online photo sharing site. SmugMug charges $39.95 per year to store unlimited photos online. Other sites, like Shufferfly, Flickr, and WebShots, offer photo storage for free. Ostensibly, the reason SmugMug is able to charge a fee is that it offers higher levels of customer service and has a more user-friendly interface (in terms of how you view photos online) than its competitors. But the owners of SmugMug feel that its ability to charge goes beyond these obvious points. Some of the free sites have closed abruptly, and the users have lost photos. (Who wants to lose their photos?) SmugMug, because it charges, might be seen as more reliable and dependable for the long-term. In addition, the owners believe that when people pay for something, they innately assign a higher value to it. As a result, SmugMug users tend to treat the site with respect by posting attractive, high-quality photos that are in good taste. SmugMug's users appreciate this facet of the site, compared to the free sites, where unseemly photos often creep in.[6]

Quentin's Friends: Turning a Social Networking Site into a Money-Making Endeavor by Charging Users

During the late 1990s, Quentin English frequently fielded e-mail messages from friends who wanted help finding roommates and apartments in New York City. In early 2000, he decided to set up an online forum to more efficiently help his friends swap tips about apartments and living in the city.

The forum, called Quentin's Friends, started with about 25 people but quickly grew as Quentin's friends invited their friends to join the forum. By 2000, the number of members had swelled to about 5,000. For

Quentin, this meant extra work, so he gradually started trying to make money on the site. He tried ads and several other ideas with only limited success. In 2004, he decided to start charging a subscription fee of $4.50 a month or $12.00 a year to participate in the site. Skeptics told him he'd be lucky to keep 5% of his participants, but about 25% agreed to pay. Today, the site is growing and is reportedly profitable. People exchange information about jobs, apartments, kitchen and computer equipment, reliable doctors, and other types of everyday interests and concerns. People can only join Quentin's Friends if they're invited by a current member, and they can get kicked out for inappropriate behavior or for giving out deceptive information.

Quentin acknowledges that his subscription approach was a gamble, given that people can get information about apartments, roommates, and similar things through free services like Craigslist.com. It's one more example of the multiple ways that people make money on the Internet when they provide a product or service for which someone is willing to pay.[7]

Other

There is a variety of other ways that individuals and businesses make money online. Redfin (www.redfin.com), for example, allows customers to buy and sell homes online and charges a commission on each real-estate transaction it brokers. Sermo (www.sermo.com), a social networking site for licensed physicians, makes money by monitoring discussions and determining how doctors feel about new drugs and then sells data reflecting aggregated trends. The names of the individual doctors, of course, are omitted, and the practice is fully disclosed to Sermo's members when they register.

Platforms That Help Freelancers Sell Their Products and Services Online

One exciting group of Internet businesses, which are increasing in prominence and use, are Web sites that serve as platforms to help freelancers sell their products or services online. There are many people who have full-time jobs and earn extra money on a "freelance" basis as a consultant, business plan writer, artist, photographer, or through some other means. Historically, a challenge these folks have had is getting the word out about their work. Many people are excellent photographers or Web site designers but have never made much extra money because they haven’t found a practical way to connect with people who need what they do.

A growing number of Web sites are sprouting up to solve this exact problem. These sites not only help people earn extra income but in some cases have helped people start home businesses and transform a hobby or skill into a full-time job.

This section discusses two categories of Web sites that act as platforms to help freelancers and others sell their products and services.

General Web Sites That Help Freelancers Sell Their Work

There are a number of general or all-purpose Web sites that help freelancers find work. The largest and best-known sites in this category are Guru.com, Elance.com, and Sologig.com. The primary purpose of these sites is to match individuals or businesses that need work done with freelancers who specialize in a specific area. The breadth of specialties that these sites cover continues to grow. Guru.com, for example, claims that it has helped over 30,000 companies employ over 629,000 freelancers to do various jobs.[8] The jobs range from data entry to Web site design to installing kitchens.

Most of the sites are free to the employer and charge freelancers a monthly or yearly membership fee and a 6% to 10% commission on the money they earn. Some sites allow freelancers to bid on jobs, while others introduce companies to freelancers and allow the two parties to negotiate a price. Nearly all of the sites post ratings and reviews of freelancers provided by the companies they’ve worked for and vice versa, so there is a strong incentive on the part of everyone to perform. Although the sites do not indemnify the work of the freelancers, several of the sites will hold a company’s money in escrow, and the freelancer is only paid when a job is completed satisfactorily. On some of the sites, YouTube videos of freelancers demonstrating their work are available. In most cases, you can also privately chat or instant message with freelancers without sharing personal contact information.

To get a good sense of what these sites are like, spend a few minutes browsing around Guru.com or Elance.com. Pay particular attention to the sheer number and variety of freelancers who are involved and the amount of money they’ve made. One of the biggest advantages of these sites, from a company’s point of view, is that a freelancer can normally be "tried out" fairly inexpensively. So if you’re an advertising or public relations firm, and you design logos for your clients, you can normally find someone on Guru.com or Elance.com to outsource this work for $200 or less. If you like the work the person does, you can use them for future jobs. If you don't like their work, the most you lose is $200 (or whatever the fee was). This logic makes it easy to understand why so many companies are opting to use freelancers to do work for them rather than taking a much larger risk by hiring additional employees.

The one thing that sites like Guru.com and Elance.com are not, and are not intended to be, are job sites like CareerBuilder.com. The matches they make are for project-based work, like copywriting an article or a book, designing a Web site, or photographing a wedding. In fact, the average contract handled by Guru.com is less than $700.[9] This aspect of Guru.com and similar sites is their biggest strength in the eyes of many freelancers. Freelancers are not typically looking for a full-time job, but are looking for ways to earn income by doing project-based work in their free time.

Specific Web Sites That Target Freelancers Who Work in Certain Areas

There are also Web sites that focus on specific types or categories of freelance work. A sample of these sites is shown in Table 8.2. Many of the sites have interfaces that resemble Guru.com and Elance.com. Their fee structures and setups vary. Freelance Switch (http://freelanceswitch.com) provides a directory of niche freelance sites like those shown in Table 8.1.

Table 8.2. A Sample of Web Sites That Target Freelancers Who Work in Certain Areas

Web Site	Area	Web Site Address
Altpick	Artists, illustrators, photographers	www.altpick.com
Design Crowd	Web site design	www.designcrowd.com
Proz	Translation services	www.proz.com
RentACoder	Software development	www.rentacoder.com
Writerlance	Freelance writing	www.writerlance.com

There is also a growing number of Web sites designed to help freelancers in another way. Instead of directly matching freelancers with companies, these sites provide a marketplace or storefront to help freelancers sell their products directly to the public. eBay is an obvious example. Another example is Etsy (www.etsy.com), mentioned earlier in the chapter, which is an online marketplace for the sales of handmade products. Etsy provides a platform for people who make crafts and similar products to display their work, and the Internet provides the leverage Etsy needs to reach a global audience. It also reconnects buyers with handmade items. Started in 2005, the company now has nearly 550,000 registered users, 60,000 of whom are individual artists selling more than 700,000 different handmade items.[10] There are 30 different categories of items listed on the Etsy Web site ranging from Accessories (aprons, belts, umbrellas) to Woodworking (carvings, clocks, home décor). Each Etsy freelancer is provided an Etsy store to sell his or her products. Kate Black and Karen Adelman are Etsy freelancers. Their Etsy stores can be seen at www.kateblack.etsy.com and www.kartdesign.etsy.com, respectively.

A similar example of a Web site that provides a platform for freelancers to make money is Zazzle.com. Zazzle is an online service that allows its customers to upload images that can be printed on T-shirts, stamps, posters, cards, coffee mugs, and a variety of other items. This approach allows freelancers to place digital images they've produced on products, like coffee mugs and posters, and resell them at craft shows and through other outlets. In addition, Zazzle maintains an inventory of digital images that are posted on its Web site, many of which are provided to the company by freelance photographers. If an image provided by a freelancer is used to create a T-shirt, poster, coffee mug, or other item by a third party, the creator of the image is paid up to a 17% royalty.

Summary

It's important to know the most common ways that businesses and individuals make money online. Almost all businesses now have Internet strategies, so the extent to which the various ways of making money online are appropriate for a business is an essential issue to discern. It will also become increasingly important to know how to utilize the Internet to make various forms of a business more effective. For example, a growing number of businesses are utilizing the services of Web sites like Guru.com and Elance.com to find good people to complete project-based work.

The final chapter of the book focuses on the myth that it's easy to start a business, but it's difficult and stressful to grow one. This myth is a tough one to grapple with because it sometimes is true. As indicated in the chapter, growing a business can be a joy or a nightmare—it all depends on how the process is managed. In the chapter, we tackle the most important issues pertaining to firm growth and lay out a roadmap for how to approach this important topic.

Endnotes

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Chapter 9. Myth No. 9: It's Easy to Start a Business, But It's Difficult and Stressful to Grow One: Truth No. 9: Businesses Can Be Grown Profitably and Enjoyably

Introduction

A fear that many prospective business owners have is that once they get their businesses started, they won't be able to grow them successfully. It's easy to understand where this fear comes from. There is a prevailing notion that successful businesses are growth businesses, which has been bolstered by common phrases such as, "If you're not moving forward, you're moving backwards," and "Businesses either grow, or they die." There are also signals that remind us of just how difficult growing a business can be. Think about the number of times that we've all heard about businesses that have downsized or laid off employees. While there may be many reasons for those events, it's easy to infer that these businesses weren't able to sustain their growth. There are also sobering statistics that pertain to business growth. For example, Chris Zook, an expert on firm growth, has found that over a 10-year period only 1 in 10 businesses achieve more than a modest level of sustained and profitable growth (defined as 5.5% or more per year).[1] Reading that statistic would cause any prospective business owner to pause and think, "Wow, if only 1 out of 10 *existing* businesses grows by more than 5.5% per year, what chance does a *new* firm have?"

The reality is that if that you have a business that meets a defined need, and are a capable owner, in most instances you can grow your business profitably and enjoyably. It doesn't happen by happenstance, however. Growing a business successfully takes preparation, good management, and an awareness of the key issues involved. It also takes a business owner with a high degree of self-awareness and a strong, consistent sense of the type of business that he or she wants to have. Growing a business can be a joy or a nightmare. There are many businesses that have started, grown prudently, and are thriving, returning to their owners just the sort of lives they had hoped for. Sadly, there are also many businesses that have done just the opposite—they've started, grown either too slowly or too quickly, and have failed, leaving their owners financially and emotionally damaged. In most cases, these businesses had no plan for growth, and their owners didn't try to build their companies in a focused and purposeful manner.

The key to keeping the myth described in this chapter from coming true is to take determined steps to prevent it from happening. All businesses would rather grow profitably and enjoyably rather than in a difficult and stressful manner.

Improper growth can also ruin a business. For example, some businesses start slow and then get a string of large orders. If they're not careful, they can over commit and find themselves struggling to fill the orders and manage their cash flows in ways that allow them to regularly pay their employees. Similarly, early success can cause a business to become overconfident and hire too many people or lease too much manufacturing or office space, resulting in financial hardship. It's easy to err in either direction, which makes it doubly important to remain vigilant and follow a growth plan.

To discuss these important topics and further dispel the myth that it's easy to start a business but difficult and stressful to grow one, this chapter is divided into three parts. The first part focuses on preparing for growth. The second part focuses on managing growth. The third part describes the most common strategies businesses use to grow their firms.

Preparing for Growth

While there is some trial-and-error involved in starting and growing any business, the degree to which a firm prepares for its future growth has a direct bearing on its level of success. Many of the early decisions that a business makes, such as whether it will focus on a single product or become a multi-product firm, have an influence on the nature of its growth. This section focuses on three issues that are important as a business starts and prepares itself for growth. These issues are:

- Appreciating the nature of business growth
- Determining a business's core strengths and capabilities
- Planning for growth

Appreciating the Nature of Business Growth

The first issue that helps business owners prepare for growth is to gain an appreciation of the nature of business growth. Not knowing much about business growth, including the full range of outcomes that can occur, might cause a well-intended business owner to make decisions that cripple or ruin his or her business. The best way for a business owner to learn about growth is to access resources described throughout the book, such as talking to a SCORE advisor, attending a class on business growth hosted by a Small Business Development Center, or finding a mentor. Many businesses also form a Board of Advisors, which is a panel of experts who are asked by a business's owner to provide counsel and advice on an ongoing basis.

The first thing for a business owner to appreciate about growth is that not all businesses have the potential to be aggressive growth companies. The businesses that have the potential to grow the fastest over a sustained period of time are ones that solve a significant problem or have a major impact on their customers' productivity or lives. This is why the lists of fast-growing firms are often dominated by healthcare and technology companies. These companies have the potential to make the biggest impact on their customers' businesses or lives. This point is affirmed by contrasting the sporting goods industry with the biotechnology industry. From 2004 to 2006, the average sporting goods store in the United States grew by 3.3%, while the average biotechnology company grew by 13.1%.[2] While there is nothing wrong with starting and owning a sporting goods store, it's important to have a realistic outlook of how fast the business will likely grow. Even though an individual sporting goods store might get off to a fast start, as it gets larger, its annual growth will normally start to reflect its industry's norms.

The second thing that is important for a business owner to appreciate about growth is that businesses can grow too fast. Many businesses start fast and never let up, which is stressful for everyone involved. Other businesses start, grow at a measured pace, and then experience a sudden upswing in orders and have difficultly keeping up. This scenario can transform a business with satisfied customers and employees into a chaotic workplace with people scrambling to push the business's product out the door as quickly as possible. The way to prevent this from happening is to recognize when to put the brakes on and have the courage to do it. This set of circumstances played out early in the life of The Pampered Chef, the company that sells kitchen utensils through home parties. Just about the time the company was gaining serious momentum, it realized that it didn't have enough inventory to serve what it expected to be a busy Christmas season. This reality posed a serious dilemma. It couldn't instantly increase its inventory (its vendors were all low), yet it didn't want to discourage its home consultants from making sales or signing up new consultants. One option was to institute a recruiting freeze (on new home consultants), which would slow the rate of sales. Doris Christopher, the company's founder, remembers asking others for advice. Most advised against instituting a recruiting freeze, arguing that the lifeblood of any direct sales organization is to sign up new recruits. In the end, the company decided to institute the freeze and slowed its sales enough to fill all orders on time during the holiday season. The freeze was lifted the following January, and the number of Pampered Chef recruits soared. Reflecting on the decision, Doris Christopher later wrote:

> *"Looking back, the recruiting freeze augmented our reputation with our sales force, customers, and vendors. People saw us as an honest company that was trying to do the right thing and not overestimating our capabilities."*[3]

Other businesses have faced similar dilemmas and have sometimes made the right call and sometimes haven't. The overarching point is that growth must be handled with kid gloves. A business can only grow as fast as its infrastructure allows (a subject we talk more about later). A list of indicators that a business is growing too fast in provided in the following bulleted list.

- Borrowing money to pay for routine operating expenses.
- Extremely tight profit margins.
- Over-stretched staff.
- Quality is slipping.
- Customer complaints are up.
- Employees dread coming to work.
- Productivity is falling.
- The business's accountants are starting to worry.

The third thing it's important for a business owner to appreciate about growth is that business success doesn't always scale. What this means is that the very thing that makes a business successful might suffer as the result of growth. For example, Wadee, a company talked about throughout this book, sells hand-made gifts and toys for children. It would be hard for Wadee to grow quickly and still produce hand-made products. There might also be an upward limit on the number of people who are willing to pay extra for hand-made goods. To accelerate its growth, Wadee could start selling machine-made children's gifts and toys along with its hand-made products. But it would then lose its distinctiveness and cease being what it once was.

Similarly, businesses that are based on providing high levels of customer service often don’t scale or grow well. An investment brokerage service, for example, that initially provided high levels of customer service can quickly evolve into providing standard or even substandard service as it adds customers, opens new offices, adds new product lines, and starts automating key functions. Its initial customers might find that it’s harder to get individualized service than it once was and start viewing the company as just another ho-hum business.

There is also a category of businesses that sell high-end or specialty products that earn high margins. These businesses typically sell their products through venues where customers prioritize quality over price. These businesses can grow but only at a measured pace. If they grow too quickly, they can lose the "exclusivity" they are trying to project or can damage their special appeal.

The Case Against Quick Growth: Timbuk2’s Short-Lived Partnership with CompUSA

In early 2003, Mark Dwight, the CEO of Timbuk2, the San Francisco-based manufacturer of urban shoulder bags, was on the top of the world. The company had just inked a deal with CompUSA to carry its bags, and it looked as if it had caught a big break. Impressive company growth was nearly assured for some time to come.

Yet just three months later, Dwight had second thoughts. It wasn’t the sales. Sales were booming. But financially, Timbuk2 was being squeezed by the relationship. CompUSA’s slim margins and high-volume demand were difficult for Timbuk2 to cope with. In addition, Dwight became increasingly worried that selling through a mainstream retailer would change how consumers viewed his company. He wanted to see his company increase sales, but he didn’t want it to lose its quirkiness and unique appeal either.

So Dwight cancelled the CompUSA deal and refocused Timbuk2. In refocusing the company, he compared it to Coach, a company that sells primarily through specialty stores. Specialty stores, like the Sharper Image and the Apple Computer Store, appeal to consumers who prioritize quality and brand image over price. This attribute of specialty stores allows vendors like Timbuk2 to earn higher margins (than they would earn at a big-box retailer like CompUSA), which compensates for lower-volume sales.

The results of Dwight's decision have been impressive. Although Timbuk2 missed its chance for fast growth, sales are up, and the company has an increasingly attractive product line featuring items that are sold online and through specialty stores throughout the United States.

Determining a Business's Core Strengths and Capabilities

The second issue that helps business owners prepare for growth is to clearly identify their core strengths and capabilities. While this recommendation may seem self-evident, it continues to surprise us how many businesses aren't sure of what their most important strengths and capabilities are. The reason this topic is so important is that a business achieves healthy growth when it matches its strengths with opportunities. If a business doesn't know what its strengths are, it can easily stray into areas where it finds itself at a competitive disadvantage. This happened to Amazon.com early in its life as a company. Just months after it announced that it intended to become "a place where you can buy anything for anyone," Amazon laid off 15% of its workforce and started eliminating product lines under the slogan "Get the Crap Out." The company quickly realized that it was competing in areas that were not well-matched with its strengths, and its competitors had a decided advantage.[4]

The way successful businesses typically evolve is to start by selling a product or service that is consistent with their core strengths and capabilities and increase sales by incrementally moving into areas that are different from, but are related to, their core strengths and capabilities. Apple is a good example. It utilized its core strengths and capabilities in the areas of technology and design to create the Macintosh and its iMac line of computers and is now using those same strengths and capabilities to produce MP3 players (the iPod) and digital phones (the iPhone). In fact, Steve Jobs, Apple's co-founder and CEO, has been quoted as saying Apple is as proud of the things it doesn't make as the things it does. All of the company's products have fit within the scope of its unique strengths and capabilities.

LA Gear: How Straying from Its Core Strengths Nearly Cost a Firm Everything

For LA Gear, the late 1980s were golden. The company developed a core strength in designing and selling shoes with a distinctive "hip" Los

Angeles style, and the shoes were a hit. It produced a line of "Valley Girls" sneakers for teen girls and young women. The shoes were made of denim and patent leather and were adorned with feminine fringes. Then, in the mid-1980s, the company created children's shoes with small lights in the heels that blinked when the walker's soles hit the ground. The shoes, dubbed L.A. Lights, flew off the shelves. The company's sales increased from $11 million in 1985 to $820 million in 1990. The company became a Wall Street darling, and its share price increased from $3 per share in 1987 to $50 per share two years later. But just as quickly as LA Gear heated up, it turned cold. The company filed for Chapter 11 bankruptcy protection in January 1998. What went wrong? Three things—all related to growth.

First, instead of focusing its efforts on making its core products better, rapid growth was LA Gear's first priority. When its leaders found an opportunity to expand, they pursued the opportunity, regardless of the relationship of the opportunity to the company's core strengths and capabilities. Second, in its thirst for growth, LA Gear quickly moved beyond producing shoes for teen girls and young women and rolled out a full line of sneakers to appeal to a broad spectrum of customers. Without changing its brand, which most people still associated with girls, the company was now trying to be all things to all people. Quality and timeliness of delivery started to suffer. Finally, LA Gear found that a company that lives by the notion of "cool" can also die by the notion of "cool." By failing to change its image and develop additional core strengths before it branched out, the company produced products that just didn't sell. Most people still saw LA Gear as a company that was good at making feminine-looking shoes for young girls regardless of how many markets it entered. As a result, by 1991, LA Gear had 12 million shoes in its warehouses that nobody wanted. The company still exists today but has never fully recovered from these missteps.[5]

Planning For Growth

The third thing that a business owner can do to prepare for growth is to establish growth-related plans. This task involves a firm thinking ahead and anticipating the type and amount of growth it wants to achieve.

The process of writing a general business plan greatly assists in developing growth-related plans. A business plan normally includes a detailed forecast of a firm’s first three to five years of sales along with an operations plan that describes the resources the business will need to meet its projections. Even though the business will invariably change during its first three to five years, it’s still good to have a plan. Many businesses periodically revise their business plans and allow them to help guide their growth-related decisions.

It’s also important for a business to determine, as early as possible, the strategies for growth that it will try to employ. For example, Proactiv, the acne medicine company discussed in several chapters of this book, is a single-product company and has grown by steadily increasing its domestic sales, introducing its product into foreign markets, and by encouraging nontraditional users of acne medicine, like adult males, to use the product. Proactiv’s decision to stick with one product and to avoid growing through initiatives like acquisitions and licensing has allowed the company to focus on marketing and building its brand. Similarly, Cranium, the board game company discussed in Chapter 7, has grown rapidly but made the decision early on to avoid the temptation to simply take its flagship Cranium game and develop "age appropriate" versions of it. Instead, each of the 14 games the company has developed has been built from the ground up and has been extensively tested within their age groups. For example, Cadoo is a board game for kids seven years old and older. The game fits in a backpack and is designed for two players (instead of four, like the original Cranium) given that kids normally have only one friend over at a time.[6]

On a more personal level, a business owner should step back and measure the company’s growth plans against his or her personal goals and aspirations. The old adage, "Be careful what you wish for," is as true in business as it is in other areas of life. For example, if a business has the potential to grow rapidly, the owner should know what to expect if the fast-growth route is chosen. Fast-growth normally implies a quick pace of activity, a rapidly rising overhead, and a total commitment in terms of time and attention on the part of the business owners. The upside is that if the business is successful, the owner will normally do very well financially. The tradeoffs implied by this scenario are acceptable to some business owners and aren’t to others. If a person is starting a business to improve his or her quality of life, running a fast-growth firm might not be worth the sacrifices involved. A person in this situation might deliberately throttle back a business’s growth potential in exchange for more leisure time and a less stressful life.

Managing Growth

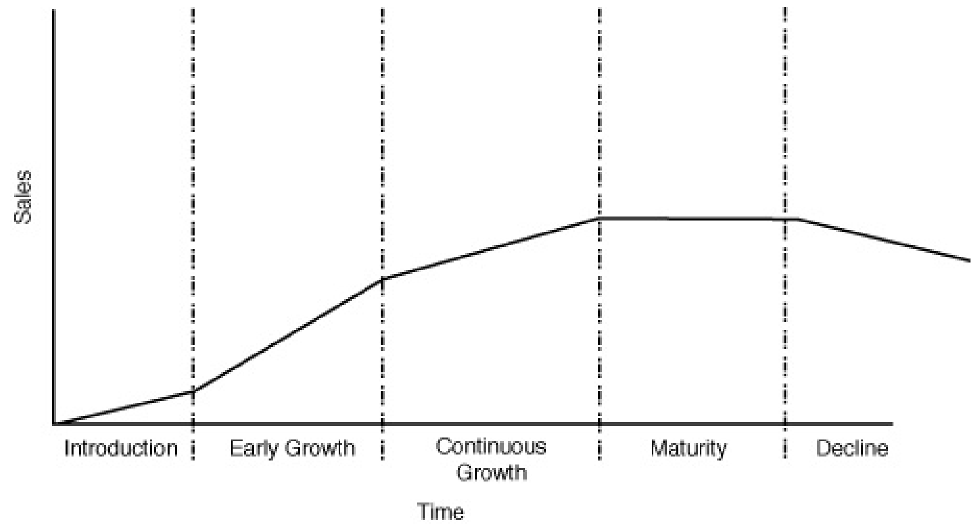
Many business owners are caught off guard by the challenges involved with growing their companies. One would think that if a business got off to a good start, steadily increased its sales, and started making money, things would get progressively easier for the business owner. In many instances, just the opposite occurs. As a business increases its sales, its pace of activity quickens, its resource needs increase, and the owner usually finds himself or herself busier than ever. Major challenges can also occur. For example, a business might project its next year's sales and realize it will need more people and additional equipment to handle the increased workload. The new equipment might need to be purchased and the new people hired and trained before the increased business generates additional income. It's easy to imagine a business owner tossing and turning in bed at night trying to figure out how that will all work out.

The reality is that a company must actively and carefully manage its growth for it to expand in a healthy and enjoyable manner. As a business grows and becomes better known, there are normally more opportunities that present themselves, but there are more things that can go wrong too. Many potential problems and heartaches can be avoided by prudently managing the growth process. This section focuses on two topics regarding how to manage growth: knowing and managing the stages and challenges of growth.

Knowing and Managing the Stages of Growth

The majority of businesses go through a discernable set of stages referred to as the *organizational life cycle*. The stages, pictured in Figure 9.1, include introduction, early growth, continuous growth, maturity, and decline. Each stage must be managed differently. It's important for business owners to be familiar with these stages, along with the unique opportunities and challenges that each stage entails. The introduction, early growth, and continuous growth stages are discussed in the following sections.[7]

Figure 9.1. *Stages of growth*



Introduction

This is the start-up phase where a business determines what its core strengths and capabilities are and starts selling its initial products or services. It's a very "hands-on" phase for the owner who is normally involved in every aspect of the day-to-day life of the business. The business is typically very nonbureaucratic with no (or few) written rules and procedures. The main goal of the business is to get off to a good start and to try to gain momentum in the marketplace.

The main challenges for a business in the introduction stage are to make sure the initial product or service is right and to start laying the groundwork for building a larger organization. It's important not to rush things. This sentiment is affirmed by April Singer, the founder of Rufus Shirts, a company that makes high-end shirts for men. Before growing her business beyond the introduction stage, Singer made sure that her unique approach for making men's shirts worked and that it resonated in the marketplace:

> *"Before growing too much too fast, I wanted to spend two seasons making sure that the concept worked, that I shipped well, and that consumers liked the product. They did."*[8]

This affirmation gave Singer the confidence to expand her business and move into a more aggressive growth mode. In regard to laying the groundwork to build a larger organization, many businesses use the introduction stage to try different concepts to see what works and what doesn't, recognizing that trial-and-error gets harder as a business grows. It's important to document what works and start thinking about how the company's success can be replicated when the owner isn't present or when the business expands beyond its original location. Betsy

Ludlow, the founder of Slim and Tone, a fitness center for women, documented nearly every move she made during the early days of her business. This practice paid off when Slim and Tone moved into its early growth phase and became a franchise organization. Reflecting on her experience, Ludlow recalls:

> *"I documented everything. When I bought something, I kept receipts. I made notes of every step I went through to open my first club. By the third club, I realized, hmmm...I have material to start putting together the training curriculum and operating manuals so that someone could do exactly what I just did. That's how I turned it into a franchise concept."*[9]

Early Growth

A business's early growth stage is normally characterized by increasing sales and heightened complexity. The business is normally still focused on its initial product or service but is trying to increase its market share and might have related products in the works. The initial formation of policies and procedures take place, and the process of running the business will start to consume more of the owner's time and attention.

For a business to be successful in this stage, two important things must take place. First, the owner of the business must start transitioning from his or her role as the hands-on supervisor of every aspect of the business to a more managerial role. As articulated by Michael E. Gerber in his excellent book *The E-Myth Revisited*, the owner must start working "on the business" rather than "in the business."[10] The basic idea is that early in the life of a business, the owner is typically directly involved in building the product or delivering the service that the business provides. As the business moves into the early growth stage, the owner must let go of that role and spend more time learning how to manage and build the business. If the owner isn't willing to make this transition or doesn't know that it needs to be made, the business will never grow beyond the owner's ability to directly supervise everything that takes place, and the business's growth will eventually stall. After all, even the most energetic people have limits on how much they can do.

The second thing that must take place for a business to be successful in the early growth stage is that increased formalization must take place. The business has to start developing policies and procedures that tell employees how to run it when the owner or other top managers aren't present. This is how a McDonald's restaurant runs so well when it's staffed by what appears to be a group of teenagers. The employees are simply following the policies and procedures that were originally written down by Ray Kroc, McDonald’s founder, and have been added to and improved upon over the years. An early growth stage business will not develop policies and procedures as elaborate as McDonald’s, but it must start formalizing how it achieves its success. This task was clearly on the mind of Emily Levy, the founder of EBL Coaching, a tutoring service for children who are struggling in school or trying to overcome disabilities, when she was asked by Ladies Who Launch early in the life of her business her growth plans:

> *"My future goals include continuing to spread EBL Coaching’s programs nationally, using our proprietary materials and self-contained multi-sensory methods. I have already developed a series of workbooks, called ’Strategies for Success,’ addressing specific study skills strategies, that are being used in a number of schools across the country. The real challenge will be figuring out how to replicate our programs while maintaining our high quality of teaching and personalized approach."*[11]

Levy was clearly trying to envision how her business would replicate its initial success in other locations. This is a task that all business owners need to do during the early stages of growth.

Continuous Growth Stage

As a business moves beyond its early growth stage and its pace of growth accelerates, the need for structure and formalization increases. The resource requirements of the business are usually a major concern, along with the ability of the owner and manager to take the firm to the next level. Often, the business will start developing new products and services and will expand to new markets. Smaller firms may be acquired, and the business might start partnering with other firms. When handled correctly, the business’s expansion will be in areas that are related to its core strengths and capabilities, or it will develop new strengths and capabilities to complement its activities.

The toughest decisions are typically made in the continuous growth stage. One tough decision is whether the owner of the business and the current management team have the experience and ability to take the firm any further. This scenario played out for Rachael Ashwell, the founder of Shabby Chic, a home furnishing business. Ashwell expanded her company to five separate locations, inked a licensing deal with Target, wrote five how-to books related to her business, and hosted her own television show on the Style Network before she concluded that her business had stalled. Her choice was to continue running the business or find more experienced management to grow it further.

She opted for the latter, and Shabby Chic is growing again.[12] Another decision that often is made is whether to continue to grow a business or sell it to a larger company. This is often a very personal and difficult decision for a business owner.

The importance of developing policies and procedures increases during the continuous growth stage. It’s also important for a business to develop a formal organizational structure and determine clear lines of delegation throughout the business. Although "formalization" is a term that is often frowned upon by business owners who want to free themselves from the trappings of Corporate America, well-developed policies and procedures lead to order, which typically makes the process of growing a business more organized, enjoyable, and successful.

Challenges of Growth

There is a consistent set of challenges that affects all stages of a firm’s growth. The challenges typically become more acute as a business grows, but a business’s owner and managers also become more savvy and experienced with the passage of time. The challenges illustrate that no firm grows in a competitive vacuum. As a business grows and takes market share away from rival firms, there will be a certain amount of retaliation that takes place. This is an aspect of competition that a business owner needs to be aware of and plan for. Competitive retaliation normally increases as a business grows and becomes a bigger threat to its rivals.

The following is a discussion of the four most common challenges of firm growth.

Cash Flow Management

As a firm grows, it normally requires an increasing amount of cash to service its customers. In addition, it must carefully manage its cash reserves to make sure it has enough money in the bank to meet its payroll and cover its short-term obligations. There are many colorful anecdotes about business owners who have had to rush to a bank and get a second mortgage on their houses to cover their business’s payroll. This set of events usually occurs when a business takes on too much work, and its customers are slow to pay. A business can literally have a million dollars in accounts receivable but not be able to meet a $25,000 payroll. This is why almost any book you pick up about growing a business stresses the importance of properly managing your cash flow.

Growth usually increases rather than decreases the challenges involved with cash flow management because an increase in sales means more money is flowing into and out of the business. Some businesses deal with potential cash flow shortfalls by establishing a line of credit at a bank or by raising investment capital. Other businesses deliberately restrict the pace of their growth to avoid cash flow challenges. The latter option is preferred by Dave Schwartz, the founder of Rent-A-Wreck, a discount car rental company, who grew his firm through earnings rather than debt or investment capital. Commenting on this issue, Schwartz said:

> *"One of the main things I tell people starting out is not to grow too quickly. Often it's better to grow slowly, and when you do expand, try to grow with cash flows [meaning grow with your own money]."*[13]

Price Stability

If a new business grows at the expense of a competitor's market share, price competition can set in. For example, if a new video store opens near a Blockbuster store, and the new store starts to erode Blockbuster's market share, Blockbuster will probably fight back by running promotions or lowering its price. This type of scenario places a new firm in a difficult predicament and illustrates why it's so important to start a business by selling a differentiated product in a niche market. There is no good way for a small firm to compete toe-to-toe against a much larger rival on price. The best thing for the small firm to do is avoid price competition by serving a different market and by serving that different market very well.

Quality Control

One of the most difficult challenges that businesses encounter as they grow is maintaining high levels of quality and customer service. As a firm grows, it handles more service requests and paperwork and contends with an increasing number of prospects, customers, vendors, and other stakeholders. If a business can't build its infrastructure fast enough to handle the increased activity, quality and customer service will usually suffer. What happens to many businesses is that they run into the classic chicken-and-egg quandary. It's hard to justify hiring additional employees or leasing more office space until the need is present, but if the business waits until the need is present, it usually won't have enough employees or office space to properly service new customers.

There is no easy way to resolve this type of quandary other than to recognize that it may take place and to plan for it the best you can. Many businesses find innovative and inexpensive ways to expand their capacity to try to avoid shortfalls in quality control or customer service. An example is an online merchant that utilizes drop-shipping rather than maintaining its own inventory as discussed in Chapter 8. Another example is a firm that utilizes temporary workers to plug resource gaps created by faster than expected growth.

Capital Constraints

Although many businesses are started fairly inexpensively, the need for capital is typically the most prevalent in the early growth and continuous growth stages of the organizational life cycle. The amount of capital required varies widely among businesses. Some businesses, like restaurant chains, might need considerable capital to hire employees, construct buildings, and purchase equipment. If they can't raise the capital they need, their growth will be stymied.

Most businesses, regardless of their industry, need capital from time to time to invest in growth-enabling projects. Their ability to raise capital, whether it's through internally generated funds, through a bank, or from investors, will determine in part whether their growth plans proceed.

Want to Minimize the Amount of Capital Needed to Grow? Follow the Lead of CD Baby and Act Like a Hedgehog

CD Baby, an online music store, has the largest catalog of music in the world, even though you've probably never heard of the majority of its musicians. Since its founding in 1997, CD Baby has maintained a laser-like focus on its primary mission—to provide a way for independent musicians to sell their music at a profit. The results have been impressive. Over 100,000 independent musicians now sell their music through the CD Baby Web site.

One thing that is extraordinary about CD Baby is that with the exception of partnering with Apple's iTunes and the other online music services, CD Baby has built its business without expanding beyond its core service. Although the company gets inquiries nearly every week about potential business opportunities, it has never bit on any of the offers. Derek Sivers, the company's founder and CEO, likes to use the fable of the Hedgehog and the Fox to explain why.

The tale of the "Hedgehog and the Fox" was written by Isaiah Berlin. Because he is sly, cunning, and strong, everyone thinks that the fox is better than the hedgehog. All the lowly hedgehog knows how to do is one thing—curl up in a ball, with its spikes out, to deter intruders. The ironic thing is that no matter what the fox does, and no matter how many of its 100 tricks it tries to use, the hedgehog always wins, because it knows how to do one thing particularly well—roll up in a ball and stick its spikes out. Sivers was reminded of this story while reading Jim Collin's book *Good to Great*. In *Good to Great*, Collins says businesses that are successful over the long-haul are like hedgehogs—they find their niche or market space and learn how to do one thing exceptionally well.

Sivers has taken Collin's advice to heart and has centered CD Baby's growth philosophy on one thing—being an online music store. The company is successful and continues to grow. An added benefit is that by focusing on one thing and executing it particularly well, Sivers has built his company less expensively than similarly sized companies that have more multifaceted product lines.[14]

Growth Strategies

The practical side of growth is the actual strategies that businesses employ to grow their companies. It's helpful for business owners to be acquainted with the breadth of growth-related strategies that are available, so they can select the strategy or strategies that make the most sense at a certain point in time in light of their individual situations.

This section discusses the most common strategies for growth utilized by expanding businesses. The strategies are divided into internal growth strategies and external growth strategies, as shown in Figure 9.2 and discussed here.

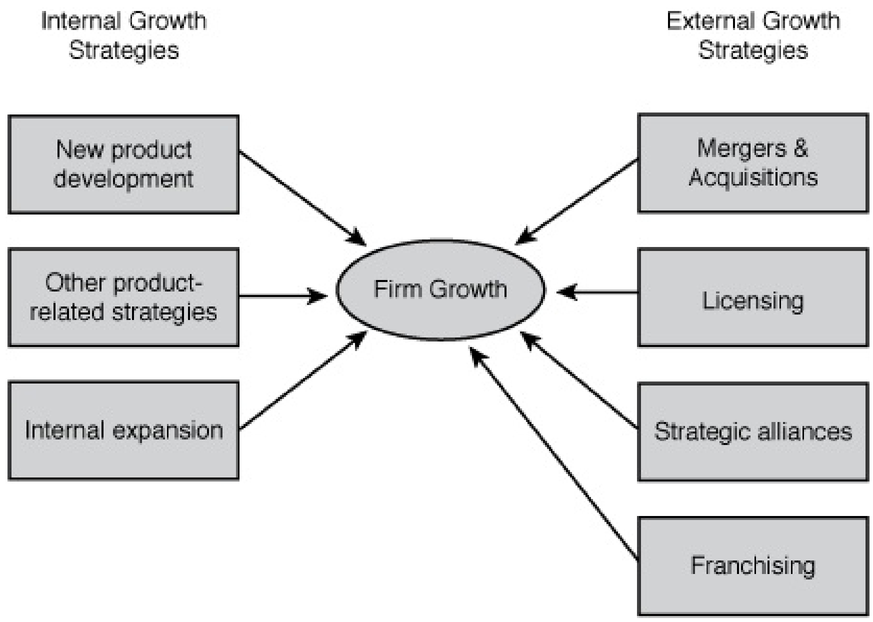


Figure 9.2. *Internal and external growth strategies*

Internal Growth Strategies

Internal growth strategies involve efforts taken within the firm itself, such as new product development, other product-related strategies, and international expansion. Almost all firms start by featuring internal growth, and many firms, such as Flavorx, Proactiv, and Daisy Rock Guitar, stick with this strategy as they grow. A firm that features internal growth relies on its own strengths and capabilities to spur its growth, rather than going into the marketplace and creating growth through an acquisition or a strategic alliance. The full range of internal growth strategies available to businesses is shown in Table 9.1.

Table 9.1. Internal Growth Strategies

Growth Strategy	Description
New product development	Involves designing, producing, and selling new products or services as a means of increasing firm revenues and profitability.
Improving an existing product or service	Often, a business can increase its revenue by improving an existing product or service—enhancing quality, making it larger or smaller, making it more convenient to use, improving its durability, or making it more up-to-date.
Increasing the market penetration of an existing product or service	A market penetration strategy involves actions taken to increase the sales of a product or service through greater marketing efforts or through increased production capacity and efficiency.
Extending product lines	A product line extension strategy involves making additional versions of a product so that it will appeal to different clientele or making related products to sell to the same clientele.
Geographic expansion	Many businesses grow by simply expanding from their original location to additional geographic sites.
International expansion	Growing a business by expanding its sales to international markets.

Many businesses prefer internal growth because it typically leads to an incremental, even-paced approach to growth. For example, a company like Shabby Chic, the home furnishing business introduced earlier, is growing by opening stores and selling its products through distributors. By growing in this manner, the company can control its pace of growth and time its store openings and new distribution agreements to coincide with the resources it has available. It's also easier for a business to control its culture by growing through internal means. If a company grows by adding employees as new products come online, it can socialize the employees into its culture. In contrast, if a firm grows via an external strategy, such as an acquisition, it will have employees who have been raised in different corporate cultures and will normally have a more difficult task creating cohesion among its employees.

The primary downside of internal growth is that it tends to be a slow form of business growth. While a slow, deliberate approach to growth has many advantages, in some industries, relying strictly on internal growth does not permit a firm to develop sufficient economies of scale or broaden its product offerings fast enough to remain competitive. An example is Google. Google has completed a number of acquisitions, like its recent acquisition of YouTube, to stay ahead of Yahoo! and Microsoft in online search, pay-per-click advertising, and related activities. Google's industry is moving too fast for it to develop all of its new products and services internally.

External Growth Strategies

External growth strategies rely on establishing relationships with other firms, such as mergers, acquisitions, strategic alliances, licensing agreements, and franchising. It is increasingly common for businesses to utilize one or more external growth strategies as early as the early growth stage of its organizational life cycle. The full range of external growth strategies available to businesses is shown in Table 9.2.

Table 9.2. External Growth Strategies

Growth Strategy	Description
Merger	A merger is the pooling of interests to combine two or more firms into one.
Acquisition	An acquisition is the outright purchase of one firm by another.
Licensing	Licensing is the granting of permission by one company to another company to use a specific form of its intellectual property in exchange for a flat fee or royalty payments.
Strategic alliance	A strategic alliance is a partnership between two or more firms that is developed to achieve a specific goal.
Franchising	Franchising is a form of business organization in which a firm that already has a successful product or service (franchisor) licenses its trademark and method of doing business to other businesses (franchisees) in exchange for an initial franchise fee and an ongoing royalty.

A business can normally grow faster through external growth than internal growth because it immediately adds a product or capability that might have taken months or years to develop internally. For example, when eBay acquired PayPal, it acquired PayPal's proprietary electronic payments system, something PayPal worked diligently to perfect over a period of several years. Similarly, by forming a strategic alliance, a firm can tap into the resources of its alliance partner and reach new markets without having to build out its own infrastructure.

For example, many American food companies have strategic alliances with large European food companies, like Nestlé, to gain access to their European distribution networks.

The primary downside of external growth is that by relying on other firms to help develop its growth, a business losses some of its flexibility and decision autonomy. It also complicates its business and runs the risk of joining forces with an unreliable partner. The net result of engaging in external growth is usually to speed up a business's pace of growth. As a business's pace of growth increases, the challenges of growth, such as cash flow management, quality control, and capital constraints, are usually exacerbated.

Many businesses blend internal and external strategies for growth as they pass through the stages of growth and expand their businesses. The important thing to remember as a business owner is that you should select the means of growth that is best for you and your company, given the conditions you face.

Summary

There is no topic more deserving of study on the part of a business owner than how to successfully grow a firm. It is not uncommon for a business to start successfully, provide an initial period of satisfaction and joy for its owners, and then turn sour as the owner struggles with the pressures and challenges imposed by growth. The good news is that it doesn't have to turn out that way for you. If you start a business and decide to grow it beyond the scope of a small firm, reread this chapter periodically and seek out mentors and other forms of assistance and advice. Businesses can be grown successfully, but it does take perseverance, hard work, and a willingness to make tough choices.

As you glance down and realize that this is the final paragraph of this book, we'd like to leave you with one final piece of advice. There are some books that will tell you that starting a business is the smartest thing you can do—regardless of your alternatives. We hope we haven't conveyed that message. Starting a business is the right thing for some people, and it's the wrong thing for others. What we do believe, however, is that you shouldn't let the myths discussed in this book make your mind up for you. Our guess is that if you picked up this book and spent the time to read it, you're a capable, passionate, and responsible person. If starting a business is the right decision for you, you can do it!

Endnotes

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