STRATEGY

Choosing a Strategy for Your Startup

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Joshua Gans, a professor at the University of Toronto's Rotman School of Management, advises against trying to commercialize a new technology or product before considering all the strategic options. He talks through some questions entrepreneurs should ask themselves — like, collaborate or compete? — and outlines a framework he and his fellow researchers have found to work best for startups. Gans is the coauthor of the article "Do Entrepreneurs Need a Strategy?"

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SARAH GREEN CARMICHAEL: Welcome to the HBR IdeaCast, from Harvard Business Review. I'm Sarah Green Carmichael.

So, you've quit your job because you have such a fantastic start-up idea. You're really confident in what you've invented. And now you just have to figure out a strategy for how to make money. It's easy to assume you'll be disrupting everything. Because that's what people do nowadays, right? They disrupt.

Well, actually, our guest today says if that's your assumption, you're selling yourself short.

JOSHUA GANS: For any given idea, there are a myriad of strategies that can be pursued. And it's very hard to determine which one is the best strategy right at the outset.

SARAH GREEN CARMICHAEL: That's our guest, Joshua Gans. He got together with a few other researchers to develop a framework that would help start-up founders make sense of all their options.

He's here to explain what those options are and how to pick one.

Joshua is a professor at the University of Toronto's Rotman School of Management. And he's the co-author of the HBR article "Do Entrepreneurs Need a Strategy?"

SARAH GREEN CARMICHAEL: Well, Joshua, thank you so much for making some time for us today.

JOSHUA GANS: Happy to be here.

SARAH GREEN CARMICHAEL: What is it that you see entrepreneurs most often getting wrong when they're in this process of trying to choose a business strategy and just trying to get their business off the ground?

JOSHUA GANS: There are two errors that get made. One error is the sort of search for the one true strategy that will fit everything. And there is no one's true strategy because your idea's different from other people's ideas. There's a lot of uncertainty regarding the consequences of the choices you might make. And similarly, the other error is well, OK, it's so uncertain, I shouldn't do anything — whatever comes first to mind, off we go; I'll just leap right into it. So, you can see the problems of both of those approaches. One approach leads you to perhaps a fruitless and too long search. The other approach leads you to leap in without fully thinking about what options that might cut off.

And what we suggest in the interim is, OK, we don't want you to plan forever. What we want you to do is we want you to consider some options in a systematic way. And then basically you're gonna come down to one, two, maybe more, and then you just choose. In other words, you earn the right to do that. By doing a little bit of work, you earn the right to then choose and perhaps even go with your gut, but at least you could discard bad options, and you can discard options that are going to really cut you off from doing other things in the future.

SARAH GREEN CARMICHAEL: Why is that kind of rapid experimentation, just sort of trying stuff, what's the problem with that?

JOSHUA GANS: Well, it does have a merit to it. No one's going to be against experimentation and learning about the market. It's just in some situations, that can really distract you and take you off on the wrong path. You know, one obvious way in which that is a real problem is, in order to do this experimentation with the market, you have to put products out there in the market. Well, people can see that. So, if it turns out later on that you discover you've got a whole lot of imitators and a whole lot of people ripping off your ideas or incumbents breathing down your neck with their own copycat ideas to yours, it's too late to sort of go back. You've already let the cat out of the bag. Had you forecast that situation and realized that perhaps your idea and your products were easy to replicate, you may well have chosen another strategy that gave you more control. And this might be a strategy that could involve some intellectual property protection, could involve some secrecy, could involve launching in a very limited domain that doesn't attract the attention of incumbents. Don't cut off those options. And that's the kind of thing that we want people to think about before they act rather than regret it later on.

SARAH GREEN CARMICHAEL: So, one of the first decisions you say that startups need to make is whether they will be collaborating or competing. What are the pros and cons of going in either direction?

JOSHUA GANS: By collaboration, we mean you're entering the market, and you're trying to come up with deals that effectively treat existing businesses in that market as your customer. The pro of that is, of course, you're not competing with them. Competition tends to make it harder to make profits, for instance, and that's true for you and also for the people you're dealing with. And secondly, often the established firms in these industries have a whole lot of assets, market position, expertise and other things that you can tap into. So, collaborating can be, for some startups, a very quick way of being able to get a foot in the market. The downside of it is, of course, you are then tied and potentially beholden to the people you were dealing with. In other words, you're not the master of your own domain.

If, on the other hand, you compete, you don't have to do that. You don't have to ask permission. You can go and choose your technology that may be slightly different from the standards that the incumbents have had. You can follow a vision that might be very different than the incumbents' vision for the entire value being brought to consumers. You can make those choices. And that is obviously attractive to many entrepreneurs and is also very attractive because you don't have to go find those right partners in the first place. You can just get down to business and start making a product.

SARAH GREEN CARMICHAEL: So, maybe give us an example of a startup that successfully went with the collaboration route.

JOSHUA GANS: Well, there are quite a few of them. Some startups, you know, going back a while, Dolby. Dolby was the system of being able to reduce the amount of noise in recorded music, in particular, recorded sounds in general. And what they did was that they took their intellectual property. They could have, if they wanted to, built the next big hi-fi company and had it just say, our products have better sound and beaten Sony and whomever. But they didn't. Instead, what they did is they licensed their algorithms that technology, etcetera, on very good terms, too all those incumbents in the industry and made Dolby a standard throughout the industry. So, they didn't have to go through this rigmarole of building out, downstream manufacturing, or anything like that. They could then come back, and they could focus on their IP, and that's how they ran their business. In other words, it's the ultimate cooperation strategy. They could've competed, but they chose not to, and they did very well for now decades.

SARAH GREEN CARMICHAEL: So, how does Dolby fit into the other sort of strategic choice you talk about in the article, which is whether to storm a hill or build a moat?

JOSHUA GANS: Well, the way we think about that — and it's a colorful metaphor we put in there for the article — but our two real choices are, do you try to control the future, or do you execute so that you just have a better product overall now and in the future? And those are really choices. You know, often you go to business schools, and everybody's talking about building a moat. Where's your moat? Where, when you do all this hard work, are you going to be able to in the future rest on your laurels and not have people come and take it away? You know, that sounds very attractive. But the

alternative is not to worry about any of that and just try to develop capabilities and run ahead of the competition all the time. And there's some merit to that.
So, what Dolby chose to do was incredible control. They had patents. They had deals that required a little Dolby switch to be put on the front of any manufacturing things so that, you know, consumers could switch it on and off and see exactly what Dolby was adding to it and that they would want an appliance with Dolby in it. And so, they kept very tight control over that. So, effectively, what Dolby was saying is, we've built this stuff. You pay us money in perpetuity, and we don't have to worry about any competition. We can go back to inventing new stuff instead of doing that.
One can imagine that other companies do very different things in that regard. One of the criticisms of Apple is that it comes up with products, and it always has to keep on innovating in order to continue to keep its market position. Well, that's what we mean by storming the hill. And let's face it, Apple have been quite successful at that strategy. There's no reason why you can't choose one or the other.
There are some tradeoffs, however. When you choose to control, it takes a lot of time to establish control. You've got to be secret for a time. You can't get to market as quickly. You've got to plan it all out. You're going to invest in lawyers and other things like that to help you along. But if you're focusing on execution, well, you can run to market right away. You want to get to market early so you can get the signals before everyone else so you can build the better products. So, you wanna have more hustle.

SARAH GREEN CARMICHAEL: But you also talk about a value chain strategy. Maybe just tell us a little bit about what that is and kind of the pros and cons to that approach.

JOSHUA GANS: So, value chain strategy is a situation where you choose to orient yourself towards execution, that is, trying to keep ahead and stay ahead of your competitors, but you think of your customer as being other firms within the same value chain that you're in. The greatest example of this is of course, Foxconn, that make iPhones. They make devices for Samsung and all of that. They have no products of their own, no brand of their own. They make products for other people. And they've got very, very good at doing that and doing it at scale and being able to be flexible for product design changes, all the other things that go with that. That's quintessential value chain strategy.

SARAH GREEN CARMICHAEL: Is it wrong to say it was a little bit less sexy than some of the other strategies out there?

JOSHUA GANS: Oh, well no, that's not wrong at all. We had enough trouble coming out with the name "value chain strategy" because let me tell you, we tried to sex that up, and we really couldn't find anything. And look, when it comes down to it, yes, it's not the same. No one's writing books about this stuff. However, in our experience, it is one of the best ways to go initially, and here's why: it is often the case that entrepreneurs have some experience in an industry, they have some context in an industry, and then they have a good idea. They don't want to spend the resources to try and work out how to control that idea, and they're not interested in sort of just selling IP.

And so, when they go through this exercise of thinking through these different strategies, we found so often that the first strategy they liked to pursue, the path of least resistance, is in fact the value chain strategy. Now, they have to think through that. They have to think through whether their product is going to be good enough that they won't be squeezed by their own customers and things like that. There are lots of things to worry about, but as a path of least resistance to enter quickly and to leverage on some very important skills, it's surprising how often, despite the name, entrepreneurs come up to us and say, yep, we're gonna do value chain.

SARAH GREEN CARMICHAEL: Now, we've spent most of our time today talking about the intellectual property strategy, the disruption strategy, and the value chain strategy. But of course, there is a fourth strategy, which is the architectural strategy. I don't want to sort of let you go without asking you about that one. So, maybe first just briefly describe what that one is.

JOSHUA GANS: It's a strategy where you're trying to get control, trying to build a moat. You're either competing head-to-head with existing incumbents, or sometimes you'll end up with that strategy building out something completely new. The problem with that is it's really, really hard. When you conceive of something that might architect a whole industry, I mean, you're basically saying, I want to pursue this strategy that's going to make me the god of this industry, OK? Now, there's a bit of hubris involved in that, but let's put it simply: when you think about all the things you have to do to achieve that, it's going to be a very, very long list. It's going to potentially take a very long time. So, it's a really, really ambitious strategy.

Now, obviously, risk versus reward, there may be, it may well be worth pursuing that. Maybe that's the sort of person you are. And there are examples of companies that have pursued that successfully. Obviously, the most quintessential one in recent memory is Facebook.

SARAH GREEN CARMICHAEL: What if, in thinking about these different options, you're deciding which one to pursue, and you think, well, there's only really one here that works for me. Is that reassuring? Should you feel like, aha, this is good, my idea, so clear it fits into one specific thing? Is there maybe a downside to only having one option?

JOSHUA GANS: So, I think if you came through that exercise and had only one option, you should start to have some self-doubt. You may overcome it, but you might have some doubt with this is the right idea. And the reason is, if you come down to one option, what that's telling you is your idea is so on tender hooks that if you don't pursue this one thing and you slightly misstep, it's all going to fall over. That sounds like a lot of risk, and there's already a lot of risk in this.

SARAH GREEN CARMICHAEL: So, if you have a couple of options, how do you choose which one is best?

JOSHUA GANS: Well, we don't have any science on that. One of the things we want to emphasize is that choice is choice. So, what we say is basically when you've done this process and you've got one or two, you know, got two or more options sitting there before you, you then go with your gut essentially, or you come up with a rationale saying why you are the right person; you feel better with one path and another. It may be what your team is capable of. And those are the things that end up driving which way you're going to go, uh, but you know, you've at least had the assurance that you've got there and you've got a few options and that you've actually made a choice and considered those alternatives.

SARAH GREEN CARMICHAEL: Well, and if you choose one option that in the end starts to feel a little bit like, whoops, that was the wrong thing, how hard is it to switch to a different one?

JOSHUA GANS: Well, how hard is it to switch? It really depends on the option you choose. You might have two options sitting before you, and you know if you choose one, that's it: you're either doing that. Whereas the other one, you know, if it doesn't work out, I can switch to plan b. And obviously, all things being equal, it might be better to do the one which gives you the option of switching later on. So, that's another criteria, and you won't know if that's the case for sure ever, but you'll be able to think through whether you're going to be constraining your ability to switch.
We think that these approaches are very useful for thinking and thinking through what strategies to pursue. but we're not so dogmatic to say, this is it; these are the only ones. This covers a lot of the space. It covers some of the main choices, but sometimes it's not necessarily going to be easy to box a particular strategy, especially by successful company into one of these four boxes; and moreover, as companies grow, they tend to do more stuff and so it gets blurrier and blurrier. We ourselves, the authors, have argued over whether Tesla, is it disruptive, is it, is it trying to build out a new architecture for cars and things like that; and truth be told, there's some elements of both in that. What Tesla has that other companies don't have is they have a master plan. Elon Musk actually points out exactly what his strategy was going to be in pursuing this. He thought through it, thought through all the options, and then went and implemented that. He wasn't doing it as, here's the first thing to come along. He was doing it as a deliberate choice.

SARAH GREEN CARMICHAEL: Mhm. And does it matter if your ultimate goal is a successful IPO or you want to be acquired? Do you kind of have to have the end game in mind when you're making that choice?

JOSHUA GANS: Partly you do and partly you don't. That's a very different set of decisions of how you think about having a successful exit. It is true that if you tend to align yourself with the incumbents, being acquired by them is going to be much easier. Then again, sometimes when you're a big annoyance to the incumbents, you're a strong competitor to them, when it comes down to thinking about an exit, they may actually want to purchase you just to, well, just to, to soften the blow for themselves or to keep control. We can argue about whether that's good for society, but for the entrepreneurs involved it may be very lucrative.

And in fact, I did a study a few years ago in the speech recognition industry that showed that actually startups that were pursuing the most disruptive technologies tend to, to compete first and then a pivot to cooperation later, whether it be by acquisition or some licensing deal. And the best reason for that is because seeing them as competitors, seeing them be successful in the market, gave the incumbents some assurance that what they were purchasing was real.

SARAH GREEN CARMICHAEL: Well, Joshua, just out of curiosity, if you were going to start a company, which of these strategies would you choose?

JOSHUA GANS: Oh, well, I already started a company the other week. I was doing some work with a Canadian company that allows entrepreneurs to quickly establish an online business. And because I was doing that, I was curious and I, I actually in a day managed to design and launch my own tee shirt business. Now, I won't call it disruptive, because I'm not sure who I'm disrupting. I won't call it architecture because I have no desire to do the work involved. There's definitely no IP involved. And I'm not dealing with an end customer, so it's no value chain. So, the answer is what happens when the professor does his own medicine? Apparently, he follows none of the rules. But I'll tell you, I'll tell you one thing I've learned from that is it's very hard to earn money.
I've currently had zero sales. Now, the reason it's had no sales is I was interested in how hard it was — how easy it was to start a business. It's easy. You can start a business. But had a make a business, how to grow a business, how to do anything real, that's a lot more work. And I wasn't, you know, clearly I wasn't in that, that bucket. And one of the things is if I was prepared to do that work, I should also be prepared to think about, what am I trying to achieve here? What is my strategy going to be? I shouldn't just leap into it this way and hope that all of a sudden the money might flow in, although to be sure, I kind of was curious to see if that would occur. It didn't. But, you know, you would actually plan it out. You think about your brand, you're thinking about your product line, and all that sort of stuff. That's the message of our article.

SARAH GREEN CARMICHAEL: There you go. Well, Joshua, this has been tremendously fun talking with you today, and I really appreciate it.

JOSHUA GANS: It's been fun for me, too. Thank you.

SARAH GREEN CARMICHAEL: That's Joshua Gans. He's a professor at the University of Toronto's Rotman School of Management. He's the co-author of the article "Do Entrepreneurs Need a Strategy?" Read it in the May–June 2018 issue of Harvard Business Review, or on HBR.org.

Our show's produced by Curt Nickisch and Amanda Kersey. Adam Buchholz is our audio product manager. And we get production help from Rob Eckhardt.

Thanks for listening to the HBR IdeaCast. I'm Sarah Green Carmichael.

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