Chapter 3

Pathways to entrepreneurial ventures

Learning objectives

- Creating New Ventures.
- Acquiring an Established Entrepreneurial Venture.
- Franchising: The Hybrid.

1. Creating New Ventures

Creating New Ventures

- The most effective way to start a new business is to create a new and unique product or service.
- The next-best way is to adapt an existing product or service or to extend an offering into an area wherein it is not presently available.
- The first approach is often referred to as ***new-new***; the second, as ***new-old***.

New-New Approach to Creating New Ventures

- Trends in Creating Business Opportunities
  - The new-new approach indicates the importance of people's awareness of their daily lives (work and free time) for developing new business ideas.

Emerging Opportunities
Green Products
Organic foods
Organic fibers/textiles
Alternative Energy
Solar
Biofuel
Fuel cells
Energy conservation
Health Care
Healthy food
School and govt-sponsored programs
Exercise
Yoga
Niche gyms
Children
Nonmedical
Pre-assisted living
Assisted living transition services

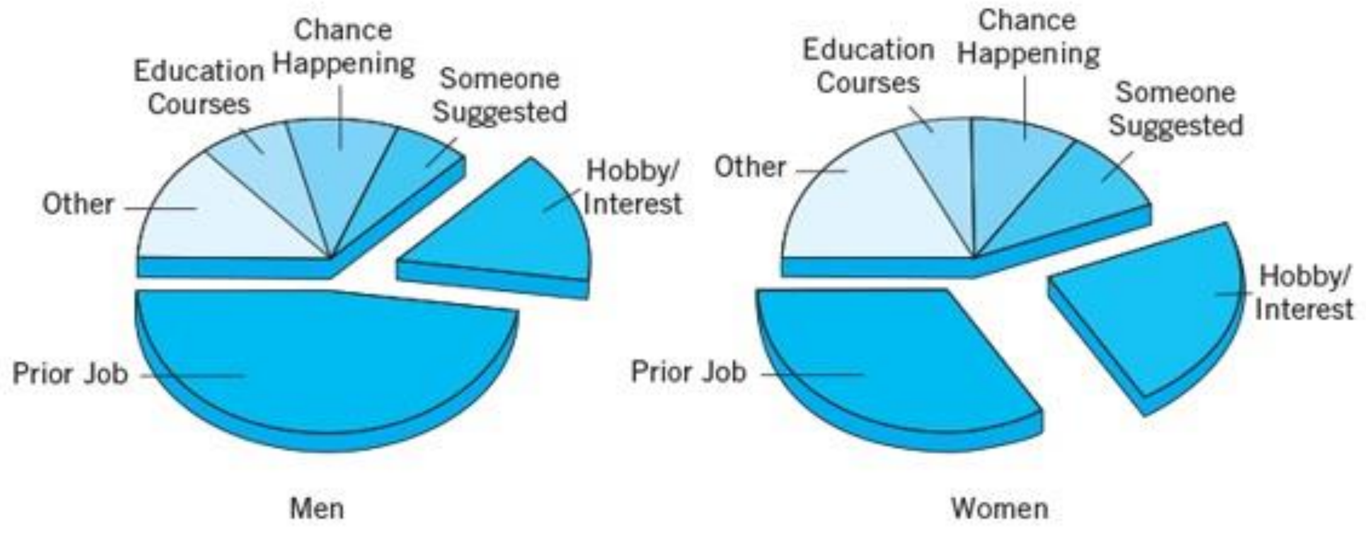
Emerging Opportunities
Niche Consumables
Wine
Chocolate
Burgers
Coffeehouses
Exotic salads
Home Automation and Media Storage
Lighting control
Security systems
Energy management
Comfort management
Entertainment systems
Networked kitchen appliances

Emerging Internet Opportunities
Mobile Advertising
Cell phones
PDAs
Concierge Services
Niche Social Networks
Seniors
Music fans
Groups of local users
Pet owners
Dating groups
Virtual Economies
"Online auctions"
Educational Tutoring
Human Resources Services
"Matchmaking"
"Virtual HR"
"Online Staffing"
Nanotechnology
Wireless Technology

New-New Approach to Creating New Ventures (Cont.)

- Trends in Creating Business Opportunities
  - ❖ Most business ideas tend to come from people’s experiences.

Figure 7.1 Sources of New Business Ideas among Men and Women



Source: William J. Dennis, *A Small Business Primer* (Washington, D.C.: National Federation of Independent Business, 1993), 27.

  - ❖ Main sources for both men and women are prior jobs, hobbies or interests, and personally identified problems.

New-Old Approach to Creating New Ventures

- Most small ventures do not start with a totally unique idea. Instead, an individual “piggybacks” on someone else’s idea by either improving a product or offering a service in an unavailable area, hence the term new-old approach.
  - ❖ Examples are restaurants, clothing stores, or similar outlets in suburban areas that do not have an abundance of these stores.
  - ❖ These kinds of operations can be risky because competitors can move in easily.
  - ❖ Potential owners considering this kind of enterprise should try to offer a product or service that is difficult to copy.

Examining the Financial Picture When Creating New Ventures

- Prospective Entrepreneurs of new ventures must evaluate an enterprise's financial picture.
  - ❖ How much will it cost to stay in business for the first year?
  - ❖ How much revenue will the firm generate during this time period?
  - ❖ If the outflow of cash is greater than the inflow, how long will it take before the business turns the corner?
  - ❖ Etc.

Examining the Financial Picture When Creating New Ventures (Cont.)

Monthly	Expenses	Cash Needed to Start The Business	What to Put in Column 2
Item	Estimate based on sales of $___ per year	(see Column 3)	(These figures are estimates. The owner/manager decides how many months to allow, depending on the type of business)
	Column 1	Column 2	Column 3
Salary of owner/manager	$	$	3 times Column 1
Other salaries and wages			3 times Column 1
Rent			3 times Column 1
Advertising			3 times Column 1
Delivery expense			3 times Column 1
Supplies			3 times Column 1
Telephone and telegraph			3 times Column 1
Other utilities			3 times Column 1
Insurance			6 times Column 1
Taxes, Social Security			4 times Column 1
Interest			3 times Column 1
Maintenance			3 times Column 1
Legal and other professional assistance			3 times Column 1
Miscellaneous			3 times Column 1

Start-Up Costs		
Item	**Estimate**	**To Arrive at Esttimate**
Fixtures and equipment	**$**	Determine what is typical for this kind of business; talk to suppliers.
Decorating and remodeling		Talk to a contractor.
Installation of fixtures, equipment	**t**	Talk to suppliers.
Starting inventory		Talk to suppliers.
Deposits with public utilities		Talk to utility companies.
Legal and other professional fees		Talk to a lawyer, accountant, or other professional.
Licenses and permits		Contact appropriate city offices.
Advertising and promotion		Decide what will be used; talk to media.
Accounts receivable		Estimate how much will be tied up in receivables by credit customers and for how long.
Cash		Allow for unexpected expenses and losses, special purchases, and other expenditures.
Other Expenses		List them and estimate costs.
TOTAL CASH NEEDED TO START	**$**______	Add all estimated amounts.

2. Acquiring an Established Entrepreneurial Venture

Acquiring an Established Entrepreneurial Venture

- A prospective entrepreneur may seek to purchase a business venture rather than start an enterprise. This can be a successful method of getting into business, but numerous factors need to be analyzed.
  - ❖ Personal Preferences.
  - ❖ Examination of Opportunities.
  - ❖ Advantages of Acquiring an Ongoing Venture.
  - ❖ Evaluation of the Selected Venture.
  - ❖ Key Questions to Ask.
  - ❖ Negotiating the Deal.

Personal Preferences

- Entrepreneurs need to recognize certain personal factors and limit their choices of ventures accordingly.
  - ❖ Entrepreneur’s background, skills, interests, and experience are all important factors in selecting the type of business to buy.
  - ❖ Personal preferences for the location and size of a business should guide the selection process.
  - ❖ If an entrepreneur has always desired to own a business in the South or West, then that is exactly where the search should begin.
  - ❖ Etc.

Examination of Opportunities

- Entrepreneurs in search of a possible venture to buy need to examine the available opportunities through various sources:
  - ❖ Business brokers.
  - ❖ Newspaper ads.
  - ❖ Trade sources.
  - ❖ Professional sources.

Advantages of Acquiring an Ongoing Venture

- Of the numerous advantages to buying an ongoing venture, three of the most important are as follows:
  - ❖ Because the enterprise is already in operation, its successful future operation is likely.
  - ❖ The time and effort associated with starting a new enterprise are eliminated.
  - ❖ It sometimes is possible to buy an ongoing business at a bargain price.
- Each benefit of these three advantages includes:
  - ❖ Less fear about successful future operations.
  - ❖ Reduced time and effort.
  - ❖ A good price.

Evaluation of the Selected Venture

- The business environment.
- Profits, sales, and operating ratios.
- The business assets.
  - The tangible (physical) and intangible (e.g., reputation) assets of the business need to be assessed. The following assets should be examined:
    - Inventory (age, quality, salability, condition).
    - Furniture, equipment, fixtures (value, condition, leased or owned).
    - Accounts receivable (age of outstanding debts, past collection periods, credit standing of customers).
    - Trademarks, patents, copyrights, business name (value, role in the business’s success, degree of competitive edge)
    - Goodwill (reputation, established clientele, trusted name).

Key Questions to Ask

- Why Is the Business Being Sold?
- What Is the Current Physical Condition of the Business?
- What Is the Condition of the Inventory?
- What Is the State of the Company's Other Assets?
- How Many of the Employees Will Remain?
- What Type of Competition Does the Business Face?
- What Does the Firm's Financial Picture Look Like?

Negotiating the Deal

- The potential buyer must negotiate the final deal. This negotiation process, however, involves a number of factors.
- Four critical elements should be recognized:
  - ❖ Information.
  - ❖ Time.
  - ❖ Pressure.
  - ❖ Alternatives.

Negotiating the Deal (Cont.)

- Additional considerations that a person should keep in mind when purchasing a business include the following:

1. Request that the seller retain a minority interest in the business or establish the final purchase price dependent on the performance of the business over a three-to-five-year span, to keep the seller concerned about the immediate future performance of the business.
2. Buyers should be careful of any promises made without written corroboration.

Negotiating the Deal (Cont.)

- Additional considerations that a person should keep in mind when purchasing a business include the following:

3. Spend time with the seller's books, reconstructing financial statements to determine how much cash is actually available, is an absolute.
4. Investigations should be thorough and wide-ranging, encompassing interviews not only with the owner but with vendors, competitors, customers, and employees as well.

3. Franchising: The Hybrid

Franchising: The Hybrid

- One form of business that incorporates some of the independence of an entrepreneur with the larger umbrella of a corporation is the franchise. Thus, it is a “hybrid” form of entering business.
- A franchise is any arrangement in which the owner of a trademark, trade name, or copyright has licensed others to use it in selling goods or services.
- A franchisee (a purchaser of a franchise) is generally legally independent but economically dependent on the integrated business system of the franchisor (the seller of the franchise).

Franchising: The Hybrid (Cont.)

- Some factors to consider for franchising are as follows:
  - ❖ How Franchising Works.
  - ❖ Advantages of Franchising.
  - ❖ Disadvantages of Franchising.
  - ❖ Franchise Law.
  - ❖ Evaluating Franchising Opportunities.

How Franchising Works

- Business franchise systems for goods and services generally work the same way.
- The franchisee, an independent businessperson, contracts for a complete business package based on carrying on the following terms.

1. Make a financial investment in the operation.
2. Obtain and maintain a standardized inventory and/or equipment package usually purchased from the franchisor.
3. Maintain a specified quality of performance.
4. Follow a franchise fee as well as a percentage of the gross revenues.
5. Engage in a continuing business relationship.

How Franchising Works (Cont.)

- A franchisor provides the following types of benefits and assistance.

1. The company name.
2. Identifying symbols, logos, designs, and facilities.
3. Professional management training for each independent unit's staff.
4. Sale of specific merchandise necessary for the unit's operation at wholesale prices.
5. Financial assistance, if needed, to help the unit in any way possible.
6. Continuing aid and guidance to ensure that everything is done in accordance with the contract.

Advantages of Franchising

- A number of advantages are associated with franchising. There are four of the most well-known advantages.
    - ❖ Training and guidance.
    - ❖ Brand-name appeal.
    - ❖ A proven track record.
    - ❖ Financial assistance.

Disadvantages of Franchising

- The prospective franchisee must weigh the advantages of franchising against the accompanying disadvantages.
- Some of the most important drawbacks are franchise fees, the control exercised by the franchisor, and unfulfilled promises by some franchisors.
    - ❖ Franchise Fees.
    - ❖ Franchisor Control.
    - ❖ Unfulfilled Promises.

Disadvantages of Franchising (Cont.)

- The Cost of Franchising
  - ❖ Don’t let the advantages of franchising cloud the significant costs involved. Although the franchise fee may be $75,000, the actual cost of “opening your doors for business” can be more than $200,000! Depending on the type of franchise, the following expenditures are possible:

    1. ***The basic franchising fee***. For this, you may receive a wide range of services: personnel training, licenses, operations manuals, training materials, site selection and location preparation assistance, and more. Or you may receive none of these.
    2. ***Insurance***. You will need coverage for a variety of items, such as plate glass, office contents, vehicles, and others. You also should obtain so-called “umbrella” insurance. It is inexpensive and is meant to help out in the event of crippling million- or multimillion-dollar lawsuits.
    3. ***Opening product inventory***. If initial inventory is not included in your franchise fee, you will have to obtain enough to open your franchise.

Disadvantages of Franchising (Cont.)

- The Cost of Franchising
  - ❖ Don't let the advantages of franchising cloud the significant costs involved. Although the franchise fee may be $75,000, the actual cost of "opening your doors for business" can be more than $200,000! Depending on the type of franchise, the following expenditures are possible:

4. ***Remodeling and leasehold improvements***. Under most commercial leases, you are responsible for these costs.
5. ***Utility charges***. Deposits to cover the first month or two are usually required for electricity, gas, oil, telephone, and water.
6. ***Payroll***. This should include the costs of training employees before the store opens. You should include a reasonable salary for yourself.
7. ***Debt service***. This includes principal and interest payments.
8. ***Bookkeeping and accounting fees***. In addition to the services the franchisor may supply in this area, it is always wise to use your own accountant.

Disadvantages of Franchising (Cont.)

- The Cost of Franchising
  - ❖ Don’t let the advantages of franchising cloud the significant costs involved. Although the franchise fee may be $75,000, the actual cost of “opening your doors for business” can be more than $200,000! Depending on the type of franchise, the following expenditures are possible:

9. ***Legal and professional fees***. The cost of hiring an attorney to review the franchise contract, to file for and obtain any necessary zoning or planning ordinances, and to handle any unforeseen conflicts must be factored into your opening costs projections.
10. ***State and local licenses, permits, and certificates***. These run the gamut from liquor licenses to building permits for renovations.

Franchise Law

- The growth in franchise operations has outdistanced laws about franchising.

- Much franchise litigation has arisen over termination provisions. The franchise agreement is normally a form of contract the franchisor draws and prepares, and because the bargaining power of the franchisee is rarely equal to that of the franchisor, the termination provisions of contracts are generally more favorable to the franchisor.

- Franchisee invests a substantial amount of time and money in the franchise operation to make it successful and may receive little or nothing for the business upon termination. The franchisor owns the trademark and hence the business.

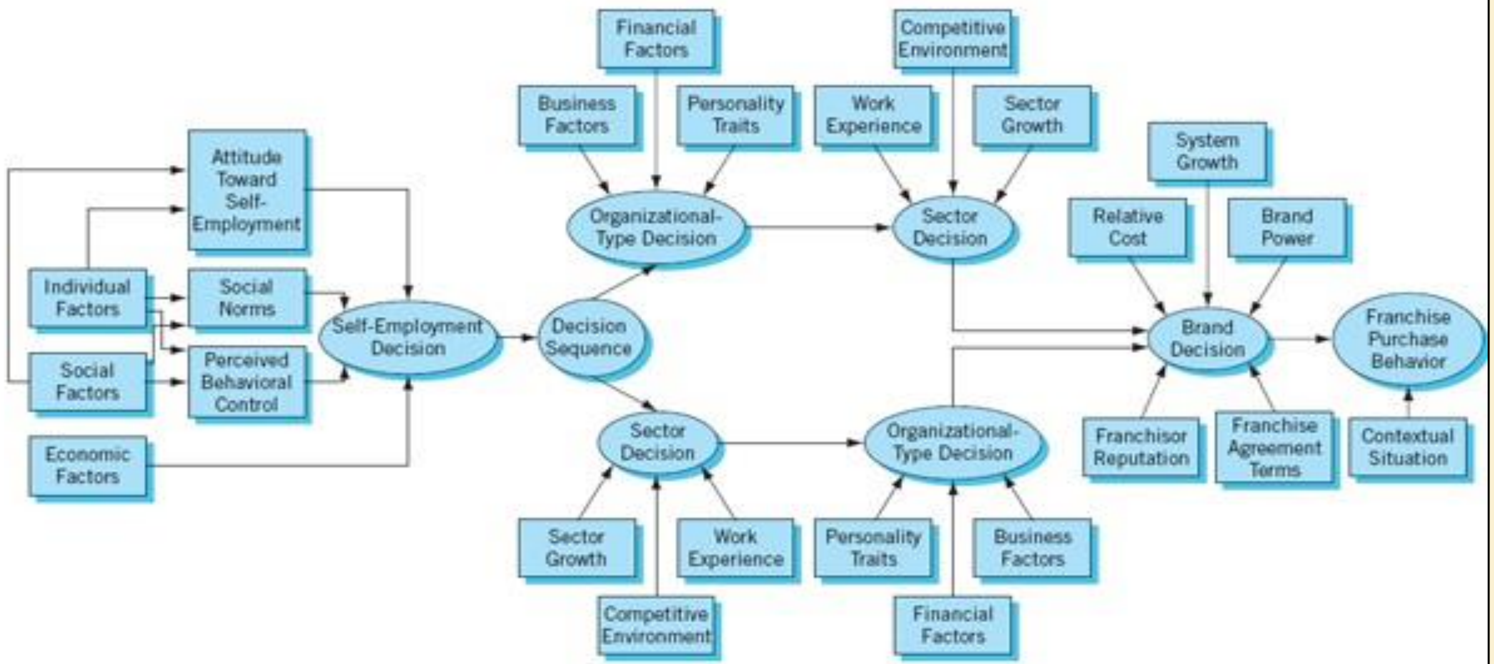
Evaluating Franchising Opportunities

- One of the first things a prospective franchisee must do is find a trustworthy source of information about franchise opportunities.
  - ❖ Learning of Franchising Opportunities.
  - ❖ Investigating the Franchisor.
  - ❖ Seeking Professional Help.
  - ❖ Making the Decision: It’s up to the Entrepreneur.

Evaluating Franchising Opportunities (Cont.)

- The Decision to Purchase a Franchise: Process Model.

Figure 7.2 The Decision to Purchase a Franchise: Process Model



Source: Patrick J. Kaufmann, "Franchising and the Choice of Self Employment," *Journal of Business Venturing* 14, no. 4 (1999): 348.

In conclusion

- The pathways from intention to entrepreneurial action.
- Factors that promote startup ideas.
- Factors that hinder the intention to start a business.

THANK YOU
FOR YOUR ATTENTION

Q&A