

Introduction to Entrepreneurship

TUM School of Management
Entrepreneurship Research Institute
Prof. Dr. Dr. Holger Patzelt



like us on
facebook

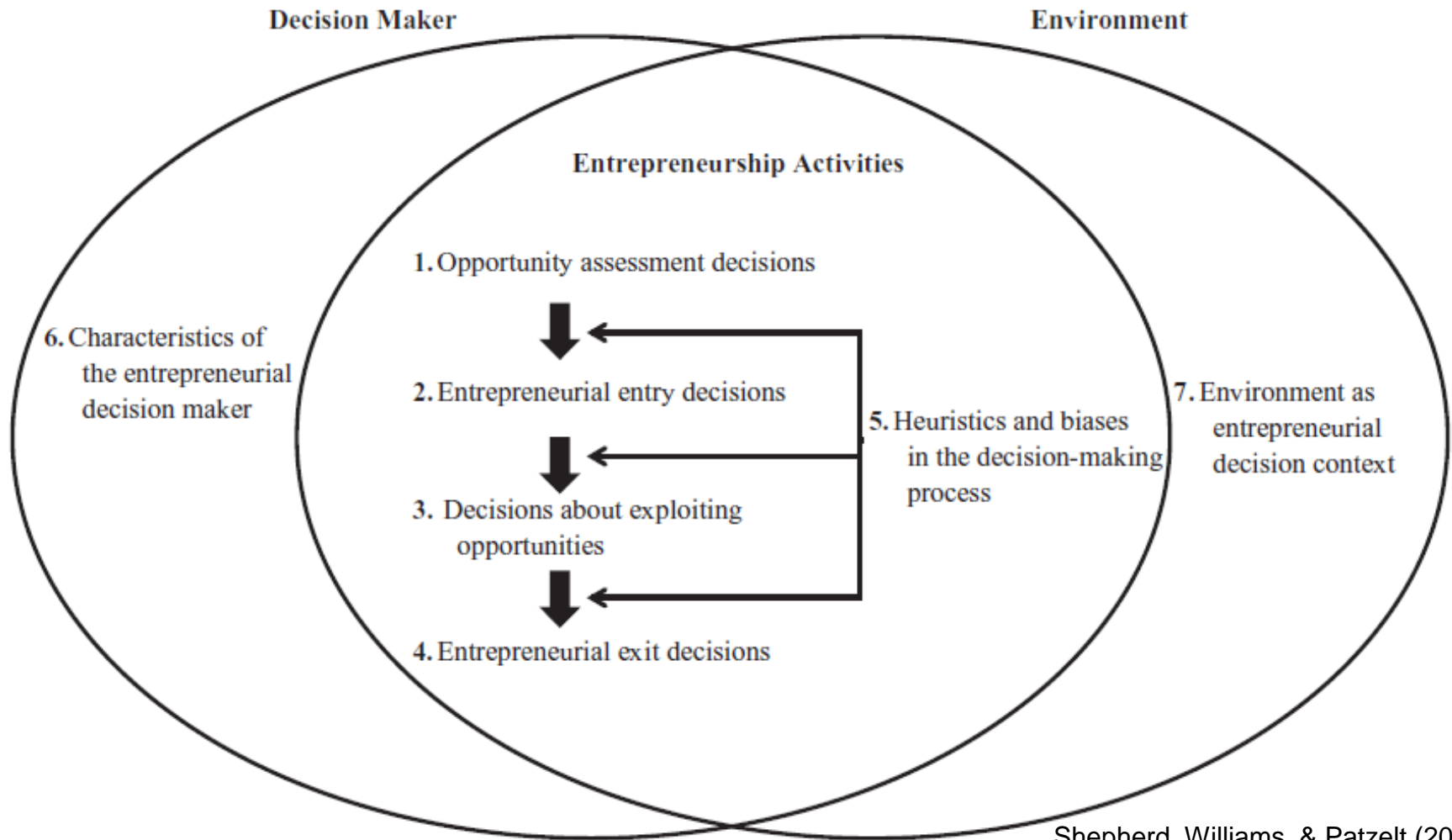


Entrepreneurial Decision Making

In this video you will learn:

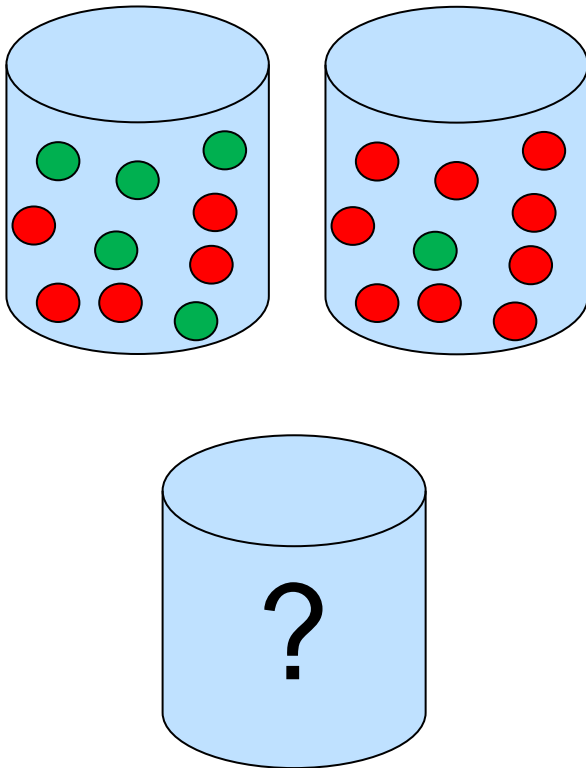
- What types of decisions entrepreneurs face
- How entrepreneurs make decisions without knowing their market
- What is the difference between entrepreneurial and managerial cooking
- What Viagra and Post-ist have to do with lemonade

Map of entrepreneurial decision making



Shepherd, Williams, & Patzelt (2015)

Risk vs. uncertainty



Risk: when the probability of an outcome is possible to calculate or is knowable

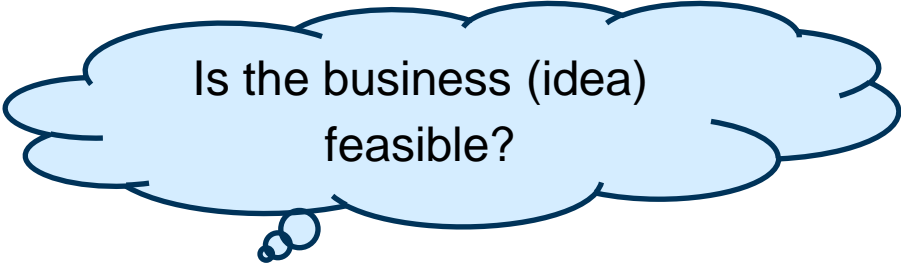
Uncertainty: when the probability of an outcome is not possible to determine or is unknowable

Uncertainties around a business idea

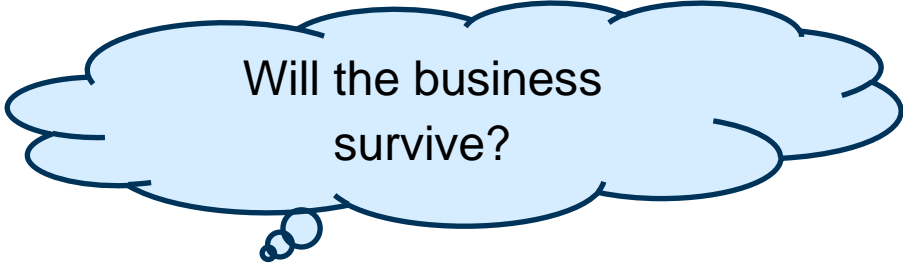
Consequences of the decision to start a business based on a new idea:

New, well defined product concept

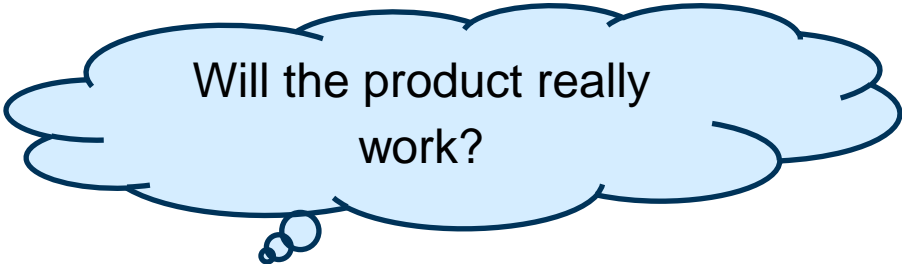
Little experience in setting-up a business



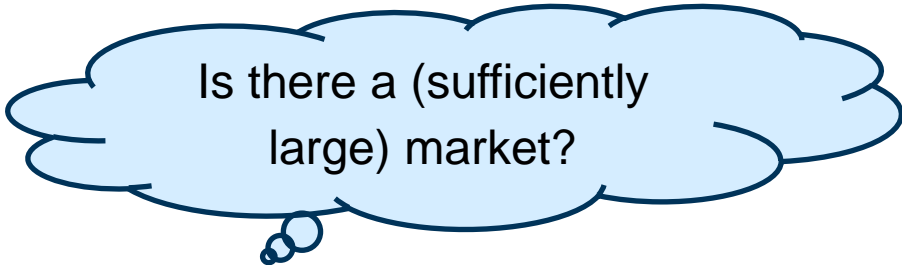
Is the business (idea) feasible?



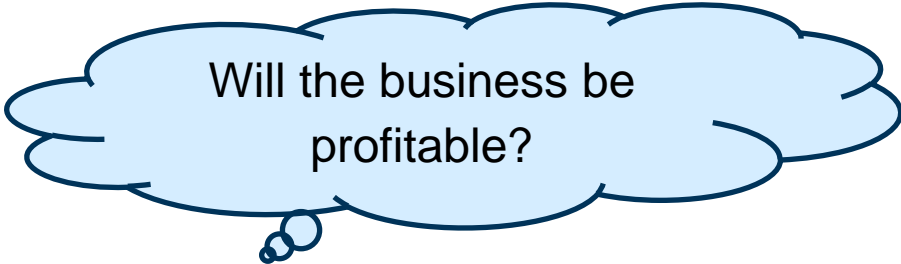
Will the business survive?



Will the product really work?



Is there a (sufficiently large) market?



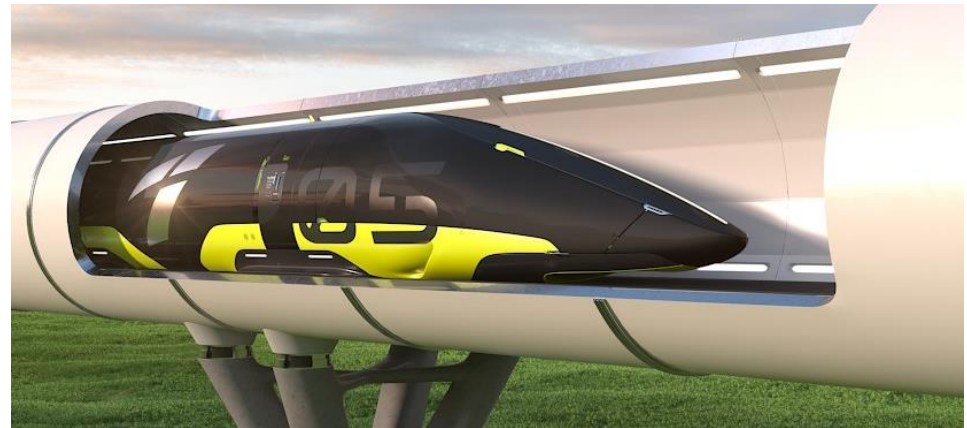
Will the business be profitable?

Fundamentally different challenges

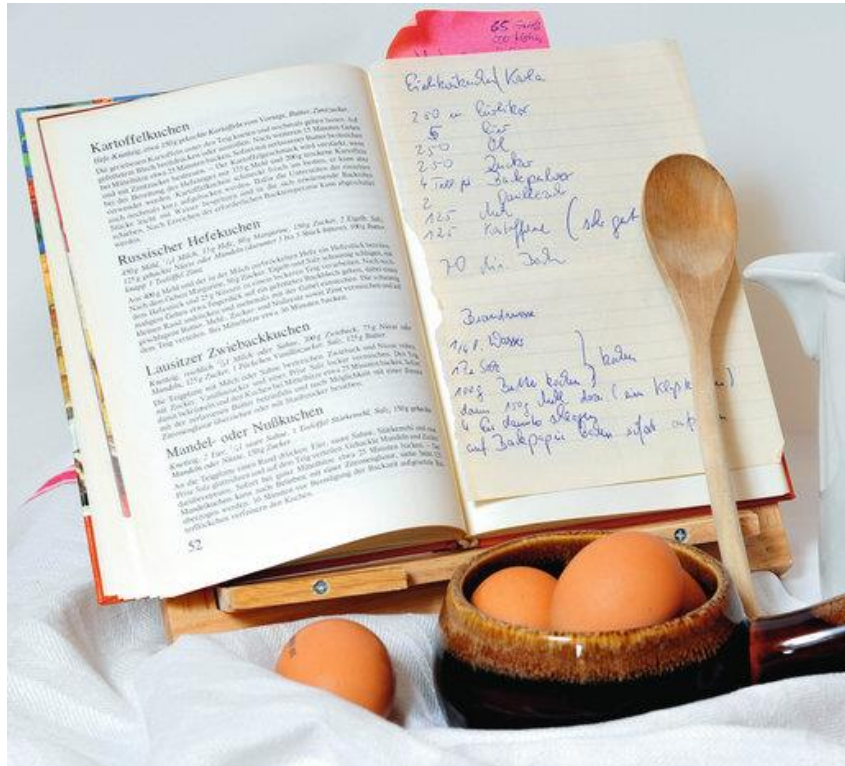
Hairdresser's shop



Hyperloop



Why Entrepreneurship is not Business Administration



Causal

vs.



effectual logic

Effectual Decision Making

To cope with uncertainty, entrepreneurs tend to use an effectuation process more often than a causal process. **Effectuation framework** (Sarasvathy, 2001) helps us understand how successful entrepreneurs deal with uncertainty.

Four key principles

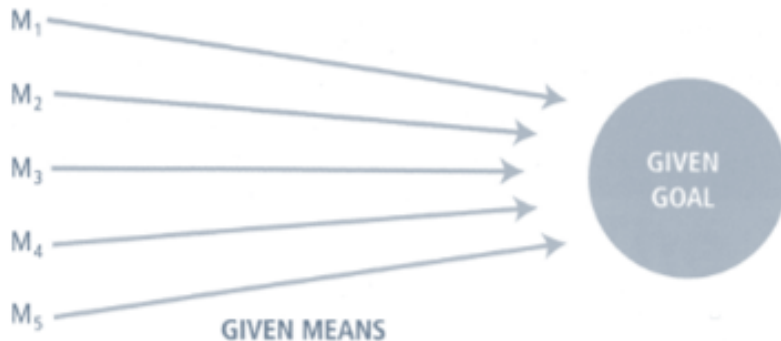


The worldview 'Control vs. predict' is sometimes referred to as a 5th principle

Principle 1: Start with means (The Cooking Metaphor)

Causation

Start with a desired outcome.
Focus on means to generate the outcome.



Effectuation

Starts with resources.
Selects among possible outcomes.

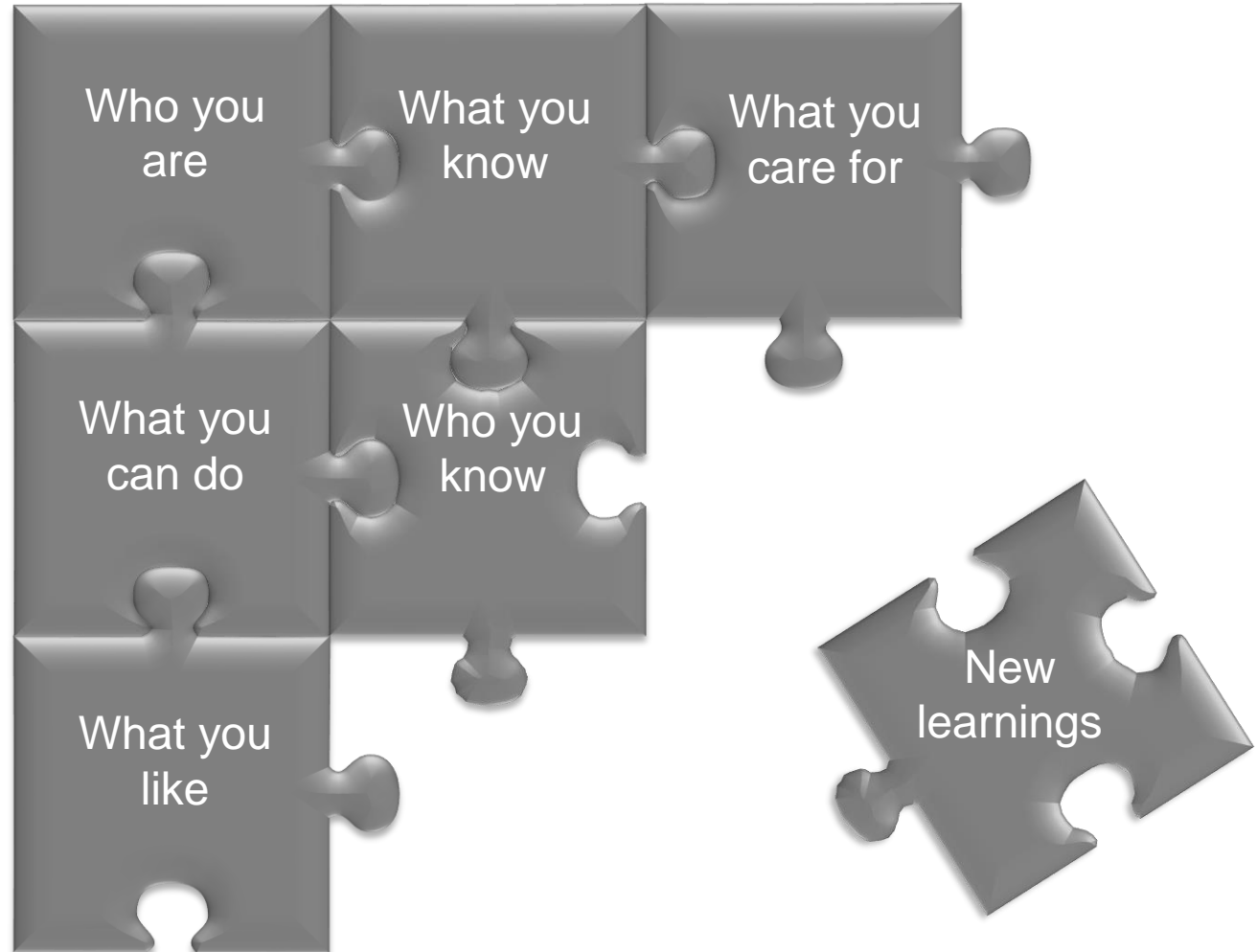


The basis for
decisions and new
opportunities:

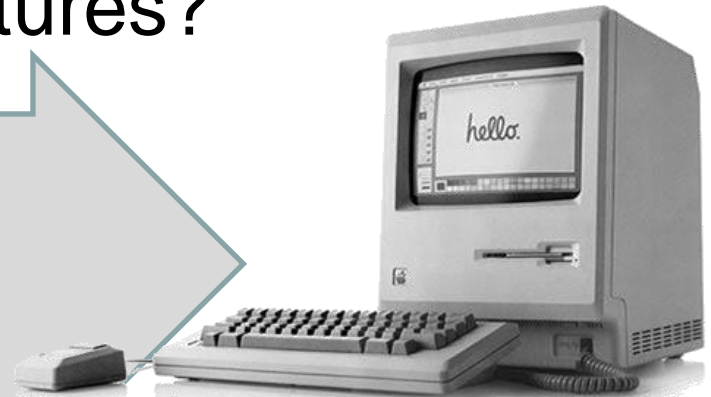
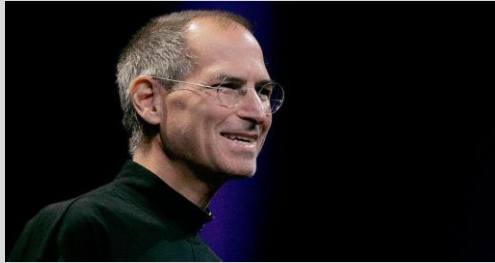
Who I am
What I know
Whom I know



Unique pool of resources



Your task (5 minutes):
What unique resources did Steve Jobs and Ben Cohen have to start their ventures?



Advantages of being means-driven

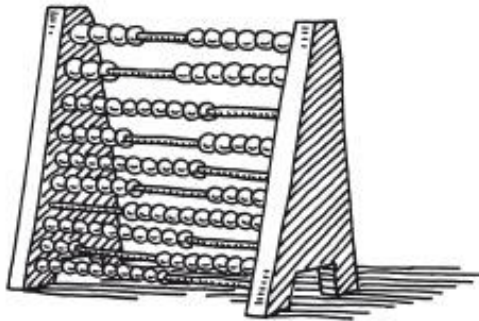
- You are **not chasing** investors
- You are **not waiting** for the perfect opportunity
- You are working on your **strengths**
- Good **stakeholders** want to shape goals – provide the means
- You are increasing the likelihood of finding or creating **opportunities that fit for you**
- You are forcing yourself to be **creative with few resources**



Principle 2: Affordable loss

Causation

Calculate upside potential and pursue the (risk adjusted) best opportunity.



Effectuation

Calculate downside potential and risk no more than you can afford to lose.



Your task (5 minutes):
How did Richard Branson start Virgin Airlines?



Principle 3: Form partnerships

Causation

Set up transactional relationships with customers and suppliers.



Effectuation

Build your future together with customers, suppliers, and even competitors.



Form partnerships: Crazy quilt principle

- Quilter has a wider latitude than puzzle solver in putting together pieces and can choose the arrangement
- Good quilters in large projects work with others
- Quilt not only has to be meaningful and pleasing, but also useful and valuable for keeping the body warm



Sarasvathy (2001)

Your task (5 min):
How did the FlixBus founders build their fleet?
How many buses do they own?



Advantages of forming partnerships

- Each stakeholder brings **new means** to the venture
- Each stakeholder only strives to invest what they can **afford to lose**
- A partnership environment contains **unexpected contingencies** which can be **leveraged**



Principle 4: Leverage surprise

Causation

Avoid surprises.



Effectuation

Surprises and even failures can represent new opportunities



Sarasvathy (2001)

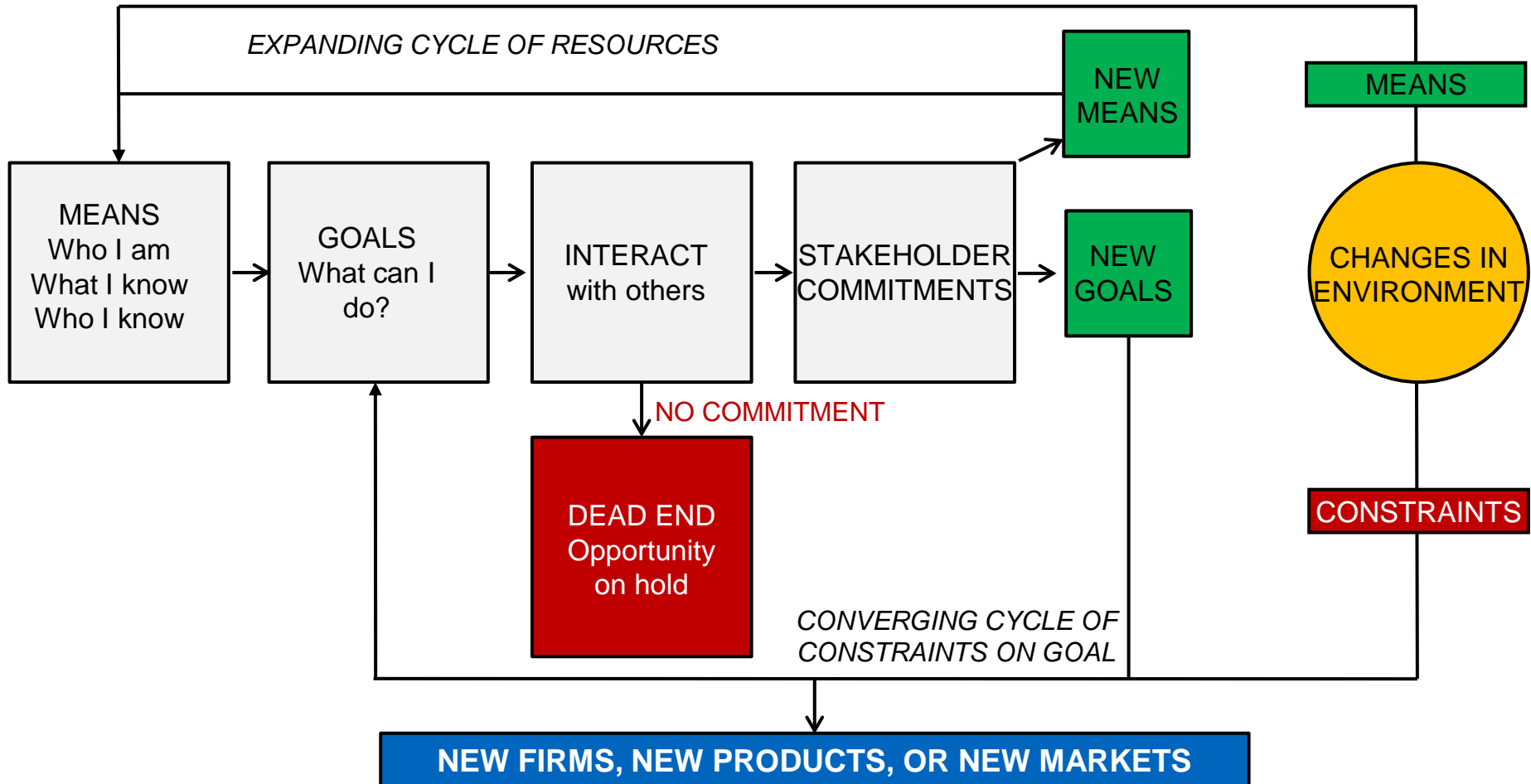
From lemons to lemonade: Turning initial failures into opportunities



Lemonade principle: Leverage surprise

- The unexpected is not a cost but a **resource**!
- Unexpected information can provide you with **new business opportunities** or trigger you to make adaptations to your idea.
- Although failure might be a setback, opportunities might be hidden in it.

Summary: Effectuation in action



Session summary:

- Entrepreneurs must frequently make decisions under uncertainty
- Effectuation is a creative way of making entrepreneurial decisions
- Your unique means are often the most important resource to get started
- If you effectuate, you do not have to wait for the killer idea – you develop your opportunity as you go. You can start now!

References from the class

Knight, F. H. (1921). Risk, uncertainty and profit. New York: Hart, Schaffner and Marx.

Read, S., Sarasvathy, S., Dew, N., Wiltbank, R., & Ohlsson, A.-V. (2011). *Effectual entrepreneurship*. New York: Routledge.

Sarasvathy, S. D. (2001). Causation and effectuation: Toward a theoretical shift from economic inevitability to entrepreneurial contingency. *Academy of management Review*, 26(2), 243-263.

Shepherd, D. A., Williams, T. A., & Patzelt, H. 2015. Thinking about entrepreneurial decision making: Review and research agenda. *Journal of Management*, 41(1): 11-46.