Strategic

Entrepreneurism™

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Shattering the Start-Up Entrepreneurial Myths

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SelectBooks, Inc.
New York

Strategic Entrepreneurism™: Shattering the Start-Up Entrepreneurial Myths

This edition published by SelectBooks, Inc.
For information address SelectBooks, Inc., New York, New York.

First Edition

ISBN 978-1-59079-189-9

Library of Congress Cataloging-in-Publication Data

Fisher, Jon B., 1972-
Strategic entrepreneurism : shattering the start-up entrepreneurial myths / Jon B. Fisher, Gerald A. Fisher, Wallace Wang. -- 1st ed.
p. cm.
Summary: "Discusses the way to design a startup company specifically with the goal of being acquired by a larger one"--Provided by the publisher.
ISBN 978-1-59079-189-9 (hardbound : alk. paper)
1. New business enterprises--Planning. 2. Entrepreneurship. 3. Consolidation and merger of corporations--Planning. I. Fisher, Gerald A. (Gerald Allen) II. Wang, Wally. III. Title.
HD62.5.F5328 2008
658.1'1--dc22
2008031658

Printed in the United States of America

10 9 8 7 6 5 4 3 2 1

This book is dedicated to Gerald, Anita, Danielle, Dave, Reido, Peter, Alice, Coleen, Ray, Barry, Dexter, Dennis, Jerry, John, Umang, Hank, Thomas, Bosco, Phil, Tony, and my favorite, Darla.

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There's an old saying that if you don't know where you're going, you'll probably never get there. This is particularly true for starting a company. If you're going to start a company, you're probably going to think big. The ultimate dream of every entrepreneur is to create the next big success story. Whether you want to create a company that sells a specific product (such as Apple's iPhone) or provides a unique service (such as Google's search engine), the one key to starting up any company is that you must make money so your company can grow, thrive, and ultimately dominate its market.

Unfortunately, the odds of success may seem stacked against you from the start. For every 100 companies that start up every year, 98 of them will never raise enough money to get off the ground. Out of the remaining two ventures that do manage to get start-up money (often called "seed capital"), the odds are 90 percent that they will fail despite any amount of funding they may receive. Out of the few ventures that manage to stagger past this high failure rate, another 6 percent may go out of business within three years while 3 percent may become a moderate success. Less than 1 percent of all startups ever survive long enough to go public through an IPO (Initial Public Offering).

But even an IPO is no guarantee of future success. Wall Street is littered with the wrecks of once-hot IPOs that fizzled and disappeared or survived only long enough for another company to buy their assets for pennies on the dollar. If your ultimate dream is to turn your startup into the next Google or Apple, you might succeed, but the odds are so heavily stacked against you that it's more likely that you may never receive any compensation for all your hard work. In today's business climate, there are so many factors out of your control that chance plays a huge part of any successful IPO. This makes the idea of starting up the next Google or Apple possible, but statistically improbable.

Of course, just because something is improbable doesn't mean you shouldn't strive for that kind of success. The problem with trying to become the next household corporate name is that too often entrepreneurs view this as an all or nothing proposition. They believe that you have to shoot for the moon to succeed. If they don't succeed in achieving this lofty goal, their company, which they worked so hard to create, develop, and maintain, usually crashes and burns into bankruptcy.

Given a choice between becoming the next Google or Apple, or going out of business entirely and fading into obscurity, is it any wonder that so many startups fail miserably? If you try to hit home runs every time you step up to bat, you're going to strike out nearly as often as you hit a home run. In the world of sports, you can strike out and step up to the plate over and over again. In the world of business, one or two strikeouts can wipe you out financially so that you may never get another chance to correct your mistakes and succeed.

By following the old rules of starting up a company, you have to shoot for that one in a million shot if you want to succeed, even though the odds may be stacked heavily against you. If you can free yourself from the blinders of these old rules, you'll find that you always have other options for starting up a company. This new way of starting up a company, which I call Strategic Entrepreneurism (SE), can maximize your chance of success while minimizing your risks.

The basic idea behind Strategic Entrepreneurism is to refocus your goal. Instead of trying to become the one dominant company in your market, Strategic Entrepreneurism says that you want to be the one company that a larger and more dominant company wants to acquire.

From day one, create and design your company to become an attractive acquisition candidate. Identify the companies that you believe would most benefit from acquiring your company. Of course, you can never control what another company does, but by understanding which companies may acquire you and what their own needs may be, you can steer your company in their direction as an acquisition target. Then when your company gets acquired by a larger corporation, everyone will remark about how lucky you are, not knowing that this was your goal from the beginning.

After you understand how Strategic Entrepreneurism works, you'll never look at starting up a company the same way again.

THE REAL LIFE OF AN ENTREPRENEUR

Being an entrepreneur really means taking action. You don't necessarily need an MBA, or any college degree at all (although it can help). What you really need as an entrepreneur is a lot of guts, faith, trust, and support from people around you. What you do with all these ingredients is up to you.

When you're the boss, all responsibility falls on your shoulders. It's not always easy and not always fun. Even worse, it's not always financially rewarding either, especially if your company goes belly up and dies before your eyes. However, being the boss means you get to call the shots; you get to define the direction for your company, and you get to reap the rewards of your efforts. If you're looking for job security with plenty of paid vacation time and a fixed time limit for working, you won't find it as an entrepreneur. If you're looking for a way to express your creativity and play the game of business on a large scale while making a difference in the world, then being an entrepreneur may be for you.

The dream of an entrepreneur is to have success and to enjoy the fruits of that success. When I ran Bharosa, our law office had a sweeping view of the entire San Francisco Bay. On particularly stressful days, my cofounders and I would stare out the windows to watch the fantastic yachts glide serenely across the water on a weekday afternoon. That's when we'd wistfully look at each other and then out at the yachts and tell ourselves, "That guy closed."

That meant that whoever was piloting that yacht had probably sold his company for millions of dollars and now had all the time he wanted to relax and enjoy life on his million-dollar yacht on a Wednesday afternoon. While it was more likely he inherited the money, it was nice for us to imagine he was one of us.

So many entrepreneurs have achieved massive success and there's no reason why you can't do it too. However, let me caution you that being an entrepreneur isn't all about making an unbelievable amount of money without doing much hard work. If you want to be an entrepreneur, you must love being an entrepreneur or be driven and ambitious enough to choose this path, because it won't always be easy.

My wife clearly remembers the day she returned home to find me dripping with my own perspiration because of the pressure and activity of the day. I had a large rash under each arm and down my sides from the perspiration. She wanted to take me to the hospital, but a cold shower and dinner at a nice restaurant helped me unwind and relax long enough for the rash to fade away on its own.

I still have framed MRI scans of my body on my office desk taken at the conclusion of each of my ventures. I have an L5S1 (left disk protrusion) in my lower back that causes significant pain in my left leg, which was caused from too much running on treadmills and possibly from long hours sitting at my desk at Bharosa.

I also have a scan of my neck and head resulting from a severe neck strain from the stress of running my second company, NetClerk.

One time I had been asked to give a report on Internet operations (as head of Internet operations) to the board of directors of a 3000 employee company (AutoReach/Tasha). I was 23 years old at the time and was cut off after speaking just 90 seconds. (The company even fired me six weeks later.)

In addition to the physical stress one must endure, succeeding as an entrepreneur requires being able to perform under pressure. I have walked into meetings knowing I needed to convince the attendees to invest $10 million in my company or I would have to fire 30 percent of my employees. I have sat across the table with the largest enterprise and most acquisitive software company in the world, and answered a barrage of questions knowing that each answer was putting my own money at stake.

I don't want to discourage anyone from becoming an entrepreneur, but I don't want you to think that being an entrepreneur is a path to easy money. It takes a lot of work, a lot of persistence, a lot of determination, and a lot of courage. I did it and I survived, so that means you can do it too. Just keep your eyes wide open and understand that the life of an entrepreneur may not be easy, but it can certainly be worth it.

MY LIFE STORY

(as told by the *San Jose Business Journal*)

To get to know who I am, it's probably best to read about my past from an objective point of view, in this case, from the *San Jose Business Journal*, which has printed various stories about my different companies:

Friday, June 28, 1996

ONLINE AUTOS: Fremont's Tasha Automotive Group has joined AutoReach Inc., a leading car leasing and buying service on the Internet, to put its fleet of Chryslers, Hondas, Lexuses, Nissans and Toyotas on the information superhighway.

Tasha has 12 dealerships and 17 franchises in the Bay Area. It was the region's largest car dealer last year, with $529 million in sales. The company hopes to boost its record of 25,000 new and used vehicles sold by adding cyberspace to its territory.

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Friday, September 17, 1999

Internet venture NetClerk Inc. has signed on a group of blue-chip investors to wage a war on red tape.

The South San Francisco startup is taking aim at an obscure niche, helping home contractors comply with local government building regulations, but nevertheless has attracted participation from Oracle President Ray Lane, BroadVision CEO Pehong Chen, Verisign CEO Stratton Sclavos and Keynote Software CEO Umang Gupta. That group and a handful of founders and other investors have scraped together $1.3 million to build a site and services that will begin testing in six Bay Area counties next week.

The system will allow small contractors, including plumbers, electricians and roofers, to process routine permit applications electronically on the NetClerk web site, which customizes the submissions to meet the requirements of local jurisdictions. In its initial rollout, NetClerk employees will suffer the various quirks of local records offices, but ultimately the company aims to help those offices standardize to a more efficient electronic model.

NetClerk is an example of second-generation web companies that are not necessarily targeting multibillion-dollar markets, but seek to own lucrative niches by meeting specific needs. So rather than aiming for a big venture capital war chest right away, the company took a strategic approach in lining up key allies at the same time it proved its product.

"The core offering needs to succeed immediately to prove its worth, but we think we can quickly establish a destination site for contractors," said Jon Fisher, founder and CEO of NetClerk, adding that expansion into other markets will occur early next year. The company's niche focus was attractive to its entrepreneurial investors in a way that may not have immediately struck the fancy of venture capitalists on the prowl for the next mass-market score. While an initial minimum venture financing in the e-commerce realm now hovers in the $5 million area, Fisher recognized the importance of establishing credibility before capital.

"I think the future successful startups in the Internet space are mostly going to be companies that provide a unique service with a sustainable business model," said Gupta, an early Oracle executive and founder of two public companies. "I felt I could help them because of my entrepreneurial experience and their eagerness to learn."

Fisher approached Gupta because he is a director of his and partner Phil Wohl's high school alma mater. He found the other investors through similarly personal ties.

Fisher said the $1.3 million has allowed an early build out of the system to prepare its launch, but that it now believes it is ready to take its message to the venture capitalists.

"We anticipate we will raise at least $5 million by the end of the year to really begin to scale the product," Fisher said.

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Friday, October 8, 2004

A start-up in Santa Clara today is launching a new way for consumers to thwart online identity thieves without requiring them to install new hardware or software on their computers.

The company, Bharosa Inc., has designed a means of transmitting screen names and passwords without typing them on a keyboard, where phishers or hackers using key-logging programs could surreptitiously capture the data.

If Bharosa succeeds, it could put a big dent in phishing, the category of computer attack in which criminals set up fake bank or e-commerce sites to steal a computer user's personal information. Information security firm Symantec estimates that 1.78 million Americans have been caught by phishing expeditions over the last year that have cost banks and credit card issuers $1.2 billion.

Some security companies have been pushing a technology known as tokens—small keychain-style gadgets that display a new password every minute. In addition, Bharosa CEO Jon Fisher and Thomas Varghese, president and chief technology officer, expect that improvements in biometric systems that let users authenticate themselves with a fingerprint or a retinal pattern may become secure methods of identification. Still, they tout their technology as a hardware-free approach that is available right now.

"We can have this up and running at any Fortune 500 company in 30 days," Mr. Fisher says.

The two technology veterans came up with the concept at a Starbucks in San Mateo and jotted it down on a napkin.

That first design was a graphic representation of a combination lock. The user could make the dial on the lock spin by clicking on arrows to direct the wheel to turn clockwise or counter-clockwise. Clicking on "enter" would select the appropriate letter or number.

The beauty of this design, they say, is no keyboard activity for key-loggers to record. The only information sent over the Internet would be something like 20 degrees clockwise or 30 degrees counter-clockwise.

But there was a flaw to this design, Messrs. Fisher and Varghese realized: An attacker who captures the entire screen could see which letters and numbers are selected.

Eventually, a better idea occurred to Mr. Varghese—use two wheels instead of one.

Here's another way to picture it: Imagine two wheels, one inside the other. One has letters printed on it, the other numbers. Colored patches make pairs of the letters and numbers. Every time you go to a log-in screen, the wheels will have turned to form a new combination.

To sign on, a user locates the first letter or number of his password. If that initial letter lines up with the number "7" and the color yellow, then 7-yellow becomes the marker by which the rest of the password can be entered. The user then clicks on arrows to move that marker around to each additional character of the password, clicking on an "Enter" button to submit each letter or digit. Someone capturing the screen or looking over the user's shoulder would see two wheels rotating but would have no clue as to what their movement meant.

"It's just two wheels that interact in a way that only the user understands," says Mr. Varghese.

Bharosa plans to license its security wheel to banks, Internet service providers and e-commerce sites for $100,000 to $1 million, depending on the number of users. At least initially, Mr. Fisher believes, customers of client companies will be able to choose whether they wish to use the wheel for greater security. Bharosa is testing its concept with two large e-commerce companies and several large financial companies, says Mr. Fisher, although he will not reveal the names.

The privately held company has been self-funded and has some angel backing, Mr. Fisher says.

Analysts are interested, but cautious.

"This is a step in the right direction," says Gartner analyst Aviah Litan. But she still puts her security hopes in tokens. "In the end it's not a good substitute for a good card token," she says.

Users may also find it difficult to adjust to the new concept of circles instead of spaces to type passwords.

"It's hard to do real innovation on user interfaces," says Alex Aiken, professor of computer science at Stanford University. "People tend to acclimate slowly to new ideas and even small changes." And, he adds, "even now 10 percent of Internet surfers don't know how to use a scroll bar."

Still, the security industry acknowledges that something must change—and soon.

"There has been a dramatic increase of threats from piracy in general and spyware and key-logging in particular," says Oliver Friedrichs, senior manager of Redwood City-based Symantec Security Response. Symantec offers software designed to catch key-logging and spyware software that some attackers use to grab your information.

Other companies such as RSA and ActivCard have designed gadgets called keys, or tokens, that look like a digital pocket watch. Instead of telling time they display a number, which the user employs to log onto a Web site. The key is coordinated with the Web site's server, and the number it displays changes every minute. America Online recently adopted this method for its PassCode token program for subscribers who want to pay for added security.

Mr. Friedrichs sees these keyfob tokens as the most secure password technique.

"If it's just software running on a computer, it's not as secure as a token you have in your pocket," he says.

But Mr. Fisher wonders if the token idea will ever catch on.

"So people really want to carry around a token for online access to their bank and another for access to their Internet service and others for eBay and PayPal and Amazon?" he asks. "Our design is radically different and asks for new behaviors. But consumers don't have to keep track of various pieces of plastic. Adoption of our technology is simply a matter of saying 'yes.' "

WHO IS JON FISHER?

2007 was a great year.

That was the year I served as Bharosa, Inc.'s CEO until its successful acquisition by Oracle Corporation. For the next six months I worked as Vice President Product Management to integrate Bharosa within Oracle. My assignment with Oracle ended just in time for me to enjoy the holidays. Later I won Ernst & Young's Entrepreneur of the Year award in Silicon Valley and lectured across the country.

After 15 years as an entrepreneur, I also learned my most valuable business lesson about Strategic Entrepreneurism. To show you how important Strategic Entrepreneurism has been to my work, I would have gladly traded everything that materialized in 2007 if only I could have understood Strategic Entrepreneurism 10 years earlier.

Although Bharosa was my biggest success, I don't want you to get the idea that I got lucky or that I haven't had my share of failures, because neither is true. While luck always plays a part in any type of success, you can create your own luck by being prepared for opportunities as they arise. The main part of my success with Bharosa came about after I had already started up and worked as the CEO for two previous companies as well[1].

I started my first company while studying political science and economics at Vassar College and dropped out of school to run this company, which I later sold at age 23. Afterwards, I returned to school where I finished my degree in organizational behavior at the University of San Francisco.

After graduating I jumped into my second startup, which turned into a classic example of a company that had all the elements of success, but failed because of the simple mistake of

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[1] My first two companies were AutoReach and NetClerk. AutoReach was later acquired by the Tasha Automotive Group, which merged with AutoNation. NetClerk failed and its assets were bought up by BidClerk.

sacrificing long-term strategic performance in exchange for short-term profits and growth. Of all the possible mistakes an entrepreneur can make, this can be the most fatal error that can doom a company since it comes disguised as a Trojan Horse masquerading as growth and increased revenue.

While every company should strive for growth and revenue, unchecked, rampant growth can actually choke a company and kill it by diverting limited resources towards multiple and tiny sources of income. You may think that as long as you're making money, you can never go broke, but if the cost of servicing and managing multiple, tiny income sources takes too much time and effort, you may never make much of a profit either.

The trick is to manage growth and revenue intelligently. You want maximum growth and profit that you can sustain now and in the long-term. It's one thing to get plenty of customers, but it's an entirely different thing to service those customers. McDonald's started selling hamburgers from a single restaurant and gradually branched out across the world, but imagine if in the beginning they had started trying to sell millions of hamburgers from their first restaurant. They would have been swamped with too many orders and not enough resources, so they would have wound up failing no matter how large their potential profits might have been.

By knowing how to recognize and avoid this problem of rapid growth, you can make the most crucial decision of an entrepreneur that can spell the difference between success or failure for any company. The lessons that I learned from my first two companies ultimately helped me create Bharosa correctly from the start.

Finally, luck had little to do with the fact that the sale of Bharosa to Oracle gave investors a six-fold return on their investment within a three-year time frame. (The typical successful startup delivers a three-fold return on an investment in five years, so Bharosa became twice as profitable in nearly half the amount of time.)

Bharosa, which had 25 million users at the time of its acquisition, was Oracle's 32nd purchase since its $10.3 billion takeover of PeopleSoft Inc. in January 2005. Oracle Chief Executive Officer Larry Ellison has spent more than $25 billion on his deals, making the company the most acquisitive in the software industry. On September 20, 2007, Larry Ellison even stated Oracle's long-term plan:

> Our strategy for growth is to find a way to add more value to the same customers we already serve, which are the large end of the mid-market and large companies. What we're doing here is moving beyond ERP to industry specific software. So in the telecommunications industry that would be billing systems and network provisioning systems and network inventory systems; core applications to run their business. Core applications to run a bank. Core applications to run a retail chain of stores. Core applications to run a utility. That's our focus, and that allows us to leverage the existing relationships that we have because we already sell databases to these companies, we sell middleware to these companies. We sell ERP and CRM to these companies, and now we want to sell this industry-specific software.

What allowed Bharosa to earn millions of dollars for me and my founding team was applying the principles of Strategic Entrepreneurism to all aspects of the company, from its inception all the way through its growth as a viable company. I knew what types of companies Oracle wanted to buy, so I made sure I made Bharosa into the exact type of company that Oracle would acquire. The principles of Strategic Entrepreneurism turned Bharosa into a success. I'm confident that these principles will work for any business, and now I'm going to share these principles with you.

1

The Basics of Entrepreneurism

Strategic Entrepreneurism is about designing your company, right from the start, toward a clear, definite outcome. When we created Bharosa, we designed the entire company to be acquired for the maximum amount of money in the shortest amount of time. Oracle didn't suddenly discover Bharosa and decide that my company would be a natural fit. Instead, we designed Bharosa to fit right into a company like Oracle from the beginning. Everything Bharosa did from day one was aimed at making the company an attractive acquisition target.

Practicing Strategic Entrepreneurism can actually involve more discipline than trying to build a company towards an IPO. First, you must rely on far less investment capital to guard against dilution. The more money you accept to start up your company, the more you'll have to pay back to these initial investors before you can make any money yourself.

Second, you must build your company's products so that they can be seamlessly integrated with a potential acquirer in mind. This can be as simple as making sure your product doesn't compete directly with a potential acquirer's product, to ensuring that customer contracts don't contain too much liability for an acquirer, to courting the right analysts to say and print just the right things about your company. If I could make only a single bet on my entire company, I would bet on the right customer (and the right team to serve that customer) who is of maximum strategic interest to a potential acquirer.

By making the correct decisions right from the start, all entrepreneurs can increase their chances of success for their company. However, to fully understand the advantages of Strategic Entrepreneurism, you must first understand what being an entrepreneur is all about.

BEING AN ENTREPRENEUR

The best part about becoming an entrepreneur is that you can make your own rules. Given a choice, most entrepreneurs would rather start their own company than work for somebody else. It's not that entrepreneurs can't work in a typical job, but that entrepreneurs enjoy making decisions to control their own destiny. A true entrepreneur isn't someone motivated solely by money or power, but by the desire to make a difference.

Although it's true that most entrepreneurs must work long hours, especially when trying to get their company off the ground, entrepreneurs aren't necessarily workaholics; they simply enjoy what they do. Some entrepreneurs enjoy working in specific industries, such as software or alternative energy. Other entrepreneurs simply enjoy the process of creating companies, no matter what field they may be in. To an entrepreneur money is just a way to measure how well they're playing the game of business.

Anyone can become an entrepreneur. Colonel Sanders became an entrepreneur at the age of 65 when he started Kentucky Fried Chicken. Michael Dell formed PC Limited (the predecessor to Dell Computers) from his dormitory at the University of Texas in Austin when he was only 19. Julie Aigner-Clark started the Baby Einstein Company from her suburban home in Denver, Colorado. Because entrepreneurs can make their own rules, they're not limited by age, race, sex, location, or educational background. If you have a good idea, believe in your dream, and have a lot of persistence, there's nothing that can stop you from becoming an entrepreneur too.

STRATEGIC ENTREPRENEURISM REQUIRES ENTREPRENEURS TO WORK IN TEAMS

While the media loves to highlight the accomplishments of individual entrepreneurs, the truth is that entrepreneurs rarely succeed on their own. Entrepreneurs usually succeed as part of a team of entrepreneurs.

At Bharosa we needed entrepreneurs with extraordinary dedication and work ethics way beyond the call of duty, so that Bharosa would need to raise less outside capital in order to suffer less dilution. Still, we needed to be able to compete with companies with significantly more resources, including significantly larger teams. The men who were perhaps our two finest entrepreneurs, Thomas Varghese, our founder and president, and our co-founder and VP engineering, Bosco Durai, led our product and engineering organizations that were responsible for critical execution. Bharosa's attractiveness to an acquirer like Oracle was in large part due to the quality and scalability of our products. Perhaps nothing was more important to Oracle than entrepreneurs like Thomas and Bosco.

Although the media portrays entrepreneurs as loners who tinker in a garage somewhere and hit it big overnight, the truth is that most entrepreneurs team up with at least one other person right from the start. The entrepreneur may have the technical skills needed to create a product or service, while the partner may possess the business skills needed to get the company off the ground (or vice versa).

For example, Bill Gates started Microsoft with his friend Paul Allen. While both men were programmers, Paul Allen is credited with making the business deal to purchase an operating system called QDOS for $50,000. This later became the MS-DOS operating system that Microsoft sold to IBM and other computer manufacturers.

Scott Cook founded the financial software company Intuit after realizing that personal computers could replace traditional paper and pencil accounting methods. Since at that time Scott Cook was a product manager for Proctor & Gamble, he enlisted the help of Tom Proulx, a programmer who could create the actual software known as Quicken. With Scott Cook handling the business affairs and Tom Proulx handling the programming chores, the two of them eventually turned Intuit into a billion dollar company.

The foundation of any company's success starts with the entrepreneur's vision, but achieving that goal requires a team who possesses the necessary skills to turn raw ideas into a concrete reality. Just as a quarterback can't win a football game by himself, so an entrepreneur can't succeed alone.

Every entrepreneur needs the right people on his or her team and every entrepreneur also needs the right mentors, who act like coaches. These mentors can give you advice and suggest different ways of thinking or studying problems. Mentors can be friends, acquaintances, or business associates, but whoever they might be, mentors are a necessary part of every entrepreneur's success.

Mentors can often provide an objective view of your current situation and give you advice from their own experience. Often mentors have gone through similar situations before, so they can help you identify opportunities and avoid pitfalls that you might have not seen otherwise. Although it's possible to startup and run a company without mentors, it's extremely difficult to go it alone. Mentors simply act like guides, showing you the shortcuts through a seemingly impenetrable jungle of confusion and opportunities.

Ultimately if you have the right idea but the wrong people, your plan for success will never get executed properly. If you have the right people but the wrong idea, you'll just move quickly in the wrong direction. The key to winning the game of business is to combine the right idea with the right people.

ENTREPRENEURS SOLVE PROBLEMS

Entrepreneurs don't just create companies for the sake of building a business. Entrepreneurs create companies to solve crucial problems for individuals or other businesses. By their very nature, entrepreneurs often find new ways to solve existing problems. As a result, entrepreneurs often avoid competing directly with existing companies and tackle problems that existing companies ignore or haven't recognized in the first place.

At one time, the only way to watch movies was to visit a theater or wait for the movie to appear on TV. After inexpensive videocassettes appeared, 29-year-old David P. Cook wanted to help people solve the problem of watching their favorite movies at home without having to buy them each time. So in 1985 he formed Blockbuster Video to make it inexpensive for people to rent the latest movies and watch them at their convenience at home.

Although the video rental business solved the problem of watching a movie at your convenience, it soon created another problem. Video rental stores like Blockbuster could offer only a limited selection of movies due to space restrictions in their stores. In 1997 Marc Randolph and Reed Hastings provided the solution to this problem by forming Netflix, a mail-order video rental service. Now consumers have the convenience of watching movies at home with the added convenience of having a virtually unlimited library of movies to choose from.

At the time of this writing, entrepreneurs are creating companies to solve the problem of having to wait for movies to arrive in the mail. Perhaps by the time you read this, some clever entrepreneur will find a way to make it easy to download movies directly to your television set, personal computer, or even a mobile device like a personal digital assistant or mobile phone. Then you can watch movies instantly, whether you're home or stuck in line waiting to get into a concert or ballgame.

Each new development, such as videocassettes and DVDs, spawns new opportunities and possible new solutions. Because the world is always changing, new opportunities are popping up all the time and new problems are created (and solved) every day. As a result, there will never be a shortage of opportunities for entrepreneurs to succeed.

LEVERAGING HIGH-TECHNOLOGY

There will always be new problems that require new solutions, which means the landscape for entrepreneurs will always be wide open. In general, there are two types of businesses you can start: a traditional brick-and-mortar business and a high-technology venture.

A traditional brick-and-mortar business requires physical resources such as a building and equipment. The building and equipment may not require a massive investment, but it does require a physical presence. Back in 1965 Fred De Luca borrowed $1,000 from family friend, Peter Buck, to start a sandwich shop when he was only 17 years old. Initially Fred wanted to earn enough money to pay for college, but when his sandwich shop proved popular, he expanded and franchised his restaurant. This eventually became the popular Subway restaurants, the third largest restaurant franchise behind McDonald's and Yum! Brands (which owns Kentucky Fried Chicken, Taco Bell, and Pizza Hut).

The biggest problem with a traditional brick-and-mortar business is the cost for starting up and the long period of time before such a business can grow from a good idea to a multimillion dollar company. Fred De Luca may have started Subway with $1,000, but he needed several decades to grow.

While there's nothing wrong with starting a brick-and-mortar business, another alternative is to start a high-tech business. The two biggest advantages of a high-tech business are the low startup costs and the potential for a high return on your investment in a short amount of time.

Wikipedia defines High-Technology as "technology that is at the cutting edge—the most advanced technology currently available." Basically, high-technology leverages your strengths and multiplies your potential profitability. For minimal cost and maximum potential success, take advantage of high-technology when starting up your company.

Back in 1996 Larry Page started a research project designed to study the number of links connecting various web pages. After showing friends his project, Larry with his collaborator Sergey Brin, soon formed the basis for a search engine that made searching the Internet faster and more accurate. Initially, this entire research project existed entirely on a single computer.

In 1998 Larry and Sergey incorporated his company as Google, and by 2000, Google had started earning revenue through online advertising. By 2004 Google had gone public and raised a market capitalization of more than $23 billion. In less than eight years Google went from an interesting project started on a university computer to a billion dollar company. In comparison, Subway took nearly forty years to reach a net worth of $1.5 billion dollars. There's no arguing with success, but given a choice, would you rather wait forty years to make $1.5 billion or wait eight years to make $23 billion?

Building a business around high-technology simply lowers your startup costs and increases your chance for massive profitability in the shortest amount of time. Instead of creating a physical product that needs to be made, shipped, and delivered, a high-technology business literally creates a product out of thin air.

In the case of Bharosa, we created a software authentication program that resides on a server (nothing for users to download). We needed to create Bharosa's program only once, and then we could duplicate it as many times as necessary at no added cost. Distributing our product could be done inexpensively electronically through the Internet.

The bulk of Bharosa's expenses went toward the physical cost of office space and employee salaries, which every company needs. But instead of spending additional money on a warehouse to store products, a factory to manufacture a product, or a trucking service to deliver the product to customers, Bharosa leveraged technology to eliminate those costs while increasing the speed of distribution at the same time. You can think of a high-tech company as a leaner, more efficient form of a traditional brick-and-mortar business but without the added expenses.

One reason why Netflix is killing Blockbuster's business is that Blockbuster is saddled with the cost of expensive retail stores while Netflix relies on the minimal cost of postage to deliver the products right to the customer's front door. By combining the low-tech use of the postal system with the high-tech use of databases to track and manage its massive inventory of movies stored on DVDs, Netflix can service far more customers at far less cost than Blockbuster can ever hope to do.

In many cases, a high-tech startup can compete with and dominate a traditional brick-and-mortar competitor (Netflix vs. Blockbuster) no matter how big the brick-and-mortar company may be, or how long it has been in business. Trying to compete with a brick-and-mortar business by opening another brick-and-mortar business is almost always a recipe for disaster. Hollywood Video tried to compete head-to-head with Blockbuster and lost. Burger King will probably never wipe out McDonald's, and Peet's Coffee will likely never wipe out Starbucks. Both Burger King and Peet's Coffee may be profitable, but if you're going to start any company, why settle for creating a company that practically guarantees you'll be forever stuck with second-rate status?

By leveraging high-technology in your business, either as your product itself or part of your service, you can create a nimble company that can service an untapped market, or provide a new service to an existing market. In either case, relying on high-technology lowers your cost of entry and helps you outmaneuver your competition to the point where you essentially have no competition. If you can carve out a niche for your company and establish your company as the leader in that niche, customers will have no choice but to turn to you.

HIGH-TECHNOLOGY + CREATIVITY = CAPITAL

Perhaps the most important use of high-technology is to leverage your own creativity. In the old days, companies measured capital by the things they owned. General Motors is worth billions of dollars because it owns so much real estate, buildings, equipment, and inventory. If General Motors shut down the company tomorrow, its assets would be worth a fortune, but once sold, it would be gone forever.

With a high-tech company, the assets aren't in physical items, but in intangible processes that are difficult for competitors to duplicate. Anyone can slap together the same parts to build a computer, which is why computer manufacturers like Gateway could not compete against Dell Computers and Hewlett-Packard. However, Apple doesn't just build computers; it also offers a unique sense of design and a synergistic ecosystem of products that not only work together, but convey a sense of being on the cutting edge of technology.

When you buy an Apple Macintosh computer, you're not only buying a physical product (the computer), but also Apple's brand

(Think Different) combined with Apple's unique software offerings that include iTunes (for easy integration with Apple's iPods) and synchronization features (for easy integration with Apple's iPhone).

The moment you buy one Apple product, it's easier to buy and use another Apple product since they work so well together. Companies such as Microsoft, Dell Computers, and Sony may try to compete with their own music players or colorful and stylish computer designs, but they'll always fall short of anything offered by Apple. By combining high-tech with their creativity, Apple has essentially raised the standards so high that it has effectively eliminated all of its competitors. If you want a computer, digital music player, or mobile telephone like the Macintosh, iPod, or iPhone, you have no choice but to buy one from Apple.

In today's world, the true value of a company doesn't lie in its physical assets but in its intellectual assets. Anyone can duplicate the physical parts of a company, but nobody can successfully copy the creativity of another company. Without high-tech, Ford can often successfully copy and duplicate anything created by General Motors and vice versa. By leveraging your unique creativity with high-tech, you enhance and multiply your creativity in ways that competitors can't easily follow. With high-tech, your true assets are nothing more than the unique way that you choose to do business with others.

ELIMINATE THE NEED TO CREATE THE IMPOSSIBLE

One of the biggest fallacies of starting an entrepreneurial venture is that you need to create a new product or service that's radically different from anything currently on the market. The truth is that you don't need to invent something impossible like a car that runs on water or a new material that's stronger than steel but lighter than a piece of paper. To succeed in business, you just need to identify a problem with an existing business and find a way to make it better.

Given the high cost of gasoline, General Motors and Toyota took two different approaches. Back in 1997 General Motors developed and marketed an electric car dubbed the EV1. At the same time, Toyota introduced the Prius, a combination gasoline-electric hybrid car.

By 2003 General Motors had cancelled the EV1 despite growing demand and interest. In comparison, Toyota continued to improve on its hybrid engine technology to the point where the Prius has become the most popular alternate energy vehicle in the world.

Both Toyota and General Motors spent millions of dollars developing their technology, but General Motor's EV1 struggled with short endurance because of the limited amount of charge its batteries could hold, as Toyota's Prius simply advanced technology just a little bit to achieve the market success and profitability that eluded General Motors.

The lesson is simple. If you try to create a radically new product, your chances of failure are much greater than if you try to improve an existing product. Not only does improving an existing product take less time and money, but it also increases your ultimate chance for acceptance and success as well.

THE TYPICAL PATH OF A STARTUP

While every startup is different, the path for each startup consists of several distinct phases as shown in Figure 1-1. First, the entrepreneur dreams up an idea for a business. Second, the entrepreneur assembles a team to help create and market the product. With a team in place, the entrepreneur may need to raise seed

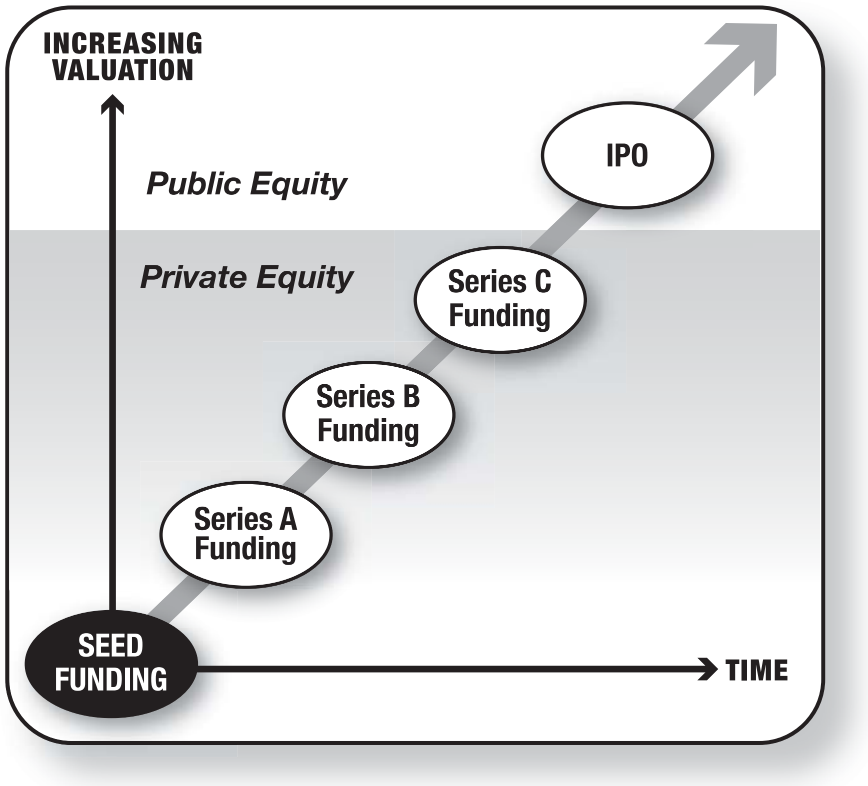

Figure 1-1. The Life Cycle of a Typical Startup.

money to get the company started. This money can be the team's own money, money from friends and relatives, or money from outside investors.

As the company grows, it may go through additional rounds of funding, which provides money necessary for the company to continue growing. Ideally the profits generated by the company can provide the additional money necessary to continue growing, but if profits are trickling in, you may need this additional funding to move the company forward much faster. For example, you may need additional funding to pay for expanding your sales force or purchasing additional equipment.

Many companies make the mistake of using additional funding to pay their bills and keep the company alive. What inevitably happens is that the company continues losing money and once outside funding dries up, the company is forced to declare bankruptcy. As a general rule, startups should only use each round of additional funding to help it move forward, not to delay bankruptcy. During this period, a startup remains a private corporation.

After several rounds of funding, a startup may decide to offer an IPO that essentially allows anyone to buy shares in the company and become part owners. This is the time where a company becomes public. A successful IPO is generally considered a major milestone, although it's really just another form of additional funding.

In the traditional model, a startup's success relies on offering an IPO. However, the long path towards reaching an IPO can take years. During the dot-com bust of the '90s, many companies issued IPOs prematurely, watched their stock price skyrocket, and then plummet into nothing.

In Strategic Entrepreneurism, the goal isn't to reach an IPO but to sell out to an acquiring company much earlier. The drawback is that the potential valuation is much less, but the major advantage is that it takes less time, which also increases the chance of success, as shown in Figure 1-2.

The typical business model for a startup assumes that the longer a company stays in business, the higher its valuation, but that's not always true for two reasons. First, the longer a company stays in business, the greater the chance of failure, either through changing market conditions or growing competition. Second, the more funding your startup receives, the greater the dilution of ownership for the entrepreneur. The longer you hold on to a company, the greater the risk that your valuation may decrease.

Even worse, the longer you hold on to a company, the greater the risk that your company will never be profitable altogether.

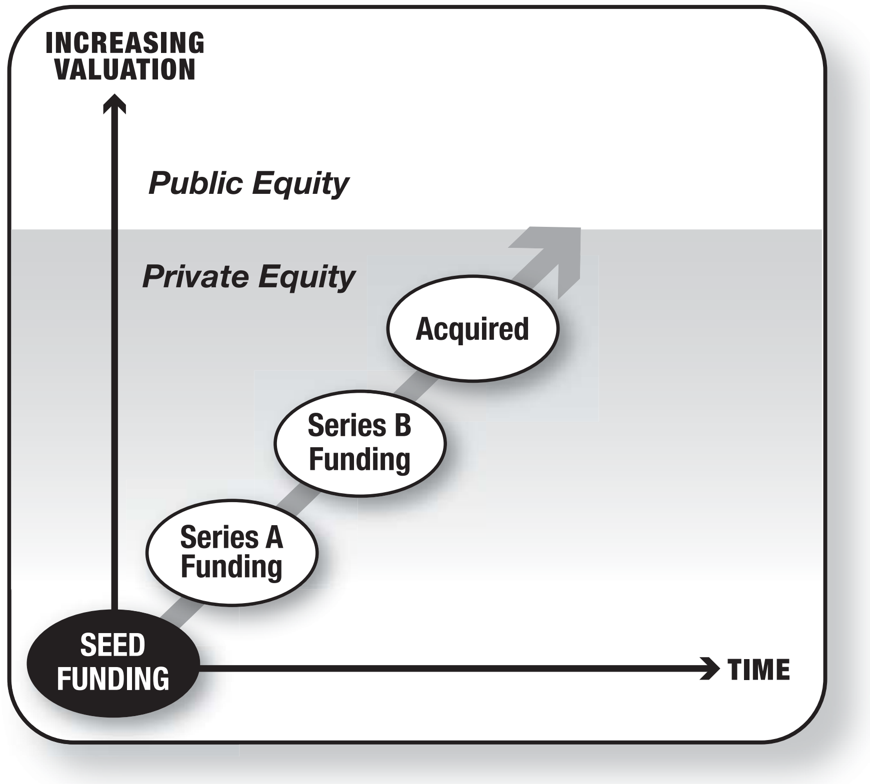

Figure 1-2. Strategic Entrepreneurism Focuses a Startup into Being Acquired Early in its Life

On July 1, 2008, the National Venture Capital Association reported that in the second quarter of 2008, not a single venture-backed company staged an initial public offering, the first time this had occurred in 30 years.

The length of time that a venture-backed company goes from founding to IPO is now 8.6 years, which hit a 27-year high in 2007.

In considering the value of a company, you must examine the investors' returns as a function of time and value, not just value. $1.00 invested for 8.6 years must become $2.30 just to get an approximate 10% compounded return to give a nominal profit for investors. $1.00 must become $4.80 after 8.6 years for a compounded 20% return that makes a company profitable to most venture capitalists.

So the math is pushing venture capitalists to swing for the fences in every way, and yet the fence is now out of reach (no IPOs). As a result, most venture-backed companies are doomed to fail or stagger along, returning a minimal, if any, return on an initial investment. Clearly, there must be a better way to build a business.

WHAT YOU'LL LEARN FROM THIS BOOK

There is no single "right" way to start up a company. However, from my experience and the experience of others, I've learned that there are general guidelines that can improve your chances of success. Think of these guidelines like markings on a road. You don't have to follow traffic lanes to get where you want to go, but doing so increases your chances that you'll get there without wiping out in the process. Likewise, the guidelines in this book won't guarantee you success as an entrepreneur, but they can steer you away from common and easily avoidable pitfalls that could derail your company from becoming the success that it deserves.

While there are plenty of books that explain the technical details of starting a company, there are far fewer books that focus on how to make the correct strategic decisions about starting a company in the first place.

The difference between this book and others is that I'm laying out the new rules for Strategic Entrepreneurism that helped me to start up three companies and succeed with two of them. Some of my ideas may seem controversial and even counterintuitive. But keep an open mind and I'll show you why these ideas work.

If you're thinking about starting up a company, my ideas can show you how to maximize your chance of success. If you're currently running a company, my ideas may help answer questions about why your company isn't profitable or may be struggling against its competitors.

Nobody can guarantee success, but Strategic Entrepreneurism can focus your efforts and steer you in the right direction toward making your company profitable in the shortest amount of time possible. Although I can't guarantee your company will become the next MySpace or Google, I can guarantee that my ideas will make you think about your company from a different point of view, and sometimes having the right perspective can keep you on the right side of the fine line between failure and success.