

Module 1. The Entrepreneurial Activity

Unit 1.1 Innovation and the Entrepreneurial Process

1.1.1 Concept of Entrepreneurial Process

To start this journey, we believe that it is important for every entrepreneur to know the different stages a venture goes through, from the moment the idea arises until it is operating in the market.

The following stages can be identified in the entrepreneurial process:

- 1) Ideation.
- 2) Development of the minimum viable product and validation.
- 3) Escalation and growth.
- 4) Constant innovation.

Stage 1: Ideation

At this stage, the entrepreneur and their team start working on the idea, analysing different perspectives and versions, exploring, researching and working on the vision (sometimes without knowing what they are doing). It is important at this stage to validate the concept with potential clients and learn as much as possible about the industry where the project will be developed. Ideas sometimes arise from the context of the entrepreneur and, therefore, they already know about the topic from the beginning. However, this can be counterproductive if they assume too much without validating.

Other ways to come up with ideas

The phenomenon of copycat—or action of copying business ideas that already exist and are working in some other market in the world— is well known within the



entrepreneurial word. Therefore, the team will have to validate if a particular idea and way of doing business can be adapted to the market where they want to launch their startup.

Stage 2: Development of the Minimum Viable Product and Validation

Once the idea has taken shape, the problem has been validated and the best version of the solution has been identified, the process of building the prototype or the minimum viable product begins in order to validate different issues of the business model and the solution with potential customers. This process also emphasizes learning as it is built and validated with clients. The first customers, known as early adopters, begin to appear, ready to test the solution in its beta or prototype version.

Stage 3: Escalation and Growth.

The minimum viable product goes through different stages until it becomes the product or the service to escalate.

In the learning process of the previous stage, enough information was gathered to determine customer segments, the monetization model, communication and distribution channels, and price.

At this stage, the entrepreneur has to focus on growing in quantity and quality of customers, advancing in the development of the product or service as they develop commercial channels.

Other activities to be developed at this stage may include the following:

- Legal constitution of the company.
- Search for funding.
- Employee hiring.

Stage 4: Constant Innovation

In the entrepreneurial world in which we live today, it is difficult to consider a company as a *consolidated company*, since, due to the aggressive competitiveness in which businesses develop, constant innovation is a necessity rather than an option. That's why large companies like Google, Facebook or Amazon should continue to innovate in different ways to remain market leaders. Later on, we will see different strategies to achieve this.



The entrepreneurial process is not as linear as it is presented and many of the stages and activities overlap as the project progresses.

Initially, it is the founding partners of the startup or the entrepreneur themselves (in the case of a sole founding partner) who carries out all the activities simultaneously.

1.1.2 Business Opportunities

There are basically two types of entrepreneurs: opportunity entrepreneurs and necessity entrepreneurs. The content of this course can be used by either of them.

- Necessity entrepreneurs are those who need to undertake a venture for economic or subsistence reasons. They quickly find an opportunity to generate income through self-employment or entrepreneurship, which can grow or simply be a one-man business.
- Opportunity entrepreneurs are those who wish to undertake a venture and choose it as a life option. Therefore, they look for opportunities until they find the one they are most attracted to or passionate about in order to start their project.

Most of the time one starts a business because an idea occurred to them from the context in which they are immersed or from a particular situation. Serial entrepreneurs are those who detect opportunities or unsolved needs in the market and design solutions.

However, the initial idea that comes up does not always end up being their final version; in fact, it almost never is. Every idea goes through a process of transformation until it finds its final version to go into production. Many entrepreneurs carry out this process in an intuitive way, but not necessarily in a systematized way, and this is how many ideas fail or find no market, since they do not solve a key problem for their clients or the solution is not the most adequate for the problem.

1.1.3 The Entrepreneurial Process

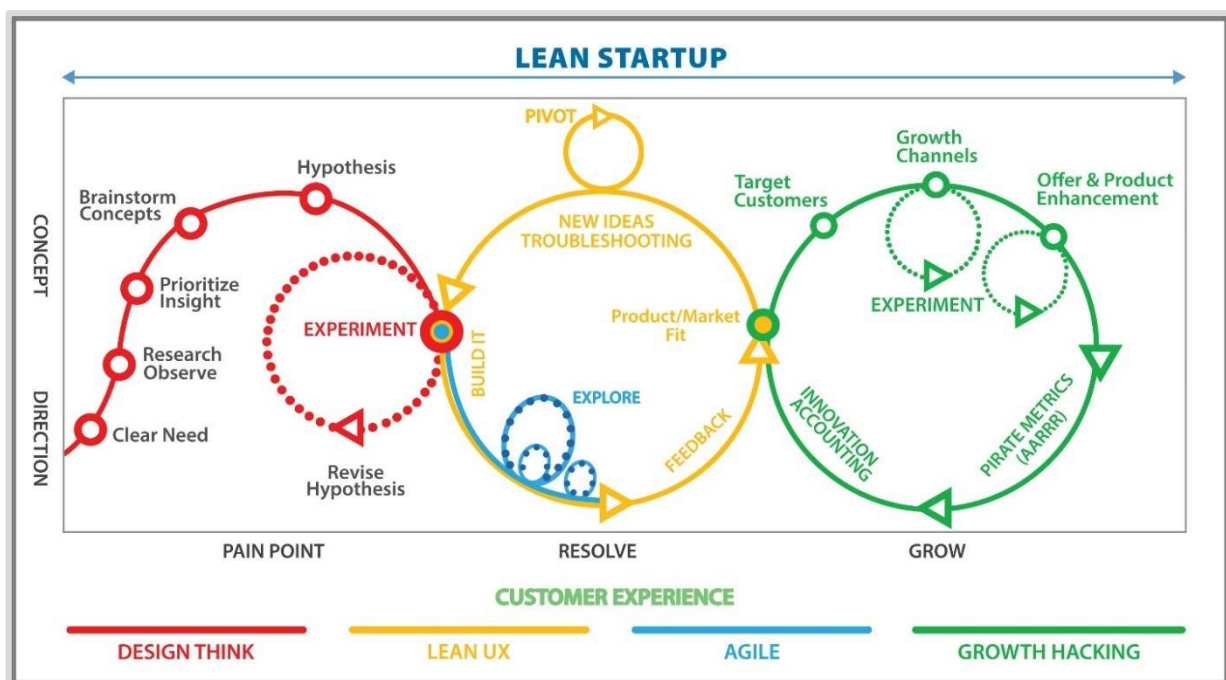
The first theories and methodologies for the development of startups and ventures began to be developed in the Anglo-Saxon and European markets.



The process that we present below begins with a stage of design thinking—a methodology that seeks to empathize with the potential client. You have two options:

- 1) From the idea you found, you can start the path of empathy with the client to discover if the problem you detected is really the most important for them and, from there, redesign your solution.
- 2) If you didn't find an idea, you have to first define the sector in which you would like to work and start interviewing people in those industries to learn more and acquire information, so you can then define the problem to work on and start designing the solution. In these conversations before you present your idea, it is essential to ask questions and get to know the client better. Learning about these issues may help you later on to develop your business model.

Figure 1: Innovation methodology scheme



Source: Incutex, 2017.

Once you have defined the idea based on validated learning from conversations with potential customers, the prototype design stage begins in order to validate the solution, receive feedback from your customers and continue refining your proposal.

At this stage the exploration is generative, since you must generate alternatives so as to find the best, in broad terms, and then define and polish up the details. The objective



here is to find the fit between the customer's problem and the proposed solution, or problem/solution fit, as it is called.

Continuing in this process, lean startup and design thinking begin to meet and the best of both worlds emerges. As you test the prototypes and validate them with customers, you can determine hypotheses and develop specific experiments and tests to validate with customers. From there, you can start validating other aspects of the business model, such as communication channels, price, key allies, among others. During this process, your project is likely to undergo several iterations (small modifications based on validated learning), and you can also choose to pivot (make major changes to the business model).

An agile management and a dynamic team are essential to this initial stage. This stage of the process may take several months or even a year, until you find the fit between the product/service you designed and a large enough potential market. This process also takes time and is part of the pivot and iteration stages. Later on, we will deal with the way to detect if you have achieved the product/market fit.

As the different stages overlap while you look for the product/market fit, you grow in number of customers and you are in a growth stage. Therefore, you start with customer acquisition and retention strategies. Thus, you test different marketing strategies, sales speech, communication channels, pricing strategies, promotions and referral programs, among others.

The Growth Hacking stage shown at the end of the graph refers to a technique of growth in sales and number of customers that has become popular in recent years.

Growth Hacking is a trend that encompasses processes, programming and market strategies, and it began to be adapted in startups to maximize their growth by increasing the number of users with a minimum investment and effort. However, many of the techniques can be applied to any business regardless of size or line of business. They are generally highly creative techniques with a low budget, fast implementation and high impact.

Many projects remain in the last stage of the search of growth for several years requiring funding sources to develop their business strategies. Through our methodology, we seek to enable entrepreneurs to make the most of the capital they have and grow as organically as possible through strategic alliances and the development of low-cost, long-range commercial channels.



There are also cases in which some entrepreneurs have the opportunity of selling their company, or they decide to do so, to a potential investor or some corporation that wants to acquire it or simply continue growing at a stable rate, but always innovating with new products and technology so as not to be removed from the place they have reached in the market.

1.1.4 Beating Competition through Innovation

In the book *Zero to One: Notes on Startups, or How to Build the Future*, Peter Thiel, co-founder of PayPal, raises the question: what valuable company is nobody building? What is interesting about this question is the difference between creating value and knowing how to capture it.

Many companies are good at creating value, but not at capturing it. This means that a company can be very good at delivering value at their clients through their services and products, but without a business model that allows capturing the return of that value to the customers, i.e. revenue; and, without a structure to scale up without increasing fixed costs, its growth will be strangled. That's why the margin the business leaves behind is as important as the net income.

When Thiel talks about monopoly, he is referring to a company that is so good at what it does that no other company can offer a close substitute. Google is a good example, because it does not have search engine competitors since the year 2000.

Thiel's advice to differentiate yourself from the competition is not to create an undifferentiated commodity business, that is, if you are going to have a business that sells something that is considered a commodity, you have to have a clear differentiator so as to avoid competition; otherwise, you have to create something totally different from a commodity.

Besides being leaders in their market, monopolies have the benefit of staying that way as they can afford long-term thinking unlike a business that is in a market made up of existing industries with high competition, worried all the time about margins without being able to afford long-term thinking about the future. This is when the monopoly gets an even bigger advantage than its competitors.

It's like a vicious circle. According to Thiel (2014), monopolies drive progress because they promise years of monopoly profits which provide a powerful incentive to innovate.



“Then monopolies can keep innovating because profits enable them to make long-term plans and to finance the ambitious research projects that firms locked in competition can’t dream of” (Thiel, 2014 p. 487).

According to Thiel (2014), each monopoly is unique, but there are characteristics and patterns that allow identifying them:

Network Effects.

Economies of Scale.

Branding.

Proprietary Technology.

The last point is one of the most difficult characteristics to achieve, but one of the most valuable, since, once reached, it is almost impossible to replicate by the competition. Approximately, Thiel (2014) states that a proprietary technology has to be at least 10 times better than, in some important respect, its closest substitute so as to have a real competitive advantage.

Examples:

- **PayPal:** made buying and selling on eBay at least 10 times better.
- **Amazon:** 10 times more books than any other library.
- **Quirky:** 10 times faster in the development of products (consumer goods).
- **Valve:** 30 times more market engagement per employee.

These features can also be applied to design, such as it is the case of Apple with its iPad, which popularized the use of tablets. However, the case of design is more difficult to measure.

These are cases of exponential organizations which main characteristic is to have a performance 10 times better than the rest and other qualities that differentiate them, such as the massive and transforming purpose by which they are governed.

Network Effects

What generates network effects is that, as more people use it, products become more useful. Such is the case of platforms like Uber, Airbnb or Wallapop.

Part of the trick with network effects is that the product or service must be valuable even to its first users, without having to wait for the network to grow; otherwise, there is



a risk of failure. Even businesses which differentiate themselves by their network effects, according to Thiel (2014), must start with specifically small markets so as to be able to validate and then escalate massively. For example, Facebook started with Harvard students.

The other part of the trick is that these businesses which are differentiated by their network effects are initially so small that they often do not even appear to be business opportunities at all.

Economies of Scale

According to Thiel (2014), a monopoly gets stronger as it gets bigger, since the fixed costs that support the product or service can be better spread out as sales increase. Software startups are a clear example of how economies of scale can be enjoyed considering that the marginal cost of producing another copy of the product or opening another user account is close to zero.

Service based business, especially personal or customized, are difficult to turn into a monopoly. For example, Thiel (2014) describes the case of a yoga studio where you can only serve a limited number of clients. You can expand and grow, but your income will grow in similar proportion to your fixed costs. However, if you could somehow give online yoga classes, through a website, an application or simply Youtube, your economies of scale would be activated.

Branding

Building and developing a powerful brand, according to Thiel (2014), is an excellent way to claim a monopoly. An example that Thiel (2014) highlights is the case of Apple which has managed to build a global and powerful brand completely: on the first hand, because of its purpose (later on, we will develop Simon Sinek's golden circles theory), and, on the other hand, because of the products it develops, the advertising campaigns, the positioning of premium products and the empathy with the user when connecting emotionally.

Basically, Apple generates fans and followers capable of camping out three days in a row outside one of its stores to buy the latest iPhone: that's the power of the brand. However, Thiel (2014) states that starting with the brand first instead of a good substance from behind can be very dangerous. Therefore, it is important to lay the foundation first and, from there, build.

Unit 1.2 Concept of Startup

1.2.1 What is a Startup?

Steve Blank, in his book *The Startup Owner's Manual*, defines startup as “a temporary organization designed to search for a repeatable and scalable business mode, which can be repeated” (2013, p. 24).

Likewise, Eric Ries expresses “a startup is a human institution designed to deliver innovative products or services under conditions of extreme uncertainty” (2013, p.26). In that line, he also states the following:

The goal of a startup is to figure out the right thing to build, what customers want and will pay for, as quickly as possible. In other words, the Lean Startup method is a new way of looking at the development of innovative products that emphasizes fast iteration and customer insight, a huge vision, and great ambition, all at the same time. (Ries, 2013, p. 21).

The concept of startup has expanded to any type of venture, especially in the technology sector. Generally, a new startup entails conditions of uncertainty, especially if it proposes an innovative business model. The goal is always to find a model that can be repeated and scaled, but many startups are transformed into SMEs (micro, small and medium-sized ventures) in this scope of growth, and very few evolve into large corporations, not to mention those that die in the attempt.

Something that is a trend in the world is the link between startups and corporations through processes called *open innovation* or *technology transfer*.

On the one hand, large consolidated companies are running successful business models with difficulties in creating new ones due to their large structures, their bureaucracy, the focus on growth objectives of that proven model, and, of course, due to their fear of failure and the lack of an innovation culture.

On the other hand, startups and ventures—small, dynamic and very flexible structures—are able to detect opportunities and design innovative solutions that can be scaled. This is where these two worlds meet generating benefits for both and new opportunities for the markets.



Within FC Barcelona, the Barça Innovation Hub project promotes recurrent collaboration with startups from all departments of the club. Under a product and service co-development program, startups in the sports sector work with club employees to improve or create new solutions that fit the needs of the club and the market.

1.2.2 Basic Principles for Developing a Startup

Eric Ries (2013) presents the five principles of this method, which will be developed below.

- 1)** Entrepreneurs are everywhere: This means that this method can work in any size company, sector or activity.
- 2)** Entrepreneurship is a certain form of management: Taking into account that a startup is an institution, it requires a kind of management specifically geared to a context of extreme uncertainty.
- 3)** Validated learning: Startups exist not just to make stuff, make money, or even serve customers. They exist to “learn” how to build a sustainable business.
- 4)** Build – Measure – Learn: The fundamental activity of a startup is to turn ideas into products, measure how costumers respond and learn when to pivot or persevere.
- 5)** Innovation accounting: To improve entrepreneurial outcomes and hold innovators accountable, we need to focus on the boring stuff: how to measure progress, how to set up milestones and how to prioritize work. This requires a new kind of accounting for startups and the people who hold them accountable. (Ries, 2013, pp. 13-14).

As an entrepreneur, you must put in extra effort and be rigorous with your measures and actions. If numbers are not among your strengths, partner with someone for whom they are one.

Another key principle that emerges from point 2 is to focus on the core processes of the startup. Today, successful organizations follow this practice and achieve the outsourcing of non-core processes, whenever possible with a variable and not fixed cost so as not to strangle growth. This is also another of the qualities of the exponential organizations mentioned above.

Most of the results obtained depend more on perseverance than on any other factor.

The CEO (chief executive officer) has to think outside the box. The manager has to make sure that things happen and that the objectives are met. At the beginning of a startup, the entrepreneur fulfils both roles, which is why this job is so challenging. This is because a person's greatest challenge is to know how to handle contingencies and their ability to plan for the long and medium term. It is usual to have one of the two qualities; it is difficult to have or develop both.

1.2.3 Why Do Startups Fail?

Continuing with Eric Ries' perspective, in response to this question the author lists some problems that would cause this situation:

- **Problem 1 – Allure of a good plan, a solid strategy and a thorough market research.** There is a tendency to apply them to startups, but this doesn't work because they operate with too much uncertainty and without historical data to predict the future.
- **Problem 2 – Chaos emerges as a response to lack of management.** Clearly, startups need management to take care of very valuable resources. "Most people think of the management process as boring and dull, whereas startups are dynamic and exciting. But what is actually exciting is to see startups succeed and change the world." (Ries, 2013, p. 14).

The following motives may arise:

- They do not create something people love.
- They have no customers or not enough customers to use and pay for their products and services.
- They run out of capital to continue scaling the business model. This is linked to customer growth and loyalty, as they cannot generate enough revenue from the sale of their products or services because they did not create something that people really need and they did not solve a need so that the customer pays for it.

The team is fundamental: 80% of the success of a startup depends on the team that carries it out. The idea may not be good, but if the team is not good, the project fails. For a team to be considered good, it has to meet with half plus one of these characteristics:

- Having founding partners who have a full-time availability.



- Knowing each other from previous projects and having worked together.
- Having vast experience in the sector in which the startup is developed.
- Have an expert technology partner.
- Having experience in corporate sales or digital marketing.
- Having previously failed in other projects or having previously undertaken a venture on their own.
- Not growing fast enough when they should, and being outpaced by later startups with a faster rate of growth
- Having management and communication problems. When they turn into companies (growth stage), the skills needed to lead the project are different from those needed to create the startup.

In some cases, the entrepreneur does not have all the skills and, therefore, acquires them along the way, on his own, and with the help of mentors and guides.

In some other cases, the entrepreneur dedicates himself to what he likes, product development, customer sales, strategic alliances, among others, and lets an experienced manager lead the daily operations of the company. In order to do this, the entrepreneur must first recognize their weaknesses, and then have their ego flexible enough to step aside. Sometimes, the startup investors are who force these changes.



References

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