

Knowledge-Based Entrepreneurship: Analyzing A Start-Up

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ABSTRACT

Successful entrepreneurial companies are those that realize the benefit technology can provide before the competition does. Additionally, there are intangible benefits for companies that utilize technology before their competitors. While the competition is attempting to catch up, companies can build off of their current technology and continue to out-distance themselves from the competition. Although there are many positive and negative forces associated with entrepreneurial start-ups today, there exists a multitude of opportunities for entrepreneurialism to grow. A start-up company's staff located in Pittsburgh was interviewed for their insights and several strategies were examined in this paper.

INTRODUCTION

As Chell (2000) and Keogh (2002) noted, at present the developed world is in the throws of an information revolution. Thus, this information revolution heralds change and vast opportunities for entrepreneurialism and enterprise in a truly global context. Starting an entrepreneurial company can be risky and statistics show that only 50% of startups make it past the four-year mark, as evident from Figure 1. In addition, in today's changing world it is only getting harder for small businesses to survive. Too many investors got burnt on the dot.com bust and as a result, investors and entrepreneurs alike have become extremely cautious. This coupled with the September 11, 2001 terrorist attacks; entrepreneurs are finding less and less funding opportunities ("Small business optimism ..." 2001). In addition, there are many innovations occurring that are encouraging entrepreneurial start-up.

The Information Revolution has re-invented manufacturing processes similar to the way Henry Ford transcended the processes of his era with the development of the assembly line. "Technology enables greater speed, precision, quality, agility and collaboration. Companies will use information, analysis and real-time communication to close the gap between design and production" (Daly, 1999, p. 29). Today's technology has decreased project time, increased quality and accuracy, and provided companies with a type of dynamic processing that they once thought of as unimaginable. "Manufacturers will move away from mass production and begin producing customized products in response to customer demand" (Daly, p. 29). If you build it, they will come will eventually be the driving force behind consumer demand because the technology will exist to allow for this demand and consumers will know this. Dell Computer has already implemented this production mentality where customers design their own computer based off of hundreds of possible scenarios. Once the order is placed, Dell has instituted the technological capability where the customer can track every single order from start to finish. Even though customers did not ask for this benefit, Dell knew that this would provide their company with a sustainable competitive advantage over their competitors.

"All companies must look at the effect that new technologies will have on them or else they won't be ready to adopt these when business and competition demand that they do" (Daly, 1999, p. 30). Successful companies are those that realize the benefit technology can provide before the competition does. Additionally, there are intangible benefits for companies that utilize technology before their competitors. While the competition is attempting to catch up, companies can build off of their current technology and continue to out-distance themselves from the competition.

There is an important concept that an entrepreneurial company’s must realize and that is do not implement technology for technology’s sake. There must be a sustainable competitive benefit to the technology, either an actual benefit or a perceived benefit. If the available technology does not have any benefit to one’s organization, then there is no need to sink the capital into the implementing this technology. This places a heavy burden on a company’s IT department because they need to fully understand what benefits this technology offers. Moreover, they need to communicate these benefits to those managers that are ultimately responsible for deciding whether or not to implement this technology. Failure to see both the benefits and repercussions of technology can rapidly lead to a loss in market share that may not be recoverable.

Analysis Of An Entrepreneurial Start-Up

We will specifically examine a local Pittsburgh startup formed by employees of a high technology company, whose identity will be concealed for the purpose of frankness of the comments received from the employees interviewed in the entrepreneurial company that left to form a real company that will be masked for the same reasons. Several employees from this high technology company resigned from their jobs and started a company to be referred to as Entrepreneurial Company-XYZ. At the time of this study, Entrepreneurial Company-XYZ is only six months old and is in direct competition with Armstrong Laser Technology. Building upon this knowledge, and interviews of several employees’ experiences, and the management strategies, we will attempt to outline some possible reasons why startups have so many problems getting off the ground. We will use these tools and the history of Entrepreneurial Company-XYZ to try to predict its fate.

Figure 1: The Cost Of Failure Of Entrepreneurial Company Can Be Risky Business

PROBABILITY OF SUCCESS & FAILURE		FINANCIAL STATUS & NUMBER OF YEARS IN OPERATION	
Rate Of Survival For New Businesses (<500 Employees)		Profitability (1999)	
Closure within 2 years of start-up	24.0%	40% of Startups Claim Profitability	
Closure within 4 years of start-up	50.4%	Yes	41%
Closure within 6 years of start-up	60.5%	No	59%
Characteristics Of Closures		Revenues (1999)	
Company sold or owner decided to shut down	57.4%	None	21%
Company owed money to creditors	42.6%	< \$100,000	26%
Probabilities For:		\$100,000 - \$249,000	16%
Mergers, Liquidations	30.0%	\$250,000 - \$499,000	8%
Bankruptcies	60.0%	\$500,000 - \$999,000	8%
IPO (initial public offering)	9.7%	\$1 million - \$1.9 million	8%
Time Taken For A Start-Up To Get To An IPO	5 Years	\$2.0 million - \$4.9 million	6%
		>>\$5 million	6%
		Avg. # of Years in Operation	2.8

Source: <http://www.ktec.com>.

Dealing With The Myriad Of Issues In An Entrepreneurial Company Start-Up

To begin, anyone who is entering the world of entrepreneurship should ask themselves at least these three questions; “Am I the right person for the job?” “Why am I entering the entrepreneur arena?” “Is there a market for the product/service?” Dealing with the first question, it is obvious that not everyone is professional qualified to run his/her own business. An entrepreneur must be willing to multi-task, and when needed must be willing to delegate work. Pfeffer and Veiga (1999) make the argument that a major dilemma facing managers today is the tendency to

spread them too thin. If an entrepreneur cannot delegate work they will become overwhelmed and items that need to be addressed will fall by the wayside. For example, the president of Entrepreneurial Company-XYZ refused to delegate money matters to the facilities engineer (interviewed for this research study), whom has more financial experience from a previous job. As a result, a phone bill was late in getting paid, and the registration deadline for an important conference was missed. When issues like this arise, it is a sure sign that management is not properly delegating the work. A large sacrifice, both financially and emotionally, must be made when seeking to open an entrepreneurial business. Acknowledging these barriers in the beginning and developing a strategy to overcome them can save all those involved a great deal of stress.

After answering whether you are the right person to become an entrepreneur, the next question posed should be “Why am I entering the entrepreneur arena?” Too many people start new businesses for the wrong reasons. Sure, everyone would like to be independently wealthy, but starting a business does not guarantee success. Entrepreneurial Company-XYZs current president formerly worked as a Quality Manager for the previous high technology company that several employees left to go with the current entrepreneurial venture. Subsequently, he was fired for attempting to buy the company. As a result of his termination, a former employee transferred his desire for revenge into his motivation to directly compete with this previous high technology company in the form of employment with Entrepreneurial Company-XYZ. More traditionally accepted reasons to start a company include offering a superior product, uncovering an untapped market niche, or introducing a patented new idea. Revenge is not usually a component of sound business decisions.

The final question before taking the leap into entrepreneurship should be, “Is there a market for the product/service?” All too often, potential entrepreneurs get an idea in their heads and become convinced that everyone sees the world as they do. Most importantly, an entrepreneur must do preliminary market research to determine if the market will accept the product/service he or she plans to offer. Having a solid understanding of the market he or she is entering and knowing that a potential customer base exists is the first step in meeting future customer needs. Taking this crucial first step can alleviate the possibility of great financial and personal loss. Starting a new business does not mandate an advanced degree (or any degree at all); it simply requires having the business sense to acknowledge and truthfully answer the three key questions previously outlined.

MAJOR ISSUES ASSOCIATED WITH ENTREPRENEURSHIP

Issues Associated With Honesty And Credibility

Throughout works by Quinn, Anderson, and Finkelstein (1996a, 1996b), Porter (1996, 1999) and Roberts, Kossek, and Ozeki (1998) have indicated that issues associated with honesty and credibility are two of the most important elements in running an entrepreneurial business. When dealing with a startup company these two factors are magnified to an even greater degree. Colvin (1997) quoted a former Shell executive who stated, “...without very high trust you will never get maximization of brain potential” (p.300). This statement is even more significant when relating to the success to of a startup. In the initial phases of a startup company, honesty is key. Trust and honesty become the foundation on which the motivation and creativity that is so critical to the initial launch of a startup organization is built. As such, there are four things that entrepreneurs need to keep in mind:

1. Be honest with your investors and potential investors;
2. Be honest with your employees;
3. Be honest with your customers and potential; and,
4. Most importantly, be honest with yourself

Once violated, the trust in a relationship is nearly impossible to rebuild. This can cost a new company investors and customers, both of which are essential elements of success. Credibility is a valuable tool in all phases of a business. It gives you the ability to attract and hire qualified personnel, to negotiate better contracts, and to be recognized as a sound investment for future capital. Once credibility is lost, all aspects of the business will suffer. Entrepreneurial Company-XYZ has lost credibility with its employees. The employees were sold on promises of

superior benefits, additional stock options, and aggressive deadlines. To date, none of these promises have been met and morale has been extensively damaged.

The Importance Of Sound Strategy And Financial Planning

In a startup company, one of the most important strategic aspects of planning to be completed prior to hiring any additional personnel is to create short-and long-term financial forecasts based on existing and predicted capital. Porter (1996) emphasizes the need for a company to build strategy around the industry's forces while others suggest that companies need to identify its core competencies and build strategy around them. Operational effectiveness can be a source of short-run competitive advantage, in the long run it's nowhere near sufficient" (Surowiecki, 1999, p. 2). Companies will obviously gain an advantage over the competition if they can produce a higher quality product at a lower cost, but this will not solidify their position in the market for very long. Companies should position themselves differently from their competitors by figuring out where the opportunities in the industry lie. Hence, "strategy is choosing to run a different race because it's the one you have set yourself up to win" (Surowiecki, p. 2). By putting forth the effort to develop a product niche or focus on an untapped market, companies are placing themselves in a position where the opportunity for success is far greater than operational effectiveness or total quality management. However, there are greater risks associated with this strategic focus, so companies must make sure they have the resources to succeed and potentially fail.

"Clusters are those regions where competitors congregate and quickly develop the region into a product or service specific mini-city" (Surowiecki, 1999, p. 3). Pittsburgh is a good example of a financial services/banking cluster with the successful corporations of PNC, Mellon, National City and Dollar Bank. "These clusters show how the benefits of proximity to your competitors outweigh the costs because it is easier to pick up on trends, employees from around the world gravitate to the cluster, and there are improvements in productivity" (Surowiecki, p. 3). Suppliers will soon open up distribution centers closer to clusters in order to focus on higher service standards and decreased shipping costs. Furthermore, the talent pool for potential job candidates is relatively worldwide because clusters will attract global candidates because of the advantage of more than one player in the geographic market. More companies can lead to rapid advancement with regards to both intellectual growth and an increased salary because the candidate can bounce back and forth between companies because there are more opportunities.

"Porter does not feel that time-based competition, total quality management, and re-engineering are favorable sources of strategy because they only represent incremental changes in execution and quality" (Surowiecki, p. 2). These incremental changes are strategically important, especially if an entrepreneurial company can remain consistently competitive. There is too much uncertainty in today's internal and external environment, so companies must be able to maintain pace with competition and consumers in order to survive. Incremental changes are not the answer to a sustainable competitive advantage, but smooth transitioning is a competitive advantage that consumers will realize when they purchase a company's product or service on a repetitive basis.

Once it is established that a sustainable competitive advantage can be strategically maintain and the financial capital is in place to stay in business for an extended period of time before profits are generated, employees can be brought on. One must consider all of the financial resources that are available to emerging businesses. As an entrepreneur, you must be willing to consider all of the possible paths, as it is important to explore different possibilities when raising capital. Survey potential lending institutions for small business loan opportunities while keeping your eyes open for investment angels. Research venture capitalists and seek out private investors. All of this should be done once you have evaluated your own financial situation. When done simultaneously, entrepreneurs can begin their business with an interesting mix of capital. Traditionally, utilizing a combination of investment sources will improve the company's possibility of success.

With potential success also comes potential risk. Consequently, this was not the situation Entrepreneurial Company-XYZ faced. In fact, just the opposite transpired. Entrepreneurial Company-XYZs president emptied his bank account, closed his retirement fund, and maximized the balance on his credit cards. However, what he failed to do was institute the long-term vision imperative to survival. At the time of this study, Entrepreneurial Company-XYZ is currently waiting on capital from a bank via a SBA (Small Business Association) guaranteed loan. Instead of

initially forecasting cash flows and budgeting for future salaries, Entrepreneurial Company-XYZ hastily hired a number of employees. As a result, the president has been forced to give up much more interest in the company than he originally intended. He originally wanted to maintain 65% ownership of the company, however due to poor planning he will more than likely have to settle for 20% causing him to lose majority ownership. Additionally, the president of Entrepreneurial Company-XYZ did not pursue several funding avenues at once. Rather he focused on only one opportunity at a time, letting others slip away. After one source of funding would fall through, the terms of the other possibilities suddenly changed, usually to the detriment of the company

Develop The Basis Of A Business Plan

As with any new venture, direction is a key element to success. As an entrepreneur, you must have a map for your company to follow; and that map is your strategic plan. This is the company scripture and is the first thing that every potential investor will ask for prior to any investment consideration. The strategic plan includes items such as: the business plan, a company summary, a market analysis, goals of your company, and projected financials. Usually the financials are “guesstimates,” however you should be prepared to defend your numbers when asked to do so. Most strategists will admitted that even after their companies were established, they continually updated their business plans and use them as a steering mechanism to direct the company. Strategy is difficult to define and Porter (1996, 1999) addressed several issues that bring strategy to life. There were five direct issues addressed that help define strategy. These issues will help organizations define what they are and what they want to accomplish. These five ideas were: Operational effectiveness is not strategy, strategy rests on unique activities, a sustainable strategic position requires trade-offs, strategic fit drives both competitive advantage and sustainability, and rediscovering strategy is important, especially in entrepreneurial companies.

Within the first four ideas, the Porter (1996) described several areas to focus on. Each of these areas addresses issues within each organization and among its competitors. Once firms are able to discuss and research these issues, a clearer picture will form of where they want to go in their particular market. Operational effectiveness is truly not a part of strategy. Operational effectiveness is part of an ongoing organization. Whether or not an appropriate strategy has been chosen, you need to know how your business is run in order to succeed. This should be the beginning step in creating a working and profitable organization. Once this has been done, you can then move on. The next step is trying to choose unique activities that reflect your particular products or company image. When companies are unique, they create a position within the market that they hold with their customers. Companies need to make or market their products in such a way that sets them apart from the competition. No matter how much this is said, it is always a difficult task.

After an entrepreneurial company has created a unique activity or activities, they need to address this with the rest of their company. If that is the position that they want to hold, they may need to make trade-offs with other product line or other organizations within the larger scope of the firm. Once firms have defined their unique activities and choose their position in the market and make their trade-offs, they are ready to choose the fit that drives both their competitive advantage and sustainability. This is the true final test to completing your strategy. After the completion of this stage, firms are able to become leaders in their businesses. Lieber (1998) also suggested that strategies should be build around attributes of employee loyalty. Lieber’s three factors included establishing an internal sense of purpose motivates employees to meet overall organizational goals. A company’s business plan is the first place that you can begin developing that purpose and company direction.

Aside from the business plan, other key elements must be in place for a business to run day-to-day operations successfully. An accounting system, proper payroll procedures, and compliance with federal and state employment laws are a just a few of the considerations to be made. Entrepreneurial Company-XYZ was fined for reporting taxes late for the last quarter because the president of the company did not understand how to properly report them. When asked about the 401K plan that was presented as part of the compensation package, employees were told, “you know you can open your own IRA account just as easily with whomever you want.” That was not exactly what employees wanted to hear. Additional benefits such as medical, dental, visions, and paid time off, are all part of what attracts and retains quality employees. In today’s market, salary and stock options are not enough to lure employees into an unfamiliar and challenging environment.

Understanding The Potential Leveraging Of Knowledge Management Strategies

As discussed in the last section, upper management has to deal with the interacting issues of reward, cultural, and technological dynamics within the firm. Any entrepreneurial start-up has a real opportunity to redefine their purpose and add significant impact in their value chain to their customers through the proper implementation of knowledge management principles. However, they must specifically deal with the emerging challenges ahead. For example, should they "shrink-wrap" their system and marketing to other consulting firms? Another important question is "It was fine to say that people would be rewarded for using knowledge base but what would really make this happen?" It is clear that using knowledge-management effectively, a number of new habits and connections between the reward structure at Integral and how consultants were measured in the past needs to be re-examined. It is one thing to encourage sharing of information among consultants at Integral, but since their rewards were based on their individual intellectual capital contributed to the company, incentives must be in place to encourage knowledge workers to share their intellectual capital with others. The current reward system is holistically inadequate and needs to be significantly redesigned. Unfortunately, there is no consensus by the principals at Integral on how to achieve this transformation in rewards system. Management at Integral are simply not willing to give up the tracking and centralized control they enjoyed under one old system. True sharing of information in a knowledge market environment may mean that the various knowledge bases have no attribution the magnitude of people who contributed to its creation. As one manager stated "We are creating a class society of folks who have and haven't contributed to the intellectual capital of the firm" (p. C-489).

Also, the culture of promoting sharing of knowledge among teams that needs to be enhanced. Personally, it has its roots in the reward system. We essentially pay for what we value, and if Integral wants a culture of sharing of ideas then it needs to develop a reward system that rewards not only creation of information by an individual, but also group sharing and creation of information. The difficult aspect that needs immediate attention is how to motivate employees to contribute to the knowledge bank when the client could not yet be billed for the types of activities. A method of creating value to knowledge bases needs to be developed independent of direct billing of specific customers. As stated by the prevailing opinion: "If I'm rewarded based on new knowledge that I create, why should I use someone else's knowledge?" (p. C-485).

Integral needs to promote contribution in a holistic approach instead of rewarding only individual effort to generate a sharing knowledge culture. People must feel that they are adding value to the firm at a very personal level. The contribution to standardized and dependable solutions will save the firm great expenses, as long as they do not discourage innovation and creativity. The concept of a virtual idea-trading zone, where individuals would be rewarded for the value of their contributions made to the knowledge base, has great potential to keep information from becoming secrets from colleagues. Of course, management must be willing to open in deciding what is of value and what is not of value to the organization. Certainly, the driving force behind knowledge management initiative is the advent of technologies that are capable of formality knowledge gathering.

Conserve Resources And Leverage Them Wisely

One of the biggest mistakes an entrepreneurial company startup can make is to burn through its working capital on unnecessary items. Every expense should be placed under a microscope to determine the value its purchase will add to the company. According to surveyed employees of Entrepreneurial Company-XYZ, the company has been "the poster child for wasting money." The president absolutely needed a \$7,000 display booth to go to a conference in Albuquerque, New Mexico. With flight, lodging, and meals, the trip to Albuquerque was an additional \$1,500. As a result of the conference, the company was out \$6,500. To add insult to injury, the president returned empty handed--not one potential customer, contact, or even a single lead was generated. Now Entrepreneurial Company-XYZ has a new \$7,000 display booth that will be used, maybe, three times a year. In the beginning phases of a startup company, being frugal with money was imperative. Instead of presenting at the conference, the president should have merely attended to gauge its potential future value.

Choosing office/warehouse/production space is another essential element of a startup company. At the time of Entrepreneurial Company-XYZs search for commercial space, local newspapers printed weekly articles featuring numerous commercial landlords who were unable to rent their properties as a result of the economic slump in the Pittsburgh region. Entrepreneurial Company-XYZs president should have taken advantage of this perfect opportunity to get a great deal on an ideal facility in the Pittsburgh region. Instead, the president went to one real estate agent, looked at two or three buildings, and signed the dotted line without exploring all of the possibilities. Now Entrepreneurial Company-XYZ is stuck in a sub-par facility with higher than budgeted lease payments. In Lieber's (1998) article, "Why Employees Love These Companies," Lieber states that another important reason given for employee loyalty is the presence of a company's "knockout" facility for employees' use. The article states that knockout facilities "may be the most persuasive way to tell employees they're valued" (p.73). According to employees of Entrepreneurial Company-XYZ, "the employees have been given a round hole and must fit a square peg into it. The facility the employees are in does not meet their functional needs." Once again, for the perspective of employees, the president demonstrated poor judgment and made a bad money decision at a time when poor decisions absolutely cannot be made.

The Hiring Process

As stated before employees should not be hired before the funding to cover salaries is secured. As an entrepreneur you must be honest to your employees right off the bat regarding all elements of compensation. In most companies, specifically startups, your employees are your only competitive advantage until such time when your product/service is available to the market. Quinn, Anderson, and Finkelstein (1996a) suggested, "...once a company gains a knowledge-based competitive edge, it's difficult for [the] competition to catch up" (p.75). Along the same lines, Colvin (1997) quoted Patrick Harker: "...machines can't give you a competitive advantage. It's all about the people" (p.300). Both of these examples try to express the importance of the employee in today's company structure. Entrepreneurial Company-XYZ has done a good job at hiring the proper employees, but that is not always enough. Having top-of-the line employees in place is only effective if they stay with the company.

Entrepreneurial Company-XYZ has broken another startup rule that some consider taboo. That unwritten rule is hiring relatives ("Keep family out of executive slots." 2002). As an entrepreneur, important decisions need to be made during the setup of the company to help guarantee success. The president decided that he could work with his family so he hired family members to fill some of the available slots. The president's stepson was hired as facilities engineer; his daughter was hired as a secretary; and his wife was hired as a consultant. This idea of hiring relatives was not met with much resistance until the CTO of Entrepreneurial Company-XYZ confronted the facilities engineer regarding his job performance. At that point, the hired consultant (who, if you recall, is the facilities engineer's mother, as well as the president's wife) took exception to this idea and told everyone that the CTO was fired from a previous job due to personnel problems. The CTO went to the president to discuss this matter, and was told that he was wrong for confronting the facilities engineer -- when in fact, he was right. From the perspective of the employees, this soap opera environment can compound the existing issue and in this case, the hierarchy of Entrepreneurial Company-XYZ was totally ignored. Successful entrepreneurship requires that the following points should be considered: (1) have all the money you need up front; (2) have established legal counsel; and (3) avoid business ventures with family members. One of the arguments presented by the speakers is that the introduction of family members into a business setting only complicates an already complex situation. In the example of Entrepreneurial Company-XYZ this clouded the employees' abilities to make the proper business decision as a result of the personal involvement in the situation.

GENERAL CONCLUSIONS AND IMPLICATION TO ENTREPRENEURSHIP

Going back to Lieber's (1998) work, two of three reasons have already been reviewed: knockout facilities and sense of purpose. The third reason is inspiring leadership. Unfortunately, it appears from the interviews of the effected employees, inspiring leadership is one intangible strategic asset that Entrepreneurial Company-XYZ lacks most. If you look at the problems within the company, they read like a laundry list of things not to do in a startup. To review, here are the highlights of Entrepreneurial Company-XYZs problems:

1. The company was opened to seek revenge on a past employer;
2. The president was not honest with, and has lost trust of his employees;
3. The company began hiring before all the capital needed was raised;
4. The company wasted what little capital it had on unnecessary items;
5. The facility is a round hole and Entrepreneurial Company-XYZs process is a square peg;
6. Entrepreneurial Company-XYZ has relatives directly working for each other.

Complete ignorance of basic business knowledge has posed a serious threat to company's sustainability.

The president of Entrepreneurial Company-XYZ and his past poor decisions, as listed above, can be seen as foreshadowing of the company's future. Surprisingly, there is still some possibility that the company could flourish from the interviewed employees' perspective. The president's daughter is returning to college in the fall, which will eliminate some family friction. The product that Entrepreneurial Company-XYZ provides is actually top-of-the line in laser technology. But, if Entrepreneurial Company-XYZ does not achieve success, there will be little question as to where the problems originated as far as the employees interviewed are concerned. As Pfeffer, Hatano, and Santalainen (1995) noted, "...security of employment signals a long-standing commitment by the organization to its workforce" (p.57). With this in mind, the employees of Entrepreneurial Company-XYZ may want to consider seeking alternative employment.

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