CHAPTER 6

The Life Cycle of Entrepreneurship

LEARNING OBJECTIVES

After studying this chapter, the reader will be able to:

- Identify the phases in the development of an entrepreneurial venture from creation to closure
- Analyse the reasons for the high growth of some entrepreneurial ventures
- Analyse the reasons for business closure
- Understand what happens to an enterprise that closes
- Understand what happens to entrepreneurs who close a business
- Appreciate the nature of serial entrepreneurship.

INTRODUCTION

Entrepreneurship is closely associated with new venture creation, one of its key properties identified in Chapters 1 and 2. The idea of entrepreneurship as the 'identification, evaluation and exploitation of an opportunity', itself suggests a focus on the early stages of setting up a new enterprise. Much of the research and literature in entrepreneurship concentrates on this creative and developmental period of entrepreneurial activity. However, the entrepreneurship process encompasses the complete life-span of an enterprise and the career of an entrepreneur. Entrepreneurial ventures mimic the pattern of life on earth in that there is a beginning and there is an end. Businesses open and sooner or later they close. The only question is how long they will survive – at least in their current form. Therefore it is important to consider phases other than the start-up of an entrepreneurial venture, including its closure.

Similarly, individuals undertake entrepreneurial ventures at different stages of their lives and careers. There is also a cycle of entrepreneurship that relates to what the entrepreneur is doing – which may not coincide with what is happening to the enterprise. At one extreme, an enterprise may be thriving but the founding entrepreneur may wish to leave it for a variety of possible reasons; at the other end of the spectrum, the business may fail and close but the founder remains an entrepreneur by starting a new venture. This chapter investigates what typically happens to an enterprise as it develops and declines and also to the entrepreneur as they enter into and exit from an enterprise.

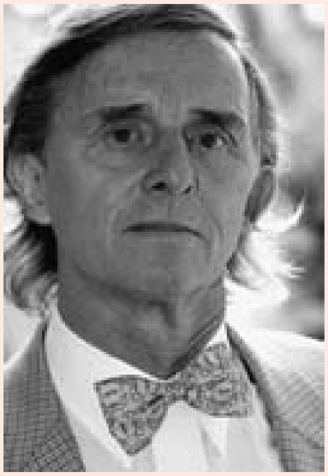
PREVIEW CASE

The successful entrepreneur who studied failure

Christopher Fogg addressed a group of students who were eager to learn from this successful portfolio entrepreneur. Not only had he developed and run his own businesses, he had helped countless others through his enterprise incubators.[1] To the students' surprise, Fogg began by claiming that he had had a string of business failures and that he wanted to talk about these rather than his success stories. He went on to describe ten business ventures he had been involved in that had not achieved their objectives and had closed down. These ranged from Chinese bicycles to 'ball ponds' for children and the sale of used aircraft.

Many entrepreneurs seem keen to talk about their successes. Why do you think Christopher Fogg wanted to talk first about his failures rather than invite the students to emulate his success? Do you think he is unusual in having been involved in several ventures, many of which have not worked out?

(Find out what he said in the case study 'Fogg's Failures' at the end of the chapter.)



Christopher Fogg, a portfolio entrepreneur

6.1 THE LIFE CYCLES OF AN ENTERPRISE

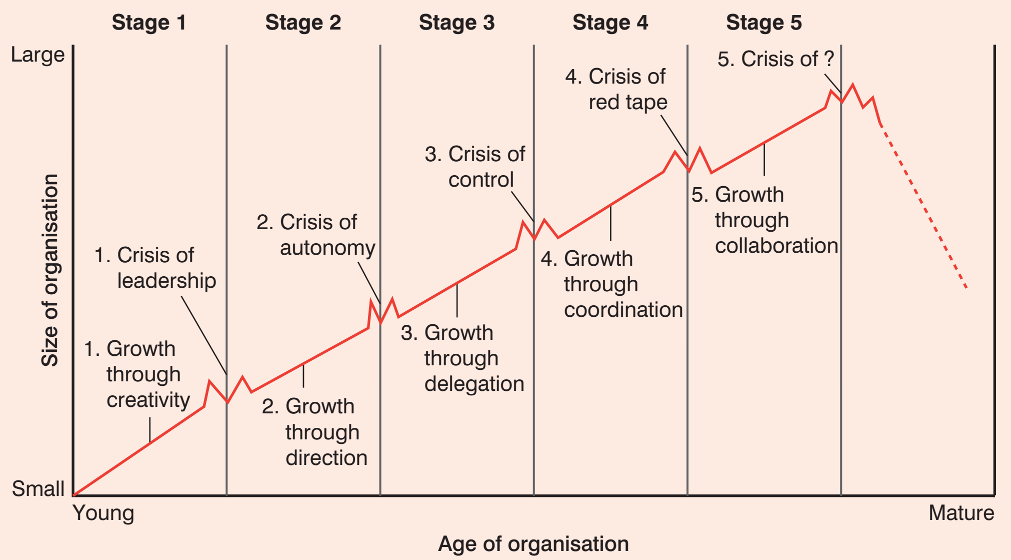
6.1.1 Life Cycle Models

Entrepreneurial ventures evolve over time through various stages from start-up, development and growth through to decline and closure. The enterprise changes its characteristics in each of these stages in a way that often requires different skills, structures and resources to manage them. A number of models – or ways of categorising and predicting these characteristics – have been put forward in order to conceptualise the life cycle of an enterprise from start to finish.

Greiner (1972) developed an early model of evolution and revolution in the growth of an organisation (see Figure 6-1). Greiner proposed that an organisation evolved through various stages but that movement from one stage to another was precipitated by a crisis that led to more revolutionary change. If the firm managed its way through this period it progressed to the next stage. For example, the first stage of 'growth through creativity' leads to a 'crisis of leadership'; once this is resolved the next stage of 'growth through direction' begins. By the fifth stage, a more collaborative management approach emphasises teamwork and matrix style organisational structures, but Greiner was unable to predict what crisis might precipitate the move into yet another phase.

Other models follow Greiner's five-stage approach but with different descriptors for each of the stages. Churchill and Lewis (1983) identified the stages of: existence; survival, success, take-off and maturity. Scott and Bruce (1987) described the five stages as: inception, survival, growth, expansion and maturity. In each of these stages, they suggest that the role of the top manager, the style of management and the organisational structure will change accordingly. Thus the management role moves from 'direct supervision' in stage 1 to 'decentralisation' by stage 5. The organisational structure evolves from 'unstructured' in stage 1 to 'decentralised' by stage 5. In the first stage of 'inception' the management style is assumed to be

FIGURE 6-1 Greiner's model of organisational growth



Source: Greiner, 1972

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'entrepreneurial, individualistic'. By the fourth stage of 'expansion' this has changed to 'professional, administrative' and by the final fifth stage of 'maturity' the style has become that of 'watchdog'.

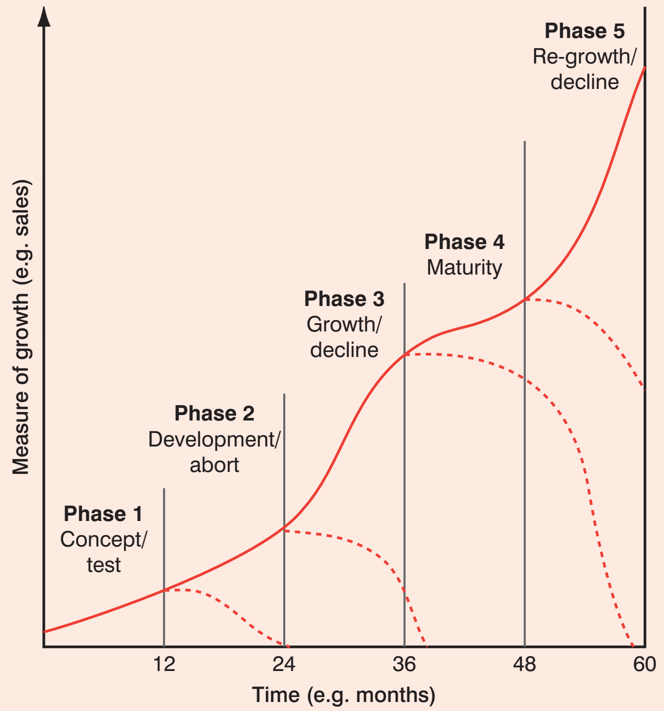
A common feature of these models is that they describe the management style of the entrepreneur and the key functional activities in each phase of development. A composite model by Stokes and Wilson (2006) described the five stages, shown in Figure 6-2, as follows:

- **Stage 1: Concept/test**
  Before a business is launched, it undergoes some form of conception and planning. This may involve a market test or running the business as a part-time operation, before the owner places complete dependence on it. Creative thinking, information gathering and networking are key activities in this stage.

- **Stage 2: Development/abort stage**
  The business is launched and either develops to a viable size, or it is aborted at an early stage. This will depend critically on whether sufficient customers in the marketplace adopt the product or service on offer, hence marketing linked to cash flow management are often the key functional activities. Typically an individual entrepreneur manages the enterprise in this stage largely through their own efforts. This is a particularly vulnerable stage for a business as statistics indicate that it is the smallest and youngest firms that have the highest rates of closure (more on this below in section 6.3).

- **Stage 3: Growth/decline stage**
  Some enterprises that have developed into a viable entity in the marketplace continue their growth quickly or, in some cases, more steadily. Such growth may place strains on the internal structure of the enterprise. The management of internal processes and people are often the critical functions. The one-person entrepreneurial management style may prove inadequate to fully sustain growth. A division of managerial tasks, the recruitment of non-owner-managers and the development of a functionally organised team are often prerequisites to take a business through this phase, without which it may struggle and close.

FIGURE 6-2 **A composite life cycle model**



Source: Figure 7.4 from Small Business Management and Entrepreneurship (2006) David Stokes and Nicholas Wilson (Thomson Learning, London)

- **Stage 4: Maturity**
  Most surviving business go through a period of stability, when growth flattens and the enterprise matures. It may at this stage lose its simple structure of centralised decision-making, use more sophisticated business processes and become more bureaucratic in its procedures. In other words, it takes on some of the characteristics of a larger organisation.

- **Stage 5: Re-growth/decline**
  Once an enterprise has established itself in the marketplace with a competitive advantage over its rivals, profits or external investment may be available to exploit further the successful business model. The so-called 's-curve hypothesis' suggests that such investment may trigger a second period of growth. Without this further period of growth, the maturity stage can turn into stagnation and decline, as competition intensifies from existing rivals or new entrants into the market.

6.1.2 Limitations of Life Cycle Models

Several commentators (Storey, 1994; Deakins, 1996) have pointed out that such stage models have considerable limitations as *predictors* of enterprise development and growth:

- Growth is rarely as smooth as the curve of the graph suggests. It is more likely to represent spikes of growth and contraction rather than rounded peaks. For example many small businesses have relatively few customers, so that the addition of one new significant client will lead to a sudden growth spurt. Conversely, the loss of one large client can significantly shrink the size of the business.

- The transition from one stage to another does not necessarily take place in the order predicted by the model. Economic or trade cycles outside the control of the firm may contribute substantially to the growth or decline of an enterprise at any time irrespective of the stage of development. The economic downturn of 2008/9 forced a large number of businesses to decline in size, whatever stage in their development they had reached.
- The contention that the transition from one stage to the next is triggered by a particular kind of crisis has not been tested through empirical research. The development of an enterprise is likely to be subject to many different internal and external variables so that isolating one primary cause for the evolution of a firm from one stage to another is an over-simplification of a very complex process.
- Many enterprises reach a stable size and never make the transition out of this phase. Once they have developed a business to a stage of survival, life-style entrepreneurs will have little motivation to grow it further. Some take deliberate steps to avoid growth which they see as threatening the very independence they sought when they created the enterprise (Stokes and Wilson, 2006).

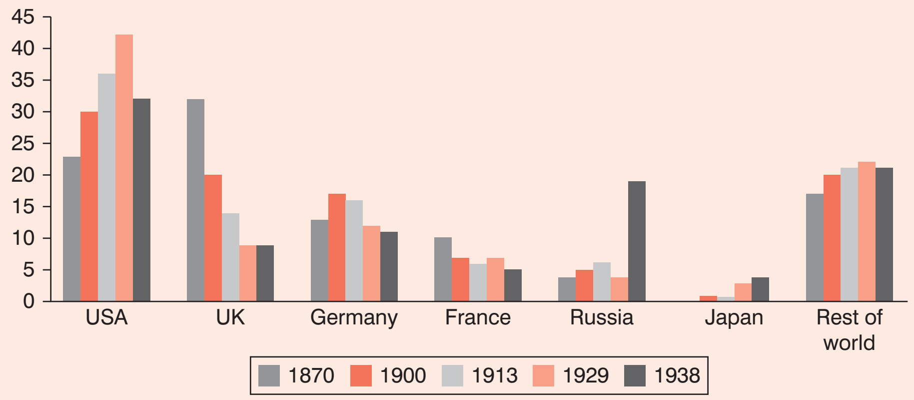
The economic life cycles of nations

The economies of nation states exhibit cyclical phases like the many enterprises that make them up.[2] The competitiveness of one nation compared to others changes over time, sometimes gradually, sometimes more rapidly. National economies go through phases of evolution and revolution, just as the enterprises in Greiner's life cycle model develop gradually until a crisis precipitates more fundamental change.

The graph in Figure 6-3 shows the share of worldwide production of leading industrial nations from 1870 to 1938, a crucial period in the formation of modern states that began with the unification of Germany and ended with the Second World War. Industrialisation and the creation of modern capitalism has taken place in phases of development that have favoured different countries at different times. Great Britain led the first industrial revolution in which the traditional energy reliant on humans and animals was replaced by new sources of power derived from steam and coal. Visionary entrepreneurs such as Stephenson and Brunel created the transport and communication infrastructure of a commercial empire that represented 32 per cent of the world's output in 1870.

By then the advantages of being the first industrialised state were already slipping away. A second industrial revolution was underway that used new forms of power based on electricity and the internal combustion engine and new materials such as rayon and plastics. Entrepreneurs in the US such as Henry Ford and E.I. du Pont laid the foundations of an industrial nation that controlled over 40 per cent of the world's production by 1929.

FIGURE 6-3 **World's industrial production: percentage by country 1870–1938**



Source: Rostow, 1978: 52–53

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When Germany became a unified state in 1871, it changed the economic balance of Europe and the world. By 1900 it had become a major economic force with 17 per cent of the global industrial production, challenging the UK's position and well ahead of its continental rivals, France and Russia. By 1913 it was the largest exporter of iron and steel goods, led by entrepreneurial dynasties such as the Thyssen and Krupp families.

The aftermath of the First World War and the economic problems of the 1930s saw a decline in the share of world production of the Western leaders and the rise of new stars in the East. Japan's first 'economic miracle' was underway including the transformation of its textile industry into the world's largest exporter of cotton goods by the late 1930s, helped by entrepreneurs such as Sakichi Toyoda who invented an automatic loom and his son Kiichiro Toyoda who diversified his father's company into cars under the Toyota name. (See below for more of this story).

Such economic cycles can only be viewed over relatively long periods and other examples of enterprise life cycles in this chapter take a more historical perspective for this reason. Today, the picture looks very different with the emergence of new world economies such as China and India and the continued decline in the share of global production of Western economies in North America and Europe.

Source: Rostow (1978: 52–53)

6.2 THE GROWTH OF AN ENTERPRISE

6.2.1 To Grow or Not to Grow

One of the key limitations of the life cycle models described in section 6.1 is the assumption that growth is a part of the natural order of business ventures. Entrepreneurial success is often linked to growing a new venture or small business into a much larger one. Examples of successful entrepreneurs and enterprises are usually taken from those that start small and grow into an international giant (for example, Steve Jobs and Apple; Richard Branson and Virgin; Rupert Murdoch and News Corporation). Much less attention is given to entrepreneurs who have succeeded in meeting their business objectives but remained relatively small (no examples, to prove the point that they would be unknown to most readers).

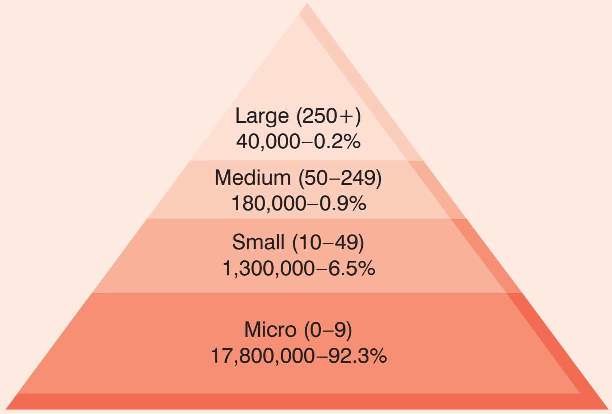
This narrow view of success does not take into account the vast majority of businesses and their owners. A few will grow quickly and in time become medium or large firms employing over 250 people with substantial turnovers. However such high-growth firms are very small in number as can be seen from the business population data: less than one per cent of enterprises in Europe qualify as medium or large, employing more than 50 people; only 40,000 of the 140 million enterprises in Europe are large, employing more than 250 people (Observatory of European SMEs, 2004). As a result, if the size distribution of the population of businesses is visualised as a triangle, the base of very small businesses is extremely broad and the apex of large firms is very small (see Figure 6-4).

If success means moving from the base to the tip of this triangle, then it is rare indeed: most very small businesses do not grow beyond their classification as a micro firm; only a few small firms grow to become medium-sized, and even fewer grow into the large companies of the future.

This has led some commentators to classify enterprises and entrepreneurs by their propensity to grow. Storey (1994) suggested three groups: *'failures'*, '*trundlers*' and *'flyers'*. Hisrich and Peters (1995) divided start-ups into:

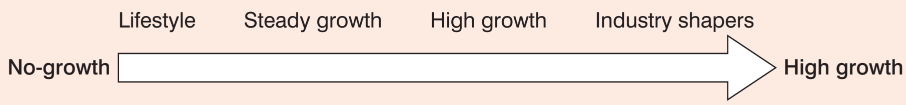
- *A lifestyle firm* that exists primarily to support the owners. Privately owned, it achieves modest growth due to the nature of the business and/or the motives of the entrepreneur. These are typically micro business with up to ten employees.

FIGURE 6-4 **Size distribution of the European business population**



Source: The Observatory for European SMEs, 2004, http://ec.europa.eu/

FIGURE 6-5 **The spectrum of growth in entrepreneurial ventures**



- A *foundation company* is created from research and development and lays the foundation of a new industry. Its innovation changes the nature of an entire sector. This category includes companies like the Apple Corporation founded by Steven Jobs and Stephen Wozniak that turned computing from a specialised technology into a mass market.
- A *high-potential venture* achieves rapid growth because of its innovative product/service in a large market, and also receives greatest investment and public interest. For example, Rupert Murdoch's News Corporation has grown from a loss-making newspaper in Adelaide, Australia into the world's largest media conglomerate.

The complexity of entrepreneurial ventures makes it difficult to categorise business growth into so few types. The characteristics of an enterprise in relation to business growth can best be described as a spectrum with low growth, lifestyle enterprises at one end and rapid growth companies that change the shape of an industry at the other (Figure 6-5). In between there are many possible patterns of enterprise growth.

6.2.2 Factors Influencing the Growth of an Enterprise

Finding out what influences an enterprise to grow is obviously very important for policy-makers, investors and advisers as well as business owners themselves. Although there has been much research and commentary in this field, no single theory that adequately explains the interplay of all the factors influencing growth has been developed. The wide variety of different circumstances surrounding each individual enterprise, and the complex interactions of forces that influence them, has so far prevented the development of such a model. However the research does suggest a general framework of factors

ENTREPRENEURSHIP IN ACTION

The Toyoda family:[3] The 'first Japanese miracle'

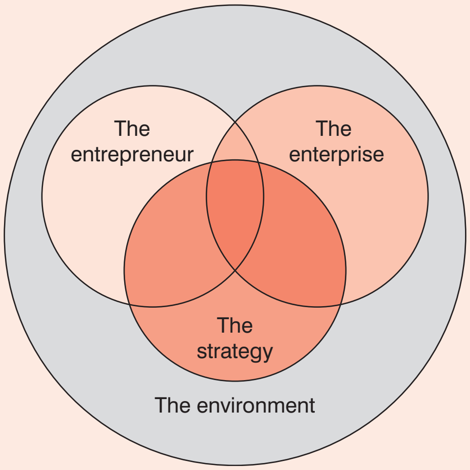
In 1929, the economic life cycles of nations (described in subsection 6.2.1) indicate that Japan's share of global manufacturing was miniscule, although the country's first 'economic miracle' was already underway. The UK was still one of the world's largest producers but in decline. Symptomatic of these changing economic fortunes was a deal signed that year by Sakichi Toyoda, a Japanese inventor and entrepreneur, and Platt Brothers, the world's leading manufacturer of textile equipment (Bernstein,1997). The deal was a licensing agreement giving Platt Brothers the right to make and distribute Toyoda's automatic loom. That such an international company should agree to sell a Japanese innovation was a huge achievement for the entrepreneur behind it. His fast-growing business was a *foundation company* that helped transform the textile industry and enabled Japan to overtake the UK as the world's largest exporter of cotton goods. Toyoda achieved his success after many failed attempts. Trained as a carpenter, he built loom after loom from wood but when he set up in business to sell his patented invention he closed down his first business after only a couple of years. He persisted and began designing steam-powered looms but left the business that had been founded to make the product when sales fell. Benefiting from a textile boom during the First World War, he finally found the necessary investment and time to develop a loom that automatically replenished the yarn when it ran out and was thus more productive. By 1929 when he signed the deal with Platt, Toyoda had a large group of companies involved in textile manufacture that was an integral part of the fast-growing Japanese textile industry.

even if it cannot predict which will influence particular enterprises and entrepreneurs. As Burns (2001: 271) put it: 'we know the ingredients, but the precise recipe can vary from situation to situation'. Burns (2001) suggested that the important ingredients are: the *entrepreneurial character*; the *business culture*; *company strengths*; and *business decisions*. This overlooks the crucial influence of the external business environment, a factor that is taken into account in the framework presented by Smallbone and Wyer (2006) who modified a model first suggested by Storey (1994). This proposes that growth is influenced by: the characteristics of the entrepreneur and of the enterprise, the management strategy and the external business environment (as shown in Figure 6-6).

The Entrepreneur The characteristics of the entrepreneur are widely accepted as *the* vital ingredient that influences growth (see Chapter 7 for a more detailed discussion of entrepreneurial characteristics). Research indicates that the particular characteristics of the entrepreneur that are associated with growth of the enterprise include:

- *Motivation* – if the entrepreneur's reasons for starting the business originated in 'pull' or 'opportunity-driven' motives such as the desire to exploit a market opportunity, rather than 'push' or 'necessity-driven' motives such as unemployment, then the resulting enterprise is more likely to grow. The commitment of the entrepreneur to growth makes a considerable difference.
- *Previous management experience* – prior experience of managing people and processes is valuable in maintaining growth.
- *Demographics* of the entrepreneur – age and education can influence growth. Some research suggests that middle-aged founders benefiting from some experience yet still retaining the energy necessary to drive a business forward are more likely to grow their business. Entrepreneurs with higher educational qualifications are more likely to found high-tech and knowledge-based firms which tend to be linked with higher rates of growth.

FIGURE 6-6 A framework of influences on enterprise growth



Source: Storey, 1994; Smallbone and Wyer, 2006

- *Number of entrepreneurs* involved – enterprises founded by a group of entrepreneurs are more likely to grow than one-person bands. Access to a wide range of skills, experiences and resources is important to growth, and an entrepreneurial team is more likely to possess the attributes needed than just one person.

Other characteristics of the entrepreneur have also been put forward as influencing growth including: family history; training and functional skills; gender; social marginality; and experience of the sector. However there is less evidence to support the influence of these factors (Storey, 1994).

Type of Enterprise The characteristics of the enterprise also have an influence on its growth prospects:

- *Legal form* – limited companies seem to grow more than sole traders or partnerships. This is probably associated with the number of entrepreneurs involved as there are likely to be more in a limited company. Limited companies may also lend greater credibility to an enterprise which can assist in attracting both the customers and resources needed for growth. The equity investment needed for growth is facilitated by incorporation into a limited company (see Chapter 15 on the types of entrepreneurial finance). It is also possible that as companies grow they adopt limited liability status so that the legal form is a result, rather than a cause, of growth.
- *Firm age* – younger firms tend to grow more quickly than older ones, although this partly reflects the need for young firms to achieve a critical mass to survive in the marketplace.
- *Firm size* – the very small firms find it hard to grow, partly because many entrepreneurs with micro firms do not wish to grow, and partly because of resource constraints and lack of competitiveness.

The Management Strategy The management decisions and actions taken by the entrepreneur once trading has begun significantly influence growth:

- *Market position* – the adoption of clearly defined niches and market segments is a key ingredient for growth.

- *Introduction of new products* – growth companies cannot rely on a narrow product/service range so that continuous innovation in the form of new introductions is also key to growth.
- *Devolution of decision-making to non-owning managers* – the change of management structures as the organisation grows was an important feature of the growth models described in section 6.1. The development of a management team to lessen the reliance of the enterprise on one entrepreneur is needed to maintain growth.
- *Sharing of equity* – the willingness to include others in the ownership of the business attracts resources that aid growth including additional finance, innovation through partnerships and retention of the management team with share options.

The Business Environment Key factors outside of the internal environment of the enterprise influence its likelihood to grow. Enterprises exist in external business environments which are more or less favourable to growth depending on such factors as:

- *Market sector or industry* – the growth rate of the market conditions the potential for the enterprises within it. However this influence may be relatively localised: for example, if one firm is supplying a company that is growing rapidly, it is more likely to grow faster than a firm supplying a more stagnant player in the same industry or trade.
- *Competitive forces* – competitive conditions between direct and indirect rivals, and the relative power of suppliers and buyers in the market, represent forces largely outside of the control of an individual enterprise but which influence its growth prospects (Porter, 1980).
- *Location* – the geographic location of an enterprise may affect its business environment depending on the market sector. For example, retail growth is dependent on the economic health of the local population.

Growth Factors Important to the Entrepreneur Research into the reasons for growth, and the factors that might curtail this, is important. But what lessons does it offer entrepreneurs who are attempting to grow their business? Some of the factors discussed above (such as the business environment and demographics of the enterprise owner) are outside the control of individual entrepreneurs. However, there are key messages for those who wish to grow an enterprise:

- No growth is not a good long-term option as a very small firm is more likely to succumb to the vagaries of the external business environment.
- The need to refresh the products or services on offer also indicates that an enterprise needs continuous development if it is to survive and grow.
- The entrepreneur and the enterprise need a competitive edge derived from answering the following key questions about the market place:
  - Who are the customers – what is the target market or niche?
  - What benefits do these customers get from what the enterprise is offering?
  - Why will they buy from this enterprise and not another?
- The organisation cannot depend totally on the skills and efforts of one entrepreneur if it is to continue to grow. An entrepreneurial team – both within and outside of the enterprise is needed (see Chapter 13, The entrepreneurial team).

ENTREPRENEURSHIP IN ACTION

The Toyoda family: The 'second Japanese miracle'

Sakichi Toyoda helped transform the Japanese textile industry, but he encouraged his son Kiichiro to follow his own dream. Kiichiro Toyoda wanted to make cars not looms, and in 1933 he established an automobile division within Toyoda Automatic Loom Works, Ltd. It was a risky diversification as the Japanese automobile market was small and dominated by Ford and General Motors. Changes to the market environment soon endorsed Kiichiro's decision however. In 1936, driven by military considerations, the Japanese government restricted motor manufacturing to domestic producers only, thereby removing all foreign competition. Kiichiro understood the changing market well enough to develop not only cars but trucks which the military needed. Kiichiro ran a competition to re-brand the car company. The winning entry was 'Toyota'.

During the Second World War the Japanese government converted most textile firms into armaments' producers whilst the need for trucks and buses boomed (Bernstein, 1997). Thus, Kiichiro's diversification proved a wise business decision and led to the emergence of a successful car company from the old textile conglomerate. After the war, the company became one of the great innovators of modern production techniques such as 'lean manufacturing'. By the 1980s, Japan had the highest productivity in the world, a key part of the 'second economic miracle'.

6.3 THE CLOSURE OF AN ENTERPRISE

6.3.1 The Churn of Entrepreneurial Ventures

The enterprise population is a dynamic and continuously changing one. The population of businesses in an economy may seem relatively stable at the macro level for considerable periods of time; for example, the UK business population was relatively stable around 3.5 million for the decade 1992–2002. But even in periods such as this when the total population is neither growing nor declining, there was turbulence beneath the surface. The total number of enterprises is affected by the number of new ventures being created on the one hand and the number of businesses that close down on the other. At any one time a large number of new ventures are in the process of being formed and others are being closed down.

This is happening in most economies at relatively high levels. In the UK, there were 425,000 start-ups (9.5 per cent of the total population) and 490,000 closures (10.9 per cent) in 2007 so that the business population contracted slightly during the year (Barclays Bank, 2008). Start-up and closure rates of around 10 per cent of the total population are fairly typical of developed economies in normal economic conditions. Some countries are higher particularly in Asia and Latin America. For example Australia recorded a 17 per cent start-up rate and a 15 per cent closure rate in 2007 in a total business population of 2 million.[4] The US has also exhibited a high start-up and closure rate of around 15 per cent (Headd, 2003). Several European countries, including Italy, Portugal, Finland and Sweden have had somewhat lower start-up rates of 6–7 per cent (Vale, 2006). The percentages may vary but it all adds up to a very large number of enterprises that start up and close down every year. The Global Entrepreneurship Monitor (Bosma *et al*., 2008) estimates that more than 50 million new businesses may start each year around the world and a similar number may close. (See Chapter 4 for more on the importance of enterprise creation in the global economy.)

This movement in and out of the business population is referred to as business '*churn*'. It is central to the process of entrepreneurship and the role of 'creative destruction' it plays in the economy, as described by Schumpeter (see Chapter 1).

Churn can be viewed in different ways:

- At the micro level of the individual entrepreneur, high levels of churn indicate that a large number of businesses have closed which may mean personal and financial difficulties for some of the owners and a loss of jobs for employees. However not all closures can be considered 'failures' and it is important to distinguish between businesses that close leaving indebtedness and those that close for more positive reasons. This is a theme which is developed in section 6.4 below.
- At the macro level of the regional and national economy, churn can generate benefits as it helps to renew and improve the competitiveness of the business stock. The competitive market system operates as a process of natural selection of enterprises. Some businesses take market share and customers away from other firms which may be forced to close as a consequence. Assuming that businesses survive based on their higher levels of efficiency, innovation and customer service, the result should be a more healthy population of high-performing enterprises and entrepreneurs. In this way, churn is desirable so that market mechanisms can motivate entrepreneurs and reward investors whilst detering those who are less productive and unwilling to change.

A low churn rate in an economy can be symptomatic of restricted competition, lack of incentives to innovate and high barriers to new business entry – an economy in need of more entrepreneurial activity. Conversely a high churn rate is usually indicative of an entrepreneurial economy in which new entrants with novel products and processes force out complacent competitors or stimulate them to improve and innovate in order to remain competitive. In this way, high rates of churn are often associated with stronger economic growth. An economy that is growing relatively quickly exhibits a higher start-up rate; more start-ups lead to more closures as many new ventures do not last very long and so churn is increased. For example, Australia exhibited relatively high rates of churn (over 15 per cent start-up and closure rates) at a time when its GDP was growing at 3–4 per cent per annum from 2003 to 2007 (Australian Bureau of Statistics, 2007). In times of economic downturn, closures continue at high rates or accelerate whilst start-ups slow down so that the total business population declines and economic growth is depressed further.

Iceland's meltdown

As we have seen, there is cyclical churn amongst the economies of nation states in that some rise as others fall in terms of economic output and wealth. Iceland has recently risen and fallen in spectacular fashion. From the 1990s, Icelandic entrepreneurs used a combination of favourable factors in the commercial environment to acquire business assets around the world. Backed by cash from fish quotas and a stock market based on stable pension funds, they found it easy to obtain international credit for rapid expansion through acquisition. For example, Johannes Jonsson and his son, Jon Asgeir Johannesson, founded 'Bonus', a cheap food store in Reykjavík in 1989 which developed rapidly into a national chain within a few years. Changing the name to Baugur (the 'Ring of Steel') after merging with another Icelandic chain in 1992, the new group provided the platform for a host of overseas acquisitions. They focused particularly on well known brands in the UK High Street such as the fashion chains Oasis, Karen Millen and Whistles, the toy store Hamleys, the department store House of Fraser, the tea company Whittard of Chelsea, the jeweler's Mappin and Webb and the supermarket chain Iceland (of course). This international expansion was good for the home economy and Iceland's small population enjoyed one of the highest incomes per capita in the world.

It all went badly wrong during the financial crisis in 2008 when Iceland's banks ran out of money. Iceland's currency devalued and inflation increased rapidly. Baugur's expansion was facilitated by leveraging debt on a large scale to buy stakes in companies around Europe. The international financial crisis left Iceland's three major banks particularly exposed and two were nationalised to avoid collapse. This effectively left part of Baugur's debts in the hands of the government. They considered selling off parts of their empire, asking for help from entrepreneurs such as Philip Green, owner of BHS and other UK retail chains, but found the deals unacceptable at first. In February 2009, Baugur's UK division were put into administration with the Chairman Johannesson complaining of 'British vultures' circling over his collapsed empire hoping to pick up bargains. In March the company was declared bankrupt. Johannesson had already set up his next venture, Tecamol, to buy different retail businesses in a more focused way.

6.3.2 Which Enterprises Close and When?

The data on business closures indicate that there are two groups of enterprises that are most vulnerable to closure (Observatory of European SMEs, 2006):

- *Smaller enterprises* – the very small micro firms are most likely to close as closure rates are lower amongst medium-sized and larger firms. The largest numerical segment of SMEs – micro enterprises – are most at risk of closure. This indicates that standing still and staying small is not a good survival strategy even though many business owners do not want to grow.
- *Younger enterprises* – the chances of survival improve as the business ages so that the most vulnerable are the very young, relatively new enterprises.

The message to the founding entrepreneur is clear: the longer you can keep going and the more you can grow your business, the greater chance you will have of survival.

Survival Rates As the youngest enterprises are the most vulnerable it follows that survival rates are lower in the early years and improve as a firm ages. However, claims that a very high percentage of firms close in the first year of trading are unfounded. Phillips and Kirchhoff (1989) investigated the myth that nine out of ten new businesses close in their first year in the US and found that 76 per cent of firms were still trading after two years. More recent research by Headd (2003) indicated that 66 per cent had survived two years. In the UK, survival figures seem more optimistic with 80 per cent surviving two years (see Table 6-1), but this could be because the data are derived from VAT registered businesses that have a turnover above £60,000 (2005/6) and therefore have an above average size distribution (Office for National Statisitcs, 2008).

TABLE 6-1 Enterprise survival rates in the UK and US

Percentage of firms still trading after	US	UK
1 year		96
2 years	66	80
3 years		65
4 years	50	54
5 years		45
6 years +	40	

Source: Headd (2003) and Office for National Statistics (2008)

The general picture seems to be that approximately one-third of start-ups close within three years, and one-half after five years.

6.3.3 What Happens to Businesses that Close?

At the macro-economic level, active churn amongst enterprises with a high level of business start-ups and closures is normally a sign of a healthy economy. However at the micro level, we tend to regard the closure of an individual business in a negative way, assuming that it has somehow failed. 'Business closure' and 'business failure' have come to be used as interchangeable, negative terms. Until relatively recently there was little research to contradict or support this gloomy picture but now there are insights into this final stage of the business life cycle.

There are clearly positive and negative reasons why an enterprise closes. Using financial criteria, business closures can be placed on a spectrum with large monetary gains for the owners at one end and significant losses at the other. In between many businesses are closed down because either they no longer meet the owners' objectives, or they have already done so. Even after a relatively short time, an enterprise may have met the objectives set by the founders. For example, ventures in the creative industries often have a natural, short existence to fulfil a particular project such as the making of a film or an advertisement. A new business entity is often set up to facilitate this objective and closed down when it is completed.

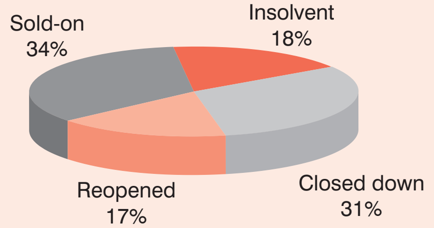
A research study by Kingston University (SBRC, 2002) examined the closure of over 300 businesses and classified their fate into four main groups: sold-on, reopened, closed down and declared insolvent (as shown in Figure 6-7).

At the positive end of possible financial outcomes, around one-third of businesses were sold on by their owners for a monetary gain, mainly for modest amounts as the well publicised multi-million pound deals are rare.

On the negative side of financial outcomes, up to 20 per cent of businesses that close do so with debts that are left unpaid. In the UK, there are approximately 40–50,000 liquidations of companies and bankruptcies of sole traders and partnerships in a typical year outside of an economic recession. This represents around 1 per cent of the total business population or 10 per cent of all the businesses that close. Although in the economic downturn of 2008/9 bankruptcies rose by over 25 per cent, this still represents less than 2 per cent of the total business stock. Financial insolvency is not very common therefore, although it can have profound effects on those involved.

Between these extremes of financial gain and pain, a large number of enterprises simply close down and stop trading. Some close because they no longer meet their owners' objectives. Others are undoubtedly ailing financially and are closed before they can cause too much damage. Some owners prefer to concentrate on a different idea for a business venture, or maybe they are attracted back into employment. A business may close for negative, non-financial reasons such as the breakdown in relationships between partners or the ill health of the owner. In many cases the 'business' or trade does

FIGURE 6-7 What happens to enterprises that close?



Source: SBRC, 2002

WHEN THINGS GO WRONG

Brunel goes to prison

The rise of Britain as the leading economic nation in the world was not without many business casualties, some involving well known names. Isambard Kingdom Brunel is famous as one of the giants of the Victorian era, an engineer and entrepreneur who built the bridges, railways and ships at the heart of Britain's trading success in the nineteenth century. The achievements of his father Marc Brunel are less well known but also very significant. The Brunels[5] were in fact French, but Marc fled the excesses of the French Revolution to the US where he became chief engineer to the City of New York. He fell in love with an English woman, Sophia Kingdom and moved to England to marry her in 1799. As well as ensuring his famous son was English (rather than French or American), he was also partly responsible for the defeat of France through his entrepreneurial activities. A prolific inventor, he became aware of one of the British navy's greatest needs during the Napoleonic wars – pulley blocks that controlled the rigging ropes of the sails. Each year the fleet needed 100,000 of them and they could not get enough as they were made laboriously by hand from a solid block of oak. Marc Brunel designed a system using machines to do the work, one of the first examples of automated manufacturing replacing craft-based production. He also designed a production line process to make boots for the army, many of which were worn at the Battle of Waterloo when Napoleon's army was finally defeated. The end of the war also meant the end of a thriving business for Brunel as neither the navy nor the army needed his mass-produced products in viable quantities. The penalties for failing to pay off debts were severe in the nineteenth century, and when his enterprises could no longer meet the bills, he was sent to debtor's prison as his businesses collapsed. Fortunately the Duke of Wellington remembered the contribution of this French émigré to the English war effort and arranged for his release.

not really cease at all as it is passed on to another business entity. 'Technical closures' are often motivated by tax or legal reasons and one business entity takes over the trade of another – for example, when a sole trader or partnership is changed into a limited company.

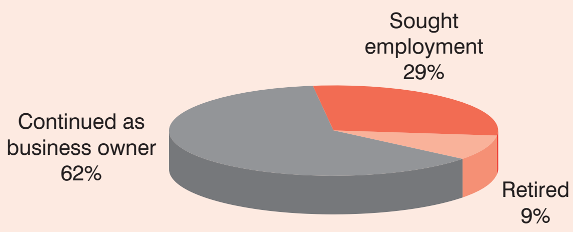
These findings from UK research are broadly supported by studies in other countries. Headd (2003) examined a large dataset of businesses that had closed in the US and found that 34 per cent of those that closed within four years were considered 'successful'. He concluded that: 'potential entrepreneurs … have less to fear than is commonly believed. Their prospects of survival are reasonable, and if they close, their prospects for being successful at closure are reasonable' (Headd, 2003: 59).

6.4 THE LIFE CYCLE OF THE ENTREPRENEUR

6.4.1 What Happens to the Entrepreneurs Who Close a Business?

In the introduction to this chapter, we made the point that the life cycle of an enterprise might be very different from that of the career of the entrepreneur involved. So what does happen to entrepreneurs who close down their enterprise? There is still an assumption that most entrepreneurs that close down their business have been unsuccessful and may therefore give up the entrepreneurial trail, but this is not reflected in what entrepreneurs actually do when they exit from an enterprise. The majority of entrepreneurs who close one business become involved in another one. The SBRC (2002) study tracked what the owners of closed businesses had done on exit. The results are illustrated in Figure 6-8: The majority (60 per cent) continued as business owners by opening or buying a new or similar business to the one closed, or through the existing ownership of another business. Around 10 per cent

FIGURE 6-8 What happens to the owners of enterprises that close?



Source: SBRC, 2002

of owners retired from active involvement. Only 30 per cent dropped their entrepreneurial ambitions by returning to employment or becoming unemployed.

6.4.2 The Revolving Door of Enterprise Ownership

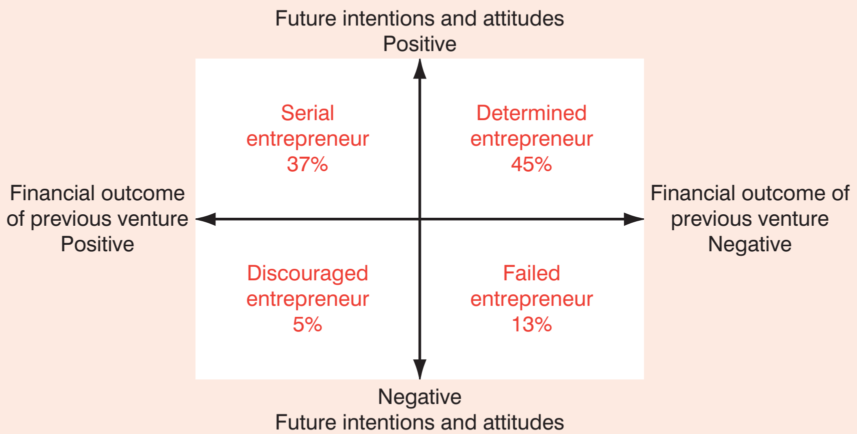
The way out of entrepreneurial ventures resembles a revolving door rather than a one-way exit. Most owners re-enter because they are sufficiently encouraged by their experiences the first time round. Even those who experience financial difficulties in one venture, try again. Figure 6-9 illustrates the outcomes as described by the entrepreneurs who had closed a business (SBRC, 2002). This classified entrepreneurs who leave a business according to:

- how their business performed financially – positively or negatively; and
- their future intentions and attitudes towards running a business – positive or negative.

This resulted in four categories as shown in Figure 6-9:

- *Determined entrepreneurs* (45 per cent of those who close a business). Even though they experienced financial difficulties in their previous venture, they returned to business ownership determined to do better. They often regarded closure as a beneficial experience.

FIGURE 6-9 A typology of entrepreneurs who have exited from a business



Source: SBRC (2002)

- *Serial entrepreneurs* (37 per cent). Having succeeded financially in a previous venture, this group returned to invest their human capital and other resources in a new business.
- *Failed entrepreneurs* (13 per cent). The financial problems of a previous venture discouraged this relatively small group from re-entering into business ownership. They have 'failed' in that they have closed a business in financial difficulty, often leaving bad debts, and returned to employment, or unemployment.
- *Discouraged entrepreneurs* (5 per cent). Although their previous business venture succeeded, they did not wish to repeat the experience. Often the strains of running a small business outweigh the financial rewards, so this relatively small group also withdraw from business ownership.

A number of studies in Europe (e.g. Stam, Audretsch and Meijaard, 2005; Metzger, 2006), the US (Headd, 2003; Henley, 2004) and Japan (Harada, 2005) have confirmed that entrepreneurs who exit one business tend to go back into business ownership and that people with experience of entrepreneurship, even if it has been problematic, are more likely to start new ventures.

Some entrepreneurs believe that coping with setbacks and crises is the best way to learn about entrepreneurship and running a business. When asked to rate their skills after closure compared to when they started, entrepreneurs cited a number of improvements including business planning, building a customer base and financial record keeping. However, they rated managing and motivating themselves through the changing fortunes of their venture as the most valuable learning experience (SBRC, 2002).

The start-up that never gave up

Julian Harris formed an IT company in 1989 with high growth ambitions. However it coincided with an economic recession that particularly affected technology companies and the company was moth-balled until 1993. It was re-born three years later and soon rated as one of the fastest-growing UK companies. By 2000 the cyclical nature of the IT industry caused problems again and Julian decided to restart as a new company, Smart421. After a period of high losses, the business turned round and Julian sold out in 2006.

6.4.3 Serial and Portfolio Entrepreneurs

The above analysis indicates that many entrepreneurs own more than one business. They can be classified according to whether they do this either concurrently or sequentially:

Integrative Case Link

Read more of Julian's roller coaster ride in Case Study 9 on Smart421 at the end of Part 3.

- A *portfolio entrepreneur* owns more than one business at the same time;
- A *serial entrepreneur* runs a business, sells it and moves on to another venture in a relatively short time.

Some portfolio entrepreneurs build up a series of ventures as a way of de-risking their investments. They are prepared to sacrifice the high growth or profitability of one venture by owning several businesses with lower growth and profitability that overall meet their financial and personal needs. Others are just very good at entrepreneurship and build up a series of successful enterprises.

Serial entrepreneurs often excel at the early stages of venture creation but are less motivated or able to build a business over a lengthy period of time. They thrive on the psychological reward of creating

ENTREPRENEURSHIP IN ACTION

The Thames Tunnel

Marc Brunel was typical of many entrepreneurs in that he was already planning his next venture whilst suffering the consequences of the first. When he was imprisoned for debt following the bankruptcy of his manufacturing businesses, he spent much of his time working on a problem that was threatening the supremacy of nineteenth-century London as the world's commercial centre – traffic congestion. As the city developed around the docks both north and south of the Thames, a major bottle-neck for carts and coaches developed on London Bridge, but other crossings could not be built downstream without impeding shipping using the docks. Brunel realised that the only alternative was to build a tunnel under the Thames, but under-water tunnelling was an undeveloped skill at the time. First he designed the 'Great Shield', a patented method that provides protection for workers who dig and build the walls at the same time. It was an innovation that formed the basis of modern tunnelling technology and was used during the construction of the Channel Tunnel that now links Brunel's country of birth with his country of adoption.

Next, he formed the Thames Tunnel Company, raised the necessary capital from private investors and began work in Rotherhithe in 1825 on a tunnel to Wapping, a quarter of a mile away on the north bank. He employed his son Isambard as one of the engineers. Three years later they had reached the middle of the Thames, but water burst through several times, precipitating a financial crisis that halted the work and temporarily closed the business. Marc Brunel had already demonstrated his resilience in the face of problems and five years later in 1836 he had raised new capital from the government to begin the project again. He was 73 years old when the Thames Tunnel[6] was finally completed in 1842, 17 years after he had begun the project.

something new but are less interested in the management and day-to-day running of an established business. They also tend to regard closure and even failure as an experience that will make them stronger to take on new challenges.

6.5 FACTORS INFLUENCING THE DECLINE AND CLOSURE OF AN ENTERPRISE

What are the problems and key issues that confront entrepreneurs and ultimately drive some out of business? Many researchers and practitioners have attempted to answer this question concerning the causes of the closure and failure of an enterprise. The earlier sections of this chapter have argued that many of the reasons for closure are positive: entrepreneurs may sell up or lose interest in their business for a whole variety of reasons that are not related necessarily to significant business problems. However, there are many business issues that cause significant problems and in some cases, the closure of the enterprise. These can be classified broadly into external and internal factors:

- *External influences:* conditions in the macro-economy such as interest rates and overall levels of consumer demand have an influence on the fortunes of enterprises in general. However, it is likely that localised, micro-environmental factors will be more crucial in determining whether an enterprise will survive. Changes in demand within the local catchment area or industry sector can have a rapid and devastating effect. For example, the arrival of a superstore will often reduce the numbers of small, independent retailers in the neighbourhood. The demise of a large player within a particular industry will have an adverse effect on the many smaller companies that were dependent on it. As we have noted, young and very small firms are particularly vulnerable to these changes in the business environment as they tend to have fewer resources and less experience to deal with them. Much will depend on the entrepreneur's ability to adjust swiftly to changes in the business environment. Longitudinal research suggests that enterprises that are most active in making adjustments, particularly in relation to their products or services and the approach to the market, are more likely to survive (Storey, 1994).

- *Internal factors.* We have already noted that the entrepreneur's characteristics and the decisions they take are crucial factors in the growth of an enterprise and they are equally important influences in whether it declines or closes. A number of studies have focused on the particular functions or areas of expertise that are most likely to influence entrepreneurial failure (Berryman, 1983; Cromie, 1991; Birley and Niktari, 1995; Stokes and Wilson, 2006). A composite list of internal functions and factors which have been found to have particular impact on survival include:
  - Accounting
  - Marketing
  - Management of people
  - Availability of finance
  - Management capability and behaviour of the owner.

Such a list is rather broad and covers most of the functions of an enterprise except for manufacturing and business operations and processes. How to make things or the methods of delivering a service appear not to be a significant, survival issue for entrepreneurs. Whilst numerous studies of business closure have categorised the causes of failure in different ways, the one factor that is common throughout is the influence of the entrepreneur who remains central to whether or not the business survives. This influence will evolve as the nature of the enterprise changes. In the early days, the founding entrepreneur's judgement in selecting the type of business and their skills in creating a

ENTREPRENEURSHIP IN ACTION

A social entrepreneur who knew when to let go

Jamie Oliver is a social and a portfolio entrepreneur with chains of restaurants as well as publishing and television enterprises. 'Fifteen' is a good example of how he manages to keep all of his entrepreneurial ventures running successfully. Named after the first cohort of trainees, Fifteen is a high-class restaurant that doubles as a training programme for disadvantaged young people interested in becoming chefs. As a social enterprise it takes on trainees with backgrounds of crime, addictions or homelessness who are given a year-long work placement at the restaurant. Those who finish take work placements around the world or open their own restaurants. Jamie Oliver set up the first restaurant in London, tracked by a very successful TV show *Jamie's Kitchen* and it now has spin-offs in Amsterdam, Cornwall and Melbourne. He now has only non-executive involvement, leaving the management to a CEO, Penny Newman, who used to run Cafédirect. Jamie has gone back to doing what he does best as a celebrity chef.

© FRANTZESCO KANGARIS / ALAMY

Jamie Oliver, a social and a portfolio entrepreneur

Source: http://www.fifteen.net

customer base will be crucial. As the business develops, financial influences and the cash flow become more significant. If the business continues to grow, the unwillingness or inability of the entrepreneur to draw others in to help with the management of the enterprise can cause closure. Drucker (1985) made one of the earliest summaries of what is required to keep an enterprise going through the various stages of its life cycle and it stills seems valid today. He proposed that the four key factors, in chronological order were likely to be:

1. Focus on the market
2. Financial foresight, especially planning cash needs
3. Building a management team – before it is needed
4. Finding an appropriate role for the founding entrepreneur in a developed enterprise.

6.6 SUMMARY AND ACTIVITIES

The entrepreneurship process encompasses the complete life-span of an enterprise and the career of an entrepreneur. This chapter has therefore considered what happens to businesses as they grow and decline, and also what happens to entrepreneurs as they enter into and exit from an enterprise.

Life cycle models of an enterprise from start to finish typically describe five stages:

- Concept/test stage
- Development/abort stage
- Growth/decline stage
- Maturity
- Re-growth/decline.

Such models have limitations as growth is rarely smooth and does not necessarily take place in the order of the model; many enterprises reach a stable size and never grow out of this phase.

Enterprise growth is on a spectrum with low-growth, life-style enterprises at one end and rapid-growth companies that change the shape of an industry at the other, although the latter are relatively rare. In between there are many possible patterns.

Growth is **influenced** by:

- The *entrepreneur* – their motivation, previous management experience, demographics (age and education) and the number of entrepreneurs involved in the enterprise;
- The *enterprise* – the legal form, age and size of the business;
- The management *strategy* – the market position, introduction of new products, devolution of management to non-owning managers, and sharing of equity;
- The external *business environment* – the market sector or industry, competitive forces and location.

Business Closure Business '*churn*' refers to movements in and out of the business population. In most economies this is at relatively high levels – typically 10 per cent of the business population close down and 10 per cent are new start-ups in any one year. At the *macro-economic level*, churn can generate benefits as it helps to renew and improve the competitiveness of the business stock. A low churn rate in an economy can be symptomatic of restricted competition, lack of incentives to innovate and high barriers to new business entry.

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The two most vulnerable groups of enterprises to closure are: *smaller enterprises* and *younger enterprises* – the chances of survival improve as the business grows and ages. Approximately one-third of start-ups close after three years, and one-half after five years.

Not all closures can be considered 'failures' as there four main groups: sold-on for monetary gain; reopened in a different form; closed down with neither pain nor gain because it no longer meets owner's objectives; declared insolvent and closed down with unpaid debts (under 20 per cent of closures).

Entrepreneurs Who Close a Business A high proportion (60 per cent) of owners who close a business, continue as entrepreneurs by opening or buying a new or similar business to the one closed, or through the existing ownership of another business. Even entrepreneurs who suffer financial losses return to try again.

Many entrepreneurs own more than one business: A *portfolio entrepreneur* owns more than one business at the same time; a *serial entrepreneur* runs a business, sells it and moves onto another venture in a relatively short time.

Business issues that may **cause the closure** of the enterprise are:

- *External influences:*
  - Macro-economic influences such as interest rates and levels of consumer demand
  - Localised, micro-environmental factors – changes in demand within the local catchment area or industry sector especially the loss of a major customer. Entrepreneurs who can adjust swiftly to changes in the business environment increase the chances of survival.
- *Internal factors* found to have particular impact on survival include:
  - Accounting
  - Marketing
  - Management of people
  - Availability of finance
  - Management capability and behaviour of the owner.

REVIEW QUESTIONS

1. Outline five possible stages in the life cycle of a business from its beginning to its closure.
2. What are some of the limitations to the usefulness of business life cycle models?
3. Name the four key influences on the growth of an enterprise.
4. What key factors in the character of the entrepreneur are likely to influence growth?
5. What advice based on research evidence would you give to an entrepreneur who wished to grow their business?
6. Why is business churn good for an economy?
7. What happens to businesses that close? Give both positive and negative outcomes.
8. What typically happens to entrepreneurs who exit from a business venture? Give a range of possible outcomes.
9. What is the difference between a serial entrepreneur and a portfolio entrepreneur?
10. What are the key internal factors that may cause a business to close? Give four strategies that help to minimise these problems.

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SEMINAR TASK

Rudyard Kipling's view was that both success and failure were nothing more than different life experiences and should be treated equally as such. In his poem 'If', he described to his son the attitude of a man of character:

If you can meet with Triumph and Disaster
And treat those two impostors just the same

Consider how this advice might relate to running a business venture. *Can the success or failure of an enterprise be treated 'just the same'?*

Preview case continued

Fogg's Failures: The entrepreneur who studied unsuccessful ventures

Christopher Fogg was invited to address a group of students who were interested in developing their entrepreneurial capabilities. This he said:

'Since qualifying as a Chartered Accountant I have become a portfolio entrepreneur and have started over 50 businesses – alone and with others. But I am going to talk about my "failures" not my successes as I believe we can learn more from what doesn't work than from what does.

Recently I have set up a number of Business Incubators including an "Incubator Without Walls", based on Connect San Diego, which is regarded as the best private model to help entrepreneurs start and develop high growth businesses. This work involves assessing large numbers of new ventures. I have developed a simple methodology to help me carry out the first stage assessment based on "Four Anchors" (see Timmons, 1999) relating to the business itself and then a review of the business environment.

The **Four Anchors** are

1. *Value – does the business create or add value to a customer or end user?*
2. *Client's willingness to pay – is the customer or client likely to pay for this added value? Does the business solve a significant problem, or meet a want or need, for which someone is willing to pay a premium?*
3. *Money making characteristics – is the market large enough for sufficient money to be earned? Has it got high growth potential and early positive cash flow? Will it produce profits to satisfy investors? Will the rewards balance the risks?*
4. *People – is the business a good fit with the characteristics, knowledge and expertise of the founding entrepreneur and their management team?*

I recently asked myself whether my methodology would have helped predict my own failures. A review of my **"Top 10 business failures"** against these Four Anchors went as follows:

▶

Venture 1: Gambling with marbles

When I was 10 years old, I encouraged fellow students to roll their marbles towards holes that I had cut into a shoe box. If they didn't get through one of the holes, I kept the marble. It was perhaps the highest rated business I have ever had satisfying each and every one of the four anchors: it met a need – the excitement of gambling that clients were willing and able to pay for with their marbles. It had instant cash – or rather marble – flow, and I was the perfect entrepreneur with experience – I loved marbles and started gambling on horses with a postal tote service at a young age.

Why did it fail?

Children at my school quickly caught the gambling habit and soon began asking their parents for more money to buy marbles to replace the ones they had lost to me. I was reported to the headmistress who not only made me close my business but also return all the marbles I had won because I fell foul of the rules of gambling in schools. I learned that although a new venture might meet all the business criteria, it also has to be legal.

Venture 2: Reproduction MG sports cars

Whilst travelling in Brazil, I noticed absolutely brilliant reproductions of old MG sports cars, based on the structure of VW Beetles. I started to import the kits, but for UK safety regulations these had to be built on the base of used right-hand drive VW Beetles imported from Europe.

Why did it fail?

Clients did not want to take the risk of a car based on an old VW Beetle – even though it looked beautiful. The entrepreneur (me) had no knowledge or experience of the import and sale of specialist cars (Anchor 4).

Venture 3: Chinese bicycles

I was in China endeavouring to sell very large-scale capital equipment for the manufacture of paper. Selling to China is very difficult so I tried a different tack – bartering. I was dealing with a Chinese trading company that also sold Chinese bicycles and I made the gesture of buying 1000 of their bikes. Everyone was delighted and I received a lot of publicity for the first sale of Chinese bikes to the UK.

Why did it fail?

I overlooked one thing – when the bikes arrived in the UK I discovered that I had not bought finished bikes but components for 1000 bikes – which is a lot of components. By the time I had paid for the assembly of these, the profit margin was low, especially as I could hardly sell old fashioned Chinese bikes at a premium. Obviously, the entrepreneur (me) had no knowledge or experience of bicycle importing, manufacturing or marketing (Anchor 4).

Venture 4: Second-hand Jumbo Jets

I was running an international trading company and received an enquiry (from my local Bangladesh Restaurant) for three used Jumbo Jets for Bangladeshi Biman (the national airline). Having contacted other airlines and agents, I flew out for a meeting in Dhaka with a portfolio of eight used Jumbo Jets for sale in my briefcase. A group of about 20 people from government, banks, the air force and the airline grilled me with a barrage of technical, product and commercial questions.

Why did it fail?

I could not answer any of their questions! I was also very immature in understanding what "individual commissions" would have to be paid to secure the business. Once again the entrepreneur (me) had come up short as I had no knowledge or experience of the business of selling used aircraft (Anchor 4).

Venture 5: Siemens vacuum pumps

Siemens market a vast range of electrical and electronic products, including a mechanical pump for producing a vacuum that was technically superior to competitive products. Its sales were almost zero. We persuaded Siemens to let us market the product through a ▶

network of 30 agents in the US. We poached engineers and salesmen from the brand leader and the business was an amazing success with sales in excess of our most optimistic projections. At the end of six years, Siemens advised that they would not continue our contract. They were using too many of their own resources to service our clients, and, even more critically, they deemed it too risky to continue as they could not control us.

Why did it fail?

The business was too successful. If our sales were more modest Siemens would have let us continue. (It met all four anchors but failed on barriers to entry.)

Venture 6: Hunt Wesson tomato products

On a visit to the US in connection with Siemens, I looked out of my hotel window and saw an enormous factory with a name on the side that I just did not recognise – Hunt Wesson. Intrigued, I found out they were the largest producers of tomato-based products in the US – bigger even than Heinz. I hadn't heard of them for the simple reason they did not sell to the UK. So I approached them for the UK marketing rights. To my surprise, they gave it to me on the spot for a trial period of 18 months.

Why did it fail?

It proved too difficult to get the product introduced to UK supermarkets without massive marketing budgets that Hunt Wesson expected us to fund. We did not have the financial resources to establish a new brand to compete with Heinz. The entrepreneur (me) had no knowledge or experience in selling products to supermarkets (Anchors 3 and 4).

Venture 7: Orville Redenbachers Gourmet Popping Corn

When Hunt Wesson acquired Orville Redenbacher's business I used my contacts there to negotiate the rights to sell their Gourmet Popping Corn in the UK. We had a massive launch at the UK Trade Centre and attracted a lot of PR.

Why did it fail?

We could not interest retailers in stocking up-market, highly priced popcorn. The consumer was just not ready to pay the premium for this specialised product (Anchor 2).

Venture 8: Honour snacks

This was another idea that I borrowed from the US. You leave a tray of snacks and sweets in offices with an honest box for payment. Each week you top up the tray and, in theory, collect the cash. Today in the UK this is a successful business model operated by "Snacks in the Bar" and a number of charities.

Why did it fail?

The trays and the cash boxes were both empty at the end of the week. At that time office workers in the UK were not willing to pay for the product (Anchor 2) – but happily took advantage of my 'gifts'.

Venture 9: Fortune teller balls

An entrepreneur approached me to help him to import glass fortune teller balls into the UK. I did identify the dangers of this business in advance, but I have included it here as it led to a much bigger opportunity.

Why did it fail?

The entrepreneur gave up as he did not sell enough balls. The market in terms of size and profit margins in cash was not big enough to sustain the business and the entrepreneur (Anchors 2 and 3).

Venture 10: Waterless swimming

A director of Trust House Forte went to Blackpool beach and had his fortune told. He asked the fortune teller where he could find a supplier of plastic balls that he had seen in an amusement centre in the US. The fortune teller said she did not know, but she gave him my details as I had supplied her fortune teller ball. I then received an enquiry for 100,000 plastic balls – which I took up immediately. The business was a massive success – I was even pictured in the *Financial Times* lying in a ball pond of balls. ▶

These "Ball Ponds" – a tank or inflatable filled with 20,000 plastic balls – are still around today.

Why did it fail?

Once we had established the market, our supplier began to sell direct. If we had not been so successful, the ball manufacturer would have left us with the market. There were few barriers to entry so we lost the market and withdrew. (Met all the Anchors but failed through very low barriers to entry).

Should I have spotted my mistakes?

I believe my assessment methodology of the four Anchors would have identified eight out of ten of my failures. The other two (Siemens Pumps and Waterless Swimming) needed higher barriers to entry to make them into viable long-term businesses. Their success meant that competitors in the form of the manufacturers entered the market. But note that four of what I call failures led directly to other opportunities.

Today, one of my most important roles is to facilitate "good business failures". That is, I help entrepreneurs to know when to quit, so that they do not leave debts behind nor suffer other trauma, when one particular venture does not work out. Most importantly I encourage them to learn from what went wrong.'

Questions

1 *What is the most likely cause of 'Fogg's Failures'?*

2 *Why does Chris Fogg believe that:*
  a *failure is an essential part of business success?*
  b *the study of failures is a very important part of learning about entrepreneurship?*

3 *Why does Chris Fogg have so many business ventures to his name? Should he have concentrated on researching just one of them to make it into a long-term success?*

4 *Check a successful business that you know about against Fogg's Four Anchors. For example, how would you assess the business of text messaging from mobile phone operators against each of the four criteria?*

Source: http://www.connectlondon.org

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6.7 NOTES, REFERENCES AND FURTHER READING

Notes and Further Information

1. Chris Fogg's current venture is 'Connect London' which obtains funding for technology and high-growth entrepreneurs and connects them to a network of like-minded business owners, mentors and supports (http://www.connectlondon.org).
2. For more on economic development life cycles see Chapter 4, section 4.3 'The nature of the relationship between entrepreneurship and the economy', which explores economic life cycles within phases of economic development. See also the Introduction to McCraw, T.K. (1997) *Creating Modern Capitalism: How Entrepreneurs, Companies, and Countries Triumphed in Three Industrial Revolutions,* Cambridge, Mass.: Harvard University Press. This gives not only some background to world economic development cycles but also examples of entrepreneurs who were influential in each stage.
3. The remarkable Toyoda/Toyota story is well documented. See for example Bernstien, J.R. (1997) Toyoda automatic looms and Toyota automobiles, in *Creating Modern Capitalism: How Entrepreneurs, Companies, and Countries Triumphed in Three Industrial Revolutions.* Cambridge, Mass.: Harvard University Press.
4. Most countries keep data on the business population including total numbers and indications of starts and finishes. The data here are taken from the Australian Bureau of Statistics (2007) *Counts of Australian Businesses*, including Entries and Exits 2003 – 2007 (www.abs.gov.au/AUSSTATS).

5. Both Marc and Isambard Brunel kept diaries and there are many books that document their lives. See for example: Brindle, S. (2006) *Brunel: The Man who Built the World*, London: Orion Books.
6. The Thames Tunnel is still in use today as part of the London transport network. There is a museum on the site which has an interesting website with educational material (http://www.brunel-museum.org.ik).

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