

# New Business Formation in Business Networks

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## SUMMARY

The broad consensus is that entrepreneurship and new business development impact economic growth and are important drivers of society as a whole due to their capacity to create wealth, product and process innovations, technological and organizational knowledge, and new jobs. Although in recent years we have witnessed a growing interest in academic research and policy initiatives for supporting new entrepreneurial activities, the relationship between the births and deaths of new businesses in many countries is alarming: The risk of failure for new ventures has been estimated at more than 50% in the first year and rising to 85% over three years. The casualty rate of new businesses continues to be an interesting phenomenon; to date, the available theories offer - at best - partial explanations of the high failure rate. The high failure rate of newly established businesses suggests that many questions remain about the complex process of new business formation still to be solved and warrant additional exploration. It appears to be of great interest, for both academics and practitioners, to gain more insights in explaining the difficulties that new companies face in their early development stages.

The aim of this study is to explore the difficulties encountered during the development process of a new business and contribute to identifying the causes of the frequent failures. In pursuit of this aim, we need to understand the factors involved in starting a new business and the difficulties related to establishing a new business as well as unpredictable obstacles to its successful continuation. The central assumption in this study is that key factors in explaining the success or failure of new ventures are the characteristics of the market context in which the new venture must become embedded through business relationships primarily with customers and suppliers. We, therefore, examine and interpret the difficulties a new business encounters in the course of its founding process through the use of a more contextualized view (or context oriented approach) of entrepreneurship and argue that embedding the new business in the pre-existing context is a central process in clarifying these difficulties.

The study comprises seven chapters divided into three parts; the first part of this study consists of a literature review, the second part is an empirical study of three new businesses, and the third part is a discussion of the findings and conclusions.

The literature review has led to identify in past research four theoretical approaches – namely, the neoclassical economic, the Austrian school of economics, the socioeconomic, and the marketing perspective – that offer different conceptualizations of the market and highlight several distinctive features of the business landscape in which new businesses emerge. On the basis of the literature review we find the marketing perspective – in particular, the view of market as a network– as a highly relevant concept for our purpose. The industrial network approach acknowledges the existence and centrality of relationships in markets and has had an important influence in formulating the concept of markets – or rather business networks – as a set of interdependent relationships that have significant consequences for the new business development process. Accepting that markets tend to display network-like structures implies that businesses are a node in a business network and that establishing a new venture is about creating a new node in the existing business network. Despite scholars' general acceptance of the importance of external interaction processes required to establish business relationships and become part of the context, these processes have seldom been the basis for understanding the difficulties characterizing the new business formation.

Empirically, this study is based on the elaboration of three case studies of newly founded businesses about to develop initial business relationships. The analysis of the case studies is particularly focused on configuring the activities, interfacing the resources, and negotiating the meanings with the actors involved when new relationship is developed. Methodologically we follow an inductive approach involving longitudinal qualitative research methods and multiple sources of evidence - namely, in-depth semi-structured interviews with key informants as well as secondary data resources - to investigate the topic. In all, we conducted 21 formal interviews with informants working in different functional areas of the involved three new businesses and 12 interviews with different external informants.

The findings provide support for the argument that building business relationships is critical for the development and success of a new business. In particular, that the difficulties and the unpredictability characterizing the processes of new business formation is related to difficulties in connecting to the pre-existing context in the dimensions of the resource constellations, activity patterns, and webs of actors when developing new business relationships. We further confirm that the difficulty of the task to develop new business relationships with customers and suppliers is related to the need to manage simultaneously all three layers of substance of business relationships - activities, resources, actors - as the failure in one layer, while the others are in place, can hinder the effective development of the initial business relationships. With regard to the difficulties encountered in developing new business we reached four main conclusions. The first difficulty in starting a new business is related to the fact that entrepreneurs (and management) in the initial states of the new venture tend, plausibly, to devote most of their attention and efforts to questions related to the internal issues of the venture - namely, the continuous improvement of the product/service features and production. Looking inward, rather than at the external relations and dynamics, leads to perceptions that interacting in customer-suppliers relationships and being externally interconnected are less important. This inward-looking orientation in the new venture tends to endanger the venture's successful development. The second difficulty is related to the fact that new businesses face greater difficulties in generating revenues from the potential customers than finding funds from investors and other funding bodies. Funds from investors means running the risk of neglecting efforts to seek customer approval and acceptance that translates into sales revenues. The third difficulty for new businesses concerns the organizing dimension, which is twofold; it includes both internal and external issues. The ways new businesses try to relate with the context shapes how the market is organized; at the same time, new businesses organization are influenced by the respective actions and reactions of the business partners. Finally, the fourth explanation of the difficulties facing new ventures is related to the fact that, to succeed, a new company must be economically viable. It has to generate positive economic outcomes for the partners (affecting their assets positively) and be economically sustainable by

generating sufficient revenues to cover the operating costs. We conclude the thesis by examining the implications of our findings for practice and further research. Discussing the implications for practice, we discuss the challenges to cope with and manage interaction activities so as to develop relationships with customers and suppliers. As for the implications for further research, we argue that the need exists to address more systematically and in depth the issue of interaction in the initial relationships of new ventures.

*Keywords:* entrepreneurship, new business venturing, business relationships, interaction

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*A mountain ... of thanks*

I really love mountains and the challenges the great outdoors has to offer: I enjoy the opportunity to confront myself with my limits; moving them forward a little bit every day is of pivotal importance for me in order to « grow » and to satisfy my innate curiosity. But I must admit that in terms of duration and commitment, writing this manuscript has been my biggest challenge by far.

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# Chapter 1

## Introduction

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### 1.1 NEW BUSINESS FORMATION AS A RESEARCH FIELD

The topic of this research is new business formation in business networks, and the background of this topic is entrepreneurship. Entrepreneurship and new business have become popular topics not only in academia, but also among policy makers, business practitioners, and international institutions. Reflecting this growing interest in recent years is the proliferation of journals, conferences, and other academic forums devoted to entrepreneurship. There is a broad consensus that entrepreneurship is an important driver of the economy and of society as a whole (Thurik & Wennekers, 2004; Van Praag & Versloot, 2007; Landes, Mokyr, & Baumol, 2010). This is due to its capacity to create new wealth, product and process innovations, technological and organizational knowledge, and new jobs (Drucker, 1985; Acs & Storey, 2004; Audretsch, Keilbach, & Lehmann, 2006). An extensive study by the Global Entrepreneurship Monitor (Results 2006) has shown a relationship between a country's level of economic development and its level of entrepreneurial activity. The economic magnitude of new business activities has been particularly apparent in the U.S. in the past 25 years, where two-thirds of net new jobs and 95% of radical innovations have been attributed to new businesses (Timmons & Spinelli, 2003; Reynolds, 2005). Because of this impact on economic

growth, many countries foster an entrepreneurial environment (Reynolds et al., 2001; Wong, Ho, & Autio, 2005; Ahlstrom, 2010).

## 1.2 AN INTERESTING PHENOMENON

The second aspect of this topic is more disappointing. Although in recent years we have witnessed significant rapid growth of academic researches and of policy initiatives for supporting new entrepreneurial activities, the relationship between births and deaths of new businesses in many countries is alarming; a high rate of new business failure can undermine the efficient operation of a market economy (Storey, Keasey, Watson, & Wynarczyk, 1987). That is, despite the growing interest and numerous studies conducted on entrepreneurship research, available mid-range theories offer, at best, partial explanations of failures and successes in new business venturing.

Numerous researches reveal that more than half of new ventures fail within the first year of setup (e.g. Bhide, 2000; Corman, Lussier, & Lussier, 2005), and that about 80% to 85% of all new ventures disappear within three years of their founding (Shane, 2003). In other terms, the risk of failure for new ventures has been estimated at more than 50% in the first year, rising to 85% over three years; accordingly, few survive more than a handful of years (Headd, 2003; Short et al., 2009). According to the U.S. Small Business Administration (SBA), more than 572,900 new businesses opened in 2003 but an estimated 554,800 closed that same year, and an additional 35,037 declared bankruptcy<sup>1</sup>. Regarding the Swiss context, the Confederation is characterized as one of the European countries with the most dynamic entrepreneurial activity; nevertheless, the survival of new Swiss companies is not high in the short-to-medium term. A study conducted by the Swiss Federal Office of Statistics (Results 2003) on the survival rate of new businesses shows that about 20% of them go out of business during their first year of life. That means almost 80% of new start-ups continued their activity at the end of

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<sup>1</sup> For further information, see: <http://appl.sba.gov/faqs/faqindex.cfm?areaID=24>

their first year and that after the second year, this number decreased to 72%. Only 54% of newly established enterprises survive the first four years<sup>2</sup>.

The casualty rate of new businesses is an interesting phenomenon. At the end of the day, various statistics reveal that of the 20 million businesses in Europe, if we count them as formal, about a million are born per year and about a million die each year, but we don't have a very good explanation for this phenomenon. Even if the topic of new business formation has received increasing attention both in the business management literature and in business practice, no acknowledged answer about the critical success factors that can influence the processes of new business formation has been given to date. A common perception is that the available theories that have been formulated offer, at best, partial explanations for failures and successes in new business development. Moreover, in the research literature on new business, which is credited with various beneficial outcomes, it is difficult to find a generally shared conceptual framework for further conceptualization (Koppl & Minniti, 2003).

We continue to know very little about the complexities that characterize new business formation processes (Zahra & Nielsen, 2002). The ongoing high failure rate of newly established organizations suggests that a better understanding of why new businesses fail and succeed is of great interest to public policy makers concerned with economic development. Entrepreneurship and the difficulties encountered during the process of new business formation are, in the broadest sense, our field of research

### 1.3 RESEARCH QUESTION

Abundant studies have focused on and reported many reasons for the success or failure of new business development (Song, Podoyntsyna, Van Der Bij, & Halman, 2008; Kumar & Ravindran, 2012). Nonetheless, empirical outcomes are often contradictory and fragmented (Shane & Venkataraman, 2000). More than 20 years ago, Low & MacMillan observed that "the list of potential pitfalls associated with starting a new

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<sup>2</sup> For further information see: Statistics on business demography: New businesses and their survival in the short-to-medium term, Swiss Federal Office of Statistics, June 2003.

venture appears limitless" (1988, p. 142). Why start-ups have such a short life could be related to very different matters. Gaskill et al. observed that "there are many questions still to be resolved and warrant additional exploration... previous studies do not provide a comprehensive or unified explanation for small firm failure... comparisons are needed between successful and failed small business owners" (1993, p. 28). We don't have very many theories that explain this phenomenon, and the available theories do not seem to provide much guidance for potential entrepreneurs. In fact, alternative ideas of the various dimensions contributing to success or failure have emerged gradually in a number of researches (Lussier, 1995). We thus return to the new venturing phenomenon to investigate what could be the reading keys of it, by revisiting the traditional literature that apparently offers three alternative interpretations of why start-ups are still highly vulnerable and prone to failure.

The recent resurgence of interest in the study of the entrepreneurial phenomenon, in particular the critical factors that can influence the process of new business formation, is evident in the proliferation of multidisciplinary studies and investigations. Scholars from different disciplines have focused their research insights on the identification of a variety of relationships and tools to help entrepreneurs meet and overcome the uncertainties and difficulties that characterize the early stages of the process of new business formation (Cunningham & Lischeron, 1991; Kuratko & Hodgetts, 1998). In particular, scholars of disciplinary research grounded in economics (Casson, 2003; Minniti & Lévesque, 2008) have been committed to producing new research approaches that have led to abundant new findings on and insights into new business development. These approaches have tried to acquire new evidence mainly with regard to entrepreneurs' personal traits and motivations and how these influence the way entrepreneurs recognize and exploit opportunities. But nowadays, as McKenzie, Ugbah, & Smothers (2007) argue, is the question: who is an entrepreneur, the right one? McKenzie et al. refer to an article written by Gartner (1988) in the late eighties in which he argues that new businesses and the formation of new businesses or the development of new businesses cannot be explained by the goodness or badness of the entrepreneur and by how good or bad he is at discovering and exploiting opportunities. According to

Gartner (1988) the critical thing to do is to shift the research focus from entrepreneurship towards new venturing processes since every new venture implies organizing – putting together resources and combining them to construct an organization. Hence, if we want to explain and try to understand how new business is developed we should be looking into this process because it seems to be laden with difficulties. Gartner pursued that particular direction and developed this issue by arguing that new businesses are born in a kind of pre-organizational form. And in order to explain why and how new businesses are born and how they are developed, we need to look at this pre-organizational stage. That is, we must examine how an organization is assembled before it starts producing and selling. These observations gave rise to a new stream of research in these studies of new business development, which is called new venturing. Two approaches have thus characterized the research on entrepreneurship: one examines the characteristics of the entrepreneur's personality and the abilities of this personality to discover and exploit opportunities; the other approach examines the problem of organizing and putting together a new business.

Another telling argument presented in the literature on entrepreneurship and new venture formation is that the context of a business is relevant for all companies, particularly for engendering an understanding of how new businesses are developed. A few years back, there was a significant shift from focusing on entrepreneurs' characteristics and the internal properties of an organization towards a more context-oriented approach. Accordingly, if we are to explain how and why new businesses are born, we have to look at the context in which they are born because the contextual characteristics influence the behaviors of a business. For instance the Resource Dependent Tradition (RDT), which was formalized in 1978 with the publication of "The External Control of Organizations: A Resource Dependence Perspective" by Pfeffer & Salancik, studies the degree to which external resources of organizations affect the behavior of those organizations. In this book, the two authors explain how and in what way businesses are context dependent. According to Pfeffer & Salancik, organizations are resource dependent, and the resources on which they depend ultimately originate from the context. Given that the environment, or context, to a considerable extent

contains other organizations, the resources one organization needs are in the control of other organizations. Through the analysis of some empirical case studies, e.g. Microsoft and Dell, the two authors emphasize how the external context might be an important factor for the way in which businesses develop. Also, more recent entrepreneurship research seems to recognize the complexities of the interplay between the new business and its context (Lechner & Dowling, 2003; Stuart & Sorenson, 2007; Sarasvathy, Dew, & Ventresca, 2009; Jack, 2010; Welter, 2011) and the consequences for the relevant unit of analysis, which are new businesses. Several different approaches examine the organization contexts (Stuart & Sorenson, 2005; Dyer & Gregersen, 2008; Boettke & Coyne, 2009); some of these study how the entrepreneur interacts with the context (social network) and how such interaction might influence the entrepreneurial process. Among those who have studied the structure and dynamics of business contexts is a research stream in industrial marketing – the International Marketing and Purchasing Group (IMP), that started 30 years ago with empirical studies on how business-to-business markets work. And here comes an interesting juxtaposition: on one side there is a research tradition on new business formation, the Resource Dependence Theory (RDT), that is context dependent (Pfeffer & Salancik, 1978); on the other side is a research tradition that has produced abundant empirical material on how these kinds of context work, the IMP Group. In 30 years of researches, the IMP tradition has highlighted many aspects about the functioning of the business-to-business markets. Taking this perspective, for businesses about to start, the importance of the surrounding context seems to be warranted by the presence of existing interconnected business relationships, which impose on the businesses wishing to enter a market a need to merge with an existing relational network context. Also, more recent entrepreneurship research tends to acknowledge that markets can be seen as complex networks of relationships that are the result of collective entrepreneurial action (Sarasvathy & Venkataraman, 2011). Hence, in this perspective, the “outside” matters and it is not possible to explain new business development without looking at how it merges into the pre-existing context. The idea is that in order to explain how new businesses develop, we have to look into the processes of interaction between the new businesses and the existing context (Davidsson, 2005).

Even if new entrepreneurships (Venkataraman, 1997; Shane, 2003) and marketing (Kohli & Jaworski, 1990; Narver & Slater, 1990) have long been acknowledged as two key concerns for new businesses, just recently the relationship between marketing and new business formation has attracted the interest of researchers (Ireland & Webb, 2007; Mohr & Sarin, 2009; Webb, Ireland, Hitt, Kistruck, & Tihanyi, 2011). The marketing focus on entrepreneurship has given less attention to the individual aspects within the new business formation process. Rather, the focus of marketing scholars in terms of entrepreneurships has actually been the new venture and its context.

To conclude, the relevance of the context in entrepreneurship research is not new; the argument that economic behavior can be better understood within its context is now well established. The review of the literature, on the one hand, confirms that managing business activities and becoming a successful entrepreneur is not an easy task; on the other hand, it clarifies that the context of a business is relevant for all companies.

Even if there is a growing consciousness in the business marketing literature of the relevance of the context for understanding how new businesses are developed, understanding why some new businesses succeed remains a major challenge for the entrepreneurship research community. That is, questions about the complexities underlying the processes of new business formation are still open. It seems desirable, therefore, for both practitioners (entrepreneurs, those who support and advise them, those who provide funding for their ventures, and public policy makers) and scholars to have access to a conceptual tool that would permit better analysis of the difficulties that are generated during the early stages of the process of new business formation. In other words, although we recognize the importance of the different insights about the many facets of entrepreneurial processes delivered by the various schools of entrepreneurship, we believe an original understanding of these issues could provide an alternative way for a new interpretation of the complexities that characterize the new business development process.

Since the reasons for new business failure or success remain unclear, the scope of our research is to review the process. In other words, this study deals with new business formation processes and the difficulties encountered during the initial

development stages of business relationships. Our main interest is to establish why it is so difficult to start a business and ensure its successful continuation.

Since we have found contrasting explanations about the difficulties encountered in developing new businesses, this study's primary objective is to make a contribution in this direction. Clearly, our aim is not to investigate the survival factors for new businesses but rather to explore the difficulties encountered during the development process of a new business and attempt to identify the causes of the high attrition rate. In pursuit of this aim we need to understand the critical factors involved in starting a new business and the difficulties of establishing a new business and unpredictable obstacles to its successful continuation.

In the next paragraph we will explain the understanding upon which the proposed study is founded. In particular, we will briefly introduce the analytical perspective of the IMP network approach which, in our opinion, has marked a significant evolution in thinking concerning the relationship between entrepreneurship and new business formation, while moving from a different starting point from that of the individual/internal perspectives outlined above.

#### 1.4 THE STUDY APPROACH

It would be grand if we could say we are able to provide answers to the specific question of what makes a new business succeed. But such an objective would be overly ambitious and not realistic. Instead, our aim is simply to contribute to a better understanding of how new businesses are born and what make them fail so frequently. In principle, we hope to better explain why and how a new business develops by examining what the entrepreneur's new business does in merging into the pre-existing context. This is a starting point we think can be useful in better capturing the interacting process between the new business and its context. Furthermore, we seek to establish whether we can better understand the development of a new business by examining problems relating to the organization itself, or whether we need to extend our examination to the contextual factors as well. To date, researchers from the business network theory (IMP group)

research areas, have provided us with a different perspective. A clear conclusion of the IMP's business market researches (e.g. IMP Journal, Issue 1, Volume 5, 2011) is that the success of a new business will depend on the effects the new entity have on the existing assets of other entities (Håkansson & Waluszewski, 2007). That is, if there are strong interdependencies in relationships between firms, these will have certain implications for the development of the new business. In particular, any new business will have to establish and develop a large number of interfaces with a variety of entities and activities (Håkansson & Olsen, 2012). Following this logic, the survival and subsequent prosperity of a new business is dependent largely on how it develops relations with others and how it interacts with them. The argument is that we cannot explain the failure or success of a new company simply by relying on the features of one entity. Instead, as suggested by extensive empirical researches, we need to look at the matching of the two entities and the impact the assets of one has on the other (Baraldi, 2008; Ingemasson & Waluszewski, 2009; Waluszewski et al., 2009; Bernardi, Boffi & Snehota, 2011). Consequently, it must be emphasized that the unit of analysis cannot simply be the features of the new business. Indeed, if we aim to explain why businesses fail or succeed, we cannot do this by examining the personality traits of the entrepreneur alone or by examining the internal organization processes. In addition, as suggested by the IMP researches, we need also to look at new business formation from an interaction perspective; we need to observe the context and nature of the interplay that exists between the newly developed business and the context.

Despite the general acceptance by scholars of the importance of external interaction processes that comprise the first steps towards becoming part of the context, and related management practices (Ford, Gadde, Håkansson, & Snehota, 2005; Palmatier et al., 2006; Tuli, Kohli, & Bharadwaj, 2007; Sarasvathy & Venkataraman, 2011), it must be recognized that these processes have seldom been the basis for understanding new business formation (Welter, 2011; Aaboen, Dubois, & Lind, 2011). In other words, despite the evident importance of the early interaction processes between the new business and its context (Håkansson & Snehota, 1995; Håkansson & Waluszewski, 2007; Milanov & Fernhaber, 2009), little is still known, both conceptually and

empirically, about how the early development of customer-supplier relationships and the interaction within these relationship impact the development and success of new businesses (Andersen & Kragh, 2009; Cornelissen & Clarke, 2010; Lowe, Purchase, & Ellis, 2012).

Given that there is a call for new studies that combine existing research on entrepreneurship in the context of business networks (e.g. Achim, Auer, & Ritter, 2006; Jack, 2010; Snehota, 2011) as it shows the potential for synergies that can yield additional insights into new business formation, we decided to "borrow" much of what has been understood by the IMP research on business networks as it would seem to offer a valuable perspective in identifying the possible variables that make the processes of developing a new venture so difficult. This perspective that highlights the interdependencies could be the underpinning of the major difficulties entrepreneurs have in founding a new business. Business activities involved in the formation of business relationships, namely the interaction processes between the firm and context and their implications for the development of a new company, will be the subject of our research. We will discuss this issue in more detail in Chapter 5, but we can anticipate that to clarify the implications for the configuration of early business relationships, we will focus our analysis on certain aspects widely discussed in studies of the entrepreneurial-related network approach. In particular, our study draws on a recently proposed model which summarizes an extensive empirical research on interdependencies and interaction in business relationships (Håkansson et al., 2009), and distinguishes three layers of interaction in business relationships: actors, resources, and activities.

Some research views new venture success as conditional on relating or contextual fit (Ingemansson & Waluszewski, 2009; Welter, 2011; Snehota, 2011, Johanson & Vahlne, 2011). In addition, we emphasize the role of the ability to relate to other parties in business relationships and to interact with them as highly important in developing new businesses. We believe a venture failure may be the unanticipated consequence of interaction between multiple actors interfacing with each other in a pre-established business network. As we will discuss in more detail in Chapter 5, empirically investigating these interaction issues amounts to investigating at the activity

level, at the resource level, and at the actors' level what kind of (arrangements) interdependencies have been put in place by the actors involved in setting up a business relationship. These interaction issues, that we will empirically explore through three case studies (cfr. Chapter 6), will qualify the underlying question of our research. That is, what are the difficulties in configuring activities, and interfacing resources, and the critical issues that arise in coping with unshared meanings among the actors in developing a new business relationship?

What we argue, is that a deeper investigation of the interaction activities involved in founding a new businesses, taking the business network approach, could provide novel insights into the difficulties encountered by entrepreneurs during the first stages of new businesses formation and their effects on new business development. Our intention will be to determine whether this approach offers some additional analytical concepts that more effectively illustrate the difficulties and unpredictability of this merging of the new venture into the market.

## 1.5 MOTIVATIONS

The interest in new business formation and entrepreneurship is linked to the author's personal background. I concluded my undergraduate studies in communication sciences with a master's degree in Marketing with a thesis about the business development models in the Swiss-Italian region of Tessin. Later, when I started my PhD course program in Business Studies and Communication, I became particularly interested in business-to-business marketing. In the course of my PhD studies I had the opportunity to do part-time work as a marketing assistant for the Start-up Promotion Center, a service set up between the Università della Svizzera Italiana (USI) and the Scuola Universitaria Professionale della Svizzera Italiana (SUPSI), in order to assist and support Swiss and foreign graduates who plan to start a new business in Canton Ticino. During this experience, which lasted a few years, I had the opportunity to establish contact with a group of people who intended to turn an innovative idea or project into an entrepreneurial venture. It intrigued me to see that some of the enthusiastic people I met

who wanted to become entrepreneurs were more successful than others. Some start-ups have been transformed into entrepreneurial realities; others, despite very serious efforts, stopped after a while. The question that spontaneously arose was: Why are some start-ups successful; and why do others fail after a short time? What are the main difficulties for start-ups? It turned out that although research on the success or failure after the start had been studied by many scholars, the literature offered various and contrasting, and mostly unconvincing, explanations for the difficulties in developing new businesses. I therefore found this field of study particularly challenging because it offered me the opportunity to take advantage of my marketing background and competence in that area and to apply it to the entrepreneurship issue – the formation and development of new businesses.

## 1.6 HOW IS THE WORK ORGANIZED

This thesis is structured as follows: In *Chapter 2* we articulate the research approach and the research methodology used to achieve the objectives of the thesis. Currently, the prevailing mode of doing research is to follow a confirmatory research approach, very sophisticated methodologically. By following a PhD seminar given by Tellis (2008)<sup>3</sup>, we became convinced to follow a discovery-oriented research paradigm that seems particularly suited to the kind of phenomena we want to investigate as it suggests starting from an empirically observable phenomenon. Since we are interested in tracing and understanding the undertakings a new business has to deal with in developing new business relationships during its formation processes in order to merge into the market – by nature an empirical phenomenon – this approach seemed indeed to be best suited for studying a phenomenon which is simultaneously much studied but still in need of producing valuable insights. Given that approaches and theories available to address a univocal phenomenon are countless, we are set to start from an empirically observable phenomenon, namely the new business development process. However, while the

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<sup>3</sup> PhD IPSS Innovation Seminar, Tellis (March, 2008), “Alternate Paradigm of Research”; Marshall School of Business, University of South California.

discovery-oriented approach serves as an interesting starting point, it is also true that any observation of the empirical phenomenon is theoretically laden (Glaser & Strauss; 1965, 1967). Therefore, the understanding upon which the proposed study is founded derives also from the literature review. In fact, this will be the aim of chapters 3, 4, and 5 in which we discuss some very central concepts about entrepreneurship, business markets, and business relationships proposed in economics and social science, including marketing theories. The discussion about the research approach is followed by a discussion about how this research examines, explains, and illustrates significant facts. In particular, we have chosen the case studies research method. In this thesis we report three case studies of new ventures. The three case studies in this thesis have been constructed from two main data sources: in depth semi-structured interviews and secondary data resources. The cases in this study lean predominantly on a historical reconstruction – through key informants’ interviews – of past events that occurred in the development of business relationships, as well as on the description of current relationships. At the conclusion of the chapter we provide a description of the case selection, data collection, and analysis.

In *Chapter 3* we will review the main contributions from the literature on entrepreneurship and new business formation and review studies that have addressed the issue from different perspectives. To better understand the evolution of studies related to entrepreneurship and new business formation, we have directed our literature research on the concepts of entrepreneur, entrepreneurship, and new business formation, with the dual objective of capturing state-of-the-art studies in academic works and understanding the major research perspectives adopted to study the phenomenon we are interested in. This allows us to introduce the three major contributions in the literature that have focused their investigation on identifying different critical factors that enable or limit new business development processes: the trait approach, the functional approach, and the new venturing approach. The first line of research we identify, the ‘trait approach,’ embraces all studies concerning the “entrepreneur's personal and individual variables” that play a key role in the process of genesis and further development of new businesses. We will see how insights gained from this research have been influential in shaping the

research on entrepreneurs' managerial functions and their influence on venture creation, founding, success, and survival (Stuart & Sorenson, 2005). This is particularly true for the second approach we examine, the 'functional approach,' which identifies the entrepreneurial phenomenon in the accomplishment of certain functions and activities or in the possession of certain requirements. We will conclude this chapter by discussing the more recent research approach, the 'new venturing approach,' which posits a shift from internal factors, such as entrepreneur personality traits and managerial functions, towards the study of external factors, such as the context and the resource conditions. This review brought us to argue that current research on entrepreneurship not only acknowledges the importance of the context of entrepreneurship activities, but that such thinking also implies entrepreneurship is no longer recognized as an individual phenomenon but as a phenomenon that depends (heavily) on its context. This allows us to introduce the argument that it is important to broaden the research to the relevant business landscape and to see how the new company is connected to the context and how this affects its development.

In *Chapter 4* we will discuss the different conceptualizations of the market that highlight relevant characteristics of the market landscape in which new businesses emerge. We will review the literature on market theory to present approaches to the market in different disciplinary fields with the aim of showing how the ideas and conceptualizations of business markets are related to numerous empirical studies that have highlighted several distinctive features affecting the conduct of market actors and the new venture development process. We will see that contributions to the topic can be found not only in prevailing ideas proposed in neoclassic economic theory, but also in other disciplines such as socioeconomics, in the Austrian school of economics, and in marketing research. We will discover how in marketing research there have been conceptualizations that provide an idea of the scale and complexity of industrial markets and how the network perspective in the marketing literature seems to provide a more comprehensive description of the characteristics underlying the dynamics of industrial markets. Before turning our interest to the juxtaposition between the social network and the business network perspectives, we will briefly comment on the main specificities that

distinguish industrial markets from consumer markets. Successively, we present and illustrate the conceptual framework that we will refer to as the *business network perspective* and then discuss why the network approach highlights some market characteristics that could be the underpinnings of the major difficulties that can make the process of new business formation so uncertain and complicated. In particular, the picture of the “market as a network” suggests that the development of new business entails merging in a pre-established network of business and the need to develop multiple relationships in order to become connected and to make use of the other economic organizations. We conclude the chapter by inferring that it is this merging process on the pre-existing network and the development of new business relationships that represents a critical point in the development of a new business.

**Chapter 5** is dedicated to the issue of analyzing business relationships and the critical processes underlying their development. Firstly, we review different research streams that look at business relationships as a phenomenon critical to explain economic behaviors. In discussing some of the current ideas and conceptualizations in business relationships we argue that the perspective suitable to guide the analysis and reflection on the formation of new business relationships is the one that refers mainly to the literature in industrial marketing research, especially the one related to the IMP (Industrial Marketing and Purchasing) tradition. This allows us to introduce the Activity-Resource-Actor (ARA) model (Håkansson & Snehota, 1995) that provides a framework for analyzing the content and function of business relationships. It is argued that business relationships are characterized by intense and complex interaction processes and that these processes are important for relationships development dynamics, for how the parties interface resources, coordinate activities, and build joined and shared meanings, and ultimately for the dynamics of the business networks. Dynamics and interaction in business relationships are discussed in order to point out *why* and *how* interaction processes are fundamental to explaining the undertakings and difficulties a new business has to deal with in developing new business relationships during its formation process. As discussed in Chapter 2, our study deploys both longitudinal qualitative research methods and multiple sources of evidence to investigate the topic.

The qualitative research approach, rather than focusing on questions of “how much” and “how many,” seeks to understand more than to explain, as it answers questions of “what” and “why” and “how” as in our study. Hence, our focus was not to develop a falsifiable hypothesis, but rather to articulate dependable, credible, and transferable propositions. We therefore conclude the chapter by formulating four propositions derived from the literature on the nature of businesses developing new business relationships that have guided our empirical investigation. In particular, the four propositions we will investigate empirically and that will qualify the underlying question of our research are the following:

1. The difficulty in developing a new business and the relatively high failure rate are related to the complexity and difficulty of the task of developing new business relationships;
2. The complexity in developing new business relationships is attributable to three different aspects related to the development of effective solutions in business relationships. These aspects or layers are, (i) configuring activities (Håkansson & Snehota, 1995; Dubois & Araujo, 2006), (ii) interfacing resources (Bengtson & Håkansson, 2008; Baraldi, 2008), and (iii) creating shared meanings (Hodgkinson, 2005; Weick, Sutcliffe, & Obstfeld, 2005; Waluszewski, Baraldi, Shih, & Linne, 2009);
3. Relational business solutions and arrangements cannot be developed unilaterally (Sawhney, 2006; Baraldi & Strömsten, 2006; Tuli, Kohli, & Bharadwaj, 2007; Vargo & Lusch, 2008). Novel solutions, on which the relationship development of a start-up depend, are defined jointly by the parties involved and are the outcome of a process of coping with many arrangements that aim at interfacing a large and complex set of operations (Harrison & Waluszewski, 2008; Oliva & Kallenberg, 2003; Davies, 2004; Kapletia & Probert, 2009).

4. Emergent business solutions and arrangements that are conceived in conjunction with others in order to embed them into users contexts (Håkansson & Waluszewski, 2002; Håkansson et al., 2009; Ingemansson & Waluszewski, 2009) will be successful only when they have positive economic consequences for the assets of the parties involved (Håkansson & Harrison, 2006).

In *Chapter 6* we present three different case studies of new ventures selected to illustrate and highlight some aspects required of a new business to become a node in the pre-existing business network through the development of new relationships. The cases have in common that they are start-ups in early stages of development of the initial business relationships but their activities are in different businesses and the focus of the case studies is on different aspects of new business development. Each of the cases focuses on one of the three facets of ARA model discussed in Chapter 5, namely on activities, resources and actors. The first case study, SafeVine, concerns a new venture born as a project that aimed to find a solution for the development of particular vineyard diseases through an innovative system based on wireless sensor networks; the thrust of this case is on the activity layer in business relationships. The second case study, Ekobike, revolves around the idea of three partners developing and selling high-performance electric motorbikes; the Ekobike story hinges on the resource dimension of a new business venture. The third case study, Concertlab, concerns a new business formed with the aim of creating a web platform dedicated to music to facilitate interactions and communication between the various interested parties operating in the live-music business; this case highlights issues related to connecting actors. The cases are organized as follows: Each case is introduced by a brief case summary that provides a first picture of the new businesses and the roots of business idea to get an overall view. Subsequently, we organize the story of each of the three cases around the following topics: 1) for each of the three start-ups we describe the path followed by the new venture in order to turn their business idea into an organized business; 2) we describe the

business model and the business practices such, as the request for funding, that new businesses performed in order to develop their product or service; 3) we report how each of the new ventures managed the development of their first customers' or suppliers' relationships during the process of new business formation; 4) for each of the three start-ups we then make a brief exposure of the economic results in order to provide an indication of the investment success of the start-up observed; 5) the case ends up with a description of the specific business context in which they aim to merge. The purpose of these cases is to illustrate some of the critical issues involved in embedding the new venture in the existing business network through developing the initial business relationships. We will describe how these processes occurs and which are the main problems and needs of synchronization that may arise. The case description presented in this chapter will be further developed in Chapter 7.

Finally, in *Chapter 7*, we discuss the findings and implications of the study. On the basis of the findings we argue that indeed the difficulties in developing new ventures depend largely on merging into the pre-existing business network, because any new venture needs to address the issue of interdependencies, creating resource interfaces, and connecting activities. This is a complex, collective task performed jointly among the partners in the relationships being developed. The need to interact with others implies that the process cannot be handled and controlled entirely by single entrepreneurs. Using a discovery-oriented approach as some business researchers advocate (Golder, 2000; Tellis, 2008), we then present our findings with regard to the possible theoretical and managerial implications related to the theoretical propositions advanced in Chapter 5. We argue that the critical point of developing a new business is not only to discover opportunities or to find a way to conceptually exploit a new solution or product. Neither is it just about formally organizing the new business internally. Rather, we suggest that a moment of extreme vulnerability and difficulty for the development of a new business is related to the unpredictable, costly, and complex interaction activities of several actors interfacing with each other in a continuously evolving pre-existing context. We conclude the chapter by discussing the implications of our findings for practice and further research. Among the implications for practice, we discuss the challenges to management

in relating to other parities. In particular, a greater awareness of the centrality of interactive communication, in which learning, interpretations, perceptions, and expectations are mutually developed and adjusted, can help to manage the development of a new business more effectively. Among the implications for further research, we suggest that research should address the issue of interaction in the initial relationships of new ventures more systematically and in greater depth.



## Chapter 2

# Research Approach and Methodology

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This chapter will present the research approach and research methodology used to achieve the objectives of the thesis. We will first present our research approach, the so-called discovery-oriented paradigm, which deals primarily with the description and analysis of empirical phenomenon to explain significant facts that characterize the “real” context. A discussion of the research approach is followed by a presentation of the methodological framework used in this study. In particular, we will discuss why the multiple case studies research method is used for the purpose of this thesis. This is followed by an explanation of how we choose the three convenient and representative cases of firms in the early stages of their development. In the following section, we discuss the selection of data collection tools used in this study. Finally, we discuss how the data have been analyzed.

### 2.1 CHOICE OF THE EPISTEMOLOGICAL APPROACH

Given our research topic, the difficulties in starting a new business, we could start developing our study from a theory, but this is tricky and pathless. Several mid-range theories have been formulated about the features of the new business development process; nonetheless, it is difficult to find a conceptual framework that could be considered a generally shared platform from which to start further conceptualizations

(Koppl & Minniti, 2003). Not the least because there are a number of theories relating to new business enterprises we will discuss in more detail in the following chapters.

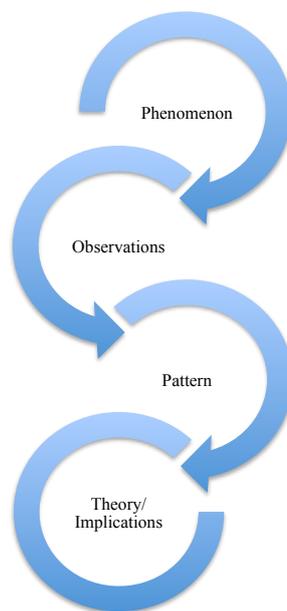
Therefore, while the empirical phenomenon we want to observe is rather univocal and the approaches and theories available to address the phenomenon are countless, our thesis starts from an empirically observable phenomenon, namely that it is difficult to develop new businesses. In particular, through a careful observation of the relevant phenomena, we will then try to develop some novel insights and implications. It might seem we go against some academic traditions; however, the epistemological approach we intend to adopt is not as unusual as it might appear at first (Tellis, 2008; Golder, 2000; Wiklund et al., 2011). It has been observed that even academics from leading business schools are building upon empirical data and questioning the way we view marketing phenomena (Hauser, 1985). Hence, in the next paragraph we will discuss the starting point of our research, namely the role of the empirical phenomenon on theory construction according to the discovery-oriented research approach.

### 2.1.1 THE DISCOVERY-ORIENTED RESEARCH APPROACH

Regarding the role of the empirical phenomenon in theory construction, some scholars suggest starting with a description of the phenomenon the researcher is interested in and then, afterwards, going through the analysis of it to find some possible inferences (Hauser, 1985; Varian, 1997; Tellis, 2008). This research approach, called the discovery-oriented approach, as opposed to the prevailing confirmatory-oriented approach, is discovery oriented in the sense that it tries to gain new insights, starting from empirical observations. In some ways, it can also be intended as a refutational method as it usually refutes what the literature holds as true, or what people generally believe is true. Some scholars argue that this approach can be much more impactful than others since much more interesting insights can be developed from getting in the empirical phenomenon and then coming to theories or implications (Davis, 1971; Tellis, Chandy, & Ackerman, 1999; Golder, 2000; Tellis, 2008). As in our case, it is also of interest that Wiklund et al., (2011, p. 5) “strongly recommend that entrepreneurship research be unified as a field

approached theoretically and empirically in terms of the phenomenon.” The pattern that is usually kept in discovery-oriented research is the following (Fig. 2.1):

Figure 2.1 The Discovery-Oriented Research Pattern



(Source: Adapted from Tellis, 2008)

According to Tellis, Chandy, & Ackerman (1999, p. 129) "Empirical articles are those that primarily deal with the description or analyses of phenomena." Hence, here the focus of a scientific work is to examine, explain, and then determine significant facts in "nature." The idea is that empirical phenomena really embody the bedrock of science and theories and, in the particular field of entrepreneurship, "...they address issues that really matter and make important contributions to scholarship but also to making the world a better place" (Wiklund et al., 2011, p. 7). Carrying this logic to the extreme,

understanding empirical phenomena, describing them and trying to explain them is what science is all about. Furthermore, since empirical phenomena are permanent and always present, they also contain problems that permanently haunt researchers and are juxtaposed with the theory construction that starts from the hypothesis (Tellis, 2008). The empirical phenomena contain puzzles that beg for solutions that can be difficult to provide and puzzles may remain without solutions for a long time, in some cases decades or centuries. Hence, given this permanency, those interested can investigate the same empirical phenomena and develop fresh insights from such investigation. In other words, description or analyses of empirical phenomena allow for fresh, unique observations and interpretations (Tellis, 2008; Carter, 2011; Wiklund et al., 2011).

As Hauser (1985) and Tellis (2006; 2008) suggest, if we look at eminent theories of the past there are various examples of people who have advanced great theories, starting from the description and observation of empirical phenomena. Examples of such scholars are scientists such as Thomas Kuhn (1922–1996), Georg Mendel (1822–1884), Charles Darwin (1809 –1882), and Johannes Kepler (1571–1630). They didn't start from a theory, and then developed some hypothesis, and finally tested this hypothesis. For instance, Thomas Kuhn, the well-known American historian and philosopher of science, in his most popular and controversial book "The Structure of Scientific Revolutions" (1962) presented a meta-theory of science, a theory about the development of science where, outwardly, he didn't start with a theory. Rather, he looked at how science had developed and then came out with his "paradigm shifts" theory. Mendel, the famous Augustinian friar, biologist, and mathematician, was considered the precursor of modern genetics for his observations and laws on the hereditary characteristic. In order to demonstrate that the inheritance of traits follows particular laws, between 1856 and 1863 he performed about 29,000 experiments to cross one variety of peas with another. Through these experiments, he could observe some patterns and from these he derived what is today known as Mendel's law about hereditary (Henig, 2001). Darwin, famous for having formulated the theory of evolution of plant and animal species by natural selection, and for having theorized the lineage of all primates (including humans) from a common ancestor, is another example. After long

and careful observation of plant and animal species that inhabited different lands, he came up with his famous evolution theory. His theory was actually based on 25 years of observations that brought him to the formulation of a revolutionary biological principle that turned out to be the only scientific way of interpreting the dislocations and variety of species living in different contexts (Pievani, 2012). Kepler, the well-known mathematician, astronomer, and astrologer, used empirical data to formulate his laws governing the movement of the planets, which are today known as Kepler's planetary motion laws. In fact, even if these eponymous laws bear only the name of Kepler, they have been codified on Brahe's works of 20 years' of empirical observations. After the death of Brahe, Kepler came into possession of the largest quantity of more precise data ever collected on the positions of the planets. The inheritance of these empirical measurements allowed him to develop the laws that regulate the movement of the planets. Kepler has thus reproduced Brahe's measurement by setting out to complete Brahe's unification. However, Kepler would not have been able to do so if he had been true to the data collected by Brahe. Therefore, "With his genius and his faith in the accuracy of the measurements made by Brahe, Kepler has been able to see simplicity where his contemporaries saw complexity" (Hauser, 1985, p. 347).

If we consider these four great theories from four quite different fields, we find that some of the greatest theories have been developed not by looking initially at the 'literature' and then developing a theory; rather, they have been developed by getting in the phenomena and then coming up with theories.

A good theory is the simplest explanation for the most complex phenomena (Tellis, 2008). For example, Darwin's theory of evolution actually can be reduced to two very simple principles (the principle of adaptation and the principle of heredity). Kepler's three laws of planetary motion are illustrations of how great theories rose from the observation and explanation of complex phenomena. There is no reason to complicate what is simple, and a demonstration should seek simplicity and conciseness. This means that – among other possible explanations for an event – we must accept the most "simple," not in the sense of the most "naive" or the one that spontaneously comes to mind, but one that appears to be reasonably true without attempting an unnecessary

complication of it by adding additional causal factors. Conceptually, the principle of simplicity was well known throughout medieval scientific thought, but it acquired a certain dignity with the Ockham's Razor methodological principle expressed in the 14<sup>th</sup> century by the English philosopher and Franciscan friar William of Ockham. What his principle suggests is that among the explanations of natural phenomena, we should choose one that does not multiply unnecessary entities: "*non sunt-multiplicanda entia*"<sup>4</sup>.

When we are building or expanding a theory, our purpose should be to gain more insight rather than to lose some from expanding the theory or adding more detail. However, research today seems to favor complexity or the adoption of complex models above simple theories or simple models (Tellis, 2008). The most common methods used today in the social sciences are surveys, experiments, and econometrics techniques to test theories (Franses, 2005). However, the discovery-oriented approach suggests observations should be made to confirm or reject the inferences about phenomena. Comparing the two approaches, the confirmatory-oriented one that starts from the literature, and the discovery-oriented one that suggests starting from empirical phenomena, it appears that the goal of the confirmatory approach is to see if the theory withstands a strong test, while the goal of the discovery approach is to find a pattern that is unexpected with respect to the current belief. The key value in the confirmatory approach is a strong theory developed by the mean of tight test (statistics), while what it is being proposed in the discovery-oriented approach is brevity, simplicity, and deep rich data.

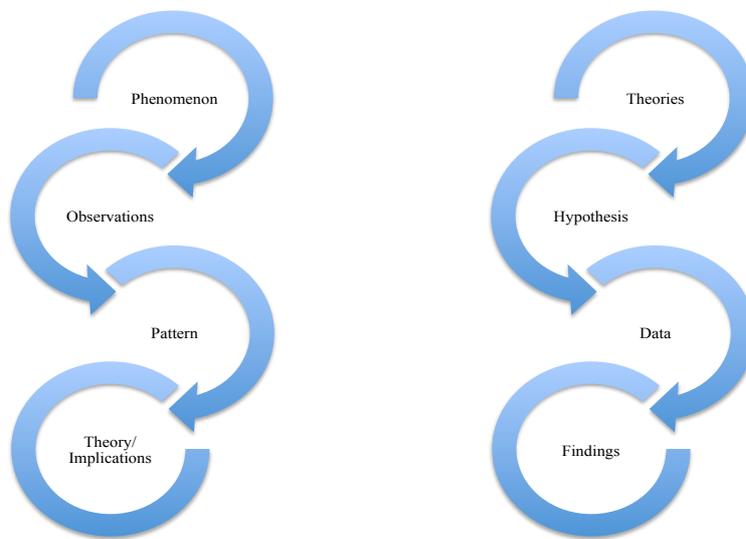
According to Tellis (2008) the existence of assumption per se is not a limitation of a theory, but the strength of a theory is whether it is parsimonious, simple, and that it can explain a number of facts. That is something we would like to aspire to. In our study, we will strive for simplicity and parsimony in explaining the empirical phenomenon we are interested in. As a result, the path of the discovery-oriented approach (Fig. 2.2),

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<sup>4</sup> For further information see William of Ockhams' Biography in Encyclopedia Britannica: <http://www.britannica.com/eb/article-9056715/William-of-Ockham>.

which will be followed in this thesis, appears to be different from what is most common in business studies today (Fig. 2.3):

Figure 2.2 Discovery-Oriented Approach    Figure 2.3 Confirmatory-Oriented Approach



(Source: Adapted from Tellis, 2008)

### 2.1.2 IMPLICATIONS OF THE PROPOSED APPROACH

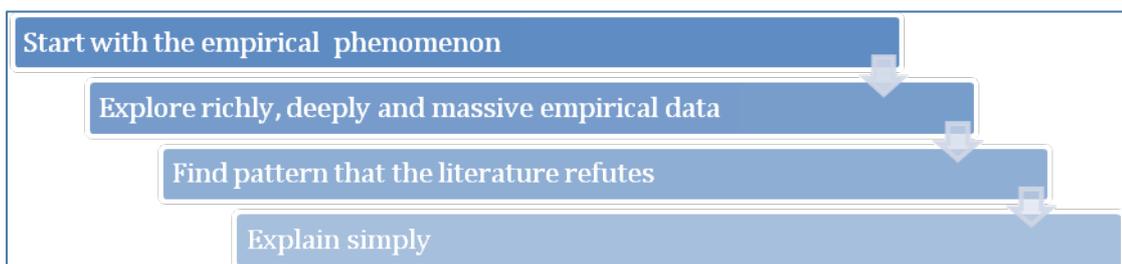
Of course, the proposed discovery-oriented approach is not exempt from weaknesses. One of the risks is to grasp spurious patterns. To overcome this problem, Tellis (2006; 2008) suggests collecting abundant empirical data and getting extensively into the phenomena rather than doing quick little studies and testing the hypothesis. It is implied that creativity is needed to see the new pattern; that is, we may collect a lot of data and see no pattern. Kuhn (1962) points out that some people look at the data and see nothing, and others look at data and see something extraordinary. In that sense, creativity is

needed, because if you don't have your own point of view, you can't make sense of what you are looking at and it is almost as if you are looking at nothing. Tycho Brahe, for instance, spent 25 years collecting data and didn't see the three planetary motion laws, but Kepler saw them. From the technical point of view, Brahe's contribution was decisive. He was able to make observations of great accuracy. He revolutionized previous methods by collecting a huge amount of observations with a precision that was unprecedented in history. His information offered a new approach to the problem, a prerequisite for solving the "problem" which, for so many centuries, the astronomers had questioned. According to Kuhn (1962), Kepler was able to take advantage of the excellent measurements made by Brahe and was finally able to solve the problem of the planets, transforming the complicated system of Copernicus with a very simple and accurate technique to calculate the position of the planets.

What we have seen is that data collection (e.g. Kepler & Brahe) and observation (e.g. Darwin & Linnaeus) are critical factors in the discovery of scientific knowledge. And it seems this applies to marketing research too (Hauser, 1985; Tellis, 2008).

To sum up, following the discovery-oriented approach, the research path we will respect in our research is the subsequent (Fig. 2.4).

Figure 2.4 The Discovery-Oriented Research Path



(Source: Adapted from Tellis, 2008)

Although this discovery-oriented approach may seem controversial, a number of scholars with a noble past have recognized the advantages of employing this methodology. But, of course, we must not forget that all the observations, even those

guided by the discovery-oriented approach, are also always guided by some pre-existing theories (Khun, 1962; Feyerabend, 1965, 1975; Kordig, 1971; Hanson, 1971; Toulmin, 1976). According to Morgan, “practice is never theory free, since it is always guided by an image of what one is trying to do. The question is whether we are aware of the theory guided action” (1986, p. 336). What such a position suggests is that observations of practice too are also never theory free, and the question of whether the theory is guiding the researcher’s action, and to what extent, remains open. No empirical observation is theory free in the sense that observations of practice are never free of some assumptions or interpretations. Theory’s role in practice is in organizing a “mind’s eye” of the cognitive experience of a phenomenon (Margenau, 1966). Hence, any empirical observation is “filtered” by an idea. Some great pioneers of science, e.g. Darwin, Kepler, Kuhn, Mendel, and Linnaeus, made classifications of what they observed, starting with an idea. They observed a particular phenomenon and then made the classifications according to the similarity or by using other hierarchical classification schemes<sup>5</sup>. Therefore, all classifications are manifestations of an instinct guided by the will of taxonomic ordering of the world. And because of these acquired schemes, observations account for what reality is. That is, we will have a good appreciation of the reality but not the complete truth. According to Hayek, “Science does not explain the unknown by the known as is commonly believed but, on the contrary, the known by the unknown” (Hayek, 1967, p. 5). We cannot describe the reality in full, because it's too complicated. “The early developmental stages of most sciences have been characterized by continual competition between a number of distinct views of nature, each practically derived from, and all roughly compatible with, the dictates of scientific observations and method” (Kuhn, 1962, p. 4). Hence, observations are never theoretically free because what is observed is still filtered by prior ideas.

What is a good theory then? According to Davis (1971) a theory is considered good not because it is true, but because it is interesting. Having said that, when can a theory be considered interesting? A theory is interesting when it engages the attention

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<sup>5</sup> Carl Linnaeus (1707–1778), Swedish physician and naturalist, who is considered the father of the modern scientific classification of living organisms defined the basis of the method of taxonomic classification, which is still used today.

(Ibid. 1971). That is, the defining characteristic of a theory, which some audiences may consider interesting, is that it stands out in their attention in contrast to the web of routinely taken-for-granted propositions that make up the structure of their everyday life. Expressed concisely, as Weick (1995) notes, a good theory explains, predicts, and delights.

However, while this discovery-oriented approach is an interesting starting point, it is also true that any observation of empirical phenomenon needs to be theoretically laden (Glaser & Strauss, 1965, 1967). Theory is critical in deciding which empirical phenomena to observe. “To understand reality, we must abstract from reality. We model the world in its ideal case and only then do we work backwards to incorporate troublesome everyday effects” (Hauser, 1985, p. 350).

That is why, in our thesis, we start by reviewing existing theories in the literature. In particular, we look at different currents of thought that can help us organize the observations. We begin, therefore, with a literature review to which we devote chapters 3, 4, and 5. In particular, as the topic of entrepreneurship is the object of study of multiple disciplines, in Chapter 3 we review ideas of what entrepreneurship is by retracing the main contributions in this regard. This review brings us to argue that current research on entrepreneurship not only acknowledges the importance of the context surrounding entrepreneurship activities, but such thinking also implies that entrepreneurship is no longer recognized as an individual phenomenon but as a phenomenon which depends (heavily) on its context. In Chapter 4, we therefore turn our attention to the context, particularly the different conceptualizations of industrial market theory. This literature review outlines which of these different approaches on business markets should constitute the main theoretical framework of this thesis. In particular, with regard to our research approach, we adopt the network approach that, by studying the interdependence of business relationships and their effects on the businesses involved, we introduce the concept of industrial markets as business networks. By taking this business network perspective as a framework of analysis, our aim is to investigate the problem of new business ventures as merging into a pre-existing business network. In Chapter 5 we proceed to review different research streams that examine business relationships as a

phenomenon critical to explanations of business market processes and dynamics. In discussing these different streams involved in analyzing business relationships we argue that the perspective suitable to guide the analysis and reflection on the formation of new business relationships seems to belong to the IMP research tradition with its ARA model as a tool for describing and analyzing business relationships.

Methodologically we follow the multiple case studies research method. We conduct three empirical case studies guided by four major research propositions that, according to Tellis (2008), are necessary to abstract from the real and helpful in focusing the study, since they will guide both the data collection and the discussion of the findings (Yin, 2003).

The methodological choice will be discussed in more detail in the next section.

## 2.2 CASE STUDIES AS METHODOLOGICAL CHOICE

In this section, we will discuss our methodological choices. The focus on the research method is important because it allows for the generation of theories and implications, avoiding the “data to say what they cannot say,” or worse, to enunciate theories that contrast with empirical evidence. The research method is mainly a choice between alternative ways of proceeding. Certainly, the choice of research method should be functional to the nature of the problem, the characteristics of the empirical situation we want to investigate, and to the purpose of the study.

The present work has two main objectives of empirical investigation: describe the business relationships development dynamics taking place in the formation of new businesses, and examine the impact of business relationship development on the development of the new business venture. According to the assumption of the qualitative research paradigm, the "sense" of the empirical phenomenon should not be assumed *a priori* by the researcher and translated into some tools (such as the items of a questionnaire) to be then empirically verified following a confirmatory logic, which will necessarily be asymmetric because the sense is made only by the researcher; the “sense” of the empirical phenomenon should rather be discovered through methodologies that

facilitate its emergence (Denzin & Lincoln, 1994). For instance, for the current research we excluded from the beginning the possibility of using the experimental method, which tends to be adopted in disciplines in which it is possible to conduct experiments under conditions of imperturbability or certainty. The reason for this is that in order to understand the implications of developing new business relationships for new businesses it is unthinkable to manipulate independent variables and conduct randomized experiments to establish causal relationships, as a physical scientist does. We used the methodology of case study in the form of descriptive multi-case studies (Yin, 1993, 2003), as we believe this to be the most appropriate of the five main methods used in the social sciences (experiments, archival analysis, surveys, histories, case studies). In the next paragraphs we will discuss in more detail why we adopt qualitative methodological approaches such as multiple case studies.

### 2.2.1 THE CASE STUDY

In Chapter 5 we will argue in more detail that business relationships are multifaceted and complex since they are consolidated through interaction processes, rather than by individual and isolated transactions; furthermore, they involve specific investments and mutual adaptation between and within the parties involved. Studying business relationships thus requires us also to consider the context in which they occur, a purpose that cannot be achieved through methods that maximize data integrity (Yin, 2003). Rather, what we need is an approach that facilitates the description of a phenomenon within its context using a variety of resources. According to Dubois & Gadde, “The interaction between a phenomenon and its context is best understood through in depth case studies” (2002, p. 554). As such, the case study, as an empirical inquiry, appears to be particularly useful whenever the phenomenon to be investigated is closely related to the context in which it occurs (Pyecha, 1988; Dubois & Gibbert, 2010). Furthermore, according to Dubois & Araujo (2004), the intrinsic flexibility of this method fits with the study of complex evolving relationships and interactions in business markets. Briefly, the use of case studies helps the study of a phenomenon in its context. Several

researchers have claimed the helpfulness of case studies when studying industrial networks (e.g. Easton, 1998; Dubois & Araujo, 2004; Halinen & Törnroos, 2005; Dubois & Araujo, 2007; Easton, 2010). For our purposes, therefore, it seems useful to base our description and analysis of the phenomena we are interested in on case studies so that we can verify whether the propositions we can formulate after reviewing the existing ideas, can find correspondence with the new business investigated and analyzed.

Of the various means through which case studies can be distinguished – exploratory, descriptive, and explanatory – we opted for the second, as our intent is to describe a phenomenon within the context in which it occurs. In particular, if the purpose of the study is to collect information to provide a picture that describes business practices in the development of a new relationship, then the nature of the study we will undertake is substantially descriptive and of course, as discussed, discovery oriented.

A second step in our investigation has been to decide whether the study is to be a single or multiple-case study (Yin, 2003). In this work, we use multiple-case studies as it is considered a valid means of investigation when it is intended to describe, as in our case, a particular pattern in certain processes and explains the differences throughout the different cases by comparing them to each other (Aaboen et al., 2012). In addition, since the single case study appears to be more justified when the single case represents a critical test of a theory or an existing, rare, or unique event (Yin, 2003), to elude the problem of the non-generalizability in other settings we thus decided not to use the single case as it may produce results that are too context specific. On the other hand, according to Aaboen et al.: “...multiple case studies may, based on the variety between the phenomenon and contexts, contribute both to a better understanding of the interfaces between the phenomenon and the contexts and also to identification of different patterns in the interplay between them” (2012, p. 236). Hence, the multiple case studies method, has been frequently applied in business marketing in recent years (e.g. Hulthén, 2002; Hjelmgren, 2005) as it provides opportunities to capture a variety of patterns of the observed processes.

## 2.3 CASES SELECTION

Even if we decided to follow the discovery-oriented approach, the description cannot be a-theoretical but must be based on some prior analytical framework in order to maintain the focus on the same phenomena across cases (Dubois & Araujo, 2007; Aaboen et al., 2012).

Usually, new ventures start with limited resources and few, if any, contacts and business relationships. Relationships between businesses offer opportunities and limitations. Developing relationships can reduce uncertainty and facilitate cooperation and coordination. Business relationships involve specific investments and mutual adaptation between and within the businesses involved. Various studies have shown the close dependence between the business's ability to develop and maintain stable relationships with other companies and its survival, but they also provide a point for reflection on “networking” activities (Johanson & Vahlne, 2011; Aaboen et al., 2011). As such, the interaction processes underlying the development of business relationships are an important aspect of the development process of a business. What this implies, for our research, is that to better understand how a new venture succeeds, we need to focus the analysis on the new business relationships development process. Though we are interested in examining the consequences of this process, namely the process of developing new business relationships for new businesses, at the same time we are aware that this is difficult to analyze. That is, the complex nature of business relationships, in particular, the complex interactions that cover a wide range of functions and activities in firms, makes the empirical study of relationships development a challenging goal.

The industrial network approach has had an important influence on how the analytical framework can be structured in such cases, and we believe it offers the right motivations for applying the network perspective to our study. In fact, in Chapter 4, we will see that among the many approaches – economic, organizational, sociological, and marketing oriented – that have enriched the theory of business networks, we can place the theoretical contributions of the business network perspective on business markets that appear to be more directly related to the analysis of relationships in business

networks. Within these studies on business networks, the more consolidated perspective of analysis appears to be that of the industrial network approach (cfr. Chapter 5). Numerous researchers advocate the use of the industrial network approach framework for the analysis of industrial relationships (Dubois & Araujo, 2007) starting from the interaction between actors, resources, and activities (ARA model) (Håkansson & Snehota, 1995). In line with the analytical focus on the new business relationships development process, we decided to set the main components or building blocks of our framework on the three relationship layers model. We believe conceptualizing and analyzing the development of business relationships through this model will reflect the way in which new businesses connect with their first counterparts and interact in order to coordinate their activities, resources, and actors, and capture the impact of these connections on overall business development. In sum, these are aspects that characterize the development of a business and we intend to describe them in order to examine how they can affect the development of a new business. Hence, in order to capture the first relationship development patterns of new businesses, we searched for three start-ups to serve as exemplary cases that would be capable of effectively reflecting the three facets of the relationships – activity configuration, resource interfacing, and creation of actors’ shared meanings – and to provide examples of outcomes (Yin, 1993).

Having decided to adopt the case study methodology and chosen the framework, the selection of the case becomes fundamental. If the sample is large and random in the survey research methodology, it cannot be randomly chosen in the case study. In qualitative research we cannot make use of traditional ‘statistically representative’ sampling, incompatible with in-depth interviews or other qualitative methods, as well as with generally limited resources for research. In fact, the qualitative methodology of case study implies that the selected sample is not representative from a statistical point of view, but is significant in relation to the issues the research intends to address. That is, case study research is not sampling research (Stake, 1995; Yin, 2003), but selecting the cases must be done in order to exploit what can be learned in the time available for the study (Tellis, 1997). In our research, the screening of the potential case studies was based on four criteria:

1. *General recognition as start-up*: What is a new business? There is no formal or legal definition of what a new business is (Stevenson & Gumpert, 1985; Cunningam & Lischeron, 1991). The term start-up, more commonly known as a new business, signifies the very first stage of a business's life, the beginning of its operations. To some, new business formation is about a form of business that is new because it develops or provides a new solution. In that sense, new businesses are those innovative organizations that create new solutions. The term new business formation has also been extended to include forms of business activities that bring discontinuity into the normal operations of an organization, by doing or developing new things the organization didn't do previously, activities or products aimed at revitalizing a mature organization. But, generally speaking, the term indicates a new venture in its early development stage that typically identifies periods in which there are organizational processes in progress. Identifying new businesses at different stages of their formation process remains a major problem for many scholars (Reynolds & Miller, 1992; Carter, Gartner, & Reynolds, 1996; Liao & Welsch, 2002) in delimiting the term. In fact, during new business formation many processes and transactions occur involving the acquisition of resources, the definition of production methods and research of staff, and other activities engaged in to access the market. Given the many flows of organizing processes in founding a new business, it is difficult to define a point in time that establishes the presence of a new business. Therefore, to us a basic criterion in defining new businesses is that those new businesses have not yet developed the initial business relationships with customers and suppliers. Having defined new businesses in these terms, we decided to form the sample in a way that best allows us to answer our research question. Consequently,

just to highlight this process, we decided to find some businesses that were in the process of developing new relationships.

2. *Relevance Qualification:* In order to build the sample selection, we also wanted to understand if the context of the Swiss Italian region, the one closest to us, qualified as an attractive market to be observed in terms of creation and survival rates of new businesses. In order to determine whether the selection of the sample could be restricted to the Swiss Italian region, we used the results published by the Swiss Federal Office of Statistics (Results 2003) that provided us evidence on the evolution of the business population in different Swiss regions<sup>6</sup>. In Switzerland the trends on the survival rates of new businesses are comparable to those highlighted by analogous studies conducted in Europe. In particular, the results indicate that in Switzerland the survival rate of a new business after one year of activity – 81.6% – is approaching the average value in some EU countries where about 85% of new businesses are still active after their first year of existence. That is, after one year, only four out of five new businesses will remain. The study also showed that after two and four years the "fight" for survival continues. In fact, the survival rate of new companies still in business after two years in Switzerland – 72.5% – is practically identical to the average in EU countries considered in the analysis – 72.2% – while this figure drops to 54% after four years. This means about half of newly established businesses no longer exist after four years. It would seem, therefore, that mortality (as a relative value) decreases over the years. Compared with new businesses observed in the rest of Switzerland, in the Swiss Italian region new business

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<sup>6</sup> The Federal Office of Statistics submitted new businesses' statistics for the first time in 1999. The statistics concern new businesses created between July 1996 and July 1997. Subsequently, new results have been published for 1999, 2000, and 2001. The limitation of this analysis is that the census is conducted only every three or four years. The results of the investigation mentioned above were presented in 2003 (Grossi, 2003).

survival rates are very low. In particular, we found that the region Ticino comes last compared with the six main Swiss regions (Geneva – Lausanne region; Mittelland region; Northwestern Switzerland – Basel; Central Switzerland – Lucerne – Zug; Zurich area, Eastern Switzerland – Bern – Fribourg-Solothurn). In fact, as mentioned above, in Switzerland about 20% of new businesses cease operations during the first year of life, while in the Swiss Italian region, the phenomenon appears slightly higher. In particular, more than 21% of new businesses were no longer active after the first year of activity. For the Swiss Italian region after two years the survival rate was 67.8% and after four it was 48.7%; respectively, for the rest of Switzerland instead, the figures are 72.5% after two years and 54% after four years. The data provided by this study on new businesses and survival rates in Switzerland tell us that new companies in the Swiss Italian region tend to survive less than in the rest of the country. However, the same study (ibid.) has not revealed the cause of this peculiarity in the Swiss Italian region. This aspect has led us to believe that the Swiss Italian context would be interesting for performing an empirical analysis.

3. *Access Convenience:* To move more effectively and successfully in the selection of the sample, we decided to exploit our own relational network and position. Therefore, having identified the area of interest for the selection of cases, the Swiss Italian region, the criteria for selecting the new business to be studied have been relatively simple. This work was conducted at the Università della Svizzera Italiana in Lugano, the institutional seat of the research doctorate for which this work was done, and also the institutional seat of the affiliated new business accelerator. Due to time and resources limits, we found reasonable to consider and exploit this pragmatic opportunity. In fact, my participation as a marketing assistant between 2006 and 2008 at the business accelerator of the Università della Svizzera Italiana has been a good opportunity to

select two start-up businesses to take part in an empirical investigation and, at the same time, to interact with parties involved in different stages of the development process. This has not only increased access to empirical data, but has also been suitable from a practical point of view. In fact, given the geographical proximity to the accelerator, the interviews were conducted mainly at the premises of the start-up businesses at the university business incubator. To complete the sample, in addition to the two start-ups housed at the business accelerator, we selected one other new venture whose plant was located in the Canton Ticino. This proximity facilitated the collection of data and information otherwise not available, besides affording the concrete possibility of conducting some direct interviews.

4. *Willingness to cooperate*: all three start-ups agreed to cooperate in the development of this research and to be available for several interviews.

Based on these considerations we identified three firms that provide multiple descriptions of newly founded businesses engaged in developing new business relationships.

## 2.4 DATA COLLECTION

Our research is based on the assumption that initiatives aimed at configuring activities, interfacing resources, and creating shared meanings with the actors involved in developing a business relationship are at the origin of difficulties experienced in developing new businesses. Therefore, the present study aims to describe how new business relationships are developed in the early stages of development in three firms. In order to do that, longitudinal qualitative research methods and multiple sources of evidence have been used to investigate the topic. According to Easton (1995, p. 385) "...the complexity of the links within and between actors requires a methodology which

can handle rich resources of data and multiple forms of data collection. Networks have consistently been portrayed as dynamic forms. Again the case method with this attention to changes over time is well suited to providing longitudinal data.” As such, we believed this research could be settled into a longitudinal approach, that is by capturing the process of developing the sample firms’ first relationships by collecting past, present, and future data at several point in time. By following a longitudinal approach we will be able to reveal more of the “dead-ends, chance events, and controversies” that, according to Hoholm & Araujo (2011, p. 935), are important to uncover in studies of development processes. For our data sources, we use both primary and secondary complementary data.

#### 2.4.1 PRIMARY DATA

The first contacts with the start-up firms were made by phone or email. On these occasions, we introduced ourselves and gave our motivations for contacting the company. Once the informants agreed to participate, we set a meeting with them in order to proceed with the interview. Prior to the first meeting, we gathered some information about the businesses to be interviewed in order to have background information, and prepared an interview guide. This allowed us to more effectively manage and allocate time for the interview. In the first round of interviews we met the founder or co-founders of the new ventures since they were involved from the beginning in organizing the new venture and had the best overview of the start-up’s development. In all cases, the founders described the companies to us in detail. We collected out start-up “stories” mostly by using the snowball method. That is, to enable the comprehensive collection of information, after the interview we asked the founder to indicate or suggest other suitable respondents we could contact for subsequent interviews.

For the questions we developed and used a semi-structured “interview guide” to get a comprehensive account of how relationships had been initiated and developed. We didn’t use a default track of topics and questions, but rather asked respondents to develop certain topics by giving them the opportunity to talk freely about the relevant issues. When necessary, we reformulated questions or adjusted them to the specific

situation. Questions were aimed at gaining information about the company's main networking practices with their first customers and suppliers. Accordingly, we asked questions concerning issues related to the development of the first business relationships in terms of coordinating activities, interfacing, resources, and creating actors' shared meanings. We also asked the organization questions about exchange activities implemented. Significant space has been devoted to descriptions of the organizational logic with regard to relationships built with other actors, e.g. the kinds of problems that were encountered and how they were treated through the development of the business interaction. These strategic questions were usually preceded by more general questions to develop a good understanding of the new venture. We first asked the respondents to describe their position in the business structure and then to describe the company's business idea. During the interviews we also asked about the founding roots of the company and about its future plans. At the end of the interview, we proceeded with some verification questions to control the accuracy of statements and to iron out any possible contradictions. In particular, each time we conducted an interview we wrote a clean copy of the collected field notes as a first draft. This procedure allowed us to identify ambiguities or pitfalls in the data previously collected. To complete or clarify some of the information collected during the first interviews, other interviews were subsequently necessary.

We conducted 21 formal interviews with six different informants working in different functional areas of the three new businesses. In addition, we conducted 12 (mainly informal) interviews with 12 external informants. Table 2.5 presents key sample characteristics of informants and their companies, and Table 2.6 presents key sample characteristics of external informants. The interviews with informants not formally associated with the businesses we studied, were often conducted by phone or through previously fixed one-on-one interviews. These involved a general discussion of the industry and perceptions the interviewees had of the three new businesses. All three companies were personally visited and interviewed more times. These series of interviews were conducted mainly at the business's premises. The duration of each meeting ranged from an hour and a half to three hours. We decided to stop our

interviews when we reached theoretical saturation. The interview period lasted from December 2007 to June 2012.

Table 2.5 Key sample characteristics of informants and their new businesses

<b>Name</b>	<b>Participant Background</b>	<b>New Business</b>
Claudio D.	Co-founder & CEO	Ekobike
Massimo M.	Co-founder & CMO	Ekobike
Marco A.	Co-founder & CEO	Concertlab
Martino P.	Co-founder & CMO	Concertlab
Mauro P.	Co-founder & CEO	Hippo Engineering
Antonio T.	CTO	Hippo Engineering

*Note.* Names are pseudonyms.

Table 2.6 Key sample characteristics of external informants and their business network roles

<b>Name</b>	<b>Participant Background</b>	<b>Business Network Role</b>
Alessandro Z.	Singer of a music band	Musician
Arianna C.	Singer of a music band	Musician
Fabrizio F.	Bassist of a music band	Musician
Francesco S.	Live music events manager	Venue manager
Ivan C.	Live music events organizer	Concert organizer
Michele C.	Shop manager	Music store
Paolo P.	Talent scout and manager	Promoter
Richard F.	Fan and Supporter	Fan
Stefano M.	Fan and Supporter	Fan
Monica G.	Local Winemaker	Wine producer
Sandro T.	CEO of a local company	Wine trader
Giorgio V.	Phytosanitary Center Director	Public service

*Note.* Names are pseudonyms.

## 2.4.2 SECONDARY DATA

Additional sources of information that have been used to complete the illustration of the case histories were secondary material, such as company brochures and Web sites, annual reports, business plans presented to various stakeholders, and various articles from newspapers, magazines, and books (for a detailed list see appendices). All the relevant secondary information collected was then compared and integrated in the description of the cases. Both sources of information, the semi-structured interviews and the written and electronic documentation, have been useful for triangulation and to clarify the meaning of events and the inconsistencies among informants and in acquiring additional perspectives on key issues (Miles & Huberman, 1994).

## 2.5 DATA ANALYSIS

In case study research it is not easy to separate the description of cases from the analysis (Dubois & Araujo, 2007). According to Eisenhardt (1989, p. 540) the first thing to do in case analysis is to write a detailed transcription for each case "...because they (write-ups) help researchers to cope early in the analysis process with the often enormous volume of data." Hence, for the interviews, we used a digital recorder to record the content and were sure to report the content of that interview as accurately as possible. If tape-recording was not allowed, we jotted down notes to capture respondents' answers during the interview. After each interview, we wrote a clean copy of the collected field notes and produced the first case draft. We transcribed the content so the original language, concepts, and expressions the interlocutor used would be maintained for the coding. The full transcript of the interviews allowed us to extrapolate key issues, key concepts, and recurrent or constant critical issues and to identify ambiguities or pitfalls in the data collected. If it was necessary to complete or clarify ambiguities, we gathered additional information during subsequent interviews. All the respondents were willing to concede a second or third interview or to respond by mail or telephone to any additional demands. The interviews to complete and integrate relevant information were thus

fulfilled. By following this procedure we were always able to go back and reinterpret earlier interviews in the light of the following ones. Successively, after we conducted the in-case analysis in which we first wrote the description of the new venture with all the material collected, for each case, all the transcribed start-up's descriptions were rewritten following a format based on the ARA model framework in order to provide a comprehensive description of the relationship development process. After writing the story and having identified the difficulties that the start-up faced in developing its first relationships, we also collected raw data on the economics of the venture to see if the start-up was close to or distant from reaching balanced economics. Therefore, in the analysis of the cases, we will also reflect on the economy of these business ideas by analyzing the origin of the business's revenue.

## 2.6 LIMITATIONS

One the most common criticisms of the case study research method concerns its scientific rigor and the generalizability of the results (Yin, 2003). It has been noted that this problem can be adjusted with an appreciation of the conceptual difference between the inductive and deductive method. Hence, compared to the research methods that pursue a statistical generalization of the results towards the universe (deductive), the case study becomes eligible in cases where it is followed by the type of generalization that goes from the empirical evidence towards a theory (inductive), the so-called analytical generalization (Eisenhardt, 1989; Yin, 1999, 2003). In that sense, analytical generalization differs from statistical generalization in that it refers to generalization from empirical observation towards a theory, rather than towards a population. Examples of businesses in their early stages of development can be found throughout different industries, in different sizes and regions. This research, of course, does not look at every new business company case in business history, but uses a cross-section of cases, each case unique in terms of its business solutions – product, process, or service – and all its related entrepreneurial activities. The goal of this thesis is to cover what can be described as the prototypical cases, and not to exhaustively describe every case that has

ever occurred. The purpose of an empirical interpretation that distinguishes this work is thus to give a plausible interpretation of the empirical phenomena observed that is not contradicted by the results. We will do that by drawing a comprehensive picture of the reality through observation and analysis of highly contextual facts in order to evolve towards some good structured insights (Golder & Tellis, 1993; Chandy & Tellis, 2000; Golder, 2000).

As we will see in the next chapters, the patterns we identified in our analysis indicate some possible general patterns in the development of the new businesses' first relationships. But we also realized that we were only scratching the surface of more noteworthy processes. According to Campbell (1975) "pattern-matching," i.e. a setting in which several fragments of information from the cases may be related to some theoretical propositions, is a useful technique for linking data to propositions. But, because case studies data are observational, the researcher cannot conclude that the dominant factors that emerge from pattern matching are causal. Consequently, we cannot make statements about causal relations in the "strict" way postulated by the standard view of science; that is, without any influence of the researcher's knowledge. This methodology, of course, does not allow drawing a statistical generalization about the phenomena, but it definitely allows highlighting some relevant aspects and to generate new hypotheses and reflections that in turn might become important to look at more extensively in future research (Flyvbjerg, 2011). Assessing the internal and external validity (Gibbert & Ruigrok, 2010; Dubois & Gibbert, 2010) is a challenging task in qualitative research.



## Chapter 3

# Entrepreneur, Entrepreneurship, and New Business Formation

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Entrepreneurship is certainly not a new research topic; in the past this subject has, in fact, seen a growing body of research in different disciplines, from mainly economic research to more managerial and sociologically oriented research that has highlighted the importance of entrepreneurship in explaining economic growth and business development (Drucker, 1985; Audretsch & Fritsch, 2002; Audretsch, 2004; Acs & Storey, 2004; Carree & Thurik, 2006; Sheshinski et al., 2007; Ahlstrom, 2010). There are numerous specialized academic journals dedicated to entrepreneurial studies: *Entrepreneurship Research Journal*; *Entrepreneurship: Theory and Practice*; *Journal of Business & Entrepreneurship*; *Journal of Business Venturing*; *International Entrepreneurship, New Business Development, Technology, and Innovation*; *Journal of Small Business and Entrepreneurship*, just to mention a few. Among those studies, increasing interest has recently been given to the particular role new ventures play in catalyzing economic and the social welfare (Fritsch, 2004; Audretsch & Keilbach, 2005; Acs & Armington, 2006).

This increased interest seems to originate from many factors. Among these is the fact that despite the growing number of publications on the subject of starting new businesses, the process of creation and development for new firms always involves great difficulties and uncertainties. Indeed, the failure rate of new businesses is always very

high: as mentioned in Chapter 1 it is estimated that nearly 50 percent of new ventures cease their activity before reaching five years of life (Headd, 2003; Short et al., 2009).

As a popular topic of research in many different fields and in scientific debates, “entrepreneurship” has been subject to numerous interpretations and conceptualizations<sup>7</sup>. Therefore, in this chapter we will review the main contributions from the literature on entrepreneurship and new business formation and sum up what has been studied so far. We will photograph “the state of the art” in this field of study, paying particular attention to the stream of research that focuses on new business development. We will also take a “census” on different perspectives in the field of entrepreneurship in order to identify which are the leading ones. We will also bear in mind that the common aim of the various scientific communities is to investigate the modalities and circumstances of starting new businesses, and define some characteristics of the phenomenon.

In particular, having reviewed the literature, we have identified three leading approaches that are recognizable in two main perspectives. The first perspective, which we will call “entrepreneurship perspective,” includes all those studies belonging to the “trait approach” and the “functional approach.” As we will discuss, these are the two approaches in the literature on entrepreneurship that have focused mainly on the characteristics of the entrepreneur, who is considered the main actor of economic dynamics, and on entrepreneurship, which is a function of the types of people involved in entrepreneurial activity (Schumpeter, 1934; Baumol, 1968; Reynolds, 1997). However, these person-centric approaches have been generally unsuccessful in explaining entrepreneurship (Gartner, 1990). In fact, in tracing the ideas about entrepreneurship, we will find that recent research in this area has shifted the unit of analysis from the internal factors, such as entrepreneur personality traits and managerial functions, towards the study of external factors, such as the context and resource conditions, as it seems the process of developing a new businesses involves internal and external organizing (Shane & Eckhardt, 2003; Stuart & Sorenson, 2007; Sarasvathy,

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<sup>7</sup> For a compilation of different definitions on entrepreneurship see: Stevenson & Gumpert, 1985; Gartner, 1990; Cunningham & Lischeron, 1991).

Dew & Ventresca, 2009; Welter, 2011). We will call this second main perspective the “new venturing perspective.”

In the next paragraphs we will scrutinize this shift from the “entrepreneurship perspective” toward the more organizational, process-oriented perspective – the “new venturing perspective” (Davidsson, 2008). This review will bring us to argue that current research on entrepreneurship not only acknowledges the importance of the context of entrepreneurship activities, but such thinking also implies that entrepreneurship is no longer recognized as an individual phenomenon but as a phenomenon that depends (heavily) on its context.

### 3.1 ENTREPRENEURSHIP: AN INTERDISCIPLINARY FIELD OF STUDY

The interest in the study of the entrepreneurial phenomenon can be observed in the proliferation of multidisciplinary theoretical studies and investigations. In fact, in recent years the topic of entrepreneurship has seen growing interest among many scholars from different disciplines, who have focused their research insights on identifying a variety of relationships and tools capable of enhancing the processes of entrepreneurship by helping the entrepreneur to meet and overcome the difficulties that characterize the initial stages of the process of new business formation (Boettke & Coyne, 2009). Hence, in recent years, the study of the entrepreneurial phenomenon has become a crossroads of several interdisciplinary research approaches. Academics from different fields, primarily the fields of economics (Casson, 2003), sociology (Thornton, 1999), psychology (Carsrud & Krueger, 1995), anthropology (Dana & Anderson, 2007), and political science (Homer-Dixon, 2000), have been committed to producing new research approaches that have led to a wealth of new findings and insights about new business development. Research in this field has tried to find out more about the entrepreneur’s personal traits and the motivations that drive the creation of new businesses, and the factors that enable their growth and development, including sources of funding. As a result, the research field of entrepreneurship appears as a collection of different issues

and approaches that co-exist, but remain somewhat difficult to connect (e.g. Shane & Venkataraman, 2000).

### 3.1.1 THE DOMAIN

Given this co-existence of different conceptualizations and interpretative perspectives on entrepreneurship, it is difficult to identify the leading contribution and to understand the major research perspectives that have been generated from the different fields (Audretsch, 2004; Davidsson, 2004; Zahra, 2005). In fact, the presence of this multitude of interdisciplinary approaches has impeded a conceptual uniformity to the study and analysis of the entrepreneurial phenomenon, precluding a fully shared theoretical interpretation (Low & MacMillan, 1988; Bygrave & Hofer, 1991; Lambing & Kuehl, 2006). Some even have claimed the impossibility of having a well-articulated, fully shared statement of the domain of the field (Gartner, 2004; Minniti & Lavaresque, 2008). Therefore, one of the consequences of the interdisciplinary approaches to the research on entrepreneurship is the lack of clarity regarding the field's boundaries.

The existence of a large number of approaches and interpretations makes it difficult to propose a common and shared definition of the notion of entrepreneurship (Hisrich, Peters, & Shepherd, 2006). The notions/concepts applied to denote the empirical phenomena and to define fields of research can be very different (e.g. entrepreneurship, new business formation, new venturing, etc.) depending on the perspective adopted. If we go through the entrepreneurship literature it's almost impossible to find a shared definition of what exactly entrepreneurship is. This is partly due to the diversity of disciplines involved in the study of this phenomenon, as we have already discussed, and in part to the complexity and heterogeneity of the phenomenon itself. This complexity has oriented every school of thought to provide a different answer to the question, "What is entrepreneurship and how do new businesses develop?" (Stevenson & Jarillo, 1990; Timmons & Spinelli, 2003).

### 3.1.2 THE ENTREPRENEURIAL PHENOMENA

Although the concept of entrepreneurship can take on different meanings, the notion of entrepreneurship or entrepreneur is not new. The earliest citations of meanings attributed to the term entrepreneur date back to 16th-century Europe. The term entrepreneur was, in fact, used to define the mercenary captain who hired troops to serve the needs of princes or other mandators. It was only during the 18th century that the figure of the entrepreneur acquired its modern connotations. In the agricultural sector, the entrepreneur was a landowner, in the manufacturing sector, he was the one who produced goods to be distributed, and in the public sector he was the one who realized the infrastructures (Gallino, 1989). But today, the distinction between the business owner and the nascent entrepreneur is even clearer. The Global Entrepreneurship Monitor (GEM)<sup>8</sup> marks a clear distinction between nascent entrepreneurs and business owners. Nascent entrepreneurs are those people in the process of starting a new business; those individuals who have taken some action towards creating a new business in the past year. In order to qualify for this category, these individuals must also expect to own a share of the business they are starting and the business must not have paid wages or salaries for more than three months. New business owners are individuals who are active as owner-managers of a new business that has paid wages or salaries for more than three months, but for less than 24 months. Viewing entrepreneurship from another angle, according to Reynolds & White (1997), the creation of a new venture is a process that starts when one or more persons begin to commit activities and resources to founding a new firm, and the main actors of the first steps of this process are nascent entrepreneurs.

Most definitions associate the entrepreneurial phenomena with the establishment of new organizations and their development in the early years (Audretsch, 2002; Acs & Audretsch, 2010)<sup>9</sup>.

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<sup>8</sup> Founded in 1999, The Global Entrepreneurship Monitor (GEM) project is an annual assessment of the entrepreneurial activity, aspirations, and attitudes of individuals across a wide range of countries.

<sup>9</sup> The essay by Audretsch, D.B. "*Entrepreneurship: A survey of the literature*" (2002) is a roadmap of classical literature on the subject of entrepreneurship.

Our thesis embraces what Wiklund et al. (2011) recommend, that is: “entrepreneurship research should be unified as a field approached theoretically and empirically in terms of the *phenomenon*.” We propose that the phenomenon of the “emergence of new economic activity” lies at the heart of entrepreneurship” (p. 5). This definition that entails the word “emergence,” in our view, prompts us to acknowledge the importance of the context in which entrepreneurship takes place.

### 3.2 ENTREPRENEUR AND ENTREPRENEURSHIP: DIFFERENT PERSPECTIVES

Given this co-existence of different interpretative perspectives, to better understand the evolution of the systematization in the field of entrepreneurship, we tried to trace the main schools of thought. Pursuing our research objective, namely to investigate the difficulties encountered in starting a new entrepreneurial activity, we examined the most significant research perspectives that have focused on the specific setting of starting a new business. In particular, we explored how the literature deals with the concepts of entrepreneur and entrepreneurship, particularly those aspects relating to the moment of genesis of a new business.

In tracing ideas about entrepreneurship and the entrepreneur, we have identified three leading approaches. The first main approach we will discuss is the ‘trait approach,’ as Gartner (1988, p. 12) called it. The second approach is the one adopted by the economic theorists, namely the ‘functional approach’ (Casson, 2003). And last, but not least, we will discuss a more recent research approach on entrepreneurship, the ‘new venturing approach’ (Gartner, Carter, & Reynolds, 2010). What will follow from the analysis of the literature is that the trait approach has focused predominantly on the characteristics of the entrepreneur. While the functional approach argues that “an entrepreneur is what he does, in the sense that it specifies a certain function and deems anyone who performs this function to be an entrepreneur” (Casson, 2003, p.19), the new venturing approach is concerned with the process of forming and organizing the new business. At the end of this review, we will discuss the growing recognition in

entrepreneurship research that the context in which entrepreneurship takes place is important for understanding the difficulties in setting up a business.

### 3.2.1 THE TRAIT APPROACH

Numerous studies have been carried out on the factors that may affect the success or failure of a new business. One of the aspects to which the economic and sociologic literature has devoted increasing attention is that of the “personal traits” that characterize the successful entrepreneur. Hence, several studies of a social, psychological, and economic background have focused on personal, psychological, and motivational characteristics of the new entrepreneur, considering them determinants of his actions and his modus operandi. Most of these studies clearly refer to the peculiar and specific characteristics of entrepreneurs, of the family context, and its “history,” as well as at the set of innate attitudes and skills induced through the paths of education, formation, or work experience (e.g. Cox, Mueller & Moss, 2002; Lazear, 2004; Burmeister & Shade, 2007; Hellmann, 2007; Obschonka, Silbereisen, Schmitt-Rodermund, & Stuetzer, 2011).

Taking a step back in time, the first studies on entrepreneurship, dating from the nineteenth century, used to place strong emphasis on individual traits. For instance, Jean-Baptiste Say in his *“Traité d'économie politique”* written in 1803, described and emphasized the central role played by this figure in the domain of capital, production, trade, and consumption; and Joseph Schumpeter, in 1911, in his *“Theorie der wirtschaftlichen Entwicklung”* dealt with the role played by the entrepreneur in innovating production factors. Entrepreneurship, therefore, has often historically been seen as an individual phenomenon.

Even though many academics of entrepreneurship have argued against confining the focus of research to entrepreneurs’ personal traits and characteristics (Van de Ven, 1980; Drucker, 1985; Gartner, 1988; Low & MacMillan, 1988; Stevenson & Jarillo, 1990; Shane & Venkataraman, 2000), several recent studies have approached entrepreneurship from an internal and individual perspective, but have focused more on the individual attributes and characteristics and on the individual’s ability to discover

and exploit opportunities (Lévesque et al., 2002; Kaulio, 2003; Djankov et al., 2006). In the economic and psychology literature, especially, a series of studies has investigated the individual and personal variables of the entrepreneur that may play a key role in starting a new business (Minniti, 2004; Zahra, Sapienza, & Davidsson, 2006; Van Praag & Versloot, 2007; Davidsson, 2008). A common assumption in these studies is that to effectively conduct the entrepreneurial function, the entrepreneur must possess or acquire certain personal traits that in some circumstances can become real expertise. These attributes can be related to the so-called entrepreneur's innate predispositions or to the entrepreneurial expertise acquired, in various ways, over time. Gartner (1988) labeled this search for characteristics and traits of the entrepreneur as the "*Trait Approach*." According to some researchers, a series of personal skills is required in order to translate a business idea into a successful business (e.g. Wagner, 2003; Michelacci, 2003; Baum & Locke, 2004; Rauch & Frese, 2007).

Yet, much of this entrepreneurship research, where the entrepreneur is assumed to be a specific personality type, carried out to find and enumerate the set of characteristics describing the entrepreneur, has never brought agreement on who an entrepreneur is (Gartner, 1988; McKenzie, Ugbah, & Smothers, 2007). It has been argued that the attempt to define the ideal mix of traits and personal characteristics of entrepreneurs "will neither lead us to a definition of the entrepreneur nor help us to understand the phenomenon on entrepreneurship" (Gartner, 1988, p. 48). Indeed, empirical evidence in this regard has shown that there is a non-generic definition of the entrepreneur; and that between research on the successful entrepreneur and the non-successful entrepreneur no significant differentiating features have been found (Sexton & Smilor, 1986). Subsequent studies of entrepreneurs' attributes have shown that most of these subjective variables may affect the propensity to choose the way to become an entrepreneur, rather than demonstrate the propensity to successfully conduct the development of a new business (Chandler & Lyon, 2001; Antončič & Hisrich, 2003). That is to say, the entrepreneur's characteristics appear to impact the way to run an enterprise and do not correlate with the success of new business development. Other scholars, such as Ensley et al. (2000) and Gartner (1988) have also shown that the

intrinsic characteristics of individuals represent a secondary issue in explaining the entrepreneurial attitude and, especially, in predicting the outcomes of their entrepreneurial actions. This aspect, in our view, summarizes much of the research that has been done on the characteristics of entrepreneurs; That is, that the entrepreneur's characteristics are related more to the way of doing business than to the outcome of developing a new business.

Another aspect of the trait approach discussed in the literature on entrepreneurship is the contribution of the entrepreneur's education and past work experiences to the success of the new venture (e.g. Ronstadt, 1985; Solomon, 1986; Robinson & Sexton, 1994; Heper & Douglas, 1997; Young, 1997). The interest in entrepreneurial education is evidenced by the growing number of courses on entrepreneurship developed in schools, universities, and colleges of education, and from the large amount of contributions including books, magazines, and conferences dedicated to this theme (e.g. Matlay, 1996; Katz, 2003). This issue has long been the subject of a debate in the research on entrepreneurship; many researches have studied how the entrepreneur's education may affect the successful development of a new business.

According to some scholars, adequate training processes can have a positive impact on the development of the attributes, entrepreneurial skills, and expertise of new entrepreneurs (e.g. Fayolle, 2000; Finkle & Deeds, 2001; Von Graevenitz, Harhoff, & Weber, 2010). However, these scholars do not necessarily agree on the strength of the relationship between education or training and entrepreneurship (Johnson & Lundvall, 2000; Chell & Oakey, 2004).

Though the field of entrepreneurial education is expanding considerably, the research devoted to it seems to be fragmented and extremely descriptive, as there is a lack of extensively accepted paradigms, theories, and models on entrepreneurial education<sup>10</sup>. *Moreover*, a direct systematic correlation between entrepreneurial-specific education/training and the successful foundation/development of a new business has not

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<sup>10</sup> For a wider discussion about the fact that entrepreneurship capabilities can be taught or not, refer to; Garavan & O'Kinneide, 1994; Henry, Hill, & Leitch, 2005.

always been found (Entrialgo, Fernandez, & Vazquez, 2000; Galloway & Brown, 2002). For instance, according to Johnson & Lundvall (2000), the issue of entrepreneurial training cannot be separated from the context in which the entrepreneur is operating, a context characterized by forms of learning carried out by social and cooperative relations.

Also, the weight of past work experiences of entrepreneurs is a controversial issue in the entrepreneurship field of study. Founders with an educational background and previous work experience have access to a stock of knowledge needed to identify entrepreneurial opportunities and reduce the degree of uncertainty more than non-educated experienced entrepreneurs (Shane, 2000). According to other research (Bhaduri & Worch, 2008; Oosterbeek et al., 2010), past experiences can be a limiting factor as they lead the entrepreneur to focus only on small groups of opportunities, namely those related to the “core competencies” they have learned, and tend not to recognize other opportunities. Bhide (2000) found there are several good examples of founders of successful companies who succeeded without a strong track record and years of experience in their field. He observed that two out of five successful entrepreneurs (40 percent of Inc. 500 interweaved founders) had no prior experience in the industry they were entering. Moreover, according to his research, more than a third of the 500 entrepreneurs interviewed (33%) were out of work when they started their companies. He also found that founders often have few if any contacts in the field they are going to enter.

In summary, what we found in this “trait approach” review is that for some scholars entrepreneurial skills are intrinsic and innate. For other scholars entrepreneurial skills can be learned and taught. It also appears that for some, entrepreneurial talent is the product of the entrepreneurs’ past experiences. Hence, from this perspective, new business development is seen as a process in which the outcome is determined or at least dependent on some of the characteristics and learned skills of the entrepreneur. However, according to other scholars, the skills that make one a successful entrepreneur are not the kind of skills that can be typically taught in lectures and seminars or through previous work experiences (Oosterbeek et al., 2010), which suggests the focus on entrepreneurship should be moved away from the enterprising individual.

To conclude, it seems entrepreneurial characteristics, attitudes, and skills aren't aspects that we can dissect and parameterize and codify into procedures any entrepreneur can follow and become good at starting a new business. The latter studies, which have questioned the factors that lead some people to become entrepreneurs and how to transmit these entrepreneurial characteristics, introduced the debate over whether or not entrepreneurship is teachable. These observations point to another issue that may be relevant for understanding the entrepreneurial phenomenon, namely that entrepreneurship cannot be considered a purely individual undertaking, and other factors may determine its outcomes. This draws our attention to the perspective that considers entrepreneurial activities as happening outside the business as individual, indicating the link between entrepreneurship and its contexts.

### 3.2.2 THE FUNCTIONAL APPROACH

In the previous section we reviewed studies about the personal characteristics and traits of entrepreneurs and how these investigate the role entrepreneurs' personality traits, past education, and previous work experiences play in starting a new business. Now, rather than trying to identify the typology of personal attributes that are important for the ability and propensity towards starting a new business, we will turn our attention to research that has focused on the role of entrepreneurs with regard to managerial skills (Cole, 1959; Leibenstein, 1968; Baumol, 1968). This is the mainstream of economic thought, which recognizes the distinctive attributes of the entrepreneurial function in the ability to recognize opportunities and to deal with difficult situations. Here the approach is more functional as it identifies the entrepreneurial phenomenon in the accomplishment of certain functions and activities or through the possession of certain requirements (Stevenson et al., 1999; Timmons & Spinelli, 2003).

The so-called functional approach literature is fairly diverse and heterogeneous; there are a number of different perspectives on entrepreneurs that are offered in this literature. Each one of these perspectives has distinct attributes and, within these trends, different entrepreneurial functions can be identified.

There are two distinctive notions of the generalized entrepreneurial function, a wider one and a narrower one (Klein, 2010). The wider notion, that builds on some basic starting points of theorizing in the Austrian economic tradition<sup>11</sup>, considers the entrepreneur as a decision maker who acts under conditions of uncertainty and attempts to use scarce means or resources to achieve particular ends. For example, the notion of “means and ends” that comes from Mengers’ “Principles of Economics,” published in 1871. According to Mengers human action is about the achievement of particular ends or goals, although human beings must employ scarce means and resources to achieve these goals. This view of the function of the entrepreneur as a decision maker allocating resources under conditions of uncertainty can be related to the most influential early works of Cantillon (1755), Say (1803), and Mill (1848) and their systematic treatment of entrepreneurship in the economic literature. The second, narrower notion of the generalized entrepreneurial function is proposed by Mises (1949), one of the most influential economists of the Austrian school. Mises argues that, whether an individual is an entrepreneur or not, whenever that individual employs resources under conditions of uncertainty and pursues objectives that may or may not be realized, he is acting as an entrepreneur. According to Mises, an entrepreneur is someone who invests in and employs financial or physical capital and resources to try to earn profits by transforming these resources into consumer goods that can be sold and bought in the market. Following this logic, the entrepreneur is not only acting under uncertainty, but he is acting in a condition of uncertainty in a particular way, by acquiring, combining, and employing capital resources in an attempt to produce consumer goods that can be sold.

Another economist working in the entrepreneurship area is Israel Kirzner, probably the best-known modern Austrian economist. In his popular book, “Competition and Entrepreneurship,” published in 1973, he expresses a specific perspective on the entrepreneur, emphasizing the notion of alertness. In his formulation, the core of the entrepreneurial function is awareness, alertness, or recognition of particular opportunities that subsist in a market characterized by disequilibrium. What Kirzner

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<sup>11</sup> The Austrian School, also known as the Vienna school, is a school of economic thought that proclaims strict adherence to methodological individualism. Basically, the Austrian school argues that the only valid economic theory should follow logically from basic principles of human action.

criticizes is the intent to embed the concept of the entrepreneurial function within the model of the market equilibrium of the neoclassical paradigm. Ultimately, in Kirzner's view, the development of new businesses comes from the potential entrepreneur's ability to promptly capture new opportunities (in terms of profit) and new information within a market characterized by uncertainty.

Reviewing the Austrian literature on entrepreneurship, we should of course mention Joseph Schumpeter who made several important contributions in a number of fields, particularly to the theory of entrepreneurship. Many scholars believe he should be considered the first person to propose a functional approach of entrepreneurial activity, namely the first approach that identifies a specificity in entrepreneurial performance. Schumpeter's (1911) main contribution was his introduction of the concept of the entrepreneur, not as an equilibrator as in Kirzner, and neither as a bearer of uncertainty as in Mises, but rather as an agent that introduces new products, services, processes, sources of supply etc., thus disturbing an existing market equilibrium. Schumpeter synthesizes this idea in his famous concept of "Creative Destruction": "For actions, which consist in carrying out innovations, we reserve the term Enterprise; for the individuals who carry them out we call Entrepreneur" (Schumpeter, 1939, p.100). Hence, according to Schumpeter, new businesses are born from the thrust of the potential entrepreneur who, in envisioning new combinations of production – in terms of goods, services, or modes of production – decides to start a new venture. Schumpeter, however, whose perspective is slightly different from that of Mises and Kirzner, believed the successful entrepreneur should possess the ability to create new productive combinations.

Another famous economist who theorized about entrepreneurship was the American, Knight (1921), who argued that entrepreneurs have a particular faculty of anticipating what future conditions will be alike. This particular ability, that Knight called "judgment," is the entrepreneur's ability to make decisions in a particular situation of uncertainty. According to Knight, it is not possible to parameterize all future outcomes in terms of formal models. The entrepreneur can use past experience or objective probability calculation to assess the risk an entrepreneurial action entails. But in many cases he is forced to rely on subjective judgments or estimates, in which an

element of uncertainty exists. If every individual was capable of calculating all the expected changes each one of them would make the same decisions. Therefore, the distinctive feature of the entrepreneur is thus the ability to endure generic uncertainty and translate it into a ponderable risk.

There is an interesting formulation of Kirzner (1979) to characterize the thought of Knight. As Kirzner noted, it is not necessarily true that the entrepreneur's function is to translate a generic uncertainty into ponderable risk. For Kirzner, the entrepreneur is one who claims to have identified new opportunities and who earns entrepreneurial profit if his judgment about the risk proves to be correct. That is, even if the functional idea of Knight that refers to "decide what to do and how to do" is certainly an entrepreneurial activity, it is conceptually quite far from having to withstand a non-quantifiable risk.

Functional backgrounds of the entrepreneurial figure have also characterized the research of some scholars not belonging to the Austrian tradition. Among these was Baumol, whose work "The Entrepreneurship in Economic Theory" (1968) integrates the Schumpeterian innovation function with the one of leadership. Chandler (1962) identifies the entrepreneur as someone who takes strategic decisions to achieve the fundamental objectives of a company.

In the strict economic meaning of entrepreneurship, the entrepreneur is assigned with a specific function: to recognize an opportunity under uncertain conditions. Opportunity discovery thus involves dealing with the chances of a business coming into reality in an uncertain context. Opportunity, therefore, is the determining factor, which must be either discovered or constructed. From this perspective, the entrepreneurial function is thus to perceive the contextual conditions and understand how to operate within them in order to make the most of the opportunity. Hence, the context can influence opportunity recognition of (prospective) entrepreneurs as well as opportunity exploitation and access to external resources. Thus, with regard to conditions entrepreneurs have to deal with, applying an opportunity-oriented perspective to entrepreneurship demonstrates the value of going beyond the individual perspective, as this captures the influence of the contextual conditions on opportunity recognition.

There is no doubt that opportunity discovery and exploitation have been and remain a central concept in entrepreneurship research (Venkataraman, 1997; Shane & Venkataraman, 2000; Davidsson, 2002; Timmons & Spinelli, 2003; Shane, 2003; Shane & Eckhardt, 2003; Baron, 2006; Casson & Wadeson, 2007; Dimov, 2011). The opportunity-oriented conceptualization of entrepreneurship that has its roots in the classical definitions of Kirzner's (1973) "alertness to opportunity" has received widespread recognition and support in the literature. More recent studies on entrepreneurship, for example, explore how opportunities are recognized and constructed through social relations (Koning, 2003; De Carolis & Saporito, 2006; Fletcher, 2006). Thus, with regard to the influence of the contextual conditions, these studies stress the value of going beyond the individual-internal perspective toward a more externally oriented perspective.

In sum, the difference between the trait approach and the functional approach is that the latter, in order to explain the success and development of a business, does not refer to the personal characteristics of the entrepreneur but rather to certain organizational and managerial functions. That is, the functional approach focuses more on the role of the entrepreneur in relation to the entrepreneurial functions that are rather conditions that should be complied with. The opportunity enactment perspective emphasizes the fact that it is not only personal characteristics that influence entrepreneurship, but rather that entrepreneurial activity can also be influenced by the context condition, indicating that there is a nexus between the entrepreneurs' perceptions and actions, and the context.

All considered, what we found in the review of these two approaches is that while many of these considerations have been useful for improving our understanding of the challenges the entrepreneur faces, many important topics, particularly those more relevant to the process of forming a new business, would still seem to be a little vague.

Since many of the studies applying the functional perspective acknowledge that attention must be paid to more external issues, the challenges in conceptualizing entrepreneurship as well as enterprise development through a more thorough and more expanded view of the phenomenon will be explored in the next paragraph.

### 3.2.3 THE NEW BUSINESS VENTURING APPROACH

Academic research on entrepreneurship has focused significantly on profiling the individual characteristics and personality traits of entrepreneurs and their ability to identify and exploit an opportunity within the context of new business formation. However, although these studies offer useful insights into the entrepreneurial field, this research has not really enhanced our understanding of the many facets and complexities involved in forming a new business. Hence, several studies show there is no direct relation between the entrepreneurs' innate characteristics and education, and positive or negative business development (Gartner, 1988; McKenzie, Ugbah & Smothers, 2007). According to Van de Ven, "the study of entrepreneurship is deficient if it focuses exclusively on the characteristics and behaviors of individual entrepreneurs, on the one hand, and if it treats the social, economic, and political factors influencing entrepreneurship as external demographic statistics, on the other hand" (1993, p. 226). The reason is that it is rather difficult to prove that certain innate predispositions and/or acquired skills are not self-interpretations, but subjectively measured characteristics (Ensley et al., 2000; Chandler & Lyon, 2001). Also, it is very difficult if not almost impossible, to define an ideal mix of traits, skills, and expertise, an approach which only complicates tracing the ideal profiles or personality of the successful entrepreneur (Oosterbeek, Van Praag & Ijsselstein, 2010). According to Van de Ven "Researchers wedded to the conception of entrepreneurship for studying the creation of organization can learn much from the history of research on leadership. Like the studies of entrepreneurship, this research began by investigating the traits and personality characteristics of leaders. However, no empirical evidence was found to support the expectation that there are a finite number of characteristics or traits of leaders and that these traits differentiate successful from unsuccessful leaders." (Van de Ven, 1980, p. 86: in Gartner, 1988, p. 22). Indeed, according to Gartner (1988), these features, namely the concerns about entrepreneurial personality traits and functional skills, are inadequate for clarifying the complex development process in entrepreneurship. The "trait approach," in particular, has diverted attention from the primary phenomenon of

entrepreneurship – the creation of organization, the process by which new organizations come into existence (Vesper, 1982). According to Gartner, “New venture creation is the organizing of new organizations” (1985 p. 697). And to Weick, this organizing of a new organization means “To assemble ongoing interdependent actions into sensible sequences that generate outcomes” (1979, p.3).

The notion of “organizing” that stresses the importance of the organizational dimension in starting an entrepreneurial activity, points out that these researches approach the phenomenon of interest from a particular perspective. In particular, this perspective assumes that the creation of an organization is a contextual event and the entrepreneur should be considered part of the complex process of new venture creation. Following this logic, the approach to studying entrepreneurship should place the organization at the prime level of analysis, and the entrepreneur should be considered as the one who undertakes some activities in order to enable the organization to come into existence (Hebert & Link, 1982; Vesper, 1982; Shapero & Sokol, 1982). Similarly, it is impossible to clearly separate the actor, i.e. the entrepreneur and the environment in which he/she operates. An aspect that characterizes the process of forming a new business is the provision of an organizational configuration for the new firm (i.e. taking strategic, management, and organizational decisions). According to this perspective, a specific responsibility of the entrepreneur is thus to arrange for the new company an organizational system to start the internal and external activities necessary for the formation of the new business. Hence, the critical process in starting a new entrepreneurial activity is not related primarily to discovery of the opportunity, but more to the exploitation of opportunity. The idea is that the difficulties for new entrepreneurial businesses do not lie in discovering an opportunity and conceiving an original way of exploiting or developing it. Rather, according to the overall new venturing perspective, the difficulties encountered in the early stages of developing a new business are related to putting together critical resources and organizing the flux of complex activities necessary to seize the opportunity (Gartner, 1988, 1995). This perspective on the entrepreneurial phenomenon as an organizational process has recently become a popular way for the study of entrepreneurial issues as it focuses on issues such as the change and

dynamism that are closer to entrepreneurial reality than models focusing on "entrepreneurial characteristics" (e.g. Sorensen & Fassiotto, 2011). Agreeing with those standpoints, rather than dwelling on the various entrepreneurs' personal characteristics and functions, it would seem more appropriate to give greater credit to the organizational dimensions in studying the difficulties that affect the development processes of a new venture.

### 3.3 FINAL CONSIDERATIONS

Through the analysis of the literature we have identified the elements that have influenced the progress of research related to entrepreneurship in recent years. We have observed that in the entrepreneurial literature over the years a series of contributions, gained from the disciplinary research grounded in economy, psychology, and sociology, has been developed. We have found that the issues discussed in greater depth are those related both to character traits and functions of the potential entrepreneurs and to those related to activities necessary to organize a new business.

In our attempt to systematize contributions regarding studies on entrepreneurship and new venturing, we have come to identify three lines of entrepreneurial research: The trait approach, the functional approach, and the new-venturing approach. Each of these research approaches proposes interpretive perspectives that aim at identifying some key variables in the process of starting and developing a new business. In particular, the first line of research we identified, the trait approach, embraces all studies concerning the "entrepreneur's personal and individual variables" that play a key role in the process of genesis and further development of new businesses. We have, in fact, observed that for some scholars entrepreneurial talent can be expressed as a set of individual characteristics such as the entrepreneur's personality, skills, and formation (e.g. Michelacci, 2003; Van Praag & Versloot, 2007; Davidsson, 2008). Most of these studies clearly refer to the peculiar and specific characteristics of the entrepreneur and of the "history" the entrepreneur possesses, and to the set of innate attitudes and skills induced through education, formation, or work experience. There have also been studies aimed at

discovering the determinants and motivations of an entrepreneur to start a new business (e.g. Davidsson, 1995; Zahra, Sapienza & Davidsson, 2006). Insights gained from this research have been influential in shaping the research on entrepreneurs' managerial functions and their influence on venture creation, founding, success, and survival. This is particularly true for the second approach we identified, the functional approach. The mainstream of economic thought identifies the distinctive attributes of the entrepreneur's managerial functions in the ability to recognize opportunities and to deal with difficult situations. In comparison with the trait approach, here the perspective is more functional as it identifies the entrepreneurial phenomenon in the accomplishment of certain functions and activities or in the possession of certain requirements. In particular, the functional approach tries to explain the success of a new business in identifying the specific duties and functions associated with the entrepreneur.

All considered, what we have found in the review of these two approaches is that the trait approach aims to explain the success and development of a business by focusing on the personal traits of the entrepreneur. On the other hand, the functional approach helps us to understand the entrepreneur as one capable of identifying new business opportunities and making decisions on which a business organization's birth, survival, and development depends.

The third stream we have identified, the new venturing approach, seems to be more focused on businesses and their contexts, rather than on individuals and the discovery of opportunities. According to this latest perspective, which extends the concept of entrepreneurship from an individual level towards an organization level, the development of a new firm should be considered as a collective organizational process that, because of the conjoint internal and external organizational dimensions, needs to take into account the interdependencies with the business context (Sorensen & Fassiotto, 2011). Hence, adopting this perspective, the birth of a new business is a phenomenon that lends itself to be examined and interpreted through the use of a more contextualized view of entrepreneurship (Welter, 2011). The difficulties a new business encounters in the course of its founding process, can be related to the need to organize and arrange the business for the necessary internal and external support. Agreeing to those standpoints,

rather than dwelling on various personal traits and functions of the entrepreneur, seems more appropriate to give greater credit to the collective organizational process of new business formation.

Through the foregoing literature review we have reached the conclusion that future research needs to extend the unit of analysis beyond the single entrepreneur and to take a more context-oriented approach. Entrepreneurial activity cannot be considered an autonomous entity that emerges in isolation but, as suggested in recent entrepreneurship research, new business development should be regarded as a collective entrepreneurial action (Sarasvathy & Venkataraman, 2011; Ciabuschi, Perna, & Snehota, 2011). So much so, that recently entrepreneurship scholars adopting the traits approach have moved their focus towards the entrepreneurs' external environment, demonstrating the value of going beyond an individual perspective (e.g. Ucbasaran, Westhead, & Wright, 2001; Davidsson & Honig, 2003; Greve & Salaff, 2003; Aldrich & Kim, 2007; Ruef, Aldrich, & Carter, 2003). Moreover, scholars belonging to the functional approach take a step further and understand the context as the place where opportunities are socially recognized and constructed through social contacts (e.g. de Koning, 2003; Fletcher, 2006; DeCarolis & Saporito, 2006). This suggests it is relevant and important to broaden the research to the relevant business landscape and to see how the new company is connected to the context and how this affects its development.

So, if the context variables may be determinants of the development of a new company, our next intent will be to go to see what available conceptual frameworks exist that concern the context. In particular, studies on business marketing have distinguished some typical features of business markets that appear to have consequences for the new business development process. Therefore, in the following chapter, we will go through the review of the literature on market theory to capture the nature and characteristics of the landscape in which every business has to operate to develop. Thus, with regard to the influence of the contextual conditions, we will further develop our discussion on what is going on in business markets and why the business context is relevant for the new venture formation.

# Chapter 4

## Perspectives on Markets

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What we have seen in the previous chapter is that recent research supports the claim that external organizational dimensions are a weighty factor for the development of a new business (Stuart & Sorenson, 2007; Sarasvathy, Dew, & Ventresca, 2009; Ciabuschi, Perna, & Snehota, 2011; Aaboen, Dubois, & Lind, 2011). An implication of this proposition for research is the need to extend the unit of analysis from internal factors, such as entrepreneurs and internal organizations, to other external dimensions.

Thus, in this chapter we will start looking outside the company in order to interpret the external context with the intention of highlighting the relevant characteristics of the business landscape in which new businesses emerge. We will go through the review of the literature on market theory to present approaches to the market in different disciplinary fields such as economics, both the neoclassical and Austrian schools of thought, and socioeconomics and marketing research. The purpose is to evidence how the ideas and conceptualizations of markets are related to numerous empirical studies that have highlighted several distinctive features affecting the conduct of market actors and the new venture development process. This investigation will provide us with an idea of the scale and complexity of business markets and how the network perspective in the marketing literature is more concerned with how markets are ‘in practice’ rather than with a normative idea of how markets should be in economics. Indeed, the market-as-network perspective highlights relevant characteristics of business

markets, namely the existence and centrality of business relationships, which may help us to cope with the phenomenon of new venture development that we are interested in. In particular, we will present and illustrate the conceptual framework, which we will refer to as the business network perspective, and then discuss why it constitutes the theoretical basis of our research.

#### 4.1 DIFFERENT PERSPECTIVES ON MARKETS

The literature has proposed various ideas about how to conceptualize the market, and many scientific disciplines have debated the subject. Contributions on the topic can be found in economics and also in disciplines such as philosophy, history, political science, sociology and, more specifically, in marketing theories. Depending on the point of view and the perspective through which the business market has been studied, many of the questions have been answered differently. Until now, it appears that none of the main disciplines has proposed an overarching and complete market theory. Although there is no market theory in the strict sense, prevailing ideas about what markets are and how they work come from neoclassical economics. We believe an overview on alternative and complementary viewpoints is useful. Therefore, we will review the literature on market theories outlined in various scientific fields and extract what the research on business-to-business markets states about the typical characteristics of those markets. We engage in this review to gain a better understanding of the environment and context when creating a new business. This rereading of the literature on market conceptualizations is indispensable for determining the theoretical perspective that forms the cornerstone of the framework for discussing this thesis.

As we will see in the final considerations, three main ideas of market emerge from our literature review. On the one hand, according to the neoclassical economic perspective, the market is conceived as an anonymous mechanism that facilitates, through price determination, the exchange between a set of buyers and sellers of a given product in a given period of time. On the other hand, according to the Austrian school of economics and the sociological interpretation, we will find the idea of the market as a

mechanism of knowledge and information coordination, where different actors, linked by exchange relationships, are engaged in recurring patterned behavior. Finally, we will introduce the idea of the business network in marketing, which highlights some market characteristics that could be underpinnings for the conceptualizations of the business markets phenomenon. We will emphasize the characteristics highlighted in numerous empirical studies. In particular, we will argue that the typical features of these markets, or business networks proposed in the leading literature of business marketing are characterized by:

- The existence and centrality of business relationships;
- The presence of interdependencies between market actors;
- Network-like structures;
- Centrality of buyer-seller interaction processes.

#### 4.1.1 THE NEOCLASSICAL ECONOMIC PERSPECTIVE

The market concept has been extensively elaborated in economic theory, and many efforts have been made to develop explanatory theories and models of markets. The most accepted conceptualization of the market comes from the economists of the neoclassical tradition<sup>12</sup>. According to this tradition, the market is defined as a set of firms or individuals selling and buying a certain good (and its closed substitutes). In this sense the business market would be defined as a set of buyers and sellers that interact in order to exchange particular goods or services. The neoclassical economic theory of the market deals with analyzing the different market forms such as perfect competition, monopoly, and oligopoly. These are considered market forms that have as a model “the perfect market.” In the perfect market, according to traditional theory, there are no costs of transacting nor uncertainty, and information asymmetry. One of the most popular

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<sup>12</sup>This prevailing economic theory, at least as regards microeconomics, refers to the neoclassical assumptions that are often called marginalists. Conventionally, the neoclassical economics school dates from 1871-1874, years of the publication of the first systematic works of William Stanley Jevons, Carl Menger, and Léon Walras.

theories about the market in the neoclassical economic view is, without doubt, that of perfect market competition. The theory of perfect competition suggests a market situation where several competitors offer similar products or services. All buyers are fully aware of the characteristics of the product, and prices are determined by the classical curve of demand. Thus, according to neoclassical microeconomics theories, perfect competition is a market characterized by the inability of entrepreneurs to set the selling price of the goods they produce. Prices are derived exclusively from the encounter of supply and demand. On the whole, the neoclassical interpretation takes the market for granted, a place driven by price theory, where the entire structure tends to a stable equilibrium. Interactions among buyers and sellers are limited to price signaling; counterparts tend to agree on the best price since no additional information is needed for making the right choice. This means the price represents the major and sufficient source of information. Customers and suppliers enter and exit the single exchange situation with no associations to past or future experiences; the market exchange is instantaneous and has a discrete and not continuous nature. The market is to be intended as an established system in which companies have limited influence and the exchanges that take place are viewed as isolated events, single transactions without connections, neither with previous exchanges nor among those who participate (Håkansson, Harrison, & Waluszewski, 2004). In this view, the business transactions are discrete events, isolated and impersonal. This view emphasizes an atomistic structure of the market composed of numerous anonymous and interchangeable buyers and sellers.

To conclude, in neoclassical economic theory, the market is seen as an anonymous mechanism that facilitates exchanges, a mechanism capable of ensuring an efficient allocation of resources through price determination. A key assumption in the neoclassical economic conceptualization of the market is that the actors involved in business exchanges are capable of making rational decisions. In this view, the individual who behaves rationally is assumed to have complete knowledge of the possible alternatives of choice, namely the chance to check the results associated with each

alternative and the ability to solve every problem of choice<sup>13</sup>. Consequently, the economic value and economic costs determine the decisions of buyers and suppliers during the exchange processes (e.g. Frank, 1997; Varian, 2005). In markets with these characteristics, actors are supposed to be engaged in independent transactions with a large number of counterparties. Stable and long-term collaborative relationships would constitute a distortion of the market mechanism.

Though the theory of the perfect market has been revalued for a long time, economists have identified some shortcomings that limit the formation of these markets (Brezinski & Fritsch, 1997; Lindblom, 2001)<sup>14</sup>. Although the classical economists meant markets as physical and concrete places, their interest has focused on economic production and on an understanding of price formation (or pricing), to the detriment of understanding the exchange phenomenon (Biggart & Delbridge, 2004). According to other disciplines, the neoclassical microeconomic analysis of business markets is qualified to explain how the market works only on the basis of the interaction of the elements constituting demand, supply and price, but it tells us nothing of the contractual behavior of individuals, of the influence of the economic environment on them, and of the modalities in which individuals come together to sell and buy goods (Kahneman, 1994; Thaler, 2000; Goyal, 2009). Critics of the neoclassical conception of markets, rather than defining it as undeniably unfitting, argue that it does not take into consideration the various behavioral and empirical dynamics taking place among the various market actors within the market. This aspect of exchange patterns behavior has received much attention in other theories of the market, in particular in the Austrian school of economics to which we will devote more attention in the next section. It would thus appear that neoclassical economists have probably lost sight of the empirical evidence, focusing almost exclusively on theoretical modeling. In fact, today

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<sup>13</sup> The theme of rational choice has been the subject of study by many scholars, including Simon (1955) and Kahneman & Tversky (1979).

<sup>14</sup> The theory of perfect competition, like other neoclassical market theories that have been proposed has undoubtedly strongly influenced the way the literature on business markets has developed the concept of the market. The equilibrium between supply and demand, as well as the mechanism of price formation, remain the most accepted basic aspects of the market.

neoclassical economists tend to be confronted by other schools of thought such as in sociology and in business marketing.

#### 4.1.2 THE AUSTRIAN SCHOOL OF ECONOMICS PERSPECTIVE

Some other researchers, in particular scholars of the Austrian school of economics, extended the perspective on the market primarily in terms of its functions. In opposition to the dominant trends in neoclassical economics, policy and philosophy, these scholars regard the market as an institution (Von Mises, 1949; Hayek, 1945; Kirzner, 1997; Boettke & Coyne, 2009). Coase, for example, notes in this regard that, “although economists claim to study the market, in modern economic theory the market itself has an even more shadowy role than the firm” (1988, p. 7). He also suggests that contemporary economists are concerned only with the determination of market prices. This, in Coase’s opinion, has led to a condition in which considerations of the marketplace itself are missing entirely. About ten years later, Kirzner in his book “How Markets Work” stated that: “Surprisingly standard economics does not provide satisfying explanations of exactly how and why markets work” (1997, p. 9). The Austrian school of economics, also known as the Vienna school, like the neoclassical economists, argues that valid economic theory should be derived logically from basic principles of human actions. According to this perspective, in markets, supply and demand meet through governed and decentralized exchange processes. This means markets are intended to be mechanisms of coordination (Arndt, 1979). This concept essentially originates in the work of Hayek (1945), one of the most important representatives of the Austrian school, who argues that the market has to be intended as a mechanism to connect and make use of the knowledge distributed among members of society and that, after the exchange, the single agent increases its information. According to Hayek, like many economists before him, including Von Mises (1949), the market ensures the best use of resources, and price is used to communicate information. The only system able to give an optimal allocation of resources is the system of the free

market<sup>15</sup>. In “*The Use of Knowledge in Society*” (1945), Hayek explains how the price mechanism allows the sharing of individual knowledge through the principle of self-organization, and argues that pricing a system is not the result of intentional human intervention, but the result of spontaneous human actions.

The interesting argument is that the Austrians, in contrast to the neoclassical school, consider that information or knowledge is always something subjective, which cannot be ‘given,’ but must be constantly created or generated by the market players when they pursue a revenue opportunity. From the Austrian perspective, entrepreneurship is indeed as fundamental and as essential to the understanding of economics as any of the core concepts that make up the Austrian tradition. The function of the market is, therefore, not only to allocate resources, but the market is an institution that facilitates the process of connecting and applying the knowledge of various actors between them. The concept of the business market as a mechanism of knowledge and information coordination is to be intended as a prerequisite for evolution and innovation in economic systems. We can, therefore, conclude that the concept of market as an institution developed by the Austrian theorists moderates the extreme conclusions developed by the neoclassical economists.

This new way of observing, theorizing, and modeling market dynamics has inevitably led to new perspectives of analysis. For example, Barnhill & Lawson (1980) consider that the market as an institution offers a broader and more comprehensive perspective on the dynamics characterizing the market. According to them, the market should be understood as an active process that involves exchanges between customers and suppliers but also involves the actions of those entities, such as intermediaries, that facilitate business interaction.

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<sup>15</sup> The free market is a market in which prices of goods and services are accessed only by the mutual interaction of buyers and sellers. By definition, free-market sellers and buyers do not force or deceive each other, or are forced by a third party. The aggregate effects of individual decisions are described by the natural laws of supply and demand.

### 4.1.3 THE SOCIOECONOMICS PERSPECTIVE

The conceptualization of the market has not only concerned scholars of economy, but has aroused some interest in other disciplines such as sociology and in more managerial disciplines such as marketing.

Perspectives on markets in social economics, which will not be treated in-depth in this study, allow us to understand, differently from neoclassical market theory, the importance of the role actors play in business markets. Indeed, an important issue in sociology is the analysis of the individual consumer in interaction with other agents in the market (Lucas, 1972; Fligstein, 2002).

“Economic Sociology” is a term introduced by Weber and Durkheim to refer to a sociological perspective applied to economic phenomena (Smelser & Swedberg, 1994). However, most scholars agree it has been Granovetter’s (1985) idea that market exchange is embedded in social structures that paved the way for a re-interpretation of the notion of markets from a sociological perspective. According to Granovetter “in a general way, there is evidence all around us of the extent to which business relationships are mixed up with social ones. [...] That business relations spill over into sociability and vice versa [...] firms are connected by networks of personal relations, but at all levels where transactions must take place” (ibid. p. 495-496). Business exchanges, as well as economic relations between actors interacting in the market “merge” through social relationships. To conceptualize the merging process of business relationships Granovetter introduces the concept of embeddedness, which indicates the idea that economic activities are rooted in society’s grounds. Granovetter’s idea of the market is that social relationships are embedded in social networks that generate trust and create exchange relationships that differ from those suggested by economic rationality. According to Granovetter, the production, distribution, and consumption of goods depends indeed on social factors such as culture, habits, sense of responsibility, and reciprocity. That’s why Granovetter argues that the economy is embedded in society. In contrast to rational choice proposed by the neoclassical perspective, embeddedness theory leads instead to an assessment of the centrality of actors and institutions.

Successively to Granovetter, whose contribution has been to illustrate how social structures play a supporting role in building and sustaining business exchanges, Callon (1998) suggests another interesting sociological concept of the market. Callon, credited for important contributions in the field of social economics, offers an approach that focuses on the understanding of what constitutes the heart of market exchanges. According to Actor Network Theory (Latour, 2005), of which Callon is one of the main proponents, in any description of market phenomena we should treat networks as actors and actors as networks. Callon argues that elements connected in the networks are at the same time formed and forged by the networks themselves. He denies the existence of a market background consisting of social, economic, or technical factors because this background is built simultaneously with the construction of the network. According to Callon, the market should be viewed as a means of coordination, in which agents pursue their own interests by calculating, optimizing, and maximizing. In addition, he believes agents have different and conflicting interests, and that the resolution of these conflicts can be achieved only through transactions with defined prices. Callon's idea is that the actor network isn't reducible to an actor nor to a network. Networks are composed of a series of heterogeneous elements, animated and unanimated, which have been linked to one another for a certain period of time. Callon, therefore, considers market agents as "strangers" who enter and leave the transaction process and lose their anonymity only during the brief period of effective exchange (Callon, 1998).

What the social economics perspective allows us to understand better than the neoclassical market theory, is the importance of the role the actors play in business markets. This also has some consequences for the theory explaining how markets work. In fact, as we will see, social economics grounded theories have inspired other disciplines such as marketing.

#### 4.1.4 THE MARKETING PERSPECTIVE

Research on market dynamics and peculiarities can be considered one of the most relevant issues, not only in economics and sociology, but also in business management

and marketing. However, whatever is outlined in marketing research is eclectic and draws on the Austrian school of economics and on socioeconomics.

Markets, and the associated phenomena, are of particular interest from the perspective of business management, and particularly marketing studies. Many publications dealing with issues concerning marketing or business management, such as pricing, consumer behavior, products, and distribution channels, are based on, or at least make reference to, the functioning of the market (Mattsson, 2003; Araujo, 2004). Within the marketing and business management disciplines, however, we can find different definitions that try to describe the business market landscape and understand its nature and dynamics. In particular, in the literature of business-to-business marketing market conceptualization has been put in relation to the different types of exchange mechanisms that take place between business organizations (Alderson & Cox, 1948; Cook & Emerson, 1978; Easton & Araujo, 1994). Studies in this field recognize the “depth” of the market as an organized behavior system in which series of transformations take place. These studies investigate the different ways in which companies organize their business exchanges with the surrounding context, believing that the existence and understanding of these business exchange typologies could offer an explanation for the peculiarities that characterize different markets (e.g. Webster, 1992; Möller, 1994). Some researchers, such as Sheth (1973) and Möller (1981), argue that in order to understand the “behavior” of the market, we must also include the behavior of the buyer, seller, intermediaries, and regulators/mediators during their exchange relationships. Early marketing research, based primarily on a number of empirical findings that focus on the behaviors of market participants, suggests that the market is intended to be an organized behavior system. According to Wroe Alderson: “A system is a set of interacting elements. A behavior system is a system in which the interactions take the form of human behavior” (1965, p. 25).

The behavioral conceptualization of markets has continuously recognized the patterned behavior dimension of markets and has studied the impact of this variable on how the market works. Consequent to new insights of business market peculiarities,

scholars began to conceptualize business relationships in more detail. This is particularly true for the development of relationship marketing perspectives.

#### 4.1.4.1 THE RELATIONSHIPS MARKETING PERSPECTIVE

Compared to the neoclassical literature that considers business relationships as a series of independent transactions, the business marketing literature, which considers the market as a system of interacting elements, suggests that business relationships are a series of organized business exchanges (Snehota, 2004). Accordingly, business market conceptualizations seem to be more concerned with how customers and suppliers connect to each other than with distinct isolated market transactions (Håkansson & Snehota, 1995; Håkansson et al., 2009). Since the first idea of the market as a system of economic exchanges in which organizational companies are connected through a series of organized exchange mechanisms, there has been a considerable increase in the number of empirical studies on various aspects of inter-organizational relationships in the business context. Collectively, these business marketing researches have made a strong case for the relevance of creating close business exchange relationships with key suppliers or customers; they have also provided important insights into the features of such relationships (Fraizer, 1983; Dwyer et al., 1987; Heide & John, 1990; Anderson & Narus, 1990; Morgan & Hunt, 1994).

A significant contribution to the development of market conceptualizations in relationship marketing theories was made in the seventies by researchers in the IMP (Industrial Marketing and Purchasing) group, contributions of which can be found in numerous publications (Håkansson, 1982; Håkansson & Johanson, 1992; Håkansson & Snehota, 1995; Ford, 1997; Håkansson et al., 2004; Håkansson et al., 2009)<sup>16</sup>. The IMP group started at the University of Uppsala in Sweden with the objective of conducting empirical research on marketing approaches of companies in the field of industrial goods.

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<sup>16</sup> The main theoretical impulses of the IMP research tradition can be traced back to sociology, while the empirically oriented methodology carries an imprint from anthropology (Håkansson & Waluszewski, 2002; Mattson & Johanson, 2006).

The initial goal of the research was to develop appropriate schemes of interpretation for describing the empirically observable reality of industrial markets<sup>17</sup>. In 30 years of research, the IMP tradition has highlighted many aspects of the functioning of business-to-business markets, but there are three features that characterize industrial markets.

The first is that businesses tend to do business with few customers and suppliers. The IMP research shows that for most businesses the major part of turnover comes from continuous relationships that a company has with a limited number of customers (and on the purchasing side with suppliers) (Håkansson & Östberg, 1975; Gadde & Mattsson, 1987; Håkansson, 1987; Anderson, Håkansson, & Johanson, 1994; Möller & Halinen, 2000; Araujo, Dubois, & Gadde, 2003; Ford & Gadde, 2008). Expressed in quantitative terms, often more than 60% of the volume of sales of many business companies depend on no more than 10 customers and on the side of the suppliers, typically the top 10 suppliers of a company account for about two thirds of total purchases, which in turn represent more than two thirds of the total costs in a business (Håkansson, 1989; Gadde & Snehota, 2000). That is to say, sales and purchases are concentrated in a few important relationships. These relationships, according to IMP empirical research, are long lasting depending, of course, on how old the company is. In most cases, the first customer and first supplier are still there after many years of activity. That means business relationships are continuous and that the change in the customer and supplier base is slow and gradual. Research has acknowledged that every business needs to establish more or less continuous relationships with other businesses through which indispensable resources are obtained from suppliers and provided to customers (Achrol, 1997; Håkansson & Waluszewski, 2002; Ford et al., 2005; Cantù & Corsaro, 2011). The existence and importance of stable business relationships has been shown to be beneficial for both customers and suppliers involved as they represent the source of sales, purchases, profits, and new ideas (Björk & Magnusson, 2009; Rampersad, Quester, & Troshani, 2010). This is theoretically significant because, according to our literature review, until now no one has proposed a good theory for it. For example, economic

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<sup>17</sup> Between 1977-1978 IMP scholars have tracked 1,200 b2b relationships between companies in European countries.

theory assumes that those continuous business relationships do not exist and, if they do exist, they are a distortion of the ideal of full competition that assumes no preferential relationships between customer and supplier for reasons other than the features of the offering. The customer judges strictly how good the product or service is compared to the competitors' products or services and, depending on quality and price, it will choose the one that can better satisfy his needs. This is how economic theory concerns the market mechanism. In the reality of business markets there are continuous relationships that are preferential, in which several important processes are going on. It has been observed that in these continuous "high-involvement" business relationships (Gadde & Snehota, 2000) that characterize business markets, the product items and services elements are not only transacted but also mutually developed through continuous adjustments to apply workable solutions (Windhal & Lakemond, 2006; Håkansson et al., 2009; Ciabuschi, Perna, & Snehota, 2011; Andersson et al., 2011). Following this logic, the product or service offered tends to become a variable with respect to the business relationships (Håkansson, 1982; Håkansson & Snehota, 1995). Taking this perspective, markets are primarily defined by the set of business relationships between businesses rather than by the products exchanged. This contrasts with economic theory where the product is the defining feature of the market.

The second feature that comes through in empirical studies of business-to-business markets is that the continuous and long-term relationships with partners are characterized by frequent interactions and information exchange that enable the parties involved to meet each other's requirements and adjust to specific needs (Hallén, Johanson, & Sayed-Mohamed, 1991; Ford et al., 2010). Unlike the neoclassical transaction process concept that considers the business purchase or sale as an isolated event, in the business marketing perspective, there is often frequent interaction and information exchange between the two companies, involving a number of actors on both sides coming from different functional areas. For example, between a supplier like Bosh and a customer like Mercedes, there are probably hundreds of people on one side and thousands on the other side of the two companies that interact with each other to design, produce, and implement solutions required by customers. These interdependent

relationships occur because of interactions between the representatives of the companies involved, and also because the resources implicated need to be interfaced in order to go on in production (Håkansson, 1982; Håkansson & Snehota, 1995; Håkansson et al., 2009). These intense flows of interactions, both between the two companies and within them, aim at achieving mutual adaptations in the product or service exchanged. In this logic, the relationship moves radically away from the transaction process, towards a continuous interactive relationship that serves to access, obtain, and adapt the necessary resources (Harrison & Waluszewski, 2008; Ingemansson & Waluszewski, 2009).

This brings up another critical feature of business markets highlighted in studies in the IMP tradition. Since businesses are strongly connected via extensive intense ongoing relationships, they are also significantly interdependent (Håkansson & Snehota, 1995) on each other. All businesses provide resources to other businesses, and in turn, all businesses utilize resources controlled and provided by other businesses. Since businesses do not control all of the resources and activities needed to carry out their business activities, every single firm is dependent on its customers and suppliers. Every relationship cannot be considered in isolation, but is part of a broader contest of interdependent relationships. This interdependency is the reason why business relationships are profoundly interrelated; each of them is linked to others in a network-like structure. Inevitably, what happens in one business relationship affects what happens in another (Håkansson & Snehota, 2006). This picture, of a pattern of interconnected and interdependent relationships, suggests that the business market can be seen as complex network of relationships that “emerge” from the development of business relationships (Håkansson & Snehota, 1995).

These insights about how business markets work that appear from past IMP research, suggest that in business markets businesses are embedded in a limited number of economically relevant, interdependent business relationships with other customers and suppliers. The interesting aspect of this research tradition is that scholars belonging to this stream offer some theories to explain certain business market phenomena; or at least they have been proficient in explaining why business relationships exist. In our literature review, outside the IMP research tradition, we haven't found any convincing explanation

for why relationships arise. The IMP research stream attempts to explain why business relationships develop in business-to-business markets and why they are important. What we have seen is that one basic assumption of why we have these business relationships is that businesses are dependent on the activities and performance of other companies in carrying out their own operations. That is, the way relationships between customers and suppliers work will impact both potential developments of the customer and of the supplier. The interaction processes underlying business relationships development thus seems an important aspect of the development process of a new business.

Taking the network view of firm-market relationships, which differ from the perspective assumed by neoclassical economic theory, the problem of the strategic development of a business becomes “relating” to the network of connected business relationships (Håkansson & Snehota, 1995; Achrol & Kotler, 2011; Johanson & Vahlne, 2011).

Having reviewed in the business-to-business marketing literature the mainly original insights about how business markets work, in the next paragraph we will briefly illustrate the main features of business-to-business markets that distinguish them from the consumer market.

#### 4.1.4.2 BUSINESS-TO-BUSINESS MARKETS

Most of us have experience of the consumer market and assume that features we know apply to markets in general. Empirical evidence indicates that business markets have several specificities. Numerous studies show that business markets are much more complex and substantially different from consumer markets (Axelsson & Easton, 1992; Easton & Håkansson, 1996; Ford, 1997; Håkansson & Snehota, 2000). In recent decades an extensive amount of research has captured the particular nature of business markets that distinguish them from consumer markets; this research has also examined marketing practices adopted by companies operating in these markets. In fact, the aspects that characterize different markets have been widely discussed in the literature (Guatri, Vicari, & Fiocca, 1999; Ford, 2002; Håkansson, Harrison, & Waluszewski, 2004;

Anderson, Narus, & Narayandas, 2008; Håkansson et al., 2009; Ford et al., 2010; Hutt & Speh, 2012).

Transactions between companies, organizational customers, and end customers are at the center of every business activity. However, transactions between companies, organizational customers, and final consumers take place in different marketplaces. Business-to-business markets (also called B2B markets) are those in which the actors taking part in transactions are organizations in all their forms, be they companies (industrial, commercial, or service companies) or public or private institutions. Organizations taking part in the marketplace can be placed in any position along the supply chain of each sector, starting with those that work the raw materials to those that obtain the finished product. Business customers are those organizations that buy goods or services for productive activities and/or services that support their operations.

The distinctive elements of business markets are not to be found in the typology and characteristics of the product or service exchanged. That is, the term “business” does not refer to the typology of goods exchanged, but rather to the nature of the business actors (Fiocca, Snehota, & Tunisini, 2009). Thus, it is not the product or service exchanged that gives business markets their distinctive characteristics; rather, it is the behavior of customers and suppliers that gives business markets their peculiar features. But before we explore the major issues that characterize business markets, namely the buying behavior and nature of the multiple interactions that precede and follow the purchasing event, we review the most readily visible distinctive features. The purchased volume is one of the main elements that distinguishes business markets from consumer markets. Business markets considerably exceed the transaction volume of consumer markets (Hutt & Speh, 2012). Individual business clients can account for a considerable level of purchasing in relation to the buying volume of consumers in consumer markets (Håkansson & Snehota, 1995; Wynstra, 1999). Another element that differentiates business markets is the concentration of sales both in geographical terms and in relation to the number of customers. The turnover of a company operating in a business market commonly depends on a small number of buyers. Thanks to studies conducted for over 20 years, it is now recognized that often more than 60% of the volumes of sales of many

business companies depend on no more than 10 customers (Håkansson, 1989). This means that for each company there is a relatively small number of exchange relationships that become central and critical (Fiocca et al., 2009). A similar concentration exists on the purchasing side and for most companies the ten major suppliers in terms of value represent a major portion of the spending on purchasing. Business and consumer markets are also distinct in other aspects, such as market demand. Demand in business markets has specific features and poses distinctive challenges. Business market demand is derived and fluctuating (Kotler & Armstrong, 2010; Hutt & Speh, 2012). The demand for industrial products or services is strongly linked to the demand coming from the consumer market. The demand for industrial products or services is more or less directly derived from the demand of the consumer market. Another feature that characterizes industrial demand is its fluctuating nature. With respect to the demand for consumer products, in business markets the demand for many industrial products and services tends to fluctuate more. This situation is attributable to adjustments business actors make in response to the variation of end user demand adjusting the level of stock, which produces the multiplier effect. Industrial demand, in fact, reacts significantly even to a small variation in final demand. But it must also be considered that, beyond the demand expressed by final customers, there are other elements that affect demand of the industrial manufacturer. Among these elements it is necessary to include the features and evolution of competition and technology in customer-belonging sectors; variations of demand expressed by business customers are not generated only as a result of final consumer demand, but are also influenced by the competitive position of the business customer as well as by the evolution of technology and how it is managed by business companies (Guatri, Vicari & Fiocca, 1999).

The distinctiveness of the business-to-business market reflects the nature of buying businesses, which are organizations and not specific individuals, and the manner in which they purchase and employ the product or service bought. In business markets the customer usually purchases products or services for the purpose of sustaining its own operations. Businesses usually re-elaborate the purchased good or item before selling it to their customers. Business customers purchase industrial goods to incorporate them,

transform them, use them in their production processes, or even re-sell them. The importance of the business-to-business market is incontestable; however, this significant reality of the necessary transformation of primary resources into products often seems to be less visible in some way than the market in which we are all the final consumers, who daily buy what we need and sometimes sell what others need.

Being less visible – also for marketing and management scholars – does not mean business markets are not of economic importance. What consumers buy are the end products of multiple business activities. Each purchase the final consumer makes is the result of a massive arrangement of business activities that are not easy to perceive and are carried out by many companies, often unfamiliar to us. There would be no goods or services for final consumers without business production processes and firms' interactions that permanently precede the commercialization of a product or service. It is through these continuous relationships between customers and suppliers that products and services are designed, developed, produced, combined, delivered, bought, and sold (Anderson, Håkansson, & Johanson, 1994). A number of individuals are likely to be involved in a business exchange; this may be from a different number of functions, such as marketing, finance, or purchasing. The great number of individuals involved means that business purchases are more complex than those in consumer markets (Håkansson & Snehota, 1995). Therefore, given the high number of actors involved, buying behavior and buying patterns differ significantly between the business market and consumer market. In the literature, business buying is usually presented as a multi-stage process, influenced by a multitude of internal and external forces. It is assumed that at each stage of the buying process the buying business has to deal with several alternative solutions that are ultimately turned into the final choice of the right supplier (Hutt & Speh, 2012, pp. 55-84). Yet, the phases presented in different models of the purchasing process do not always progress sequentially. Indeed, the phases may vary depending on the complexity of the goods exchanged and of the distinct business production processes. Attempts to model the process of business buyer behavior can be found in many studies (Sheth, 1973; Nicosia & Wind, 1977; Johnston & Bonoma, 1981; Ward & Webster, 1991; Johnston & Lewin, 1996). However, the selection of the supplier is not the end-

point of the business buying process for the final consumer markets (Axelsson & Wynstra, 2002). Some studies suggest the buying process in business markets is usually a long-term process, characterized by the repetition of purchases, and suppliers prefer to develop close and lasting relationships with customers. It appears that a further distinctive feature of business markets – in contrast to consumer markets where purchases are considered isolated events – is that business buyers and sellers tend to have continuous, long-term relationships with their partners (Håkansson & Snehota, 1995; Håkansson et al., 2009).

So far we have distinguished two types of marketplaces, consumer markets and business markets, and briefly illustrated the main features of the latter. The purchased volumes, the concentration of sales, the derived nature of industrial demand, and its tendency to fluctuate are the major factors that distinguish the business market from the consumer market. However, there are other business market peculiarities that are less obvious and somewhat ignored. We refer to the business market specificities that can be traced back to the nature of buyers and sellers, which are not single persons but organizations, and the way they will buy and use the product or service bought. It is the behavior of customers and suppliers, characterized by multiple transactions that precede and follow the purchasing event, that gives the business market its peculiar features. What the characteristics of business markets suggest is a need to take a very different approach to the analysis of business markets than that usually adopted for consumer markets.

Having reviewed the business-to-business market peculiarities, in the next paragraph we will briefly clarify the meaning we intend to give to the concept of business networks.

## 4.2 SOCIAL NETWORK AND BUSINESS NETWORK PERSPECTIVES

At this point, it becomes necessary to clarify the meaning we give to the concept of business networks, particularly since the recent literature on entrepreneurship often

suggests new business venturing and networking are closely interrelated (Jack, 2010; Slotte-Kock & Coviello, 2010)

Analysis of social networks has become a very popular topic in organizational and entrepreneurial studies (Hite, 2005; Anderson, Drakopoulou-Dodd, & Jack, 2010). In particular, entrepreneurship research studies and considers the importance of social networks in new business development (e.g., Hoang & Antoncic, 2003; Greve & Salaff, 2003; Davidsson & Honig, 2003). The social networks perspective builds on the premise that business success does not depend on the characteristics of the entrepreneur but rather on his/her social network, such as family, friends or colleagues that can provide financial support, knowledge, contact to potential people, and also other kinds of emotional support, such as understanding and reassurance.

Other theoretical contributions, related to applications of the theory of social networks, such as the interpretive models introduced by Naphiet & Ghoshal (1998), Liao & Welsch (2005), and Abell, Crouchley, & Millis (2001), provide an original reading of the networks of relationships and of the sources and diffusion of this form of capital with reference to the processes of creating new businesses. These studies have focused on the relation between social networks, understood as social capital, and the development and genesis of entrepreneurship. Naphiet & Ghoshal (1998) define social capital as the sum of current and potential resources derived from a network of relationships and of relationships possessed by the entrepreneurs (network ties or set of relations and relationships) and thus as a significant resource for entrepreneurial action. Like other forms of capital, such as finance, materials, and humans (Simoni & Labory, 2006) it can allow access to material resources and assets not otherwise obtainable. The access to these networks can, therefore, be positively related to the formation of new businesses and their ability to achieve good performance in the early years of life (Aldrich & Zimmer, 1986, Hansen, 1995; Greve, 1995) by legitimizing, encouraging, and stimulating the processes of new entrepreneurship on the one hand, and by facilitating access to resources and information critical to the success of a new business, on the other.

We agree that every business venture may be influenced by social relationships (Young, 1998), but we refer to a different phenomenon when we talk about business networks. The social network concept is certainly interesting, but refers mostly to the interpersonal aspect. When we talk about business networks we refer to networks of business relationships among organizations. The critical aspects in the development of a new business are not traceable to the social relations of the individual entrepreneur. These explanations are inconsistent with those who criticize the theories of the self-made man. That attributes too much importance to individual talent and intelligence. In reality, it is essential to be the right person at the right place at the right time (Hargadon, 2003; Gladwell, 2009). The view expressed in such studies shakes one of the most deeply rooted beliefs in contemporary society, which is the myth of the self-made man, the man who comes over only thanks to his virtues and forces. Similarly, Taleb (2007) tends to dismount these self-limiting beliefs, the de-facto rationalism of the self-made man. In our business culture there is little space for those people who do not give visible results, instead, we tend to be more concentrated about the processes that ensure lasting results. In business organizations it is typical to reward those who acquire lots of new customers, not those who have created a process to efficiently manage sales channels or after-sales assistance (Taleb, 2007). Today, there are many who believe social success is only partly explained by personal characteristics and skills, but that is rather better explained, to a large extent, by the context (Welter, 2011).

The concept of an interorganizational network, that is, the context of reference of any business, is referred to as the network of business relationships between business organizations. The social network perspective focuses on interpersonal relationships and their role in the development of new businesses. When we talk about business networks, we talk about interorganizational relationships and the role they play in the process of new business formation.

To conclude, looking at the market as a network in which a new business emerges as a node into the wider existing network of business relationships and business entities has implications for developing new business relationships and for new business formation.

### 4.3 MARKET AS A NETWORK: IMPLICATIONS FOR NEW BUSINESS DEVELOPMENT

The aim of this chapter is to understand the context of “business markets” and how such a context affects critical issues in new business formation. What has been reported in past research as distinctive features of business markets, therefore, is the starting point from which we opened the discussion.

We have seen that in order to understand business market dynamics, several different approaches have tried to investigate and conceptualize what a market is and how it works, and to identify the mechanisms underpinning the evolution of markets. According to our review, the different perspectives can be linked to three main fields of research: the economic, the neoclassical and Austrian schools of thought, socioeconomic markets theories, and marketing theories. We have seen that although the core argument in the neo-classic economic perspective is widely accepted, it does not adequately explain some of the features of business markets evidenced in the research on business markets and marketing in general. We have also reviewed what has been reported in two other long-standing research traditions of alternative conceptualizing of business markets – the Austrian school of economics and socioeconomic perspectives – that propose different views on how markets work and what the central market processes are. What these market conceptualizations have in common is that they acknowledge that markets are characterized by the presence of interdependencies and relationships between the market actors and the need to go beyond discrete exchange transactions in explaining market dynamics.

In the marketing field, in particular, various market functioning theories have been proposed, shifting the interest from internal factors, such as the organization, to external factors such as external resources and the condition of the business (Stuart & Sorenson, 2007; Sarasvathy, Dew, & Ventresca, 2009). We found that within the marketing research, particularly that concerning relationship marketing, there is a considerable body of research that proposes influential conceptual frameworks that take

relational perspectives (Håkansson et al., 2009). Research on business markets, inspired by the IMP research stream, evidenced three aspects of business markets that appear relevant to the topic of our interest: 1) the existence of continuous and long-lasting business relationships in which product is a variable; 2) interdependencies between the actors involved reflecting that firms are embedded in a network of relationships; 3) the role played by continuous interaction processes between the parties involved.

There is substantial evidence that some of the typical features of business networks bear on new business formation. The first market feature recurrent in the IMP research emphasizes the existence of interdependencies between businesses and reflects the conviction that firms are embedded in a network of a complex set of relationships each company has with other companies (Håkansson & Snehota, 1995). Business relationships have important implications not only for the businesses directly involved but also for those indirectly involved (Björk & Magnusson, 2009; Rampersad, Quester, & Troshani, 2010). Clearly, being part of a wider network, any business has to manage several relationships with customers or suppliers, which in turn have other relationships with other business organizations (Anderson, Håkansson, & Johanson, 1994). What happens in one business relationship is influenced by what happens in related business relationships and influences what happens in other relationships. The idea is that new relationships that develop between business actors are influenced by, and exert an influence on, relationships that they already have with third parties. What follows is that every single business relationship is embedded into a complex network of business relationships and that the set of business relationships has important impacts on entrepreneurial outcomes (Hoang & Antoncic, 2003; Johanson & Vahlne, 2011). Several studies have shown that business relationships have a considerable impact on the overall performance of the businesses involved (e.g. Bowman & Narayandas, 2004; Ford et al., 2006; Baraldi, 2008; Håkansson et al., 2009). There has also been a growing recognition of the implications that business interdependencies may play in new business formation (Ford et al., 2005; Lechner, Dowling, & Welppe, 2006; Stuart & Sorenson, 2007; Sarasvathy et al., 2009).

Interdependencies as a dominant feature of the business-to-business market have

three implications for studying and conceptualizing new business formation. Firstly, they imply that every new business must develop new business relationships, which involves interaction between the parties. Secondly, they imply that every emergent business venture builds on the pre-existing business network. Hence, every new business has to develop new business relationships with customers and suppliers when entering a new business network; this suggests every new business can be seen as a new node that has to merge with a pre-existing network of business relationships. And, last but not least, there is another important implication due to the feature of the business markets highlighted in the IMP research: whatever happens between companies, in terms of development of business relationships, amounts to organizing of the business market (Håkansson & Snehota, 1995; Anderson, Narus, & Narayandas, 2008). Changes in an existing business relationship or the development of a new one affects relationships with other businesses and shapes relationships through the network. For example, if a European company develops business relationships with a new Chinese customer and finds a new supplier in Indonesia, it connects previously unconnected actors and redefines the organization of the business market system. In other words, any change or development in business relationships amounts to changes in the market structure and is part of the process of structuring and organizing the business network from within.

Our literature review suggests that new business formation involves the development of new relationships, or change in existing business relationships (Håkansson, 1989; Dubois, 1998; Waluszewski, 2004; Cantù & Corsaro, 2011; Andersson et al., 2011). Hence, the network's evolution is related to how new relationships are developed, and this evolution reflects the way business organizations develop business relationships. Therefore, the merging process of a new entity in the pre-existing business network implies that every new business builds on it and modifies it. Formation of new business ventures will thus have organizing effects in the market (Sarasvathy, Dew, & Ventresca, 2009; Ciabuschi, Perna, & Snehota, 2011). According to Ingemansson & Waluszewski (2009), understanding how organizing the business network will be influenced by the development of the new business can be useful in clarifying and explaining the formation pattern of a new business. This aspect of

*“business development as an organizing process”* is relevant in new business formation in one main aspect: studying the formation of a new business requires not being isolated from its context (Welter, 2011). The unpredictability of market reorganization, the consequences of this continuous network motion, and the evolutionary effect on all businesses is evident if we view successful new business development as becoming a “new connected node” of business relationship in a pre-existing network.

#### 4.4 WRAPPING IT UP

To conclude, the market-as-network conceptualization has highlighted some market features we believe can help us to better understand the reasons why new business formation is so uncertain and complicated. As has been shown, there is a close dependence between a business's ability to develop and maintain stable relationships with other companies and its survival (Hoang & Antoncic, 2003; Ford et al., 2005; Lechner, Dowling, & Welppe, 2006; Stuart & Sorenson, 2007; Sarasvathy et al., 2009; Johanson & Vahlne, 2011). The market-as-network perspective also provides a point for reflection on the activities of “networking.” The picture of the “market as a network,” where markets are seen as complex networks of relationships resulting from collective entrepreneurial activities (Sarasvathy & Venkataraman, 2011), suggests that the development of new business entails merging in a pre-established business network, and the need to develop multiple relationships to become connected with, and to make use of, other economic organizations. What we infer is that this merging process on the pre-existing network and the development of new business relationships is the critical point of the development of a new business. In other words, we are inclined to assume, not surprisingly for practitioners, that the critical task in the development of a new venture is to establish, develop, and maintain new business relationships with customers and suppliers. The interaction processes underlying business relationship development thus appear crucial to the new business development process. Therefore, in the next chapter we will review different research streams that examine business relationships as a phenomenon critical to business market processes and dynamics. We will further extend

our discussion to cover some of the issues involved in analyzing business relationships as these emerge in the IMP research tradition.

## Chapter 5

# Developing New Business Relationships

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In Chapter 4, in tracing the ideas of different streams of research on business markets, we discussed the distinctive features of business markets. What has come to the fore is that the business network perspective on business markets, widely accepted in the marketing literature, has evidenced some features that describe and qualify the context structure under which businesses operate as a network of interdependent and interconnected business relationships that are relevant for market actors and that can bear on the development of new ventures. In particular, research in this stream suggests that given the characteristics of business-to-business markets, businesses cannot be viewed as entities that are built up and operated in isolation. Rather, if we accept the idea of the market as a network-like structure, then each firm appears to be a node in the network of business relationships. Looking at a business as a node in the network of relationships has two consequences for our research question. Firstly, this means that starting a new business – as it acquires an organizational configuration and performs commercial activities – becomes a new node in the pre-existing business network. Consequently, as the new node becomes merged, the existing network will not maintain the same configuration, but its structure will change. Secondly, when a new business becomes part of the network as a new node, it becomes involved with developing new relationships. This means that to merge with the network, every new business must develop a set of new business relationships.

Since the recent entrepreneurship research appears to acknowledge that the interplay between a new venture and its context is particularly complex (Davidsson, 2003; Lechner et al., 2006; Stuart & Sorenson, 2007; Sarasvathy et al., 2009; Jack, 2010; Welter, 2011), in this chapter we will firstly review different research streams that look at business relationships as phenomena critical to explanations of business market processes and dynamics. In discussing some of the issues involved in analyzing business relationships, we will argue that a suitable perspective for guiding the analysis of, and reflection on, the formation of new business relationships seems to be one of the IMP research tradition. We will present the ARA model, developed by the IMP stream of research (Håkansson & Snehota, 1995) as a tool for describing and analyzing business relationships. According to this model, business relationships can be analyzed starting from the interaction at the three layers that characterize the content of the relationships: actors, resources, and activities (ARA) that are equally important in building and developing business relationships. The focus on the peculiarities underlying the content of business relationships will mark the importance of the interaction processes for developing new businesses in business markets (Håkansson et al., 2009). We will further extend our discussion, towards the variables that impact the outcomes of a business relationship. We will finally argue that the development of a new business, its formation and its growth, is enabled and constrained by the way in which the parties involved in developing a business relationship interface resources, configure activity flows, and negotiate the meanings of the actors involved.

Our final consideration will be that the development of new business relationships requires the involvement of others and extensive interactions in business relationships necessary to create workable business solutions, which means that new business development cannot be achieved by unilateral action but is to be intended as a collective process. We will conclusively argue that the network perspective that suggests new venturing is mainly a process of plugging the new venture into a pre-existing context provides a better explanation of the issues critical in developing a new business. We will conclude this chapter by presenting four propositions that guide our empirical investigation.

## 5.1 SETTING THE SCENE

In the previous chapter we have seen that companies operate in a network context where relationships have an influence on the relationships themselves, on the companies' involved, and on the entire network (Anderson et al., 1994; Björk & Magnusson, 2009; Rampersad, Quester, & Troshani, 2010). The existence of business relationships, interdependencies, and interaction, and the fact that businesses are embedded as customers and suppliers in a limited number of business relationships with other businesses, has led to framing the context as a business network (Håkansson & Snehota, 1995). The relationships serve to access resources held by others and to make use of activities already carried out by the other actors. From this perspective on a new venture it is clear it cannot be isolated from the context and development of business relationships with customers and suppliers, which are the means to get connected with the pre-existing network (Hoang & Antoncic, 2003; Johanson & Vahlne, 2011). All new businesses need to involve existing supply chains to provide external resources critical to starting up; they also need to deliver to customers that are other businesses (Håkansson, Ford, Gadde, Snehota, & Waluszewski, 2009).

As we have seen in the previous chapter, the multitude of business relationships is always in a state of change and appears intrinsically complex because of the continuous adjustments that occur in the relationships (Andersson et al., 2011). Business relationships are characterized by varying degrees of complexity, depending on the product or service exchanged. Business exchanges are not characterized by a simple transaction in which the exchanged good is standard – as in the case of consumer markets where customers and suppliers usually handle predefined and known products or services – but the content exchanged in business relationships always tends to be complex (Hallén, Johanson, & Sayed-Mohamed, 1991; Ford et al., 2005). In the case of standard products, the relationships between buyers and sellers tend to be more linear, as the product exchanged does not require particular adaptation efforts. But this does not mean the product or service adjustment is not needed; rather, it is less visible but there are other dimensions of the relationship content that can be complex (e.g. logistics,

administrative routines, etc.). Business relationships are less linear and the exchange processes are more difficult and uncertain, not only because the product or service exchanged is constitutionally complex, but also because the products and services exchanged require adjustments in order to fit with the customers' specific needs (Tuli, Kohli, & Bharadwaj, 2007; Vargo & Lusch, 2008; Aaboen, Dubois, & Lind, 2012). Since business customers use products or services in different ways and re-elaborate them before selling them or integrating them in their production processes, they may require some adaptations of the standard product or service offered to meet their specific requirements (Hallen et al., 1991).

Hence, different customers can buy the same product or service for quite different reasons and have different views of the same product or service offered, and will only be concerned with how effective the offering is as a solution to their problems. Reasonably, customers are not interested only in the products or services exchanged, but also in other aspects such as the way the logistical, financial, commercial, and administrative activities and other managerial arrangements are worked out (Tuli, Kohli, & Bharadwaj, 2007; Ciabuschi, Perna, & Snehota, 2011). To ensure the adaptation of the product or service to the needs of the specific buyer, close cooperation between the buyer and supplier and a high degree of collaboration between different business functions of both companies is usually required (Anderson, Håkansson, & Johanson, 1994). What follows is that the exchanged product or service is not the sole determining aspect that makes the development of a business relationship a complex task. The difficulty in developing relationships thus depends on the nature of the product or service exchanged and on the distinctive features of the counterparties involved, by the way they connect their performed activities, and by the way they combine the resources they control (Harrison & Waluszewski, 2008).

These are the network effects: relationships develop in order to meet each other's companies' requirements and to link their resources and skills to solve their problems and generate new business solutions. What this implies for our research is that in order to have a better understanding of the complexity and difficulty of the issue concerning

the development of new business relationships in the relevant network we need to take as the unit of analysis the new business relationships and not only one of the parties.

## 5.2 DEVELOPING NEW BUSINESS RELATIONSHIPS

We have already seen that the content of business relationships is complex. There is much more than the exchange of products going on between buyers and sellers: working out the right business solutions encompasses organizing for the transaction, which means that many different product features and organizational units need to be adapted and adjusted for those involved in doing business.

Typically, a start-up comes with a business solution that is novel for the market and its actors. These business solutions are not made inside a single new venture, but are often designed, built, and arranged between networked companies. Indeed, it is through continuous adjustments and changes in relationships among businesses that new business solutions, products, and services are conceived and developed. There is a connection between new business development and new business solutions: introducing new solutions requires developing business relationships (Ciabuschi, Perna, & Snehota, 2011; Aaboen, Dubois, & Lind, 2011), and new solutions often emerge in relationships.

Developing a new business relationship with others in a given network context, however, includes connecting complex activity chains already in place, interfacing various existing resources, and relating to several actors (Ford et al., 2005). The implications of this relational context for new business development are far reaching. On the one hand, it explains why new businesses need grafting onto the pre-existing context; on the other hand, it explains why new ventures inevitably need to start developing complex relationships and connections among customers and suppliers of the network. Any new business will have to develop and establish business relationships with a variety of entities and activities (Håkansson & Olsen, 2012). New business survival and prosperity is dependent on its relation to, and interaction with, others. We cannot explain the failure or success of a new company simply by examining the features of one entity. Instead, as suggested by extensive empirical research, we need to look at

the complex matching of the two entities and on the mutual impact of one on the assets of others (Ingemasson & Waluszewski, 2009; Waluszewski et al., 2009; Baraldi, 2008; Bernardi, Boffi, & Snehota, 2011). Consequently, the unit of analysis cannot simply be the features of the new business. Indeed, if we aim to explain why businesses fail or succeed, we need to look at the content and at the nature of the interplay between the actors in developing a business relationship. Given that we adopt this perspective, we need richer conceptualizations of how to describe, analyze, and categorize the interplay between the new business and the context.

### 5.3 ANALYZING BUSINESS RELATIONSHIPS

Since the main thrust of this study is the development of business relationships and how these are relevant for the development of any business activity, we need to find a framework that helps us to analyze and understand the processes involved in developing new businesses relationships. That is, recognizing that business relationships are broad in scope, have various significant consequences for the businesses involved, and are quite complex in content, an analysis of the critical process underlying the development of business relationships requires the development of concepts that can capture the complexity of their content.

#### 5.3.1 RELATIONSHIPS IN MARKETS

Currently, the relevance of business relationships for market dynamics and for business market participants appears to be widely acknowledged in the marketing literature (Palmatier et al., 2006; Tuli, Kohli, & Bharadwaj, 2007; Johanson & Vahlne, 2011).

While the idea that business relationships are critical for both customers and suppliers in achieving economic efficiency and for the development and innovation of any business has entered the mainstream of the marketing literature in general, the first systematic empirical studies that explored the buyer-seller relational processes in greater

depth come from business-to-business marketing (cfr. Chapter 4 paragraph 4.1.4.1). Actually, this interest in exploring the relational processes in business markets is not noticeable only in business relationship literature. The issue of analyzing relationship formation has also achieved prominence in the service-marketing field (Vargo & Lusch, 2004; Grönroos, 2007a; Payne et al., 2009). The two research fields have in common a focus on the interaction processes that occur in relationships and influence the outcomes of these processes for the parties (Grönroos & Ravald, 2011). However, most of the research that investigates relationships commonly tends to study the antecedents and results of relationships between existing and ongoing businesses, rather than focusing on the process underlying the development of new relationships in the market.

In the classical economic perspective, the behavior of the parties involved in the exchange is seen as a function of parameters that characterize the transaction, which are typically identified in terms of product/service and price. Thus, market relationships are intended as consequent to the objects of the exchange and not vice-versa, as in the network approach. However, buying and selling organizations seldom have full *a priori* knowledge of what product-solution will be exchanged. They develop relationships not just to allow the exchange of particular products or services, but also to identify, develop, and then exchange specific solutions. Thus, the effects, positive or negative, that business relationships have on the actors involved are not given simply from the item exchanged but rather result from the consequences of the interaction. In this sense, the traditional view that assumes relationships are established on the basis of what the actors have or need, contrasts with the idea that the actors know they have a problem and that because of this, develop a relationship to obtain solutions to their problems.

Since this thesis is interested in the processes underlying the development of new business relationships between businesses and other organizations, we will explore what has been suggested in the business-to-business marketing literature as the critical process underlying this process. As we will see in the next paragraph, this need is met by using the ARA model, which will help us to systematically approach the empirical study of business relationships and find a way to analyze the interaction processes involved.

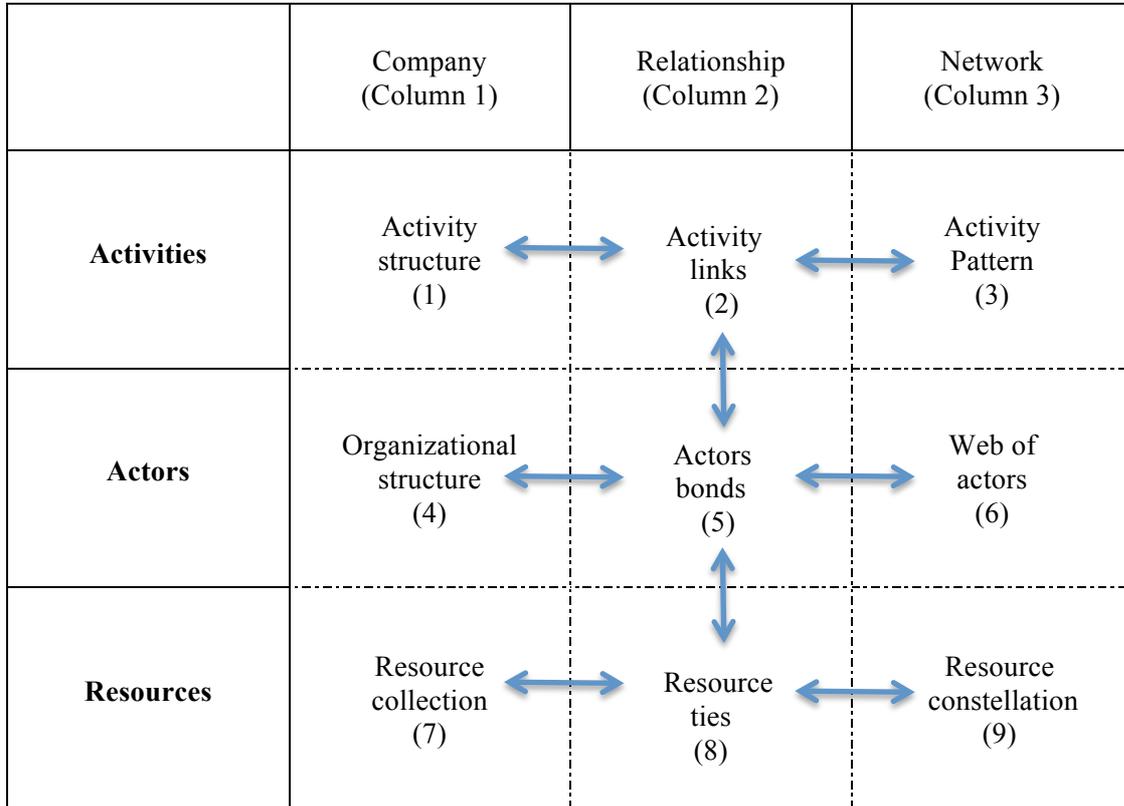
### 5.3.2 FRAMEWORK FOR ANALYZING BUSINESS RELATIONSHIPS

Several studies on business relationships have produced empirical evidence, particularly in the marketing literature; these studies have proposed various conceptualizations, assumptions, and theories of how business relationships work (Håkansson & Snehota, 1995). The IMP (Industrial Marketing and Purchasing group) research tradition, in particular, has concentrated on the study of factors that govern business relationships (Håkansson & Wootz, 1979; Håkansson, 1987; Ford, 1997). Studies in this tradition have proposed the ARA model to deal with the analysis of buyer-seller relationships in industrial markets.

#### 5.3.2.1 THE ARA MODEL

The ARA model, proposed by the IMP research tradition, provides a framework for describing and analyzing the content of business relationships (Håkansson & Johansson, 1992; Håkansson & Snehota, 1995; Håkansson et al., 2009). The ARA model distinguishes three layers of interaction that characterize the content of business relationships: Actors, Activities, and Resources, layers that are equally important in building exchange relationships and are closely interrelated. The three layers of content of business relationships are illustrated in Figure 5.1.

Figure 5.1 Scheme of analysis of development effects of business relationships



(Source: Håkansson & Snehota, 1995; p. 45)

*The activity layer* in a relationship refers to connections among the various activities of the two firms that are parties to the relationship. Every organization is characterized by activity structures such as production, transportation, and delivery processes of a product that are connected in a relationship. When two companies interact, the activities of the two counterparts must be synchronized (for instance their systems of production and distribution). Depending on the current activities' conditions of the existing organizations, a series of adjustments and adaptations is likely to be needed in order to find acceptable activity synchronization. This means that specific activities, such as production, logistics, and distribution, need to be connected and coordinated in

specific ways. Activity links describe these connections between different activity systems; in particular they describe those operations carried out within and between firms in networks, and how activities are coordinated between the actors involved in a relationship. This coordination of different activities has consequences for the economic outcomes (Dubois, 1998; Gadde & Håkansson, 2001).

*The resource layer* refers to how resources of the two companies are connected. Resource ties develop as companies exchange or access each other's resources, which can be physical, human, or financial, in carrying out their activities. In particular, any tangible resources, such as plant equipment or physical components, or intangible resources, such as knowledge and experience, have no value if they are not used in combination with other resources; thus, their value depends on their connection with others. That is, resource value depends on the ability of businesses to combine them with each other and to use them efficiently.

Each solution, and especially any new business, requires combining numerous resource elements that need to be interfaced. When these resources are not compatible a problem arises of how to match them and make them useful. This means both parties need to create, among the various elements of the resources, specific resource interfaces (Baraldi, 2008; Harrison, & Waluszewski, 2008).

Interfacing resources requires adaptations that have implications in terms of costs and time invested for all the actors involved. That is, besides the benefits of resource ties, such as cost efficiency and the creation of new resource combinations, other economic consequences are to be linked to the cost of resource interfacing and adaptation processes.

*The actor layer* refers to the ties between the various actors, individual or organizational, involved in the relationship, who manage business activities and control resources. Resources become the means through which the actors perform their activities, i.e. those processes put in place to transform resources (Håkansson, 1987). Bonds between the actors are thus a prerequisite for the development of resource ties and activity links. Actors' bonds require trust, commitment, and some degree of shared meaning that influence the way the counterparts involved perceive and conceive

problems and new solutions and perform their activities and use resources (Håkansson & Johansson, 2001). Actors' bonds between two business organizations are necessary in order to develop a mutual orientation about how to connect and coordinate activity links and combine resources. Actors' bonds affect the way in which actors see and interpret different situations, as well as their identities in relation to each other and to third parties (Axelsson & Wynstra, 2002; Welch & Wilkinson, 2002).

It is through their perceptions of each other, their responses and their mutual trust and understanding that these bonds arise over time. Identity attribution and mutual trust between the counterparts are usually made from elaboration of previous experiences. That means that when a business relationship develops, businesses become mutually oriented; they start dealing with each other on the basis of some assumed identity of the counterpart (Håkansson & Snehota, 1995; La Rocca, 2011).

The idea of the ARA model is that the three layers of business relationships – activities, resources, and actors – are interdependent and not only have implications within the businesses themselves but also within their other relationships: “Activity links may limit or facilitate resource adaptations; resource ties may limit or favor the possibility of activity co-ordination and actor bonds may open up the possibility of developing activity links and resource ties” (Håkansson et al., 2009, p. 34). These three dimensions of interaction in business relationships and networks have been the subject of several studies showing that what matters for the actor's layer of interaction is the negotiation and production of meaning, i.e. of what the actors represent for each other. What matters for the resource layer of interactions is the interfacing processes so that resources can be connected and combined; what matters for the activities layer of interaction is the way they are configured so they can be coordinated.

These findings appear relevant to new business formation since they have been the point of departure of several studies on how the activity, resource, and actor dimensions impact new business formation (e.g. Aaboen, Dubois, & Lind, 2011; Mele, Spina, & Colurcio, 2010; Ciabuschi, Perna, & Snehota, 2011). We will rely on this model since it has proven to be a useful “tool” for observing and analyzing business relationships. We believe that analyzing the three layers of business relationships can

help us gain more insights about the implications for the new venture that has to develop new business relationships. How the emergent business will develop depends on the way in which the parties involved in developing a business relationship interface existing resources, configure ongoing activities, and create new shared meanings. Hence, every new business relationship involves connecting to new networks of activities, new networks of resources, and new networks of actors. These are the three processes that seem to evolve; new businesses always need to merge with something that existed before them.

Given the functions of business relationships, namely the important consequences for the business directly involved and for those indirectly involved, an interesting aspect would be to understand the numerous and frequent adaptations that stem from the need to modify, more or less continuously, products or services exchanged as well as the administrative and logistic routines and procedures in order to coordinate the individual activities within the relationship. We believe that by following this perspective it is possible to investigate different aspects of the observed processes and describe and analyze them more systematically.

In the next paragraph we will dedicate particular attention to how business relationships develop between customers and suppliers and how the interaction processes affect the development of business relationships.

#### 5.4 BUSINESS RELATIONSHIP DYNAMICS

The complexity of the product or service exchanged in business markets justifies the presence of more complex forms of interaction (Mason, 2011). That is, in industrial markets, where the product or service offering is often complex and customized, the business relationship involves complex interaction processes as the parties involved need to interact extensively in order to learn how to adjust, integrate, and implement the product or service exchanged in their ongoing activities (Ahuja, 2000; Håkansson et al., 2009). Business relationships contain frequent interaction and information exchange between the actors involved in which they learn about each other and match their

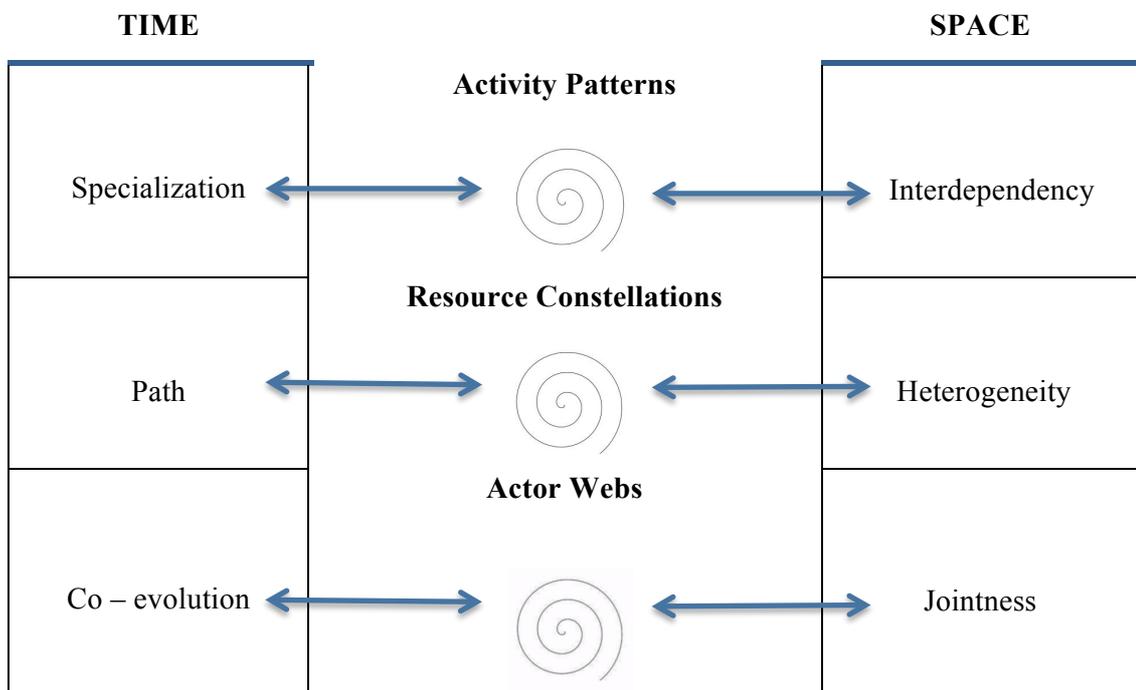
business solutions to each other's specific requests (Hallén, Johanson, & Seyed-Mohamed, 1991). Under such circumstances, the exchanged products, services, or processes tend to undergo continuous adjustments and adaptations of many aspects in order to become business solutions for customers. Businesses usually do not offer "a ready-made" solution to their customers; rather, businesses are active in defining and renewing existing solutions or generating new ones by interacting. It has been shown that it is in-between businesses that major innovative business solutions, in terms of products, services, and processes originate (Von Hippel, 1986), and that as a consequence, new businesses will have to cope with these mechanisms (Shane, 2001; Rampersad, Quester, & Troshani, 2010). Recent research has recognized that developing a new solution is a collaborative activity that requires the involvement of multiple actors who interact through complex relationships (Anderson & Lilliecreutz, 2003; Roy, Sivakumar, & Wilkinson, 2004; Cantù, Corsaro, & Snehota, 2011). These findings suggest that the involvement of actors external to the new venture, such as suppliers and customers, is a way of finding out and developing new business solutions in interaction. It has also been observed that the higher interaction levels are, the more likely it will be that the two businesses will share resources, information, knowledge, and other types of tangible and intangible resources (Perks, 2000; Roy, Sivakumar, & Wilkinson, 2004). That is, the potential to generate new solutions increases particularly when there is an extended level of interaction between customers, suppliers, and other intermediaries (Ahuja, 2000; Håkansson et al., 2009). This implies that the solution a new business offers cannot be conceptualized and realized in abstraction from the environment but has to become arranged and connected with activities in the delivery and supply chains, with the resources others possess, and this also requires integrating knowledge and ideas from different fields (Håkansson & Waluszewski, 2007).

Evidence that interaction processes are central to business relationships – in particular to relationship development for parties involved directly or indirectly, and for the evolution of the business network – has emerged from extensive empirical studies (Håkansson, 1982; Håkansson & Snehota, 1995; Ford et al., 2006; Håkansson et al., 2009). As we have seen, The IMP research tradition has put special emphasis on

analyzing customer-supplier interaction (Ford & Håkansson, 2006) and has been reiterated as “central,” specifically in a recent contribution by Håkansson et al., that defines business interaction as: “an important economic process through which all of the aspects of a business, including physical, financial, and human resources, take their form, are changed and are transformed” (2009, p. 33).

In fact, starting from the so-called ARA model, IMP scholars emphasize current developments and suggest that the interaction between actors in the network and the main issues involved can be traced to one or more of the quadrants illustrated in Figure 5.2. What this model attempts to capture is the time and space dimension of the interaction processes in business relationships and their consequences both at the level of the businesses involved and at the network level.

Figure 5.2 A model of the interaction process



(Source: Håkansson et al., 2009, p. 41)

*Interdependency of activity patterns* means that through interactions businesses coordinate various activities of different businesses, and thereby achieve greater efficiency. The interdependencies between the activities a company develops by and the activities other organizations develop are the result of past interactions. Interaction activities become interdependent from a spatial point of view (dependent on other activities), and over time the activity patterns change in terms of the specialization involved.

*Heterogeneity of resources constellation* means that different resources are combined and the new resources' characteristics are formed through conjoint adjustment and adaptation from both parties involved in the relationship. The resources provided and used are the result of how heterogeneous resources are matched, interfaced, and adapted over time. An important consequence is that resources (physical or intangible) are not given *a priori*, but their features are created in interaction with the context in which they are embedded. In fact, the idea of path dependency indicates that the development of a resource is affected by the interaction in which the resource is used. This representation reinforces the idea of how resources are actually defined by the interaction process between customers and suppliers.

*Jointness of actors* refers to the fact that the combination of resources and coordination of activities requires that the actors interact selectively with each other, and interacting actors become joint in space and co-evolve over time. Jointness of actors implies that actors in a relationship need to teach each other about their own resources and activities, and need to learn from each other's. Through interaction actors develop jointness and lay the foundations for the enactment of the adaptation and coordination processes. However, jointness of actors refers to more than activity interdependency and resource combination. It involves trust and commitment and has some effects on the actors' autonomy and involves reduced weight of the intentions and actions of the single actor.

Combining previously unconnected resources, connecting to activities carried out by others, and integrating others' knowledge, requires a series of mutual adaptations and the creation of workable interfaces among the various parties involved. That makes

developing a relationship a complex process, because adjustments are made in conjunction with all the actors involved, finding workable solutions at the three layers of interaction in business relationships. Consequently, intense interaction between customers and suppliers seems crucial, since it reduces the complexity and enables the parties to reap benefits from each other. Such relationships become strategic for both players when there are open lines of interaction between multiple layers of the involved organizations (Håkansson et al., 2009). Following the logic of the interaction process model, a new business solution is to be considered as a result of the interplay between the actors in mobilizing resources and coordinating activities in a combination that caters to each actor's specific needs (Håkansson, 1987; Perks & Jeffery, 2006, Håkansson et al., 2009). Thus, new business solution development in a relationship cannot be considered a linear process, but is instead an evolutionary process that is the result of complex interactions taking place in business relationships involving many actors – such as the new business itself, its suppliers, and its customers – that continuously seek the right solutions (Baraldi & Strömsten, 2006; Tuli, Kohli, & Bharadwaj, 2007; Vargo & Lusch, 2008).

To conclude, what follows is that a fundamental aspect in business relationships is the interaction process between business actors, which does not involve simply the transfer of a “given” product; rather, the object of exchange becomes “a new solution” which, to a large extent, is enacted by the process of exchange itself, in which resources, activities, knowledge, and other skills of heterogeneous interacting actors are combined and adapted through collaborative commitments. This seems to be a complex issue in developing new business relationships. Also, the value consequences for both customer and supplier originate in various aspects of the solutions and arrangements applied in the relationship.

## 5.5 CONTEXTUALIZING NEW BUSINESS FORMATION

Adopting a network perspective highlights that the development of any business draws heavily on external resources from both suppliers and customers and that new solutions

come into being when buyers and sellers, by interacting in business relationships, exchange and adapt each other's resources and activities, information, and skills (Penrose, 1959; Hoang & Young, 2000; Håkansson & Waluszewski, 2002; Waluszewski & Wedin, 2003; Baraldi, 2003). Taking this perspective on business markets implies that the need to interact is what explains the presence of business relationships and the presence of business networks.

Since "The existence of business relationships is a condition for the very existence of a business and the role of interaction in relationship development and maintenance, a central process in new business formation appears to be the continuous enactment of solutions at various levels" (Snehota, 2011, p. 6), it seems that the development of a new business is not necessarily attributable to the merit of the individual entrepreneur, but rather because of the interplay of the actors involved. From the IMP perspective, it is clear business opportunities are collectively enacted and are the result of joint interactive behaviors of different inter-actors over time. Interaction between actors is the driving force in developing business relationships. This means the joint "actorship" between agents that represent the businesses involved is more critical than the intent of the single actor to start a successful new business. Therefore, in this perspective, what drives the development of a new business is the jointness of the business inter-actors. That implies a shift away from the assumption that the individual entrepreneur and the business are more or less autonomous actors.

Whereas, if we consider the basic traditional economic idea of the market, it is clear that market comprises a set of indistinct buyers and sellers of a given product that is conceived and produced by a firm and then adopted by others. Such a perspective tends to assume it is the exchanged product itself – its features compared to those of existing alternatives – which will determine the success of a new business (e.g. Rogers, 1962).

When we consider the market as a network of business relationships, then every company is unique. Companies that produce and sell apparently similar products or services will have different customers or suppliers, and the offering is likely to differ in its various components (e.g. logistical and administrative arrangements if not in product

/service specifications). In a business network every company is unique and has its own set of customers and suppliers. If we look at new business formation from the network perspective it becomes clear that the moment a new venture enters the market and connects to it to become a node, it will modify the form of the network. That is, the development of a new business involves developing new relationships through which the emergent venture merges into a pre-existing structure, and at the same time changes the pre-existing structure (Håkansson, 1989; Dubois, 1998; Waluszewski, 2004; Cantù & Corsaro, 2011; Andersson et al., 2011). This means that developing a new business has evident organizing effects on the network of business relationships. What all this implies is that new business formation processes should be examined from an inter-organizational perspective (Davidsson, 2003; Lechner et al., 2006; Stuart & Sorenson, 2007; Sarasvathy, Dew, & Ventresca, 2009; Jack, 2010; Welter, 2011). Therefore, because many studies suggest that new business formation is about collective enacting of change in the business network, if our research aims at understanding new business formation, we must focus on the interdependencies between the actors involved.

## 5.6 BENEFITS & COSTS

Business relationships bring about various benefits for new ventures (Sorensen & Stuart, 2000; Hoang & Antoncic, 2003; Johanson & Vahlne, 2011). Among the benefits of a recurrent relationship and its stabilization is that it can lead to lower costs for the research of new suppliers and customers, of lower organizational problems related to the maintenance of customers and suppliers, and of greater opportunities to improve the adaptation of resources and the coordination of activities between the parties (Baraldi & Strömsten, 2006; Håkansson et al., 2009; Aaboen, Dubois, & Lind, 2011; Ford et al., 2010; Ciabuschi et al., 2011).

A major benefit of being involved in a relationship is that the confrontation between the parties involved provides the impulse for the development of new business solutions (Roy, Sivakumar, & Wilkinson, 2004; Rampersad, Quester, & Troshani, 2010). According to Khalid (2002), sharing risks and costs for new solutions and process

expenditures appears to be another motivator for engaging in relationships. The capacity for mutual control and comparison over the progression of a business solution develops thanks to business relationships that provide the ground for the exchange of information and learning contents. That is, it is in these terms of exchange, of information and learning, that the relationship generates the capabilities of mutual control and comparison useful for the development of a new solution. The benefits a business relationship generates are a certain degree of mutuality, commitment and trust between the parties, as well as a series of rules and procedures, more or less implicit, which are formed and institutionalized as routines over time as mutual reciprocity is reinforced (Håkansson & Johansson, 1993). These routines are created, reinforced, and modified through communication processes that occur during the relationship. Hence, communication practices are an essential process through which the decisions about the type of adaptations of various technical, administrative, and commercial activities are made and through which routine collaborations and other activities are coordinated and formalized for mutual commitments. That is, the “routinizations” and formalizations that are usually critical for the cost efficiency of specific relationships mature because of the establishment of communication patterns between the actors involved in the business relationship. Another benefit that motivates a business to invest in developing and maintaining business relationships with its customers and suppliers is that relationships help to cope with, or at least reduce, the environmental uncertainties and knowledge of the company and to expand the influence and power in the network (e.g. Håkansson & Snehota, 1995).

There are also several negative aspects of being engaged in business relationships. There is no doubt that developing and maintaining relationships involves costly interactions and adaptations. The costs are related to the time, effort, and investments necessary to put effective solutions in place in relationships. But there are other negative aspects; for instance, business relationships can be exclusive. In certain cases a large number of customers has been found to have positive effects on new solution development since they provide more access and exposure to external knowledge, which leads to more scale effects in development processes. That is, the

more customers a business involves, the faster the development of new solutions (e.g., Gulati, Nohira, & Zaheer, 2000). However an excessive number of business relationships can pose some difficulties. Other research has underlined the importance of concentrating on a more limited number of business relationships (e.g., Lettl, Herstatt, & Gemunden, 2006) since developing and maintaining relationships requires a lot of managerial and arrangements efforts, costs, and trade-offs. In particular, interaction with many customers or suppliers may become counterproductive at a certain point (Yli-Renko & Janakiraman, 2008).

Besides the positive and negative aspects of being engaged in business relationships, the process necessary to develop and maintain a business relationship generally entails some costs that precede the potential benefits. Developing business relationships and maintaining contact requires a significant amount of time; for example, Aldrich & Reese (1993) found that, on average, entrepreneurs spent more than five working hours a week developing and maintaining their relationships. It is not only the amount of time the entrepreneur spends on developing and maintaining contacts that entails some costs. Interacting with customers and suppliers entails other kinds of costs that are often difficult to trace and assess (Baraldi & Strömsten, 2006). Interacting with purchasers and sellers certainly requires investments of time and money, but it also takes management efforts to adapt the resources, coordinate the activity flows, and process information and communication practices of the actors involved on both sides of the business relationship (Andersson, Aspenberg, & Kjellberg, 2008; Geiger & Finch, 2009; Ellis & Hopkinson, 2010). For example, when customers face problems with a proposed new business solution, they search for advice through discussion with the supplier that in turn will refine the new solution to the customer's needs. The refinement of an effective solution will certainly require adjusting or developing a set of new and costly procedures for both parties involved.

All considered, the development of a relationship between two businesses involves interaction that is a condition for developing workable solutions between the parties involved. Conversely, the need to adapt complex activity chains, and interface various resources and several joint actors entails some collective costs that are often

difficult to record and assess. What we are arguing is that, apparently, a relevant key issue in helping to explain the complex dynamics concerning the development of new business relationships in the relevant network is the economic consequences of interaction for all parties involved. For this reason, our study will carefully examine the implications of creating these resource interfaces in configuring and running the activities and in bonding numerous actors by creating shared meaning.

## 5.7 FINAL CONSIDERATIONS

Adopting a network perspective on business markets implies that industrial markets are characterized by business relationships that are interconnected in complex ways, and the business market appears as a network – a set of nodes (actors and organizations) linked by interactive relationships. Hence, each business is always part of a network and is connected to it by a set of relationships. This means businesses can be considered as nodes of the business network in which they are embedded.

The process of business formation inspired by the network approach is thus based on assumptions that differ from those discussed in chapters 3 and 4. It associates the birth and development of a new business with the process of merging into a solid existing network of exchange relationships and becoming a node of it by developing new business relationships with others.

Each new venture must fit with pre-existing networks because it makes use of resources that the other actors in the market can provide (Håkansson, Ford, Gadde, Snehota, & Waluszewski, 2009). However, dependence on the network is not only about access to the variety of tangible resources held by other actors, but also about access to information flows, advices, and other more intangible resources critical for the business activities (Aldrich & Zimmer, 1986; Bates, 1997; Freeman, 1999; Hoang & Young, 2000). Business relationships with customers and suppliers are also prerequisites for finding solutions that improve the functionality of a product or service and for developing new workable solutions collectively and cooperatively. “Relating” to pre-existing networks is a critical business process since it has a positive impact on

entrepreneurial business growth, particularly with respect to generating innovative business solutions (Johanson & Vahlne, 2011).

This process, namely the merging (or embedding) of a new business in the pre-existing context, has several open issues (Snehota, 2011; Welter, 2011). As suggested in the previous research on business networks, we can assume that merging the new business on a pre-existing business network requires developing relationships with other actors who control and provide resources, coordinate activities, and negotiate the meaning with those who are involved (which is a communication issue between the actors). Only very recently has research come about that any new business involves negotiating conceptually with other counterparts and how such businesses interpret each other's features and characteristics through interaction. How the interaction develops, therefore, depends largely on the meanings ascribed by each of the interacting actors to the other actors (Andersson et al., 2011; La Rocca, 2011; Geiger & Finch, 2011). In other words, the conduct in the interaction is highly dependent on what the actors represent for each other, which is how they see each other. Indeed, what a business represents for those who interact with it and how it negotiates boundaries of the concept that the actor represents seem to be central issues for producing more robust explanations in new business formation.

The merging of a new business into a pre-existing business context also means interfacing resources that exist and on which the new product has to be grafted and built. Nevertheless, whether a company needs to interface specific components into its production or has to sell a customized product, negotiating the meanings and interfacing the resources are critical processes that entail a flow of activities in which the company needs to be plugged in (Gadde et al., 2001).

Indeed, interfacing resources is the result of interaction processes among the involved parties that requires time to develop a workable resource combination and negotiating the meanings of how they can benefit each other. Therefore, interaction in business relationships is a condition for interfacing the required disseminated resources (Ford et al., 2010), and these extensive interactions are collective, nonlinear, and onerous (Ciabuschi, Perna, Snehota, 2011).

We have also seen that IMP scholars have been trying to study different aspects of these collective, nonlinear, and onerous processes such as the costs that arise from the need to interface resources, adapt activity flows, and negotiate the meanings of the actors involved (Baraldi & Strömsten, 2006). That is, the complex processes experienced in the development of new business relationships can both favor and constrain the customers and suppliers involved since they can be a vehicle for developing conjoint business solutions and gaining economic efficiency. However, on the other hand, linking resources, coordinating activities, and creating a substrate of shared meanings between the actors can also become an expensive and complicated task. Our hypothesis is that the costs incurred in handling the merging into an existing context are no less than the R&D costs incurred in developing a new product.

Focusing on this process of plugging the new venture into a pre-existing context might provide an explanation for the evident and widely documented difficulties in developing a new business. It would seem that the development of a new business, its formation and growth, is enabled and constrained by the necessity to develop new business relationships. It is also reasonable to assume that the way in which the involved parties in a business relationship combine and develop the three layers of interfacing resources, configuring activities, and creating shared meanings becomes crucial for the development of a new venture.

## 5.8 PROPOSITIONS

Once we have framed the problem of the new business venture as merging into a pre-existing business network, we can formulate some propositions that have the function of guiding our empirical investigation. According to Yin (2003), the study's propositions are helpful in focusing the study's goals since they will later guide both the data collection and discussion of the findings. In particular, propositions allow us to define the scope of observation, to help us identify the process we intend to study, and to select the means by which to collect data. Thus, we extracted from the literature four main

propositions concerning the development of a new business that we're going to illustrate and investigate through empirical study.

1. The difficulty in developing a new business (and the relatively high failure rate) is related to the complexity and difficulty of the task of developing new business relationships.
2. The complexity in developing new business relationships is due to the fact that there are the three layers involving different issues in developing effective solutions in business relationships. Namely, configuring activities (Håkansson & Snehota, 1995; Dubois & Araujo, 2006), interfacing resources (Bengtson & Håkansson, 2008; Baraldi, 2008), and creating shared meanings (Hodgkinson, 2005; Weick, Sutcliffe, & Obstfeld, 2005; Waluszewski, Baraldi, Shih, & Linne, 2009).
3. The relational business solutions and arrangements cannot be developed unilaterally (Sawhney, 2006; Baraldi & Strömsten, 2006; Tuli, Kohli, & Bharadwaj, 2007; Vargo & Lusch, 2008). Novel solutions, on which the relationship development of a start-up depend, are defined jointly by the parties involved and are the outcome of a process of coping with many arrangements that aim at interfacing a large and complex set of operations (Harrison & Waluszewski, 2008; Oliva & Kallenberg, 2003; Davies, 2004; Kapletia & Probert, 2009).
4. Emergent business solutions and arrangements, that are conceived in conjunction with others in order to embed them into users' contexts (Håkansson & Waluszewski, 2002; Håkansson et al., 2009; Ingemansson & Waluszewski, 2009), will be successful only when they have positive economic consequences for the assets of the parties involved (Håkansson & Harrison, 2006).

These are the four propositions derived from the literature we analyzed. Therefore, we will investigate them empirically and this will qualify the underlying question of our research. That is, what are the difficulties that occur in configuring activities and interfacing resources; and what are the critical issues that arise in coping with unshared meanings among the actors in developing a new business relationship? Empirically investigating these interaction issues amounts to investigating at the activity level, at the resource level, and at the actors' level what kind of (arrangements) interdependencies have been managed by the actors involved in setting up a business relationship.

Empirically investigating the interdependencies at the activity patterns level means questioning whether there is or has been the need to sequentially and jointly coordinate activities or whether there have been only pooled (or generic) interdependencies (Thompson, 1967; Håkansson et al., 2009). In generic or pooled interdependencies, the output of the actors involved in relationships or their input of resources from a common source contribute to an overall outcome. In practice, the generic interdependence is established between the parties by the simple fact that their contribution depends on the overall level of results without this implying a significant set of intense and direct relationships. On the contrary, the sequential activity interdependencies link two activities when the output of one helps the input flow of the other. In practice, there is sequential interdependence when a one-way sequential relationship is established between the parties, according to which changes in behavior on one side require adaptation of behavior of the other part. Typically, in the assembly or production line there is much sequential dependence. An example would be the exchange relationship of a semi-finished product between the production departments of the supplier and the manufacturing departments of the client. With regard to the reciprocal coordination of the activities, this means the activity of one directly affects the activities of all others and therefore the parties must work simultaneously. This implies co-action with mutual and simultaneous adjustment of the activity flow. Basically, this type of interaction occurs when the performance of one activity is dependent on another, because both are related to a third activity and the activity of one directly affects the

activities of all the others and vice versa. In practice, this can happen in a situation in which there is the need to jointly develop products or where the activities of two suppliers need to become jointly interdependent in order to supply together the process of a common customer. The Interdependencies at the activity patterns level can be traced to one or more of the quadrants illustrated in Table 5.3.

Table 5.3 Interdependencies at the activity patterns level

Task Interdependence	Rules and Procedures	Schedules and Plans	Mutual Adjustment
Pooled	X		
Sequential	X	X	
Reciprocal	X	X	X

(Source: based on Thompson, 1967)

Therefore, in order to find out to what extent there was a need to develop activity patterns, we will try to determine what activity configurations were required to generate a particular outcome such as a new end product, or which adjustment of activities was required to coordinate, for example, the implementation activities of a service provider and the manufacturing activities of a customer. The aim is to find out if there was a need to find solutions for the synchronization of production activities in and between businesses, or if there was a need to adjust the transportation, logistic, and administrative activities, and so on to integrate a functioning and valuable solution into the customer's ongoing activities.

As previously seen, resource ties are mutual and specific resource adaptations that imply the creation of interfaces (Håkansson & Snehota, 1995). This involves the creation of specific adaptations on products, on production facilities, and on

organizational assets by both parties involved in the relationship (Håkansson et al., 2009). Regarding this aspect, we want to determine to what extent the actors involved in developing the relationship are required to mutually adjust and interface the exchanged resources in combination with the possessed resources in order to become useful, functional, and profitable. In practice, this could be investigated by examining the extent to which there has been a need to develop resource variations in the production facilities, in the product, in the business units, or at the relationship level (Håkansson & Waluszewski, 2002; Baraldi, 2003) in order to enable the resource interfaces to function appropriately.

An exploration of the actors' dimension, as suggested by the IMP approach, is proposed by trying to answer a series of questions about how the actors interpret the context of action, how they define the objectives, and, ultimately, how they use the means for achieving their objectives (Snehota, 2003). The issue here is to understand through which arrangements actors attempt to become bonded in the interacted environment. Therefore, we will focus on specific issues such as to what extent the actors involved in developing new business relationships cooperate in order to learn the "language" of their counterparts, create a substrate of "shared meanings," and develop a mutual orientation to complement each other's activities. Another interesting issue would be to investigate the different approaches and examine the logic the actors followed in order to mediate and negotiate their perceptions and interpretation of mutual commitment and expectation. The main idea is to capture the ways in which an actor relates and becomes mutually and selectively associated with other actors and also to understand the counterparts' perceptions in matching their operations, ambitions, beliefs, behaviors, and problems (Håkansson et. al., 2009) within the development of a new business relationship.

These are the research questions that result from our analysis of the literature. We argue that a better understanding of the process of creating resource interfaces, of configuring and coordinating activity patterns, and relating different actors in the process of developing new business relationships in young organizations should extend and complement the current understanding of the processes of new business formation. Thus,

our aim is to describe the main difficulties in creating resource interfaces, in configuring the activities, and in developing shared meanings. In order to do that we will take three business stories that will be used to illustrate the various pitfalls and different problems connected with the merging of a new business in the pre-existing market. The ambition is to capture some aspects of the difficulties and criticalities involved in developing new business relationships and make use of them.

# Chapter 6

## Three Cases of New Business Formation

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In this chapter, we discuss three case studies of new ventures. The cases are all start-ups in the early stages of the development of initial business relationships, but their activities are in different businesses and the focus of the case studies is on different aspects of new business development. Each of the cases focuses on one of the three facets of the ARA model discussed in Chapter 5 - namely, activities, resources, and actors. Two of these were incubatees at the business incubator affiliated with the Università della Svizzera Italiana. The three cases reported here are:

1. SafeVine a start-up proposing an innovative solution for predicting diseases of vineyards that has been developed in an ongoing project called Safe-Vineyard. The thrust of this case is on the activity layer in business relationships.
2. Ekobike is a new venture engaged in importing, marketing, and developing and producing high-performance electric motorbikes. The Ekobike story hinges on the resource dimension of a new business venture.
3. Concertlab is a new business formed with the aim of creating a web platform dedicated to music to facilitate interactions and communication among the various interested parties operating in the live-music business. This case highlights issues related to connecting actors.

The cases are organized as follows: Each case is introduced by a brief case summary that provides a first picture of the new businesses and the roots of the business idea to get an overall view. We then organize the story of each of the three cases around the following topics:

1. For each of the three start-ups, we describe the path followed by the new venture in order to turn their business idea into an organized business.
2. We describe the business model and the business practices, such as requests for funding, that new businesses performed in order to develop their product or service.
3. We report how each of the new ventures managed the development of their first customers' or suppliers' relationships during the process of new business formation.
4. For each of the three start-ups, we then briefly expose the economic results in order to provide an indication of the investment success of the start-up observed.
5. The case ends with a description of the specific business context in which they aim to merge.

The emphasis will be on the different layers of business relationships and the key issues in these. We examine what difficulties exist in embedding the new venture in the preexisting context with respect to one of the three layers of ARA describing the different paths followed in each venture to configure activities patterns, create resource interfaces, and negotiate the meanings among actors involved in the process of business relationship development in the emergent organizations. In particular, the analysis of the SafeVine case will focus on exploring the possible reasons for difficulties encountered in acquiring paying customers with particular attention on the activity pattern level of analysis. The case analysis of Ekobike centers on investigating the need of interfacing resources with suppliers when a company is developing a new solution. The case

analysis of Concertlab investigates the reasons of the limited success of the start-up thus far and explores the apparent difficulties in particular in the actor dimension.

On the whole the purpose of these cases is to illustrate some of the critical issues involved in embedding the new venture in the existing business network by developing the initial business relationships. We will describe how these processes occur and which are the main problems as well as the needs for synchronization that might arise. The case description presented in this chapter will be further developed in Chapter 7.

*Glossary of Terms:*

Agroscope: Swiss Federal Office for Agriculture.

ALaRI: Advanced Learning and Research Institute of the Faculty of Informatics at Università della Svizzera Italiana.

CP Start-up: The Start-up Promotion Center is a business incubator affiliated with the Università della Svizzera Italiana (USI) and the Scuola Universitaria Professionale della Svizzera Italiana (SUPSI), which assist Swiss and foreign graduates who plan to start a company in Canton Ticino.

CTI: The Swiss Commission for Technology and Innovation Promotion, which lends support to R&D projects, entrepreneurship, and the development of start-up companies.

SUPSI: University of Applied Sciences and Arts of Southern Switzerland.

USI: Università della Svizzera Italiana.

## 6.1 SAFEVINE

### *CASE SUMMARY*

SafeVine is an innovative solution for predicting vineyard diseases, a problem that reduces winegrowers' profits due to decreased production. The SafeVine technology – based on wireless sensor networks, weather stations, and prediction algorithms – allows farmers to predict the evolution of these diseases and alerts them to implement “just-in-time” targeted treatments. Such a system permits winegrowers to employ the right phytosanitary treatment only where and when it is needed, significantly reducing the cost of treatment. Mauro P. developed the SafeVine solution as part of the Safe-Vineyard project, an ongoing project funded by the Swiss Commission for Technology and Innovation promotion (CTI). The project originated in 2005 when Mauro P., an electrical engineer, came across the idea by chance during a training workshop for young entrepreneurs. At that time the idea, despite positive evaluation by the workshop committee, was temporarily shelved. Mauro P. then decided to invest his time in the founding of a new company, Hippo Engineering, which specialized in developing and selling consultancy, services, solutions, and products based on computer and electronic systems. After three years, in fall 2008, Mauro P. decided to review his idea when Agroscope, the Swiss Federal Office for Agriculture (promoting economic activity in the agricultural, nutritional, and environmental sectors), which was concerned about resurgence of the flavescence dorée in Canton Ticino (a disease of the vine with the potential to threaten vineyards) approached him and asked him to further develop his old idea. In October 2008, Hippo Engineering and Agroscope agreed to carry out the Safe-Vineyard project. Currently, the new solution is still in an experimental phase, and was projected to end in late 2012; thereafter, the goal is to market the product and to test the possibility of applying the system to other cultures. The case analysis is focused on exploring possible reasons for the start-up's lack of paying customers, with particular attention to the activity pattern level of analysis.

## 6.1.1 FROM THE IDEA TO THE VENTURE

### THE ORIGINAL IDEA

The first idea of a system capable of monitoring vineyard microclimate conditions to predict vineyard diseases came up by coincidence in 2005, when Mauro P. attended a training course on entrepreneurship. During the course, participants were asked as an exercise to think out a business idea and to discuss its potential development. Shortly before attending the course, Mauro P. learned about some American researchers who had developed a wireless sensor network system to monitor the diffusion of some vineyard pests. Having a specific knowledge of the Ticino territory, which is rich in vineyards, he recognized an opportunity and decided to develop and present a similar idea: a monitoring system based on wireless sensor networks able to inspect the vineyards' micro-climate conditions, such as humidity and temperature, with the goal of predicting vineyard diseases. Although the project committee positively evaluated the project, Mauro P. did not pursue it. However, three years later, in November 2007, Mauro P. started his own company, Hippo Engineering, which specializes in developing and selling consultancy services, solutions, and products based on informatics and electronic systems.

### THE BUSINESS IDEA

The idea behind SafeVine is a wireless sensor network that is able to measure, within the network coverage, the microclimate of the vineyard, registering the air temperature and humidity conditions. The collected data are then sent to a server where they are analyzed in real time by a series of software algorithms. This data are finally reported and displayed in an end user-friendly application. Data measurements provide enough information to allow a farmer to identify in advance conditions conducive to the spread of the insect vectors of disease and thus permit the farmer to combat them effectively at

an early stage. As Mauro P. clarified, “In this way, the system we have developed is able to accurately inform winegrowers and regional plant protection services and allows for the optimal planning of actions to combat the spread of the insect.” Mauro P. highlights the collective benefits derived from the use of this system: “Using this service, anyone involved in viticulture will be able to optimize the resources to be used for the defense of his or her own vineyards with a consequent saving of time and financial resources.” The timing of the system is a peculiarity of the solution: the system informs winegrowers about two to three weeks in advance when to start the treatment necessary to fight the disease. The capacity to plan this type of operation provides an optimization of the vineyards’ maintenance costs and, according to Mauro P., winegrowers should be able to reduce their vineyards epidemic control costs by about 25%.

Moreover, the system is based on an auto-adaptive control algorithm that allows for the adjustment of the parameters to the specific conditions as soon as the sensor inputs are processed. This means the auto-adaptive power is capable of adjustments in accordance with the processed data and can provide useful information for growers who have to take decisions concerning their activities. According to Mauro P., this auto-adaptive property makes the SafeVine solution different from that of its competitors: “This system, based on what has been registered during the past season, can provide useful information for what is needed to be done for the following seasons. This characteristic differentiates us from our competitors.”

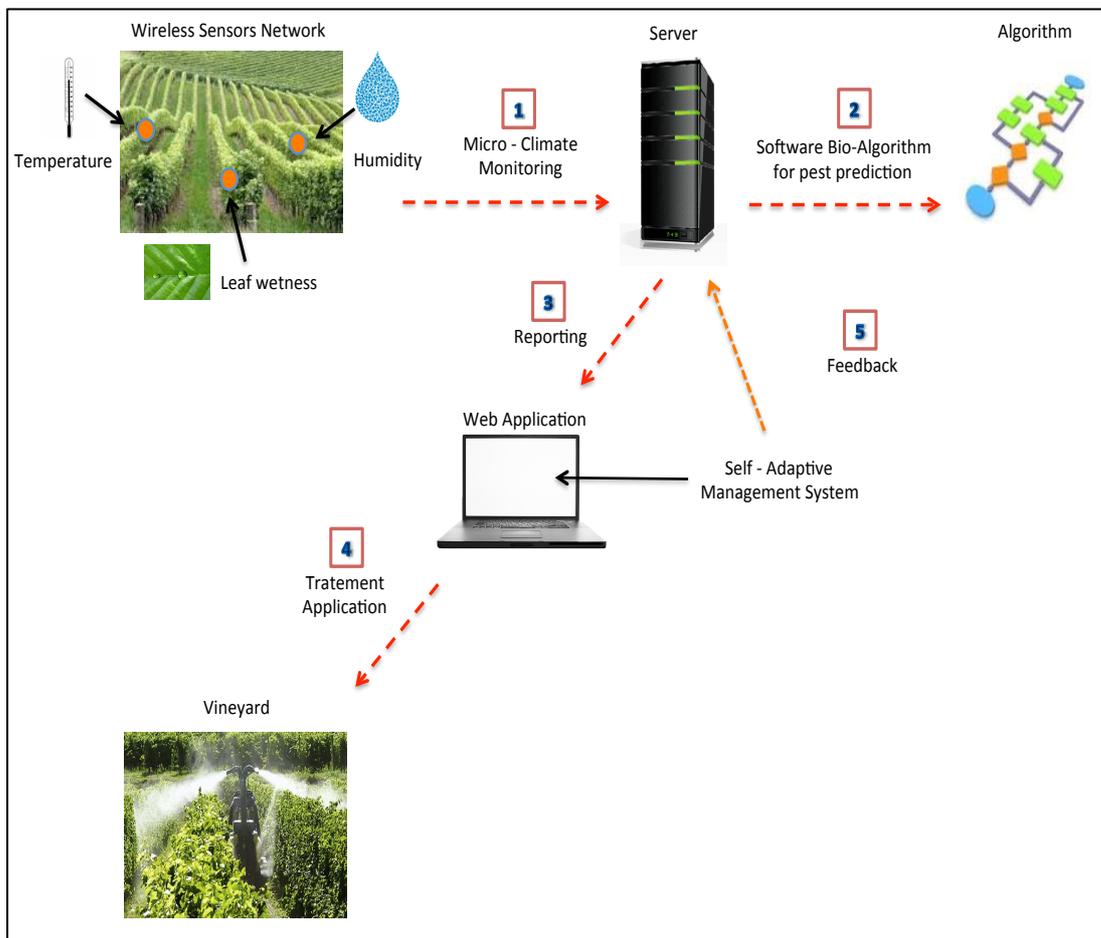
The system developed offers two advantages. First, it presents a customizable Web interface that enables the winegrower to interact in a very simple way with the tracking system. Second, the system can be potentially applied for the detection of many diseases that threaten crops other than vines. In fact, as Mauro P. clarified, “Using the same infrastructure, it is possible to substitute or add the algorithm that realizes the phenological model for the organism that has to be fought<sup>18</sup>. Of course, everything has to be validated with field and laboratory tests, since it has not yet been examined and verified whether the system could also be effectively applied to monitor other types of

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<sup>18</sup> The phenological models applied in agricultural meteorology allow for the estimation of the evolution of the development cycle of crops using climate and weather information to integrate the phenological information, which is often too discontinuous in time and space, or even nonexistent.

crops.” The SafeVine system, shown in Fig. 6.1, offers winegrowers the main benefits of cost savings and quality improvement in terms of: 1) Knowing in advance which kind of disease will appear, as well as where and when it will appear; 2) Optimizing the workload of human resources, acting only when it is needed; 3) Optimizing the usage of phytosanitary products; 4) Getting a higher grape quality.

Figure 6.1 The SafeVine System



Mauro P. shelved the idea until 2008 when the vineyards in Ticino and other wine-growing regions of Switzerland, France, Italy, Spain, Slovenia, Serbia, and Portugal, were heavily affected by the return of a grapevine disease, flavescence dorée (hereafter FD), which had been previously eradicated. In Switzerland FD was first recorded in some areas of Canton Ticino, in particular in the borough of Mendrisio in 2004, and in the boroughs of Lugano, Locarno, and Bellinzona in 2005 and 2006. Later, it appeared in some vineyards in the Lake Geneva area in 2008. Flavescence dorée is a bacterial disease of the vine with the potential to threaten vineyards; its vector is the leafhopper *Scaphoideus titanus*. This bacterium is the cause of an epidemic disease in grapevines characterized by spreading rapidly within vineyards. When proper and immediate initiation of phytosanitary measures is not applied, this infection may kill young vines and greatly reduce the productivity of old vines. It also increases wine production costs due to additional insecticide applications. Insecticide treatment against the vector is mandatory in vector-affected vineyards. Since the symptoms of FD are very similar to those of a less dangerous infection, blackwood disease, the detection of FD is somewhat difficult. Moreover, the prevention of FD is made particularly difficult by the fact that infected plants may not show symptoms for months or even several years after being infected. The disease can only be diagnosed and differentiated from blackwood by means of costly and complex biomolecular lab tests (Gugerli, 2007). Visual inspection, is insufficient to detect latent contaminations and is often misleading due to similar symptoms of the two different diseases; however, it remains the most common practice for detecting the presence of FD because it is less expensive than laboratory tests.

## STARTING UP

The opportunity for Mauro P. emerged when Agroscope, the Swiss Federal Office for Agriculture Research with a mandate to support economic activity in the agricultural, nutritional, and environmental sectors, started to conduct a series of research projects and observations on the dynamics of the development of the insect vectors of FD. The Office was convinced that a deeper understanding of the development dynamics of the

grasshopper, the carrier vector of FD, could help reduce the risk of diffusion into other grape-growing regions of Switzerland, especially north of the Alps, an area that is currently free of the disease. In fall 2008 Agroscope, concerned that the active spread of the disease represented a serious menace to Swiss viticulture and winegrowers' business, contacted Mauro P. Agroscope got to know about the activity carried out by the founder and CEO of Hippo Engineering and decided to sound out Mauro P's interest in developing his idea in collaboration with the federal office in order to find a solution to limit the diffusion of the lethal disease. Since laboratory techniques for the detection and diagnosis of FD, amongst other drawbacks, were complex, expensive, time-consuming, and required trained personnel as well as expensive equipment, Mauro P. became convinced he could develop the new technique. The system was expected to monitor the development cycle of FD and to systematically provide information about the phytosanitary measures to be implemented in order to fight the disease. In October 2008, Mauro P., urged by Agroscope, decided to reactivate his project idea and agreed to participate in the Safe-Vineyard project by first conducting a feasibility study to develop a new computer-aided monitoring system for viticulture.

## 6.1.2 THE VENTURE

### THE BUSINESS MODEL

The main objective of the Safe-Vineyard research project was to develop a reliable, cost-effective, and easy-to-use non-technical staff device, which would allow for the early detection of FD. The core of the SafeVine solution, the software algorithms, was the only technology developed in-house by the various engineers and computer science students involved in the project. The other required components, the weather stations to measure the humidity and temperature parameters and the wireless sensors to collect and transfer the data, were acquired externally. Mauro P. believed that any winegrower or

wine maker who owned a PC with the appropriate capacity could support the Web application winegrower.

Identifying the right suppliers was not particularly difficult. Mauro P's only concern was to remain independent from the integrated technology. Being technologically independent would not only make it possible to match the software algorithm with wireless sensors based on different technologies, but it would permit greater compatibility with weather stations using previously installed technology. In short, the SafeVine software algorithm should have been widely compatible.

Hippo Engineering bought the sensors for the first four wireless networks from Detect, a young company based at Tecnopolo Lugano. Since the two young entrepreneurs knew each other, they had no difficulty collaborating, and this facilitated the development of a business relationship between the two new ventures. Detect develops and produces innovative automatic natural hazards detection systems<sup>19</sup>. These systems are little autonomous wireless sensors that can constantly monitor many areas. For instance, in case of recorded natural hazards, such as wildfires, floods, or landslides, the sensors send an online notification to a mobile phone within a few seconds.

The cost of the five Detect wireless sensor networks was about 15,000 CHF. However, in order to remain independent from the technology used for the data collection and transfer, Hippo Engineering decided to purchase one different type of wireless sensor for one network from a U.S. company.

The weather stations required to collect data on humidity and temperature were bought from an Italian company. The total cost of the purchase of two weather stations amounted to about 5,000 CHF. The investments made to purchase the eight components required for assembling and building some of the devices designed by SafeVine were around 20,000 CHF.

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<sup>19</sup> Tecnopolo Lugano SA is an organization that supports and assists start-ups in the region of Lugano. In particular, it intends to encourage new business ideas by guiding them while entering the market, directly or through other agencies or organizations having similar purposes.

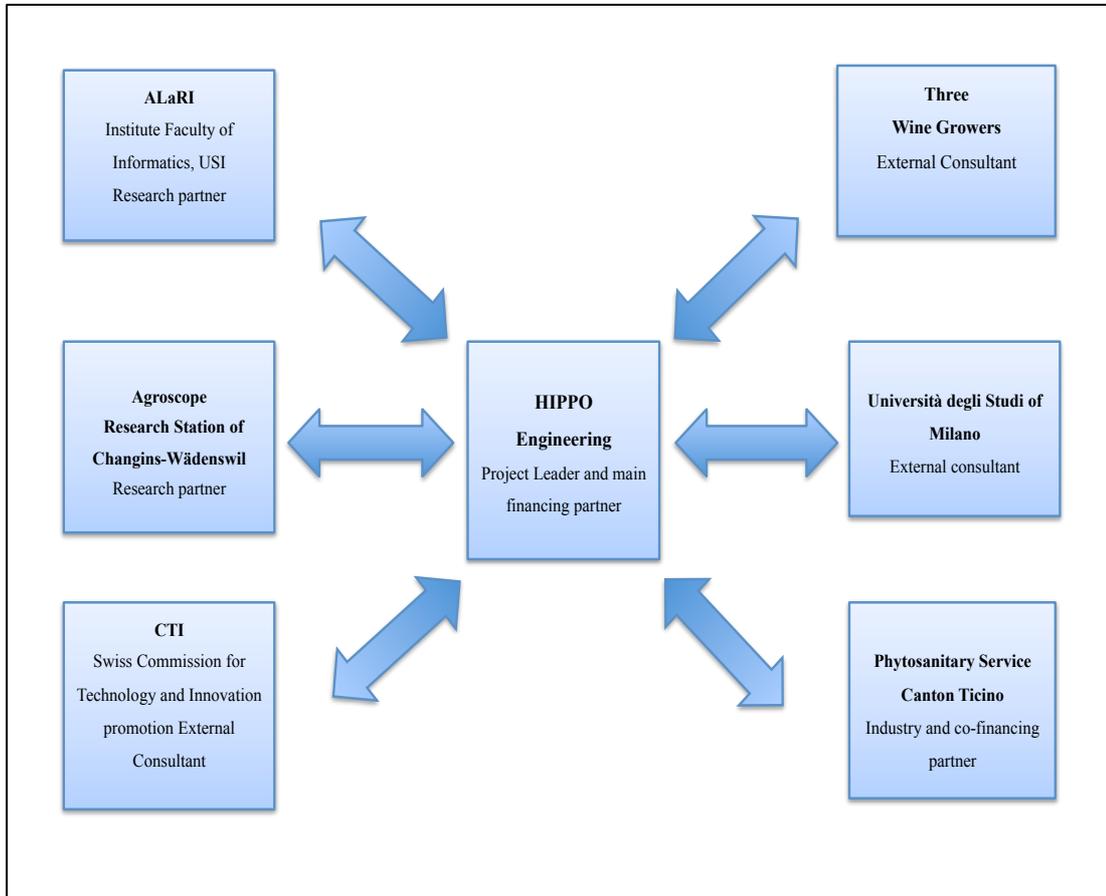
## PRODUCT DEVELOPMENT AND FUNDING

The complexity of the system solution idea required considerable funds for research and development. Mauro P. therefore decided to apply for funding to the Swiss Commission for Technology and Innovation promotion (CTI). In May 2009, Hippo Engineering received an innovation check of 7,500 CHF to sustain the Safe-Vineyard research project. Thanks to this first funding, the research group, comprising Hippo Engineering and Agroscope, also involved a trainee from the Università della Svizzera Italiana (USI), who worked part-time for five months on a first wireless sensor network prototype and on the algorithm to calculate the spread of the disease vector.

A few months later, in October 2009, Hippo Engineering passed the first evaluation phase of the expert committee of the Start-up Promotion Center (CP Start-Up) an incubator of USI. According to Mauro P, “The company finally could make use of startup incubator infrastructures and start working seriously on the project.” Access to this business incubator not only allowed the start-up to use offices equipped with everything they needed for free, but also enabled them to rely on the support of about a dozen employees prepared to follow and coordinate different new business projects.

In fall 2009, the Safe-Vineyard team realized the project needed additional resources and funds to continue developing the prototype. Other partners were invited to take part in the project: the Advanced Learning and Research Institute of the Faculty of Informatics at Università della Svizzera Italiana (ALaRI), the University of Milan, the Phytosanitary Service of Canton Ticino, and three winegrowers. The aim of the enlarged research group was to prepare a further funding application that was submitted to the CTI. Figure 6.2 illustrates the Safe-Vineyard team project.

Figure 6.2 The Safe-Vineyard team project



In April 2010, the CTI approved a request for funds of 170,530 CHF for a two-and-a-half-year research and development project that would run until September 2012. These funds made it possible to finance the second part of the project, namely concluding the prototype phase and starting with the product development phase. In this regard, Mauro P. stated, “Obtaining the funds from the CTI allowed the project to effectively start with product development. We got the appropriate amount of money at exactly the right moment: an amount sufficient to prove that the project was feasible.”

In November 2010, the project finally moved from the implementation to the development phase of the solution for monitoring the evolution and occurrence of FD disease. In order to start field-testing the technology, the first three experimental devices

were installed in three vineyards of Canton Ticino owned by the regional authorities and managed by specialized phytosanitary research centers. The Canton Ticino region, which is characterized by very scattered vineyards, was the ideal place to test the product, because, according to Mauro P, “This type of conformation, characterized by lands that are very different for slope and microclimate, is of particular interest to our project because we can use them as distinctive laboratories for testing our product.” In early 2011, two more wireless sensor networks were installed in two different vineyards in Piedmont in Italy, which were also owned by the regional authorities and managed by specialized phytosanitary research centers.

Detect installed the four wireless sensor networks sold, while the sensors purchased from the American company were installed by technicians and Mauro P.

The five installed sensors served not only to test the system, but also to validate it for the market. Mauro P. believed that, “This field test and the validation will allow us to be able to glitch-free the system and offer a readily deployable product to the winemakers potentially interested in buying the wireless sensor network for pest control.”

By October 2011, the Swiss Commission for Technology and Innovation Promotion defined Hippo Engineering as a "success story." However, this is not the only achievement obtained. Hippo came through to the semifinals of the European Venture Challenge, a contest that rewards the most innovative companies with the potential to impact their industry and contribute to increasing European competitiveness and growth. In addition, in October 2011, they were invited to a scientific conference on viticulture in Bordeaux to present their project. On that occasion they had the opportunity to develop the first contacts with potential customers. More recently, in January 2012, Hippo Engineering won 30,000 CHF from the "Microcredito Città di Lugano," an award that supports the most innovative projects/start-ups that are headquartered in the town of Lugano. Finally, in April 2012, the start-up became part of the CTI "coaching acceptance" program that offers to the winning start-ups the support of experts in the later stages of business development.

## MANAGING CUSTOMER RELATIONSHIPS

In June 2012, the project entered into partnerships with 14 regional phytosanitary research centers, eight in Canton Ticino, two in Canton Geneva, two in Piedmont, and two in the Veneto region, with the purpose of installing several wireless sensor networks in their cultivated grapevine area. Most of these strategic partners already had a system that would permit the running of SafeVine technology. The core technology of SafeVine, the software algorithm, and the Web application were transferred to the 14 research centers, some of which installed additional components. In particular, SafeVine installed five different networks of wireless sensor, and two weather stations.

The start-up has not yet acquired any private winegrower customers. Of the contacts made at a scientific conference on viticulture in Bordeaux, in October 2011, none has resulted in a business relationship. In spring 2012, Mauro P. met the founder and CEO of an established wine-trading and viticulture business, one of the largest in the canton of Ticino. The partnership with this important winemaker could have developed in two different directions. On one side, this business could have become a strategic partner that would provide useful elements and feedback to improve and further develop SafeVines' technology. On the other side, it could have become the first paying customer. However, the winegrower decided against becoming a SafeVine customer because the Canton Ticino's phytosanitary center had already informed vine growers for free how and when to treat vineyards against grape diseases, including treatment against FD. In the case in point, Tamborini's opinion was that, "A similar monitoring system already exists and is offered by the canton. Obviously this system is much cheaper and does not involve investments. For me, the proposed technology is not applicable in the terms set but requires much more precision. Moreover, I get the impression that the costs involved are not worth the savings unless it is on a very large scale." Mauro P. replied, "It is true that the cantonal phytosanitary center offers a monitoring service for free but it is not as accurate as ours. They have some monitoring stations scattered across the region, but the climatic conditions vary significantly within a few kilometers. With our

technology, the vine grower can monitor his own vineyard with much more precision and accuracy.”

This important vine grower and vine trader, although not willing to purchase the technology, did not exclude the possibility of developing a partnership and collaborate in some way in the project Safe-Vineyard. For Mauro P. maintaining contact with this strategic partner was imperative: “Although the possibility of developing a business relationship with this winegrower failed, we still manage to maintain active contact for a possible strategic partnership. The opinion of one of the major winegrowers in Ticino can become significant for us. With him we have some agreements for a strategic partnership that has to be developed.”

Concerning future strategies, Mauro P’s ambition is to start with the commercialization of the technology by the end of 2012. He argued: “Since the wireless sensor network for pest control is ready for the market, by the end of the year our objective is to start selling our system. I’m convinced there are winegrowers of about 100 or more vineyards’ hectares that are interested in our technology.” According to data collected on the dimensions of the global wine market, approximately 50% of wine production comes from the neighboring countries of Switzerland, Italy, France, and Spain. “This aspect is very interesting because the geographical proximity with those countries allows us to access these markets at relatively low cost; from 10 to 15 customers should be sufficient for our business to be profitable.” However, “At the moment we have not defined who will be responsible for installing the technology, or who will be accountable for the maintenance. For us it is clear that if we go to install the sensors ourselves, then it will be the winemaker’s task to maintain it. We don’t even know precisely what the costs will be because they will vary depending on the number of vineyards that the single customer will monitor. We have some ideas, but we still have to consider a strategy.” Hence, SafeVine technology still needs to be turned into a marketable product. And for Mauro P. it was precisely this planning and management of the commercial issues that posed a major difficulty in developing the business: “We are engineers and thus have no knowledge about these business aspects. The team definitely lacks a figure who has a marketing and business background.” Mauro P. and some other

members of the team of the Safe-Vineyard project plan to discuss how to develop a strategy for acquiring their first customers with their coach, an expert from the CTI.

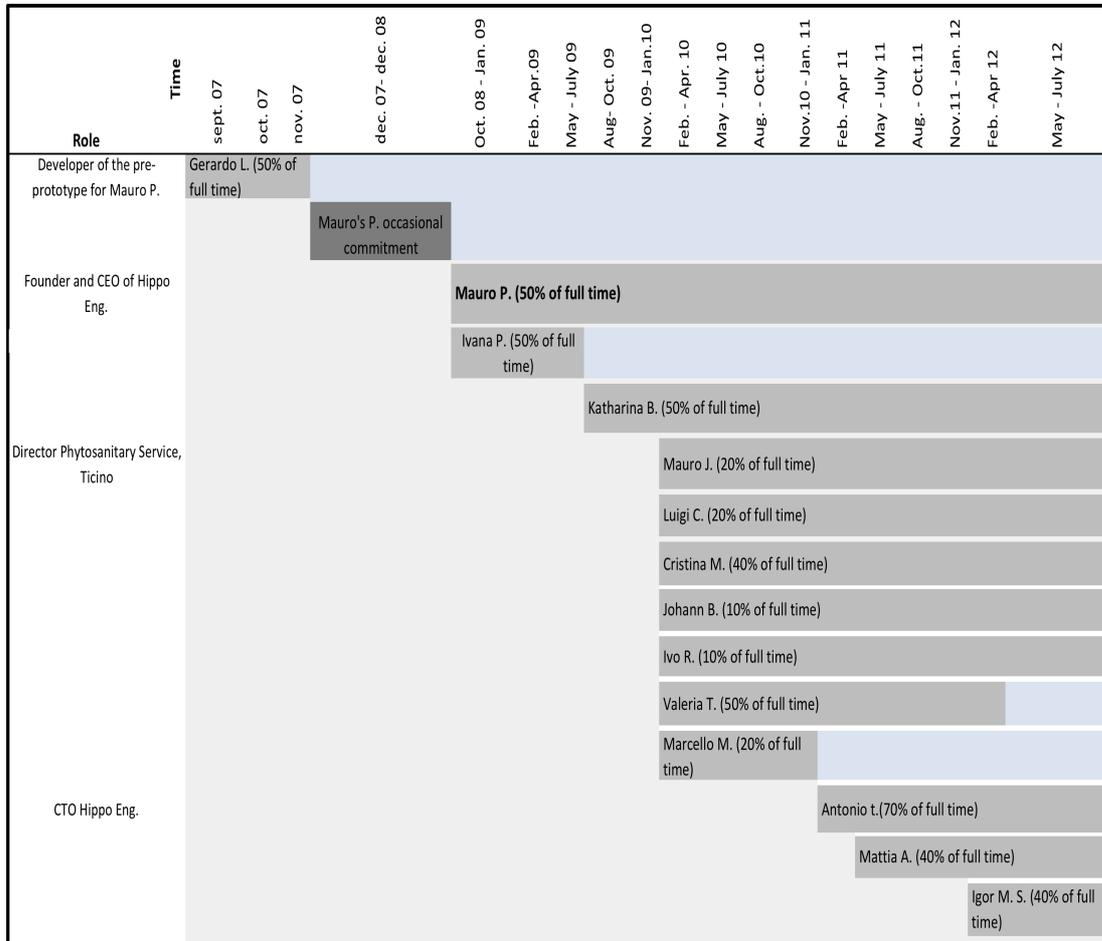
### 6.1.3 OUTCOMES AND FUTURE OUTLOOK

#### ECONOMIC OUTCOMES OF THE VENTURE

In reporting the development of this venture, an analysis of its economic result is relevant to understand whether the new business will survive or not. Indeed, the new business will survive only if its activities generate revenue, and not because they entered the market with external financing; and they will survive only if they generate more than they consume. Therefore, we reflect also on the economy to see if it actually holds. In hoping to do an analysis of the situation in June 2012, it seems worthwhile to reflect on the exercise of this new venture by examining the approximate data of income and expenditure up to that date, to see how this was near the break-even point. These observations are not designed to discuss the financial flows in detail, but allow us to have a first index of investment success.

In September 2012 most of the funds received, about 200,000 CHF, were used to pay the various people who assisted in the project. So far, there have been 14 people working on the Safe-Vineyard project. Table 6.3 (below) details the chronology, tasks, and time spent by members of the project team.

Table 6.3 Safe - Vineyard Team



Concerning the work time spent on the project, Mauro P. said only two people worked daily on the project: Mauro P. himself (at 20%) and Antonio T. (at 50%); however, he explained, "Although few people have worked full-time, we managed to achieve a good result compared to what we set out to do at the beginning. Even if our team consists of people with very different skills, we are now looking for another figure to help us acquire some customers. Actually, we are looking for a person responsible for sales."

As regards the total cost of purchasing the components, the five wireless sensor networks bought from the Swiss supplier amounted to 15,000 CHF. We do not know the

exact cost of the sensors produced by the American company but it is reasonable to assume about the same amount. The total cost for the purchase of two weather stations from the Italian company amounted to about 5,000 CHF. The investments made to purchase the eight components required to assemble and build some of the devices, which SafeVine installed in some vineyards belonging to the regional phytosanitary research centers in order to start to field test the technology, amounted to around 20,000 CHF.

By failing to acquire customers, it is reasonable to assume that the new venture did not generate any revenue from its activities.

## BUSINESS NETWORK CONTEXT

So far, we have described the business idea, related activities, and their role in the market from the entrepreneur's point of view. In this section, we report how potential customers and professionals have perceived the product in the business network context in which SafeVine should be embedded. In line with the aim of this case analysis, we asked some people in the vine production industry to explain what the main activities of the winemaker are.

According to a winemaker, the main task of a winegrower is to “daily observe the vineyards ...monitoring the development cycle of the grapevines, such as the advance or delay of the flowering of the grape.” The most critical aspect in observing the vineyard's life cycle is recognizing the right moment of the grape veraison, i.e. the phenological stage of fruit ripening, because from this moment on the grape will be immune to the two main diseases of the vine: *downy mildew* and *powdery mildew* (but not from botrytis). Consequently, when the grapes start ripening, which is followed by the grape harvest, the vineyard management requires fewer evaluations of preventative measures against grape infections. The leaf of the grapevine, however, remains subject to diseases, even after the start of the ripening phase. Hence, the winegrower must fight grapevine diseases during the whole course of its vegetative phase.

The grapevine is very sensitive to three fungal diseases. In many European regions the most common and dangerous grapevine disease is downy mildew, a microorganism whose development is strongly influenced by climatic conditions. The traditional active substance for fighting this fungal disease is copper. Cupric fungicides have the disadvantage that they are only covering products. This means after each rainfall, the covering for this product must be restored, which means recovering several times during the season to prevent infection. If the leaves are slightly infected, it is still possible to stem the disease with treatment. But if the disease spreads throughout the grapevine, the harvest will be lost. Hence, this treatment can prevent or contain an ongoing infection, but not cure it. Powdery mildew is the second typical disease of the grapevine. The development of this disease occurs predominantly in environmental conditions where the temperature and relative humidity are moderate. Wind helps spread this disease, while heavy rains have a contrasting effect because they leach mildew from the leaves. The chemical defense against powdery mildew is traditionally made with powdered sulfur. Even this treatment should be carried out repeatedly during the growing season. If this disease affects most of the grapevine leaves, the harvest will be lost. *Botrytis*, usually called grey mildew, causes the most serious damage in vineyards worldwide. This disease develops rapidly during and after the ripening of the grapes and can significantly damage the harvest. Two systematic preventive treatments made of synthetic or natural phytosanitary products are used to fight grey mildew.

Vineyard treatments are typically made six to eight times per year. Depending on the climate, i.e. temperature and rainfall, these treatments are made at intervals of 10 to 15 days. Ticino Cantonal legislation states that the last synthetic pesticide treatments against downy and powdery mildew must be made no later than August 15. The last synthetic pesticide treatment for botrytis must be done by July 31. These laws were instituted to avoid pesticide residues on grapes. However, if August is very rainy, the last part of the leaf apparatus but not the grape may be treated with natural phytosanitary products (copper and sulfur) only. These regulations are prescribed all over Europe, but not all follow the same timetable.

The costs of these phytosanitary treatments vary depending on the size of the surface to be treated. On average, 3 kg of each specific phytosanitary product are consumed per hectare. The treatment against a specific disease costs hundreds of CHF per hectare a year. Hence, to produce about 10,000 kg of grapes, winegrowers will spend from 3,000 to 5,000 CHF only on phytosanitary products. The labor costs to treat the vineyard do not impact production costs too much. Generally, to treat an acre of vineyard requires half a day's work by one person. The maximum production of vine grapes per hectare is 10,000 kg of grapes a year (Swiss ordering specifies that one can produce a maximum of one kilogram of grapes per linear meter). As a rule, 10,000 kg of harvested grapes produce, on average, 10,000 bottles of wine. In Canton Ticino Merlot is sold at 4 CHF per kg.

The most critical decision for the management of a vineyard concerns the date of the first treatment of the season. To optimize this choice, winegrowers can access a free online service [www.agrometeo.ch](http://www.agrometeo.ch). This Web platform was created as a tool to support farmers' decisions on phytosanitary treatments, and is currently managed by Agroscope, a research organization that is part of the Federal Office of Agriculture. Agroscope consists of three research centers: the headquarters is located in Changins-Wädenswil (Western Switzerland), a subsection is located in Zurich (Northeast of Switzerland), and another subsection in Cadenazzo (Southern Switzerland). The main task of these research centers is to conduct research for the Federal Office for Agriculture and to provide useful information to the cultivators.

Agrometeo.ch is a Web site that provides useful information for the management of phytosanitary problems. It provides updated data of the temperature, humidity, and rainfall measured through different stations in different parts of Switzerland. As described in Figure 6.4, the meteorological data acquired from the weather stations are also integrated into two vineyard disease risk-prediction models. The idea of these prediction models is to help winegrowers reduce the number of phytosanitary treatments. The two disease prediction models currently running are for downy mildew and grapevine moths (a moth known for the severe damage it causes by eating the grapes). A prediction model for powdery mildew is currently under development.

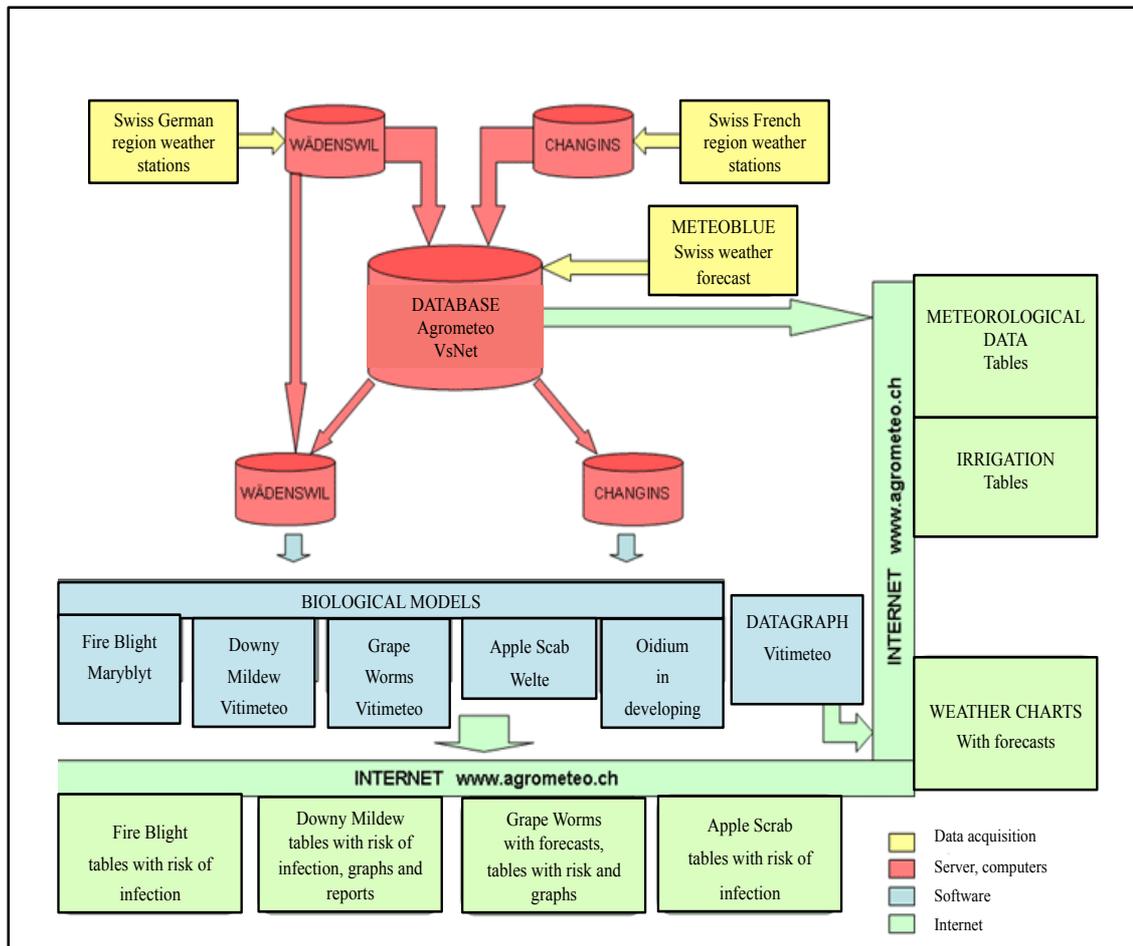
The current network of measuring stations includes about 50 in Western Switzerland, eight in Canton Ticino (Southern Switzerland), and more than 80 in the Swiss German region. Two foreign companies, Campbell<sup>20</sup> and Lufft<sup>21</sup> supplied the measuring stations that collect and transmit daily values measured at 10-minute intervals over the GSM network. Agroscope, which developed the software for modeling the collected data, is concerned only with data management. The stations belong instead to regional associations of winegrowers and winemakers. Each of these stations costs 14,000 CHF. The responsibility for station maintenance falls on the owners who, by contract, commit themselves to regularly monitor the station. According to the people working for Agrometo.ch, this is fundamental to ensure the reliability of long-term data. An agreement with suppliers of measuring stations establishes that in the case of complex breakdowns, which the owners of weather stations cannot handle, the same suppliers will intervene to fix the problem.

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<sup>20</sup> Campbell is an American company that has been designing, manufacturing, and supplying customized data acquisition, measurement, and control systems since 1974.

<sup>21</sup> Lufft, a German company founded in 1881, deals worldwide with the production of climatological measuring equipment.

Figure 6.4 Flow Chart: from data acquisition to disease risk prediction



(Source: Adapted from www.agrometeo.ch)

According to the winegrower we interviewed, “The eight stations placed in Ticino are not enough and too far from our vineyards to be useful for our decisions. The decisions I made about when and how to mark the vineyard with treatments are based only on the meteorological observations I made ... I do not even measure temperature or humidity.” That is, in the vine-growing business weather data on a large scale is of little use in deciding how to intervene in specific vineyards. “What I think is that to further increase

the efficiency of the data delivered by Agrometeo, a higher coverage of weather stations would be required. As far as I know the Agrometeo service has expanded in Alto Adige, and perhaps also in Austria and Germany.” The high costs and complexity in running the weather stations appear to be major obstacles to their spread: “In Ticino, vineyards are managed by many hobbyists, and it is not easy explaining to a hobbyist how to use the Agrometeo.ch Web site and to follow the indications instead of doing treatments every second Saturday. For professionals it is certainly much easier to recognize the advantages in using Agrometeo.ch’s services.”

As previously seen, since 2008, when FD reappeared in Swiss vineyards, Agroscope became concerned with finding safe and effective FD control methods. In Switzerland FD is classified as a quarantine organism<sup>22</sup>. Swiss legislation states that the Federal phytosanitary protection inspectorates in Changins and in Wädenswil (Agroscope), in close collaboration with other federal and cantonal phytosanitary protection centers, are obliged to supervise the state of health of the territory and to verify the presence of quarantine pests that can seriously damage agriculture, such as FD<sup>23</sup>. The responsibility of monitoring the presence of FD is not left only to the various federal and cantonal phytosanitary protection centers, but also to single winegrowers who are required to report any suspected cases of FD to the competence centers. Moreover, the grapevines that manifest symptoms of the disease must be compulsorily grubbed up.

FD is a virus transported by an insect called *Scaphoideus Titanus*, which infects the grapevines by stinging them. The problem is that it is not possible to counteract the virus, as with other typical fungal diseases of the vineyard, and the only way to fight this disease is to stop it spreading by using an insecticide after the insect eggs are detected.

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<sup>22</sup> "Quarantine" organisms is that group of parasites of plant diseases considered particularly dangerous for the damage they can cause to agriculture or to the environment because they are not yet widespread in a defined territory.

<sup>23</sup> Regarding phytosanitary resolutions, Switzerland is related to the EU that establishes the list of quarantine organisms. At the European level, phytosanitary coordination actions are provided by the European and Mediterranean Plant Protection Organization (EPPO).

Since 2010, Swiss law has made the fight against the insect vector of FD compulsory in contaminated vineyards and surrounding areas (Federal Ordinance on Phytosanitary Protection (OPP) of 27 October 2010). The various cantonal phytosanitary protection services indicate the right periods to treat FD. In Ticino this decision, when to treat FD, is communicated to winegrowers by the Phytosanitary Protection Service of Cadenazzo, which, in collaboration with Agroscope, executes targeted controls. To monitor the development of FD, the Ticino cantonal phytosanitary protection center has placed some sensors that detect temperature, a factor that seems to favor the development of the insect. A mathematical model then processes the data collected on the temperature trends and forecasts the beginning of the egg-laying period (generally between May and June). The IT platform used by the central plant in Ticino to interface with the data collected is that developed by SafeVine. However, as a model makes the projections, a person is required to verify the presence of the eggs in the vineyard. The data empirically observed are then transferred to the model that further develops new estimates on egg laying. These data exchanges will last as long as human observation does not confirm the presence of eggs. Once the presence of the eggs is verified, it becomes compulsory to intervene with the first two treatments of the vines. The model, according to data entered by the observers, will then indicate if it is necessary to intervene with a third treatment. However, this third treatment will become mandatory only after phytosanitary protection services empirically verify the presence of adult insects on the vines. These three treatments, however, do not guarantee eradication of the disease. In fact, despite elimination of the insects, the disease often persists. For researchers, the mechanism underlying the spread of the disease is still unclear. Recently it has been suggested that *Scaphoideus Titanus* may not be the only carrier of FD. According to the winegrower of a well-known farm near Lugano-Ticino that produces and retails about 25,000-30,000 bottles of wine a year, “What we know for sure is that *Scaphoideus Titanus* is the vector of FD disease, but we don’t know why the disease continues to occur despite the insect being killed. Therefore, I think the technology developed by SafeVine cannot help winegrowers defeat the disease, but it can help the winegrower to decide when to treat the vineyard against the insect. But this help has

already been given by cantonal phytosanitary protection services. Since I started working in this four-hectare vineyard, i.e., since 2009, every year I found only two to three strains infected by FD. However, I know some winegrowers that had to uproot their entire vineyard because of FD. And since there is no insurance against this disease, the financial loss can be enormous. Therefore, I see the SafeVine technology as a potentially useful solution only for a vineyard that has been strongly affected by FD in the past.”

The expert interviewed made it clear that this technology cannot replace the observations made in the field by winegrowers, who are always a little indisposed towards innovation and change, especially when it involves putting some sensors in the vineyards to solve the problem. Moreover, he also explained that today no winegrower goes to monitor the presence of the insect because it is being monitored by the cantonal phytosanitary protection services. Therefore, the perception is that installing such technology would only give them more work: “If the technology is free, and the same people who offer the solution are in charge of installing the sensors and providing maintenance, and it is not my duty to check for the presence of the insect, then I can begin to evaluate the usefulness of this technology. The parties who should take the first steps and test the technology are the cantonal phytosanitary protection services. In fact, winegrowers trust the models currently offered by Agrometeo because they have been previously tested. In my opinion, the potential customer of this technology is not so much the private winegrower, but the cantonal phytosanitary protection services because FD is a quarantine organism and they are responsible for telling us when to make the treatments.”

## 6.2 EKOBIKE

### *CASE SUMMARY*

This business venture began formally in the urban district of Paradiso, Lugano, in August 2005, when three partners who shared a passion for motorcycles, Claudio D., Massimo M., and Alessandro T., decided to launch a company called Division 48. The company aimed to import, market, produce, and sell two-wheeled vehicles with electric motors for sport or city use. The original goal of this start-up was to import an electric motorcycle from the United States and to develop high-performance electric motorbikes. The partners decided to develop an electric motocross bike, initially acquired from an Italian supplier that specialized in the production of motorcycle frames, a frame complete with forks, wheels, handlebars, and brakes. The remaining components, a rechargeable battery (Swiss company), electric motor (English), motor controller (United States), and electrical system (provided by a local company), were assembled by two workers based in Lugano-Paradiso. In April 2006, after almost a year of R&D, the small company began to produce its first electric motocross model, the EKO1 Track, an electric battery-powered sports motorcycle for freestyle excursions or city use. To promote the EKO1 Track effectively, Ekobike set up Ekopark in August 2006, which contained indoor and outdoor tracks for practicing motocross. By the spring of 2007, sales were not going according to plan and Ekopark was about to close. So, in April 2007, the team decided to design an electric scooter and to start a new company: Ekobike SA, which was engaged in the production and marketing of electric scooters for city use. However, in November 2011, since electric motocross bikes and scooters were not getting off the ground, they decided to launch another enterprise, Ekobike Engineering Sagl, with the goal of finding new partners to develop the designs and, above all, to manufacture the products. Ekobike Engineering would therefore remain active in designing electric motorcycles. This case analysis is focused on investigating the need to interface resources with suppliers when a company is developing a new solution.

## 6.2.1 FROM THE IDEA TO THE VENTURE

### THE ORIGINAL IDEA

The idea of developing an electric motocross bike was the result of the constant increase in the price of fuel and new European standards promoting environmental protection. In Switzerland, as in the rest of Europe, it was becoming harder to organize motocross and supermoto competitions due to the noise and air pollution caused by such events. The desire therefore arose to develop electric motocross bikes that were economically and ecologically compatible; they would be capable of being used on an everyday basis on city streets and would also make it possible to continue to organize motocross competitions.

How could an electric motorcycle be a valid response to the increase in fuel prices and environmental problems, without compromising performance and the spirit of a typically “performance-based” and emotional means of transport? This was the question the three friends pondered when they decided to launch a new enterprise. The process of starting a new business began formally in the summer of 2005: Claudio D. (at the time director of Cagiva Motor Suisse, a Swiss importer of Cagiva, MV Augusta, and Husqvarna bikes), became CEO of the new venture; Alessandro T., who, thanks to contacts made during his earlier work selling technical parts for motorcycles, became responsible for buying and selling; and Massimo M., thanks to his IT knowledge, took charge of communication and marketing. All three left their jobs in order to focus completely on developing their “product idea,” namely an electrical motocross bike. They therefore decided to found Division 48 and registered the company in the Ticino canton in August 2005. They began to establish the starting blocks for launching their new business and looking for suppliers.

## THE BUSINESS IDEA AND STARTING UP

Starting with the idea of producing an electric motorbike, the three partners began by testing a few products and by designing and developing a generic motocross bike.

The partners considered the possibility of building an electric motocross bike for use not only in motocross competitions and events, but also as a valid alternative for those who use their bikes as a means of transport in the city and who have one eye on the environment and the cost of maintenance. Claudio D. was convinced that even “urban” bikers were becoming more aware of environmental matters and the constant increase in the cost of fuel. He was certain an electric motorcycle that was more economical and ecological than a petrol bike would arouse the interest of motocross enthusiasts and of city bikers: the idea, therefore, was to try to conceive of a product that was suitable for dual use.

Factors that would improve the distribution of the electric motorbike, not only as an alternative to petrol-driven bikes but also as a substitute for a car, were therefore linked to lower maintenance costs and other economic and logistical benefits. In particular, the rechargeable battery, lasting 30 minutes, cost 0.50 CHF compared to 1.70 CHF per liter for 95-octane fuel. Another incentive to promote the distribution of an electric motorbike was the lack of parking for cars and the cost. Road tax on electric motorbikes was much lower than that applied to petrol-driven bikes and cars, a factor which could also promote sales. Finally, state subsidies for electric vehicle owners would later encourage the distribution of such vehicles.

In addition to these ecological and economic arguments, Claudio D. and his team believed their electric bike could satisfy emotional needs. Claudio D. was convinced that electric means of transportation available on the market at the time created no sort of emotion: the inability of electric vehicles to compete with traditional motorcycles and to transmit certain emotions effectively was a factor that caused most attempts to market electric motorbikes and scooters to fail. Claudio D.’s interpretation was as follows: “It has always been difficult to get across the idea of an electric means of transport since people are used to associating this type of vehicle with a lower level of autonomy and

performance than traditional motorcycles. Furthermore, electric motors produced thus far have been unable to arouse in users the emotions that engine-driven bikes have typically been able to generate. To overcome the reasons that have led to the failure of all attempts to bring electric motorcycles and scooters onto the market, we wanted to build a bike that was able to guarantee emotions for the user that have never before been experienced with electric motorcycles.” The special attention that Division 48 paid to performance would lead to the creation of an eco-conscious electric motorbike capable of stimulating emotions in users; this aspect, according to the founders, would guarantee success over their competitors.

In August 2005, when Division 48 was recorded in the commercial register, the three partners began to design the EKO1 Track, an innovative electric motocross bike, with the aim of producing one hundred. To build an electric motocross bike, five basic parts are required: the frame, the engine, the motor controller, the electrical system, and the battery. Having formally established the new company, the three founders started to look for suppliers of the five components and to plan how to coordinate the development of electric motocross bikes using this basic part.

## 6.2.2 THE VENTURE

### THE BUSINESS MODEL

The motorcycle Division 48 wanted to produce was classified according to EU standards as an unregistered off-road vehicle, for use exclusively on private land or appropriate tracks such as motocross circuits. The bike emitted no exhaust fumes and made very little noise, granting it impunity from regulations restricting off-road access. Obtaining EU approval, according to Claudio D., was not an obstacle and fast approval was expected since the level of noise and air pollution produced by the motorbike clearly did not reach the limits. However, there was concern that there may be complications caused by the electromagnetic field produced by the motorcycle, which exceeded expected

limits. In fact, the proximity of an electric motor controller might interfere with the motorcycle's motor controller, causing unexpected fluctuations that would accelerate or decelerate the bike suddenly and, in turn, lead to interference with the electrical system. In any case, if changes were required to turn the motocross into a city bike, these arrangements should not have been an obstacle for production. According to Claudio D.'s predictions, "Our motocross will probably be approved in the second quarter of 2007 for city use." European approval would apply to all European countries as well as the US, while to get the motorcycle onto Swiss streets it would be necessary to carry out other tests stipulated by national highway legislation. Table 6.5 (below) details the features of the electric motocross bike.

Table 6.5 The electric motocross bike features

Maximum weight: 85 kg	Noise level: 45Db
power: 18 CV	wheel diameter: 18"
battery life: ~30 minutes	front disc diameter: 220 mm
average battery charge: 60 minutes	rear disc diameter: 200 mm
battery change: <1 minute	estimated price: 8,800 CHF

The timeliness of Division 48's entry onto the market with a previously approved electric motorcycle meant that the company could beat the competition. According to Claudio D.'s analysis, at the time, i.e., between 2005 and 2007, there were still no potential competitors on the market who were able to provide an electric motocross bike whose performance was equal to, or greater than, that of the EKO1 Track. Only Blade, an American producer of a variety of electric products, could be considered a potential competitor. However, Blade was not considered a dangerous adversary since the electric bike it produced did not have the same level of performance as the EKO1 Track.

Claudio D. explained: “The technology was already in place but not with the level of perfection that we had reached and therefore was not applicable to this type of product; this was, therefore, a new product on the market.” Moreover, according to Claudio D.’s estimates, the motorcycles proposed by potential rivals would not have passed the approval tests for use as street vehicles, at least not in the time predicted for approval of the EKO1 Track, i.e., the second quarter of 2007. However, the start-up was aware of the fact that other competitors could emerge, even in a short time, but this would not have been a problem as it would have led to useful efforts for the development of new and better solutions.

## PRODUCT DEVELOPMENT AND TESTING

The bike was manufactured by assembling parts available on the market; in fact, the five parts had already been used for various purposes in the industrial sector. Even if the cooperation forged with suppliers did not lead to the development of a radically innovative product, relationships were, however, formed that primarily made it possible to adapt the product to the technical requirements of Division 48. Only later did Division 48 develop closer cooperation with the battery supplier to create a product innovation of a new type of lithium ion battery.

## FRAME: RELATIONSHIP WITH CH RACING

The frame is an essential component of any means of transport; it is the load-bearing structure that defines the form and position of various parts of the motorcycle. The company that provided the frame and the forks, swing arms, wheels, and braking system to make the EKO1 Track was CH Racing in Varese. In other words, this provider supplied the motorcycle structure, without the engine, batteries, motor controller, or electrical system. The main activity of CH Racing was the production and marketing of mini motocross bikes with combustion engines (with a maximum speed limit of 50 km/h) throughout Europe. The company sold about 150 engines annually in Germany,

80 in France, 200 in Italy, and 200 in Switzerland. Alongside this, the company specialized in the production and marketing of frames and other units for small-cylinder motorbikes.

Claudio D. had known this supplier for six years, from the time he imported and marketed 50 cc mini motocross bikes in Switzerland that were made by CH Racing. The relationship with this supplier, therefore, did not emerge after the birth of the new venture, but was a continuation of a relationship that had begun earlier. Predicting that from October 2007 it would no longer be possible to import this type of motorbike to Switzerland due to changes in the law, CH Racing prepared to abandon one of the largest markets in terms of the volume of sales. Taking into account the reference market's ever-increasing awareness of environmental problems, the company predicted a subsequent drop in sales of petrol-driven bikes. With this in mind, CH Racing saw that production for the three remaining countries would not be profitable enough, meaning it became useful to work with Division 48 to acquire new market outlets.

The frame of the EKO1 Track motorbike made by CH Racing, based on an existing model, was adapted to the client's specific requirements; the cost of the operation was about 45,000 CHF. If an order had been placed for at least 100 frames and not just 40, due to a decrease in predicted sales, Division 48 could have benefited from a lower rate. The development of the relationship with this supplier made it possible to integrate the production and processing skills of the CH Racing team, which had been acquired after many years on the small-cylinder motorcycle market, allowing Division 48 to identify the most efficient solutions in terms of time, cost, and product quality. Claudio D. provided an interpretation of the importance of this type of close relationship with CH Racing. He said cooperation with a family business like CH Racing had been much more efficient and effective than with larger companies with which the participation and involvement of suppliers had been practically non-existent.

## ELECTRICAL SYSTEM: RELATIONSHIP WITH PERISO

The electrical system is the set of machines, equipment, and connections that enable the production, transformation, transmission, distribution, and use of electricity. The company that provided Division 48 with the electrical system was Periso, which was also located in the Ticino canton and was active on the international market, specializing in the design and construction of electro technical parts for industrial and professional use. Division 48 became aware of Periso accidentally after seeing an article in a specialist sector magazine. A relationship quickly developed with this supplier that made it possible to design and develop an ad hoc electrical system for the EKO1 Track. In fact, based on plans the client provided, Periso designed and developed an electrical system suited to the technical characteristics of the motorbike in order to make it suitable for assembly. The agreement with Periso was ideal and the cooperation was worthwhile; Division 48 continues to enjoy a close relationship with this supplier.

## MOTOR CONTROLLER: RELATIONSHIP WITH ALLTRAX

Alltrax is the company that provided the electric motor controller, namely the electronic device capable of detecting the engine's performance conditions and changing the functioning of the part in question. Alltrax, an American company based in Oregon, was founded in 1996 by two young engineers. In 2007, with about 30 employees, it developed, produced, and sold electric motor controllers (high-power motor controllers for electric racing vehicles) for export all around the world. Division 48 discovered Alltrax just as the latter was considering exporting electric motorcycles from the US. Division 48 decided to purchase Alltrax motor controllers because this was the only company able to meet EKO1 Track's technical requirements. Cooperation between the two companies developed quickly, and the standard product was finalized and optimized on an industrial scale, providing the best technical and economic results for Division 48. There were no great difficulties in jointly finding the best product solution; therefore, on a practical level, the motor controller had no compatibility problems. Alltrax, which

produced roughly 3,000 motor controllers per year, was considered the best provider of electrical motor controllers, and Division 48, predicting an annual production rate of 100 motorbikes, sought to maintain a stable, long-term relationship with this provider.

#### BATTERY: RELATIONSHIP WITH ERUN

To power the electric motors, the first 40 EKO1 Track models Division 48 produced used conventional lead batteries, which were the only type available at the time. However, this type of battery did not feature in Division 48's plans, as it was already developing and testing a prototype lithium polymer battery in cooperation with the same supplier of lead batteries. The lead battery supplier, which also worked on designing and producing a new type of battery, was Erun, located at Yverdon-les-Bains.

Lithium batteries per se were not new. In fact, they were already used in some types of vehicle (e.g. Iveco electric cars) and various electric boats in Germany and France. Other prototypes of means of transport, such as Swisspirit (a solar-powered car) or "SAM," a three-wheeled electric vehicle created by the Swiss company Cree, as well as Division 48's electric motorbike, were in the experimental phases. Thus, with the Swiss company based in Yverdon-les-Bains, close cooperation emerged with the aim of developing and designing a lithium polymer battery that met the specific requirements of Division 48 and was suitable for use in the EKO1 Track. In this case, Division 48 and Erun sought to develop a system of battery charging and de-charging that could be managed electronically. It was necessary to develop an electronic system that stabilized as the battery charged and de-charged, since otherwise there would be a risk of damaging the lithium polymer once it had lost its properties. Compared to lead batteries, the battery in question had the advantage of performing better at any temperature. In fact, whether at +60° or -20°, it maintained its properties, while the lead battery halved its properties between +15° and 0°. Lithium batteries, in addition to being much lighter, had a longer half-life: 1,200 recharge cycles, compared to 150 for conventional lead batteries. With the latter, EKO1 Track had a battery life on the road (i.e. "economy" setting) of approximately 30 minutes, while the lithium battery lasted almost three hours.

For sports use (motocross circuit setting), the difference was from eight minutes to 40 minutes of battery life. With this new battery the EKO1 Track would be able to run on the economy setting for 60-70 km. Despite the predicted 50% decrease in lithium battery prices when Korean lithium suppliers entered the Chinese-dominated market, the new batteries would cost four to five times more than lead batteries. From this perspective, the most expensive part of the whole motorbike, at roughly two-thirds of the overall cost, was the lithium polymer battery. According to Claudio D.'s estimates, a few months of developing and testing would still be required for design, after which the new lithium polymer battery would be able to enter into production and be mounted onto the new EKO1 Track bikes.

If the timetable had been followed, Division 48 would have become the only company on the Swiss market that adopted lithium polymer batteries to power its electric motorbikes. Division 48, hoping to produce around 100 electric bikes, predicted that it would become the main client of Erun, and more besides; an agreement was made with Erun to distribute and market new lithium batteries in the Ticino canton and in Italy.

#### ENGINES: RELATIONSHIP WITH LYNCH

The identification of an engine supplier for the EKO1 Track was not simple due to the range of offers on the market. To find the most suitable engine, extensive research was carried out, including over the Internet, which led to the identification of four possible suppliers. To determine which of these four would be able to supply the engine that was best suited to the technical specifications of the EKO1 Track, tests were required. The most economical engine among those tested (at approximately 350 EUR) had never been used in motocross, and, in addition to other functional problems caused by overheating, it wore out quickly. Another engine that was tested (priced at about 625 EUR) was not suitable: this model also broke shortly after ignition. The third engine available on the market, which was a similar size to the one produced by the fourth supplier, was one-third less powerful than the Lynch engines. The engine that best responded to the tests was made by the English firm, Lynch Motor Company Ltd., which was named after the

inventor of a type of electric motor, Cedric Lynch. The English company produced three types of electric motor, which differed in size but not in integrated technology. These were usually used in go-karts, golf carts, and for other industrial uses. Although Lynch's production units were located in India (where the costs of production were lower), the price of their electric engines was on average four times higher than their competitors. The high price of Lynch engines, according to Claudio D., was justified by the greater use of copper: a very important element in the functioning of the electric motor because, thanks to the high level of electric conduction, it reduced the energy loss and overheating, a factor that had caused the other electric motors that were tested to break. This also meant that, because of the lower temperature, the engine lasted longer and did not require as much use of fans, which was not inconsiderable owing to the smaller dimensions of the motocross bike.

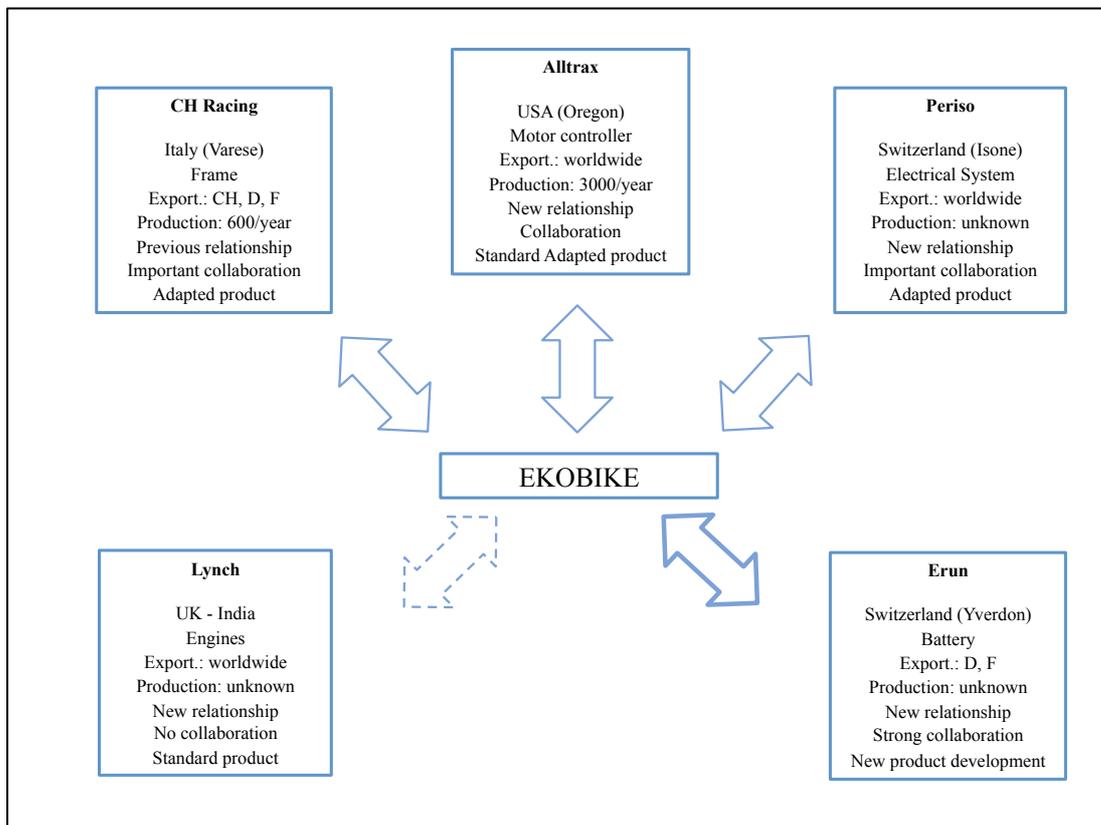
After two years of cooperation with Lynch and after purchasing 40 electric engines, Division 48 began a functional relationship with this supplier with the aim of buying and selling electric motors. In fact, there was no cooperation between the two companies in terms of agreeing to requests for technical changes to the engines they made: the electric engine provided for the EKO1 Track was therefore a standard product and was neither developed nor changed ad hoc. However, though the relation did not develop through close cooperation, Claudio D. believed Division 48 had become one of their most important clients.

## FORMS OF COOPERATION AND ADAPTATION

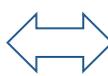
Division 48, in building a motorcycle, acquired one of the five closed-box parts. In other words, regarding the electric engine, there was no desire on the supplier's part to adapt the product to Division 48's requirements. This meant the company, in one case in five, could not benefit from any cooperation to make the product ad hoc on the part of the supplier. Relationships developed with the suppliers, as shown in Figure 6.6, concerning the four other parts – the frame, electrical system, motor controller, and battery – enabled close collaboration that made it possible to adapt the three elements to

the technical requirements of the electric motocross bike. There was no substantial cooperation with any of the five suppliers that led to the development of radical product innovation, but relationships were formed that led mainly to product adaptation. Only with Erun, the battery supplier, did close cooperation develop, allowing the design and manufacture to be in line with the new product, but this product was still in the future.

Figure 6.6 Supplier relationships



Note: Arrows indicate the supplier's level of adaptation

-  : High level of adaptation
-  : Mean level of adaptation
-  : No adaptation

## COMPATIBILITY AND TESTING

Of the five suppliers, four did not want to guarantee the correct functioning of the product once delivered and used for the construction of the motorcycle. The factor that most compromised the project, therefore, was the coordinated assembly and functioning of all five parts and the interfaces between them. Ideally, to better compare the quality and compatibility of the parts of the electric motorbike, the Division 48 team wanted to be able to test the products of other suppliers. However, testing whether other products on the market were more or less compatible would have required capital that the company did not have. In fact, of the various manufacturers contacted, none was in favor of providing free samples for compatibility tests. Uncertainty about the compatibility of the various parts considerably affected the development time for the EKO1 Track. Claudio D. commented, “Those who produce engines are not interested in providing an electric motor controller to make it work. The same applies to those who manufacture the electrical system or the battery. The suppliers sell their own products and guarantee performance but not compatibility with other parts. We therefore had to improvise with a number of situations.” The main problem for Division 48 was therefore the assembly and interfaces of various parts in order for them to work together. Division 48 spent the first 12 months testing compatibility, a year in which many resources were invested with the aim of identifying the best parts.

In 2005, with the suppliers found and the parts conceived and designed, there were two possible initial strategies for the production of the new electric motocross bikes. The first possibility was to use technology developed with the parts studied for EKO1 Track at motorbike manufacturing sites, in order to enable cooperation when carrying out the project. But the manufacturers contacted showed no interest in this type of cooperation. An attempt at this type of cooperation was initiated with Verlicchi, an Italian company that specialized in designing and building steel and light-alloy structures on a large scale for clients such as Honda, Ducati, and BMW in the motorcycle and bicycle sector. However, it was thought that this solution would not only have meant changing the frame supplier but would also have increased costs by too much. Verlicchi

asked for approximately 150,000 CHF to develop the initial design and to produce a frame conceived specifically using the parts designed by Division 48. With this solution being too costly, the start-up opted for a different strategy: assembling all the parts at their own site, where the Division 48 offices were located. Massimo M., head of communication and marketing, explained that, “Since the parts were delivered ready for assembly, we did the assembling of the engine, the battery, the motor controller, and the electrical system on the frame.” Understandably, since the three partners had no specific technical or constructional skills, they decided to employ two full-time mechanics. The initial prototype, designed by the three partners and built by the two employees, was made at the Lugano site in April 2006.

## CUSTOMER RELATIONSHIPS

At that time, in the summer of 2006, after producing the first bikes, Division 48 did not yet have an accurate analysis of the potential market, let alone a communication and marketing strategy, but it decided to publish a few adverts in English and German magazines to present the product to what should theoretically have been the reference market, namely motocross enthusiasts or competitors, bikers who were aware of environmental problems and those who were enthusiastic about motors in general. Even without developing a real marketing plan, the three partners were certain about promoting themselves and making the market aware of their company and their product by creating a reference point and contact for motocross enthusiasts. With this in mind, and also to test the EKO1 Track, in August 2006 they decided to set up a motorcycle circuit called Ekopark. The park would offer the chance of using either an indoor motocross track that would be accessible all year round or an outdoor track that could be used when the weather was favorable. Inside there would be a bar with a raised area and stands. Fees would range from 20 CHF to 100 CHF, depending on the number of laps. Discounts were envisaged for under-14s and groups of more than five people. Electric motorcycles made by Division 48 would be available for sale at the park. As well as developing electric motocross bikes, the start-up company was busy managing the park

itself. In fact, managing the whole park was entrusted only to the promoters themselves, without employing any external staff. The park, which opened in August 2006, welcomed visitors five days a week: Wednesday, Thursday, and Friday, from 6 pm to 10 pm, and Saturday, Sunday, and public holidays from 2 pm to 10 pm. Despite good progress at the park, it was closed for good in May 2007 due to a lack of time and interest from the promoters in managing the park and the inability to take on external staff, which would have been too expensive.

Having closed the park, Division 48 had the option of trying to enter the business-to-business market with the aim of identifying clients that could purchase more units and not focus only on a large number of clients who would purchase a single bike for personal use. Having established that the strength of the electric motorcycle lay in its low environmental impact and the enjoyment of driving it, the EKO1 Track began to be associated with a non-urban landscape and with the opportunity for use during leisure time and for fun. Therefore, Division 48 believed that motorcycling excursions were an area with considerable development potential. In fact, they considered trying to promote the sale of electric bikes by suggesting other contexts for use, such as mountain trips. To achieve this, says D., it would be enough to contact a few ski resort or amusement park managers and put forward their idea of renting out the motorbikes during the summer months when the ski tows were not in use. The choice of combining the motorbike with a trip would be in the spirit with which the product was created and would highlight its uniqueness. According to Claudio D., “On the one hand we could say that the EKO1 Track was born and grew along with Ekopark, a place where enthusiasts as well as those with a mere interest could test motorcycles and the thrill of various experiences; on the other hand, there was no need to neglect the natural appeal of environmentally compatible outdoor activity.”

Between April 2006 and the beginning of 2007, 40 EKO1 Track bikes were produced, half of which were made available at Ekopark, while the other 20 were sold to private clients (seven in Austria, eight in Italy, three in Switzerland, and two in America). Apart from one of the two American clients, who knew Claudio D. personally, the others contacted the company after coming across the Web site. In fact, Division 48 had not

envisaged any distribution channels other than sales directly to private clients; the whole activity required for the product to reach the final customer was thus limited to personal selling. Since no new clients came forward with the intention of buying other EKO1 Track bikes by the beginning of 2007, production came to a halt. However, the company received a series of requests from clients interested in the new motorcycle powered by a lithium battery. The Division 48 team was therefore convinced that with the presentation of the new battery they could sell larger numbers of the motorbike. Claudio D. elaborated, “There are few people willing to buy a motorcycle costing more than 8,000 CHF that has limited battery life, but we have various clients who are waiting for us to show the latest generation of battery.”

## VENTURE DEVELOPMENT AND A NEW PRODUCT

Despite the imminent closure of the park and the smaller number of motorcycles produced, the three partners continued to believe electric vehicles represented the future of the two-wheel market, and embarked on designing an electric scooter. The idea of entering the scooter business began to take the form with the creation in April 2007 of a new company, Ekobike SA, aimed at developing this new product and promoting sales of it to obtain a greater share of the market. In June 2009, two years after the new company was founded, Division 48 ceased its activity.

The clear conviction that the increase in fuel prices and the environmental impact would convince a large number of bikers to ‘convert’ to electric motors, led the Ekobike team to try to diversify their product. The idea was to develop an electric scooter based on the model already used for motocross. The three partners thought that for the development and production of an electric scooter it would have been sufficient to change the design slightly from that of the electric motocross. The scooter would therefore contain the same engine, motor controller, batteries, and electric system as the motocross bikes and only the frame would be altered. According to Claudio D.’s estimates, the electric scooter, with a new-generation lithium battery developed in cooperation with Erun, would be able to run for 200 km at an average speed of 50 km/h.

The scooter's longer battery life, compared to 30 minutes for the electric motorbike, was calculated based on the physical characteristics of the frame which, being larger and wider than the motocross, would be able to contain a greater number of batteries. There were no drastic changes to enter into production with the electric scooter, and with this strategic choice, the partners aimed for much higher sales volumes than for the almost specific electric motorcycle destined for 'outdoor' leisure use that was possibly inconvenient for city use.

In the past, various producers had attempted to develop electric scooters, such as the failed experiments of Malaguti, an Italian motorcycle company in business since 1930, which manufactured scooters weighing 150 kg that were not easy to handle and were too expensive. Almost 3,000 items remained unsold, stored in Malaguti warehouses. However, Ekobike ruled out the possibility of retrieving and adapting the unsold Malaguti frames, since it was a retrograde line and therefore too heavy and cumbersome. However, at the beginning of 2007, Ekobike tried another solution and asked Malaguti if it was interested in developing their concept of electric engines on another of their models of scooter that was apparently better suited to this type of change. The possibility of producing and selling an electric scooter with Malaguti came to naught, as the Italian company did not agree to cooperate<sup>24</sup>. Since then, the scooter has remained a "promise." The project was sidelined due to a lack of funds and problems regarding the need for investment to maintain production and marketing on a very large scale.

### 6.2.3 OUTCOMES AND FUTURE OUTLOOK

The new venture's initial provisions were for the production of a first batch of 100 electric motorbikes. However, since it was not easy to sell the bikes and there were few potential clients, the project ended after 40 items were produced. The founders believed the limited interest in electric motocross bikes as a functional and non-polluting

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<sup>24</sup>The Bologna firm Malaguti, which experienced difficulties for some time, terminated its activities entirely in 2012.

alternative in the field of two-wheeled transport was due to resistance to change from consumers. There were two reasons: the first was ongoing technical problems related to battery life, performance, and recharge times and the limited logistical possibilities of refueling in the street; the second problem, relating to the high price of this product, was the reality that the electric motorbikes' worth was not really understood and that the benefits they offered did not meet consumers' needs or preferences.

Even if in May 2007 the Ekopark closed, the idea of the park was not abandoned, but was transferred to Ekobike's German importer who, developing the concept under the name of Ekoparx, obtained good results in Germany. In particular, between 2007 and 2008, the Ekopark idea, as a place to practice off-road motor sports such as motocross was "sold" to the German importer of electric motorcycles produced by Ekobike, which was better able to develop the concept with apparent success. Ekobike further developed the idea of a franchise or joint venture to design and build private tracks for electric motorbikes. The franchise now runs under the name Ekoparx and is a brand name owned by Ekobike UK Ltd. It relates to a franchise of hire-and-ride activity centers each known as a Ekobike Park. The parks use only Ekobike electric motorcycles. The German importer had the idea of opening another 50-70 parks in Germany and Austria. Now, in 2012, several Ekoparx are operational and successful in Austria, Germany, and Spain.

Although the idea of developing and building electric motocross bikes and scooters did not seem to get out of the starting blocks, in November 2011 Ekobike Engineering Sagl was founded. The aim of this new company was to find additional partners to facilitate the industrialization of the electric motor. In fact, the proposal to develop the subsequent design of an electric scooter was approved by the Von Roll industrial group, one of Switzerland's long-established industrial companies that specializes in products and systems for power generation, transmission, and distribution. Von Roll, therefore, prior to marketing, had many of the characteristics of the electric scooter prototype that Ekobike had begun to develop in 2007; in fact, on various occasions during conferences and exhibitions, some designs and prototypes from the Von Roll firm had been presented.

## ECONOMIC OUTCOMES OF THE NEW VENTURE

An overview of the economic situation of the venture, by examining the approximate data of income and expenditure up to that date, June 2012, seems worthwhile to reflect on the exercise of this new venture and to see how it was near the break-even point.

The founder of Division 48, Claudio D., invested approximately 800,000 CHF to develop the EKO1 Track prototype and produce the first 40 items, without the support of private or institutional outside funding. The cost of the parts of the EKO1 Track alone amounted to 5,800 CHF, while the sales price was fixed at 8,800 CHF. It was necessary also to cover the costs of labor and other management costs. The cost of the entire Ekopark complex (excluding the 20 bikes made available to customers) was 60,000 CHF. This did not include staff expenditure as the park was managed directly by the promoters.

At the end of January 2007, the financial accounts submitted by the firm indicated that the total amount earned partly from the sale of 20 motorcycles and partly from entrance fees to the Ekopark was 152,860 CHF and that the overall costs amounted to 130,000 CHF. The company therefore reported a profit of 22,860 CHF. At the same time, the balance of the company's stock was 326,200 CHF, with a predicted amortization of approximately 118,700 CHF per year (estimated over three years).

Division 48 requested and received social subsidies from the cantonal administration, but did not raise any other funds, such as entrepreneurial awards, since the three partners submitted no requests.

## 6.3 CONCERTLAB

### *CASE SUMMARY*

Concertlab is a start-up company which was formed at the beginning of 2010 with the aim of creating a Web platform dedicated to music, which could be used interactively by artists, clubs, venues, fans, organizers, talent scouts, operators, and service providers, to facilitate interactions and communication between interested parties and to support mainly small, independent music groups.

Created along these lines, the Web platform would act also as a virtual agenda providing information on all musical events, subdivided by region and musical genre. It would also offer a search engine that would find information quickly on various actors and live music events in the musical world (artists, clubs, fans, schools, music shops, associations, recording studios, sound and light services, etc.).

Four young university students with a passion for music conceived of the idea, after discovering that there was no Web platform in the music sector that was constantly updated to meet the requirements of those involved in this business in real time.

In September 2011, the team entered the market with a beta version of the site Concertlab with the idea of revolutionizing communication and interaction between the parties, making it easier, faster, and more intuitive. However, despite conspicuous funding used for the technical improvement of the product, the venture did not take off. The case analysis investigates possible reasons for the limited success of the start-up to date and explores the apparent difficulties, in particular at the actor level.

### 6.3.1 FROM THE IDEA TO THE VENTURE

#### THE ORIGINAL IDEA

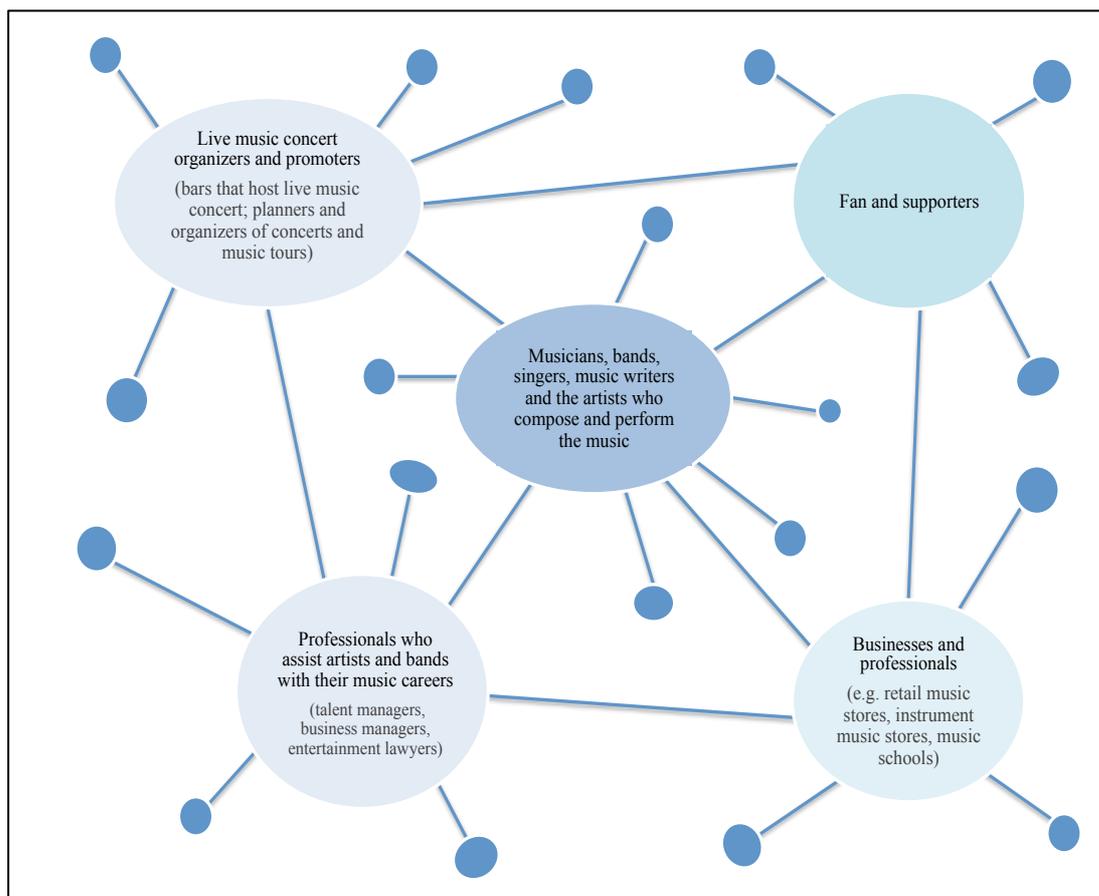
The initial idea began to take shape in the spring of 2009, when Marco A., a student specializing in information systems at the Faculty of Economics in Fribourg and Lausanne, considered the possibility of creating a Web platform dedicated to the music industry, a sector he knows very well because he played in a band on stages in Switzerland for over 10 years.

It was then, during his university studies (Strategic and Corporate IT), that Marco A. was able to understand how to transform his passion into a real business: “During this course the lecturer illustrated the case of a Japanese B2B company that produced T-shirts on demand. The company itself did not own anything but made use of external partners who carried out all the procedures, from supplying to printing the T-shirts.” From that experience Marco A. grasped the importance of brokerage and partners for the businesses in the musical industry too: “The world of music is not simply made up of artists, fans and venues, but an infinite number of partners are involved, such as recording studios, producers, promoters, etc.” He realized that in this particular market, there were still unmet needs for most of the people involved: “I had to find a solution to accelerate and facilitate the interactions between the actors of the music business.” The idea to provide a solution to this need arose from his desire: “As a member of an emerging band, I’ve noticed that a connecting system was missing and nobody, at that time, was offering an efficient solution. Therefore, I thought that by combining the new multimedia technologies with my music industry know-how and experience I would have been able to create something that really worked.”

## THE BUSINESS IDEA

Marco A. recognized the need for a solution to support the activities of young independent bands and facilitate interactions and communication between the various interested parties of the live music market. Accordingly, he decided to develop a Web platform to connect the various actors. As the music industry is a complex system comprising many different actors, businesses, and organizations, it became necessary to define some major categories of people operating within the live music industry and to understand their needs and how to meet them. The live music industry is composed of five major categories shown in Figure 6.7.

Figure 6.7 The main players in the live music network



To best meet specific customers' needs and to turn the idea of "connecting various music actors" into a business, Marco A. decided to develop a virtual agenda, called Concertlab, that would provide information on all musical events in Switzerland, according to region and musical genre. This agenda would be continually updated. He would also offer a search engine that would make it possible to add and quickly find information about various actors and live music events. The offer would be adapted to potential customers' specific needs. The initial idea was to develop four types of services for four different types of customers.

The first type of customers was young independent bands, musicians, singers, and artists, who usually promote and market themselves using only free services such as YouTube or other social media. The proposed solution aimed to support these customers, who included solo performers, singers, and bands without their own managers, in organizing and promoting themselves. In practice, the platform hoped to give them the possibility of uploading information, such as pictures, videos, demos, or descriptions of music genres, to promote themselves on the Web site and gain more visibility. This should have been a solution for bands and other live music performers to increase the exposure of their concerts and reach bigger audiences without investing too much time and money. Another idea was to offer the independent musicians and bands the opportunity of looking for live music concerts, pubs, bars, etc. at which they might perform.

Concertlab also wanted to reach out to fans and supporters, enabling them to browse through the platform and easily and quickly find information about the locations where their favorite artists would be performing. In practice, fans and supporters could use different filters; by date, by geographical area, by music genre etc., in order to find precise information about the different scheduled music events. The idea was to offer to fans and supporters the most comprehensive information database about all the live music happenings that until then had required specific research on different Web sites where such information was available. Fans and supporters could also access the latest news regarding preferred artists, discover new and emerging bands, or find detailed information about bands or artists by looking up their profiles.

Marco A. also intended to offer technical partners operating in the music market the opportunity to discover new talents. These technical partners would include promoters and organizers of live music concerts (i.e. those who bring musicians or bands to live music venues or organizers who help arrange live music happenings by delivering stage lighting, sound support, transportation, and other logistic activities). Marco. A also wanted to attract professionals who assist musicians with their music careers (e.g. artist managers who usually oversee all aspects of a musician's career in exchange for a percentage of the artist's income, or talent scouts who discover and promote new bands). This would help Concertlab identify emerging bands, singers, musicians, or other musical artists interested in performing in any live music space, and facilitate contact and interaction with them. By browsing through the Web site, live music venue organizers or talent scouts could check out, for example, profiles of bands or artists who had enrolled in the platform and had created a profile. Moreover, live music organizers or promoters could also promote themselves by generating a profile full of information, including the venues at which they staged music performances.

Music instrument stores or music schools could benefit from the services offered on the platform in still another way. The idea was to offer these players competing in the music industry the opportunity to become more visible and thus facilitate their contact with new customers. In practice, music stores and schools could generate a profile featuring the most important information, such as contacts and a short description of the kind of services or products offered. They could present themselves in a clear and intuitive way, thus increasing the possibility of being seen and approached by new potential customers.

The idea was to facilitate the process of finding information about live music bands and events. However, in becoming registered users, people could become more involved and linked to the live music community and more visible toward actors (especially clubs and bands) in the music arena by managing and updating the status of their user profiles. The more the user would be involved, the more helpful the content of the Web page would become. The idea was to be a collaborative agenda in the sense that the contents of the platform would be inserted and updated directly by users themselves.

The agenda would thus become auto-generated. Therefore, the main concern when starting a business activity based on this idea was to encourage the various players in the music industry to sign up on the Web site and get involved in updating the Web pages by adding information about the live music events happening, the performing artists, and so on.

According to the founders, the advantages of generating a profile on a music platform were numerous. Firstly, emerging live music bands, artists, and music venue organizers would become more visible to potential fans. Music venues are public spaces that offer live music happenings of all kinds; they range from concert halls to pubs, bars, art exhibitions, town fairs, etc. that host a variety of live music events. Another advantage would be that the music happening would be shown on the mobile agenda of Concertlab App for iPhone. Thirdly, with one click it would have been possible to make the live music events visible not only on the Concertlab platform but also in other diaries that did not require payment of fees, such as social networks (Facebook and Twitter).

This was the solution Marco A. had in mind and upon which he would have liked to build a start-up when he finished his university studies in September 2009 and returned to Ticino, determined to put his idea into practice. The first step in starting his business was to develop a business plan. He therefore enrolled in a workshop for future entrepreneurs, organized by the Swiss Commission for Technology and Innovation promotion (CTI). Having enjoyed the first workshop, he decided to take the second workshop designed to support nascent entrepreneurs, not only because of the course content but rather for the potential contacts the occasion would provide. Indeed, he said, “At that workshop I met many people from the entrepreneurial world, key figures who helped me in directing my business idea into a concrete business.”

## STARTING UP

In September 2010, one year after finishing his university studies and having taken part in the workshops for future entrepreneurs, Marco A. decided to start developing his new business. To put the entrepreneurial idea into practice, he sought colleagues who could

support him in all the activities that were not exactly in his area of expertise. Two of the three people he involved in his project and who became co-founders of Concertlab, Oscar M. and Martino P., were fellow students at university. The third, Mattia M., attended the workshops for future entrepreneurs together with Marco A. As they all shared a passion for music, it was not hard for Marco A. to convince his future partners to commit themselves to setting up a new business in the music sector.

Following their different school education and professional experience, the four founders decided to take different roles in the new venture. Marco A. took on the role of CEO (Chief Executive Officer) and decided to dedicate 60% of his time to manage the activities for setting-up the new business. For the remaining 40% he would continue to work as an IT consultant at an administrative office. Oscar M., who specialized in information systems, took on the role of CIO (Chief Information Officer) and would become responsible for the information technology and computer systems. He decided to dedicate 20% of his time to the new activity, while he would devote the remaining 80% of his time to his job as head of the IT department of a bank. Mattia M. took on the role of CTP (Chief Technology Officer) and as CTP he would become the project manager in charge of the implementation of technology systems. He decided to dedicate 20% of his working time to the new work, and spend the remaining 80% working as a project manager for an informatics company. Martino P., after studying economics and marketing, took on the role of CMO (Chief Marketing Officer), in which capacity he would be responsible for Concertlab's marketing and communication strategies. He decided to dedicate 20% of his working time to these new activities, while the remaining 80% of the time he would continue to work for a dental products company.

Being a start-up activity still in progress the four founders knew they would not receive a salary for an indefinite period. At that time, Marco A. was concerned that, "Fortunately at that time we were all able to dedicate part of our time to create the project but I knew it would be hard to find other colleagues who were able to work freely only for their passion for music." For Marco A. such a solution was clearly temporary.

The entry in the commercial register as a “limited liability company” formally constituted the new venture on December 22, 2010.

### 6.3.2 THE VENTURE

#### THE BUSINESS MODEL

After the team was formed at the end of 2010, the founders started to think about the business model and how to enter the market with their Web platform. Their initial idea was to stretch the introduction over one-and-a-half years in two separate phases. Once the beta version<sup>25</sup> of the Web platform was ready, it would become available for free. But access would be restricted to only some basic functions. In practice, during this first phase, which lasted about three months, users could register for free by creating a “Free Profile” subscription on the platform, and take advantage of a series of basic functions. This phase should have been focused on developing contacts with the largest possible number of potential users, i.e. live music venues, bars, artists, and event organizers. It would also be a period of testing to see whether there were any bugs in the software as well as other problems related to the performance of the Web platform.

The company planned to release the full version to the public in the second phase. This version would be subject to some charges. By paying an annual fee, users would be able to choose between two different profiles that would extend access to an increased number of functions, such as the option to synchronize their own status directly on other social network pages (i.e. Facebook or Twitter). The idea of waiting three months before proposing the full version of the Web platform was related to the potential entry of a competitor. Marco A. explained the intentions: “This two-phase strategy had two main objectives. The first was to initially acquire a sufficient number of potential customers

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<sup>25</sup> The beta is a pre-release version which is made available to a number of users who can test it, and eventually report to the manufacturer defects encountered. This facilitates the further development of the technology.

and fix possible software bugs. Offering the second set of functions for a fee was thought to reach our second objective, namely limiting the risk of imitation.”

Selling two different types of subscriptions and advertising space would allow Concertlab to work as a profitable business. In particular, the first subscription, called “Free Profile,” was free and would be introduced in the first phase. It included the following services and features:

- An online catalogue where the location of any live music activity could be inserted;
- A staff list featuring a list of members, e.g. of a band, with a direct link to their profiles created on Concertlab’s Web site;
- A Google Maps link that allowed members to link to live music events featured on Google Maps. By clicking on a ping that showed the location of a music happening, a bubble with detailed information would open.

In the second phase, three months after the introduction of the first profile, the founders planned to introduce two profiles subject to a fee: an “Advanced Profile” and a “Pro Profile.” The “Advanced Profile” would cost 199 CHF/year and, in addition to offering all the features of the “Free Profile,” it included:

- Displaying the business logo of the relevant music store or music school and featuring a more detailed description of the business activity;
- A link connecting the business Web pages to other social networks (i.e. Facebook, YouTube, Twitter);
- Displaying the business email address and linking it to the official Web site;
- Synchronizing the own status directly on the Facebook page (i.e. by writing a message on Concertlab, this would end up on the Facebook page).

In addition to offering all the features of the “Advanced Profile,” the “Pro Profile” was planned to include the possibility of using the “Special Offer” function, a true shop window to display a business’s special offers (e.g. informing about discounts

on instruments or, in the case of a school of music, informing customers about package deals for music lessons). The Pro Profile would cost 299 CHF/year.

The founders believed that emerging bands, musicians, event organizers and promoters, music schools, and shops would purchase these subscriptions in order to save money, time, and effort by simplifying and speeding up everyday interactions in organizing and participating in live events.

The business model would also have another source of revenue: selling advertising space for banner ads. Concertlab also hoped to publish details of the products or services of businesses operating in the music market on their Web platform. Such businesses would include music schools, instrument music stores, clubs, music venues, and live music concert organizers. The idea was to approach those actors with an offer of advertising space that would give them greater visibility rather than advertise on many different Web sites and live music happenings. In order to reach a break-even point, the founders calculated that they would need to acquire about 1,000 users in the first year of activity, distributed among paying and the non-paying users.

## PRODUCT DEVELOPMENT

After about a year of development, on September 16, 2011, the beta version of Concertlab started to run in four languages: Italian, English, German, and French. Potential users could begin to sign up for free and start adding, promoting, or simply searching for information about live music events or favorite bands in their region. With the takeoff of the beta version, the founders discovered that it was no longer an absolute novelty. While the team was dealing with the design and development of the platform, a competitor developed and introduced a comparable product. A start-up based in Zurich, apparently founded in 2009, entered the market with a similar offering: an online music collaboration community platform intended to help musicians, producers, and other music industry professionals to freely collaborate over the Internet. In less than three years it gained about 15,000 subscriptions. Marco A. commented, “When we started setting up our project at the end of 2010, few Web sites offered services for online music

collaboration and none of those were decently made; but today, two years later, these music collaboration Web sites are diffused and work quite well.”

Concertlab could have entered the market earlier when the basic technology to make the platform functioning was working, but Marco A. clarified, “Although in early 2011 we were ready to enter the market with our technology, we preferred to wait and to further develop the technology behind the platform. We wanted to introduce something really innovative, and of much better quality compared to existing solutions; perhaps it might have been better to enter the market with a very early beta version of the platform and then improve it and develop it over time following users’ feedback.”

With the launch of the beta version another aspect emerged: the public could hardly recognize the value of the service Concertlab offered. For instance, Concertlab received several requests from emerging bands asking for help in organizing a concert, a service that was not contemplated. In this regard, Marco A. said: “We found it hard to make people understand that we were not a platform dedicated to music among many; the value of the service we offered was hardly recognized... we were probably not effective in making clear the value and the benefits of registering on our platform.” To address the problem the founders chose to invest in further development of the technology behind the Web platform in order to clearly stand out as different (and better) than its competitors. The founding members believed that additional funding was needed to secure and accelerate this process and decided to search for new potential funders.

In March 2012, they came out with something new. They launched the App Concertlab, an application that runs on mobile phones downloadable for free from well-known music stores. With this application, Concertlab wanted to offer the opportunity to consult a wide program of live events using the geolocation system usually integrated in most of the new-generation smartphones. This function allows users to view a list of live music events nearby. Once the user selects the event of interest, the application shows the venue’s location on a map and how to reach it. In addition, the application allows the user to preset a list of favorites cities, artists, or clubs and music festivals, in order to have direct access to these items without having to search for them every time. Another

feature is 'MyAgenda,' a function that reminds the user on the day of the event he saved in his agenda.

## MANAGING CUSTOMER RELATIONSHIPS

When the four founders started the business at the end of 2010 there were no direct potential competitors on the market, none was offering a Web platform updated with useful information and other services for the actors of the music industry. Since competition was not perceived as a threat, Concertlab opted for a non-aggressive marketing strategy to enter the market and to create awareness. Hence, the initial idea was to acquire the first 1000 users by “tapping the word-of-mouth potential of PR.” Tapping word of mouth would have started with two activities: the distribution of company flyers and PR. The four founders decided to distribute the company flyers by themselves at live music concerts and in various bars where bands were performing.

The strategy adopted at that moment was to exploit this unfulfilled demand by proposing, as quickly as possible, a technologically advanced platform including many innovative functions (in order to avoid a possible leakage of information, the founders have never disclosed all the innovative solutions they had in mind). However, the platform was not ready: “We couldn’t approach our potential customers by offering them something that did not exist. Therefore, our first main concern was to focus on the development of the new technology behind the Web platform and then, only after we were ready with the finished product, the strategies to achieve the marketing objectives would have been defined.

After the launch of the beta version, the founders started to develop relationships with a few potential partners to intensify their promotion efforts. Concertlab agreed to write a column once a week for a free daily newspaper distributed throughout Switzerland and available online. The column would feature the independent music scene, musical curiosities and suggestions and, in particular, updates on new albums, concerts, and events. The articles would simultaneously be displayed on a well-known information portal in the Swiss-Italian region. Concertlab also established a partnership

with a small local radio station. Every Friday, Saturday, and Sunday Concertlab offered suggestions for inclusion in the existing program dedicated to the weekend agenda.

At a later stage, the founders visited some potential paying customers, such as music schools and organizers of live music venues to directly present the benefits of paying a subscription to the platform. By June 2012, nine months after the activation of the platform, the new company sold some small ads and six subscriptions for a fee. In all, Concertlab cashed in about 6,000 CHF. The first six paying customers were acquired when the founders decided to sell the product directly to a dozen music stores and music schools. Marco A. recalls, “Of the ten customers we encountered, six decided to buy one of the two subscriptions subject to a fee while the other four decided for a free subscription.” Marco A. believed this was quite a positive response by going directly to the customers to promote the platform.

By that time the customer base included about 1,000 subscribers, of which 670 were fans, 300 were bands, and 33 were clubs. Ninety percent of these users came from the Canton Ticino region (the Italian part of Switzerland), and the other 10% came from the German side of Switzerland and from the French part.

Given that both the sales of paid subscriptions and advertising space were expected to grow, the founders began to think of how to better promote the product and increase awareness of their product in the German and French parts of Switzerland. In order to acquire new customers beyond the Italian Swiss region, the four founders considered hiring a full-time salesperson and delegating him the promotion and sales activities all over the Swiss market.

## FUNDING

When they started the business at the end of 2010, the four founders invested 20,000 CHF in the company in the form of initial capital. They also decided to work more or less for free during the first phase of the company’s development. Once they had defined the business model, the four partners knew they needed some more funds to develop the platform. They decided then to apply for some funding and professional support. Among

the funding bodies was the CTI. At the beginning of 2011, the evaluation commission of CP Start-up evaluated their project and qualified it for support and the use of the facilities of the technological park run by CP Start-up. This structure provided the necessary logistical support, including an office where all the colleagues could work together. “The technological park in Lugano supported us by providing an office in which to centralize our operations,” one of the founders said. “We could also benefit from access to a network of important contacts in the world of start-ups in Canton Ticino and the rest of Switzerland.”

In early 2011 the team got their first funding of 8,000 CHF from the ATED-ICT Ticino as the best IT business idea of 2010 in Ticino. ATED-ICT Ticino is an independent association active in the Canton of Ticino; it is open to all people, companies, and organizations interested in information and communication technologies (ICT). Shortly afterwards, in spring 2011, Concertlab received an innovations check of 350,000 CHF from the Swiss Commission for Technology and Innovation promotion (CTI). Apart from financial support to sustain their project, Concertlab was also selected to receive professional support. They entered an agreement for professional coaching support from the local bodies of CTI called “coaching acceptance.” That would have helped them for two years to prepare the project and possibly obtain the federal certification of quality.

Shortly after the launch of the beta version in fall 2011, the founders decided to further develop the platform to include new features. Therefore, the start-up applied for other funding, and in December 2011, the City of Lugano granted the company a microcredit loan of 30,000 CHF as support for developing local economic activity.

Marco A. commented on the fund received saying that, “These small successes in acquiring funding were confirmation of the robustness and potentiality of the Concertlab project and, not least, a considerable motivational boost.”

## THE EMERGING ORGANIZATION

Concertlab started with the partial involvement of the four partners at the beginning of 2011. Marco A. would work 60% of this time, and the other three partners contributed 20% of their time each; none of them received any salary.

In spring 2011, two others joined the team: Lorenzo C. and Andrea W., who were both research doctors at the Artificial Intelligence Institute of SUPSI. Both Lorenzo C, an IT consultant, and Andrea W., a programmer specializing in intelligent graphic design, were employed at 80% for a period of 17 months so they could work on the design and development of the Concertlab Web site. Shortly afterwards, in May 2011, a third external collaborator, employed at 100% of his work time, was engaged. This person, a computer programmer, was meant to contribute to the design and development of the platform and, as soon as it was put online, he also had to manage and update the contents.

While the partners divided the responsibilities according to their competences, the organization remained rather informal initially. In fall 2011, when the founders were satisfied that the beta version of the platform was no longer an absolute novelty, Marco A. decided to become a full-time employee, moving from an unpaid 60% work time to a remunerated 100% time commitment. When Marco A. entered at 100% and three people became employed, the organization started to take shape. In May 2012, Martino P., Chief Marketing Officer of Concertlab, became part of the start-up as a full-time unpaid employee to follow the communication and marketing activities more closely. Thus, by mid 2012, Concertlab had seven people working for it (more or less formally).

### 6.3.3 OUTCOMES AND FUTURE OUTLOOK

By mid 2012 Concertlab had acquired a few customers, but is trying to strengthen its position. Concertlab's main concern remains that of finding more funds for further development of the product. As one of the founders noted, "We still have many innovative ideas, and that is why we are still here. We are still looking for other investors

who believe in our project. Their support would boost the entire project, enabling us, this time, to enter the market with a renewed solution before our competitors.”

This can be seen against the background of the economic outcomes to date and what emerges as the current business network context. The data on the economic outcomes of the venture to date have been collected through Concertlab and are contained in the above report on the Concertlab case analysis. The Concertlab platform has been designed and conceived to work on the idea of offering a range of benefits to different actors, individuals, and businesses and organizations operating within the live music industry. To better understand the potential of this business idea we explored how other actors in the music business network context perceived it at the end of the case – that is by mid 2012. We therefore asked professionals and amateurs operating in the live music business to explain how they perceived the live music agenda platform developed by Concertlab.

## ECONOMIC OUTCOMES OF THE VENTURE

It seems worthwhile to reflect on the exercise of this new venture by examining the approximate data relating to income and expenditure up to that date, June 2012, to see how near the venture is to break-even point. The founder told us that in about two years of activity the start-up has invested about 70,000 CHF. Unfortunately, it has not been possible to establish accurately where the total amount has been invested. However, according to the founders, 20,000 CHF was invested to form a limited liability company. Regarding the other expenses, since accurate data are not available, we will make some approximate estimation as shown in Table 6.8.

Table 6.8 Economic outcomes

<b>Costs</b>	
Labor (Four partners and three employees part-time for 1,5 years)	400,000 CHF
Equipment/Material	50,000 CHF
<b>Total Costs</b>	<b>450,000 CHF</b>
<b>Revenues</b>	
Subscriptions	<b>6,000 CHF</b>
<b>Funds</b>	
ATED - ITC	350,000 CHF
City of Lugano	30,000 CHF
CTI	8,000 CHF
<b>Total Funds</b>	<b>388,000 CHF</b>

The economic situation Hypothesized in Table 1 indicates how close or distant the new business is away from being self-sustaining. By mid 2012 the number of paying customers was quite low, and the commercial revenues were very limited (about 6,000 CHF). However, the business has been successful in raising funds to develop the company's own operations. In all, external funding from various sources has been close to 400,000 CHF.

In order to carry itself, the company needs to generate revenues to cover at least the current cost of personnel to sustain operations. In all, the development of the company has cost 450,000 CHF in two years in estimated labor costs. How much is needed to support operations is more difficult to estimate but it is likely not less than 3-4 full-time working people, equivalent to a conventional remuneration of 50,000 CHF per year. This means that in order to be self-sustaining, the operations need to generate no less than 200,000–250,000 CHF per year in revenues.

While the new business will survive only if the revenue generated can cover operating costs without external funding, from the discussion with the partners it emerged that their major concern was the investment of about 20,000 CHF to form a limited liability.

# Chapter 7

## Discussion and Implications

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### 7.1 INTRODUCTION

At its broadest, the aim of our study has been to examine the difficulties developing new businesses that have been documented in numerous studies we reviewed in Chapter 1. At the outset of our work, we found that current research falls short of providing a comprehensive explanation for the difficulties observed. We approached the issue taking a perspective that builds on extensive research on business markets that were reviewed and discussed in Chapter 4. This research has produced substantial empirical evidence of the existence and importance of relationships between businesses and other economic organizations and has led to formulating a business network view of markets. The research has focused on various aspects of business relationships and how these impact the operations of business organizations.

Taking the business network perspective on the phenomenon of new business formation has led us to turn attention to the process through which the new business venture merges with the existing business network and thus develops new business relationships through which the new venture becomes connected to its context. Acknowledging the importance of business relationships in explaining new business formation processes requires shifting attention from internal (or individual) to external (or context) aspects in an attempt to explain how these merge with the existing relational

network context. It also implies the need to focus on how new customer-supplier relationships develop and, consequently, the interaction processes that evolve in the formation of new business relationships. This constitutes the background to the findings (we reached) and the conclusion we will discuss in this chapter.

Recent research, particularly that related to marketing, has found that the process of interaction between new businesses and the existing context is an important element in explaining how new businesses develop. We reviewed some of the main ideas relating to this literature in Chapter 5. Our review shows that in marketing, the IMP research stream has addressed the issue of the interaction in business relationships and recently proposed some reflection on new business development in business networks. In the literature under review, we identified four themes that resulted in four propositions we introduced in Chapter 5, themes which became central to our study.

*The first proposition* is that the difficulties in developing a new business are related to the need to develop new business relationships through which the venture becomes connected to the pre-existing relevant business network. *The second proposition* is that the complexity in developing business relations depends on the need to connect three layers of business relationship content activities, resources, and actors in order to put workable solutions and arrangements in place between the customer and the supplier. *The third proposition* is that new business solutions and arrangements in relationships cannot be developed unilaterally but are developed jointly by the parties involved and created in interaction between the parties. *The fourth proposition* is that the emergent solutions and arrangements jointly conceived, as well as new relationships on the whole must be economically advantageous for the parties involved in order to be accepted and continue to exist.

While the four issues underlying the propositions have been proposed in various studies and appear relevant for an interpretation of the complexities that characterize the new business development process, empirical studies of these in the context of new venture development are mostly rare. Limited empirical research on the four aspects above may also reflect methodological challenges inherent in exploring longitudinally relational processes.

With the aim of contributing to filling the gap in research, we undertook three case studies of new businesses, carrying out interviews with entrepreneurs involved in developing their business ideas and with some potential customers. The three cases are reported in Chapter 6. The findings of our empirical investigation confirm and, in various aspects, enrich the four broad propositions. The findings provide support for our argument that the difficulties and unpredictability characterizing the process of new business formation reflects the difficulties connecting to a pre-existing context through developing new business relationships.

Although in Chapter 6 we reported the empirical findings at the end of each case study, in this chapter we will first sum up key indications that emerge from the cases regarding the critical issues in developing the new venture's initial business relationships. After discussing the difficulties developing new business relationships in the next section, we will return to our original research question, regarding the difficulties and unpredictability characterizing the process of new business formation, and discuss what emerges in our study as key explanations of these difficulties. We conclude with considerations on the limitations of our study before discussing the theoretical and practical implications of our conclusions.

## 7.2 CASE ANALYSIS

In this paragraph we will briefly sum up what we observed from the cases we have described in the previous chapter. Then we will extract the critical variables in developing new business relationships from the analysis of the empirical material collected. As we will see, several important aspects emerged from the cases discussed that help us to comprehend why it is so difficult for new businesses to develop new exchange relationships. In particular, we have found that the difficulties in developing new relationships may be identified in each of the three layers that characterize the content of the relationships: actors, resources, and activities.

### 7.2.1 SAFEVINE: CONFIGURING ACTIVITIES

The difficulty of this start up in acquiring paying customers that generate commercial revenues from its activities can be related to the problem of becoming connected to the already existing activity patterns. In particular, the SafeVine case is emblematic of the gulfs that occur when a new business tries to position itself within a system of activities that is already well organized.

From the beginning, the founder was mainly concerned with the core of SafeVine solution, which is the software algorithms used to analyze in real time the microclimate data collected in the vineyards and the web application to interact with the tracking system. The other required standardized components - two weather stations to measure the humidity and temperature parameters and six wireless sensors to collect and transfer the data - have been acquired externally from three different suppliers. These components have not been used to sell a functioning product, but to test the algorithm developed by SafeVine. In order to field-test the developed solution, the SafeVine project entered into partnerships with 14 regional phytosanitary research centers. Connecting with these public research centers in Switzerland and the continued relationships with them were essential to SafeVine as they gave certain feedback on, for instance, algorithms used to further develop the technology. Relationships with these strategic partners were also developed with the idea that these partners would buy the entire product package. However, that did not happen as most of these strategic partners already possessed some of the basic components that would enable them to run the SafeVine technology.

After about four years of developing, prototyping, and testing, the solution was technically finished, but quite far away from production and selling the product for use. How this new solution could be inserted in the vine-growing industry was rather vague. To cope with their phytosanitary problems, the winegrowers of the European Community currently rely on alert systems, maintenance procedures, and various other routinized practices and controls warranted by the different national phytosanitary protection inspectorates. What regard to the Canton Ticino's plant protection system, a

local phytosanitary center already informs winegrowers for free on how and when to treat the vineyards to protect them against grape diseases, including treatment against the FD. In certain cases, the treatment specified by this institution is mandatory. Similarly, the different winegrowing regions where SafeVine intends to market its technology (e.g., Switzerland, Italy, France, and Spain) already have a free phytosanitary monitoring service that informs winegrowers about the procedures and products to adopt in order to prevent and fight a wide range of plant diseases. At the European level, the phytosanitary coordination actions are provided by the European and Mediterranean Plant Protection Organization (EPPO), which is the regional plant protection organization for Europe. The main task of this organization is to develop an international strategy against the introduction and spread of pests that damage cultivated and wild plants in natural and agricultural ecosystems and make recommendations to the National Plant Protection Organizations of its member governments.

Among the various measures envisaged by the UE directive of obligatory control to counter the spread of the FD in the UE territory, it is expected that the different regional plant protection services annually ascertain the presence of gold and flavescence *Scaphoideus titanus* in the area of competence. Therefore, the implementation of specific insecticide treatments against this insect is prescribed and compulsory by the various regional plant protection services of the different countries. As the regional plant protection services inform, through various media such as newsletters and websites, about the mandatory treatments in their respective areas of competence, according to the people in the winegrowing industry we interviewed, winegrowers freely dispose of information about when and how to implement the treatments to prevent and fight the FD disease without incurring any additional costs. According to the people in the winegrowing industry we interviewed, compared to the SafeVine product, such a public service for the growers is a much cheaper solution that does not involve any investments.

This picture of the business network context in which SafeVine should become embedded indicates that it is quite difficult for a new business to position itself within an already organized system of activities. Given this legitimized activity pattern of

phytosanitary coordination actions against the spread of pests that can damage vineyards and other cultivated and wild plants, SafeVine would have had to configure its role and function within these activities, thereby implying the need to find its own position with respect to the various international and regional authorities - at the European, federal and cantonal level - that already provide a functional planning of actions to combat the spread of many phytosanitary diseases. The difficulty for SafeVine lay in the fact that it was never made clear who the potential users were: private winemakers or regional phytosanitary services. In fact, according to the winemakers and traders we interviewed, the proposed solution was nowhere applicable in the terms set by SafeVine, but would have required much more accuracy. This insight occurred when it was about to sell the product. In particular, the business relationships with the two potential customers with whom Mauro P. interacted never developed. The first potential customer that the founder of SafeVine accidentally met in October 2011 at the wine conference in Bordeaux never became a paying customer. Even the contact established in spring 2012 with the founder and CEO of an established wine trading and winemaker business of the Canton of Ticino, who could have become both a customer and a strategic partner, never became a business relationship.

Four years after its founding, SafeVine stands as a start-up capable of developing an innovative and efficient technology; however, as the evidence shows, it remains unable to convert the project into a business solution for customers. It was not clear to whom to commercialize the developed solution. From the beginning the founder has had no doubts about what the product solution will be, although the uncertainty about who the potential customers would be persisted for more than four years. In practice, determining to whom to market the final product, the selling conditions, the installation techniques, and maintenance procedures all remain open issues. Therefore, the major difficulties for this new venture emerged when it became necessary to define how its product could best be fitted from the technical and business point of view in the existing phytosanitary protection activities warranted by the various national and regional phytosanitary protection centers. This inconvenience has clearly slowed the development of the new business. Discovering with a remarkable delay these critical aspects, such as

who can actually make use of this technology and how the product idea can be inserted and interfaced with the already existing pattern of activities, made the start-up's takeoff problematic.

### 7.2.2 EKOBIKE: INTERFACING RESOURCES

The case illustrates some interesting issues regarding the need to combine resources in a new combination to create a new solution and connect the new resources to the existing resource combination in the network. The first interesting aspect is the way in which the new venture is morphing over time to become related with the context on the customers' or users' side. A second aspect of resource combining and interfacing relates to assembling the resource elements that compose the product in the production process.

Difficulties inherent in introducing an electrical motorbike in the market (and the electrical vehicles in general) are a very typical example of the need for the new venture to become embedded in the existing network in its resource dimension. The preexisting structure conditions the success of the new venture unless the venture finds a way to combine the new solution with what exists. For example, given that the possibilities to recharge the vehicle in general traffic are limited and the autonomy with current battery technology is limited, solutions required to make the electrical bike accepted at any significant scale are clearly beyond the possibilities of a venture like Ekobike as this requires extensive changes in the current resource constellation. The initial business idea of Ekobike - to focus on motocross bikes, a niche business that has size and connotations of a feasible new business development - is compatible with the resources of the company and the scale of the necessary adaptations. Electrical motocross motorcycles are a niche product; if practiced on, for instance, national or European scales, they would probably be sufficient to sustain a new venture like Ekobike. The Ekopark, the indoor/outdoor motorcycle park initially intended as a promotional "tool" for electrical cycles, appeared to have attracted a consistent number of customers. Apparently the company closed the park because the partners found no time to manage it directly and employing staff would entail costs they were not willing to sustain. Yet the concept was

feasible as the German buyer of the concept apparently started to operate a certain number of these each endowed with a few dozen of electrical motorbikes from other producers. The idea was feasible when Ekobike started it; it was also attractive enough and within reach. It involved embedding in an existing context where some tendencies favored such an idea. A consistent demand for motocross exists, and electrical bikes in this context are an attractive novelty for those who practice it as they meet the various emergent regulations of the environmental impact (noise, pollution).

However, the entrepreneurs clearly did not see this developmental road as a desirable one and abandoned it in order to aim at much larger volumes and breakthroughs as electrical scooters for road applications as a general means of transport, which was their original idea. However, sensing the limited resources while searching for a partnering manufacturer (and distributor), they began to see the business of the company as design and engineering, rather than manufacturing and marketing of electrical scooters. This related to the organizing of the new venture. After the formal constitution, the entrepreneurs' team started to organize various work processes in order to accommodate how to consolidate their business idea. The transition from EM-City to Ekobike S.A. and, subsequently, to Ekobike Engineering illustrates the search for a working business model for the new venture that started with the idea of importing electrical motorbikes, which morphed into designing and producing electrical motocross bikes and later into attempts to produce electrical scooters. When they decided to open a park to promote electric motorcycles, they actually came close to a feasible venture, albeit much different from their original intent. This might have been the reason why they decided to close the motocross park and sell the idea (indicating the economic validity of the idea).

The idea of entering into the scooter business was realized with the foundation of a new company, Ekobike S.A., that searched for partners to achieve large-scale production. The attempt to negotiate with a large Italian motorcycle producer for the development and production of scooters did not lead to any agreement and ended with dissolution of the company a few years later. At this point, the entrepreneurs launched another business, Ekobike Engineering Ltd., to design electric motorbikes and find new

partners to develop and market any products. Ultimately, it leased the whole project to one of Switzerland's old industrial companies in the field of products and systems for power generation, transmission, and distribution. During the various phases of the venture the owners were running more businesses simultaneously. The new venture gradually attempted to find an appropriate formal organization and establish effective relationships with other business partners.

The second aspect of resource combining and the need to interface various resource elements internally is illustrated by how the Ekobike proceeded to put together the electrical cross motorcycle. The case highlights inherent problems in assembling and interfacing existing elements. A first interesting aspect is the difficulty the new business faced in identifying suppliers capable of providing the necessary components. This was facilitated by previous contacts in the field, particularly an Italian supplier of frames. This idea of developing and producing an electric motocross bike was put into practice by contacting five suppliers for five basic constituent parts of the electric motorbike: the engine, frame, the battery and electrical system, and controller. During the first phase, the compatibility of the parts was tested and the first difficulties emerged. Indeed, there were a few significant issues involved in interfacing the five parts, particularly as three of the suppliers were not ready for any kind of adaptations. There was various degrees of supplier collaboration to adapt the part of the electric motorbike, but not all cooperated in developing and providing a product to be integrated with the other parts. Ekobike initiated the relationship with the frame supplier, who was able to produce a frame, based on an existing model, and adapt it to the specific requirements of the client. The other relationships were initiated shortly after the company was founded with four other suppliers. Three of these four suppliers - of the electrical system, the motor controller, and the battery - were able to provide solutions and adaptations to the client's specific needs, which when possible were integrated with other parts to create a functioning product. The producer of the electric engine was not willing to offer anything but a standard engine, which was neither developed nor changed ad hoc. Ekobike acquired all these components from the suppliers with only limited interactions because the suppliers were not willing invest in cooperating with the new venture. For Ekobike, it was

necessary to carry out a series of tests to check the compatibility and, above all, obtain technology that enabled them to produce electric vehicles that demonstrated performance in all respects. These tests and the subsequent adjustments of the parts for the production of the final version required a lot of time and affected the development timetable of the electric motorbike. The difficulty for Ekobike was that of interfacing different components. In addition, Ekobike initially had no production facilities; they were only gradually constructed. Apparently, a critical point for the development of this business was the life of conventional lead batteries. Ekobike wished to resolve all these problems in cooperation with Erun, the lead battery supplier who at the time worked on designing and producing a new type of lithium ion batteries and was interested in collaborating with Ekobike as a test.

What became apparent during this case was that successful completion of the product depends on the willingness of the suppliers to cooperate. Without the active involvement of external actors, it becomes problematic to find the right resources or assemble and interface them in order to make them compatible and working (Waluszewski, Baraldi, Shih, & Linne, 2009; Baraldi & Strömsten, 2009).

### 7.2.3 CONCERTLAB: INVOLVING ACTORS

The very idea of Concertlab was to connect various actors in the business network related to live music events and assume the role of a mediator. However, this case demonstrates that the difficulties and thus far limited success of this start-up can be related to the difficulties involved in networking the various parties of the live music market (e.g., artists, clubs, venues, fans, organizers, talent scouts, operators, and service providers). During the start-up period, the founders related with potential customers through the distribution of flyers, presenting the platforms' range of functions and services available. Creating the first contacts was meant to operate the word-of-mouth promotion. Even if the founders planned, depending on their availability and willingness, to develop their first contact with customers, this approach does not seem to have been adequately arranged; Concertlab found it hard to reach and connect with the critical mass

of users necessary to create a networked music community that auto-generated the website's content by adding information about the live music events and happenings. In fact, two years after its founding, the new venture was far from self-sustaining. By mid-2012, the new company had acquired a few paying customers, and the commercial revenues were quite limited.

Concertlab founders' conviction of knowing well how the various actors behave and their expectations led them to overlook the importance of engaging in interactions with new potential customers in order to learn more about how they see and interpret certain proposals and then to teach and explain to them the benefits of the services offered via the platform. In fact, most potential customers operating in the live music industry that we interviewed were not aware of what the platform offered and failed to perceive any practical benefit or added value in creating, maintaining, and managing a profile on the platform. Potential customers perceived the cost of buying and using the platform to be too high; less costly platforms aimed at building music business contacts and offering updated live music agendas already existed. In addition, the potential customers interviewed showed an explicit preference in personally knowing and communicating face-to-face with live music concert promoters and organizers rather than via the Internet because the mutual commitment among strangers was perceived to be high risk. Hence, without actively interacting with others, it became difficult to infer customers' needs and facilitate customers' perception of an immediate utility and value of the new service.

In the early phase of the company consolidation, a chief marketing officer (CMO) worked part time for Concertlab's marketing and communication activities; he was given the responsibility of managing and running the promotion activities during the first development steps of the new venture. After two years, when it was recognized that the number of subscribers on the platform (about a thousand) was below the potential of a product/service that is self-generated mostly on the information shared by users, the CMO became a full-time employee. Although the promotional activities initially relied nearly exclusively on word of mouth, with the full-time employment of the CMO, marketing goals and strategies were reformulated and adapted. In fact, Concertlab had

quite a random approach to prospective customers, but over time it realized that there was a need to get more involved in developing relationships with customers, which required more direct and complex interactions. Therefore, given that the paying customers were acquired through the intermediation of the founders, who personally presented the product, the founders began to evaluate the possibility of engaging a full-time salesman to sell subscriptions all over the Swiss market. The aim was to expand the scope of the relationships and include connections to other actors. The role of an external sales representative becomes questionable because connecting the various actors operating in the live music business appears to be to a large extent a knowledge-development process and it is extremely important (as shown by ultimate failure) that the new venture learns about customers' expectations. Given that, in the developmental phase of the business, the most product-acknowledged people are the founders and much of the customer experience and perceptions are tacit and experience based, the solution of a dedicated salesperson is not likely to be effective for teaching and learning. Developing the first contacts with potential customers is a task that perhaps should not be delegated. The new solution in progress needs to be identified and tested between the new business founders and the prospective users, who should use and benefit from the new solutions. This is likely to require a series of mutual adjustments in the technical solution, but also a shared construction of meaning and understanding between the parties who have to "agree" or be aligned with the value of the solution put it into use. Yet, through the rereading of the case, we observe that the promoters of the project did not seem to acknowledge the critical nature of this aspect that would have required interacting with the various actors, individuals, and organizations that operate within the music industry.

Although the goal of Concertlab was to connect the various actors operating in the live music business, the main concern of the founders in the beginning of the business development was acquiring funds to finance the development of the software behind the web platform to further enhance the performance features that the system can offer. Consequently, by investing in the commercial issues, all the activities related to the development of relationships with their potential customers and users were

continuously postponed. Raising funds became the priority, but also created a somewhat vicious circle: Funds permitted them to focus on improving the product and postponing the testing of it by acquiring paying customers; thus, ease of funding was apparently instrumental for losing touch with the potential users as it permitted them to continue with an internal focus.

#### 7.2.4 SUMMING UP

All three cases exemplify the difficulties in establishing, developing, and maintaining new business relationships with customers and suppliers. They evidence the complexity of developing initial business relationships. The complexity in setting up business relationships illustrated in these cases is related to the need to connect the different activities of the parties, the various resources of the parties, and the set of actors involved in establishing the new relationship. The three cases show that these three layers are difficult to connect because at the resource level there is a need to interface numerous tangible and intangible resource elements and complement them in a valuable combination. Connecting the different activities becomes complicated because there is a need to configure and coordinate different activities systems taking place within the new company and between customers and the suppliers. Further difficulty in developing new relationships is related to the need to develop intense communication flows in order to establish mutual trust and commitment between the actors involved.

Our cases have shown that the design, development, delivery, and integration of new solutions, and the purchasing and integration of materials, components, or finished products and services requires defining and relating a number of more or less complicated things. In practice, what is required is defining the final offering, which includes not only the product and service features, but the packaging, delivery, costs, price policy, marketing and communication activities, sales network, and the maintenance service, as well as to establish a number of other pre- and post-sales services and so on. All three cases show that defining the features of the offering, which entails putting a new solution in place, is very difficult, if not impossible, to anticipate.

Since the features of the offering cannot be anticipated, the various dimensions involved in the definition of the latter – coordinating the different activities, involving and committing different people, and combining different resources – need to be defined through a series of attempts and trials until the right combinations are found and fixed. This way of proceeding, which consists of proving several alternatives and then verifying if they work, is potentially costly for at least two reasons. On the one hand, trial and error implies performing many aspects several times, without the guarantee of a positive result. On the other hand, it can also happen that the counterpart involved in the relationship, who may require specific and costly adaptations, is not inclined to adapt and/or modify its routines or structures to facilitate the integration of the new solution. That is, the definition of the offering involves a number of questions that need to be answered through a process of trial and error that is demanding and costly, since it requires considerable time and interaction between the customer and the supplier involved in the relationship.

While each of the cases has focused on one of the layers of the relationship content, none of the layers can be isolated. The three layers are intertwined and interdependent. In developing a new customer-supplier relationship, all three layers need to be connected. Among the difficulties of relationship development is that effective development can be hindered by failure in one of these, while all the others are in place. It is the weakest link that conditions the development of the relationship and makes the new venture's merging with the context particularly onerous and difficult to achieve.

Our cases confirm what has been suggested in recent research, namely that the difficulties and unpredictability in establishing, developing, and maintaining new business relationships with customers and suppliers can be related to the demanding but critical tasks involved in learning a way to configure activities, in trying to complement existing resources, and in creating a shared mindset between the actors involved (Aaboen et al., 2011; Ciabuschi et al., 2011).

### 7.3 EMERGENT ISSUES IN NEW BUSINESS VENTURES DEVELOPMENT

Having discussed the three cases of developing new business relationships one at a time we have encountered three circumstances common to the three cases that appear typical of the initial stages of development of a new venture. The first is that entrepreneurs (and management) in the initial stages of the new venture tend to be "inward looking." The second trait is that it appears easier for new ventures to get funds from investors and other funding bodies than to generate revenues from potential customers. Finally, what emerged as a general trait of the cases, is the ongoing organizing both internally and in the context of the new business. We will also integrate the results of the empirical investigation with some of the findings reported in the literature about difficulties that may hinder the development of a new business.

#### 7.3.1 LOOKING INWARD

In all three cases we found that the entrepreneurs (or the entrepreneur team) were devoting most of their attention and efforts to questions "internal" to the venture. They were always dedicating most of their time and attention to product/service design testing and production. The focus of the entrepreneurs (and of the management team) has been on the continuous improvement of the product/service features and of production.

The product/service features superior to those offered by others were apparently considered as a key success factor; a necessary condition for success. More or less explicitly, the entrepreneurs interviewed were convinced that a superior product would serve as a sufficient attraction to customers. In fact, the entrepreneurs' focus on "internal variables" is considered by the same entrepreneurs as the front along which they aim to build and strengthen the competitiveness of their ventures.

The start-ups we studied started to define their offerings and business idea based on broad assumptions held by the entrepreneurs about customers and their needs, and problem solving and buying behaviour. Their business ideas were then translated into a product service solution without much testing and checking out the initial assumptions.

Only when the solution was ready in some form it was brought to test in the market or with customers. In all three of our cases the entrepreneurs were somewhat surprised by the reactions of the customers and of the market in general. At best, the context moved ahead and competing solutions emerged (as in the Concertlab case); in other cases (SafeVine) when testing the viability of the product, circumstances were discovered that required adapting the business idea and redefining the various solutions. Neither Concertlab, nor Ekobike, nor SafeVine intentionally and systematically engaged in developing their contact with customers or suppliers concurrently with the development of the offering. The marketing responsibilities were rather vague and considered as secondary or solved in the belief that the original assumption would hold. While substantial effort was applied to internal issues, interaction with potential customers was intermittent and not finalized to involve these in some way in the development of the offering. When at a later stage the absence of spontaneous customer interest was to be addressed, the solution the entrepreneurs tended to adopt was to delegate the customer contacts to a sales specialist, because they clearly considered the problem a one-way sales activity.

The tendency to look inwards made the involvement of customers in the new solution development marginal. The entrepreneurs did not consider such involvement. We also found that many of the more strategic decisions, such as those related to product specification and diversification, reflected opportunities intervened casually from the outside, rather than being consequent to interacting at various levels with customers and suppliers in order to search for and identify specific solutions or testing.

### 7.3.2 SOURCES OF FUNDING

A second common issue in the cases studied is that all three new ventures benefited from external financial resources. For the period we have examined, external funding was considerably superior to revenues from paying customers. For instance, Concertlab received 6,000 CHF from customers compared to nearly 400,000 CHF raised as external funding during the first two years of its activity. Concertlab invested about 70,000 CHF

to register the company, buy the necessary equipment, and pay for the work of those involved in the R&D of the Web platform. In the SafeVine case, the company received about 200,000 CHF in external financing, and most of it was used to pay 14 people who worked on the Smart-Vineyard project developing the system. Around 20,000 CHF was used to purchase the components required for assembling and building some of the devices they installed in some vineyards belonging to the regional phytosanitary research centers. The company did not generate any revenues from paying customers as the first such sale was expected to happen in the future. In the case of Ekobike, the new venture received no external funding since the three partners submitted no such requests. However the founders claim to have invested 800,000 CHF in the new organization while the reported profit in the financial account for 2007, about 22,860 CHF, was far below expectations. While the new venture's initial forecast was to produce and sell a first batch of 100 electric motorbikes, the project ended after the production of 40 items of which only 20 found a new owner.

The result is that Concertlab, a year after having released to the public its Web platform, has gained less than 10 paying customers instead of a few hundred aimed at reaching the break-even point; SafeVine after four years of R&D and field testing has not even acquired one paying customer; while Ekobike gained 20 customers out of 100 expected. That is, none of the three new ventures in the first years of life has produced significant income from customers. Indeed, revenues from customers were marginal compared to the funds received externally, and which were used to finance the development of the organization, the product, and hiring people

What we found is that new businesses do not have great difficulty in finding funds and, moreover, once they have received these funds, they use them for product development and hiring people. This is not a unique phenomenon for our cases. It has been reported in a few other studies. (e.g. Waluszewski & Wedin, 2003; Teigland, Lindqvist, Malmberg, & Waxell, 2004) that show public funds in support of new ventures operating in the biotech industry, for example, are several times the turnover generated by the same biotech cluster.

### 7.3.3 ORGANIZING

The third aspect common to the three cases we studied concerns the organizing. The formal constitution of the new company, which means its official registration at the office of jurisdiction, appears to the founders to be a “seal” that legitimizes its convergence into an organized unit.

While the moment of the formal constitution is certainly important, we found that prior to this formal act, an organization begins to emerge as the entrepreneurs involve others attributing them different roles. After the formal constitution, new ventures tend to go toward a hierarchical structure as the entrepreneurs, or the entrepreneurs’ team, start to organize their various work processes in order to consolidate their business idea. At this stage entrepreneurs are concerned primarily with product development. At a later stage the new venture gradually moves towards a proper, more formal organizational phase, when the venture begins to organize itself towards an external context, by trying to establish relationships with other business partners. By trying to develop their first contacts with suppliers and distributors, the context in which this relationships merges, changes as a consequence of the respective actions and reactions of the business partners. That is, the ways new businesses try to relate with the context affects how the market is organized; at the same time, new business are influenced by the actual presence of business actors who interact with each other over time.

How the new venture morphs over time is interesting because it opens a discussion about the organizational dimension of new businesses. The literature on new venturing has long shown an interest in the organizational dimension of new business formation, but initially this concern was limited to the internal organizing of the business itself (Gartner, 1988). In more recently studies on entrepreneurship, the organizational dimension of new businesses has gained a wider focus and has been acknowledged as an important concern together with the interest in contextualizing entrepreneurship (Welter, 2011). In particular, researches that have focused on how entrepreneurs (and new businesses) interact with their context have advanced the idea of a collective dimension

in organizing and developing a new venture (Ciabuschi, Perna, & Snehota, 2011) and organizing consequences for the market of developing customer-supplier relationships.

#### 7.4 FINAL CONSIDERATIONS AND CONCLUSIONS

Our study is an attempt to explore the question, “Why is it so difficult to start a new business?” We investigated the problem of a new business venture as merging into a pre-existing business network. Therefore, we traced the issues a new business has to deal with in developing new business relationships. Studying the cases, we have observed that in order to develop, a new business has to connect with the existing relational network context, which is done by setting up business relationships. The criticalities and difficulties we identified in developing new business relationships with customers and suppliers are all related to the fact that the actors who represent the parties to the relationship need to relate all three substance layers, and a lack (shortcoming) of one of the layers by trial and error in interaction is conducive to failure in developing new relationships.

In this section, we will return to our research question regarding the difficulties and unpredictability characterizing the process of new business formation. Therefore, we will look at the problem of merging into a pre-existing context from a business perspective and we will further discuss the impact of the initial business relationships on the new business formation process. The discussion that follows provides the starting point for interpreting the phenomenon we have observed and to identify four significant aspects in the process of merging in the market as a network. In particular, we will argue that the first difficulty in starting a new business is related to the fact that new business ventures need to engage in several more or less interdependent relationships and that the resulting interdependencies limit the autonomy of the single business and the control the new businesses have of the actions, as well as of the outcomes. The second difficulty we register is related to the fact that the business context is in a state of continuing change and appears thus intrinsically dynamic because of the continuous adaptations in relationships new businesses develop. The third aspect we identified as a limiting factor

in developing a new business is related to the need to find and offer a range of cost-effective solutions in order to gain paying customers and to generate sufficient income to cover operating costs. The fourth aspect is that, since all these issues are difficult to anticipate without a great margin of error confirms that embedding through relationships, a condition for developing new businesses, requires intense and extensive interaction activities with external partners.

These findings support the claim of the importance of actively relating with others. In particular, our findings suggest that companies in their early stages need to be committed to interaction with potential partners in order to succeed in managing dependence on others' actions and reactions, in coping with the mutations of dynamic context and in finding solutions that are economically accepted.

#### 7.4.1 JOINTNESS

We found that merging into the pre-existing context can become complicated as relationships are more or less interdependent. If we look at the business as a whole, it stands out as an entity building on a system consisting of a set of actors linked by relationships oriented to the exchange of different resources. It is a node in a set of business relationships. Every new venture, therefore, has a need to connect and engage several relationships in order to start to put together critical resources and organize the flow of complex activities. In particular, as seen previously, the development of a new solution and its adaptations to the specific context of use, requires configuring the entire offering under three aspects: those relating to synchronizing how to coordinate the activities already put in place, how to combine and adapt the existing resources, and how to create a shared mindset among the actors involved.

Our findings support the idea that business solutions and arrangements cannot be developed unilaterally because the novel solutions on which the new relationships development depend, are defined jointly by the parties involved and are the outcome of a process of coping with many arrangements that aim at interfacing a large and complex set of operations (Tuli, Kohli, & Bharadwaj, 2007; Harrison & Waluszewski, 2008;

Håkansson et al., 2009). Having said that, it is clear that for any new venture the means to merge into the pre-existing network is to connect several relationships and interact with different customers and suppliers.

However, interacting with several parties is not only associated with positive outcomes, it brings some limitations to the activities of the single business. Acting jointly has two important consequences for the development of a new venture. The first concerns the fact that any new venture is simultaneously engaged in several different relationships. Acting jointly with many actors implies that certain activities are no longer done by a single actor but carried out between actors. Every form of joint actions (or interaction) with an external actor is uncertain and can involve various (potential) unexpected developments and risks, such as a certain loss of control (e.g. of the technical data of the new solution) and autonomy. The resulting interdependencies limit the activities and intentions of the single business, which implies a limitation on autonomy over its actions as well as its outcomes. The second consequence of this need to act jointly is that every actor involved in a relationship has its own ideas of goals, alternative courses of action, and expected outcomes. Because there is no complete consensus between actors about the variables that produce outcomes of the interaction, the new business needs to constantly reassure its counterparts about the expected outcomes in an attempt to find consensus. Therefore, acting in several and more or less interdependent relationships means to interact with many different entities and try to gain their consent.

The implications of interdependencies for new business development are far-reaching. On the one hand, our study indicates that the difficulty for new firms to merge into the pre-existing context is in the interference from others with whom they interact. The need to relate to others can help to explain why the process of merging the new business into the pre-existing context is so uncertain. Consequently, the outcomes of a new business's activities have to do with its strategy or plans only to a certain degree; rather, they depend on the intentions, perceptions, actions, and reactions of the interacting actors. In practice, the first major difficulty we have found in developing new businesses is that, because new ventures are conditional on others' influences, they are

not masters of their fate but, in some way, must play collectively with the surrounding context to achieve positive business development.

On the other hand, we found no support for the idea, at the centre of much of entrepreneurship research that the process of opportunity discovery and exploitation is entrepreneur centered. Rather, it suggests that since the presence of these continuous interferences from the context makes the process of new business formation a collective phenomenon, the opportunity emergence is diffused in the context and not discovered and exploited by an alert entrepreneur in a planned way. In the broadest sense, we support the idea that entrepreneurship appears to be the outcome of a joint effort, where the parties involved depend very much on each other, rather than the outcome of an individual attempt (Johannisson, 2000). Also the economic outcomes of a new business are largely dependent on combined action occurring elsewhere in the network context of the business and are never fully under the control of the new venture.

#### 7.4.2 RELATING TO THE CONTEXT IN MOTION

Relatedness has important structural and dynamic effects on the business landscape because the numerous interdependences between businesses generate a continuous change in the environment. New businesses need to succeed in connecting a set of different actors, customers, and suppliers in order to perform their commercial activities. In some way, new businesses start developing from a combination of activities, resources, and actors bound together by relationships that are formed over time in a specific context. But, as the new business becomes related, the existing context will not maintain the same configuration because its structure will change. This also means that as a new venture attempts, not without difficulties, to become constituted, it creates and modifies the context in which it acts. At the same time, however, the context in which relationships are formed exerts an influence on the same organizations. We have seen that new solutions require matching in the way actors act and connect and change the structure of organizations. The changes within enterprises, in turn, are reflected in a context that will continuously change its structure. That is to say, the moment a new

company begins to build up and organize, it indirectly affects and reorganizes the context in which it tries to merge. In practice, the changes in the businesses and context are mutually conditioning and affect the evolution of the two systems. This means the new ventures live in an unpredictable world where one never knows which actions will have which consequences.

So, the difficulty for a new business in merging with the pre-existing context is not only because the new organization needs to interact with several business partners. What emerges in our cases is that a further key explanation of these difficulties can be related to the fact that as any change in the structure of an organization affects the overall structure of the context, the setting in which the new company needs to merge is in constant motion, and the new business needs to continually adapt and cope with the collective changes.

The consequences of this changing context for new businesses are twofold. First, the new venture that's going to develop a new business idea needs to continuously monitor changes in the environment and, secondly, must be able to constantly adapt to these. The changes create opportunities as well as obstacles for the development of the new business and, at the same time, they are prerequisites for some changes to take place in order to realize effective solutions. In practical terms this means the new venture, in order to succeed in adapting to the context in motion and in translating the changes in effective solutions, needs to be externally connected so it can constantly gather information about the market structure and trends, particularly about the competition and, therefore, manage the continuous changes of the context in which they have to merge. New relationships serve as channels of interaction, which have an informative function through which new businesses can compete with the context. Therefore, the difficulty for new ventures lies in the fact that they need to keep up with the changes in the context, and this requires systematically adapting their strategies to avoid solutions becoming obsolete.

### 7.4.3 ECONOMICS OF INTERACTION

Another explanation for the difficulties new ventures encounter is related to the fact that to succeed, a new company must be cost-effective and economically attractive for potential customers to generate sufficient revenues to cover operating costs.

What we observed in our cases is that potential customers' propensity to purchase is not influenced only by the direct costs related to the purchase of the service or product (the price paid), but also to the need to adapt to and integrate the new solution in their operations and activities, which has a cost. Selling a new business solution requires defining the various dimensions of the offering through a process of trial and error in interaction between the customer and supplier. The interaction and adjustments in various dimensions make the process collective and subject to economic criteria for all the parties involved. Besides the quality of the products, there are other factors that can influence potential customers' propensity to purchase. Such factors include logistics, the outcome of joint development projects, and ideas about solutions for technical, organizational, and commercial problems. In practice, what emerges from all three cases is that potential customers the new ventures contacted were reluctant to buy and use a new product or service (or implement it into their ongoing operations) if they did not perceive the value of that product or service or were concerned about the economic convenience or consequences of the investment required to adapt and integrate the new solution in their operations and activities. Unlike financial support providers, potential customers are more averse to invest in a product or service in which they fail to recognize the economic advantages. It is interesting to note that our consideration is in contrast to entrepreneurs' perception that the lack of available funding is a major limiting factor for the development of their business.

This aspect, that we call economics of interaction, means that the development of new relationships entails some costs that reflect the problems related to coping with many arrangements aimed at interfacing a large and complex set of operations (Håkansson et al., 2009) and that success in creating and developing relationships between customers and suppliers depends on whether potential customers perceive the

economic convenience of the proposed new solutions or not. So, for new firms, it is important to find a suitable level of cost efficiency to satisfy the user side of the network.

As a consequence, the difficulty for new businesses is related to the fact that in order to carry themselves, initial costs need to be balanced by revenues generated over time and cost-effective solutions need to be applied to the business. That is, the purchase and additional costs related to the implementation and use of a new solution should be constantly measured against the advantages. The way this can be accomplished is tightly linked to how the interaction processes are organized with regard to activities, resources, and actors as discussed above.

#### 7.4.4 THE CENTRAL ROLE OF INTERACTION

Given the issues of jointness, of the context in continuous motion, and of the economics of interaction, interaction processes are key in dealing with these concerns.

Interacting with others is the core process to cope with the problems related to jointness, the mechanism that limits the autonomy of the actors involved. In this setting, the role of continuous interaction with others lays the foundations to cope with the unpredictable actions and reactions of the counterparts. For a new business, interacting is a way to handle uncertainties and limited autonomy.

Interacting with others offers the opportunity to manage problems related to the context in continuous motion. These problems require new businesses to constantly react and adapt to the changing economic context. The capabilities and potential of a new business to continuously redefine its strategies to include the external elements that are important for its development depend on its predisposition to become linked to the context and, therefore, to interact with others who, like the parties running the new business, continuously redefine the context. Interacting with others offers a way to find some kind of control in a context of unpredictable outcomes and unforeseeable influencing factors which do not allow new businesses to act in a planned way.

Interacting with others can be the means through which new businesses identify and devise profit and cost-effective solutions. To become connected to a multitude of

relationships implies finding technological solutions, making administrative arrangements, and scheduling logistics and credit and payment options that fit with networking counterparts. A product should reflect all the necessary transformations of primary resources into products that customers consider fit for use. Therefore, it becomes crucial to interact with and involve potential customers to understand how the counterparts involved perceive problems. Interacting with others helps translate customer needs and facilitate customers' perceptions of the utility and value of the new product or service. Continuous interactions in various aspects make the process costly for all the parties involved. However, as other research has shown, knowing the ideas, ways of thinking, and the preferences and aversions of potential customers allows one to recognize the necessary adaptations that will have a positive impact on cost, quality, and the flexibility of solutions for potential customers (Baraldi & Strömsten, 2006; Harrison & Waluszewski, 2008; Ingemansson & Waluszewski, 2009). In other words, interaction consequences can be considered an important variable for the economy of a new business as interaction processes involve potential cost but can also produce revenues.

Interacting with customers has a bridging function rather than only an informative one. Interaction and communication with customers allow a business to overcome the problem of managing interdependencies, the moving context, and economic issues. Considering the opportunity/necessity of becoming actively involved in relating with customers and suppliers from the earliest stages of the process becomes critical to cope with these issues. In particular, the way these problems can be accomplished is tightly linked to how the interaction processes are organized with regard to the need to act jointly with several actors, continuously monitor changes in the environment, and to constantly adapt to these, and to the need to become operationally cost efficient, namely suitably covering costs with revenues, and economically convenient for the user side of the network.

#### 7.4.5 ENTREPRENEURS' PRIORITIES AND ORIENTATION

It is of fundamental importance for a new company to create a new product or process solution that works effectively in the buyer's uses or production processes. Given that converting new ideas into workable and marketable solutions is a necessary condition for meeting customers' needs, entrepreneurs (or the management team) tend to have a strong focus on the technological features and production of products and services. Trying to conceive and test a new product or service and to find workable solutions implies that certain activities must be performed without external interventions and within the new venture. This need to solve technical matters and how these can be researched, developed, and improved internally leads to more attention on internal issues rather than on external activities directed at involving others. The focus on the questions "internal" to the venture reflects the fact that the same entrepreneurs consider the product/service features as the front along which they can build and strengthen the attractiveness and competitiveness of their ventures. That is, they tend to believe their customers will recognize that the product/service features they offer are superior to those others offer, and therefore, that a superior product or solution would be enough to attract customers. This "inward-looking attitude" among entrepreneurs is a manifest expression of the conviction that quality and product differentiation are not only necessary, but are also a sufficient condition for developing the new business.

While it is plausible that the value of a product or service is related to its attributes, it does not necessarily cause competitive success. This inwardly focused attitude causes some parties to conceal the fact that interaction leads to opportunities and thus increases the chance of new business success. Looking inward, rather than focusing on external relations and dynamics, can lead to the perception that interacting in customer-supplier relationships and being externally interconnected in order to gather information about the market structure and trends, particularly about the competition, is less important. That is, entrepreneurs appear not to recognize that confrontations and interactions with other external partners is a way to get a better and more acceptable product or service for customers.

Entrepreneurship can be a daunting task because merging into the pre-existing context requires research and the development of valuable technical ideas, solutions, and technologies; at the same time, it implies a certain degree of isolation from others. On the other hand, new workable solutions are achieved by creating and organizing new external interactions that lead to the formation of new relationships.

## 7.5 LIMITATIONS OF THE EMPIRICAL STUDY

Our study has two limitations that are common to the case study methodology. However, we think these do not need a broad discussion, as they are already well known. The main limitations of our study are the size of the sample and the fact that the study was conducted in only three business contexts. These limitations have been the basis of frequent criticisms of the case study methodology and have been argued to limit the possibility of generalizing. Obviously, it is not our intention to generalize our findings to all cases of new business development, but we believe the cases permit the identification of some interesting aspects.

However, consideration must be given to the limitations of our study. The first concern regards the approach and the model we adopted. Despite the developments that have occurred over the years in entrepreneurship research, as far as we know there is still no entrepreneurship theory offering an interpretation of the phenomena associated with the development of new businesses that is shared among researchers. It can be that the complexity of the phenomena is such that we will never fully understand new business formation, as some argue (Zahra & Nielsen, 2002; Koppl & Minniti, 2003).

Given that an appropriate specific analytical framework has not been recognized, we decided to apply a certain model and approach, namely the industrial network approach, to try to better understand the phenomenon. The network approach has made us aware of the consequences, both positive and negative, that relationships have for the development of new businesses. Having decided to use a certain approach to study a particular phenomenon doesn't mean it is the best way to study new business formation processes. It can be an approach that is less suitable for explaining other aspects of new

business formation. We are aware that the use of the network approach may lead to overemphasis on certain issues and ultimately to biased results in favor of our underlying propositions. However, because we were primarily interested in discovering how relationships form and their impact on new business development, we consider adopting the network-interaction perspective a reasonable choice.

Another limitation of our approach relates to the trade-off between including and excluding the perspectives of other actors that are also interacting simultaneously with other parties and actors. In a study aimed at exploring new businesses in a process of merging into the pre-existing business context, it would have been appropriate to extend the unit of analysis to the relevant portion of the contiguous business network. Given that the context in which the new business merges is an extended place, it is important to capture the various perspectives that different actors have as they engage in business action. In that sense, the second limitation of our study is that to better capture the phenomenon as a whole we would have had to consider multiple points of view and to explore the experiences and interpretation of the same situation (or interaction process) by others who interact with the new venture. In part, we tried to do that, but once we started to consider not only the entrepreneurs' points of view but also the standpoints of other actors operating in the context in which new businesses try to merge, our findings became richer and more consistent. In line with this, we believe it is important to consider the different actors' perceptions and interpretations of the market context in order to explain the market dynamics. However, since the interpretations and perceptions of the different actors are varied and often inconsistent, due to their position in the market, their experiences, cognitions, strategic intentions, etc., they are not easily captured. That is, identifying and choosing how to frame different perspectives, concepts, descriptions, or patterns of thought that co-exist when actors engage in business actions is difficult. This constitutes probably a major methodological challenge for future research.

Despite the limitations, the findings obtained by studying a relatively small sample consisting of three case studies and around 20 interviews indicate that the methodological choice and approach we followed appear to be fruitful for the

exploration of the phenomena. Our cases effectively illustrate the phenomena we were interested to discover in our research and can be considered a first empirical attempt in this direction. These “discoveries” can also be interpreted as evidence that it is worth further developing the framework available, the research approach, and the methodology to test the findings in a more reliable and robustly empirical way.

## 7.6 IMPLICATIONS FOR PRACTICE AND FURTHER RESEARCH

Given our conclusions, the question is how to define a future research agenda to advance understanding processes and effects in new business development. We will therefore briefly discuss the implications of our findings for practice and further research. Among the implications for practice, we would like to emphasize the challenge to management in attempting to manage multiple interdependencies, to cope with the dynamic of the business markets and to ensure the interaction and its economics. Among the implications for further research we contemplate the need to further study the issues we found that hindered the effective development of a new business.

### 7.6.1 IMPLICATIONS FOR PRACTICE

A broad conclusion of our study is that new business formation requires development of new customer and supplier relationships and that interaction in business relationships is a critical process for bringing new solutions to the market. This suggests that the ability to relate to others is critical to success in new business development.

The problems and difficulties encountered by new businesses are not attributable mainly to a product or service idea that is not strongly innovative, or to the limited availability of economic resources. The start-ups considered in this study appear to have encountered particular challenges when it came to thinking about how they should go to market with their new product or rather, offering solutions. New solutions are not restricted to product or service features but refer to the complete offering, which includes

the less obvious component of the “product delivered” (offering), including the costs, services etc. Such solutions are the outcome of a process of coping with many arrangements that aim at interfacing a large and complex set of operations (i.e., coordination of logistics, delivery, supply, and other organizational units) and to ensure technical integration (i.e., compatibility among products, services, and facilities). New businesses have to find technological solutions, administrative routines, and financial solutions that fit with their own situation but that are simultaneously compatible with those of the counterpart. It also means that such solutions need to be economically motivated for both the new venture and the users. Potential customers purchase a product or service only if they perceive the value and recognize the economic advantages.

Considering that the arrangements that will provide an effective economic solution for the parties involved are created in interaction jointly with others, the critical issue in managing a new venture is handling this jointness in developing relationships.

The first implication for practice is that management of the new venture should pay attention to the importance of relating to activities in the context of the new venture. Giving more credit to the consequences of actively relating with others implies knowing how to manage and allocate resources, attention, effort, and money in these activities. If relating is central to the development of new businesses it requires the allocation of appropriate efforts and investments to it; appropriate allocation also requires considering the development of new relationships as an investment.

The multiplicity of customer requirements can also be a valuable resource that can help the new venture optimize and foster the development of a new product or service; it also imposes the need to define interaction strategies in each relevant new relationship in order to adapt the solution coherently with specific user expectations. This requirement leads us to the second implication for practice: in order to reap such benefits from being related to others and to cope with the resulting interdependencies that limit the activities and intentions of the single business, the new venture has to develop competencies that go beyond the general customer-orientation approach. Rather, the appropriate aspects to be considered and managed are the specific interactions that

occur between the new business and the new supplier and user. At this stage, management's capability to interact with customers and suppliers to define adequate logistical, commercial, and administrative solutions and find resolutions whose economic benefits and costs are acceptable to both parties, is important, although this aspect is often overlooked by entrepreneurs. Key competencies do not merely have to do with communication, promotion, and selling capabilities to present customers with the kind of product or service the new venture offers, but rather with the ability to interact, teach, and learn from the counterpart by trial and error and to adopt others' perspectives. Such interaction capabilities provide the bases for developing new relationships.

The latter aspect, which applies to the need for particular relating abilities, leads us to a third implication for practitioners over the organizational structure (organizing) of the new venture. From the organizational point of view, some activities and responsibilities such as technical developments or the selling of the product or service, can be delegated to or shared with others, but to delegate related activities, such as those of a sales agent, appears to be ineffective. Most of the relating and interaction activities must be carried out by those who influence the capabilities and performance of the new venture.

Establishing relations with other actors generates a modification of the context. This implies that the network context is never fully under control and, therefore, new ventures have to cope with unpredictable changes of the landscape that weigh on their capability to achieve a certain degree of control over the results of their actions; thereby, they become dependent on how other actors perform their role. This complex and unpredictable process represents a challenge for the management of the new venture. Accepting the idea that what happens in the context is unpredictable and that the economic outcomes do not simply derive from the new venture company's actions appears to be the main issue of concern for management in coping with and attempting to manage multiple relationships and implies that management should focus attention on interaction and relating capabilities that are crucial for managing the unpredictable and evolving nature of the context.

So, for new businesses in the process of merging into a pre-existing context, networking competence appears central. Since networking skills are crucial, concern about interpersonal (or face-to-face) communication processes is rather central. Thus, the forthcoming entrepreneurs, or their ventures, have to develop competencies that go beyond the general concepts of opportunity discovery and exploitation (at the center of much of entrepreneurship research). Indeed, we face something different from a picture of opportunities existing out there that are there to be discovered and exploited by an attentive entrepreneur in an organized way. The new business venture must engage in interaction processes in which other parties play an active role and that shape the development of business relationships and enacting new contextualized solutions (opportunities). Therefore, the key competence in a new venture is not related to opportunity discovery, but rather to the capacity to interact and the ability to establish communication patterns in order to deal with technical, logistical, administrative, and commercial entities with positive economic consequences of interaction for all the parties involved.

## 7.6.2 IMPLICATIONS FOR FURTHER RESEARCH

Starting from the idea that the critical task in the development of a new venture is merging with the pre-existing network, which requires the establishment, development, and maintenance of new business relationships with customers and suppliers, we inferred that the critical point in developing a new business is not the individual entrepreneur's skill to discover opportunities, or finding a way to exploit a new solution or product, or to formally organize a new business. Rather, based on our findings, the critical issue in forming a new business is to succeed in relating, which means connecting to and interacting with others. This relating aspect has some implications for the individual entrepreneur's abilities. We found that without relating and interacting the ability to learn by trial and error is reduced and consequently the ability to generate economically valid solutions is reduced. As shown by the cases, it may be the same

customer who facilitates the development of the new business by providing a business solution that can be effectively implemented.

Some scholars are unlikely to find our argument surprising. In fact, our findings are consistent with the arguments put forward in the business network approach, which suggests that an extremely critical phase in the development of a new business is the process of merging with the market network. In particular, our findings regarding the difficulties in developing new businesses relationships are consistent with the arguments in the IMP research tradition that multifaceted and complex business relationships are consolidated through interactions that allow mutual adaptation, dependence, and ties, and involve varying relational investments (Håkansson et al., 2009). However, we are convinced that our study illustrates some implications for new ventures in developing new relationships that have not been documented in past research. In fact, what we found is that in the literature about entrepreneurship and new venturing few if any researchers have dealt with the interaction processes underlying the development of business relationships when a new business is formed. We believe that, given our results, the network perspective on new venturing is a promising and fruitful path to follow in order to develop our understanding of new business formation.

The structure of relationships, in particular interactions that cover a wide range of functions and activities in firms, makes the empirical study of relationship development a challenging research area. Therefore, we believe a better understanding of this process can yield insights regarding this important empirical phenomenon: the formation of new relationships when a new business forms. We believe further research exploring the processes covered in this thesis could be rewarding for practitioners and researchers.

However, an implication of this study is that we need a better conceptual framework to study the interaction aspects in developing new business relationships. In particular, three issues that emerged in this study need to be explored in greater depth.

Since developing new business relationships is critical for the development of a new business and central to the dynamics of business networks, an issue that deserves particular attention is the implications inherent in the actors' ways of actively relating to

others and how this issue can be managed in new businesses. Having remarked that interaction capabilities are central to new business development, research on entrepreneurship should focus more on the nature and importance of interaction capabilities and explore how the individual's capacity to interact, communicate, learn, and teach is transferred to a collective level.

We believe these issues not only enhance scholars' understanding of the relevant business phenomena, but are also central to business practitioners. In this regard, it is comment on the way in which we approached the problem of exploring and identifying critical entrepreneurial activities in the formation of business relationships, namely the interaction processes between the firm and market. In fact, in discovering the criticalities characterizing the processes of new relationship development, we did not really identify precise observations (recurrent categories and dimensions) that could be aggregated and compared. Therefore, it would be interesting in future research to elaborate a method as well as develop suitable measurement constructs to capture and measure more precisely the relative weight of the critical issues characterizing the interacting processes and the relating capabilities of businesses in the early stages of their development. We recognize the need to identify and develop a set of appropriate analytical concepts and apply them to different empirical cases.

It would also seem to be useful to carry out research that aims to capture the "underlying cost dimensions" for all the parties involved in developing new business relationships. In particular, we believe that the "economics of interaction" would be particularly suitable for future research. This implies the need to turn attention to the economic consequences of interaction for all the parties involved.

From a methodological point of view, it seems a better understanding of the phenomenon under study could be achieved by considering perspectives that different actors (and potential actors) have when they engage in or plan to become engaged in a new relationship. If it is true that actors' respective actions and reactions in one relationship can have an effect on other connected relationships in the network and, consequently, changes elsewhere in the network can affect a given relationship, further research should consider more longitudinal bilateral studies. In order to add knowledge

to the understanding of the dynamics in business relationships between companies, future studies should focus on the relationships of business actors and not just on those of single actors.

Since recent entrepreneurship research appears to acknowledge that new business formation is about collective enacting of change and has evident organizing effects (e.g. Håkansson, 1989; Dubois, 1998; Waluszewski, 2004; Cantù, Corsaro, 2011; Andersson et al., 2011), we believe further studies of the new business formation processes should take an inter-organizational perspective (Davidsson, 2003; Lechner et al., 2006; Stuart & Sorenson, 2007; Sarasvathy, Dew, & Ventresca, 2009; Jack, 2010, Welter, 2011), as a contextualized view of entrepreneurship contributes to our understanding of the difficulties and unpredictability characterizing the processes of merging into a pre-existing context. Hence, further research should aim at refining both the analytical schemes and methodology for assessing and measuring certain interacting features that may be related to the difficulties or special requirements encountered in developing a new business.

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# Appendix

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## 9.1 GUIDE FOR THE INDIVIDUAL SEMI-STRUCTURED INTERVIEWS

To: founders and co-founders of the new ventures;

Aim: get a picture of the new business and the roots of the business idea to get an overall view. Gain information about the company's main networking practices with their first customers and suppliers.

1. Sample ID: \_\_\_\_\_
2. Date IW Began: \_\_\_\_\_
3. Date IW Completed: \_\_\_\_\_
4. Length of IW: \_\_\_\_\_ (Minutes)
5. Interview Checkpoint:
  - a. IW completed with no interruption requiring call-back.
  - b. IW completed with one or more interruptions requiring X call-back.

## OPEN QUESTIONS:

1. What kind of business are you starting?  
(Could you tell me a little more about the product or service you intend to provide?)
2. What was the motivation to begin a new business? And when did you begin to think about it?
3. Could you describe the rationale of how this new venture creates, delivers, and captures value? (Business model)
4. What are the main difficulties you met since you decided to start with this new business?
5. What are the main problems you met since you decided to start with this new business?
6. Has the start-up been formally established by registering with the appropriate government agency? If yes, in which legal form and when?
7. Is the product or service that this new business will sell completely developed and ready for sale or delivery?
8. How long did the development phase take?
9. Have purchases been made of any raw materials, inventory, supplies, or components specifically for this new business?
10. Components, technologies or procedures, required for this product or services where generally available? (Resource adaptation)
11. How much did you invested for these purchases?
12. How many suppliers did you get in touch with?
13. Has this new business already received any money, income, or fees from the sale of goods or services?
14. Has monthly revenue ever exceeded monthly expenses for this new business?
15. Have financial institutions or other people been asked for funds for this new business?
16. How many customers do you have? And when did you acquire the first one?

17. How many potential customers did you get in touch with?
18. Today the largest customer accounts for?
19. Has an effort been made to talk with potential customers about the product or service of this new business?
20. Do you expect the product/service to be adapted to your specific customers?  
The product/service will be customer specific?
21. How easy or difficult was to explain to the customer the product/service value and advantages?
22. Developing interaction between customer and suppliers is considered to be critical for the development of a new business. Did you experience some difficulties in establishing and managing those kinds of interactions? What were the main complexities?