Chapter 12—Strategic Entrepreneurship

CHAPTER SUMMARY

This chapter explores how strategic entrepreneurship is important for keeping firms flexible in a complex, dynamic, and uncertain competitive environment, where the tendency to resist change and conform exert restrictive pressures on firms. Several topics are examined to describe how firms produce and manage innovation, including entrepreneurship in a strategic context, international entrepreneurship, and methods of innovating internally or through cooperatives and acquisitions.

CHAPTER OUTLINE

Strategic Entrepreneurship and Innovation
  - Innovation
  - Entrepreneurs
  - International Entrepreneurship
Internal Innovation
  - Incremental Innovations
  - Radical Innovations
Implementing Internal Innovation
  - Cross-Functional Product Development Teams
  - Facilitating Integration and Implementation
  - Creating Value from Internal Innovation
Innovation through Cooperative Strategies
Innovation through Acquisitions
Creating Value through Strategic Entrepreneurship
Summary

KNOWLEDGE OBJECTIVES

1. Define and explain strategic entrepreneurship.
2. Explain the importance of entrepreneurial opportunities, innovation, and capabilities.
3. Discuss the importance of international entrepreneurship and describe why it is increasing.
4. Describe incremental and radical innovations and the firm characteristics and actions that foster them.
5. Discuss how cooperative strategies such as strategic alliances are used to develop innovation.
6. Explain how firms use acquisitions to increase their innovations and enrich their innovative capabilities.
7. Explain how the practice of strategic entrepreneurship creates value for customers and shareholders of all types of firms, large and small, new and established.
Chapter 12—Strategic Entrepreneurship

LECTURE NOTES

<table>
<thead>
<tr>
<th>See slides 1-3.</th>
<th>Key Terms</th>
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| See Additional Notes Below. | - **Strategic Entrepreneurship** - occurs as firms seek opportunities in the external environment that they can exploit through innovations.  
- **Corporate Entrepreneurship** - use or application of entrepreneurship within an established firm. |

| Additional Discussion Notes for Strategic Entrepreneurship - These notes include additional materials that examine the concept of strategic entrepreneurship. |

**Strategic Entrepreneurship**

Why do we study and pay so much attention to entrepreneurship? (Clue: Not because we think that it is a sexy topic.)

The Global Entrepreneurship Monitor (GEM) started in 1997 as a joint research of Babson College, London Business School, and the Kauffman Center for Entrepreneurial Leadership at the Ewing Marion Kauffman Foundation. The long-term, multinational project included the G7 nations (Canada, France, Germany, Italy, Japan, the United Kingdom and the United States) and Denmark, Finland and Israel. In 2000 the Global Entrepreneur Monitor project added 11 countries: Argentina, Australia, Belgium, Brazil, India, Ireland, South Korea, Norway, Singapore, Spain and Sweden. All in all, more than 42,000 individuals were surveyed and nearly 800 experts were interviewed around the globe. The key findings and implications for public policy were compelling:

- *Entrepreneurship is strongly associated with economic growth.* All countries with high levels of entrepreneurial activity also have above average economic growth. Only a few high growth countries have low levels of entrepreneurial activity.

- *Entrepreneurial activity differs significantly between countries.* In Brazil, one of every eight adults is starting a business, whereas in the United States it is one in 10. It is one in 25 in Germany and the United Kingdom; one in 50 in Finland and Sweden, and one in 100 in Ireland and Japan. There were also differences between countries in the prevalence of new firms. The rates range from 9% in South Korea to less than .5% in Japan and Ireland.

- *Most firms are started and operated by men, with peak entrepreneurial activity among those aged 25–34.* Men are twice as likely as women to be involved in entrepreneurial activity. The ratio of male to female entrepreneurs varies from 5:1 in Finland to less than 2:1 in Brazil and Spain.

- *Financial support, particularly from nonventure capitalists, is highly associated with entrepreneurial activity.* Venture capital
investments in 1999 ranged from 52% of Gross Domestic Product (GDP) in the United States to 2.2% in Japan. The average amount invested per company ranged from slightly more than $13 million in the United States to less than $1 million in many other countries. Total private investments in U.S. entrepreneurial companies in 1999 was over $63 billion, which is substantially more than the $46 billion invested in start-ups by venture capitalists. Thus, the informal private investments in emerging and new businesses dwarf the more formal venture capital outlays.

- **Education plays a vital role in entrepreneurship.** If the level of participation in post-secondary education were the only factor used to predict entrepreneurial activity, it would account for 40% of the difference between Global Entrepreneur Monitoring countries. The experts interviewed in each of the 21 nations noted that providing entrepreneurship education should be a top priority.

- **Policies geared toward boosting entrepreneurial activity should not be confined to the entrepreneurship sector per se.** Countries with higher levels of entrepreneurial activity are characterized by lower levels of corporate and marginal personal income tax rates. The most entrepreneurially active countries also have a greater ease of doing business, more flexible labor markets, and lower levels of non-wage labor costs.

- **The perceived social legitimacy of entrepreneurship makes a difference.** Countries with high entrepreneurial activity also enjoyed stronger social legitimacy for entrepreneurship. Measures of social legitimacy included such indicators as (a) the extent to which fear of failure acts as a deterrent to starting a new firm; and (b) respect for those starting new firms.

To recap, improvements in our standard of living depend to a remarkable degree on the success of industrial innovations, which is highly related to entrepreneurship. The promotion of entrepreneurship, its role in society and the opportunities it presents for personal gain, appear to be critical for facilitating economic growth.


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**Strategic Entrepreneurship and Innovation** - This section defines entrepreneurship as a desirable and important mechanism for creating opportunities, helping firms adapt to change, and driving national economies.
### Chapter 12—Strategic Entrepreneurship

#### Key Terms
- **Entrepreneurship** - process by which individuals or groups identify and pursue entrepreneurial opportunities without the immediate constraint of the resources they currently control.
- **Entrepreneurial Opportunities** - conditions in which new products or services can satisfy a need in the market, due to competitive imperfections and unevenly distributed information in the market.

#### Questions
1. **What are some of the characteristics of entrepreneurial firms?**
   - a. Risk takers
   - b. Committed to innovation
   - c. Proactive

2. **Why is entrepreneurship of interest to nations in addition to individual firms?**
   - a. It promotes economic growth.
   - b. It increases productivity.
   - c. It creates jobs.
   - d. It drives the economies of the nations in which it exists.

#### Innovation
- This section describes the creation of new or enhanced resources to produce wealth through innovation, an essential characteristic of high-performance firms. Three types of innovative activity are defined.

#### Key Terms
- **Invention** - act of creating or developing a new product or process.
- **Innovation** - process of creating a commercial product from an invention.
- **Imitation** - adoption of an innovation by similar firms.

3. **How do invention and innovation differ?**
   - a. Invention brings something new into being—technical criteria determine its success.
   - b. Innovation brings something new into use—commercial criteria determine its success.

4. **What does the process of imitation often lead to?**
   - a. Product or process standardization
   - b. Products made with fewer features
   - c. Products offered at lower prices
### Entrepreneurs

This section defines and discusses entrepreneurs and the entrepreneurial mind-set needed to continuously create new innovations, an ability which is embedded in the entrepreneurial nature of the people in the organization and the systems and processes used by the firm.

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<tr>
<th>See slide 10.</th>
<th><strong>Key Terms</strong></th>
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<tbody>
<tr>
<td></td>
<td>• <strong>Entrepreneurs</strong> - individuals throughout an organization, acting independently or as part of the organization, who create a new venture or develop an innovation and take risks by introducing them into the marketplace.</td>
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<td>• <strong>Entrepreneurial Mind-set</strong> - viewpoint which values uncertainty in the marketplace and seeks to continuously identify opportunities with the potential to lead to important innovations.</td>
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<tr>
<th>See slide 11.</th>
<th>5. What are several characteristics of entrepreneurs?</th>
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<td>a. Optimism</td>
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<td>b. High motivation</td>
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<td>c. Willingness to take responsibility</td>
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<td>d. Courage</td>
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<td>e. Passion for value</td>
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<td>f. Entrepreneurial mind-set</td>
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<tr>
<th>See slide 12.</th>
<th>6. What challenges does a firm face in an effort to create an entrepreneurial culture that inspires individuals and groups?</th>
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<td>a. Identifying people with the intellectual talent and an entrepreneurial mind-set.</td>
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<td>b. Managing the intellectual talent and knowledge to realize its potential.</td>
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<td>c. Developing and expanding the knowledge base to foster entrepreneurship with tools such as:</td>
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<td>i. Information systems</td>
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<td>ii. Training programs</td>
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<td>iii. Cross-functional teams</td>
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### International Entrepreneurship

This section discusses the benefits that place entrepreneurship at the top of public policy agendas in nations throughout the world, the dimensions of international entrepreneurship, and the associated risks.

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<th>See slide 13.</th>
<th><strong>Key Terms</strong></th>
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<tr>
<td></td>
<td>• <strong>International Entrepreneurship</strong> - process in which firms creatively discover and exploit opportunities that are outside their domestic markets in order to develop a competitive advantage.</td>
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| See slide 14. | 7. What are some of the risks associated with internationalization that are relevant to entrepreneurship?  
| | a. Unstable foreign currencies  
| | b. Inefficient markets  
| | c. Insufficient infrastructures to support businesses  
| | d. Limitations on market size and growth  
| See slide 15. | 8. Describe some of the dimensions of international entrepreneurship.  
| | a. Rates of entrepreneurship across countries  
| | b. Impact of national culture  
| | i. Entrepreneurship declines as collectivism increases.  
| | ii. Exceptionally high levels of individualism can be dysfunctional for entrepreneurship.  
| | iii. Balance between individual initiative and cooperative spirit and group ownership of innovation is required.  
| | c. Level of investment outside of the home country made by new ventures  
| | d. Top executives with international experience  
| See slide 16. | 9. What are three methods used by firms to innovate?  
| | a. Internal innovation  
| | b. Cooperative ventures  
| | c. Acquisitions  

**Internal Innovation** - This section discusses the deliberate efforts by firms to develop inventions and innovations within the organization, defining both the types of innovation and the specific processes through which each type is produced.

| See slides 17-18. | **Key Terms**  
| | - **Internal Corporate Venturing** - set of activities firms use to develop internal inventions and innovations.  
| | - **Incremental Innovation** - process of internal innovation achieved by building on existing knowledge bases and providing small improvements in well-defined current product lines.  
| | - **Induced Strategic Behavior** - top-down process whereby the firm’s current strategy and structure foster product innovations that are closely associated with that strategy and structure.  
| | - **Radical Innovation** - process of internal innovation achieved by generating significant technological breakthroughs and creating new knowledge.  

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### Autonomous Strategic Behavior
- **Autonomous Strategic Behavior** - bottom-up process in which product champions pursue new ideas, often through a political process, to develop and coordinate the commercialization of a new good or service.
- **Product Champion** - individual with an entrepreneurial vision of a new good or service who seeks to create support in the organization for its commercialization.

**See slide 19.**

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<tr>
<th>Question</th>
<th>Answer</th>
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| 10. What are the two types of internal innovations and what processes are used in their development? | a. Incremental innovation - induced strategic behavior.  
   b. Radical innovation - autonomous strategic behavior. |
| 11. Describe the strategic implications of each type of internal innovation. | a. Incremental innovation - the strategy in place is filtered through the firm's existing hierarchy (does not alter the firm's current strategy).  
   b. Radical innovation - knowledge is integrated into the development of new products that are taken into new markets in new ways of creating value (tends to diverge from firm's current strategy.) |

**Additional Discussion Notes for Strategic Entrepreneurship and Innovation** - These notes include additional materials that cover discussions of innovation, autonomous strategic behavior, and incremental and radical innovations.

**Strategic Entrepreneurship and Innovation**

While imitation is one of the sweetest compliments to incumbents, entrepreneurs and strategists become successful innovators when they have the ingenuity and courage to originate—not imitate.

*How many new ideas does my company need to screen so as to obtain a single commercial good or service?* The answer, of course, will vary across industry domains and market segments, but research suggests that it takes about 3,000 raw ideas to produce one substantially new commercially successful product. To give more concrete examples, Stevens and Burley (1997) noted that drug companies typically require a higher number of starting ideas (north of 8,000 ideas) for every successful commercial new product. Alternatively, if a company is developing product line extensions, instead of substantially new products, then fewer ideas are needed for each commercial success.


**Autonomous Strategic Behavior**
How much capital does my company need to invest so as to obtain a single commercial good or service? Again, the answer varies across industry domains and market segments, but recent studies report that among publicly-traded pharmaceutical companies, the average cost of launching a new prescription drug is between $250 million and $802 million (Shulman, 1999; Tufts Center for the Study of Drug Development (CSDD), 2002). The CSDD suggests that a single daylong delay during FDA’s Phase I of new product application carries direct out-of-pocket expenditures of approximately $30,000 and that, for an average product, a single daylong interruption results in approximately $1.3 million in lost prescription sales. Additionally, only a few drugs account for much of companies’ revenues, which disproportionately punish companies unable to keep up with the race to innovation. Finally, despite blockbuster successes, most drugs and related products fail to reach their intended markets or to generate market interest. Thus, the innovation journey from lab bench to marketplace is characterized by tremendous peril and dead ends.

Incremental and Radical Innovation

What can companies, struggling to steer through these troublesome times, do to thrive?

Recently, Gary Hamel said in Fortune that when signs of shaken confidence abound, when consumers are keeping their wallets shut, when layoffs are accelerating, when profits are evaporating, it is clear that the boom times of the 1990s are truly over. In such circumstances, retrenchment is a natural instinct. Yet retrenchment cannot be the only answer to the current crisis. If there is one essential quality that underpins success in a world of stupefying change, it is resilience: the capacity to adapt to radically new circumstances and emerge from a crisis not merely unbroken but substantially stronger.

Hamel explains that there is a reason that many Industrial Age Paragons, from AT&T to Coca-Cola to Motorola to Intel, are struggling to adapt to a world where change is changing, and changing fast. Most companies are much better at optimization than they are at rule-breaking, game-changing strategies leading to innovation. Optimization and incremental innovation are wired into incumbents’ metrics, woven into their management processes, and into their compensation criteria. Radical innovation, experimentation, and creativity are tolerated when safely corralled in R&D or product-development units, or locked up inside of incubators and new venture divisions, but they are seldom full-throated rivals to optimization. Simply put, most companies do not do paradox well. To succeed, therefore, firms must embrace paradox wholeheartedly and unreservedly; to be single-minded about nothing.

This lopsided enthusiasm for incrementalism was forgivable, Hamel says, when change meandered rather than lurched. But in a discontinuous competitive space, an inability to manage the paradox of optimization and innovation leads to failure. The recipe for such failure is simple: pour ever more energy into optimizing what is already there. To thrive in turbulent times, a company must do more than retrench: It
must give customers new and compelling reasons to buy; it must reinvent its cost structure; it must build new growth platforms, and leverage on its competencies and assets. And to do all of that, it must use innovation.

Through the eons, cataclysmic change has always accelerated the pace of innovation. The unprecedented challenges that now face companies will, likewise, dramatically accelerate organizational evolution. Incumbents, already challenged by disruptions of technology, more powerful customers, relentless margin pressure, and a horde of unorthodox newcomers, will in the next few years give way to companies with entrepreneurial mindset. What will the entrepreneurial mindset company look like? A few things are certain: it will balance optimization and innovation, focus and experimentation, discipline and passion, evolution and revolution. Accommodating these paradoxes will require ambidextrous strategists.

Source: Hamel, G. 2001. What CEOs can learn from America. In these turbulent times, business should turn to a 225-year-old teacher. Fortune. October 28 (http://www.fortune.com/fortune/articles/0,15114,370431,00.html)

**Implementing Internal Innovation** - This section outlines the factors that encourage and discourage innovation in established firms executing internal innovation efforts.

<table>
<thead>
<tr>
<th>See Table 12.1: Factors Encouraging and Discouraging Innovation in Established Firms (slides 20-21).</th>
<th>12. What actions do established firms who are successful at internal innovation take?</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>a. Encourage people to discuss new ideas and take risks.</td>
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<td>b. Tolerate failure, and encourage learning from mistakes.</td>
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<td></td>
<td>c. Establish reward systems that encourage innovation.</td>
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<td>d. Establish processes and structures to effectively integrate the innovative process across functions.</td>
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**Cross-Functional Product Development Teams** - This section presents cross-functional teams that facilitate organizational efforts to integrate different activities and coordinate and apply knowledge from different functional areas to maximize innovation.

<table>
<thead>
<tr>
<th>See slide 22.</th>
<th>13. What are some of the barriers that may prevent the successful use of cross-functional teams?</th>
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<tbody>
<tr>
<td></td>
<td>a. Independent frames of reference of members with distinct specializations.</td>
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<td>b. Organizational politics that create competition for resources and interunit conflict.</td>
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<tr>
<th>See slide 23.</th>
<th>14. What four dimensions do functional units vary along?</th>
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<tbody>
<tr>
<td></td>
<td>a. Time orientation</td>
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| b. Interpersonal orientation  
| c. Goal orientation  
| d. Formality of structure |

**Facilitating Integration and Implementation** - This section emphasizes the importance of shared values and effective leadership to successfully innovate and the value of high-quality communication systems to facilitate cross-functional integration (See slide 24.)

**Creating Value from Internal Innovation** - This section illustrates the factors that create value from internal processes of new product development and commercialization.

| See Figure 12.1: Creating Value from Internal Innovation Processes (slide 25). |
| 15. What three factors contribute to value creation from internal innovation? |
| a. Entrepreneurial mindset—necessary for managers and employees to consistently try to identify entrepreneurial opportunities that the firm can pursue by developing new goods and services and new markets. |
| b. Cross-functional product development teams—important to promote integrated new product design ideas and commitment to their implementation thereafter. |
| c. Effective leadership and shared values—required to promote integration and vision for innovation and commitment to it. |

**Innovation through Cooperative Strategies** - This section describes the use of alliances, by both entrepreneurial ventures and established firms, to share the resources and knowledge required to produce continuous innovation for the firm, along with the risks associated with innovation through cooperative strategies. (See slide 26.)

**Innovation through Acquisitions** - This section describes the use of acquisitions to support innovation efforts and rapidly extend product lines strategically, along with the risks associated with innovation through acquisitions. (See slide 27.)
Creating Value through Strategic Entrepreneurship - This section wraps up the discussion of strategic entrepreneurship, comparing the ability of new entrepreneurial firms to identify innovative opportunities to the ability of larger, older firms. It discusses the balance between gaining competitive advantage and identifying entrepreneurial opportunities, the importance of a global perspective for innovation strategies, and the contribution that strategic entrepreneurship makes to nations’ economic development.

See slides 28-29.

16. Compare new entrepreneurial firms to larger, established firms in their ability to identify innovative opportunities.
   a. Entrepreneurial ventures
      i. Produce more radical innovations
      ii. Possess strategic flexibility and willingness to take risks
      iii. Do more opportunity seeking
   b. Larger, well-established firms
      i. Produce more incremental innovations
      ii. Possess more resources and capabilities to exploit identified opportunities
      iii. Do more advantage seeking

Ethical Questions - Recognizing the need for firms to effectively interact with stakeholders during the strategic management process, all strategic management topics have an ethical dimension. A list of ethical questions appears after the Summary section of each chapter in the textbook. The topic of ethics is best covered throughout the course to emphasize its prevalence and importance. We recommend posing at least one of these questions during your class time to stimulate discussion of ethical issues relevant to the chapter material that you are covering. (See slides 30-34.)