"CHOOSE YOUR BATTLEFIELD: GIVING NEW VENTURES A BETTER CHANCE"
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Summary:

Why do some new ventures succeed and not others? Traditional answers usually invoke poor management, flawed product, insufficient cash or weak marketing. This paper proposes a new set of answers. From an analysis of 377,000 new US businesses and a number of UK case studies, it is clear that other factors also play a decisive role including: a product's purchase frequency, service requirements, customer/distributor fragmentation and labour intensity. Careful analysis of such product market characteristics prior to start-up significantly increases the chances of survival and success. This paper demonstrates that choosing the right battlefield is absolutely critical. It provides a framework to guide both the new venturer and investor in making this key decision - where to fight?

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IMPROVING THE ODDS

During any single year, the Dun and Bradstreet Corporation lists over 200,000 business start-ups in the USA alone.¹ These include new, independently owned firms along with new subsidiaries formed by corporate groups as they diversify. Everyone from Aunt Agatha to millionaire entrepreneurs and corporate chairmen have advice for these budding businesses. Formulae for success abound. Yet, the odds on their long-term survival remain poor. We tracked thousands of independent businesses which started up in 1978-9, and five years later 76 percent had disappeared, meanwhile some 47 percent of new corporate ventures in our sample had been wound up².

The golden rules of new venture management, and the pitfalls, have been well rehearsed: the need for a realistic and detailed business plan, managing cash flow with an eagle eye, hiring and motivating the right staff, listening to the customer, ensuring access to relevant experience with a balanced management team, to name just a few. Clearly all these things are necessary, but will they prove sufficient? Even if you do all the ‘right’ things as a new venture, are there times when you are enthusiastically fighting a losing battle? Are there signs to look out for which can help indicate the best

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¹ The Dun and Bradstreet Corporation, Business Starts Record, annual.
² Based on a sample of 29,581 independent startups and 5,749 new corporate subsidiaries which commenced operations in the US between 1978 and 1980 drawn from Dun & Bradstreet databases.
market segments in which to start? The results of this study suggest the answer is 'yes'.

Of course there are always the exceptions which succeed by plunging into the most hostile of dens. However, we find that certain product and market environments have systematically offered new firms a greater probability of survival. In industry after industry across our database of 377,000 US businesses, certain types of customer, product and information characteristics - turning on such issues as frequency of purchase or level of service requirements, on degree of dependence on pull marketing through the media or on third party channels and push marketing - have signalled whether the territory is fertile or hostile for the new venture.

Having established the key issues for chances of survival, and made a statistical analysis of the data, we followed up with case study research, this time in Britain. These practical examples confirm our major findings and help illustrate their application. Choosing the right battlefield, it seems, is crucial to giving new ventures a better chance.

BARRIERS TO SURVIVAL AND THE COMPETITIVENESS OF NEW VENTURES

The closest analogy to economists' usual conception of barriers to entry is a 'perimeter wall'. Potential entrants, peering over the wall, assess how green is the grass and rich the profit pasture on the other side. Having assessed the cost of scaling the wall by developing competitive product, constructing a competitive plant and advertising their wares, they decide whether or not to jump. They are either 'in' or 'out' of an industry.

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In fact, as the managers of many a new venture will testify, entry is not even half the battle. Getting up and running and finding the first few trial customers among the ‘experimenters’, while not to be underestimated, is often the easy bit. The real challenges arise in meeting the requirements for long term survival. This means winning over the more conservative customers, displacing competitors, maintaining the quality of product and service, and growing the business. The second barrier is less like a wall and more like a minefield, and it has to be closed before reaching secure ground. For six or even ten years, new ventures face handicaps in competing against older, established businesses who enjoy the benefits of accumulated experience and access to well-stocked war chests built up over time. This means that each step must be taken with care so as to ensure continued existence. The critical problem for new ventures lies not so much in barriers to entry, but in barriers to survival.4

Figure 1: The Race For Survival

<table>
<thead>
<tr>
<th>Industry-specific Assets</th>
<th>Newly Required Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Incumbents</strong></td>
<td><strong>Potential Entrants</strong></td>
</tr>
<tr>
<td>Original Endowment + Accumulated Assets</td>
<td>ASSET ACCUMULATION GAP</td>
</tr>
<tr>
<td><strong>INNOVATION GAP</strong></td>
<td>Endowment</td>
</tr>
</tbody>
</table>

4 These concepts are discussed in more detail in P.J. Verdin and P.J. Williamson, 'From Barriers to Entry to Barriers to Survival', in Strategic Management Society, 1991 Conference Papers and Proceedings, forthcoming.
A new venture's survival problem can be analysed in terms of the matrix in Figure 1. It comes into the world with an endowment of assets and know-how from its founders or corporate parent. To have any chance of crossing the minefield of youth this endowment must obviously allow it to offer potential customers some advantages over their established suppliers; new technology or higher service standards, for example. A venture's early customers may enthuse over these benefits but, more often than not, they will also have to put up with some of the new venture's deficiencies in exchange. They may have to suffer reduced convenience, for example, because the new venture has limited initial distribution, lacking access to the same extensive network enjoyed by more established suppliers. Likewise they will have to take the risks of buying a brand with little track record and unproven capability to maintain after sales service. Customers may also suffer from supply shortages or quality failures which arise from new venture's inexperience in mass production. In order to continue to satisfy its 'experimenter' customers and outperform established rivals, a venture must close the 'asset accumulation gap' in figure 1 -- accumulating the raft of specialised infrastructure and knowledge necessary to add to their start-up endowments.

All this takes time. This is one luxury few new ventures have because, while they are busy learning, established rivals are unlikely to be standing still. Under threat from a new venture, they face a different problem -- how to close the 'innovation gap'. Their challenge is to copy what is best about the new venture's offering and then lever off their established assets -- brands, distribution networks, facilities and mass production experience -- to exploit the innovation before new competitors can get a safe place in the market.

Closing the 'innovation gap' also takes time. Established firms are often hampered by old habits and ingrained procedures. If they fail, they could ultimately wither and die. What figure 1 depicts then, is a race for survival. A venture's initial product or service innovations will not allow it to survive in the long term if they can be quickly imitated.
by established firms. If incumbents fail to learn new tricks quickly enough, on the other hand, new ventures will have time to gain the upper hand. Given this race for survival, our hypothesis is that by choosing their place in the market well, a new venture can systematically increase its chances of success.

PRODUCT CHARACTERISTICS, BUYING PATTERNS AND BARRIERS TO SURVIVAL: THE LINKS

In assessing the barriers to survival faced by a new venture in any particular market segment, we developed measures of three groups of characteristics:

- Customers' buying patterns
- Competitors' marketing and channel strategies
- Production requirements

Together these signal the main differences in the type and extent of infrastructure and accumulated experience a new venture requires to satisfy customer needs, to get its marketing message heard and its product distributed, and to provide competitive quality and stability of supply. Our data enabled us to measure a total of ten indicators of these characteristics for each product market segment. We expected some of these indicators to flag hostile market territory for a new venture; others, by contrast, suggested the availability of safe paths through which a new venture might cross the minefield of youth to long-term survival and prosperity. The impact of a particular characteristic might also be expected to vary between independent start-ups and new ventures launched by diversifying corporate groups. The specific indicators were as follows.

Customer buying patterns

Here we measured frequency of purchase, whether or not the purchase was a 'major' purchase for the individual buyers in the segment (a car, for example, may be 'major'
purchase for the individual but not a major purchase for a large multinational), and the degree of fragmentation of buyers.

*Purchase frequency.* This was measured by the proportion of product line which users generally purchased less than once a year, compared with products which were purchased frequently. When a product is purchased infrequently, the customer is less likely to believe that the relative quality of different brands is the same as the last time he or she examined the alternatives available. If customers reassess what is on offer and collect new information, it will favour new ventures by increasing the likelihood of a switch. In frequently purchased goods, by contrast, experience with an established brand is recent. Both individuals and firms tend to continue buying frequently purchased items from the same supplier provided they are broadly satisfied with price and service. For instance, an industrial firm doesn't conduct a tender for their business every time they go to purchase a new delivery of cardboard packaging. To capture the new customers it needs to survive and grow, a new venture must generally do more to induce trial, often at considerable cost, the higher is purchase frequency.

*Purchase significance.* We measured this characteristic by percentage of the product line which represented a major purchase for the ultimate buyer (more than $200 for households; judgmentally determined for non-household buyers). Theoretically, the impact of this characteristic on the difficulty of survival could be either positive or negative. The high cost of an error in a major purchase may deter buyers from trying the product of a new venture rather than continuing with established suppliers. On the other hand, the higher significance of a major purchase makes it more worthwhile to incur the costs of collecting new and objective information rather than relying on past experience or manufacturer's claims. On balance, we expected that risk aversion

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would be the dominant influence, so that barriers to survival for a new venture would be higher the more 'major' the purchase.

Customer/distributor fragmentation. This is measured by the percentage of product lines for which there were over 1,000 customer accounts at the manufacturer level, whether they are final users, resellers or a mix of these groups. This is thus an indicator of the degree of customer fragmentation a supplier must contend with. High levels of customer or distributor fragmentation increases the magnitude of the selling, logistics and distribution task because wide coverage is necessary for even moderate sales. Since the unit costs of sales and distribution infrastructure and systems have been found to reduce with both scale and operating experience, we might expect established firms to be at a greater advantage relative to new ventures when customer and distributor fragmentation is high. After allowing for the impact of purchase significance and frequency, a new venture will generally be better off where sales sufficient to survive can be captured by converting a few customers or distributors.

Competitors' marketing and channel strategies

This group of indicators captures the importance of ‘pull’ marketing (media promotion aimed directly at consumers) and ‘push’ marketing (promotion through the channel and point of sale) in the strategies of established competitors. We also measure the proportion of existing supply which flows through intermediate channels as against the flow direct to the customer.

Pull marketing: This characteristic is measured by expenditure on media advertising as a percentage of total sales revenue. Here the arguments cut both ways. If a burst of media advertising is a good way for new ventures to make themselves look larger and

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better established than they are, then new ventures may be able to leapfrog much of the slow process of building a brand through years of sales calls, retailer recommendation and customer word of mouth. Meanwhile, what the new venture lacks in pull marketing skills and experience may be accessible through the advertising agency. In this case, media advertising may carry the new venture safely through the minefield of youth by quickly establishing a significant base of sales. This approach will be particularly viable for corporate ventures which enjoy the financial backing of a parent corporation with deep pockets.

On the other hand, brand loyalty and customer awareness may depend on the cumulative effect of media promotion over an extended period. In this case, market environments characterised by high levels of media spending - particularly in the expensive medium of television - would present a barrier to new ventures matching the resources and brand strength of long established rivals.

*Push marketing:* This measure takes the cost of marketing, excluding media spending, as a percentage of sales revenue for the product lines in each group. In many cases the need for push marketing can aggravate problems of channel dependence (below). Rather than facing a marketing medium which is available 'for hire' such as a television slot, albeit at high cost, even the opportunity to undertake push marketing often requires breaking through the resistance of channels already committed to existing suppliers. Even where it is possible to canvass customers directly, push marketing requires building and training an effective sales team capable of holding its own against competitors who have had years to hone the skills of their salesforce and coordinate the varied elements of a push marketing strategy. Where push marketing is critical, therefore, we can expect new ventures to face a harder slog for survival against established competitors. This is especially true if the incumbents react by using their existing market relationships to increase the push marketing stakes in response to the appearance of new competition.
**Channel dependence:** The measure used here is the percentage of products which pass through an intermediary before reaching the user, that is, the degree to which the product requires access to a distribution channel in order to reach the final customer. In his book on brand choice, Porter argued that ‘for products sold through convenience outlets, ... gaining access to distribution actually becomes easier as the brand image matures’. This reflects the fact that where goods must be sold through retail convenience stores a certain density of sales is required to make it economic to handle the brand. In ‘nonconvenience goods’, meanwhile, the retailer, wholesaler or agent may be unwilling to carry the unknown brand of a new venture because it requires extra sales effort or may sour the relationship with established suppliers. In these cases, new ventures may be effectively blocked from gaining exposure to customers. The opportunity to sell direct to target customers will therefore tend to help a new venture in its early years.

**Production requirements**

This final set of characteristics uses indicators of labour intensity versus capital intensity of the operations, the level of employee skill required, the importance of after-sales service and the degree to which products must be ‘made to order’.

**Labour versus capital intensity:** We measured intensity of labour as against capital by calculating the ratio of total employees to the total book value of plant and equipment in the industry producing each group of products. Expectations about the effects of these indicators on barriers to survival go both ways. Where industries are capital intensive, new ventures have the opportunity to capture state-of-the-art knowledge by setting up with the latest equipment and a lean labour force. The established firms, meanwhile, may be saddled with earlier vintage equipment which is less productive, but not yet

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economic to replace. Conversely, the constant need to update capital equipment, often at high fixed costs, may expose the new venture to the risks of bankruptcy.

In labour intensive industries, by contrast, new ventures have a rookie team. Even if the individuals are competent and well motivated, they have not had the time and experience of working together to produce a seamless result. Yet labour intensity may also mean lower operating leverage for the entrant and hence a better chance of weathering the ups and downs of market competition.

**Employee skill requirements:** Based on job classifications, we computed the number of 'high-skilled' jobs as a percentage of total employees involved in producing the product group. To the extent that skills are specific to an industry, new ventures will be faced with the problem of hiring the necessary specialists and forming these recruits into a smoothly coordinated resource. This is notoriously difficult, particularly for businesses who are not certain of survival. In products where groups of skilled staff are an important source of advantage, therefore, new ventures are likely to suffer a greater handicap.

**Service requirements:** For each group of products we calculated the percentage of product lines requiring a 'moderate to high' degree of sales or technical service, as classified by the suppliers surveyed. In the case of after-sales service, it takes time to develop a reputation of excellence. In durable products, for example, customers of a new venture shouldn't discover how good the breakdown service is for some years. If the product sputters to a halt in the first month, they are unlikely to be impressed, no matter how quickly and efficiently it is repaired. At the same time, the customer needs to feel sure the business will still be there to deliver the service in the long run.

On the other hand, new demands for high levels of service can outstrip the capabilities of established incumbents in industries where service levels have historically been low.
High service requirements may therefore be associated with greater potential for younger, more responsive firms to differentiate themselves with the customer and overcome lack of experience in other areas. In this case we might expect new ventures to have an advantage.

**Made-to-order supply:** Here we measured the percentage of product lines which were made to order based on customer specifications. Except in the case of 'one-off' purchases, which are captured by purchase frequency, we would expect a high percentage of make-to-order sales to handicap new ventures relative to established firms. This is because successful made-to-order supply depends on a close relationship between manufacturer and customer with high exchange of information. Once a buyer has invested the time and money in explaining his or her precise needs to a particular supplier and that supplier has successfully delivered, there will be costs and risks of switching.

These then were the hypothetical relationships between product and market characteristics and the probability that new ventures would survive to grow and prosper (summarised in Table 1). Using this framework we now turn to our empirical results and their implications for defining the battlegrounds where new ventures have a better chance.
Table 1: Segment Characteristics and New Venture Survival - The Theory

<table>
<thead>
<tr>
<th>Factor</th>
<th>Hypothesised Impact on the Chances of Survival</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customers' Buying Behaviour</td>
<td></td>
</tr>
<tr>
<td>Infrequent Purchase</td>
<td>+</td>
</tr>
<tr>
<td>Major Purchase</td>
<td>-</td>
</tr>
<tr>
<td>Fragmented Customer Base</td>
<td>-</td>
</tr>
<tr>
<td>Competitors' Marketing and Distribution Strategies</td>
<td></td>
</tr>
<tr>
<td>Heavy 'Pull' Marketing</td>
<td>+/-</td>
</tr>
<tr>
<td>Heavy 'Push' Marketing</td>
<td>-</td>
</tr>
<tr>
<td>High Channel Dependence</td>
<td>-</td>
</tr>
<tr>
<td>Production Characteristics</td>
<td></td>
</tr>
<tr>
<td>High labour intensity</td>
<td>+/-</td>
</tr>
<tr>
<td>High Skill Requirements</td>
<td>-</td>
</tr>
<tr>
<td>High Service Requirements</td>
<td>+</td>
</tr>
<tr>
<td>Prevalence of &quot;Make-to-Order&quot;</td>
<td>-</td>
</tr>
</tbody>
</table>

Note: +/- reflects theoretical arguments for both effects. Which of these dominates is an empirical question.

MARKET ENVIRONMENTS IN WHICH INDEPENDENT START-UPS HAVE A BETTER CHANCE

Our first empirical investigation involved tracking the survival rates for 29,581 independent start-ups in manufacturing over five years from 1978 to 1984. A comparison of these start-ups with firms established for ten years or more in corresponding industries indicates that a new venture is on average three times more likely to exit than a well established business. However, this figure varied a great deal depending on the particular market in question. In 90 percent of markets new ventures had a higher failure rate than established firms. In the other 10 percent of markets the
new ventures actually had a higher chance of survival than a failing group of older firms. Moreover, within the great majority of market environments where the survival of new ventures was more tenuous, their position relative to established firms varied from almost level pegging in some markets to more than six times the likelihood of failure in others.

We therefore went on to test for relationships between the product market characteristics outlined above and differences in the survival rates of our new ventures relative to their well established cousins, using multiple regression techniques. The main results are illustrated in figure 2, which distinguishes hostile and fertile market segment characteristics for independent start-ups.

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8 These tests are fully described in P.J. Williamson and P.J. Verdin, 'Age, Experience and Corporate Synergy: When Are They Sources of Business Unit Advantage?', *British Journal of Management*, winter, 1992.
We found that independent start-ups had significantly better chances of survival in two types of market environments: those where the manufactured product required high levels of service support; and environments where purchase frequency was low. Products or market segments which combined both of these characteristics offered new ventures a correspondingly higher chance of long-term survival. The result on service suggests that greater flexibility, and a more responsive, listening approach to customers is one of the trump cards a new venture has to play in competing with established firms. Market segments which potentially value high levels of service therefore offer the most attractive battleground for a new venture. Among our case studies, the Domino Printing Sciences company is a good example of choosing this battlefront within its potential market and winning (see example 7 below).
Product market segments where each customer makes a purchase only infrequently also proved to be more fertile territory for our independent start-ups. This is consistent with the proposition that infrequent purchase encourages buyers to reassess the relative merits of a product afresh, so that the likelihood of buyers collecting information on and trying a new brand is increased. Datapaq Ltd in example 2 will illustrate the benefits and some of the potential costs of selling to buyers who purchase the product infrequently.

Four product-market characteristics contributed to a particularly hostile environment for independent start-ups, resulting in low probabilities of survival in our sample of manufacturing businesses. The first of these was the need for significant numbers of highly skilled employees. The second was make-to-order supply environments. Third, product market segments which were heavily dependent on channel support militated against new ventures’ likelihood of success. The final market characteristic which proved hostile to independent start-ups was a customer base which was highly fragmented. Examples 3 and 4 illustrate the issues involved through the experiences of New Covent Market Soup and Psion in surviving the distribution channel barrier to survival.
Example 1: Domino Printing Sciences - success through service

Pick up a can of Coke and you will see, printed on its base, a ‘best before’ date. Today the printing is clear, but accurately printing on a concave surface is difficult. It was this problem that Domino Printing Sciences (DPS) solved by designing a specialised ink-jet printer which provided higher speed, more accurate microprocessor control and lower risk of product damage than conventional contact methods. By subcontracting out much of the basic manufacture, DPS was able to concentrate on developing a machine that was reliable, economical and easy to use.

But a good product was not enough to overcome the concerns of production engineers responsible for mass-production lines. Should the printer fail, the bottleneck would cause millions of pounds worth of production equipment to grind to a halt; errors would be potentially devastating in a situation where the company faced consumer liability suits or had to recall a particular batch. The key to establishing the product in the market was therefore not lower prices or better technology but, as the founder put it, ‘rapid response, willing service and youthful enthusiasm’, achieved through close interaction with customers and being willing to work day and night to meet delivery commitments and ensure on-site reliability.

Sales grew from £82,000 in 1980 to £11.1 million in 1985 when the company was floated. But, seeing this success, competitors rapidly moved to close the ‘innovation gap’, copying the DPS product. As the resulting price competition intensified, the DPS reputation for reliability and the ability to provide outstanding customer service became the linchpin on which continued success depended. It has served the company well with sales for the first half of 1992 up a further 17 percent to £31 million.
Example 2: Datapaq Ltd - benefits and costs of infrequent purchase

Datapaq was founded in 1983 with a product concept - 'Tracker' - an electronic box encased in a ceramic insulating jacket enabling automobile manufacturers to accurately measure temperatures in the paint curing ovens. It is hardly the kind of product which Ford or Nissan purchase every day. Instead it is often intimately bound up with long-term re-equipping plans. In fact, it took a full three years before the company received a really substantial order for the product. By this time the patience of the venture capital investors was wearing very thin and the survival of the company was threatened. But when the breakthrough came it was a major one: Ford in the USA adopted Tracker for all of its plants. A similar agreement followed soon after with Metal Box.

This illustrates both the costs and benefits for a new venture of operating in a market segment where purchases are infrequent. The problem is that lead times are often long and dependent on the purchase cycles of key customers. But the benefit is that the buyers are much more likely to look afresh at the range of products and innovations on the market when the cycle comes around.

In getting to the stage of orders from high profile customers Datapaq had already climbed another critical barrier to survival: establishing an effective manufacturing facility for its product concept. To close this 'accumulation gap' required building up its skill base to include software development capability and technical expertise in the new ceramic materials required to house the electronics. Recognising these needs, Datapaq's founder, John Bates, deliberately chose to locate his company in Cambridge. His belief that this would help furnish him with enough technical people with the wide range of expertise needed proved well founded; almost all of those involved in the development came from the university.
Example 3: New Covent Garden Soup - surviving the distribution barrier

In 1985 Andrew Palmer seized on the idea that the distinctive flavour of truly fresh soup, not tinned or packaged, offered the opportunity to develop a new niche in the fast growing, ready-to-eat chilled foods sector. He also realised that he would have to prove his idea by selling the soup through independent retailers before he could have any chance of convincing the major supermarket chains to stock it. But there was a problem: independent retailers were unlikely to take the risk of stocking an unusual, new product with a shelf-life of only four to five days for fear of wastage in the face of low stock turn.

After two years of persistence and investment a process had been developed to produce soup with a 14 day chilled shelf life using only natural ingredients. Part of the distribution barrier associated with independent retailers had been solved. New Covent Garden Soup (NCG), however, was still faced with the need to service a fragmented customer base with a perishable product. Minimum volume requirements made it difficult to use the large chilled food distributors. Palmer built a relationship with a small, fast growing van sales business for chilled foods which served the independent food retailers in the London area. Via this route, initial sales took off quickly. The company was then able to initiate test sales through two large supermarket chains.

By the end of 1988, NCG was selling 8,500 cases per month when Sainsbury’s and Marks & Spencer launched own-label chilled fresh soups into their stores. Although Palmer regarded the products as inferior to those of NCG, the established competitors were closing the ‘innovation gap’. At the end of 1989, Unigate plc, a large dairy and fresh food manufacturer, launched a chilled soup product under its well established ‘St. Ivel Real’ brand, backed by a formidable advertising campaign. To counter these moves, NCG extended its product line with new varieties including those specially designed for summer and a ‘Soup of the Month’. Yet this expansion faced barriers. As one senior manager put it, ‘Supermarkets don’t suddenly extend the number of products they take from three to ten and award extra shelf space.’ Introducing new flavours was also resulting in the delisting of old lines in some stores in favour of new ones. NCG’s supermarket accounts were starting to ask awkward questions about how the company was going to support its brand, or suggesting the alternative of own-label products. At the same time, an increasingly dispersed customer base was leading to higher distribution costs.
NCG responded. An alliance with another chilled food producer which had acquired its own carrier and wished to improve its capacity utilisation, reduced distribution costs. By retaining a public relations firm the company was able to gain extensive free publicity in national newspapers and magazines, partly compensating for the lack of a significant marketing budget. This paved the way for intensive negotiations with a major supermarket chain which led ultimately to a nationwide roll-out of the product.

Example 4: Psion plc - bypassing distribution barriers by going direct

Over lunch in a Greek restaurant came the idea for a hand held computer with the capacity for mass storage. Fourteen months and £200,000 later Psion had a product -- the ‘Organiser’. It was a battery powered, hand held and pocket-sized device for information storage and retrieval on a large scale. Tightly controlled component subcontracting and assembly systems were set up. This left one major question: how should the Organiser be sold? The Organiser was entirely new, no market existed and the full range of its applications was uncertain. At the same time the minimum economic production run was 10,000 units to be produced over six months with a required start-up investment of £1.2 million. With a price tag of £99.50, Psion would have to shift large quantities quickly. But with unproven mass market potential, electronics retailers were cautious; with tight margins and a low unit retail price, a high volume of sales would be required before it was worth carrying the product.

Psion decided to market the Organiser directly to users by placing advertisements in computer magazines and professional periodicals, inviting interested individuals to respond by returning a coupon. The Organiser sold, but quantities took time to build up. As sales expanded, however, the direct contact with users proved to have important advantages. Psion was able to collect a wealth of information on how the product was being used and by whom. This provided the basis for product improvements such as a full inbuilt programming language with database handling and the ability to link to other computer systems embodied in Organiser II and III. The ability to continuously monitor the success of various communication channels and changing customer mix associated with going direct also meant that Psion’s market knowledge and marketing capability was continually being expanded, allowing better customer targeting and rapid response to a fast changing marketplace.
We also tracked the survival rates of 5,749 new ventures launched by established corporations over the same five year period. These were almost twice as likely to survive as the new independent start-ups. Compared with well-established firms, however, nearly twice as many exited their business. The risks of failure for corporate ventures lie midway between independent start-ups and established businesses. Again, some product market environments proved much more fertile to corporate ventures than were others. Most notably, the opportunity to use media advertising seems to act as a gateway to survival as illustrated in figure 3.

Such environments may allow these corporate ventures to draw on the financial power - and public image - of their parents and quickly close the gap between themselves and established rivals. Mars Inc’s new venture in the ice cream market (example 5 below) shows exactly how synergies with the parent company can be put to work.

In other market environments, however, young corporate subsidiaries do face barriers associated with marketing infrastructure and customer risk aversion. We found that where the purchase is a major one for the customer, older businesses enjoy a systematic advantage. Here the fact that a new venture carries the seal of approval from its parent seems insufficient. New corporate subsidiaries are also at a disadvantage when effective competition requires new infrastructure to support high levels of push marketing per unit of sales. This suggests that a long period of experience in the specific product segment is critical in building an effective network. The helping hand of a corporate parent is no substitute for time and toil.
Figure 3: The impact of product and market characteristics on the survival of corporate ventures

HOSTILE | FERTILE
---|---
Pull Marketing |  
Infrequent Purchase |  
High Employee Skill |  
Labour Intensity |  
Push Marketing |  
Major Purchase |  

Impact Coefficient of Product-Market Characteristic

Source: Estimated elasticities from a multiple regression of survival rates on product market characteristics, Williamson and Verdin (1992), op. cit.
Example 5: Mars Ice Cream - corporate synergy at work

Historically, UK adults have consumed only one third of the amount of ice cream eaten by their children. This is important in explaining why, in 1988, the British purchased an average of 7.3 litres of ice cream per head compared with 20.8 litres per head in the USA, 17.5 litres in Australia and a surprising 14.0 litres consumed by the average Swede.

Evidence from the US suggested that when adults purchase ice cream for themselves they respond to brand values, higher quality and the right packaging. This is where the possibilities for deploying Mars's marketing muscle came in. In 1986 the company purchased the Chicago ice cream maker Dove International to provide a manufacturing base. Its aim was to produce the highest quality dairy ice cream packaged in relatively small portions and capitalising on its established confectionery brands.

In Britain Mars was largely denied access to the corner shop by the existing distribution tie-ups of two dominant, existing competitors. Unilever's Walls brand accounted for 40 percent of the UK market, with rival Lyons Maid at around 10 percent market share. It therefore began by launching the product in supermarket chains, allowing it to lever off the major channel for its confectionery and pet food lines. The new ice cream product carried the familiar packaging of its Mars, Bounty, Galaxy and Marathon (now Snickers) bars; virtually confectionery in ice cream form. This synergy helped make the launch a runaway success with only a tiny fraction of the marketing expenditure normally required to introduce a new branded product. In its first year this highly branded, premium price product became the best selling take-home ice cream, notching up sales of £25 million.

Faced with new competition from an alliance between Unilever's Walls and Cadbury-Schweppes in the form of an ice cream bar branded 'Dream', Mars sought to rapidly extend its distribution reach to the freezer displays of smaller retailers. To do so it entered a fixed term distribution agreement with Lyons Maid in 1990. Having successfully accessed the benefits of corporate affiliation, both internal and external, to establish the new venture the challenge is now to strengthen and grow its position and perhaps bring the marketing order and convenience of the confectionery counter to the corner shop freezer.
Finally, manufacturing processes which depended on attracting skilled employees and moulding them into an effective team also appeared to present problems for corporate ventures. Certainly links with an established parent put them in a better position than independent start-ups, but they remained at an important disadvantage compared with well established firms. Deskilling the manufacturing process, therefore, can help to give corporate ventures a better chance of success.

THE AGE/AFFILIATION MATRIX

New ventures are, of course, not only competing with established firms, but also with each other. Independent start-ups often find themselves competing with corporate ventures and vice versa. By combining our results for start-ups with those for corporate ventures competing with established businesses the completed picture emerges in the form of the age/affiliation matrix shown in figure 4.

Figure 4: The age/affiliation matrix

<table>
<thead>
<tr>
<th>Age Advantage</th>
<th>High Advantage of Corporate Affiliation</th>
<th>Low Advantage of Corporate Affiliation</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>Made To Order</td>
<td>High Media Advertising</td>
</tr>
<tr>
<td></td>
<td>Many Customers</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Channel Dependence</td>
<td></td>
</tr>
<tr>
<td>Med.</td>
<td>Push Marketing</td>
<td>Infrequent Purchase</td>
</tr>
<tr>
<td></td>
<td>High Skill</td>
<td></td>
</tr>
<tr>
<td>Low</td>
<td>Major Purchase</td>
<td>High Service</td>
</tr>
<tr>
<td></td>
<td>Labour Intensive</td>
<td></td>
</tr>
</tbody>
</table>
LESSONS FOR THE NEW VENTURER

We all know that new ventures are not for the faint of heart. Success requires courage, perseverance, and probably some luck, as well as resources and skill. By tracking the survival rates of thousands of new ventures in different markets, however, our results lay bare another fact of life: the new venture is more likely to win on some battlegrounds than others. These differences turn out to depend on some of the most fundamental characteristics of any product: the frequency with which it is purchased, whether or not it is a major expenditure for the buyer, and the role for service. Some of the most basic features of the production process also impact on a new venture's chances of success: the need for teams of skilled employees rather than technology embodied only in machines, and whether or not the product is made to order. The way the product is marketed and sold, meanwhile, was found to have an important effect on the relative chances of survival faced by an independent start-up versus a corporate venture.

When starting out in a new venture, it pays to learn from others who have gone before. Identifying the position of your target market on the age/affiliation matrix is one place to start. Not only does it give an indication of how steep the climb ahead is likely to be, but it also helps pinpoint where the potential advantages of competitors - be they established players, independent start-ups or corporate ventures - might arise. The task is then to adjust your line of attack. For an independent start-up this may mean targeting those segments where service can play a larger role, where customers purchase less frequently, and where there are more opportunities to bypass the grip of established suppliers on existing channels by selling direct. The goal is to neutralise or side step those market characteristics which appear towards the top lefthand corner of the matrix where established firms and corporate subsidiaries can exploit their competitive strengths.
As a corporate venture, the possibility of shifting the emphasis from push towards pull marketing may be a way of improving your position. Our results also suggest that opportunities to lever off your parent’s existing distribution channels and account management systems are worth a careful look. Attempting to deskill the production process and initially build share among customers for whom your product is not such a major purchase are candidate strategies for limiting the advantages established competitors gain from production experience and customer risk aversion.

LESSONS FOR THE INVESTOR

Improving the odds and enhancing the chances of success are in the interests of both the new venturer and investor alike. These lessons for the new venturer apply just as much to any investor in a new business, although they do so in a particular way. Think for a minute about some of the key issues which a prospective investor typically considers in weighing up a new investment opportunity.

Do we really have a product (or service) which works as it is intended to? Can the product be produced? Will the volume objective be met? Why will the company gain market share? Are the costs accurate and is the target gross margin achievable? Does management have the right track record and is the team capable of delivering? If the answers to these questions are positive the investor will then proceed to the next stage in the 'due diligence' process - that is independently checking the nature, size and potential of the market opportunity.

How do investors do this? Typically the process comprises two elements: systematically searching through all secondary market data and, at the same time, cross-checking this data by talking to industry experts. Take the case of New Covent Garden Soup. Here the investors, Alan Patricoff Associates, undertook detailed market
analysis encompassing soup consumption, developments in the ready meal sector, growth in the chilled food business, the nature of comparable products and so forth. At the same time they consulted forty industry experts, drawn from food manufacturing and retailing, to check their own assessment of the product's relative market positioning (as a ready meal rather than a soup), estimated market growth (20% per annum growth for ready chilled meals), and the volume potential among key retailers (5 million pints per annum with less than 50% penetration of the available distribution). Convinced about the product, the management and the market potential, APA invested just under £1 million.

Analysis of this sort is undertaken every day of the week by investors. But this market analysis has a particular bias. Attention is focussed on issues relating to current market size, recent growth rates/future growth potential and competitors' relative market share. This is a rather narrow focus. Our research suggests a new set of dimensions which should be systematically analysed: purchase frequency, service intensity, customer fragmentation and channel dependence to name but a few. For investors the due diligence process and the elements of which it is made up is well established. But the results of this research constitute a compelling case for broadening the due diligence agenda. Assessing a product's position on the age/affiliation matrix lends a new dimension to due diligence, as does the systematic attention to potential barriers to survival as distinct from barriers to entry. The issues that we have identified constitute, in effect, a framework within which an investor's analysis might usefully be undertaken.

The risks of any new venture are apt to remain considerable. History suggests, however, that careful analysis of product market characteristics prior to choosing your battlefield can give entrepreneurs, corporate venturers and investors a better chance of survival, and with it, potential success.