GROWING AN ENTREPRENEURIAL BUSINESS

Concepts & Cases

EDWARD D. HESS

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7. Pricing innovations;
8. Branding innovations;
9. Bundling or even packaging innovations;
10. Payment innovations;
11. Different guarantees; and/or
12. Expanding along the value chain to capture a new source of value from other value chain players.

Five of the fifty-four companies in my DPGC research that had reached limits to their initial scaling efforts were at the "growth booster" stage.

The Big Customer

Sometimes, a business is catapulted to a new level of growth by the entrance of a major customer for its product or services. Seven of the fifty-four companies in DPGC research got a major boost by landing a significant public company customer. The acquisition of a big customer certainly cannot be counted on and, occasionally, even when offered, a business opts to scale according to their previous business plan. For example, Eyebobs Eyewear, Inc., turned down a big customer to keep tighter control of its operations and still grew at a compounded growth rate of more than 50% for several years.

CLASS DISCUSSION QUESTIONS

1. What do you think the biggest risk is to scaling a service business?
2. What are the biggest risks to scaling a product business?
3. Which can grow faster? Why?
4. As firms grow from $1 million to $5 million to $10 million to $20 million in revenue, why are they able to grow faster as they get bigger?
5. Do you think future scaling challenges should impact what business an entrepreneur starts? Why?
6. What do you think the major restraints are in scaling a retail business?
7. Is it easier to scale a business that sells a service or product that has a short life-span? Why?

Enchanting Travels

Enchanting Travels has grown using a joint venture model in Africa and an organic model in Argentina. Its challenge now is how to grow more quickly by expanding into new geographies. It has a scaling challenge, and the case raises the issue as to whether it should franchise to scale more quickly.

CASE DISCUSSION QUESTIONS

1. What was Enchanting Travels' differentiating customer value proposition?
2. Should Enchanting Travels franchise its business model? Why?
3. Explain the following statement: "What made Enchanting Travels successful limited its growth."
4. What are Enchanting Travels' major growth risks?
5. The founders had an unusual philosophy of hiring. How does it contribute to their success and limit their success?
6. How can Enchanting Travels expand its business without opening new locations in new countries?
7. Do you think Enchanting Travels' business model is scalable? Why?
8. Would you buy this business? Why?

CASE STUDY

ENCHANTING TRAVELS

In the early days when we were trying to build a brand and it was imperative that every single guest who booked a trip with us had a wonderful time, focusing on the operations or the issues that would have a direct impact on guest feedback or the guest experience would be of prime importance to anyone who was involved with the company—an almost fanatical approach toward guest feedback. And one of the big challenges that we faced and we continue to face is continuing to do what we have done during the past five years. Every entrepreneur goes through that very difficult task. I would say that to be able to build people's skills and abilities you have to at one point take away the safety net and let them figure it out; if the issue or the problem at hand involves solving the problem yourself as opposed to giving someone an opportunity even if they may fail, you reach a point when that focus becomes investing the time and effort in getting that person able to solve the issue or problem rather than doing it yourself.

I think that mindset is the big difference between a small start-up and a larger high-growth company that needs to enable its people to grow and do things that you would have done. I think in the first year if you had asked me what our focus areas were, I would say that I was involved in creating our product, actually "doing" rather than "managing" operations and personally fixing what went wrong. Now, if you ask me what my focus would be, I would say that investing the time to teach someone or enable someone to fix something would be the focus rather than fixing it myself. And I think that is a point to reach when growing a company. Enabling people around you to do what you do and help you grow the company is a big thing, and one of the big changes we have seen in the last couple of years.

—Parikshat Laxminarayan

Founded in 2004 by Parikshat Laxminarayan and Alexander Metzler, who met during their MBA education at INSEAD, Enchanting Travels (ET) was an India- and Germany-based travel company. Its discerning clients, mainly from Western countries, were interested in visiting exotic destinations. ET had expanded its operations to East Africa and South America, growing by 100% a year its first three years, and by 30% to 50% in 2008–09. By 2009, ET employed close to 100 people on four different continents and had booked more than 4,000 travelers, mainly from the United States, Germany, the United Kingdom, and Australia.

ET's business model was based on (1) thoroughly knowing its customers in order to customize trips that met their expectations; (2) vertically integrating and controlling every aspect of the trips; and (3) seamlessly executing all operations. This business model differentiated ET from most travel companies that typically outsourced all activities involving clients after their arrival at a destination. ET's business model required that

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 This case was prepared by Monidipa Mukherjee and Sanju Jacob of the Indian School of Business, under the supervision of Edward D. Hess, as a basis for class discussion rather than to illustrate effective or ineffective handling of an administrative situation.

its employees be highly engaged with customers and used extensive measurement and information systems to quickly identify problems that could be remedied without delay.

At this time, ET had the opportunity to further expand globally and offer customers a broader choice of destinations for their customized vacations. This opportunity created a new decision for Laxminarayan and Metzler to consider: Should ET continue to expand organically or should it consider franchising in order to gain first-mover advantage in more countries faster? The two entrepreneurs pondered the advantages and disadvantages of this decision.

Genesis of the Idea

The birth of the idea for ET was somewhat of an accident and a surprise. At the end of 2003, while a student at INSEAD, Laxminarayan had visited India with several of his classmates. During their travels around South India, one student commented that his impression of India turned out to be quite different from his mental picture of the country. Laxminarayan recalled, "That set me wondering why there was a gap between the perception that outsiders bear and what India can really be if promoted and presented in an excellent manner." He wondered if he was in the presence of a business opportunity.

Back at INSEAD, Laxminarayan and Metzler discussed opening an exclusive travel service as a potential business venture after graduation. Their research about this market was encouraging because the travel industry was fairly traditional. According to Laxminarayan, "If you take out the online space, it is very traditional in the way it works, and there were a lot of unnecessary players in the value chain that weren't adding much value." He continued:

> We found out that a foreign tour operator who might be offering India as one of the many destinations often did not have an on-the-ground presence in India. So he would contact a consolidator in Delhi or Mumbai, who would then subcontract to a final service provider in the final destination or in the region that the trip was actually happening. So there were three to four, or maybe even five parties between the traveler and the actual experience, which we thought was completely unnecessary and not an efficient way of doing things.

Laxminarayan and Metzler's business plan was focused on streamlining the value chain so that ET would be the single point of contact for each customer during a trip. The entrepreneurs attracted 16 investors and raised almost half of the initial money for their start-up before their June 2004 graduation. They flew to India in early July and, as Laxminarayan said, "We pretty much hit the ground running and started from there."

The Partners

Laxminarayan had grown up in India but as an undergraduate studied finance in the United States on a tennis scholarship. Prior to joining INSEAD's one-year MBA program in September 2003, he managed several projects at Analysis Group, a consulting firm in Washington, D.C., that provided economic, financial, and business strategy consulting to law firms, corporations, and government agencies. An avid international traveler, Laxminarayan acquired his tourism experience from organizing informal trips to India, using his in-depth knowledge of the country's various attractions and regions.

Before attending INSEAD, Metzler had worked as a project leader in marketing and sales strategies at Monitor Group, a strategy consulting firm. "We both came from a consulting background, which is normally a very different skill set and profile when you look at successful entrepreneurs," Laxminarayan said. Metzler also had traveled extensively through India and shared a passion for that country with his partner. Laxminarayan described their relationship:

> We have a very healthy partnership. And I think one of the key things we did early on was to sit down and have certain key agreements, not a sort of a contract but more a common understanding of each other's styles, each other's preferences, each other's strengths and weaknesses. This kind of open discussion has always helped us manage through challenging times in the relationship, if there were any. And we haven't had that many.

From the first day, the partners were conscious of how their roles were divided:

> There is very little overlap in day-to-day operations. We have a clear split in terms of which team is managed by whom, and there is no ambiguity in an employee's mind as to whose team he or she belongs. I think it is very important to avoid unhealthy overlap. The only decisions we make commonly are corporate level and strategy decisions. But everything else on a day-to-day level is very separated and very split. And I think that is critically important to having a successful business partnership.

Early Challenges

At first, the big challenge for the partners was managing everything themselves. They started ET with a small team: two partners, two spouses, and one employee. The five of them were responsible for sales, marketing, and operations. The initial task of deciding on a location consistent with their model seemed daunting. They spent three months combing the length and breadth of India visiting every hotel they wanted to offer to their clients. They tested everything: drivers, activities, restaurants, and cars, in detail and with a level of quality control that was taxing. They did it because they were not going to work through intermediaries. Laxminarayan explained:

> It wasn't as simple as going to Delhi and telling someone I am going to plan trips to Rajasthan so can you help me out. It was actually going to every small village and destination in Rajasthan, staying at and visiting every hotel that we wanted to sell and promote in our itinerary. I think just setting up the entire operation was a huge challenge early on.

Laxminarayan and Metzler decided that the biggest differentiator between a successful travel company and one that fails before it starts or shortly thereafter was in the execution. The five-member team had a tough first six months but managed to overcome the challenges. Laxminarayan said:

All entrepreneurial ventures have risk, otherwise they won't be entrepreneurial ventures, but I think it is not about feeling 100% sure about your business plan or that making complete sense. I think it is about having sound business logic, but then much more time should be spent on executing and actually pulling it off. So for me the appetite for risk is far more important than writing a business plan. The ability to pull off a successful operation and execute on a promise is much more challenging and important than having a very picture-perfect setup or picture-perfect brand or things like that.

Expansion

When ET opened in 2004, the plan was to operate in India. The partners had agreed that, while their customer base would be Germany and North America, the destination for customers would be India. But, by 2006, ET's success in India encouraged expansion. Laxminarayan continued:

Our India model worked very successfully, and we grew very well in the first two years. We then asked ourselves—what is it that makes us successful in India? Clearly, more than knowledge of India or the background of being Indian and our presence there, it was our concept of being able to master challenging destinations, the ability to tackle unreliability, lack of professionalism, lack of transparency, the ability to manage the entire operation in a challenging destination. And secondly the ability to connect with and basically understand the mind of a customer was our key strength and value proposition and what made us different and successful. And finally, and most important, our ability to provide world-class service from India at an Indian cost base made us very different from other travel companies.

ET also feared losing its customer base unless it offered more places for them to travel. Laxminarayan explained:

Our goal was to develop a customer base that sort of stays with us for 10 years or more and takes an exotic trip every year or two. Now we have had several people who have come back to India with us on repeat trips, but our kind of guests often have a list of six, seven exotic trips they want to take. So having a lifetime customer base locked in was one of the biggest drivers of our destination expansion.

East Africa

Enchanting Africa was started up in 2006 in Nairobi with the goal of selling and operating trips initially to Kenya and Tanzania. This was a joint ownership venture between ET and Florian Keller, a European national and management consultant, who had lived in East Africa and was familiar with business and life in Africa. This partner also had experience working with several large international companies that had expanded to Africa. Having a partner who lived in Africa and was knowledgeable about the country was thought to mitigate some of the risk of testing the waters outside of India.

The complexity of Africa presented a huge challenge for ET. In an area the size of India, there were 10 countries, with different laws, regulations, and ways of operating. Although ET maintained that one of the biggest differentiators of its model was its ability to offer world-class quality and service at an Indian cost base, the infrastructure challenges, such as no high-speed bandwidth and the lack of an affordable yet highly skilled and qualified labor pool to draw from, presented significant challenges.

In spite of the challenges, Africa was an attractive travel destination for Americans and Europeans. The ET team was convinced it could make Africa even more attractive to travelers if it could adapt its Indian business model to the African environment. By the end of 2009, Africa was ET's second-biggest destination, with ET offering tours in eight countries in East and Southern Africa. "We are fairly pan-African now, and we continue to grow. We have had challenges. . . . But we recovered and are on our way to building what I imagine is a second pillar of profitability in Africa," said Laxminarayan.

South America

By 2008, ET had incorporated and founded Enchanting South America, which focused on Argentina and Chile from its head office in Argentina. The main driver behind ET's expansion in South America was twofold—first, it was a destination that fit well with ET's concept and value proposition of providing a hassle-free experience of exceptional quality in a destination that was known to be difficult. Second, its proximity to the United States, its second-biggest customer market, made South America an attractive destination.

During the expansion to South America, the partners had to decide whether to hire and train a local manager and pay compensation or to enter into a joint ownership venture as they had done in Africa. Taking the first route required one of them spend several months in Argentina to get a feel for the market, set up operations, and hire and train local employees. They chose to build the business organically. Although they knew it would take several months to start ET in that region, they also knew that the end result would be a value proposition—the end-to-end control of the luxury travel business in South America that protected their brand. This gave those customers who had traveled with them to India or Africa the chance to explore South America and enjoy the same high-quality experience with the same reliable customized service they had received in other destinations.

Human Resources

The organizational structure of ET was linear, uncomplicated, and international in culture, with 90 employees from 14 nationalities working together across five countries. Most of them worked in India out of offices in Bangalore and Delhi, where there were employees from nine nationalities. According to Laxminarayan:

> It is a very healthy and open environment because it is international, and it is not a very typically Indian hierarchical business. . . . Our entire recruiting model is hiring freshers without any past experience but with a lot of potential, lots of drive, and lots of intelligence that we can mould into careers rather than laterally hiring people with experience. . . . Of our 90 or so people, I think only three had any idea of tourism and travel before they joined us. So it was a conscious decision not to hire people from the travel industry.

Laxminarayan admitted that hiring without requiring experience working in the travel industry posed some risk. "Our training on basic travel skills takes more time, so all of this is a challenge, but I think it more than pays off by having someone who doesn't have any preconceived notions and can adapt easily to a different process." ET stuck with this hiring strategy to eliminate people who already had learned operating procedures that were not appropriate for the company.

Another crucial and unique part of ET's HR strategy was to hire foreigners from its customer markets (e.g., Germany, United States, United Kingdom, and other European countries) in India to further bridge the gap between a customer and the travel experience. This focus evolved into a truly multinational and multicultural team in each of ET's offices around the world.

Structure

At the top, Laxminarayan and Metzler managed in tandem as managing directors. Laxminarayan oversaw trip operations on the ground and the sales and marketing, PR for the company's English-speaking markets (United States, United Kingdom, Australia), while Metzler did the same for ET's European customers. Corporate strategy, finance, and new destinations were evenly split between them, with Laxminarayan in charge of South America and Metzler responsible for Africa with their partner in Nairobi and Asia.

In line with its horizontal management structure, at the second layer, seven functional managers with an average age of 32 supervised a team and managed finance and accounts, operations, marketing, customer management, and reservations.

To keep an international work environment, Laxminarayan and Metzler created an open structure that allowed numerous opportunities for employee growth, which was not typical of an Indian work environment. Because of this philosophy, ET had not lost a person to another company in the travel industry.

ET had a healthy and aggressive performance-linked bonus that was one of its big drivers. Because the company believed that incentivized performance was a fragile way to keep employees, it invested a lot of time in training and giving employees a sense of emotional attachment to the company. This enabled ET to retain people at a time when attrition was the biggest business challenge in India. ET's turnover in the first five years was 15% to 20%, but that number was reduced to just 5% in subsequent years.

The Business Model

One of the aspects of the business model that was clear to Laxminarayan and Metzler right from the beginning was its strong focus on only offering tailor-made travels and to never have catalogues with standardized itineraries. In order to pull this off and to efficiently create highly customized travel experiences for each guest, they implemented a highly flexible and tailor-made IT system to automate an otherwise hugely time-intensive activity of individual itineraries. They recalled an apt Michael Porter quote from business school: "Strategy is about being different and it means deliberately choosing a different set of activities to deliver a unique mix of value."

With this in mind, ET set up processes geared to offer high-quality tailor-made travels and a unique mix of activities to enable the company to clearly differentiate themselves from competitors and leverage competitive advantages in its market space. As Alexander Metzler said, "We feel that large tour operators would find it nearly impossible to copy our business model and processes given that their entire setup is geared and catered for providing standard packages and mass tourism."

The first differentiator in ET's unique business model of vertical integration was that it handled all operations from beginning to end. Then there were the various nationalities and cultures of the people working in its offices in India, with some often coming from the same places as the customers. In short, ET was an international organization in India; out of its 60-odd employees, 25% were foreigners.

The partners also invested heavily in training their employees about company processes and about India, a complex and diverse country. Getting the right people and building up their destination knowledge through training, test trips, integration with ET operations, and integrating customer-facing employees with operations was another characteristic that set ET apart. Laxminarayan explained:

> If you ask our customers why they book with Enchanting Travels, this is what often comes up: "We felt very well taken care of, the quality of interaction was fantastic, the documents we got were fantastic, but most importantly, the person we were speaking to was really able to understand our needs and had a very good competence level on how to bring India alive in an itinerary that was a good fit with our personality and our needs at a very compelling value for money equation."

One of the most appreciated value propositions that helped guests feel comfortable was ET's guest management strategy of assigning a hands-on contact person to see to all the activities of guests during their stay at a destination. Carefully selected tour guides were independent contractors who went through a quality check and a training process that taught them ET's different concept and way of doing things. Tour guides who had worked with other companies underwent a stringent selection process, and ultimately approximately 80% of the guides worked solely for ET.

On average, the overall level of education, quality, sophistication, and skills was extremely low in the travel industry worldwide. Aware of this, ET selected well-educated, competent people to train. Although ET's salary costs were higher, it was able to provide American- and European-quality service in India. By hiring foreigners and Indians on the same professional level as European or U.S. employees, ET produced the same or better quality of work as a premier travel company located in Munich or New York City. And it was able to deliver that quality from Bangalore and Delhi.

Because ET was passionate about personally experiencing, testing, and validating all hotels and restaurants that it recommended to its clients, it also tracked feedback about every hotel in its portfolio. ET invested a lot of time and money in test trips to build a destination from the ground up because the possible bias of trip advisors and independent rating agencies made it important to verify that a destination was a tailor-made travel experience. This extensive, time-consuming quality control process made expansion to a new destination a major research project. Nonetheless, ET preferred to take this slower approach to growth to make sure that its system was in sync with its promise to give guests a trip to remember.

Pricing

Laxminarayan gave all the credit for the success of the ET pricing model to the absence of middlemen. He considered it "the most innovative factor of our pricing model." Explaining why ET was not completely positioned as a luxury travel company, Laxminarayan said:

> We are not as expensive as Abercrombie and Kent, the world's leading luxury travel company but neither are we as cheap as a regular tour operator. We are somewhere between those two in terms of our price positioning. We believe we offer amazing quality at a price-competitive proposition. But obviously in order to deliver that quality, we can't be playing with very small margins, which is very risky.

The Road Ahead

Sowing the early seeds of Enchanting Asia, which would initially comprise Bhutan, Myanmar, Sri Lanka, and Nepal, and then slowly include Vietnam, Cambodia, Laos, and eventually reach the Chinese borders, was ET's main focus for 2010. Also in 2010, ET planned on growing Enchanting South America to harness the potential for Argentina and Chile and in a year or so expanding to Peru and Brazil. The focus in India was to scale up by exploring avenues for new marketing channels. Laxminarayan explained:

> One of our big questions going forward is how to do China? We don't have the same comfort level as we would have in South America. In China, we are daunted by the challenge of what it would take to actually run an operation with Chinese managers or even with Western managers. We need to figure out the massive potentially viable business opportunity that China presents. Would we pull that off using Africa's [joint-ownership] model or along the lines of the South American [solely owned] model?

In Laxminarayan's opinion, "One of the big challenges going forward is how to get the managers to drive growth and independently manage initiatives as opposed to me having to spend several months setting up a new operation as I did with Enchanting South America in Argentina." He concluded:

> Whether we can become the Google of the travel world (at a relatively smaller scale given our industry of course) is a question that will hopefully be answered in the coming years, but I am hoping that we at least emerge as the world's leading company for high-end tailor-made travels to exotic destinations with a global reach in terms of markets and destinations.

Growth Strategy

As the ET partners pondered how to expand to China, they wondered whether they should franchise the ET concept and operational model to other countries in South American and Asia.

List of Relevant Cases

Scaling Cases

3 Fellers Bakery

Defender Direct, Inc.: A Business of Growing Leaders

Enchanting Travels

Global Medical Imaging, LLC

James Abrams @ Clockwork Home Services, Inc.: Lessons from a Serial Entrepreneur

Mellace Family Brands, Inc.: Building a Socially Responsible Enterprise

Motor City: A Disruptive Business Model (B)

Octane Fitness, Inc.: The Power of Focus

Room & Board

Sammy Snacks (A)

Sammy Snacks (B)

Sammy Snacks (C)

Enchanting Travels

This case is embedded in Chapter 8 and can be found on page 183.

CASE STUDY

ENCHANTING TRAVELS

Enchanting Travels has grown using a joint venture model in Africa and an organic model in Argentina. Its challenge now is how to grow more quickly by expanding into new geographies. It has a scaling challenge, and the case raises the issue as to whether it should franchise to scale more quickly.

CASE DISCUSSION QUESTIONS

1. What was Enchanting Travels' differentiating customer value proposition?
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Business/Entrepreneurship

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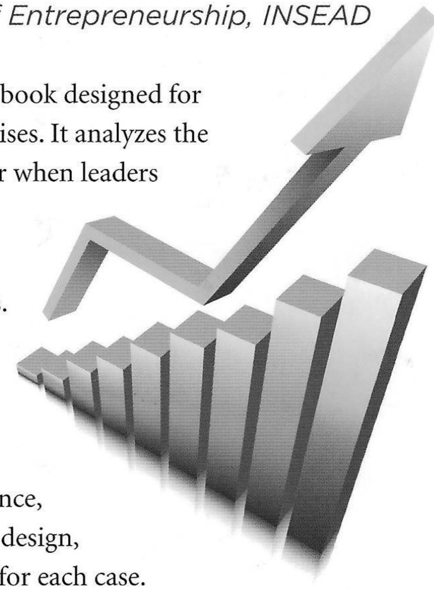
"There are several books that try to cover entrepreneurship from soup to nuts—everything you could possibly want to know about starting a company. This book is fairly unique in its focus on growing an extant entrepreneurial business."

—Philip Anderson, Professor of Entrepreneurship, INSEAD



Growing an Entrepreneurial Business: Concepts and Cases is a textbook designed for courses that focus on managing small- to medium-sized enterprises. It analyzes the major management challenges that successful startups encounter when leaders decide to grow and scale their businesses.

The book is divided into two parts—text and cases—to provide instructors with maximum flexibility in organizing their courses. The thirty-three cases can be used in conjunction with the text, or independently. Eleven cases are written as narratives with multiple teaching points, but without a focus on a particular business decision; the remaining twenty-two cases are written around specific conundrums related to strategy, operations, finance, marketing, leadership, culture, human resources, organizational design, business model, and growth. Discussion questions are provided for each case.

The text portion of the book discusses key issues derived from the author's research and consulting, and is meant to complement the case method of teaching, raising issues for conversation. In addition to the real-world knowledge that students will derive from the cases, readers will take away research-based templates and models that they can use in developing or consulting with small businesses.

Edward D. Hess is a Professor of Business Administration and Batten Executive-in-Residence at the Darden Graduate School of Business. He is the author of eight books, forty practitioner articles, and over forty Darden cases. His growth research has been featured in over 125 media outlets worldwide, including *USA Today, BusinessWeek, Forbes, Financial Times, Fortune,* Bloomberg, CNBC, Fox Business News, WSJ Radio, Dow Jones Radio, MSNBC Radio, Bloomberg Radio, and NPR. To learn more about Professor Hess, visit his website: www.EDHLTD.com.

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