

External legitimization in international new ventures

Toward the typology of captivity

Turcan, Romeo V.

Published in:
International Journal of Entrepreneurship and Small Business

DOI (link to publication from Publisher):
[10.1504/IJESB.2012.045207](https://doi.org/10.1504/IJESB.2012.045207)

Publication date:
2012

Document Version
Publisher's PDF, also known as Version of record

[Link to publication from Aalborg University](#)

Citation for published version (APA):
Turcan, R. V. (2012). External legitimization in international new ventures: Toward the typology of captivity. *International Journal of Entrepreneurship and Small Business*, 15(2), 262-283.
<https://doi.org/10.1504/IJESB.2012.045207>

General rights

Copyright and moral rights for the publications made accessible in the public portal are retained by the authors and/or other copyright owners and it is a condition of accessing publications that users recognise and abide by the legal requirements associated with these rights.

- Users may download and print one copy of any publication from the public portal for the purpose of private study or research.
- You may not further distribute the material or use it for any profit-making activity or commercial gain
- You may freely distribute the URL identifying the publication in the public portal -

Take down policy

If you believe that this document breaches copyright please contact us at vbn@aub.aau.dk providing details, and we will remove access to the work immediately and investigate your claim.

External legitimization in international new ventures: toward the typology of captivity

Romeo V. Turcan

Department of Business and Management,
Aalborg University,
Fibigerstræde 2, Aalborg, 9220, Denmark
E-mail: rvt@business.aau.dk

Abstract: This paper explores within the framework of new venture legitimization how and why international new ventures acquire external legitimacy and strive for survival in the face of critical events. Following a longitudinal multiple-case study methodology that was adopted for the purpose of theory building, the paper introduces the typology of captivity, and the four types that have emerged: captive industry supplier, captive dyadic partner, captive market leader, and free market leader. The effects of captivity types on the acquisition of external legitimacy and its survival, on reaching legitimacy threshold, and on the valuation of the venture are discussed and respective propositions are put forward to guide future research.

Keywords: external legitimacy; legitimation strategy; international new venture; international entrepreneurship; typology; theory building.

Reference to this paper should be made as follows: Turcan, R.V. (2012) 'External legitimization in international new ventures: toward the typology of captivity', *Int. J. Entrepreneurship and Small Business*, Vol. 15, No. 2, pp.262–283.

Biographical notes: Romeo V. Turcan is an Associate Professor at the Department of Business and Management at Aalborg University in Denmark. His research interests are in the area of international entrepreneurship of knowledge intensive ventures; knowledge transfer; and sociology of markets. He received his PhD in International Entrepreneurship at the Hunter Centre for Entrepreneurship at the Strathclyde University, Glasgow, and his MSc in International Marketing at the Marketing Department at the Strathclyde University, Glasgow. He has been a Visiting Professor at the East China University of Science and Technology and Grenoble Graduate School of Business.

1 Introduction

The research on international new ventures (INVs) emerged over a decade ago now with the seminal paper by Oviatt and McDougall (1994) that received a decade award from JIBS in 2005. Oviatt and McDougall's (1994) article was also at the foundation of international entrepreneurship as a new stream of research (Zahra, 2005; Kraus, 2011). Initially, the research in international entrepreneurship focused primarily on INVs that aim to derive profits from international activities right from their inception or

immediately after (Oviatt and McDougall, 2005). These INVs bear a resemblance to the firms that are usually backed by venture capitalists due to their potential for very high gains in combination with the availability of early exit strategies (<http://www.nvca.org>). At the policy level, INVs are seen as critical engines of economic growth (OECD, 2004). In this paper, INVs are defined as "...independently operated and marketed corporate entities that have no prior corporate history in the industry, and hence no prior market presence" [Fan and Phan, (2007), p.1114]. This suggests the behaviour of INVs in the early years of their existence is shaped substantially by the liability of newness (Stinchcombe, 1965) and the liability of foreignness (Zaheer, 1995). To the above one may add other concerns that ought to be considered during early and rapid internationalisation of INVs, mainly technical and market uncertainties, as well as goal ambiguity (Turcan, 2008).

From the institutional theory perspective, legitimacy is viewed as playing a key role in overcoming the above liabilities and concerns. For example, Stinchcombe (1965) views legitimacy as an antidote for the liability of newness, whereas Zimmerman and Zeitz (2002) view legitimacy as an important resource for gaining other resources. Legitimacy is defined here as "a generalised perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, beliefs, and definitions" [Suchman, (1995), p.574]. This paper will focus on investigating the role external legitimation plays in the process of the emergence of INVs. Specifically, the aim is to further our understanding of *how* and *why* INVs acquire external legitimacy and strive for survival in the face of critical events. The findings from a longitudinal research that explored in depth the rapid internationalisation of software companies during the dot.com bubble will be presented and discussed. Grounded in data, the paper will put forward a *typology of captivity* along with the four types that emerged: captive industry supplier, captive dyadic partner, captive market leader, and free market leader. Captivity belongs to the degree family of codes (Glaser, 1978), and refers to the situation when:

- 1 a firm has no practicable alternative but to sell their products via a single enterprise player
- 2 there is a limited number of customers in the identified niche market.

This paper is also in response to the call for further longitudinal, qualitative research in order to explore the legitimation process of new ventures (Zimmerman and Zeitz, 2002), as well as to the call for further research to explore the survivability among INVs in order to advance international entrepreneurship theory (Zahra, 2005). The paper proceeds with a review of new venture legitimation; the research methodology is presented immediately after. The typology of captivity is presented next, followed by a discussion and future research directions.

2 Theoretical background

Broadly speaking, the paper is positioned within the legitimation theoretical framework. More specifically, the empirical scope of the paper lies within one of the two streams of research on legitimacy, namely the creation of legitimacy in new organisations, as opposed to the maintenance of legitimacy in established organisations, as differentiated

by Johnson et al. (2006). From this theoretical perspective, the emergence of an INV could be viewed as a process that is concerned with the creation and legitimation of the new venture. With few exceptions (Andries and Debackere, 2007; Delmar and Shane, 2004; Rao et al., 2008; Sanders and Boivie, 2004; Zott and Huy, 2007), the research on legitimation strategies of new ventures is somehow scarce.

For example, Delmar and Shane (2004) argue that legitimacy enhances the ability of founders to create social ties with external stakeholders and to initiate routines to transfer resources. They analysed the life stories of 223 new ventures and found that undertaking activities to generate legitimacy both enhances new venture survival and facilitates transition to other forms of organising activities. Sanders and Boivie (2004) studied publicly-traded US internet firms and found that firm market valuation was strongly associated with corporate governance characteristics, e.g., board structure and venture capital participation. Zott and Huy (2007) explored the question of which symbolic actions entrepreneurs performed in order to attract resources and when and why these actions are effective in acquiring resources. They identified four symbolic action categories that facilitate resource acquisition: conveyance of an entrepreneur's personal credibility, professional organising, organisational achievement, and the quality of stakeholder relationships. Andries and Debackere (2007) investigated the relationship between adaptation and performance in a sample of 117 independent new ventures and business units and found that adaptation is beneficial in less mature, capital-intensive and high-velocity industries but not so in more mature, stable industries.

As to the legitimation strategies, Rao et al. (2008) distinguish between internal and external legitimacy. Internal legitimacy can be acquired by new ventures through four types of actions – market, scientific, locational and historical – whereas external legitimacy can be acquired by associating or partnering with successful and established external entities. Rao et al. (2008) examined the stock market gains of all products introduced between 1982 and 2002 by all public firms in the US biotechnology industry and found that new ventures that acquired legitimacy externally by forming alliances with established firms gained more from their new products than new ventures that did not form such alliances.

The common consensus in the extant research on external legitimation suggests that partnerships with well-established companies can enhance the legitimacy of new ventures (Barringer and Harrison, 2000), while these partnerships can be for example in the form of international cooperative agreements, partnerships, and joint ventures (Oviatt and McDougall, 1994). By entering into a partnership or an alliance, new ventures are trying to gain market, relational, social, investment, or alliance legitimacy (Dacin et al., 2007). In line with the above, Gleason and Wiggenhorn (2007) found that the firms that signal to the market the formation of joint ventures are better perceived and rewarded "...with significantly positive abnormal returns" (p.333). In the same vein, Rutherford and Buller (2007) found that the most frequent and common legitimation strategy is to secure a key customer, whereas Andries and Debackere (2007) found that the failure rates in dependent ventures are reduced as compared to independent ventures when adapting the venture business models.

These and other similar findings could be challenged by taking into account the sampling bias that dominates the extant international entrepreneurship research (Coviello and Jones, 2004; Keupp and Gassmann, 2009; Turcan et al., 2010; Zahra, 2005). Explicitly, the focus of extant international entrepreneurship research is for the most part on positive business growth, while the companies which failed or chose to withdraw from

their international activity along the way are ignored. This approach to research resembles the study of factors that lead to success at gambling on race horses in which one studies only people who have won money (received net gain) and concludes that gambling is profitable, i.e., the more you bet, the higher your gains; the more unlikely winners you bet on, the more you win (Davidsson, 2003a). By studying only surviving or successful firms, there is a risk to present these firms' behaviours as success factors when in fact they may well constitute factors that equally increase the risk of failure (Davidsson, 2003b). This paper is trying to fill in this gap by exploring how and why INVs acquire external legitimacy and strive for survival in the face of critical events. According to Zahra (2005), little is known about the survivability among INVs, and how and why these ventures change their strategic direction.

3 Research methodology

This study employs a longitudinal multiple-case study methodology that relies on purposeful sampling, the logic and power of which inhere in selecting information-rich cases for study in depth (Eisenhardt, 1989; Yin, 2003). Since the study explores the behaviour of INVs in the face of critical events, it is essential that 'critical events' is defined. Following Edvardsson (1992), an event is defined as being critical when it deviates significantly, either positively or negatively, from what is normal or expected. Several challenges await researchers when studying critical events, especially those that deviate negatively from what is normal or expected. For example, during such events, people tend to take credit for positive outcomes and attribute negative outcomes to external factors, a behaviour known as attribution errors (Lovallo and Kahneman, 2003). The effect of such attribution errors may be mitigated through the appropriate research design that in turn contributes to the enhancement of research validity and reliability. In the present study the attribution errors were controlled for by confining the study to a homogeneous empirical context, developing sampling selection criteria, and by employing triangulation.

The strategy of confining the study to a homogeneous empirical context is defined here as outer-bracketing strategy. It controls for the effect of, for example, legislation, market size, market structure across industries and countries, and the effect of time on selected cases. This means the potential cases ought to be located in the same country and/or same geographical location, and come from the same sector/industry. In keeping with the above, the potential effect of resource bias on selected cases was controlled for, whereby small was defined as a company having less than 100 employees (Storey, 1994), thus ensuring a comparable resource-base. Yet another selection criteria was the internationalisation gap defined here as the time that elapses from the emergence of the INV idea until the moment of its internationalisation; for example a gap of 0 year would denote instant internationalisation. Data collected from entrepreneurs were corroborated with the data collected from their stakeholders and secondary sources, thus further minimising the potential effect of attribution errors. A snowball sampling strategy was employed to identify and select the cases based on the above selection criteria. Five companies were purposefully selected for the study: the case companies were all *small*, operating in the *software sector* in *Scotland*, and *internationalised at or immediately after* the emergence of INV idea during 1999–2003. The cases are summarised in the

Appendix. For confidentiality reasons, interviewees' and companies' names are disguised throughout the paper.

3.1 Data collection and analysis

Critical incident technique (CIT) guided the process of data collection and analysis. It has its origins in the research undertaken by Flanagan (1954), and is defined as "...a qualitative interview procedure that facilitates the investigation of significant occurrences (events, incidents, processes or issues) identified by a respondent, the way they are managed, and the outcomes in terms of perceived effects" [Chell, (1998), p.56].¹ CIT guidelines for in-depth interviewing were followed in all interviews. According to these guidelines, researchers have to indicate to the interviewee the authority by which the interview is being held, and then make a statement about the purpose of the study, explain why the interviewee has been chosen to comment on the subject of interest, and convince the interviewee of the anonymity of the data. The researchers have to make sure the main research question states that an incident or actual behaviour is desired. During the interview, the researchers have to allow the interviewee to do most of the talking and avoid asking leading questions. The researchers control the interview by probing the incidents and clarifying one's understanding. Follow-up questions are asked to ensure that a comprehensive and detailed account of an incident has been given. In the end, the researchers conclude the interview, take care of ethical issues, and negotiate future access in case follow-up interviews might be needed.

An important feature of qualitative research is that there is significant overlap between the data collection and analysis phases (Eisenhardt, 1989; Glaser, 1978). Data were collected from decision-makers (entrepreneurs/owners) and corroborated by data collected from their stakeholders, such as investors, strategic advisors, liquidators, policy makers, and business journalists in four phases: from 2000 through 2005. On average, an interview lasted approximately 60 minutes. All interviews were recorded with the interviewee's permission, and transcribed verbatim immediately after. The interviews were semi-structured in the form of guided conversations. An interview guide was designed to ensure some comparativeness between the responses, and to allow sufficient control over the interview so that the research objectives could be met. Databases were created for each case to be organised and to document the data collected, including primary and secondary data, thus enhancing the reliability of the research. 24 semi-structured in-depth interviews were conducted yielding approximately 150 pages of interview data.²

CIT guidelines for data analysis were followed. Initially, the incidents were described. As maintained by Dubin (1978), the very essence of description is to name the properties of things, and, the more adequate the description, the greater the likelihood that the concepts derived from the description will be useful in subsequent theory-building. The exploration and description of each case was centred on critical events and started from the inception of the company. Quotes from the interviews were used extensively to illustrate the events, incidents, processes and issues that had, to various degrees, an impact on the process of legitimisation. Data pertinent to each case were coded in an iterative manner, working back and forth between theory, emerging patterns, and data.

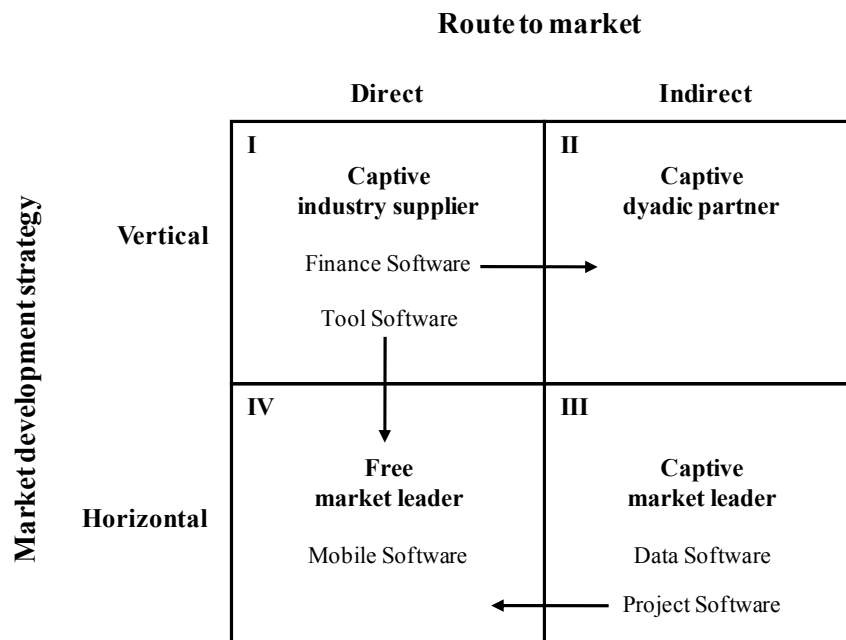
Next, the frame of reference was chosen so that it would be much easier and more accurate to classify and analyse the data. Two frames were identified. One relates to various levels of analysis, namely the entrepreneur, the firm, the home market, and the

international market. The other frame relates to various time periods that helped to map the chronological flow of critical events, namely the emergence of the new international business idea, international expansion, both at a critical juncture and beyond it. Category formulation followed next; it represents an induction of categories from the basic data in the form of incidents (Flanagan, 1954). Within-case analysis was the basis for developing early constructs surrounding the critical events in the process of legitimization, and subsequent survival decisions, such as, captivity, free market leader, and horizontal platform. The above frames were structured in NVivo around an event-listing matrix (Miles and Huberman, 1994) that allowed the exploration of what led to what, when, and why. The content of the event-listing matrix emerged after the initial 'free coding' or open coding (Glaser, 1978) for each case was completed. The cases' respective critical incidents are summarised in the Appendix.

The last step in data analysis focused on determining the most appropriate level of specificity-generality to be employed in reporting the data. In this study, middle-range theorising helped manage the complexity of data. According to Weick (1989, p.521), middle-range theories are solutions to problems that contain a limited number of assumptions and considerable accuracy and detail in the problem specification. The method of constructing typologies by reduction (Glaser, 1978) was employed to advance a middle-range theory of captivity. The term 'captivity' belongs to the cutting-edge of the family of codes (Glaser, 1978), and refers to the situation when:

- 1 firms have no practicable alternative but to sell their products via a single enterprise player
- 2 there is a limited number of customers in the identified niche market.

Figure 1 Typology of captivity



Grounded in data, Figure 1 presents the typology of captivity that was generated by cross-tabulating two business strategies, namely route to market (direct or indirect) and market development (vertical or horizontal). Three types of captivity emerged: *captive industry supplier*, *captive dyadic partner*, and *captive market leader*. When the above-identified prerequisites of captivity disappear, companies may become *free market leaders*. The next section will discuss the typology in detail.

4 Typology of captivity

The data suggest that companies which target vertical niche markets and supply their products directly to the customers in these markets (quadrant I, Figure 1) may find themselves in the situation where they outgrow their market. Tool-Software is a case in point. When the co-founders of Tool-Software saw the opportunity to transform the company into a product-led business, they had to decide, *inter alia*, on how to position their product: vertically or horizontally. Severe competition across the horizontal smart-card market prevented Tool-Software from developing a horizontal product. Instead, the decision was reached to target the telecom market only for that time. As the CEO of Tool-Software explained:

“We recognised that we could not compete in the market place [with our product] that we were creating because other players were coming in, which were much, much bigger. Therefore, there was no scope for taking this software and creating a horizontal platform. Eventually, we decided to position ourselves vertically in the mobile market as opposed to being in a general smart-card capable business. Next step then was to hunt out the key players.”

The ‘hunting out’ of the key players proved to be successful. In 1995, Tool-Software took its product to the USA, and in 1996, it opened its first international office there. In 2001, it opened an office in Japan, and several others across the USA. However, in early 2000, it witnessed a huge drop in its tool sales, which led to firm’s de-internationalisation. As one of its business strategy consultants explained:

“Tool-Software exported 90% of their sales, and by 2002 that activity seemed to have died, and they were trying to create a new business fundamentally in the UK. The reason they went backwards was that the market for their test equipment went away. Once [major telecom players] bought one, why buy another one. Tool-Software just grew out of the market.”

The recession that started in 2000, and amplified in 2001, contributed to the acceleration of this downturn. The above events were critical to the initiation of the search for new opportunities, which in turn were critical to the firm’s survival. As the lead entrepreneur noted: “after a bit of hiding, and surviving, [Tool-Software] came back”. New opportunities for developing a horizontal product were identified, and ultimately pursued. In 2000, Tool-Software secured its first round of funding to develop its platform. In 2001 and 2002, Tool-Software received its second and third round of funding, and released the platform in 2003. It became the market leader (quadrant IV) with approximately 220 customers located in 33 countries.

Finance-Software also started selling their services directly to their customers’ major international branches (quadrant I). As this service contract was about to end in five years

time, the co-founders tried to take these services elsewhere, but soon found out that they were not in demand. As the CEO of Finance-Software explained:

“We did begin to recognise that we could not really build a business on the back of those kinds of contracts. We concluded that we do not have any future in the manufacturing systems, so we have to choose another vertical.”

Eventually, having identified new business opportunities in another vertical, a financial market, which happened to be located in the domestic market, Finance-Software de-internationalised and focused entirely on that vertical market. In the meantime, Finance-Software became an early adopter of a new technology. That was a strategic move that made them “...stand out from the crowd”, according to one of the co-founders. Finance-Software started hunting out major players from the enterprise space in order to build long-term relationships with them. They soon found out that such big players demand exclusive partnerships, and therefore had to decide which one to partner with. The decision was reached to partner with one enterprise player who also happened to be an earlier adopter of the same technology and had a large presence in the financial markets. As a result, Finance-Software started developing a product that would be integrated in the frames provided by their sole strategic partner to the financial customers, thus becoming a captive dyadic partner (quadrant II). As the CEO of Finance-Software noted:

“We tried to form our bonds with [several big enterprise players]. At some point we realised that these guys do not want to work with you unless you are totally committed to their cause. They do not like if you talk to their competitors. Hence, we had to make a decision: whom we are going to go with; whom we want totally and utterly to be associated with.”

The entrepreneurs of the remaining three firms, who were aiming to develop horizontal products, also had the same dilemma in the decision making process: to partner with one large enterprise player and sell indirectly (quadrant III) or sell directly (quadrant IV) on their own. They also discovered that large enterprise players demand exclusive partnerships. Moreover, their experience, at times quite a painful one, in these partnerships showed that being dependent exclusively on one strategic partner is a very risky proposition. For example, it happened that four out of the five companies had a relationship, to varying degrees, with one of the largest software companies, which was described by the respective entrepreneurs as *spooking*, *lot of clouds*, *seriously bad company*, and *bandits*.

The data further point out that the likelihood of being acquired, or being driven out of business, for example as a result of the failure or acquisition of a strategic partner, may make entrepreneurs avoid partnering with large players in the future. For example, the co-founders of Project-Software, in trying to balance the lack of product marketing and sales experience and expertise, entered a deal with an OEM. Under this deal, the OEM would incorporate Project-Software's product into its own and market it to its customers (quadrant III). However, this deal was short-lived as the OEM was acquired by a US company. Project-Software managed however to take back the control of their product and started selling it directly to their customers (quadrant IV). As the CEO of the Project-Software explained:

“We had a deal with an OEM to sell our product. Essentially they branded our product as their own. One year after, [our strategic partner] got into trouble and was purchased by a US company. We extracted from that relationship, took back the control of the product, and started our own sales.”

The co-founders of Data-Software, having had rich experience in selling services to large enterprise companies prior to the start-up, thought that partnering with them in marketing a product would be easy as well. As it turned out, that was not the case. These large enterprise players did not even want to partner. As the CEO of Data-Software noted:

“We were exploring different routes to market. We were continuing to look for direct deals in the UK. To internationalise, we approached [one large enterprise player] and found out that they were a very difficult company to partner with. They were completely self-focused. Actually it was a very dangerous place to go. They eat their children.”

Despite these fears and several unsuccessful attempts to partner with large enterprise players, Data-Software eventually partnered with one of the largest software players in the world, who was pursuing at that time an aggressive strategy of entering the enterprise space. Under the deal, Data-Software’s product would be incorporated into a platform of its strategic partner and thus be marketed to a large number of solutions-providers who were licensed to sell their strategic partners’ products (quadrant III). As the CEO of Data-Software explained:

“The relationship with [our strategic partner] gave us a real opportunity to get their backing to recruit all those dealers. So we went from selling directly to selling indirectly to mid-market companies. In hindsight this was a mistake; it was a strategic error. We left our destiny outside of our own hands. I would not do that again.”

This deal was short-lived as well. Its strategic partner announced that it would soon start developing its own product, which overlapped substantially with the product of Data-Software and thus eventually would replace it. This intention created panic, disagreements, and scepticism among co-founders and VCs about the future of the product. The only consensus that existed at that time in the company between the co-founders and VCs was that if Data-Software were to continue with the same strategy (quadrant III), then its strategic partner would take away its business in the end. The lead entrepreneur and VCs disagreed on what strategy to adopt after this partnership was terminated. The lead entrepreneur argued for the continuation of horizontal product development and selling directly to their customers (quadrant IV). Although the VCs advocated direct sales as well, they preferred to focus on one vertical market (quadrant I), which happened to be in the UK. The lead entrepreneur stepped down and a new chief executive, brought in by the VCs, withdrew completely from the USA. Soon after Data-Software de-internationalised, it ceased trading. Interestingly, at the time of the interview in 2004, Data-Software’s strategic partner had not yet brought its intentions to fruition.

The co-founders of Mobile-Software decided from the outset not to go down the route of partnering with a large enterprise player and selling their product indirectly (quadrant III). Instead, they opted for developing and marketing their horizontal product directly to potential customers (quadrant IV). As the CEO of Mobile-Software explained:

“I think we could’ve done more to develop relationships with somebody like [this large software player], but what that would’ve meant was that if we succeeded, we would’ve been just swallowed up, or kicked to one side. So, we could not have grown the business to the extent that we wanted to independently. It was a trade off.”

The data suggest that being in quadrant IV (Figure 1) is the most desired position to be in for an INV. On the other hand, the data also point out that it is the riskiest strategy to pursue right from the inception. The development of a horizontal product requires entrepreneurs to acquire specific knowledge and experience from different vertical markets. It also requires a lot of capital to actually develop the product. In the case of Mobile-Software, its co-founders decided to achieve all the above by means of acquisition as the main external legitimization strategy. In less than one year, they acquired several software companies and established a presence in eight countries worldwide. At the same time, they raised their first round of funding, and immediately after started looking for the second round in order to support the development of the product. However, the founders had problems with integrating the acquired companies, including the firing of existing managers, with being behind in the revenue and product development schedules, having no money left to run the business, and eventually with not being successful in raising the second round of funding. As a result, in less than two years after its inception, Mobile-Software ceased trading. As the CEO of Mobile-Software explained:

“What we tried to build was too ambitious, too complicated. We were trying to solve too many problems at once. Moreover, the problems we were trying to solve were big and expensive. I think we could have made a smaller promise, deliver that, and add more value to it as we moved along.”

The liquidator of Mobile-Software further explained that “they did not have the safety net large businesses tend to have... it is a bit like a monkey putting its hand to grab the peanuts and then it can not get its hand back out from the jar”. The development, right from the inception, of a horizontal product (quadrants III and IV) rather than the development of a niche vertical solution (quadrants I and II) is a common trap that entrepreneurs fall into that is difficult to get out from (Cusumano, 2004).

5 Discussion and future research directions

Regardless of which business model and growth path an INV adopts in its efforts to develop and market its product internationally, it faces three key questions with regards to internationalisation:

- 1 how fast to internationalise
- 2 what entry mode to adopt
- 3 what market to target.

To the above, there could be identified three more issues that are INV specific, mainly:

- 1 technical uncertainty
- 2 market uncertainty

3 goal ambiguity (Turcan, 2008).

Decisions related to starting an INV or investing in such a venture are made under conditions of uncertainty regarding technology and market. In this kind of uncertain decision-making setting, the possible outcomes of the decision to pursue an INV, and the probability of those outcomes are unknown (Alvarez and Barney, 2005). As one VC mentioned: "...what we've been working on quite hard to improve during the dot.com was to get the views on the size and trends of the markets... as investors had an inflated idea of what companies might be worth". As also maintained by Zimmerman and Zeitz (2002), the IT industries – in particular software and dot.com companies – are based significantly on legitimacy, not just on hard economic analysis.

INVs may overcome the above liabilities of newness and foreignness, as well as uncertainty concerns, by seeking external legitimation through a partnership or an affiliation with highly regarded organisations. In doing so, new ventures are seeking market, relational, social, investment, and/or alliance legitimacy (Dacin et al., 2007), and the extant research supports the positive effect of new ventures' external legitimacy on new venture performance. However, when the sampling bias is controlled for, as it was done in the present study, a different picture emerges. Indeed, as the data demonstrated, in the early stages of new venture emergence, the pursuit of the external legitimation strategy makes it easier for new ventures to enter international markets, enhance their market position and authority, acquire new resources and skills, as well as to mitigate the risks associated with rapid internationalisation. In fact, the acquisition of external legitimacy could be viewed as a means to reach the legitimacy threshold, "below which the new venture struggles for existence and probably will perish and above which the new venture can achieve further gains in legitimacy and resources" [Zimmerman and Zeitz, (2002), p.427]. In line with the above, it is maintained that:

P1 External legitimation will be positively associated with reaching the legitimacy threshold.

On the other hand, the data revealed that the situation changes with the passage of time. These changes might be explained by two constructs that to a certain degree are intrinsically embedded in the proposed typology of captivity. These are the uncertainty that is associated with INVs' technology and markets and the legitimacy threshold. Technical and market uncertainty in an industry that is emerging and lacks legitimacy allows the potential for information asymmetry. Having intimate knowledge about the expected potential of the new venture, entrepreneurs tend to skew their business plans toward over-optimism, a phenomenon known as anchoring (Lovallo and Kahneman, 2003). Under such uncertain decision-making settings, external stakeholders have difficulties or are unable to refute entrepreneurs' claims about the expected potential of the new venture.

With the passage of time technical and market uncertainty will fade away. As new ventures move away from uncertain decision-making settings towards risk decision-making settings, more accurate information comes from the market that makes it possible for new ventures' stakeholders to perform much needed statistical calculations, and therefore to adjust their own assessments of the new venture. If the potential of the venture turns out to be not as expected, the existing external legitimation processes and procedures would cease to exist. Oliver (1992, p.564) defined such process as

de-institutionalisation, whereby “...the legitimacy of established or institutionalised organisational practices erodes or discontinues”. Based on the above, it is suggested that:

- P2 Information asymmetry will be positively associated with the acquisition of external legitimacy.
- P3 Information asymmetry will be negatively associated with the survival of the external partnership or alliance.
- P4 The effects of P1 and P2 will be stronger under uncertain decision-making settings.

One may also argue based on the above discussion that if the potential of the new venture is not realised as per external stakeholders’ expectations, the ability of the new venture to reach the legitimacy threshold diminishes. Therefore:

- P5 Information asymmetry will be negatively associated with reaching the legitimacy threshold.

The dynamics in the relationship between the captive new venture and its reputable partner may also change when the potential of the new venture is realised, and thus legitimacy threshold is reached. For example, the new venture may exit the partnership and continue on its own, including through an IPO; it can be internalised by its partner, or acquired by another large organisation. Hence:

- P6 External legitimization will be positively associated with the market valuations of the new venture, thus leading to higher prospects of exit.

As the data also point out, the success of external legitimization, hence the success of the exit will depend very much on the alignment of the goals of entrepreneurs to the goals of their strategic partner (Turcan, 2008). That is, being captive means to align your agenda to the agenda of your partner; this will speed up the process of reaching the legitimacy threshold that in turn will have a positive effect on the exit strategy. Summarising the above points, it is suggested that:

- P7 The external legitimization will depend on the goal alignment between a new venture and its strategic partner.
- P8 Goal alignment will have a positive effect on reaching the legitimacy threshold.
- P9 Goal alignment will be positively associated with successful exit.

Future research may also delve into the effects of internal legitimization on external legitimization, a direction suggested by the comment of a liquidator that “...when entrepreneurs tend to encounter challenges, particularly in the international dimensions, they can be extremely naïve about how they have to deal with them”. It is maintained that internal legitimization will have a moderating effect on external legitimization, and the lack of internal legitimization will be negatively associated with external legitimacy. Future research may also investigate the relationship between internal legitimization and external legitimization in new ventures by examining how entrepreneurs and their partners set up unambiguous goals and develop relevant performance benchmarks when the new venture and the industry it operates in are not clearly established and lack legitimacy. One may expect a negative relationship between goal ambiguity and the acquisition of external legitimacy. The above is summarised as follows:

- P10 Lack of internal legitimacy will be negatively associated with external legitimacy.
- P11 Goal ambiguity will be negatively associated with the acquisition of external legitimacy.

6 Conclusions

Being positioned within the legitimacy and international entrepreneurship research streams, this paper addresses the question of how and why INVs acquire external legitimacy and strive for survival in the face of critical events. In their quest for external legitimacy, INVs, more often than not, are captive to existing or emerging niche markets or to large enterprise players who demand exclusive partnerships. Being captive threatens new ventures' ability to reach the legitimacy threshold, and hence to survive. The constant drive for innovation and search for new business opportunities, as well as the urge for goal alignment and early exit strategies, may mitigate the risks associated with new ventures' captivity.

Grounded in data, this paper puts forward a typology of captivity to aid entrepreneurs and researchers in their pursuit of understanding the acquisition of external legitimacy. One potential application of the typology of captivity would be to conduct a longitudinal study to investigate how new ventures move from one quadrant to another. By mapping different new ventures onto Figure 1, researchers could develop theories about different trajectories these ventures may follow in their attempt to acquire external legitimacy; for example, whether these new ventures might take a short cut (moving from quadrant I to quadrant IV), or take a long path (from quadrant I to quadrant II, then III, and finally to quadrant IV), or take other paths in between during their growth process.

Given the nature of the case study research, as it is based on a small number of observations, the need is acknowledged for a follow-up research in the form of statistical inquiry to check the generalisability of the results, thus strengthening the external validity of the proposed typology of captivity. The results could be further tested and refined under the current global economic setting by exploring not only the acquisition, but also the maintenance of external legitimacy in INVs. In general, studying INVs using the lenses of legitimation and institutional theory is a promising area of research that may contribute to the advancement of the international entrepreneurship theory.

References

- Alvarez, S. and Barney, J. (2005) 'How do entrepreneurs organize firms under conditions of uncertainty?', *Journal of Management*, Vol. 31, No. 5, pp.776–793.
- Andries, P. and Debackere, K. (2007) 'Adaptation and performance in new businesses: understanding the moderating effects of independence and industry', *Small Business Economics*, Vol. 29, Nos. 1-2, pp.81–99.
- Barringer, B. and Harrison, J. (2000) 'Walking a tightrope: creating value through interorganizational relationships', *Journal of Management*, Vol. 26, No. 3, pp.367–403.
- Butler, J. (1991) 'Toward understanding and measuring conditions of trust: evolution of conditions of trust inventory', *Journal of Management*, Vol. 17, No. 3, pp.643–663.
- Chell, E. (1998) 'Critical incident technique', in Symon, G. and Cassell, C. (Eds.): *Qualitative Methods and Analysis in Organizational Research: A Practical Guide*, pp.51–72, Sage, London.

- Chell, E. and Pittaway, L. (1998) 'A study of entrepreneurship in the restaurant and café industry: exploratory work using the critical incident technique as a methodology', *International Journal of Hospitality Management*, Vol. 17, No. 1, pp.23–32.
- Coviello, N. and Jones, M. (2004) 'Methodological issues in international entrepreneurship research', *Journal of Business Venturing*, Vol. 19, No. 4, pp.485–508.
- Cusumano, M. (2004) *The Business of Software: What Every Manager, Programmer and Entrepreneur Must Know to Succeed in Good Times and Bad*, Simon and Schuster, London.
- Dacin, M., Oliver, C. and Roy, J-P. (2007) 'The legitimacy of strategic alliances: an institutional perspective', *Strategic Management Journal*, Vol. 28, No. 2, pp.169–187.
- Davidsson, P. (2003a) 'The domain of entrepreneurship research: Some suggestions', in Katz, J. and Shepherd, D. (Eds.): *Advances in Entrepreneurship, Firm Emergence and Growth*, pp.319–375, JAI Press, Greenwich, CT.
- Davidsson, P. (2003b) 'What entrepreneurship research can do for business and policy practice', *International Journal of Entrepreneurship Education*, Vol. 1, No. 1, pp.5–24.
- Delmar, F. and Shane, S. (2004) 'Legitimizing first: organizing activities and the survival of new ventures', *Journal of Business Venturing*, Vol. 19, No 3, pp.385–410.
- Dubin, R. (1978) *Theory Building*, The Free Press, New York.
- Edvardsson, B. (1992) 'Service breakdowns, a study of critical incidents in an airline', *International Journal of Service Industry Management*, Vol. 3, No. 4, pp.17–29.
- Eisenhardt, K. (1989) 'Building theories from case study research', *Academy of Management Review*, Vol. 14, No. 4, pp.532–550.
- Fan, T. and Phan, Ph. (2007) 'International new ventures: revisiting the influences behind the 'born-global' firm', *Journal of International Business Studies*, Vol. 38, No. 6, pp.1113–1131.
- Flanagan, J. (1954) 'The critical incident technique', *Psychological Bulletin*, Vol. 51, No. 4, pp.327–358.
- Glaser, B. (1978) *Theoretical Sensitivity*, Sociology Press, California.
- Gleason, K. and Wiggenhorn, J. (2007) 'Born globals, the choice of globalization strategy, and the market's perception of performance', *Journal of World Business*, Vol. 42, No. 3, pp.322–335.
- <http://www.nvca.org> (accessed on January 2009).
- Johnson, C., Dowd, T. and Ridgeway, C. (2006) 'Legitimacy as a social process', *Annual Review of Sociology*, Vol. 32, pp.53–78.
- Kaulio, M. (2003) 'Initial conditions or process of development? Critical incidents in the early stages of new ventures', *R&D Management*, Vol. 33, No. 2, pp.165–175.
- Keupp, M. and Gassmann, O. (2009) 'The past and the future of international entrepreneurship: a review and suggestions for developing the field', *Journal of Management*, Vol. 35, No. 3, pp.600–633.
- Kraus, S. (2011) 'State-of-the-art current research in international entrepreneurship: a citation analysis', *African Journal of Business Management*, Vol. 5, No. 3, pp.1020–1038.
- Lovaglio, D. and Kahneman, D. (2003) 'Delusions of success: how optimism undermines executives' decisions', *Harvard Business Review*, Vol. 81, No. 7, pp.56–73.
- Miles, M. and Huberman, A. (1994) *Qualitative Data Analysis: An Expanded Sourcebook*, Sage, London.
- OECD (2004) *Highlights of the OECD Information Technology Outlook 2004*, OECD Publishing, Paris.
- Oliver, C. (1992) 'The antecedents of deinstitutionalization', *Organization Studies*, Vol. 13, No. 4, pp.563–588.
- Oviatt, B. and McDougall, P. (1994) 'Toward a theory of international new ventures', *Journal of International Business Studies*, Vol. 24, No. 1, pp.45–64.
- Oviatt, B. and McDougall, P. (2005) 'Toward a theory of international new ventures', *Journal of International Business Studies*, Vol. 36, No. 1, pp.29–41.

- Rao, R., Chandy, R. and Prabhu, J. (2008) 'The fruits of legitimacy: why some new ventures gain more from innovation than others', *Journal of Marketing*, Vol. 72, No. 4, pp.58–75.
- Rutherford, M. and Buller, P. (2007) 'Searching for the legitimacy threshold', *Journal of Management Inquiry*, Vol. 16, No. 1, pp.78–92.
- Sanders, G. and Boivie, S. (2004) 'Sorting things out: valuation of new firms in uncertain markets', *Strategic Management Journal*, Vol. 25, No. 2, pp.167–186.
- Stinchcombe, A. (1965) 'Social structure and organizations', in March, J. (Ed.): *Handbook of Organizations*, pp.142–193, Rand McNally, Chicago.
- Storey, D. (1994) *Understanding the Small Business Sector*, Routledge, London.
- Suchman, M. (1995) 'Managing legitimacy: strategic and institutional approaches', *Academy of Management Review*, Vol. 20, No. 3, pp.571–610.
- Turcan, R.V. (2008) 'Entrepreneur-venture capitalist relationships: mitigating post-investment dyadic tensions', *Venture Capital: An International Journal of Entrepreneurial Finance*, Vol. 10, No. 3, pp.281–304.
- Turcan, R.V., Sørensen, O.J., Mäkelä, M. and Rönkkö, M. (2010) 'Mitigating theoretical and sampling biases in the design of theory-building research in international entrepreneurship', *International Entrepreneurship and Management Journal*, Vol. 6, No. 4, pp.399–417.
- Weick, K. (1989) 'Theory construction as disciplined imagination', *Academy of Management Review*, Vol. 14, No. 4, pp.516–531.
- Yin, R. (2003) *Case Study Research: Design and Methods*, Sage, Thousand Oaks, CA.
- Zaheer, S. (1995) 'Overcoming the liability of foreignness', *Academy of Management Journal*, Vol. 38, No. 2, pp.341–363.
- Zahra, S. (2005) 'The theory of international new ventures: a decade of research', *Journal of International Business Studies*, Vol. 36, No. 1, pp.20–29.
- Zimmerman, M. and Zeitz, G. (2002) 'Beyond survival: achieving new venture growth by building legitimacy', *Academy of Management Review*, Vol. 27, No. 3, pp.414–431.
- Zott, C. and Huy, Q. (2007) 'How entrepreneurs use symbolic management to acquire resources', *Administrative Science Quarterly*, Vol. 52, No. 1, pp.70–105.

Notes

- 1 Examples of employing critical incident technique could be found in organisational (Butler, 1991), entrepreneurial (Chell and Pittaway, 1998; Kaulio, 2003), as well as international entrepreneurship studies (Turcan, 2008).
- 2 Owing to space limitations, the interview protocols, as well as data meta-matrices and other non-confidential data are not reproduced here but are available upon request.

Appendix

Case summaries

Finance-Software had been developing business-to-business integration platforms for the financial service industry that allow effective and efficient management of industry-standard message formats. It was founded in 1996 as a consulting company after a management buy-out of a research software unit of a foreign multinational company. It continued servicing the former parent organisation, thus having a guaranteed revenue stream, 90% coming from international sales. In a couple of years, the co-founders realised that:

- 1 the opportunity they identified initially was not in demand at all
- 2 as a result, they were incurring losses
- 3 they were operating without any focus
- 4 there was a need to explore new market opportunities in order to stay in business.

To achieve the above, they decided to transform from a service- to a product-oriented company, and immediately started the search for opportunities. The transition to a new business model required the founding entrepreneurs to make two fundamental decisions: firstly, which particular technology to concentrate on; and secondly, which vertical market to focus on. They *looked around* and identified the financial sector as a potential market that eventually might adopt the new technology. At the time, in the company, these two paths, technological and financial service, were running in parallel. The convergence of these two paths was possible due to UK regulations that were forcing financial service organisations to adopt e- and internet-based solutions for their businesses in order to manage industry standard message formats (e.g., customer access to data; distribution of financial products, etc.).

Probably the most important decision to make towards the successful realisation of this financial opportunity was to decide whom to partner with from the enterprise space. Finance-Software approached several large organisations, including Sun, Oracle, IBM, and even Microsoft. Eventually, the co-founders partnered with [one of the above organisations] as it had become the major adopter of that new technology, and already had a strong foothold in the financial service market.

As a result, Finance-Software focused exclusively on the domestic financial service market and became the leading e-commerce provider in that market. It grew organically from 30 employees in 1998 to 60 in 2001, and the revenue target was almost achieved: it increased by approximately 260% by 2002. In April 2001, Finance-Software expanded its operations throughout the UK by opening three offices and forecasted a further increase in the number of employees up to 150 by 2003. By midsummer of 2001 it had launched its new product for the financial service market.

Late in 2003 however things started to deteriorate as the financial industry was slow in adopting their product, and in 2003 Finance-Software reported an after tax loss of approximately £600,000. By the beginning of 2004 only 11 members of its staff remained with the company. What the co-founders found out was that their product was "...at least 12 months too early". They decided not to keep the company going as a service company since it would not generate enough money and eventually would cease trading. Instead, the co-founders decided to cocoon, i.e., to reduce the costs of the company to the point where they could keep the company going forever, and in doing so retain ownership of their intellectual property.

Key critical events are summarised below:

- the business opportunity that allowed Finance-Software to internationalise turned out to be unreal
- the founders identified the need to diversify and deliver a tangible product, rather than service
- a new, niche market in the home country was identified and new technology adapted

- as big players were demanding exclusive partnership, Finance-Software had to partner with only one large player in the chosen vertical market
- the IT market in the USA was collapsing
- the founders realised that they were at least 12 months too soon to the market and decided to cocoon.

Project-Software has been producing estimation tools to predict costs and timescale-of-information technology projects customised for various managerial and engineering levels. It was founded as a consulting company in 1992 by two entrepreneurs. At its peak, in 1999, Project-Software employed eight full-time and two part-time employees. By 1995, the founding entrepreneurs realised the necessity to diversify and deliver tangible products to the market in the form of software. R&D activities commenced in 1995 and in July 1997 the first version of the product was launched via an original equipment manufacturer deal (OEM). The OEM deal was short-lived however, as the OEM partner, who was selling Project-Software's product under their own brand-name, got into trouble and was acquired by a US company. Project-Software managed to gain control of the product, re-brand it, and to start its own sales.

The founding entrepreneurs pitched to VCs in 1998 and received their first seed capital of £600,000 in June 1999, and a second capital influx of £150,000 in July 2000. At the VCs request, the US market became the priority market. About the same time, a non-executive was hired. Upon his proposal, and with VC backing, a relationship with a master distributor was established to target the EU market, a relationship that *did not really work*. In 2000, Project-Software was ready to take its product to the USA; during 2000 it did not get any sales from Europe, and by the end of the year had 'abandoned hopes for Europe'.

The early successful experience in the USA was *short lived* as, not long after they internationalised, the IT market in the USA started to collapse, and all the web companies that were their primary market started to disappear. Project-Software started reporting losses from the international sales: by 2000 the share of international sales had gone from 30% in 1999 down to 0%. Nonetheless, Project-Software continued its venture to the USA and in February 2001 the managing director signed a joint-venture agreement with a UK-based software-tools company that had a strong customer-base in USA, and that assumed integrating the companies' products and selling the integrated product to this customer-base.

In early 2001, the founding entrepreneurs, backed by a new non-executive who "...helped them to step back and see the big picture", presented to their investors "a really dramatic proposal to improve things". The proposal consisted of keeping a very small subset of the company, letting a number of people go, and just continuing with a small number of people; the company CEO said that "the intention really was just to cocoon ourselves to get through that period". Eventually, all the investors backed up their proposal to cocoon but one, their bank, which thought that Project-Software *was too risky*, and said they were going to withdraw the overdraft facility. Project-Software officially ceased trading in September 2001.

Immediately after the liquidation, in October 2001, the co-founders formed a new separate company, Project-Limited, and chose to only reemploy the senior software engineer who had intimate knowledge of the product. They bought the rights to their

former software product from the liquidator. The transition was finalised in November 2001. As it retained strong relationships with its joint-venture partner, project-limited re-internationalised immediately after the *resurrection*.

Key critical events are presented below:

- the founders identified a new business opportunity to diversify and deliver a horizontal product; a hybrid-led business model was adopted
- the deal with the OEM failed, but they managed to retain the IP
- to raise venture capital, the founders had to re-write the business plan in order to comply with the VCs requirements, i.e., to internationalise instantly rather than incrementally, and to adopt a product-led rather than hybrid-led business model
- despite the fact that the IT market in the USA was collapsing, Project-Software continued its exporting efforts
- together with the newly appointed non-executive, the founders presented a plan to ‘cocoon’ to the VCs, who rejected it; the company was liquidated as a result
- the founders resurrected the company by buying the IP from the liquidator and reemploying the senior software engineer.

Tool-Software has been providing tools for diagnosis, simulation, and the testing of smart-cards for chip and card manufacturers, network operators, and financial institutions. It was founded in 1985 as a service company by an entrepreneurial family to provide software engineering for embedded computer systems in the mobile telecom sector.

In 1991, Tool-Software won a project from a large enterprise to develop a smart-card test application. After the project was over, Tool-Software was left with the software. This is when one of the co-founders saw the opportunity to transform the company into a product-oriented one. One year later, the co-founders approached one of the largest telecom players. On the basis of a *gentlemen's agreement*, Tool-Software developed a tool to test mobile phone smart-cards. Although the telecom player paid for the development costs, the IP rested with Tool-Software. Based on the retained IP, Tool-Software developed the first version of its product in 1993 and immediately after decided to take it to Europe.

In 1994, when the situation was desperate, the co-founders “did dip their toes in the financial waters”, i.e., applied for funding but with no success. Nevertheless, Tool-Software moved to profitability in 1995 when the opportunity actually started to become real due to the global adoption of smart-card technology by telecom operators, and in the same year, Tool-Software took its product to the USA. In 1999, Tool-Software opened its first international office in San Jose, and in 2001 in several other US cities and in Tokyo. In late 1999, Tool-Software won a million dollar strategic contract with one of the largest players in the software industry to develop smart-card technology for second-generation mobile phones. This relationship did not last long as it was scrapped in early 2000 by that player, who was described by the CEO as a “bunch of bandits ...seriously bad company”.

Within four years, subsequent to 1996, Tool-Software had witnessed a very rapid growth in terms of sales and number of employees and became a worldwide leader in a very fast growing, niche market: smart-card technology. The sales from the USA

constituted approximately one third of the company's sales, and the number of employees grew from six in 1996 to more than 60 by 2001. In March 2000, Tool-Software secured its first round of funding to develop a platform that would allow it to create smart-card products for the telecom and finance sectors, and in January 2001, it received its second round of funding to further support the development of the platform that was valued at ~£30 million.

As it turned out in late 2001, the hype for the mobile phone as a payment device had not been realised; specifically, the 'bet' was on "rapid growth in mobile communications and a move to wireless application protocol and 3G technology". Tool-Software responded to the above downturn in its tool and platform businesses with a cost-reduction restructuring programme whereby the home-based operations were sacrificed in favour of the international ones. As a result, half of their staff was laid-off and offices in Japan and the USA were restructured but not closed. In 2001 and 2002, Tool-Software received its second and third round of funding respectively, and eventually released its platform in 2003. By 2003, 80% of its revenue from the tool business was coming from overseas as most of its approximately 220 customers were located in 33 countries.

Key critical events are presented below:

- having retained the IP, the founders decided to develop it further into a tool
- the founders tried to raise venture capital, but with no success
- the partnership with one of the largest software players in the market did not work out
- the IT market in the USA was collapsing
- the technology the tool was meant to test started being adopted globally; this allowed Tool-Software to rapidly internationalise
- as Tool-Software grew out of the tool market, it restructured its overseas operations, and focused again on the service business to generate tactical revenue
- the founders identified a new business opportunity to develop a horizontal platform, and were successful in raising venture capital.

Mobile-Software was set up with initial funding from four co-founders in 2000 to develop a platform for the industrial sector that would allow the mobile workforce of a multinational company to have access to their company's central computer via different types of hand-held devices, e.g., mobile phones and laptops. Mobile-Software internationalised right from its inception through acquisitions, aiming to enter the enterprise market and target *early technology adopters*.

As a result, Mobile-Software *grew very quickly*: three software providers were acquired within a period of six months in the UK, Netherlands, and Dubai. At the beginning of 2001, it started opening overseas offices in Denmark, Saudi Arabia, India and Bangladesh, with plans to later open offices in Germany and France. Mobile-Software expected to have a turnover of £6 million by 2002, rising to more than £15 million in 2003 and to approximately £60 million over the next five years. Within the same period, Mobile-Software already employed 60 people; at its peak, at the end of 2001, the number of employees increased to more than 100, with 30 employees in its headquarters and 75 in six countries.

The acquisition strategy allowed Mobile-Software to deploy vendors' existing products, thus ensuring a continuous stream of revenue while building the platform, as well as to deal with staffing issues. At the same time, this strategy brought up several issues that required Mobile-Software to invest additional resources in order to reduce the tensions that were arising from within. For example, as existing development and sales capabilities in acquired companies *were not good enough*, Mobile-Software had to invest a lot of resources in enhancing and bringing them up to speed. At the same time, Mobile-Software retained the owner-managers of acquired companies who "...could not work together as they had quite different views as to how to solve the technology problems". The above tensions eventually resulted in significant delays in the design and the development of the platform.

The fundraising process started about three months after the start-up. At that point in time, the IT market in the USA was collapsing and had started to worsen in the UK. Trying to get funding, the co-founders hyped their business plan; e.g., they asked for fewer funds than was required to carry out the *ambitious* business plan as originally developed. That hype was not enough to secure funding, and the co-founders turned for perspectives on Mobile-Software's market in particular and the IT market in general to a leading market research organisation and to one of big four finance players. Eventually, in May of 2001, Mobile-Software secured its first round of funding in the amount of £6 million, £3 million less than actually hyped, which was due in ten months' time and was subject to satisfactory progress.

By the end of 2001, it was clear that Mobile-Software was "...a little bit behind its revenues, and there was a delay in developing the platform". Mobile-Software failed however to secure an *eleventh-hour cash injection*. In early February of 2002, at a board meeting, one of the investors reversed its decision to provide a second-round of funding as it was being taken over; it was a hostile takeover by another investment house that withdrew all hi-tech projects from its portfolio. There was no time to look for any other options, and the co-founders had no alternative option but to put the company into administration. Mobile-Software ceased trading in March 2002.

Key critical events are presented below:

- the founders identified a new business opportunity to develop a horizontal product, and decided to internationalise instantly via acquisitions
- the founders had problems in integrating the acquired companies
- the IT market in the USA was collapsing
- the founders 'hyped' the business plan to 'buy the investors into'
- the founders received a third less than of what was 'hyped'
- the founders could not persuade the VCs to change the business plan accordingly
- two investors withdrew from the investment portfolio
- Mobile-Software ceased trading as the founders failed to find other investors.

Data-Software was founded in 1998 to develop data warehouse software to allow businesses to extract data from their operational systems and convert it into business-specific information. Backed by VCs in a multi-million pound deal, Data-Software was set-up by three entrepreneurs who bought-out an IP and a small R&D

team from a large software company. The first round of funding was used to prove the technology and the market, and to acquire marketing and sales expertise. The first version of the product was released in the middle of 2000. At its peak, by the end of 2000, Data-Software was valued at £25 million, employed 40 people, and it was expected to capitalise at £180 million in the next three years.

Data-Software was looking for a large enterprise player who would help *break into* the US market. After several *failed* attempts to partner with large enterprises, Data-Software started exploring another market niche, *second-tier* companies that are positioned behind the biggest in the technology-adoption cycle. Eventually, it secured a multimillion-dollar strategic partnership with one of the largest software companies, and immediately internationalised. Data-Software opened its first overseas sales office in the USA in late 1999 close to its strategic partner in order to support their mutual efforts in "...recruiting more dealers and train them to sell Data-Software's solutions". Concurrently, Data-Software was finalising its second round of funding aimed at "...developing global sales operations". Data-Software raised its second round of funding at the beginning of 2000 to facilitate global expansion, initially in the USA and then in Europe.

Despite the fact that the IT market in the USA had started collapsing and companies had stopped buying the technology, the co-founders continued pursuing an *out-and-out growth strategy* as they had "...to develop the company as fast as we planned". At the end of 2000, two more sales offices were opened in the USA; the company was continuing to recruit and expected to double its workforce over the next year. It was expecting to increase the number of its dealers from 50 to 300 by the end of 2001, and it had started to make inroads into Europe.

The strategic partnership did not live up to expectations, as, by the middle of 2000, Data-Software's strategic partner announced product development plans that overlapped with what Data-Software had been doing. These intentions of the strategic partner *spooked certain people*, and led to a lot of thinking and talking with regard to which route to take. The lead entrepreneur was of the opinion that the company should continue down the same path of selling the product, but switch to direct selling. The investors were of the opinion that the company should move to sell applications and also focus on direct selling; the VCs' option was eventually adopted in January of 2001.

Decisions also were taken to pull out of the USA and focus on the UK market by creating an application in a retail niche. In March 2001, the lead entrepreneur stepped down as the VCs brought in a new CEO to take the company down the decided-upon route. It became clear that Data-Software could not survive without additional funding as it was unprofitable all the way. By that time, the IT market started to worsen in the UK as well, and this made it even harder for additional funds to come by. The new CEO failed to save the company, and Data-Software was put up for voluntary liquidation. In fall of 2001, Data-Software ceased trading.

Key critical events are presented below:

- the founders identified a new business opportunity to develop a horizontal product
- the start-up to pursue this opportunity was backed by VCs
- Data-Software secured a strategic partnership with one of the largest software companies
- instant internationalisation to the USA followed immediately after

- despite the fact that the IT market in the USA was collapsing, Data-Software adhered to a strategy of fast, out-and-out growth
- the strategic partner announced market development plans similar to Data-Software's; this announcement spooked the VCs who decided to withdraw from the USA and focus on applications rather than product development
- not long after the lead entrepreneur stepped down, Data-Software ceased trading.