Entrepreneurs: Bucking the trend pays off

It's tempting for entrepreneurs to jump into a hot market, but they'd do better to go their own way, according to research by Chicago Booth's Elizabeth G. Pontikes and William Barnett of Stanford University.

The researchers examined data on 4,566 software-industry start-ups spanning 456 market categories and 13 years. They mined thousands of press releases published from 1990 through 2002, using automated text software to identify market categories and track how businesses identified themselves over time. The researchers also interviewed software-industry executives, investors, and board members to learn more about how they made decisions when breaking into new markets.

Pontikes and Barnett find that although there's a strong impulse to enter a market while it's hot, those who jump on market trends are less likely to secure funding from venture capitalists and more likely to exit that market later. Similarly, companies that receive venture funding during these rush periods are less likely to go public. However, "non-consensus entrepreneurs who buck the trends are most likely to stay in the market, receive funding, and ultimately go public," they write. And start-ups that enter a market where others have gone bankrupt are more likely to survive.—*Jane Porter*

Elizabeth G. Pontikes and William Barnett, "The Non-Consensus Entrepreneur: Organizational Responses to Vital Events," *Administrative Science Quarterly*, October 2016.

A contrary path to success in a market

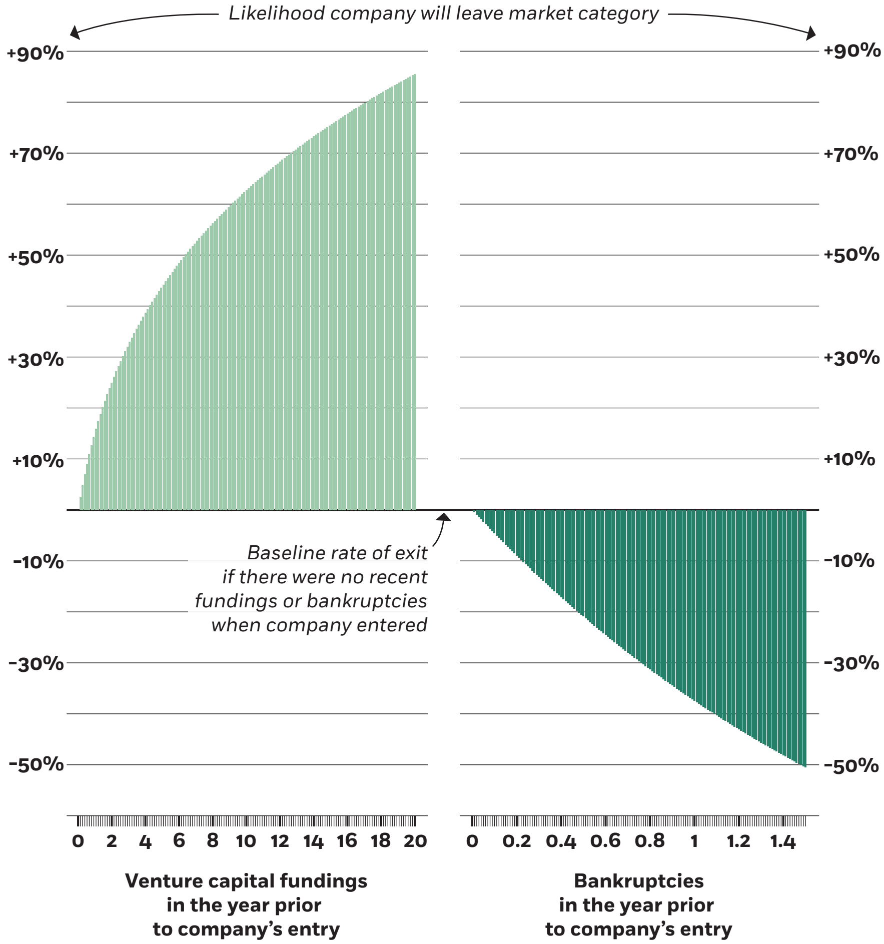
Recent action in a market category can be a good predictor of start-ups' staying power.

Chasing venture capital—and failing

If there were more recent fundings in the market category when a company first entered, the likelihood increases that the company will be gone four years later.

Following bankruptcies—and surviving

If there were more recent bankruptcies in the market category when a company first entered, the likelihood *decreases* that the company will be gone two years later.



Pontikes and Barnett, 2016

KEY INSIGHT

VENTURE BACKERS INVEST IN PEOPLE, NOT PRODUCTS

Venture capitalists backing big ideas are likely less interested in the product than the people developing that product. Harvard University's Paul Gompers, University of British Columbia's Will Gornall, Chicago Booth's Steve Kaplan, and Stanford University's Ilya A. Strebulaev surveyed 885 institutional venture capitalists at 681 firms and report that high-dollar investors attribute their willingness to invest or not to the management team.

Paul Gompers, Will Gornall, Steve Kaplan, and Ilya A. Strebulaev, "How Do Venture Capitalists Make Decisions?" NBER working paper, August 2016.