Think twice about being first to market

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New research offers fresh insight on when to launch a product or service, and shows that being first to market isn't always a competitive advantage.

In 2004, David Cohen had an idea for a social network for mobile phones that would connect users in the real world. His Boulder (Colo.)-based company, called iContact, raised $600,000 from investors and the founders' contributions, launched a beta version, and seemed poised to tap the much hyped mobile software market. Cohen, then 36, had already founded a successful software company. But after 18 months, he was unable to get phone carriers to distribute his software, and he shuttered the company, returning 80% of his investors' money. "Everybody was saying mobile was coming, it was going to be open; GPS was coming, it was going to be great," says Cohen. "That didn't really happen for another four years."

Bets on mobile applications didn't begin to pay off until Apple's (AAPL) iPhone app store opened the market in 2008. Several companies that followed iContact's path later found more traction, including Loopt, Mig33, and Brightkite, a startup Cohen invested in which was acquired last month by competitor Limbo.

The real competitive advantage

Conventional wisdom says being first to market creates a competitive advantage. Reality is more complicated. Market opportunities are constantly opening and closing, and a hit idea at one point could be a dud a year earlier or a yawning "me too" business a year later. It's tough—likely impossible—to pinpoint the best moment to enter a market, but common sense dictates new entrepreneurs can improve their odds if they weigh how much they stand to gain or lose by waiting.

New academic research suggests one way entrepreneurs can evaluate whether they should enter a market first or wait on the sidelines. The decision depends on how hostile the learning environment is; that is, how much entrepreneurs can learn by observing other players before they launch compared to what they learn from participating after they enter, according to Moren Levesque, an entrepreneurship researcher at the University of Waterloo. Levesque, along with professors Maria Minniti of Southern Methodist University and Dean Shepherd of Indiana University, used a mathematical model to weigh the risks and benefits of entering the market early. Their research, published in March in the journal Entrepreneurship Theory and Practice is among the first to explore "how different learning environments may influence the entry behavior of entrepreneurs." (Note: The article is behind a pay firewall.)

The crux of the academics' findings on timing is this: In a hostile learning environment, entrepreneurs gain relatively little benefit by watching others. For example, if the relevant knowledge is protected intellectual property, studying the market before entering wouldn't yield much advantage. In these situations, the trade-off favors entering early. But in less hostile learning environments, where entrepreneurs gain valuable information likely to increase their success just by watching other companies, companies benefit from waiting and learning lessons from earlier players. IContact's successors, for example, may have learned from watching the company's trouble getting mobile networks to distribute their software, a barrier that was removed by the iPhone's app store.

"If you enter early, you are more of a pioneer. You can have a competitive advantage," by locking in key customers, suppliers, or intellectual property, says Levesque.

"If you can not do any of this, than it may not be a good strategy, because there is always a cost to being a pioneer." But deciding when to enter a market solely on the advantages of learning is not enough. Entrepreneurs also need to launch before an opportunity closes.

Getting lucky with good timing

In the summer of 2007, Sunny Gupta, a serial entrepreneur in Seattle, began exploring an idea for on-demand software to help large companies track their IT spending and reduce costs, after a contact at Wall Street firm casually mentioned the issue. He spent that summer and early fall talking to chief information officers at Fortune 500 companies about the type of software they needed. Gupta originally planned to spend about a year building the product. But on a trip to New York in October 2007 to meet with CIOs at financial companies, he saw they were under intense pressure to cut costs and justify their IT spending—precisely what his product would do. Gupta realized he needed to speed up his launch to take advantage of the market opportunity before other companies got there.

When he got back to Seattle, he and his co-founders started working around the clock on everything from building a product mock-up and writing a financial plan to talking to investors and incorporating the business. By November, Apptio (as they dubbed the firm) raised $7 million in venture capital. By March 2008, Apptio had four paying customers using a beta version of the product. A full launch followed in June, and Gupta had already demonstrated Apptio's ability to reduce costs by the time the financial crisis erupted in September. Apptio now has nearly three dozen clients and 30 employees. "I believe the window of opportunity was within those six months: from March to September 2008," Gupta says now.

There is, of course, some element of luck. Cohen believed he was positioning iContact at a similar sweet spot in the market. But entrepreneurs who ignore timing, or assume that being first is always better, do so at their peril. Levesque suggests entrepreneurs ask themselves, "Can I try to understand what I can gain if I delay versus what I can lose if I delay?" After all, she says, deciding when to enter a market is "an irreversible decision, so it's a very important one."

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