



## Mixing Business and Pleasure for Competitive Advantage

**A recent study shows how entrepreneurial team formation can be improved by combining two established strategies.**

Entrepreneurship is a major driver for economic and technological advancement. However, we also know that about 90 percent of start-ups fail early. If this staggering percentage of initiatives fail before they get off the ground, we may have missed the next Amazon, the next Google or the next Facebook. Many opportunities fail prematurely because the start-up team cannot perform properly. Yet there hasn't been much research about the initial phase of entrepreneurial development.

Our work focuses on this initial stage when entrepreneurial teams are formed. Existing literature examines teams that already exist and perform, like most teams in organisations that are assembled by either the team leader or the HR business partners. Unlike entrepreneurial teams, they are usually not self-formed.

From our previous research, we know that the **team makeup is the magic bullet** in entrepreneurship. But why does a particular team formation strategy result in more successful start-ups? Building a team around not only skillsets but also personal affinity creates a special kind of team. Most entrepreneurial teams are either created from an interpersonal attraction based on a dense (and closed) social network or bound by the search for specific resources, i.e. to fill knowledge gaps. Combining these two strategies into a dual strategy is both

difficult and rare. Yet we and our co-authors\* found in our recent **work**, forthcoming in the *Academy of Management Journal*, that applying this dual strategy to an entrepreneurial team formation yields considerable competitive advantage at the initial stages of a firm.

Teams that mix business and pleasure have a unique approach to learning. One example is **Moovit**, a firm founded with this dual strategy. Two MBA students decided to launch a new venture together and came up with the idea of a smart urban navigation. However, they needed an expert in this specific entrepreneurial domain so they recruited the third member of their founding team. It became successful early on and the founders sold their new venture to Intel.

When teams are created keeping in mind both friendship and complementary resources, they enable *transactive memory systems*, shared knowledge and processes that set certain start-ups apart from others. The team develops a system to encode, store and use knowledge, with a clear understanding of who knows what and who does what within the team. If one team member is an expert in technology and another is an administration expert, a third team member clearly understands that they don't have to take care of those aspects and can focus on another part of the

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business, like marketing. Each team member deepens their knowledge, skills and capabilities within their own domain; when performing together as a cohesive unit, they trust each other and effectively coordinate their actions, broadening the pool of resources and capabilities.

This specific learning system is what allows entrepreneurial teams formed with a dual strategy to gain a competitive advantage very early on.

## Study results

In this research, we found that entrepreneurial teams formed with the dual strategy were very rare. We conducted three different studies, two of which involved self-formed teams. Only 17 percent of our first sample used a dual strategy and a mere 10 percent of our second sample were created with this in mind.

The first study used data from the crowdfunding platform Kickstarter. We measured how much money these teams raised on Kickstarter. Seed funding helps new ventures start off strong. During our study period, 206 teams reported about their team formation, and we used this information to sort the teams into interpersonal, resource or dual strategies. The ventures that included information about their team makeup raised more compared to those that didn't share that data. Overall, dual strategy teams more than doubled the seed funding amount compared with the interpersonal or resource strategy teams on Kickstarter.

The second study was an entrepreneurship competition; success was measured by how long a new venture survived. Each step of the competition brought the opportunity to speak with more mentors and investors. A new venture's visibility increased as it remained in this competition. In this study, although only 10 percent of the teams were formed with a dual strategy, these teams were more than twice as likely to be chosen for the competition and had about a four times higher chance of surviving the competition to the final stages. The winners in one cycle (a start-up that created a smart system that customised advertisements in web browsers) were a dual strategy team; romantic partners interested in AI who teamed with an expert in human behaviour to better understand their users and together they built a very successful company that continues to operate.

The third study was a randomised controlled trial as part of an experiential element of entrepreneurship courses at an American university. The measure for success was the amount of money the teams made from selling their initial products or services. Unlike the first two studies, we created three-member teams based on their CVs and social network

assessment. The teams were assigned using the four strategies: 1) resource seeking, 2) interpersonal attraction, 3) dual strategy, and 4) neither strategy. We found that although they were not self-selected, teams using the dual strategy were nonetheless able to develop stronger transactive memory systems, and thus performed better in terms of sales.

This third study shows that team formation strategies are also important in settings where teams are not self-selecting. HR managers, team leaders or others who build ad hoc teams can use these strategies in order to build better teams.

## Why learning matters

All teams and organisations can develop transactive memory systems. However, for entrepreneurial teams, having this kind of learning underpinning their new venture is necessary at the initial stages because they lack a meta knowledge of formalised structure and role allocation.

Entrepreneurial teams also face an incredible learning curve in an innovative environment that requires them to do all kinds of things at the same time. The entrepreneurial arena is often chaotic and turbulent. Facing different challenges from potential customers, investors and collaborators, entrepreneurs need to adapt constantly, even as they distract their competitors.

All teams could benefit from transactive memory systems as they naturally develop over time. In the initial stages of new ventures, this learning system is especially impactful because the business is in such an early stage and team members have an incredibly steep learning curve. Therefore, employing the dual strategy when assembling the founding team is the best way for a venture to start in the strongest possible position.

Our work is unusual in that we show how transactive memory systems emerge. We found that early transactive memory systems create a competitive advantage. Although team members who join later may adapt, they may be left behind in terms of learning.

Increasing or encouraging established teams to reflect on who is good at what and who does what may be less organic, yet the outcome can be the same. All team members need to share their knowledge of how the team works and talk about it openly. In many cases, people assume that other people know what they know, but this is an inaccurate assumption. Team members must be aware of this bias, but also be encouraged to share what they know so others can collectively build this shared knowledge of who knows what and does what within the team. This will eventually enable

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them to work smoothly and better assign roles.

### Finding the ideal co-founder

There's definitely a need for entrepreneurs to understand that their initial formation process will impact their start-up's success. Currently most entrepreneurship education programmes focus on idea validation, strategy and developing the right business model. However, it seems that building the right team and other "soft skills" are more important for competitive advantage.

People must know that they need to invest in both interpersonal and resource seeking strategies before they found their enterprise. But it's never too late to develop complementary skills or invest in building relationships. This may seem obvious, but our earlier **research** published in *Organization Science* suggests that it's very difficult to do both, especially at the beginning when team members both learn new tasks and about each other. Understanding the importance of investing in both simultaneously from the beginning but also throughout a firm's lifecycle is necessary for founders to thrive.

Serial entrepreneurs can attest to the success of a dual team formation strategy. Consider the start-up **Adallom** that we mentioned in our previous article. These founders sold to Microsoft and later decided to leave the software giant to found another venture, **Wiz**, with the same team.

The adage "Don't mix business with pleasure" should be left on the shelf when considering a founding team. Our research suggests that working with a romantic partner or a friend who has complementary knowledge and skills won't harm your new venture. In fact, it can help significantly.

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