



Canadian **Innovation** Centre

The Critical Factor Assessment: Planning for Venture Success

A complimentary white paper from

The Canadian Innovation Centre

*Guiding **Innovation** to be Market Ready...*

Introduction

Launching a new business is a complex and risky process. Whether it is a start-up venture or a new division within an existing company, there are a thousand things to consider and nearly as many that can go wrong. However, although any single initiative may be unique, many thousands of entrepreneurs have gone before, and there is much that we can learn from their successful experiences and even more that we can learn from their failures. Knowledge of the reasons most ventures fail, and even better, how to overcome them, is priceless.

The Canadian Innovation Centre (CIC) has worked with thousands of entrepreneurs and innovators over the course of its 30 year history. The CIC has developed a unique tool, the Critical Factor Assessment (CFA), to evaluate a venture's likelihood of commercial success. More importantly, the use of the CFA can help entrepreneurs and innovators improve the probability of success by identifying likely problem areas that need to be addressed before too much time and money are invested.

There is much we can learn from the successes of entrepreneurs, but we may learn even more from their failures.

The CFA tool has been used by both entrepreneurs and potential stakeholders to assess tens of thousands of new ventures. Initially developed as a mail-in form, which was reviewed manually, the CFA has more recently been adapted to an email version, where entrepreneurs submit responses via email, and responses are reviewed electronically and presented to the entrepreneur. In addition, the CIC has now enabled a web 3.0 online version of the CFA, which allows this valuable tool to be even more accessible. This new version also includes a “no-cost” on-line diagnostic tool, which can be used to both provide some initial feedback on critical items to be addressed and as pre-test before the more comprehensive CFA is employed.

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The Entrepreneur's Blindside

Entrepreneurs are those who see opportunity where others do not. Further, entrepreneurs are individuals who can bring such opportunities to life.

Entrepreneurs typically demonstrate such enviable characteristics as vision, determination and resourcefulness. They are often seen to be

passionate and open to feedback from others. However, in excess, each of these strengths can also be weaknesses. Those same characteristics which enable entrepreneurs to succeed where others might not, can create blind spots that can cause them to miss warning signs that others might have seen. Similarly entrepreneurs who become too attached to their venture can have difficulty recognizing when it is time to abandon a doomed venture.

Taking a new venture from concept stage to market success is not an easy process, and there are many issues which can arise at each stage of the process. Some of these issues are so serious that, if not resolved, they will prevent the venture from being successful, regardless of its other strengths. These can be thought of as "fatal flaws".

In these cases simple determination and resourcefulness alone are often not the answer. Sometimes they can be resolved by taking a different approach to the business, or by partnering with individuals or businesses who can provide a meaningful solution. However, in many cases, if a fatal flaw simply cannot be addressed, it may be better to discontinue with that opportunity and save your time, money and effort to invest in an alternate, more promising, venture.

Focussing on fatal flaws provides recognition that an inability to resolve a fatal flaw may be a reason to discontinue an opportunity, however focussing on this flaw, also provides

The very traits, such as confidence and persistence, which enable entrepreneurs to overcome obstacles and be successful, can prevent them from recognizing critical flaws that may sink their venture.

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a chance for the entrepreneur to apply their talents into figuring out how to overcome this issue. Thus the CFA tool can help entrepreneurs both validate if they have a viable opportunity and also identify issues that, if not addressed, could sink their venture.

The Secret Sauce: Inside the Critical Factor Assessment

The CFA tool was developed through working with thousands of entrepreneurs and innovators. During that work, the CIC observed that certain factors were consistently important in bringing a new offering to market successfully, regardless of the nature of the offering. And if these factors were not addressed, the likelihood of commercial success was lower.

*A **Fatal Flaw** is a factor, which if not successfully mitigated, would cause a venture to fail. Fortunately, many critical flaws can be reduced or eliminated.*

For example, in order to be successful, any market initiative, regardless of the nature of the product or service, must have a large enough potential market that the achievement of a realistic market share will generate revenue sufficient to make the venture viable. If there is not a large enough market, then even with a large market share, the venture cannot generate enough revenues, and hence profit, to succeed commercially. As such the venture would not be able to compensate the entrepreneur for his or her time, or any investor for their investment. As such, a small market potential is considered to be a critical flaw.

Notwithstanding, sometimes critical flaws can be addressed, thus removing or reducing them as barriers to success. For example, in the case above, it may be possible to increase the size of the potential market by altering the product or service or by using a partner to open up previously inaccessible markets. While there are no guarantees, recognizing and acting on critical flaws early can significantly improve the likelihood of commercial success.

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The CIC has packaged this experience into the Critical Factor Assessment tool and has used it to assess thousands of ventures with impressive results. According to an independent study which looked at the accuracy of the CFA as a predictor of venture success, in cases where a CFA has predicted failure, and the entrepreneur has elected to proceed, the venture has failed approximately 80% of the time. Conversely, in cases where the CFA has indicated a high likelihood of success, the venture has successfully made it to market approximately 80 % of the time.

The Critical Factor Assessment is now available in 3 forms: the full **Critical Factor Assessment, CFA Snapshot** and **CFA Snapshot Plus**.

The **Critical Factor Assessment** is the original, time-tested form of the service. It consists of an objective assessment of a venture's ability to satisfy 42 factors considered critical to a venture's success. These factors provide both an indication of the likelihood of success and a diagnosis of issues that need to be addressed.

*The impressive track record of the **Critical Factor Assessment** at predicting the likelihood of commercial success is based on the experience gained in evaluating thousands of new ventures.*

Here's how it works:

The entrepreneur provides information on their venture specific to the 42 factors. The information is reviewed by a team of at least two subject matter experts and then each factor is rated on an A,B,C scale where A means "Good", B means "OK" and C means "Critical Flaw". The entrepreneur receives a report with an assessment of the likelihood of successfully making it to market. The report also identifies areas of concern and provides suggestions for addressing them. The **Critical Factor Assessment** service is available for a fee of \$1395.

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The **CFA Snapshot Plus** is an abridged version of the full Critical Factor Assessment, focussing on the 8 factors commonly considered the most critical. These 8 factors were derived from the original 42 factors using a factor analysis that eliminates factors closely related to each other.

The entrepreneur uses the online tool to answer specific questions related to these 8 factors. This information is then reviewed by subject matter experts at the CIC. The entrepreneur receives an online report summarizing their ratings, and identifying the most critical issues that the entrepreneur should address before proceeding and common fixes for those issues. The **CFA Snapshot Plus** service is available for \$495.

The **CFA Snapshot** is a free online service that allows entrepreneurs to self-assess their venture against the same 8 factors considered in the CFA Snapshot Plus. In this case, the entrepreneur uses the online tool to rate their venture against the 8 factors, and receives an online feedback, automatically generated by the CFA Snapshot software's intelligent engine. This feedback summarizes the ratings and identifies the most common fixes for

The 3 Flavours of CFA: Which one is for You?

The **Critical Factor Assessment** (\$1395): an assessment of your venture by two subject matter experts against the full set of 42 critical factors. For the entrepreneur who is serious about maximizing the likelihood of commercial success.

CFA Snapshot Plus (\$495): two subject matter experts rate your venture on the 8 most critical factors and provide concise suggestions on addressing key issues. For the entrepreneur who is getting serious about their go-to-market strategy, but is not ready for a full assessment.

CFA Snapshot (free): an online tool to self-assess your venture's rating on the 8 most critical factors. For the entrepreneur whose venture is in the concept stage and who is looking for some quick ideas on how to flesh out their strategy.

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problem areas identified. Given the cost of the full Critical Factor Assessment and CFA Snapshot Plus, it is recommended that a CFA Snapshot self-assessment is done before one of the paid assessments. This gives the entrepreneur the chance to identify and address any fatal flaws identified.

First among Equals: The 8 Most Critical Factors

Of the 42 factors in the full Critical Factor Assessment, based on a comprehensive factor analysis, eight have been identified as being most critical. These eight factors, which are the basis of the CFA Snapshot and CFA Snapshot Plus, provide a concise and balanced mini-assessment of the commercial viability of a venture.

The eight factors are grouped into **Product**, **Market**, **Entrepreneur** and **Financial** categories. Below are the 8 most critical factors, along with some explanatory notes.

The 8 Most Critical Factors

Performance Advantage

Market Readiness

Product Uniqueness

First Customer

Distribution

Market Size

The Entrepreneur

The Financial Plan

Factor 1: Product - Performance Advantage

Does your proposed product/service offer performance advantages over existing solutions?

Unless a product/service offers the buyer a meaningful advantage over current solutions (or there are no current solutions), then significant adoption in the marketplace is very unlikely. Although this may sound obvious, determining performance advantage may require detailed knowledge of the market place and buyer behaviour. This highlights the importance of a detailed, independent market assessment. Many entrepreneurs

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strongly believe their product/service is superior, and they may be right, but unless the advantage is objectively quantifiable, it may be difficult to get financiers, partners and even potential customers to believe it.

If this critical factor is a weakness, a market assessment can help tune the product/service to improve its performance advantage, increase its value to the customer and expand the applicable market.

Factor 2: Product – Market Readiness

How far away are you from being able to deliver a completed product/service to your first customer?

If a product or service is not yet ready for market, it indicates the presence of substantial risk. For example, development may not be able to be completed successfully or might not be completed before the market window closes. Development may run over-budget, weakening the financial case for the product. Or competitors may leap-frog the product.

As well, if the product is not market ready, it can be difficult to verify the product's appeal to customers. And certainly, sales opportunities may be missed.

It is important to get the product ready for market as quickly as possible, but it is also important to use the development phase to ensure that the product is being developed to optimize the likelihood of commercial success. Market research and the involvement of potential customers can be very valuable here.

Factor 3: Product – Uniqueness

What is unique or patentable about your product that represents a barrier to entry for potential competitors?

If a product or service is easily copied by competitors, then the likelihood of commercial success is greatly reduced.

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It is important to have an effective defence strategy as part of your overall business strategy. Patents and copyrights are common defences, but there are many other ways to create competitive advantage, such as through distribution channels.

Factor 4: Market – First Customer

Have you secured or identified a first customer, who validates the need for your product or service and has agreed to try or buy it?

No matter how compelling a product or service is on paper, the proof is in the pudding – has a customer bought it? An initiative which has secured its first customers is ahead in many ways. A first customer:

- validates that the product/service is sellable
- acts as a test case for confirming/quantifying the value and benefits of the product/service
- is a source of feedback on the features of the product/service
- provides insight on pricing and the sales cycle
- enables reference and word-of-mouth marketing
- establishes a proof point for investors and partners

Securing a first customer is a critical milestone. If your initiative is weak in this area, it is important to invest the time and energy necessary to identify and then find that first customer. Ideally, investors (VCs and Angels) should help, but in reality, they tend to stay on the sidelines until a first customer is found. Distribution partners may help, but they also may hold off on their commitment until you can bring the first customer to the table.

Again, good market analysis can be very helpful here, by identifying potential first customers.

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Factor 5: Market – Distribution

Do you have supply chain partners to help you source products/services and reach new customers?

Effective distribution is critical to being able to reach the potential market and overcome the incumbent competitors. In fact, it is not always the best product that wins; sometimes it is the best channel.

The choice of distribution partner is also a key element of the overall strategy, since it is tied to market accessibility. This is also a critical test of whether or not the entrepreneur is able to convince external partners of the potential of their product.

Factor 6: Market – Market Size

Is market size /share likely to generate sufficient revenues and large enough to be interesting?

An all-too-common scenario is one where an entrepreneur says “the global market for our product is \$2 Billion – all we need to do is win 2% of that”. This overly-simplistic and uninformed approach is a red flag warning sign to investors and partners that the entrepreneur does not understand their market.

An independent market validation is critical. Many entrepreneurs do have a good understanding of their target market, but their views can be seen as biased and overly optimistic. In addition to verification of target market size, an independent market validation can provide valuable information on segmentation and competitive positioning.

Aside from verifying that the market exists, it is important to verify that the venture’s financial assumptions are sound. Do the math – is the potential market large enough to generate enough revenues to cover production costs and overheads, recover R&D costs and provide an attractive profit?

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Factor 7: The Entrepreneur

Do you have direct and relevant entrepreneurial, industry, or business experience?

The single greatest predictor (though not infallible) of an entrepreneur's success is past success. Entrepreneurship is a combination of personal characteristics and experience. You can educate on entrepreneurship, but you cannot instill it. VCs favour serial entrepreneurs because they have demonstrated that they have what it takes and through experience they have learned how to deal with the inevitable challenges.

In the absence of personal experience, compensate by surrounding yourself with the experience you lack in the form of partners, mentors, advisors and suppliers.

Factor 8: The Financial Plan

Do financial projections show that the company can make money and achieve cash-flow neutrality?

At the end of the day, this is the most important factor, the one to which all the other factors are building. You can't be successful unless there is a way to make money. There must be a viable financial model which incorporates all the assumptions about development, production, distribution, sales and financing. And because nothing is for certain, the model must be conservative and stand up under all of the most likely scenarios.

Building the financial model forces you to deal with all the other issues, such as sales forecasts, production costs, working capital requirements and so on. It is important for you to realize just what must be in place in order for your venture to be profitable. A robust financial plan is also required when you meet with investors (banks, VCs, etc.). If you can't make the numbers work, even by addressing the problem areas, then it is likely best not to move forward.

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The Benefits of a Critical Factor Assessment

The CFA is a very valuable tool for the entrepreneur. It has an impressive track record as a predictor of commercial success. It is also an accurate predictor of problems that can help avoid unnecessary failure by identifying barriers to commercial success and providing assistance in addressing those issues. In cases where such barriers cannot be overcome, entrepreneurs can be advised to save much time, money and effort by putting an early end to a venture that is likely to fail.

The benefits of the CFA can be summarized as follows:

- Provides a knowledgeable, objective assessment of a venture
- Provides a useful checklist of each point of importance, and a scale against which the venture can be benchmarked
- Identification of critical flaws(showstoppers) can suggest remedial actions that can still enable success
- Identification of low likelihood of success can stop the deployment of resources on opportunities unlikely to provide a return
- Creates a document for discussion with current and potential stakeholders (financers, partners, etc.)
- Provides a comprehensive checklist for entrepreneurs to review and ensure that each important factor is considered and discussed
- Enables learning from the experiences of other ventures

At a minimum, the CFA provides a useful checklist of important factors to think about in the development of a new venture. In some cases, it may trigger the early end of a doomed venture, saving time, effort and money. In other cases, it enables the entrepreneur to identify and address problem areas early, resulting in an increased likelihood of commercial success. In cases where no flaws are identified, or those

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Critical Factor Assessment Benefits

- Provides a knowledgeable, objective assessment
- Provides a useful checklist of critical factors
- Identifies possible showstoppers (critical flaws)
- Suggests remedial actions to enable success
- Creates a document for discussion with stakeholders

identified can be addressed, the CFA provides independent third party validation of an opportunity. This can give the entrepreneur the necessary confidence to continue with the venture, and/or create an independent assessment that can be used with suppliers, customers and potential investors to build confidence in the business.

Overall, an entrepreneur will find that putting their opportunity through a Critical Factor Assessment at an early stage in the venture creation process, is an excellent diagnostic test. It can provide an indication of the likelihood of commercial success prior to expending money on the next stage of the process, and either spending it inappropriately on non-critical elements, or continuing to spend money when a fatal flaw needs to be addressed. On the positive side, the use of the CFA will give the entrepreneur a valuable reality check that allows them to progress their business to the most important and risky part of its life cycle – going to market.



About the Canadian Innovation Centre

The Canadian Innovation Centre (CIC) is a not-for-profit Canadian corporation that provides services to assist entrepreneurs and innovators in the commercialization of their innovations. Through experience, networking and research, we strive to provide insight to assist businesses achieve sustainable success sooner.

We have over 30 years experience working with inventors, start-up companies, and enterprises of all sizes, validating innovations and enabling the commercialization path. Our experience, insight, and recommendations direct efforts and investment toward successful market entry with an emphasis on sustainability. This impact has been recognized by both international awards, government engagements and tens of thousands of clients who have accessed the Centre.

In addition to the CFA family of services, the CIC provides a full suite of offerings that support the end-to-end commercialization process.

The Canadian Innovation Centre can help you:

- o *Validate your product or business concept*
- o *Create a high performance business model*
- o *Optimize your intellectual property strategy*
- o *Pursue venture or non-equity financing*
- o *Develop a market-entry approach*
- o *Access government programs*
- o *Determine and enhance business valuation*

"The Canadian Innovation Centre is... an affordable expert resource in the business related skills required to successfully commercialize technological innovations."

- Venture Economics Report

For more information on the Canadian Innovation Centre and our services, visit us at www.innovationcentre.com

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