JOURNAL OF SMALL BUSINESS STRATEGY

DEVELOPING A NORMATIVE FRAMEWORK TO ASSESS SMALL-FIRM ENTRY STRATEGIES: A RESOURCE-BASED VIEW

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ABSTRACT

The decision to pursue growth opportunities is often complex and multidimensional. Small businesses pursuing these opportunities must consider many important criteria, such as resource requisites, timing and how to enter new markets. Unfortunately, there are not many systemic tools available to make these difficult decisions. One area of literature that may assist small businesses in deciding how to enter new markets is the resource-based view of a firm. The resource-based view of a firm complements current strategic management thought by refocusing efforts on the long-term accumulations of assets rather than short-term resource allocations. We synthesize concepts from the resource-based view with the literature on alternative entry strategies to develop a normative framework for small-business decision makers. Specifically, from the resource-based view, we consider: 1) different types of distinctive competencies – tangible/intangible resources owned by a firm and capabilities/processes used by a firm; 2) the degree to which these distinctive competencies can be sustained given certain environmental attributes, such as ease of imitation, abilities of competitors and industry dynamism. The interrelationships between distinctive competence and environmental sustainability are then used to identify appropriate strategies to enter new markets.

INTRODUCTION

The small business literature contains numerous studies that investigate failure rates of small firms. Failure rates have ranged from as low as 34 percent (Bates & Nucci, 1989) to as high as 90 percent (Kopf & Beam, 1992) during the first five years of operations. These high failure rates have resulted in a plethora of studies investigating reasons for small business failures. Often cited reasons include poor capital budgeting, excessive inventory, lack of formalized planning, inadequate provisions for contingencies and the inability to cope with growth (Laitinen, 1992; Duchesneau & Gartner, 1990).

All of the above-mentioned causes of failure can be attributed to inadequate strategic planning. Numerous studies have shown that small businesses committed to a formalized strategic planning process outperform firms that do not engage in strategic planning (Bracker, Keats, & Pearson, 1988; Kopf & Beam, 1992; Shuman & Seager, 1986; Shrader, Mulford & Blackburn, 1989). In one study, Lyles, Baird, Orris and Kuratko (1993) specifically found that small firms using formalized decision-making models were exposed to numerous levels of strategies, resulting in higher growth.

For those firms inclined to pursue growth opportunities, pursuit of distinctive competence and competitive advantage may become critical. A growth-oriented small business can create and sustain a competitive advantage as long as customers perceive value in the products/services the business offers and it is difficult for competitors to emulate. Therefore, distinctive competence and competitive advantage are a function of both the resources a firm possess and environmental attributes. Unfortunately it is often quite laborious for a small business to acquire the resources necessary to create a sustainable competitive advantage. Consequently, an important decision criterion when pursuing growth opportunities is whether a firm needs to consider a strategic alliance.

Several levels of strategies have been identified in the strategic management literature. These include: corporate-level strategies to identify which industries a firm should operate in (e.g., diversification strategies), entry-level strategies to identify how to enter new industries (e.g., joint-venture strategies), competitive-level strategies to identify how to compete in a given industry (e.g., low-cost and differentiation strategies), and functional-level strategies to identify how to effectively allocate resources. The small-business literature contains numerous studies investigating competitive- and functional-level strategies, as well as several studies investigating diversification strategies. However, with the exception of studies on franchising (c.f., Elango & Fried, 1997) and exporting (c.f., Brush, 1996), there is only a limited bibliography of research that investigates entry strategies available to small firms.

Specifically, based on an exhaustive review of journals publishing studies on small-business strategies[1], only three studies specifically considered alternative types of small-business entry strategies. One of the most noteworthy studies investigating various entry strategies available to small businesses is Vesper's (1990) 14 *entry wedges* for new ventures trying to enter new markets with existing competition. Additionally, Weinzimmer, Robinson and Fink (1994) identified several entry strategies available to small firms based on the occurrence of technological discontinuities in a firm's environment.

Finally, Forrest (1990) studied different strategic-alliance options for small technology-based firms, including client-sponsored research and collaborative research-and-development.

Given the absence of studies identifying entry strategies in the small business literature, one must ask the question "Is the study of entry strategies important in trying to determine small business success?" Deciding on an appropriate entry strategy is clearly important to large firms because it will impact long-term competitive position and ultimately growth and profitability. Admittedly, many small firms are never faced with a decision regarding the appropriateness of a particular

[1] Journals in the literature review over the last 10 years included *Academy of Management Journal, Journal of Business Venturing, Journal of Management, Journal of Small Business Management, Journal of Small Business Strategy, Strategic Management Journal.*

entry strategy. For example, the typical small business (e.g., a local "mom-and-pop" operation) doesn't have the resources or expertise to consider aggressively pursuing growth opportunities via implementation of a specific entry strategy None the less those small businesses that are growth oriented (e.g., a small biotechnology firm), one can argue that these same entry-strategy decisions made by larger firms are even more critical to smaller firms. In addition to being concerned about competitive position and profitability, basic survival may be at stake if a small business selects an inappropriate entry strategy.

Moreover, it has already been demonstrated that small firms which adopt formalized strategic-planning processes improve the quality of strategic decisions, including different forms of entry strategies (Lyles, et al., 1993). In order to fill this apparent gap in the extant literature and to provide entrepreneurs with additional information regarding the selection of appropriate entry strategies, we develop a normative model to provide a framework to assist small business decision makers in identifying appropriate entry strategies.

To accomplish these goals, we draw heavily on the literatures examining the resource-based view (RBV) of the firm to provide new insights into the selection of small firm entry strategies. The resource-based view has recently received considerable attention in the strategy literature, where the *Journal of Management* devoted a special issue to the topic. We chose to take this approach because the resource-based view of a firm complements current strategic management thought by refocusing efforts on the long-term accumulations of assets rather than short-term resource allocations. Unfortunately, given the relatively recent integration of the resource-based view of a firm into the strategy literature, our above-mentioned literature review identified only one study (Greene, Brush & Brown, 1997) that applied this view in a small-business context.

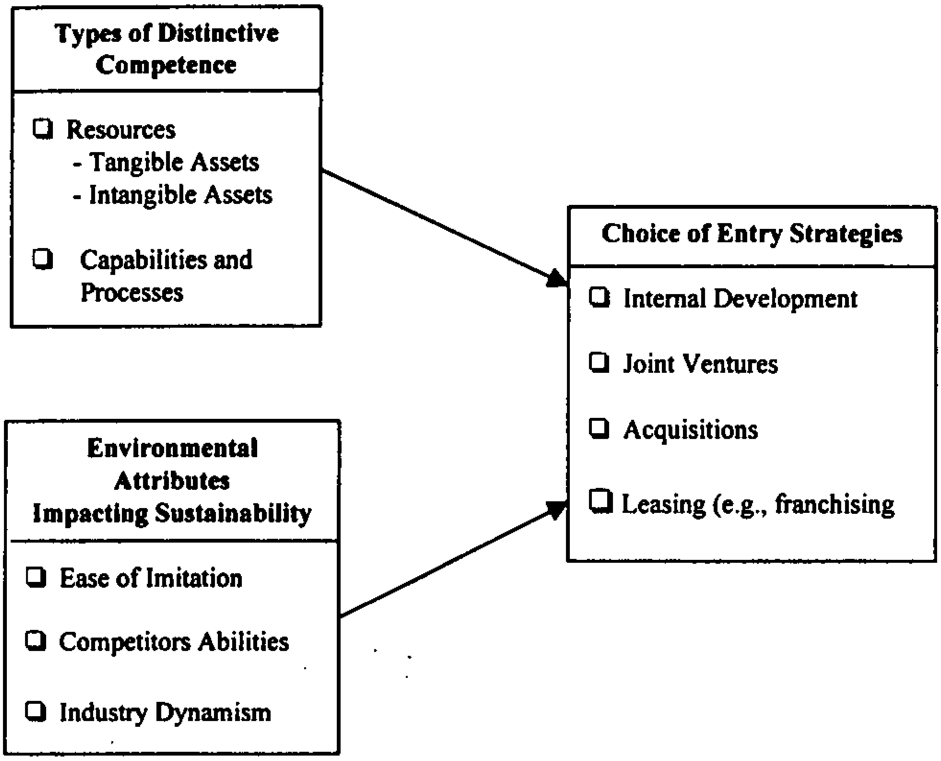
In order to develop our model, we begin with an introduction of the resource-based view of a firm to provide readers with the necessary background to apply RBV when selecting an entry strategy. We then synthesize concepts from RBV with the literature on alternative entry strategies to develop a normative framework for small-business decision makers. Specifically, from the resource-based view, we consider: 1) different types of distinctive competencies – tangible/intangible resources owned by a firm and capabilities/processes used by a firm; 2) the degree to which these distinctive competencies can be sustained given certain environmental attributes, such as ease of imitation, abilities of competitors and industry dynamism. As seen in Figure 1, the interrelationships between distinctive competence and environmental sustainability will be used to identify appropriate entry strategies for a given context.

RESOURCE-BASED VIEW OF A FIRM

When one thinks of strategic planning, the analysis of strengths, weaknesses, opportunities and threats (SWOT) comes to mind. This paradigm has been the central focus of strategic management for over a decade. Recently, the strategic management literature has begun to recognize an approach developed by industrial-organization (I/O) economists to identify distinctive competence called the resource-based view. While RBV is not intended to replace current strategy thought, it does have the potential to improve strategic analysis. The key difference between traditional strategic management and RBV is the focus on chronology.

Strategic management focuses on transitory streams of revenues and expenses (e.g., investment in improving processes to lower cost base), while RBV focuses on enduring accumulations of assets (e.g., extent to which the cost base is lowered) (Collis & Montgomery, 1997).

Figure 1 - Integration of Distinctive Competence and Environmental Sustainability for Entry Strategy Selection



For example, focusing on how transitory streams of revenue allocations create a competitive advantage may reveal how a firm achieved higher profits because it was able to lower its cost base. But the reason competitors cannot replicate this success from investing in process research-and-development is because they do not have the technological expertise. Therefore, it is not the streams of resource expenditures that allow the firm to *sustain* competitive advantage, but the accumulation of knowledge to commercialize an improvement in process knowledge.

A major contribution from RBV is that it provides a helpful theoretical framework for discussing the internal resources for firms of all sizes. It attempts to describe the way in which resources drive economic performance in a dynamic competitive environment. RBV draws on both internal and external analysis to describe a competitive environment. Through analyzing distinctive competencies, this view identifies abilities and strengths that may explain why some competitors are more profitable than others (Collis & Montgomery, 1995).

Distinctive Competence

The resource-based view focuses on resources that are tied to a firm in a relatively permanent fashion (c.f., Caves. 1980; Mosakowski, 1993; Penrose, 1959; Wernerfelt, 1984). The combination of resources and sequencing over time allows for the evolution of specific capabilities which optimally lead to competitive advantage (Amit & Shoemaker, 1993).

The most commonly used application of RBV in the strategy literature is to use it to identify *types* of distinctive competence, where distinctive competence is defined as something a firm can do better than any of its competitors. Specifically, RBV identifies two types of distinctive competence: resources and capabilities (Collis & Montgomery, 1997).

Resources - Resources as a form of distinctive competence may be either tangible or intangible. *Tangible resources* are physical assets that a firm owns, such as a unique product, plant and equipment. *Intangible resources*, on the other hand, do not physically exist, however they provide significant value, such as brand name recognition, reputation, patents, and technological or marketing know-how (Collis & Montgomery, 1995).

Capabilities - Capabilities refer to a company's skills at coordinating its resources and putting them to productive use (Collis & Montgomery, 1995). Unlike tangible and intangible resources, capabilities of a business include multiple sets of factors such as values, people, and processes (Collis & Montgomery, 1997). Capabilities specify how and where decisions are made within a company, the kind of behaviors the company rewards, and company's cultural norms and values.

Competitive Advantage

In order to turn a distinctive competence into a sustainable competitive advantage, a firm not only needs to possess a unique resource, but must also have the capabilities in place to exploit that resource. Therefore, the distinction between resources and capabilities is critical to understanding what generates a competitive advantage. A company may have unique and valuable resources, but unless it has the capability to use those resources effectively, it may not be able to create or sustain a competitive advantage.

For example, consider EMI, Ltd., the company that invented the CAT scanner. EMI had a distinctive competence in the form of a tangible resource. This was such a great accomplishment that the EMI research engineer who invented the machine won a Nobel prize for doing so. Initially, EMI was the only company that knew how to make CAT scanners. Clearly, EMI, Ltd. possessed a tangible resource as a source of distinctive competence, however it did not have the capabilities (manufacturing processes, service and support staff) to exploit this resource. General Electric, having sophisticated manufacturing processes and a sizable sales force, saw the opportunity for CAT scanner sales. They manufactured a modified version of EMI's invention (to work around the patent) and General Electric is the company that eventually realized the most benefit from the CAT scanner sales (Hill & Jones, 1998). Therefore, in order to realize the full benefits of a distinctive competence, a firm needs both resources and capabilities to turn the distinctive competence into a long-term competitive advantage.

This becomes particularly critical for entrepreneurial firms. For new ventures, achievement of a competitive advantage may be an ultimate but not immediate goal. Instead, survival or successful acquisitions of resources may be primary objective (Churchill & Lewis, 1983; Greene, Brush & Brown, 1997). However, once a small firm develops a distinctive competence, seldom does it possess both the resources and the capabilities to exploit the resource. If this is the case, choosing an appropriate entry strategy becomes critical to maximizing the benefit from a distinctive competence.

For example, if a small firm has a resource as a form of distinctive competence, but does not have the capability to exploit that resource, then it may have to consider some type of strategic alliance to overcome a potentially short-lived benefit. In the example of EMI, Ltd. and General Electric, it is quite possible that if EMI would have initially approached GE when it developed the CAT scan machine, GE would have welcomed the opportunity – not knowing it could reverse engineer a prototype and work around the patent. Instead, EMI tried to exploit a tangible resource via internal development without having the capabilities. Unfortunately for EMI, Ltd. this resulted in a very short-term benefit.

MODEL DEVELOPMENT

In order to provide a strategic decision-making framework for small businesses, our model attempts to integrate the concepts of distinctive competence and sustainability of competitive advantage to select appropriate entry strategies. The model will identify appropriate entry strategies based on two dimensions: 1) the degree of distinctive competence possessed by a firm, 2) the degree to which a distinctive competence can be sustained over time. The model being proposed in this study is presented in a 2x3 matrix in order to facilitate the reader's understanding of the interrelationships between distinctive competence and sustainability. Specifically, levels of distinctive competence are represented on the vertical axis and the degree of sustainability is represented on the horizontal axis.

Levels of Distinctive Competence

Recall that two forms of distinctive competence exist: resources (both tangible and intangible) and capabilities. While many successful small businesses possess neither form of distinctive competence, having at least one form provides future growth opportunities that would otherwise not exist. Moreover, by possessing both forms, distinctive competencies can further position a firm to take advantage of growth opportunities by providing potential competitive advantage. Therefore, we can identify three categories of firms in terms of their level of distinctive competencies. In the first category, a firm possesses neither resources nor capabilities, potentially thwarting growth opportunities. In the second category, a firm possesses one form of distinctive competence, either resources or capabilities, but not the other. In the final category, a firm possesses both resources and capabilities. The vertical axis of our model recognizes all three of these categories.

Degree of Sustainability

To select an appropriate entry strategy, we have already contended that a small business needs to consider its forms of distinctive competencies. However, environmental context must also be considered before an appropriate entry strategy can be identified. Even though a company may have unique and valuable resources and the capabilities to exploit these resources, the competitive environment will determine the degree to which competitive advantage can be sustained.

Resource-based theory provides three factors that will determine the degree of sustainability in an industry environment. The first factor is barriers to imitatibility, which assesses the degree of difficulty competitors would have in imitating a distinctive competence. Possessing a resource that competitors can easily copy may only generate temporary value. While patents may thwart imitation, if a resource provides significant value, competitors will attempt to find ways to copy it. Collis and Montgomery (1995) identified four characteristics that impact degree of imitatibility: physical uniqueness that cannot be copied, brand reputation/brand loyalty, substantial capital investments, and durability of products.

Figure 2 - Normative Model of Small Business Entry Strategies

	Degree of Sustainability	
	Unconstrained Sustainability	**Constrained Sustainability**
***Neither* Type of Distinctive Competence**	**Quadrant I** **Acquisition Strategy**	**Quadrant IV** **Diversification Strategy**
***Either* Type of Distinctive Competence**	**Quadrant II** **Joint Venture Strategy**	**Quadrant V** **Joint Venture Strategy**
***Both* Types of Distinctive Competence**	**Quadrant III** **Internal Development Strategy**	**Quadrant VI** **Leasing Strategy**

A second determinant impacting the degree of sustainability in an industry environment is the *ability* of competitors to imitate a competence. Ghemawat (1991) defined the ability of competitors to rapidly imitate distinctive competence as strategic commitment. Strategic commitment refers to the intensity in which a competitor invests in certain resources. If competitors show a pattern over time of investing in resources to imitate others, the sustainability of a distinctive competence could be threatened. Therefore, the willingness of competitors to aggressively invest in distinctive competencies may reduce the impact of the previously mentioned barriers to imitation.

The final determinant impacting degree of sustainability in an industry environment is industry dynamism. Dynamism refers to the degree of industry turbulence or change (Dess & Beard, 1984). Dynamic industries are characterized by high rates of product innovation and rapid product life cycles. Distinctive competencies in these types of industries are often short lived due to the rapid evolution of products.

While the three above-mentioned factors can independently impact the degree of sustainability, we consider their aggregate impact to identify two opposing categories. Specifically, the horizontal axis of our model categorizes constrained sustainability as an environment where it is difficult to sustain competitive advantage over a long period of time. Conversely, unconstrained sustainability is characterized by opportunities for long-term sustainability.

Selecting an Appropriate Entry Strategy

There are four basic categories of entry strategies available to a firm identified in the strategic management literature: *internal development* --entering a new market by one's self, *joint venture* -- entering a new market through a partnership, *acquisition* -- entering a new market by purchasing another company, and *leasing* -- entering a new market by offering a product/service through other firms (e.g., licensing and franchising). Clearly, each of these strategies has its own advantages and disadvantages, and given the specific context facing a small-business owner -- in terms of possession of distinctive competence and degree of sustainability -- certain entry strategies become more appropriate than others to achieving long-term success.

By considering the interrelationships between possession of certain distinctive competencies and opportunities to sustain competitive advantages, as seen in Figure 2, contexts arise that dictate specific entry strategies. In order to view these contingencies, strategies in each of the six quadrants of the model are discussed.

Quadrant I - In this instance, a firm possesses no form of distinctive competence in an industry characterized by unconstrained sustainability where factors like imitation and turbulence are low. Since the firm has no source of distinctive competence, the opportunity to pursue a strategic alliance would be minimized, as the firm has limited attractiveness for a strategic-alliance partner. If the firm were able to acquire a distinctive competence, it would have the opportunity to sustain that competence over a long-term period.

Acquisition, an entry strategy that involves the purchase of another company to enter a new market, is more common in large firms, however numerous small firms have also successfully utilized this strategy. The major advantages of pursuing an acquisition as an entry strategy in this context include access into unrelated markets entry and immediate results. The day the acquisition is completed, the firm is operating in a new market. If timing is a critical concern to secure competitive advantage, this may become a very important criteria in selecting an entry strategy -- internal development and joint ventures may literally take years to develop before a firm enters a new market.

The major disadvantages to acquisitions include initial capital outlay and potential turnover problems with existing employees of the acquiree. The most prevalent reason acquisitions are more common in large firms relative to small firms is simply cost. Many small companies don't have the necessary liquidity or leverage position to be able to afford the purchase of another company.

Quadrant II - Here, a firm has a distinctive competence in the form of either a resource or a capability in an environment that would allow for long-term sustainability. As evidenced in the EMI, Ltd. example, trying to exploit one form of distinctive competence without the other may expose a firm to considerable risk. However, when a firm possesses a distinctive competence, it may become a potentially attractive joint-venture partner. Therefore, if market timing is critical, it may be advisable to find a joint venture partner that can fill in the gaps necessary to turn the distinctive competence into a competitive advantage. Note in certain instances, if the timing of market entry is not an important issue, the firm may have the option to develop a distinctive competence in its area of deficiency to eventually pursue an internal-development strategy.

Ideally in a joint-venture partnership each partner brings a unique source of value to the partnership that other partners may be lacking. There are three major advantages of a joint venture, in this context, that make them particularly attractive to many smaller firms. First, the firm could eliminate a deficiency, such as the lack of a resource or capability. Second, the initial investment is shared between the joint-venture partners, and as previously mentioned, limited financial resources may be a limiting factor to a small business desiring to pursue new markets. Third, by using a joint-venture strategy, a small business can share risk. Unlike many larger firms, if a small business pursues new market entry by itself and fails, it may devastate the organization. By sharing risks with a partner, the potential downside risk of unsuccessfully entering a new market is minimized.

Three major disadvantages inherent of joint ventures include sharing profit, control, and knowledge. When a firm enters into a joint venture, it must share its profits with partners. Additionally, it must share control in the decision-making process with its partners. Possibly the most serious long-term disadvantage of a joint venture is that a firm may have to share valuable knowledge with its partner(s). If the joint venture partnership is terminated while the shared knowledge still has value, the joint venture partner can use the knowledge to potentially become a competitor.

Quadrant III - This context provides the most opportunity for future growth, where a firm possesses both forms of distinctive competence in an environment that is supportive of long-term sustainability. In this situation, internal development allows a firm to pursue growth opportunities without having to share the benefits of valuable distinctive competencies with other firms.

There are some other advantages to using internal development in this context. First, internal development gives complete control to a small-business owner, rather than sharing control with a partner. This may be extremely important for a small firm, given the influence an owner has on strategic-decision making. Second, all profits go back to the firm, rather than sharing them with others.

Major disadvantages include requisite financial resources, possible coordination difficulties and time in which it takes the small business to implement the strategy. Financial commitment for internal development may be substantial. Many small businesses may not have the necessary capital to pursue such a strategy. It may also be difficult for a small business to coordinate the necessary activities to successfully enter a new market.

Quadrant IV - When a firm is located in an environment characterized by constrained sustainability and does not possess any sources of distinctive competence,. new growth opportunities are limited. Investment into resources to develop competitive advantages may not be wise given the potentially short-lived benefits inherent of constrained sustainability. Moreover, the opportunity for a successful strategic alliance would be limited because the firm has no distinctive competencies to offer the partnership. If a firm is located in this quadrant and wants to pursue new growth opportunities, it may consider diversification into new markets through either geographic or product expansion.

Quadrant V - When a firm is located in a constrained market, but has a source of distinctive competence, a joint venture may be appropriate for reasons similar to discussion in quadrant II. However, trying to develop the other form of distinctive competence over time would not be advisable, given the short-term nature of a constrained environment.

Quadrant VI - In a situation where a firm possesses both forms of distinctive competence in an environment characterized by constrained sustainability, rather than investing resources in a short-lived competitive advantage, the firm could pursue a leasing strategy. Specifically, to realize the short-term benefits associated with a constrained environment, the firm could either a license or franchise its distinctive competence to minimize capital commitment while still benefiting from the competitive advantage.

This strategy is particularly attractive to small firms with limited capital to invest. If a small firm wants to enter new markets, but doesn't have sufficient capital, this may be its only option. Leasing allows a small firm to collect royalties from other firms for either licensing a specific technology or knowledge base, or it can franchise by allowing other firms to use its name and sell its product/service.

IMPLICATIONS AND CONCLUSIONS

The decision regarding how to enter a new market is complex and multidimensional. Not only should a small business consider sustainability of resources, but it must also recognize constraints. For example, even though a small business may possess a potential competitive advantage in an unconstrained market, it may not have the capital to pursue an internal-development strategy. Similarly, a small business may possess a form of distinctive competence where the possibility of a joint venture may be beneficial. However, the small-business owner may be reluctant to delegate responsibility or share control, making pursuit of a joint venture unrealistic.

Therefore, the model we offer in this study is not designed to be the single-source decision criteria for deciding on a particular entry strategy. Arguably, most small businesses never consider entering new markets, nor do they have the expertise to critically assess the degree of sustainability in their competitive environments. Rather the model we present here is intended to provide growth-oriented small-business owners with additional information to make a well-informed decision.

Potential benefits associated with this model may be realized by both practitioners and researchers. Although the notion that resources drive the sustainability of competitive advantage is simple, companies often have a hard time identifying and evaluating their own resources, assessing whether they are strengths or weaknesses, and understanding whether they can be sources of sustainable competitive advantage (Collis & Montgomery, 1997).

Having the ability to recognize strengths and weaknesses is essential to being able to attain a competitive advantage. Being able to identify strengths and weaknesses is difficult because characteristics that seem to be one or the other may, through examination, have no significance for competitive advantage. One recent method small business owners may find useful to assess resources for a competitive advantage is offered by Duncan, Ginter and Swayne (1998). Using a four-stage model they provide a systematic technique for assessing internal resources while recognizing environmental contexts.

There is also an opportunity for researchers to extend the model offered in this study. As previously mentioned, the resource-based view is seldom cited in small business literature, however its potential may be great. Researchers could try to operationalize the degree of environmental sustainability or try to develop a model that attempts to operationalize the value of a specific set of resources. Further, additional studies are needed to investigate other dimensions impacting entry strategies, such as financial resource constraints and high exposure to risk if an expansion effort fails.

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