Effectuation and Effectual Thinking

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OUTLINE

• Introduction
• What is Effectuation?
• Effectual Thinking
• Effectual Doing
• The Effectuator App
• Effectual exercises
Entrepreneurial Conventions

Three big questions surrounding venture creation

1. Are entrepreneurs born or made?
2. Are opportunities created or found?
3. What makes entrepreneurs different?
Dispelling Myths

Many myths surrounding entrepreneurship

1. Entrepreneurs Are Introverted Loners
2. Entrepreneurs See Business Building As A Path To Riches
3. Nothing Succeeds Like Success
5. With A Great Idea and Enthusiasm, Anyone Can Achieve Entrepreneurial Success.
Entrepreneurial Success

• We deem these entrepreneurs as successful – but what is success?!
• Why do we consider them so successful – they did not set out to achieve what they are known for now.
• Are we looking at the right thing?
What is Effectuation?
A rational economic approach

• Entrepreneurs thought to notice or discover a tangible opportunity such as a new product or venture
• To implement an entrepreneurial idea a normative decision-making process is followed
• Involves gathering relevant information and systematically evaluating alternatives
• Rationally choose the optimal option
A managerial approach

Causal reasoning to achieve a given goal – following pre-existing pathways

M1
M2
M3
M4
M5
A strategic approach

Creative causal reasoning to achieve a given goal – involving the creation of new pathways

M1
M2
M3
M4
M5
An effectual approach

- Effectuation and considers entrepreneurship as a series of decisions (Sarasvathy, 2001)
- Decision-making can be applied in ambiguous or uncertain settings
- Entrepreneurs imagine outcomes using these means and move into action without elaborate planning
The means of entrepreneurs

1. Who they are – their traits, tastes and abilities;
2. What they know – their education, training and experience;
3. Whom they know – their social and professional networks.

Effectuation & Effectual Thinking
An entrepreneurial approach

Effectual reasoning - imagining new possibilities using a given set of means
Effectual reasoning

Sarasvathy (2001) finds effectual reasoning to offer an alternative to causal rationality:

1. While causal reasoning focuses on expected return, effectual reasoning emphasizes **affordable loss**;
2. While causal reasoning depends upon competitive analyses, effectual reasoning is built upon **strategic partnerships**; and,
3. While causal reasoning urges the exploitation of pre-existing knowledge and prediction, effectual reasoning stresses **leveraging of contingencies**.
Effectuation & Effectual Thinking

Interactions with other people

Effectual Stakeholder Commitments

NEW VENTURE / MARKET CREATION

Who WE are
What WE know
Who WE know

What can WE do? (Affordable loss)

NEW MEANS

NEW GOALS
Taking and managing risk

EFFECTUATION

High

Risk

Low

Low

High

Return

Effectuation & Effectual Thinking
Effectual principles

- **Bird in Hand Principle** - Start with your means rather than wait for the perfect opportunity. Start taking action, based on what you have readily available.

- **Affordable Loss Principle** - Set affordable losses and evaluate opportunities based on whether the downside is acceptable, rather than on the attractiveness of the predicted upside.
Effectual principles

• **Crazy-Quilt Principle** - Form partnerships with people and organizations willing to make a real commitment to jointly creating the future—product, firm, market—with you.

• **Pilot the Plane** – Take control and remember that the future is in the making and not predetermined
Effectual principles

• Lemonade Principle - Leverage contingencies. Embrace surprises that arise from uncertain situations, remaining flexible rather than tethered to existing goals.
Effectual Doing
Preparing dinner

When you go to cook dinner how do you cook?

1. Have a specific menu, shop for the ingredients, follow the recipe
2. Have a look in the fridge, see what’s in date and make dinner accordingly
Cooking dinner

- Both following the recipe (i.e. causal cooking) and working with your ingredients (i.e. effectual cooking) will get dinner cooked
- Causal and effectual approaches demand different skills and training as part of the cooking and dining process
Effectual dining

Effectual reasoning often requires...

- Imagination
- Spontaneity
- Risk-taking
- Salesmanship
Effectual at U-Haul

- Discharged from the Navy in 1945, Leonard Shoen and his wife, Anna, wanted to rent a van to move their things from Los Angeles to Portland Oregon
- No one at that time seemed willing or able to serve that need by renting a van one-way.
Growing U-Haul

- Shoen and his wife started the U-Haul company (with the help of $5,000 from the her family).
- He began building rental trailers at the Carty Ranch in Ridgefield, owned by his parents-in-law,
- He painted his trailers bright orange with advertising on the truck “U-Haul Rental Trailers, $2.00/day”
Effectual reasoning

- They were not an “overnight success” and in the beginning, they were broke and had to move in with her parents.
- Shoen convinced friends, family, and customers to make down payments and then lend him money to buy his first trucks.
- He contracted with service station outlets to help sell the rentals.
- He offered early customers a discount if they established a U-Haul rental agent at their destination!
- By 1949, they had already built a coast-to-coast moving service.
The rise of U-Haul

• By 1955, there were more than 10,000 U-Haul trailers on the road and the brand was nationally known.

• Today, the annual mileage of North American U-Haul trucks, trailers and tow dollies would travel around the Earth 194 times per day, every day of the year.
Effectuation reasoning

• Means: Shoen started with what he knew:
  ▪ *He had his own needs (to rent a trailer one way) and figured others would want to do the same*
  ▪ *He started with small amounts of cash.*
• Attitudes towards others: Shoen partnered with suppliers, investors, customers
• Risk, return: Affordable loss—
  ▪ *Shoen didn’t start with a big investment. He improvised as he went along.*
So What?
Effectuation success

• These entrepreneurs are the same as everyone else but they are successful because they are master effectuators

• These entrepreneurs simply adopt a different approach to problem solving – they believed the future is shaped by human action and they shape it
Workshop Tasks
Reflection points

• In groups spend 5 minutes discussing whether your approach is primarily causal or effectual
• Now spend 10 minutes identifying where you might already have aspects of effectuation in your enterprise and entrepreneurship programmes
How we incorporate effectuation

In your groups spend 5 minutes to discuss how you might adapt the exercise to make it relevant for your learners...
Our smartphone application

1. How to effectuate your ideas
   - Think about your ideas, who you are, and what you know.
2. Effectual Resources
   - Network
3. Your Details
   - Name
   - Effectual Resources

What is your idea?
- Briefly outline your idea, give it a title and a description
- Description

EFFECTUATE your idea
- This section can help you develop your idea further.
- In addition to who you are and what you know, it is important to think about getting customers, suppliers, and other stakeholders to commit to your idea to minimize risk.

Additional Reading
- Theory
- Causation vs. Effectuation
- Sarasvathy’s 5 Principles
- Terms of use
- Acknowledgements
iDEAlab

NEW MEANS

NEW GOALS

LEVERAGE SURPRISE

Surprises add to means and change goals.

NEW PRODUCTS, MARKETS, AND FIRMS

MEANS

AFFORDABLE LOSS

GOALS

INTERACTIONS

COMMITMENTS
THANK YOU