RISK MANAGEMENT IN STARTUP PROJECTS: LEARNINGS FROM SELECT CASES IN INDIA

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Abstract

Startup projects constitute an essential component in building a strong ecosystem for nurturing innovation and generating viable employment that can drive sustainable economic growth in a developing country like India. However, startup projects that come up in a dynamic global business scenario face a multitude of risks that challenge their success. Our study aims at identifying various risk factors that are peculiar to startup units in India. Over 30 case studies were carried out across a variety of industrial projects and select NGOs to help identify specific risk factors that mar the success of startup units in the Indian environment. Our study finds specific risk factors at the strategic as well as operational levels that are important for success of the startup unit. It is hoped that the findings of this study will help to identify various risks during the early stages and thus improve the success rate of startup projects.

Key words: Startup Units, Projects, Uncertainty, Risks, Project Risks, Project Risk Management, Business Plan, Flexibility, Dynamic Feasibility Study (DFS)

1. INTRODUCTION

Projects are an important vehicle for the growth of industrial and economic activities. Projects, particularly the startup units, are undertaken to meet specific business or social needs in an economy. Such projects are triggered based on new needs or changes in environment. Thus projects and change go together leading to desired progress if the projects are successful. Considering the rate of change of technologies and accelerated pace of changes all over economic and techno-commercial space, managing startup projects has assumed extraordinary importance. The success of startup projects is essential for inclusive growth of any economy. No business venture will be a reality without the willingness to undertake some risk. Although risk is an inevitable part of running a business, a good understanding, analysis and effective mitigation of the risks can help to deal with risks in a proactive way. Startup units are more prone to risk factors and hence cannot afford to take a casual approach to risk management. They need to take up this aspect as a part of built in strategy. The success probability for projects will certainly enhance if the project processes for ‘Project Risk Management Processes’ are followed meticulously and proactive stances are adopted right from the stage of planning.

2. LITERATURE REVIEW

The term ‘risk’ indicates a connotation of negative impact and uncertainty. Van Scoy (1992) states that “Risk in itself is not bad; risk is essential to progress, and failure is often a key part of learning. But we must learn to balance the possible negative consequences of risk against the potential benefits of its associated opportunity”. The APM Guide on Project Risk Management (1992) indicates that “Project Risk Analysis & Management can be used on all projects, whatever the industry or project environment, and whatever timescale or budget”. When a decision maker has incomplete information, and therefore cannot determine the expected value of each alternative, he is facing uncertainty. However, when the decision maker knows the probability of every outcome, he is taking a calculated risk (Ofer Zwikael and Arik Sadeh, 2007). Kerzner (2009) defines risk as ‘a measure of the probability and consequence of not achieving a defined project goal’. Thus, project risk is a measure of “the cumulative effect of uncertain occurrences that adversely affect project objectives”. It is the degree of exposure to negative events and their probable consequences on some or all the project objectives such as scope, time, cost, quality and overall satisfaction of the stakeholders.

Gupta (2011) indicates that “Risk management in Indian companies is currently facing the problem of integration and incentivizing. The risk management function is not suitably blended into the corporate strategy and use of information technology for risk management is minimal.” It is noticed from the case studies that projects that did not pay specific attention to risk management did not succeed in reality, they failed. Coleman (2011) has aptly explained that “risk management is the art of using lessons from the past to mitigate misfortune and exploit future opportunities”. Caltrans (2012) has pointed out in the Risk Management Handbook that “although project risk management is considered to be valuable, many respondents are not familiar with the current Project Risk Management Handbook or have never participated in developing a risk register”. Debono (2016) finds that risk management is “the process involved with identifying, analyzing, and responding to risk for minimizing the impact and consequences of negative events”. Panigrahi (2012) has points out that, “to the extent that the SME project (in India) takes risk consciously, anticipates adverse change and hedges accordingly, it becomes a source of competitive advantage as it can offer its products at a better price than its competitors. What can be measured can also be managed, and risk mitigation efforts are more important than capital allocation against inadequate risk management system”. PMI USA (PMBOK, 2013) points out that Project Risk Management is “the art and science of identifying, assigning, and responding to risk throughout the life of a project and in the best interests of meeting project objectives”. KPMG report (2014) identifies “Project risk management is a continuous process of identifying, analysing, prioritising and mitigating risks that threaten a project’s likelihood of success in terms of
cost, schedule, quality, safety and technical performance. Boehm, 1991 considers risk management as a series of steps whose objectives are to identify, address and eliminate risk items before they become either threats to successful project execution or a major source of expensive rework. Organisations and owners often consider project risk management activities as “nice to have” on a project rather than as a core component of project controls”.

3. METHODOLOGY AND SCOPE
For the purpose of this study, ‘Startup’ means ‘Business Enterprise or a project endeavour that has been launched recently’. The term can refer to a ‘new business unit being set up by an entrepreneur’ or to a ‘new Strategic Business Unit (SBU) set up by an existing organization’. A period of first 5 years is taken as ‘project time frame’, because in actual practice, a typical startup unit gets out of business, even if it is not successful, only after a period of 3 to 5 years.

A case study approach was adopted using a structured questionnaire and interview process. One of the research questions was the following:

1. What are the risk factors specifically noted for the ‘startup projects in India’ apart from the conventional risk factors that are common to many types of projects?

The study undertaken covered 30 cases of which 17 were startups in different industries. The cases were selected based on ‘convenience sampling’, and in such organizations where the authors had personal working experience and contacts at senior management level.

The following specific factors were identified based on the data compiled through the questionnaire and detailed discussions with the participants on challenges faced by the startup units in Indian environment concerning Project Risk Management (PRM). These factors have been grouped under the following 5 groups for PRM.

1. Strategic Challenges
2. Company Structure / JV Partners & Challenges for Funding
3. Sales and Customer Relationship Challenges
4. Operational Challenges
5. Social & Cultural challenges

4. FINDINGS
Strategic challenges refer to comprehensive planning and flexibility in planning. It is noticed that many of the startup units make decision to set up a new initiative without a proper strategic analysis of the challenges involved in making the venture successful. This may be because the new entrepreneurs are often ‘technical’ professionals without management training or experience. Some of the risks include:

4.1 Strategic Challenges
a) Risks in Market Opportunity Analysis and Changes in Market Dynamics
Due to time lag, of 18 months to 24 months, between approvals for the project concept and time when the new venture is initiated, the market dynamics can change and the market projections are no longer valid, particularly when optimistic projections are made to suit Bankers lending norms. Strategic mistakes will have severe negative impact and will cascade into other areas of project management such as choice of technology, capital investments, scope of work, time schedules, quality and safety of the proposed project leading to financial disasters.

b) Incomplete or unrealistic Feasibility study
Startups must pay attention to feasibility studies with far more rigour rather than for routine requirement for chartered accountants and banking norms. Only a feasible business venture will generate adequate cash-flow and profits, withstand the risks it will encounter, remain viable in the long-term and meet the goals of the sponsors and stakeholders. Kelkar et al. (2016) identified the need for Dynamic Feasibility Studies (DFS) if the project environment undergoes changes.

c) Lack of judiciously developed ‘Business Plan’ or incomplete ‘Business plan’
It is noticed from the case studies that in many startup organizations, one does not find any attention (or lukewarm attention) paid to development of detailed business plan or a white paper about the proposed business venture (either short term of long term business plan). One notices that many startups organizations are set up based on more of ‘gut feelings’ rather than a judiciously developed business plans. In many cases it is also noticed that the Business Plans are prepared by CAs only for the use by the Bankers and this situation is not at all healthy and sensible from the project perspective. This can be very risky since many aspects of the fundamental need analysis, marketing strategies or the possible operational data analysis (especially about the cost data are specified without a touch of reality or cross check with field data / current data). It is admitted by some of the candidates in personal interviews that since there was absence of the business plan, there was no formal risk analysis and formal risk mitigation plans. Unfortunately no one in team also felt the need for attention to serious business plan or serious risk analysis. It may be prudent for the new era entrepreneurs to pay attention to this critical aspect before embarking on the new venture.

d) Need for Flexibility
Flexibility is required for defining scope and area of influence of the project for initial period. Flexibility is also needed at organizational level to tweak few internal rules when the situation demands, particularly for complex projects. Flexibility to alter organisational structure, decision making authority, sphere of control, accountability, etc. can help success in managing the difficult startup projects. Kelkar et al. (2015) note the need for flexibility at strategic and operational levels as a critical success factor for startup projects. Other flexibilities include change of scope, change of project team including the leader, choice of technology and partners, mode of funding, and equity structure of the project.

4.2 Company Structure in terms of equity shares / JV Partners & Challenges for Funding
a) Company structure and equity distribution
Due to paucity of funds in the initial period of struggle, the equity is often allocated in a hurry to mop up funds without due diligence. Although this looks attractive in the initiation stages it can generate 'death trap' for the unit over a period of time. Wrong choice of such equity holders, Joint Venture partners and angel funding agencies can prove be a great impediment over the
project period.

b) Choice of Partners & Executive Management
Often startups are set up by family units with pooling of money and other resources. The natural allies are relations or friends from the known circles and become equity holders for the new venture. This may be convenient to start with but over the years, and especially when the going is tough, cracks appear in the unity of the promoters. The analysis of the failed projects indicates that choice of wrong partners or the rift between the founding members can be a major source of the risk for the existence of the newly set unit. It is critical to choose the partners in business such that they complement the skills of the promoters. In case there are initial signs of lack of compatibility of values and attitudes expected it may be worthwhile to terminate the relationships.

c) Need for a 'Mentor / Senior Advisor' for the startup unit
Many of the startup units are set up by capable technical persons but they may not have adequate exposure or interest in the business and organizational issues needed for startup projects. In such cases, the entrepreneurs take decisions on ad hoc basis or critical decisions are kept pending for too long a time. This risk can be mitigated if the unit decides to appoint a 'mentor' to keep track of critical issues and guide the unit in the initial period of development. From the case studies, it is found that startup units that made efforts to seek advice from the 'mentor' finally completed the project with success.

d) Choice of funding agencies, realistic financial analysis and planning for contingencies
It was seen that many of the startup units part with certain portion of equity to the investing organizations when the new unit is facing cashflow constraints. It is also noticed that the main cause of the problem leading to cash-trap is unrealistic project plans and inadequate projections for funds required coupled with over optimistic attitudes of the entrepreneurs. Some startup owners take extreme risks and are willing to put their life time earnings and reputations on line. This foolhardiness may be motivating for the startup unit but the resulting lack of financial planning cannot be good for the startup.

4.3 Sales and Customer Relationship Challenges & need for many 'anchor customers'
Sometimes the startups are set up based on the long term promises from a large company. This is indeed a great situation for the new entrepreneurs because the market seems assured. As a long term strategy, it may not be prudent to tie all the options to a single customer as this could pose a major risk. It may be wise to ensure that right from the beginning the unit makes planned efforts to enlist support from several 'anchor' customers for the products or services.

a) Complex transactions for permissions and delays due to local factors for remote projects
It is noticed that projects which are located in the remote / mofussil locations have peculiar challenges due to interference by special interest groups. At remote locations, getting clearance for the land and other permissions such as electricity power sanctions and many other clearances from various authorities is a big bottleneck for the project teams.

b) Inconsistent and changing demands from various groups of stakeholders
Dextrous handling of stakeholder relationships is an important task, and the owner or technical person may not have inclination for such aspects. The overall success of the project needs careful handling of such issues right from the beginning. The project situations also become complicated if there are conflicting demands from various stakeholder groups. Such issues are risk traps and are generally not accounted for the budgeting exercises. Careful analysis of stakeholders (known and hidden) should help avoid such risk traps to ensure overall health and success of the projects.

c) Unprecedented challenges for clearance of pending dues (no direct correlation with deliverables)
All startup projects are cash trapped almost all the time till they reach the stage of maturity and stability of operations. Often, they adjust and tweak their offerings and policies to suit customer demands and to establish track records. This can pose a cash crunch for the newly formed unit. Customers rarely collaborate at such times (although some do). This risk is considerable and one must be alert to this risk.

4.4 Operational Challenge

a) HR Issues
Projects need multi-disciplinary personnel and this itself is a great challenge for every project manager. The selection of 'core group' is an obvious aspect for any startup. Due to shortage of funds at initial stages, compromise candidates are at times taken up on board and they may create unsolvable problems at a later stage. It is essential that, even at the cost of delays, it is better to hand pick competent persons are taken on board (even adding to costs in the initial period), since they form the foundations for success of the project. With limited availability of trained / competent leadership in local markets, and since the startup units do not have enough funds to pay competitive compensation, attracting talent is quite a challenge, obviously leading to risks. Recruiting experienced personnel for senior levels is a rather tough challenge for the startups since there is not enough funding to support such costs in the beginning. Startup projects in remote locations / mofussil locations find it difficult to attract adequate manpower for the project execution. Many organizations set up training facilities much in advance to train locally available personnel and then offer them suitable positions to solve such problems. Appropriate HR policies need to be put in place for ensuring proper training, team work and discipline, and effective communication with all stakeholders.

b) Network of reliable local suppliers
Most startup units depend heavily on the network of reliable suppliers. In remote locations it is difficult get timely support from local vendors for certain specialized skills. Startup projects may need specialised and expert contractors. Ad-hoc award of contracts and mediocre performance by critical contractors can be a serious risk. 'Due diligence' and proper legal documentation (with possible exit clause in the contract document) may help manage the situation in case of problem situations. It is also important for the startup units to develop good working relationships with key suppliers to ensure that in case of difficulties that you face they come and support your unit (even
if you are not in position to pay in time). Such relationships are crucial in the initial where cash is always in short supply.

c) Lack of control systems & availability of dependable /authentic data on the operations and technical process details. A major drawback (and significantly critical for the startups) is lack of management and project control processes right from the beginning. In most of the cases this aspect does not get due importance and is either completely missing or is lukewarm, posing a risk to the project. Inadequate or inappropriate IT structure is another problem in startups.

4.5 Social & Cultural Challenge

It is noticed that in many cases, startup organizations decide to put up the manufacturing unit in an economically backward areas where many types of concessional facilities and even tax holidays are provided for by the government authorities. It is sensible to avail these facilities especially for the startup units since they have concessions in terms of overall capital expenses and this is welcome for the startup units. However this move to backward area, also brings with it problems as well. There can be cultural mismatch and location based peculiarities. Difference in cultures certainly affect work out norms, methods of communication and developments (or otherwise) of effective relationships, camaraderie between team members, methods of influencing and thinking, difference in expectations and motivation norms. This affects working styles and output in given span of time. Additionally if the teams are 'virtual teams' then there is a possibility of very different problems that can derail otherwise well running project. Startup units need to aware about such traps if they want to be successful and should pay due attention to such soft aspects of running a new business.

5 CONCLUSIONS

Startup projects have assumed a position of significance for the overall growth of the Indian economy. In this context it is imperative that the success rate for the projects in India should improve in a significant way to ensure achievement of targets set for the economic growth in the country. This means one should be in position to identify and control the risks associated with the project environment in general and for the startup projects in particular. Management of risk has been by far one of the most neglected subjects especially for the 'startups in SME' segment in the Indian Markets. Due diligence from the stage of 'Feasibility Study' and alert watch about the effect of the changes on the concept and feasibility of the new venture may help save future losses for the entrepreneurs. Risk management is an integral part of the decision-making process and effective risk management can proactively help in overcoming the possibilities of the business failures. Our case studies indicate that in 40% of projects, no formal risk management was carried out during initiation and planning. The study undertaken and the analysis of the data compiled during the case studies and field work point out several factors that need attention while carrying out such projects, especially startup projects.

6 REFERENCES


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