

October 22, 2019

Scaling for Validation vs. Scaling for Profit

Most entrepreneurs are familiar (if only in concept) with what is sometimes called the “Wal-Mart Problem.” It’s a problem that faces a small startup when, very early in the game, it gets a huge order far beyond what it has the capacity to fill. It’s a pretty good problem to have, as far as problems go. Even as mismanaging it has been the bane of more than a few startups.

The Wal-Mart Problem can, though, be a blessing in disguise for entrepreneurs who figure out the solution. Figuring it out almost always involves a production fire drill where pretty much the entire focus is on filling the order at pretty much any cost. Scaling can be a lot of fun when you aren’t worried about COGS, just getting the product out the door. *When you are scaling to validate your opportunity, not profit from it.* Besides, raising capital to fill actual customer demand is probably the easiest venture capital shtick any entrepreneur could ever sign up for.

Unfortunately, more entrepreneurs anticipate and prepare for the Wal-Mart problem than ever actually experience it. And so, they raise capital they don’t really need (at lower valuations) to build capacity they don’t really need. If, that is, they can raise the capital at all (building capacity ahead of validation is one of the tougher venture capital shticks). It’s a classic mistake made by “premised on success” startups; startups that assume ultimate success will vindicate strategies that assumed rather than assured success.

The pre-mature scaling mistake results from an understandable but flawed perception that all scaling is the same. It isn’t. Early scaling is always more about validating your market than profiting from it. Success is proving that the dogs will eat the dog food, not that you can profit from each can of it. Sure, you have to have a path to more efficient (profitable) production (unless, I suppose, you are playing the Uber game), but you don’t have to be on it. In fact, you shouldn’t be on it to the extent that it reduces the focus and resources available for finding and feeding hungry dogs – until you have proof that dogs want what you are selling.

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The Wal-Mart problem is indeed a high-quality problem to have. But don't make the mistake of trying to solve it until you have it. Dream about it, maybe, but don't let the dream distract you from the more immediate task at hand. Finding hungry dogs, hopefully in more digestible packs.

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