

ACTIVITY 18.1

The Economic Story Behind Columbus' Expedition¹

In order to understand Christopher Columbus and his impact on history, you must first understand that Columbus was an **entrepreneur**. What is an entrepreneur? An entrepreneur is a person who has an idea for a business venture. An entrepreneur bears many of the **risks** of success and failure that are associated with starting the business. In return, entrepreneurs expect to earn profits. **Profit** is defined as income that remains after a business pays all its expenses. Entrepreneurs are important to economic growth. They help themselves and others identify new ways of doing things. They discover new resources. They innovate and advance beyond the current ways of doing things. Some economists classify entrepreneurship as one of four types of resources; natural resources, human resources, capital resources, and entrepreneurship. Columbus' "business" was his expedition, which was based on an exciting idea. He believed he could find a new trade route to the spice-rich Indies by sailing west from Europe. He was willing to accept many risks to make this journey, including the possibility of getting lost, the uncertainty of returning, starvation, etc. Before embarking, Columbus, as the entrepreneur, needed to find the resources necessary to take the trip. He needed to acquire *capital resources* such as ships and tools, and *human resources*—a crew.

In 1484, Columbus asked King John (Joao) II of Portugal to fund his venture. King John declined. Columbus then spent six years in Spain trying to convince King Ferdinand and Queen Isabella of Spain to invest in his venture. Finally, in 1492, King Ferdinand and Queen Isabella agreed to provide Columbus with three small ships, men, and supplies.

Why didn't Columbus succeed in securing private financing? Columbus needed a *royal* investor. He needed the power of the Spanish throne to defend any claims he made to the territory he discovered. Only a monarch could enforce these claims.

When entrepreneurs start new businesses, they often invest some of their own money. In Columbus' case, he invested his valuable time (nearly 10 years). Columbus asked the king and queen that he be allowed to finance one-eighth

¹ Drawn from *A Venture Capital Primer for Small Business, Financial Management Series* (Washington, DC: Small Business Administration, April 2009, http://www.sba.gov/idc/groups/public/documents/sba_homepage/pub_fn5.pdf) and *A Primer on Venture Capital* (downloaded from <http://www.vnpartners.com/primer.htm> on November 1, 2010).

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of the cost of future voyages. In return, he asked for a one-eighth share of the profits. He obviously expected to get back much more in profits than his one-eighth. Columbus also requested he be given the title Admiral of the Ocean and Governor-General, titles offering power and prestige.

VENTURE CAPITALISTS

Sometimes entrepreneurs cannot cover all of their expenses and start-up costs by themselves. Often entrepreneurs look to others for help. **Venture capitalists** provide financial resources to start-up companies that they believe have a high potential for success. Venture capitalists (VCs) make money by owning part of the companies they invest in. Many of these new businesses are selling a new technology in fields such as biotechnology or computer software. Because VCs invest in risky ventures, they do not expect that they will earn a positive profit every time. To compensate for the possibility of failure and the loss of their initial investments, VCs often expect a large share of the profits from the start-up company. Many VCs help manage such companies. When King Ferdinand and Queen Isabella agreed to fund Columbus, they fulfilled the role of venture capitalists. They were funding an untested technology: sailing west to China. They expected a great return on their investment: nearly 90 percent of the profits would go to Spain!

QUESTIONS:

1. What were some of the risks Columbus was willing to take?
2. What is profit? What kind of share of the profits did Columbus expect?
3. How was Queen Isabella and Spain's investment in Columbus like an investment by a venture capitalist today? What was new about Columbus' venture?