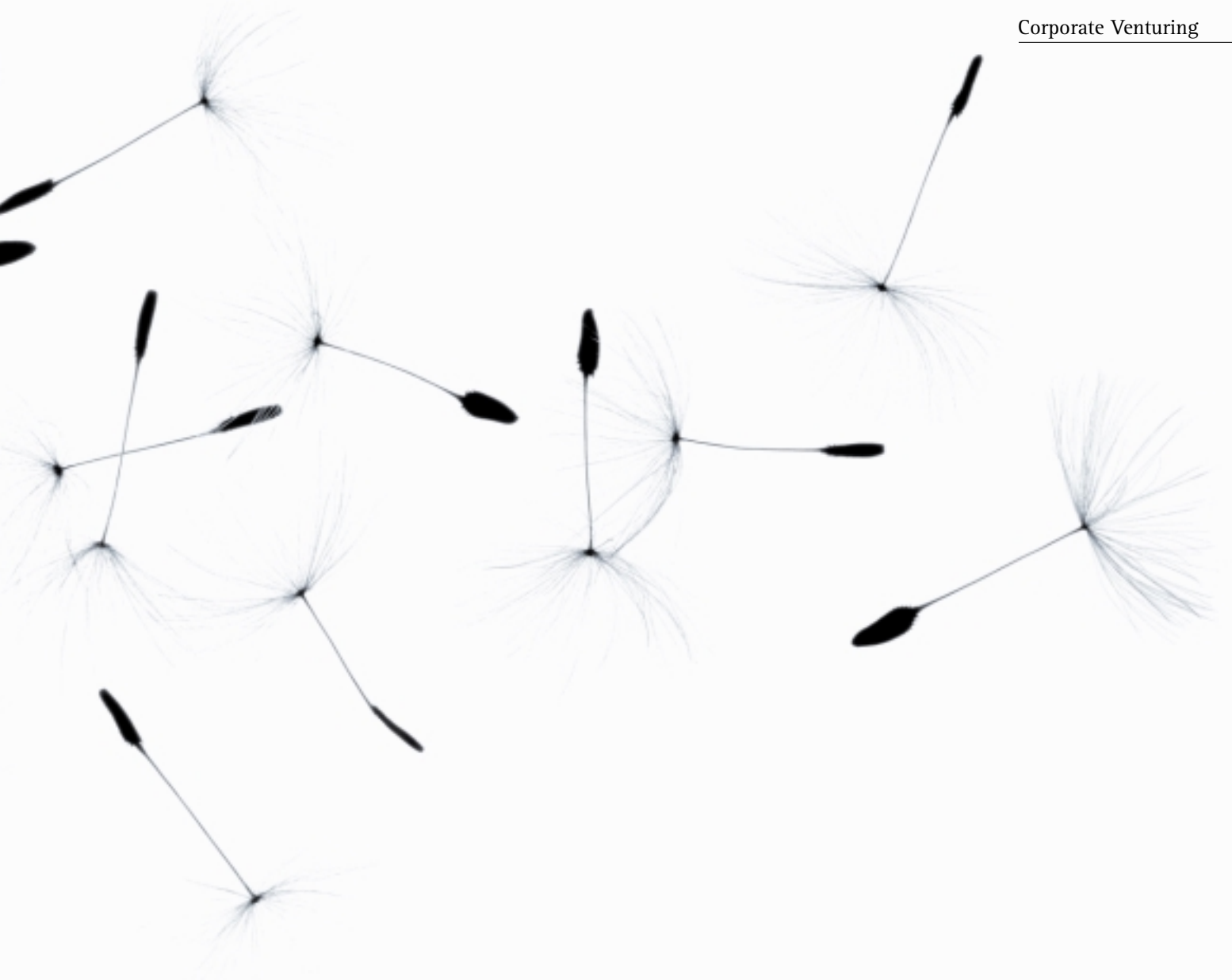




Corporate venturing

By Lawrence B. Leisure, John D. Bolze and Matthew A. Haley



without the tears

It's all the rage, but it's not for the fainthearted. More than a few companies have spent tens of millions of dollars on new ventures only to find that the market has passed them by—or wasn't really moving their way in the first place. The solution: Put the disciplined techniques of the venture capitalist to work in a corporate setting.



We expect venture capitalists and entrepreneurs to build new businesses. But should major corporations be expected to do likewise?

A growing number of companies are saying yes. The corporate venturing wave has gained momentum in recent years, driven by the changes in the new economy and inspired by the success of such well-known examples as Intel Capital. The number of corporate venture capital funds in the world grew from 70 in 1997 to 325 in 2000, with US investments totaling nearly \$19 billion. Many other corporations have entered the game via joint ventures or internal incubators.

Indeed, with seemingly everyone from natural resources companies to telecom providers launching ventures of one kind or another, a simple definition of corporate venturing is a challenge. But we know it when we see it—and we're seeing more and more of it.

Method and motivation

Approaches and participants vary, as do the reasons companies embark on ventures in the first place. Most common is the desire for growth and value creation—by boosting demand for existing products or by creating new products, a new business unit or even a new core business. Other companies seek to make money by putting underutilized intellectual property to work, using their market channels for additional purposes or otherwise leveraging corporate assets.

Sponsors of business-to-business exchanges want to save money by making their supply chains more efficient. Still others act for competitive

reasons: If they don't offer their customers the newest thing, they reason, somebody else surely will. Rounding out the list of motivations is the quest for heftier returns on free cash.

All good reasons, to be sure; and, for the most part, these strategies are reasonable. Yet too many corporate ventures disappoint.

Historically there has been a large gap between the strongest and weakest performers. In 1999, for example, the best corporate venturing program returned more than 400 percent while the worst had a negative return exceeding 30 percent. And more than a few internal projects have absorbed tens of millions of dollars only to find that the market has passed them by—or wasn't really moving their way in the first place.

It turns out that a major, unintended byproduct of the myriad motivations and methods associated with corporate venturing is a large number of ill-considered decisions. Corporations may overfund their new ventures, fail to align the ventures' objectives with those of the parent company, allow ownership and control issues to get tangled, make the wrong alliances or commit any number of other missteps.

In addition, corporate financial objectives—particularly the desire to minimize the initial impact of the venture on the parent's P&L—may lead to decisions that are completely wrong for the new business, ultimately hurting both the venture and the P&L. Throw in rapidly changing marketplaces, and the hurdles can be pretty formidable.

These challenges are difficult, but not insurmountable. In the course of helping to launch some 350 ventures at Accenture Business Launch Centres

around the world, we have encountered most of these difficulties firsthand. And we have something (in addition to a few scars) to show for it: a thoughtful framework for managing the corporate venturing program (see chart, below).

Staged, disciplined and speedy

The framework brings the staged, disciplined yet speedy approach of the venture capitalist to the corporate setting. It offers specific guidelines on what to do when—from testing an idea with potential customers to forging alliances to hiring full-time managers and building and scaling the new entity. Within this framework, fresh rounds of funding are committed only as new ventures reach clear milestones; an important part of the approach is efficiently testing and filtering out the ideas that don't work—letting them “fail fast and fail cheap.”

Based on experiences with companies as diverse as a major UK

financial organization, a global consumer products manufacturer and a US technology company, we have found the framework to be broadly applicable, either as a template for setting up a new corporate venturing program or as a model for assessing an existing one. Since the framework's usefulness has much to do with its specificity, it's too detailed to present in its entirety here. But an overview can capture its spirit.

The corporate venturing framework is divided into two distinct stages. In the first stage, the corporate venturing program itself is set up. The second stage is an iterative process for identifying ideas and then building, launching and scaling the best ones. These two stages, in turn, are subdivided into a total of seven phases, each with specific entry and exit criteria.

Why the two-staged approach? A corporation may or may not want to venture on a large scale; one

chemicals company we have worked with generated hundreds of ideas, winnowed those down to a dozen, and then moved a handful into development. But whether the goal is to build a large venture factory or a much smaller operation, the place to begin is with some fundamental principles.

Stage 1: Setting up the corporate venturing program

The beginning stage is a relatively simple yet crucial setup process that lays the groundwork for all subsequent venturing. It has three phases.

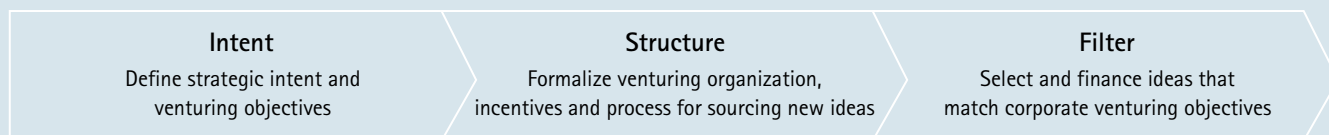
Intent

The key question in this initial phase is the obvious one: What is the company trying to achieve through corporate venturing, and is the objective aligned with overall corporate strategy? Those answers are closely linked to another fundamental question: Do the company's top

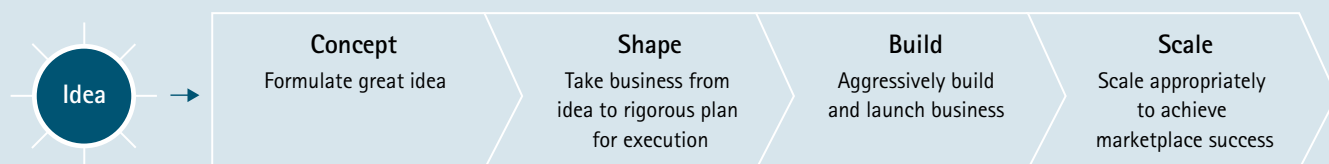
A corporate venturing framework

To launch ventures, a corporation must first go through a one-time setup to establish the strategic goals as well as the ground rules. For each new venture, the company must go through a four-step process to take it from an initial idea to a marketplace success.

One-time setup



Launch of any new venture



SOURCE: ACCENTURE ANALYSIS

Seeking outside expert help may provide huge advantages and lead to a more successful venturing program.

executives support the venturing program?

One of our clients has embraced venturing mainly as a way of accelerating innovation inside the parent company. A consumer products company, on the other hand, has a cupboard full of intellectual property whose value it wants to determine—the better to sell it or, perhaps, trade it for a stake in a new venture.

In each case, the intent is clear, management has signed on, and other fundamental questions—How much money is available? What kinds of partners and ownership structures are acceptable? What kinds of exit strategies are attractive?—have been asked and answered.

The intent phase is also the time for another important bit of corporate self-analysis. What can the company contribute to new ventures? For Global 1000 companies, the answer is often much broader than might be expected. Along with cash, intellectual property and employee skills, corporations find they can reap additional value from such assets as their distribution channels, their brand or, in the case of one chemicals company, its position as one of the world's major currency traders.

Another consideration during this phase is whether or not to bring in outside help. Starting businesses is often neither the expertise nor the focus of the typical management team within a corporation. Seeking expert help in identifying underused assets and capabilities, understanding all the funding options, and building, launching and scaling the new business may provide huge advantages—and lead to a more successful venturing program.

How the new businesses will be funded is a key consideration. Many corporations are beginning to turn to venture capitalists to fund their new ventures. Keep in mind, however, that venture capitalists are interested in ideas that offer them a significant opportunity to get a high return on their investment; therefore, these ideas must include an exit strategy for liquidation. Corporate ventures may have a different (but no less important) objective than highly extractable short-term returns.

Structure

Let's assume you're a month into the setup of the corporate venturing program, have a modest budget (say, \$200,000 to \$300,000) and are ready to nail down some more details about how the company will approach venturing. The most important questions in this stage address issues of governance, both internal and external. How will conflicts between the parent and the new venture be resolved? What level of control will the parent company have over the new venture?

The corporation also has a wide range of options for determining how to filter and fund ideas—everything from a strict venture capital approach all the way to being just a strategic investor. We will focus on the more hands-on approach of managing your own corporate venturing program and building, launching and scaling organic businesses.

Inside the company, you should determine the roles, responsibilities and rewards of the people who will be managing the venture program. Outside the company, the goal is to get more specific about the structure

of the alliances identified as appropriate during the intent phase.

For example, the Norwegian telephone company Telenor is rolling out Djice, a global wireless Internet service provider, as an independent new entity under a separate brand. To build an international presence and brand quickly, Djice is establishing a global network of alliances with independent service providers; by contributing to this network, the alliance partners will reap the benefits from being part of an international network.

Lines of control and authority are set up in this phase. What's the sign-off process for spending money? Exactly how will ideas be judged? How will the rest of the company work with the venturing team? We recommend a standardized approach; it's more efficient for managers and healthier for the ventures, too, since a quick "no" is better than a slow "maybe."

Clarity is important: The leaders of the venture program will be more successful if their performance metrics and incentive structure are closely aligned with the strategic intent of the company. There should be only one review board for the program.

Filter

At this point, key venturing management and processes are ready. Now it's time to open the idea pipeline and evaluate what you're getting. Sources of new ideas—ranging from internal workshops to outside consultants, venture capitalists or smaller companies—have been alerted and informed of your criteria. The goal is to take a large volume of high-quality ideas and quickly funnel them down to the few that have real business potential and strategic fit.

In this phase there's an important balance to be struck between making sure you get ideas that are grounded in the business and aligned with the overall corporate strategy, and assuring an adequate flow of creative thinking.

Experienced, respected managers from within the existing business should drive the filtering process—with open minds. This isn't the stage at which to reject ideas because of considerations that may be secondary, such as whether they would require external support or funding. The most important criteria here are the idea's potential and its strategic fit.

Objective external help in filtering ideas is often extremely useful. Clearly, venture capitalists excel at this kind of assessment—and even they historically have leveraged outside expertise to augment their due diligence. As mentioned earlier, some prominent venture capitalists are now taking roles in corporate venturing programs. Their expertise and contacts are obviously valuable in later stages too.

Stage 2: Pursuing the best ideas and launching ventures

Sometime around month five, the venturing unit should be ready to move to Stage 2 and to focus on the actual launch of one (or more) of the ideas that made it through the filtering phase. You're now moving rapidly from the realm of planning into the hard realities of the business and the market. This transition consists of four phases.

Concept

Time to draw up the initial business model, in the form of a five- to seven-page concept document. The topics covered: what problems the

venture will solve for customers, the venture's projected path to profitability and the competitive landscape in which it will operate. One important consideration here is the stature of the launch customers. Ideally, they'll be among the most respected in the targeted business sector.


A launch in progress from Network Solutions, Inc. met that test and several others as well. Seeking to leverage NSI's position as the registry for domain names and its subsequent capabilities in routing and storing them, the company considered how cumbersome conventional domain names can be for users of Web-enabled mobile phones and other wireless devices. Could there be a business in providing telephone-number domain names?

About a month of internal study gave the team an idea of what it would take to develop such a product. Then they went to a major airline, large wireless carriers and other potential customers to gauge their interest. The response was enthusiastic—and qualified the NSI venture, now known as WebNum, to move to the next stage and an initial round of funding.

For NSI—and for any other corporate venturer—that initial identification of a real customer problem is an absolute must if a venture is to go forward.

Shape

Now comes the work of taking an idea with some preliminary testing and analysis behind it and transforming it into a rigorous plan for execution—with clear proof that customers are willing to purchase the product or services. The point is not to create an infrastructure to satisfy the demand;



Regardless of the situation, it is important to have a credible independent management team for the new venture.

that comes in the next stage, after you prove the demand exists.

Major activities in this phase are piloting, prototyping and lining up some committed customers. Yes, you should be looking ahead to key infrastructure and staffing decisions—but you do not want to commit the resources prematurely or assume you have identified all the potential problems during the concept phase.

A good example of the shaping process is the work that went into developing an e-procurement offering for a joint venture with a leading financial services company in the United Kingdom.

The company wanted to extend value to existing customers, generate new sources of revenue and attract new customers. A portal was designed that would host a range of business services (including an e-procurement service) aimed at improving efficiency, reducing costs and helping customers be more competitive.

The company knew the potential customers well and understood their needs; it has financial relationships with a healthy percentage of the country's businesses. It also knew that these companies have core relationships with providers of other services such as communications and accounting, and it had good reason to believe that customers would be interested in a portal that combined such offerings.

What the business didn't know was just how the combination should work and what customers' priorities would be in such a setting. A hosted e-procurement pilot that targeted a small number of key customers helped to answer these questions, shape the business model (including pricing and required service levels) and pave the way for a successful commercial launch.

The e-procurement pilot program highlighted implementation challenges and added to the company's credibility with customers when building and launching the full commercial service. In addition to invaluable customer feedback, from a public relations perspective the new venture could quote customers that had already seen real business benefits.

During the shape phase, the venture moves from an internal project-based entity to a true operating entity. As a company isn't simply a set of ongoing projects with deliverables but rather an ongoing business meeting standard metrics such as sales, revenue, expense, head count and capital budgeting. The same thinking should apply to the new venture. This requires a fundamental shift in managerial approach and skills throughout the venture.

Build

The venture has come a long way. It's now in about the eighth month of the launch stage, and it has secured a second round of funding, probably between \$15 million and \$35 million. Yet the dangers it faces are considerable. The focus now should be on actually building a profit-producing enterprise. All the balls are in the air: Alliances are being formed, new customers are being signed up, a robust infrastructure is being developed, and the first product or service offering is being built and delivered.

And in almost every case, a new management team is being put in place during this phase. If you're seeking outside funding from a venture capital firm, the top management team must be in place to secure the second round of funding. The decision to bring in a new management team is related both to the business-building skills of the

existing team and to the corporation's intent for the venture.

Regardless of the situation, it is important to have a credible independent management team for the new venture—ideally, individuals with startup experience. Now is not the time to ask people with other responsibilities to manage the new business on a part-time basis.

In either case, it will pay to hire from the top down. It takes longer, but this phase abounds in directional decisions that have to come from the top. And potential senior executives want to assemble their own teams rather than inherit someone else's.

Another big-picture issue that arises during the build phase—or ought to—is making sure that the alliance agreements the venture is striking have clear exit strategies. One way or another (whether through success, failure or old age), most alliances terminate. In a similar vein, knowing the value of the new venture and the industry model for mergers is critical.

Of course, none of these concerns should be allowed to detract from the single overriding goal of the phase: producing something salable.

Scale

With an alliance network in place and marketing momentum behind it, and with robust business capabilities, a good sales pipeline and its primary product successfully launched in at least one market, the venture has earned another round of funding—and the right to think really big. The goal here is to extend the business into new customer segments, channels and geographies.

For many ventures, this is the time to begin an international expansion

or an expansion into an additional market segment. But the wisest ones first make sure they have achieved some local success—especially with advanced users.

With or without an international agenda, the idea is to build on a firm foundation. Key elements: a budget that's at least 20 percent funded by cash flows from sales, and an outsourcing strategy that helps the venture focus on its core competency. Management may also be reviewed and restructured in this phase, with an emphasis on operational skills and, where needed, international experience.

When the venture graduates from this phase, it is a self-sustaining, profitable business.

And that's the corporate venturing framework, or at least a scaled-down version of it. Experienced corporate venturers will no doubt notice parallels between our approach and theirs. Other companies may find the greatest value by drilling down for specifics in a particular phase, such as alliance building during the structure phase.

Our intent is not to offer a universal formula for corporate venturing but to codify and share some lessons we've learned—with the emphasis squarely on the disciplined techniques of venture capitalists who put money on the line. As we can attest to from experience, corporate ventures can be challenging—but also extremely rewarding. ■

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