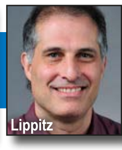
COMMENT

Selecting corporate venturing approaches

Scott Bowman and Peter Bryant, managing partners, and Michael Lippitz, principal, Clareo



Readers of Global Corporate Venturing are familiar with the rapid expansion and diversification of corporate venturing approaches. Companies have gone beyond sourcing innovation from suppliers and customers and investing in startups. Today, they are standing up accelerators and incubators, hosting hackathons and experimenting with equity crowdfunding, among other things.

This article reviews the recent evolution of corporate venturing approaches and provides guidance on which ones might be right for your situation.

In the early years of corporate venturing, companies tended to focus on accessing global technology. Companies in science-based industries such as electronics, telecoms, pharmaceuticals and chemicals were the primary players, along with a few large conglomerates seeking diversification and financial returns. With the boom in internet investment in the 1990s, a broader range of companies formed venturing units and invited small companies and inventors to submit ideas. There was also a rapid expansion of corporate entrepreneurship – the engagement and facilitation of internal corporate capabilities and entrepreneurial employees to enter new business areas, often in conjunction with externals.

By the mid-2000s, when the dust had settled from the tech-driven market crash of 2001, the disruptive potential of digital and information technologies became clear. Nimble online companies upended bookstores, newspapers, music labels, movie studios and others. Soon, companies that previously felt insulated by the large capital infrastructures or regulatory barriers – transportation, hotels, utilities, logistics – were under attack from companies that owned no assets, while startups went after lucrative niches of their value chains. FedEx today has to worry less about UPS than the dozens of small companies moving in to streamline and create new offerings in different parts of its value chain.

In their 2010 book The Global Brain, Satish Nambisan and Mohan Sawhney captured the current focus of corporate venturing. "A company can only be as innovative as the collective capacity of the people who make up its ecosystem." Competitiveness today increasingly derives from connecting to and orchestrating sources of information, building and maintaining reciprocal interdependent relationships with companies that have superior engagement with customers. Even erstwhile competitors have created multi-corporate venture capital portfolios aimed at collectively fostering an innovation ecosystem from which all can benefit. How do you decide which approach is the best fit for your company?

Corporate venturing approaches and options

One-size-fits-all is never appropriate for innovation, and corporate venturing is no different. Many executives aspire to innovate like Apple or Google, but few companies can or should. The table below summarises contemporary corporate venturing methods and different approaches within each method.

OBJECTIVE	APPROACHES
SOURCE OR CO-CREATE innovations for known problems or challenges	OPEN/COLLABORATIVE INNOVATION METHODS Go out to the crowd – challenge, hackathon, online IP market Bring the crowd in – embed with your teams Join entrepreneurs – embed yourself with them
GENERATE BUSINESS CONCEPTS around a core thesis	ACCELERATOR External – eg, hire TechStars Internal – host your own accelerator
FOSTER NEW BUSINESS CREATION around themes	INCUBATOR Join independent incubator Host incubator
PARTNER VCs OR ENTREPRENEURS to create custom new businesses focused on a particular challenge	STRATEGIC PARTNERSHIP (Alliance or JV with aligned firm) DESIGNER STARTUP
INVEST IN EXISTING STARTUP BUSINESSES in strategic focus areas, to create optionality	CORPORATE VENTURE CAPITAL Limited partner in a VC fund Equity crowdfunding Dedicated fund Multicorporate fund

The terms accelerator and incubator are sometimes used interchangeably. For our purposes, an accelerator is a discovery-oriented fast structured process for developing an initial business case and validation of market attractiveness. Incubators focus on helping early to mid-stage companies gain early traction, validating their solutions and proving out a revenue model on the path to scaling and commercialisation.

We find a five Cs framework useful for thinking about which corporate venturing approaches are appropriate for a particular organisation, and then for taking action – clarify, connect, commit, configure and collaborate.

Clarify strategic objectives

Strategic objectives should drive the choice of external venturing models, as they express the mandate that the venture group is empowered to solve. The choice of objectives affects the level of connectivity required to the core business, degree of autonomy in decision-making, type and level of resources required and very often the funding structure. While objectives such as the examples below are not mutually exclusive, at the outset external venturing groups must seek to establish and build alignment with executive leadership around what the primary objective is for the group.

Build new business options beyond the core. Castrol InnoVentures is mandated to build new offerings and businesses beyond lubricants. Merck Global Health is focused on building new growth horizons beyond the pill. These types of effort typically require dedicated capital and independent structures and processes, as well as the ability to leverage key capabilities or cross-pollinate new ideas or thinking with the core business.

Extend and add value to the current core business, with new products, services or solutions. Caterpillar Ventures is focused on technologies and business models that generate value on top of a robust core business and extend it into new territories. For instance, YardClub helps customers maximise the use and productivity of their owned equipment through an online peer-to-peer equipment rental program, and is extending into data management. Cat Ventures has dedicated capital but maintains a nimble structure and collaborates with internal and external stakeholders to identify, prioritise, pilot and scale new solutions.

Transform existing businesses through partnerships with the startup community. BP's office of the chief technology officer scans internally for high-value business problems and acts as a network builder and bridge to external solutions in the technology and venture world. The organisation relies largely on funding from within the business units – it maintains a small team and budget – acting as an advocate of transformational change.

Some firms enter the venturing game but lack a clear sense of how they support the innovation agenda of the firm

Connect with the firm's innovation agenda

External venturing is a means to an end. Some firms enter the venturing game because it is fashionable, or because of executive fiat, but lack a clear sense of how they support the innovation agenda of the firm. This connection is vital to having staying power. We think about this connection in terms of two dimensions:

Nature of the challenge – innovation strategy. As noted in the previous section, a new venture group should have clear connection to the strategic aspiration of the company, with strong alignment at the C-level of the company. For instance, Humana Health Ventures is helping extend Humana's 2020 bold goal; BMW i Ventures is highly aligned with the corporate vision to shape global mobility.

Scope of the challenge – innovation scope. Clarifying the scope of the challenge the organisation has a mandate to solve through venturing helps influence the type of model that may be appropriate:

Existing known challenges around a central thesis can benefit from deliberate and structured collaboration with the startup community. There are multiple variants with different degrees of customisation, including:

- **Designer startups:** Custom-creating businesses around known challenges emanating from a single firm as lead client, as Frost Data Capital does.
- **Incubators:** Creating an environment for co-creating, design and testing new concepts onsite, pairing experts from the business with entrepreneurs, as BMW does with its Startup Garage and venture client model.
- **Accelerators:** Engaging in structured new concept and new business creation around core themes, such as Unilever Foundry and Disney Accelerator.
- **Going out to the crowd:** Using challenges, hackathons or crowdfunding campaigns to generate new ideas from outside, such as Whirlpool's use of Kickstarter to create the Zera food recycler.
- **Bringing the crowd inside:** Bringing entrepreneurs in and pairing them with company experts to solve complex needs, like JPMorgan's In-Residence Program.
- **Setting up shop with entrepreneurs:** Freshii has set up a retail fast casual store and test kitchen inside 1871, one of the largest incubators, to build direct connections with consumer-entrepreneurs and cultivate new ways of addressing challenges in its core restaurant operations.

Emergent challenges that may seem intractable to the industry require collaborating broadly with multiple stakeholders:

- Multi-corporate funds explicitly designed to engage players from broad range of areas, such as Chrysalix, the energy fund, and Cultivian-Sandbox, which is focused on driving transformational approaches in food and agriculture.
- Organising grand challenges – Daru Darukhanavala, the former chief technology officer of BP, set up a grand challenge of pipe alignment in oil wells, a $1bn problem. A solution emerged from an unexpected place, based on an analogue of installing medical stents.
- Designer startups – in this case corporations lead the custom-creation of a startup to address known challenges.

It has been said that if you always look in the same places, you are likely to find the same answers. This axiom is what drives external corporate venturing generally, but is especially true of situations in which venture groups are seeking to address emergent challenges.

When is corporate venture capital right for you?

Much of venturing is built on the idea that capital is a ticket to the dance. This is not necessarily the case. Indeed, corporate venture capital models abound – well over $5bn in VC dollars is invested each year and over a quarter of all VC deals have corporate money in them. However, many firms have found that they gain tremendous value by simply having a robust partnering approach, not necessarily having a dedicated pool of capital or fund structure. Several models mentioned in this article do not involve CVC funds. That said, often it does make sense to set up a fund structure when the following factors are present:

- When seeking to access existing businesses, not just ideas or entrepreneurial talent.
- When seeking to gain much broader access and visibility.
- When the pace of innovation is rapid and discontinuous.
- When the locus of innovation cannot be the firm.
- When the venture capital ecosystem is robust and well-established.

CVC funds can be managed internally by dedicating a pool of capital or committing funds over a defined period, and hiring the requisite talent to run the fund. Most CVC funds operate this way. In cases where the firm does not want to stand up a fund, an outsourcing model can be pursued, and new business models are emerging that address the desire some have for externally managed CVC funds. These funds can either invest directly in startups or, increasingly, are investing in venture funds as a limited partner (LP), where those funds align well to their strategic areas of interest.

Once the model has been chosen, the remaining three Cs influence the success of the model.

Commit to the model and have a strategy

Before entering the corporate venture capital arena, a company must be willing to commit sufficient capital and demonstrate staying power

There is a difference between having a strategy and being strategic. The latter is necessary but not sufficient. To succeed in the external venturing world, a firm must have a venture strategy, venture framework, a defined approach to its ecosystem and an aligned structure and governance model that is optimised for venturing. The group must be able to establish – and, critically, maintain – solid leadership commitment at the CEO level, coupled with a strong value proposition that goes beyond capital.

Before entering the corporate venture capital arena, a company must be willing to commit sufficient capital and demonstrate staying power. Shared ownership, commitment and strategic view internally are essential for the company to be steadfast through business and venturing cycles, taking time to ascend the learning curve and build reputation.

Finally, new kinds of internal structures and processes are usually required for a large company to interact effectively with startups – particularly making decisions quickly. It is also important for the company to have structures in place to scale successful startup engagements and capture value.

Configure the structure and organisation for speed

Corporations are typically not set up to operate at startup speed. They have various process and timing mismatches with startups. Their structure and processes must be revamped and optimised for speed, exploiting optionality, investigate and learn approaches and validated learning. They also need nimble organisation structures and approval processes.

Collaborate with customers and partners to accelerate value creation

Collaborative innovation is key to harvesting strategic returns from external venturing. Startups often lack access to customers and markets. Matching the speed, resilience and creativity of startups with the brands, capabilities and access of established organisations can create powerful combinations.

Where is all this going?

We see the next horizon of external innovation involving not merely a single approach, but an integration of approaches around a central strategy for the market. For instance, Citi Ventures has adopted what we refer to as an ecosystem innovation approach, in which it is developing and integrating a portfolio of methods as part of a more holistic strategy for engaging its ecosystem.

Citi's ecosystem of approaches – innovation labs, strategic partnerships and open innovation, futures research, accelerator programs – are all supported by Citi Ventures' CVC fund and aligned with Citi's strategic mission to conceive, launch and scale new initiatives that transform the future of financial services. It focuses on areas such as commerce and payments, data analytics and machine learning, and marketing and customer experience.

Integrating multiple methods as part of a more holistic approach to engaging and cultivating ecosystems is a trend we see continuing. It represents an evolution in engagement from one-to-one to one-to-many, and an evolution from orchestrating relationships to orchestrating networks of relationships. Corporate venturing is here to stay. Winners will be those that embrace change and disruption happening in the startup world around them, and accelerate innovation from the outside in as well as from inside out, and do so in a thoughtful manner. ◆