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Corporate Innovation through Venture Building

This research was prepared by Alessandro Rampazzo (MBA class of December 2020), under the supervision of Prof. Claudia Zeisberger, Academic Director of Global Private Equity Initiative (GPEI) and Professor of Entrepreneurship at INSEAD, with the collaboration of Arnold Egg, Joachim Vandaele, Toi Ngee Tan and Ziv Ragowsky, founding partners of Wright Partners.

Introduction from Wright Partners

Wright Partners was set up by 4 co-founders who have had experience building ventures out ‘in the wild,’ as well as jointly with Corporates. Throughout this journey, we have discovered that the market has varying ideas on

1. What venture building means, and
2. How to align the disparate goals within venture building

As much as we want to gain a better understanding of the market perspective on venture building, we also recognise the importance of communicating venture building ideas with our clients. Wright Partners was at the start of its days when we began engaging with Alessandro and his research on venture building. We think that his work is an excellent primer in describing both the journey of our company as well as the complex ecosystem we are currently engaging with.

Corporate Needs for Innovation

Over the last few decades, corporations that failed to innovate have been consistently disrupted by new entrants (or, existing players) which have successfully embraced innovation as part of their strategic agenda. Out of the multitude of cases in recent history, two of them have clearly exemplified the consequences of lagging in the innovation race.

Blockbuster vs Netflix

Netflix originally operated as a mail DVD rental service, offering a service that was not dissimilar from Blockbuster. At its peak, Blockbuster could count on their 9,000 physical stores worldwide with a customer base reaching an order of magnitude higher than Netflix. Since then Netflix has repositioned itself as the leader in the digital streaming business—successfully innovating and disrupting its own business as well as those of its competitors. On the other hand, new generations nowadays do not even know what Blockbuster was anymore.

Navteq vs Waze

Navteq was a navigation and road mapping company valued at USD8.1 billion when it was acquired by Nokia in 2017. Its technology was built on their road sensors installed across 13 countries—

covering a quarter million miles. The infrastructure cost and the consequent economic barrier to entry made Navteq the monopolist of this market for many years. In 2007, Waze entered the market leveraging GPS installed in its users handsets to collect traffic information. This strategy allowed Waze to scale at an unthinkable pace with no additional costs. Within 5 years Waze became one of the most adopted navigation apps and was acquired by Google for USD1 billion. Meanwhile, Navteq was acquired by Microsoft as part of Nokia at a fraction of its 2017 value.



Exhibit 1

The two examples bear important reminders that:

1. Companies often get too comfortable with their core businesses (e.g., Blockbuster wanted to be the best at acquiring content and distributing them through stores while Navteq was steadfast with their road sensors)
2. The focus on existing core businesses render them unable to anticipate the innovations and new technology that can pose as potential disruptions targeting their very own core businesses
3. These companies are, at times, unable to fend off competitors as they struggle to disrupt themselves—in both of the aforementioned cases, the two companies have since disappeared

While many companies claim that they do innovate, they are often constrained by the existing focus on their core businesses. This limits their opportunity to challenge and disrupt the very core they seek to protect. Henceforth, this report will focus on what Corporates can expect when they seek to do just that.

Corporate Innovation Strategies

Once a company, or the Corporate, acknowledges the need to innovate, they must decide where to direct their efforts and assets in the pursuit of innovation. Key factors to this decision are the amount of risk they are willing to bear and the potential of the market they are operating in versus other markets. Depending on the two factors, the Corporate can pursue different innovation strategies such as Market Expansion, Market Entry, Product or Business Model Innovation, Market Innovation, and Venturing (see Exhibit 2).

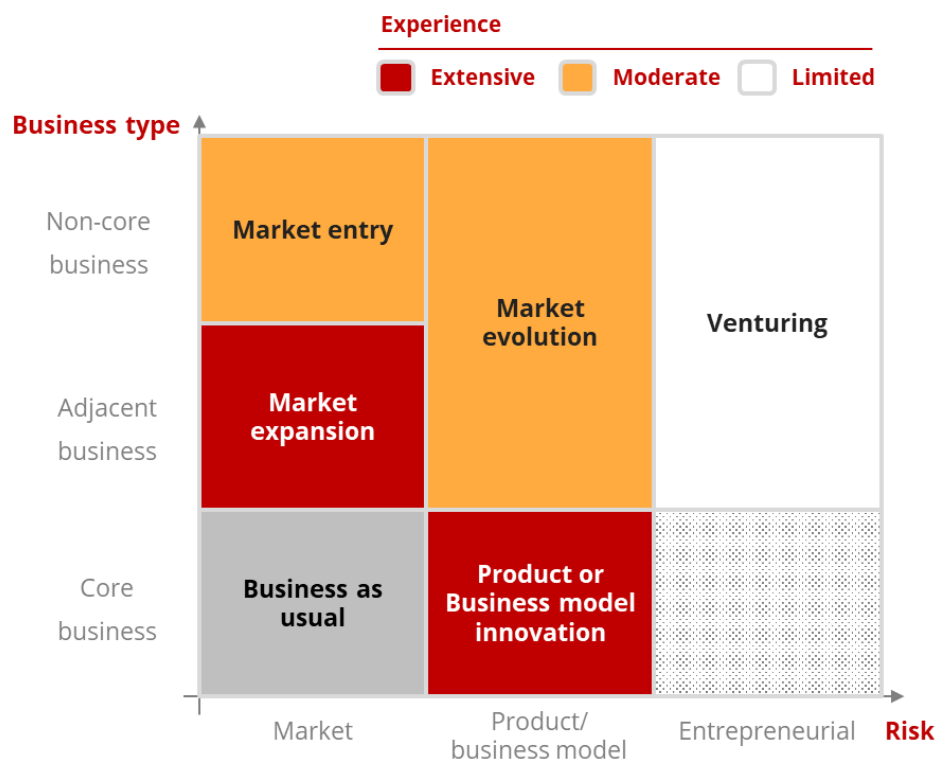


Exhibit 2

Market expansion

A Corporate entering into an adjacent business that is dictated by the rules of the existing market. This type of innovation comes with no disruption to either the existing products or the business model the Corporate currently subscribes to. It requires limited effort for the Corporate and exposes it just to the risk of the new market. It is a winning strategic move in cases where adjacent businesses are growing rapidly without presence of consolidated players.

Market entry

A Corporate operating in a stagnating business with no viable adjacent alternatives usually decides to enter a non-core business. To minimize its risk in doing so, they may adopt a similar product and business model of the ones already existing in the established business. By doing so, it will only bear risks associated with the new market.

Product or business model innovation

Creation of a new product or business model within the same type of business the Corporate has been operating into. This type of innovation is suitable to increase market share or to respond to competitors moves in the core business. It does not provide any business diversification to the Corporate and instead, exposes it to the risks associated with the particular new product or business model innovation.

Market evolution

A Corporate deciding to enter a new market with either an innovative product or business model will likely cause an evolution within the market itself. This innovation strategy typically has a higher upside than Market Expansion or Market Entry, as the Corporate is placed in a dominant position to benefit from the market evolution compared to the incumbents.

However the 4 innovation strategies described above may not protect the company from potential disruption—as compared to Venturing.

Venturing

Creation of a separate entity—detached from the parent company— which operates in a non-core or adjacent business with an innovative product or business model. This approach eliminates all constraints arising from the existing structure, business, and politics of the parent company. Thus, maximizing the potential magnitude of innovation. However, it exposes the Corporate to a higher risk level compared to the previous alternatives as the creation of a new venture usually requires dealing with a multitude of issues such as market choice, product definition, business model, team set-up and search of required resources. Managing these risks will affect the success, or failure, of the venture.

Corporates have different degrees of experience in the different types of innovation strategies based on their history. Most corporates are generally more experienced in less radical and less risky types of innovation strategies, having extremely limited to no experience in Venturing as shown in

Exhibit 2. Due to this factor, when it comes to Venturing, Corporates usually look for a partner to increase their probability of success.

Archetypes of Corporate Venture Partners

Over the last years, many players have offered different types of Venturing support for the market with varying value propositions. To better understand their offerings, it is useful to group them into six archetypes and to map them against two key factors—strategic alignment and incentive alignment (see Exhibit 3).

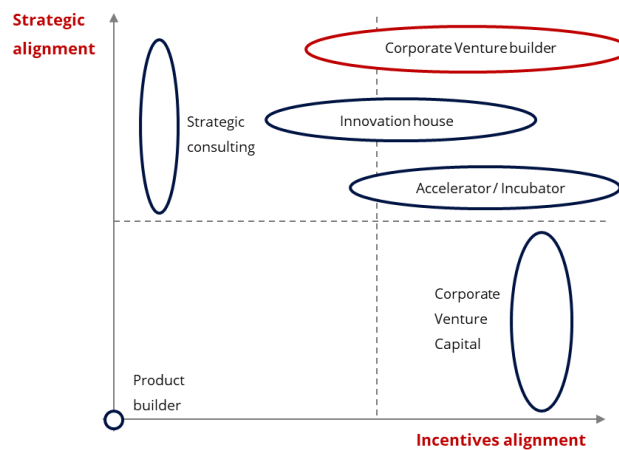


Exhibit 3

Strategic alignment refers to how the objectives of a Venture Partner are aligned with the strategic agenda of the Corporates. On the other hand, incentives alignment refers to the extent of which the remuneration for the Venture Partner depends on the success of the venture itself. Exhibit 3 shows the value proposition of different Venture Partner archetypes against the two aforementioned factors.

Product Builder

Companies like Ming Labs or Moonraft support their clients in developing end-to-end digital products, including in product design, development and project management. Typically they work on a specific mandate and have no influence or relation with the strategic agenda of the Corporate

client. Similarly, their compensation fee is solely based on the scope of work and does not include any success-based incentive scheme.

Strategic Consulting

Traditional strategic consulting firms such as BCG and OW, among others, have entered the segment of Venture building. Their approach to this new segment is mostly derived from the standard consulting approach with deep involvement in strategic alignment and limited implementation capabilities. Their services are typically compensated through fee-based schemes, with the possibility of having success-based incentive schemes.

Corporate Venture Capital

Corporate Venture Capital (CVC) is uniquely positioned compared to the other players in the market as their support is mostly focused in identifying and investing into or acquiring existing ventures at different stages. CVCs mainly pursue financial returns rather than the strategic intents of the parent company. At times, they may contribute to create strategic advantage through acquisitions.

Accelerator/ incubator

Accelerators/ incubators usually provide a twofold service. First, they provide access for Corporates to the portfolio of Ventures they have accelerated or incubated which are aligned to the strategic fit defined by the Corporates. As an alternative service, they may also offer ad-hoc acceleration or incubation programs sponsored by the Corporates with a specific intent of creating Ventures which could generate a strategic advantage for the Corporates.

Innovation House

Innovation houses set up venture teams and provide them guidance to design and develop new ventures. Their support can begin from the discovery phase or they may also enter the game once the Venture's value proposition is defined. Innovation houses usually have their own pool of founders and entrepreneurs to deploy for Ventures. They usually do not support Ventures with product building capabilities. Incentives alignment and remuneration schemes may vary from player to player—typically, equity will constitute a portion of their remuneration schemes.

Corporate Venture Builder

Corporate Venture Builders are capable of supporting Corporates along the full value chain of venture creation. This may begin right from the design phase to Serie A funding which covers product development and other critical phases of venture creation. For such a holistic approach, they prove to be the most interesting case to be analyzed and will be the core topic of the remainder of this article. As they are involved in the discovery phase vis-à-vis their Corporate partners, they can ensure high strategic alignment with the Corporate existing strategic agenda. Corporate Venture Builders may adopt different combinations of fees and equity as their remuneration schemes—but, always maintaining a good extent of “skin in the game” through equity participation.

When looking into the incentives alignment, it is necessary to consider that incentives also determine the total cost for the Corporate to bring a Venture to a Serie A (see Exhibit 4). When a Corporate decides to go for a full fee remuneration scheme, it will have to incur both the cost of creating the Venture, which was estimated by Pitchbook to be around USD1.6 million, and the cost of services of its Venture Partner. This could reach as much as double or more the cost of creating the Venture alone. When a Corporate is willing to share the equity of the new Venture, the total cost to Series A dramatically decreases along with an increase in the commitment and “skin in the game” of the Venture Partner.

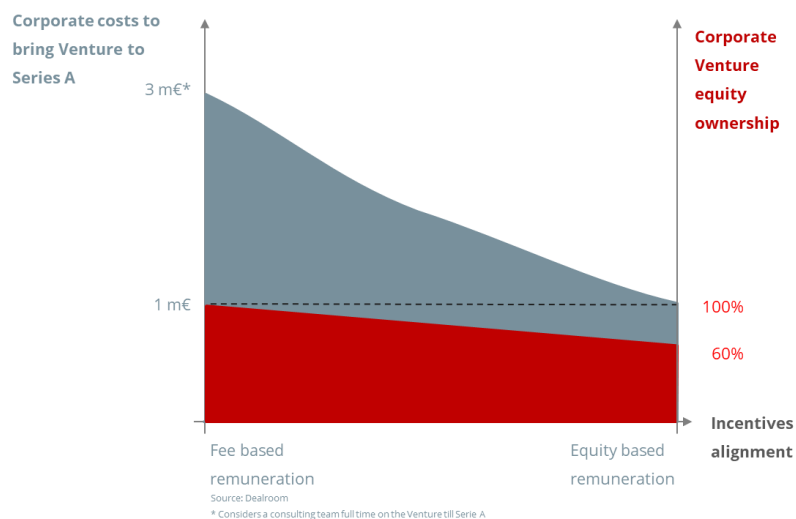


Exhibit 4

Value Propositions of Corporate Venture Partners

Analysing the value propositions of multiple players belonging to the six archetypes, it appeared that Venture Partners can be differentiated along the following 7 dimensions:

Remuneration Model

As mentioned previously, Venture Partners are usually remunerated by their Corporate partners either through cash, equity or, a combination of the two. In addition, Venture Partners may put in place variable compensation schemes to bond their remuneration to the success of the Venture.

Capital Allocation

This dimension specifically refers to the destination of the funds a Corporate allocates in creating Venture. Corporate funds may be directed either into the new venture itself or toward the Venture Partner. A secondary effect of the capital allocation is the level of transparency in funds spending for the Corporate.

Talent Background

Corporate venturing business is a hybrid of entrepreneurship and corporate activities. For this reason alone, it requires skills that can cater to both sets of success factors. Venture Partners can decide whether to support Corporates by solely bringing entrepreneurs into the ventures or to also involve experienced corporate professionals.

Stage Support

Venture Partners can decide to support their Corporate clients along the entire venture building value chain—from discovery phase to Series A funding—or, to focus on specific stages or activities such as design, team scouting or product creation.

Sector Focus

Venture Partners can adopt a generalist approach and extend their support to the Ventures in any sector or, they may also focus on specific verticals. A generalist Venture Partner usually focuses their support on the process of venture creation, whereas sector-specific Venture Partners may offer tailored support specific to the sector needs.

Expertise and Assets

In order to maximize the success probability of ventures, Venture Partners may develop expertise and assets to facilitate a specific stage of the value creation. These may include proprietary methodologies, market scouting tools and product development teams.

Networks

The quality of insights and advice a Venture can access is crucial for its success. For this reason, all Venture Partners will have their own network of experts. Two approaches to build these networks were identified into the market— in-house networks or on-demand networks. In-house network consists of a set of experts directly employed by the Venture Partner which provides faster and more constant support to the ventures than the on demand alternative. But, in-house networks also come with a greater cost. This cost difference is usually reflected in the cost of the venture building services to Corporates.

Value Propositions of Venture Partners Archetypes

Now that the report has mapped the key components of value propositions provided by Venture Partners, it is possible to, then, examine how each of the Venture Partner archetypes is positioned across the 7 dimensions (see Exhibit 5):

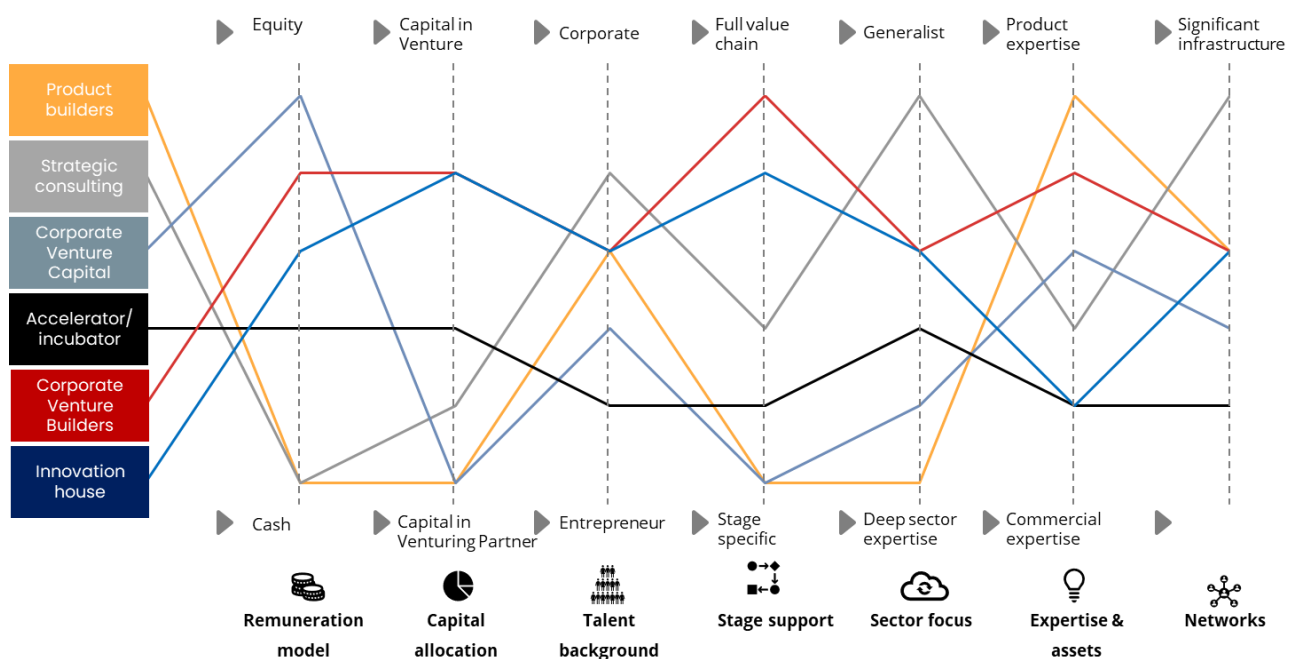


Exhibit 5

Product Builders

Since product builders offer capability-specific and time-limited stage support, these players typically support their Corporate clients in product creation of the new Ventures. This factor is strongly reflected in all dimensions of their value proposition. They are always paid through cash schemes, with no relation, whatsoever, to the Venture equity. Talents in Product Builders come

from the technical development environment with specific and functional skills. Their expertise and assets, and the network they possess are focused specifically on product creation rather than on Venture Building in general.

Strategic Consulting

Strategic consulting typically adopts a full cash-based remuneration scheme with limited room for equity sharing—which is often just a reduction of their high margin fees. In order to increase strategic alignment of their Corporate clients with the new ventures, they may set in place some variable fee schemes. However, they will still maintain a full cash-based approach. The venture design fees for strategic consulting are usually not linked to the capital allocation into the new ventures. Talents from these firms may come from a mixed background—they could be consultants from the parent company, former corporate executives or externally hired entrepreneurs. The support from Strategic Consulting firms maintains a classic consulting approach—with key focus on the design phase and is typically characterised by their limited implementation capabilities. The greatest advantage of Strategic Consulting may be found in the sector coverage and their expertise and assets. Thanks to the scale of their parent companies, these services can cover most, if not all, the sector segments with an in-house network of experts and centralized assets such as research centers.

Corporate Venture Capital

The relationship between a CVC and their Corporate partners typically does not imply a direct remuneration scheme—in both cash nor equity. When a Corporate gives a mandate to a CVC, the capital is usually allocated into the CVC entity which will later be deployed into multiple Ventures. The Corporate maintains their stakes in the CVC rather than directly in the Ventures. Talents usually come from investment and corporate backgrounds—with little to no presence of experienced entrepreneurs. CVCs are usually focused on specific segments and possess deep knowledge and strong network of experts and entrepreneurs to be able to carry the new ventures to a target stage.

Accelerator/ Incubator

There is a high degree of variability in the incentive schemes an accelerator or incubator may impose on their Corporate client. Due to the early stage in which they operate, they typically have a large cash component involved in their operations, which include mitigation of the high risk associated with the early venture building phase. Service fee and the capital for the Ventures are two distinct

streams into this business model with capital being directly injected into the Ventures with no intermediation from the accelerator/ incubator. Talents within this type of Venture Partners are typically experienced entrepreneurs adopting proprietary methodology to the Ventures in their programs. Accelerators and incubators are also generalists as they focus on the venture building process, rather than on a specific concept creation. They usually rely on a mix of in-house—or, on-demand and experienced—entrepreneurs and technical profiles who can play both counselor and active roles for the new ventures.

Corporate Venture Builder

Corporate venture builders provide wider support to Corporates in terms of stage support. One of their key features is the capability to support from the discovery phase to series A—including product development, marketing, customer acquisitions and almost all other activities that are key for Venture success. Their remuneration model is usually based on a mix of cash and equity. Cash components are aimed at covering the expenses for the venture team on the ground. While the profit is typically derived from the equity components—which can only be realized if the Venture succeeds. In terms of capital allocation, CVBs adopt a transparent model which separates the cash component from the equity injection from the Corporate to the Venture. CVBs rely on a mix of corporate and venture talents to access all the necessary experience needed along the full value chain of Venture creation. Different players within this archetype may have varying approaches to sector focus as they can range from generalist to single sector-focused. While, expertise and assets, and their network will depend on their strategic choice for sector focus. CVBs with a sector focus tend to invest more in the creation of sector-specific assets and networks.

Innovation House

Their approach is quite like CVBs as they offer support along the full innovation process with a structured approach. However, they do not provide in-house product development capabilities nor the operational and ongoing support needed for a venture. For product development, these capabilities are often outsourced or acquired through external hiring while operational capabilities are typically rendered by the Corporates.

A Look at the Market: What Corporates Look for in a Venture Partner?

Finally, to have a better sense of what the market is looking for in a Venture Partner, it is critical to understand the relevance of innovation in the strategic agendas of the Corporates. Secondly, it is also important to have a sense of the Corporates' understanding in innovation dynamics and their appetite in terms of innovation approaches. To obtain these insights, an extensive set of interviews was run with a number of Corporate Innovation department leaders, as well as Venture Partner professionals.

Results of the interviews:

All Corporate interviewees have confirmed that innovation is one of the top priorities for their companies. Nonetheless, there was no uniform answer on the preferred strategy to pursue it. Two main approaches emerged from the interviews: venturing (*make*) or acquisitions (*buy*). The key factors in deciding which approaches to adopt are succinctly explained by Christine Wang (Head of Lufthansa Innovation Hub) and Omar Valliapan (Business Development and Services at Sinamas Land) who respectively pointed out that: "The major considerations to either 'make' or 'buy' are knowledge gain and speed of deployment" and that, "The 'buy' approach is most suitable when Corporates are pursuing financial returns."

Another important consideration that has emerged in the interviews is what to do with innovation once you have it. Corporates could decide to either maintain it internally (incorporating it into a business unit), or to spin it off and offer the new venture products to the market. The choice, then, comes down to whether the Corporate is looking for financial returns or for a competitive edge. "Innovation providing a competitive edge should be kept internal whereas revenue generating innovation can be spun off" said Juandy Chua (VP Business Development and Strategy at JAPFA).

However, it should be noted that, when an innovation is kept internal, it may generate friction with the traditional corporate culture as it would be inevitably constrained by the restricted imagination and entrepreneurial spirit of a conventional Corporate structure. Moreover, "Corporate incentive schemes are usually hardly adoptable to promote innovation within the company", as Omar Valliappan pointed out during the interviews. On the other hand, when innovation is spun off into a new venture, it is not limited by Corporate traditional structure and it can lead to a disruption in the markets it operates in.

Furthermore, interviewees also acknowledged that they currently do not have the talents and capabilities required to innovate within their company. Yet, once again there was no consensus on the characteristics they might be looking for in a potential Venture Partner. Nonetheless, most interviewee agreed on the relevance of the Venture Partner reputation.

Next, it is also important that a Corporate choose a Venture Partner with the ability to guide and educate the Corporate itself with regard to its entrepreneurial journey. Venture Partners are usually selected and onboarded by the Corporate innovation department. The rest of the company is usually not used to entrepreneurship and may struggle to understand and embrace it. For this reason, Corporate professionals choosing the Venture Partners are also looking for a Partner to educate their own Company. As Omar Valliappan pointed out: “Corporates are looking into partners with the ability to coach and make themselves redundant before exiting a Venture.”

When looking into the remuneration schemes, almost half of the interviewee preferred a remuneration scheme solely based on service fee, this preference would usually come from interviewee who preferred to maintain innovation internally. This denotes a preference to keep full control over the benefits that come with the new venture. Equity sharing schemes, on the other hand, were preferred by interviewees pursuing financial returns. In this case, equity sharing is perceived as a way to reduce risk and the total cost in creating a venture.

When selecting an external Partner, Corporates are looking for experienced entrepreneurs with previous experience in Venture founding, as well experience in the relevant sectors for the new Venture. Despite this, big conglomerates have expressed a preference for generalist partners who are capable of supporting them across the multiple industries they are working in.

In terms of stage support, interviewees have expressed an overall preference for a holistic approach along the entire value chain of venture creation. They typically prefer to outsource all the Venture creation activities due to the limited experience they have.

Finally, interviewees showed limited interest into the expertise and assets of the partners as well as the type of network they rely on. On this subject, it is useful to recall that the key factor in choosing a Venture Partner is a proven track record of successful ventures. If this condition is satisfied, the interviewees are not interested in getting into the “how” a Venture Partner obtains the results they desired.

Conclusion by Wright Partners

Alessandro, in partnership with INSEAD and Wright Partners, did an excellent job completing an immense research task on venture building. As we work on 5 different ventures in the past 6 months, we have learned so much more about the various stakeholders in the venture building ecosystem and how the industry is structured. We remain steadfast in our belief that:

1. Innovation, especially non-core innovation for an organization, is important as organizations that only focus on incremental changes are likely to be under attack from disruptors
2. The strategy chosen is highly paramount when creating what seems to be non-core business innovations—typically, in the form of riskier new business models or new technology. We have seen multiple times over the last 6 months that, when companies pursue those approaches with solely service fee-based partners they might not have the risk / reward tradeoff and mindset needed to be successful

Moving forward, we intend to focus on the **“Investible Corporate Ventures”**. These are ventures who are looking to disrupt Corporates, taking on the advantage of venture capital funding and the founder’s mindset, while at the same time, maintaining their existing Corporate stakes.