A MANUAL FOR CORPORATE VENTURE CAPITAL

How Corporates Can Leverage the Advantages of Venture Capital

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1. INTRODUCTION

Venture capital has become an important element of the tech world, enabling the realization of technology-driven high-growth companies all over the globe. Every year around USD 50 billion get invested in young start-up companies – and every year the share invested by corporate investors (corporate venture capital – "CVC") grows.[1] Nowadays, roughly a quarter of all venture deals is made with CVC on board, funded by some 1,000 firms: classic technology-driven "Blue Chips" like Nokia, Intel, SAP or BMW; new media representatives like Facebook and Google; traditional media and publishing houses like e.g. Comcast, TimeWarner, ProSiebenSat. 1 or Bertelsmann; but also "old economy" corporates like General Electric, Bosch, Johnson & Johnson, Unilever and Axa.[2] All this goes to show that corporates become increasingly relevant players in the VC business as they discover its potential.

Even so, VC remains a high-risk form of investment compared to more established forms like real estate. On top of that, experience shows that most CVCs don't use their resources and capabilities to the utmost and thereby fall short of said potential. Yet, if done right, CVC can turn into a powerful tool in a company's strategy of digitalization:

> "While corporate VC investments have generated decidedly uneven financial returns, they should not be judged primarily on that basis. They should be thought of as important ways for a company to fuel the growth of its business."[3]

Many on the venture capital and start-up markets seem to see CVC as inferior compared to independent VCs. However, with the right approach, a CVC can bring in important added value to benefit their portfolio companies and their corporate parent. And this in turn provides additional levers to increase potential return rates for investments:

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[1] "Adapting and Evolving: Global venture capital insights and trends 2014." EY. http://www.ey.com/Publication/vwLUAssets/Global_venture_capital_insights_and_trends_2014/$FILE/EY_Global_VC_insights_and_trends_report_2014.pdf

[2] CB Insights. "Corporates Are In 25% Of Deals To Startups Globally, And Even More In Asia." Feb 8, 2016. https://www.cbinsights.com/blog/corporate-participation-startup-funding-2015/; "Corporate Venture Capital: Avoid the Risk, Miss the Rewards.", The Boston Consulting Group. October 2012, http://www.bcgsea.com/documents/file120517.pdf,

[3] "Making Sense of Corporate Venture Capital." Henry W. Chesbrough, Harvard Business Review, 2002, http://www.signallake.com/innovation/032002HBR_making_sense_of_corporate_venture_capital.pdf, p. 11.

"although venture investing is inherently risky, the greatest risk is not to invest at all."[4]

This paper is meant to serve as a manual for corporates considering to initate a CVC or to optimize their existing CVC arms. Accordingly, chapter 3 ("WHY: The Advantages of a CVC") shows the advantages of having a CVC.

Aims, structures, and processes should always be chosen individually for each case; there is no standard blueprint. What is important is to early on think through and decide upon relevant aspects such as the required mindset, strategy and set-up while keeping in mind the corporate's specific characteristics. Chapter 4 ("HOW: Success Criteria for Founding a CVC") contains a checklist of important points to consider when setting up a CVC.

After having implemented the proper strategy and set-up, the challenge is to find and execute deals that ensure reaching the corporate's and CVC's objectives. In Chapter 5 ("Making Deals") a framework, the "Corporate Venture Capital Investment Canvas," is introduced as a tool to define and track strategic goals for each investment case.

2. ABOUT THE AUTHOR

Iskender Dirik is Managing Director at Microsoft for Startups / the Microsoft Growth Accelerator in Berlin and Venture Partner for EQT Ventures. Before that he was Managing Director at Bauer Venture Partners, the CVC Fund of the Bauer Media Group, one of Europe's leading media companies and European market leader in magazine publishing and radio broadcasting.
Prior to Bauer Venture Partners, Iskender has founded several start-ups and was Managing Director at COPE, a Digital Management Consulting and Software Development Boutique (acquired by C3, a leading European Content Marketing Agency).
He has consulted clients like Axel Springer, Deutsche Telekom, xplosion interactive, Gamigo, Porsche, Volkswagen, Stylehaul, Deutsche Fußball Liga, TUI, Süddeutsche Zeitung and Straits Times in digital strategy and technology.
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4 "Corporate Venture Capital: Avoid the Risk, Miss the Rewards.", The Boston Consulting Group. October 2012, http://www.bcgsea.com/documents/file120517.pdf, p. 3.

3. WHY: THE ADVANTAGES OF A CVC

This chapter will present the advantages of CVC which may emerge from an ideal interaction of the corporate's core business, M&A unit, and the CVC unit. To illustrate this, the following four sections each detail several benefits that CVC has for the core business and M&A units, and the other way around.
Further start-up initiatives like accelerators and incubators won't be discussed in detail here; however, their general advantages are similar to those of a CVC.

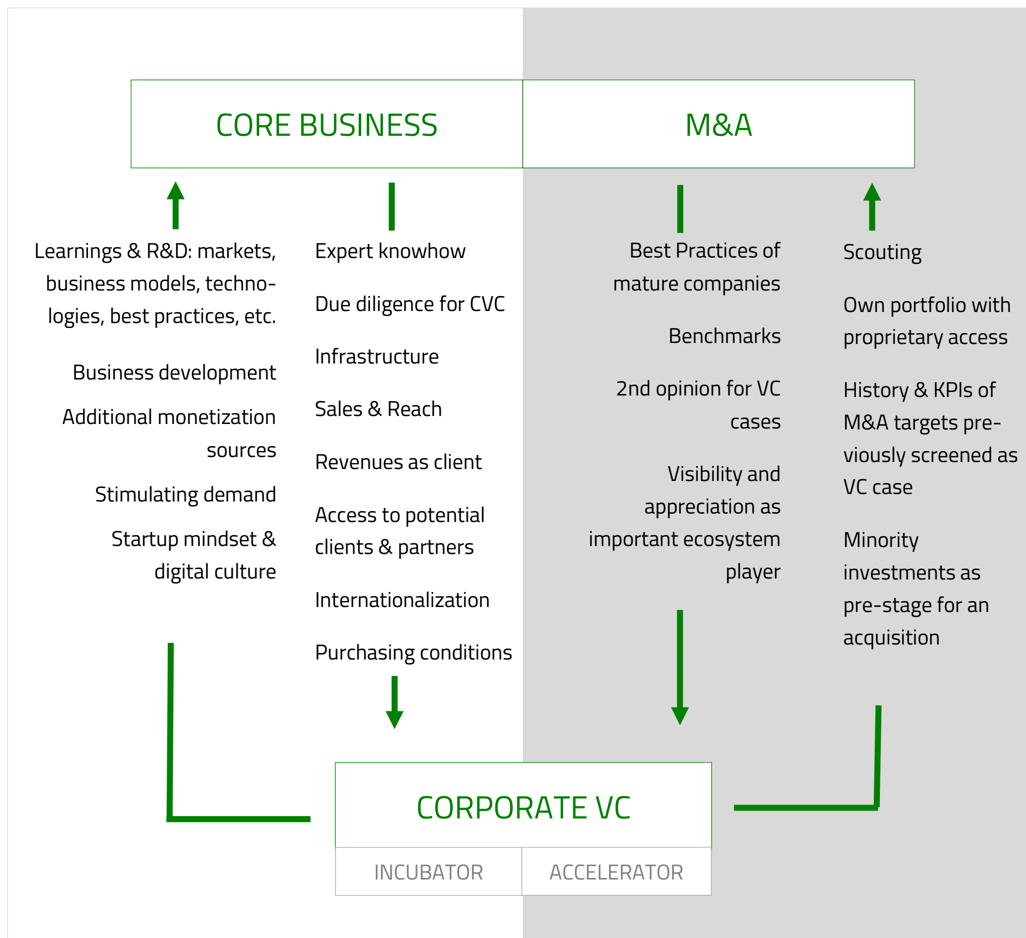

Figure 1: How Core Business, M&A and CVC offer reciprocal advantages.

3.1 CORE BUSINESS' ADVANTAGES THROUGH CVC

Core business can make use of CVC's fast pace and flexibility in multiple ways:

I. **Learning and R&D:** The CVC is able to invest not only in areas directly related to the corporate's core business, but also in sectors beyond this traditional sphere. This way, it can closely observe developments in adjacent markets and report its findings about markets, models, etc. back to the core unit. Which business and revenue models, concepts and products work? Which don't? What might be valuable for the core business? Areas of future growth can open up with this kind of scouting and learning that might not have been visible otherwise.

Example

> Corporates can use CVC to explore "strategic whitespaces" by investing in start-ups that serve customers in new markets and thus provide an indicator of those markets' potential. Panasonic, for instance, through its CVC "Panasonic Venture Group" (PVG) invested in start-ups pursuing the convergence of home computing and entertainment: [5] "Since 1998, PVG has invested in more than forty companies. As a strategic investor, the Panasonic Venture Group makes venture capital investments in companies to foster technology-centric partnerships. Companies that receive investments from PVG present clear, strategic competitive advantages to Panasonic research and product development units. Our portfolio companies have developed compelling technologies in the areas of home networking, semiconductors, reconfigurable processors, digital content, security, printed electronics, optics and other areas."[6]

Example

> BMW i Ventures, the venture capital entity of German car manufacturer BMW, has set itself the goal to invest in areas of mobility which will define the ecosystem of transportation in the future. Through investments in car sharing, parking provider apps, on-demand valet services as well as electrical vehicle-charging maps, BMW i Ventures steadily opens new areas of expertise and business for the leading car company to stay on top of innovation and change in the deeply disrupted industry that is mobility.

[5] "Making Sense of Corporate Venture Capital." Henry W. Chesbrough, Harvard Business Review, 2002, http://www.signallake.com/innovation/032002HBR_making_sense_of_corporate_venture_capital.pdf, p. 7.
[6] http://www.panasonicventures.com/investment-overview.php, 2016

Thereby, BMW allows itself to learn from its investments and adapt towards the evolving needs of its clients.

This kind of thinking also extends to R&D. CVC can be used in a targeted way as an add-on for traditional R&D to discover new tech and approaches relevant to the corporate business.

Example

"Corporates are also looking to improve the cost effectiveness and environmental sustainability of their supply chain. For instance, Nike and IKEA GreenFund invested in Dye Coo Textile Systems, a process which eliminates chemicals and water from the textile drying process and reduces energy use."[7]

II. **Customer Acquisition – Winning CVC Start-ups as Clients:** From a business development perspective, CVC is in a position to source customer groups otherwise difficult to access for the corporate. For example, a CVC connected to a media/publishing house has the potential to make investments that might end up as advertising customers; or: tax auditing firms have been known to fund start-ups that then went on to become their clients at later stages. In this manner, CVC offers new or broader ways of monetizing for the corporate.

Example

KPMG, the leading auditing and consulting firm, has set up KPMG Capital to invest Series A and B capital in promising start-ups around the world. By teaming up with young innovative companies, KMPG also engages actively in the companies' development by supporting them in areas such as auditing. This strengthens its bonds with promising tech companies that will eventually develop to a state of maturity and size at which they become interesting for KPMG's core business services.

III. **Cooperations with CVC Start-ups:** Apart from potentially being eligible as clients, the CVC's portfolio start-ups or other start-ups that approach the CVC could also be up for interesting cooperations with the corporate. In this way, the CVC is able to introduce for many interesting potential cooperation partners to the corporate.

[7] "Investing in Breakthrough Corporate Venture Capital." Volans / MacArthur Foundation / The Social Investment Business / Global Corporate Venturing, 2014, http://breakthroughcapitalism.com/files/volans-investing-breakthrough-report.pdf, p. 25.

Example

Bauer Venture Partners (BVP) is the CVC arm of Bauer Media Group (BMG). BVP has a significant dealflow from start-ups helping publishers to monetize their content with new technologies and innovative concepts. If BVP evaluates a start-up as commercially interesting for its corporate parent, the Bauer Media Group, BVP makes introductions to the decision makers at Bauer Xcel Media, BMG's digital unit. With the recommendation from BVP, BMG can then directly approach pre-selected start-ups about possible cooperations.

IV. **Sales – Selling the CVC Start-ups' Products:** The corporate can establish additional monetization channels by helping the CVC start-ups with sales and marketing. The sales cooperation would work well e.g. for big industrial players with extensive sales forces who can sell the start-ups' products along with their corporate ones and profit from the returns. Or it would work for a media company where the corporate can use their own ad sales unit to market the start-ups' ad space along their established channels and advertiser relations.

V. **Stimulating Demand:** CVCs can invest in start-ups helping to build an ecosystem that stimulates demand for the corporate parent's products. This could mean
a) investing in start-ups with offerings that are complementary to the corporate's products as well as
b) investing in start-ups with products similar to the corporate's products (in different price segments or with other differentiations), raising demand for a specific product segment.

Example

"Back in the early 1990s, long before corporate venture capital was fashionable, Intel realized it could benefit from nurturing start-ups making complementary products: Demand for them could spur increased demand for Intel's own microprocessor products. So Intel (Capital) invested in hundreds of companies whose products – such as video, audio, and graphics hardware and software – required increasingly powerful microprocessors inside the computers they ran on, thereby stimulating sales of Intel Pentium chips."[8]

[8] "Making Sense of Corporate Venture Capital." Henry W. Chesbrough, Harvard Business Review, 2002, http://www.signallake.com/innovation/032002HBR_making_sense_of_corporate_venture_capital.pdf, p. 7.

VI. **Utilizing Unused Capacities:** Taking the point above even further, further ways of monetizing internal capacities can be exploited within inventory and infrastructure assets, like laboratories, production facilities, bookkeeping or HR departments, etc. This, too, can be mutually beneficial, especially if the corporate's capacities aren't utilized to their full degree.

Example

SevenVentures as the CVC of Germany's leading TV broadcaster ProSiebenSat.1 Media SE is known for utilizing its corporate's media reach to offer exposure for their start-ups in terms of TV commercials. For many portfolio start-ups like numbrs and Zalando the TV exposure was an important growth driver. At the same time ProSiebenSat. 1 is able to utilize its unused TV inventory/advertising space to gain attractive shares in start-ups in exchange.

As iii-vi. illustrate, having start-ups as clients or cooperation partners will ideally lead to financial recoupments for the corporate – on top of the return-on-invest after exit.

VI. **Branding:** The CVC can help with the corporate's branding. Establishing itself at the core of digital innovation in the start-up market will refresh the corporate brand by association and in this way also increase the attractiveness of the corporate as an employer for digital talent.

VII. **Start-up Mindset:** Finally, apart from the market learnings mentioned under i.), corporates can extensively utilize a CVC to learn from the culture and mindset of start-ups. Attitudes towards entrepreneurship, dealing with mistakes, agility in the face of fast-paced developments, decisiveness, or flexiblility in ever-evolving markets are all part of the mindset that permeates the start-up landscape. Adopting such learnings will benefit any corporate by establishing a modern culture to gain competitive advantages in dynamic markets and to be at the frontline of innovations (for more detail, see chapter 4.1 "Mindset").

3.2 CVC's ADVANTAGES THROUGH CORE BUSINESS

Just as a corporate's core business can have advantages thanks to its CVC unit, the CVC unit and the start-ups connected to it may equally benefit from the core business.
The most far-reaching of these advantages is the possibility of using the corporate as a platform. There are benefits of expertise, infrastructure, and network already established by the core business that may open new doors into the market for start-ups or help them reduce costs for basic administration or highly specialized equipment.

I. **Sales and Reach:** Portfolio start-ups may use the reach and sales force of the corporate, both in national and international markets. A big industry corporation would be able to boost sales by offering the start-up's products to customers alongside their own, especially for complementary articles.

Example

Imagine Würth, a leading wholesaler of industrial components and the corporate with the alleged biggest salesforce on the world, investing in a hardware start-up with complementary products but a lack of resources to distribute them. In cases like this, Würth could instruct their sales managers to actively promote and sell the start-up's products side-by-side to its original brands.

Or, in another scenario, a media house might assist in the sale of advertising space of a portfolio company with their experienced marketing unit and good connections to advertisers in order to maximize revenues on both sides.

Example

Imagine a publishing house specialized in travel content, having its own extensive ad sales unit with long-lasting connections to the leading advertisers in the travel industry. If the media corporate invests in a travel portal, it could take over the ad sales for the start-up, utilizing its strong ties to the relevant travel advertisers. The media house can even offer its clients bundles that package ads on its own publications together with ones on the travel portal of its portfolio company – which can also be used to drive sales and demand on the corporate's side.

Since most corporations with CVC units have already built a multi-national conglomerate, they have gathered expertise in internationalization which is invaluable for start-ups looking to expand their business beyond home turf. Here as well, the reach of core business can turn into an advantage for the portfolio start-up.

Example

Bauer Venture Partners (BVP) is an investor in Lifesum, a leading calorie tracking app from Sweden. Bauer Media Group, the BVP's corporate parent, has strong magazine publications in the German market, many with a focus on lifestyle, fitness and health topics. Lifesum is regularly featured in various editorial variations within German Bauer publications, helping the start-up to acquire users in Germany.

II. **Corporate as Client:** A CVC portfolio start-up can win the corporate parent as client and use it as a direct revenue driver. Especially in early stages of a start-up, a steady income by the corporate can help enourmously to generate cashflow and reduce the burnrate.

Example

The Silicon Valley-based semantic recipe search engine Yummly was funded by Unilever Corporate Ventures, First Round Capital, Physic Ventures and Bauer Venture Partners. Through Unilever Corporate Ventures, the CVC arm of Unilever, Yummly was able to acquire Unilever as an important customer for Yummly's data services.

III. **Infrastructure and Buying Conditions:** Another way of cooperation comes with the existing corporate infrastructure. The corporate may offer their CVC start-ups access to useful infrastructure for prices below market standards. (The advantages this has for the corporate have been detailed in section 3.1 v-vi.) Examples here include not only production equipment and facilities, but also administration like bookkeeping or HR. In some cases, it might also mean exploiting corporate supplier networks and production structures to negotiate better purchase conditions for the start-up.

Example

Bauer Venture Partners (BVP) is an investor in Navabi, a leading online shop in the plus-size premium fashion segment for women. BVP's corporate parent, the Bauer Media Group (BMG), is a leading magazine

publisher in the women's segment. BMG was able to help Navabi in different content marketing campaigns, giving the company access to print production capacities and BMG's distribution network as well as providing advertisements in German and UK women's magazines for only BMG's production costs.

Example

Imagine a CVC belonging to a major industrial corporation with a multitude of suppliers and manufacturers. A start-up backed by a CVC of a dominant player in its field will, with corporate support, likely be able to receive discounts, better buying conditions than usual, as well as access to the corporate's infrastructure, ranging from shipping to retailer networks.

III. **Network:** The corporate can help introduce the portfolio start-up to important players in the market, thereby giving it access to potential customers and partners.
From another perspective, the CVC is able to give introductions to key figures in the corporation itself where there are chances of mutual benefit.

Example

Ringier AG is the largest international operating media company in Switzerland. Ringier Digital Ventures (RDV) is a 100% subsidiary of the Ringier AG and invests money from Ringier's balance sheet in startups. RDV has built an internal network of the most important decision makers within Ringier. If RDV was approached by a startup that could be of commercial interest for Ringier, RDV makes direct introductions to the decision makers at Ringier. Moreover, RDV pushes cooperations between Ringier and its portfolio companies and even helps to negotiate deals.

IV. **Expert Knowledge:** For the CVC, the corporate can provide experience and expertise in multiple areas: The corporate can help the CVC in terms of Due Diligence of start-ups and their products, can test products and give expert feedback, could provide benchmarks, etc. and can help portfolio start-ups as well.

Example

Axel Springer, as the owner of Stepstone (a leading German job classifieds site), Immowelt (second largest German real estate classifieds platform) and many more is an expert in the field of classifieds and therefore can provide in-depth knowledge and years of experience with business models operating in this area. In cases like this, the investment arm of Axel Springer may have access to a multitude of data, experts and relevant benchmarks enabling faster and more accurate evaluations of potential investment decisions.

Example

Ringier Digital Ventures (RDV) positions itself clearly as a financial CVC but offers its portfolio start-ups to optionally use expert knowledge at RDV's corporate parent Ringier. So, for instance, RDV's portfolio start-ups are able to get advice from Ringier's SEO experts or can talk to Ringier's CTO as sparring partner for questions about their software architecture if they want to.

3.3 M&A's ADVANTAGES THROUGH CVC

The CVC's focus on mostly early-stage start-ups (with a goal of minority shareholdings) can bring several benefits to M&A:

I. **Scouting:** For M&A projects, CVC has the potential to function as a sort of scouting unit in various ways. One of these is based on the simple fact that most start-ups are still too small and young to be considered an M&A target – but they might become one in the future. In those cases, either investing as CVC or keeping an eye on them and their development can generate an important repository of data and insights on which future M&A decisions can be based.
This kind of market scouting conducted by the CVC is able to reveal potential M&A targets before they approach structured exit processes or even before rival companies discover them. Such an early approach might achieve lower acquisition prices than would've otherwise been the case.

II. **Reducing Potential Losses:** If the corporate is very excited about an M&A opportunity, but the risk is considered to be too high, the CVC arm offers an opportunity to reduce the potential loss by initiating a minority investment that may be increased at a later stage. Even a minority investment may function as a preemptive move against competitors and

other players interested in the same start-ups, but without implicating the same potential risk profile.

Examples

In September of 2015 German media house Axel Springer acquired the renowned business magazine *Business Insider* just months after leading a financing round for a minority investment early that year. This case shows how earlier investments can lead from VC backing of a company to an M&A case in a later stage of the companies' existence.

Examples

Likewise, SevenVentures, the venture capital arm of German media house ProSiebenSat.1, is known to invest in companies that are later integrated into ProSiebenSat.1 through acquisition. Known examples include fashion aggregator Stylight, e-commerce perfumery Flaconi, as well as online erotic shop Amorelie.
These cases show how earlier investments can lead from VC-backing of a company to an M&A case in a later stage of the company's existence.

III. **Second Opinion:** CVC's start-up market knowledge can also help avoiding expensive M&A mistakes, for example when the corporate is thinking of bidding for a leading company whose business is about to be disrupted by a new start-up appearing on the market. M&A units tend to have less overview over small, recent firms, so that the CVC can function as a second set of eyes and help to better evaluate M&A targets by providing a second opinion.

3.4 CVC's ADVANTAGES THROUGH M&A

While the CVC's experiences and expertise can help the M&A unit, so can M&A experience help the CVC with minority investments.

I. **Evaluating Projections:** M&A's area of expertise is mature companies that tend to already be profitable. This knowledge can help the CVC to better judge how good a start-up's business model is, how realistic their planning is, or how probable it is that it'll become profitable. Being able to more accurately predict the future life cycle of a start-up might result in better investment decisions.

II. **Second Opinion:** Reciprocally to how the CVC can deliver a valuable second opinion on potential M&A deals, the M&A unit can give their advice/blessing on any investments the CVC is considering. The experience of evaluating mature companies and similar markets from an M&A perspective might be able to uncover new angles on a VC case previously unseen.

Example

> Imagine a corporation having a multitude of e-commerce companies in its portfolio that have mainly been acquired in more mature phases by thoroughly conducted M&A processes. In case the corporate's CVC identifies a new, very promising e-commerce start-up and initiates a due diligence process to evaluate the company's potential, the corporate's M&A division will be likely to assist in understanding the metrics the company embodies and the crucial areas an e-commerce firm will have to cover to further develop and prosper in its field.

III. **Market Reputation:** M&A activities help to position the CVC as an attractive VC investor and as a potential player in the exit market.

Example

> Bauer Venture Partners' corporate parent Bauer Media Group acquired the Zmarta Group, a leading finance marketplace in Northern Europe. News coverage after the deal not only mentioned Bauer Media, but also Bauer Venture Partners as the corporation's venture unit, as well as the Swedish portfolio start-up *Lifesum*. This shows how the acquisition increased visibility and recognition in a focal market (the Nordics) for Bauer Venture Partners, too, even when not directly involved in the deal.[9]

Having a reputation as a solvent M&A player also helps to raise the interest of other investors in the VC business to work together with the CVC.

[9] http://digital.di.se/artikel/lifesum-agare-koper-zmarta

3.5 RETURN ON CVC INVESTMENTS

Done right, a CVC therefore unfolds enormous potential for a corporate. At the same time, the CVC itself will have advantages thanks to the corporate platform which it'll be able to utilize not only in competition with other multi-LP VCs, but also to benefit its portfolio start-ups – and with that significantly increase its own returns.

From a financial perspective, a CVC's return is made up of much more than just exit proceeds, which reflect only the CVC's narrow VC activity:

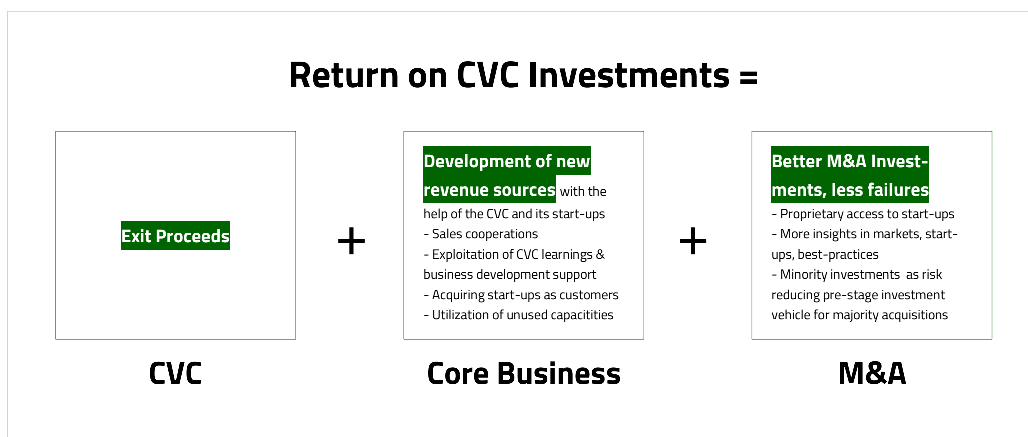

Figure 2: Return on CVC Investments

4. HOW: SUCCESS CRITERIA FOR FOUNDING A CVC

Many corporates decide to set up a CVC without first considering what detemines its success and which implications a CVC has for the corporate with its existing structures and ways of thinking.

The natural consequence is that CVCs, which fail to use their potential for either themselves or the corporate, are seen as inferior investors on the capital market by both independent VCs and start-ups, and sometimes use years before finding a proper modus operandi in respect to their cooperation with the corporate and its M&A unit.

Therefore, it's absolutely crucial for any corporate considering implementing a CVC to realize **ahead of time** which mindset a CVC demands of the corporate, how to determine the CVC's strategy, and what the ideal set-up looks like.
Accordingly, the following points are meant as both guideline and checklist for every corporate thinking of starting a CVC or trying to optimize an existing CVC format.

4.1 MINDSET

A CVC needs a mindset that's different from the classical corporate attitude. If the corporate doesn't accept and adopt this different attidude, the CVC will definitely fall short of its potential, so what's needed on the corporate side is an open mind and the willingness to change:

I. **Error Culture:** Mistakes and losses are an inherent part of the system. Use them as an opportunity to learn and move forward in an improved way.

II. **Write-offs:** Venture capital is a high-risk form of investment. Consequently, some investments will necessarily fail or possibly only return the sum invested in the first place. The Boston Consulting Group states that "experienced CVC players expect that roughly three of ten investments may fail, approximately five should perform acceptably, and the rest may exceed expectations." Write-offs are a normal part of business, not a reason to withdraw funding.

III. **Minority Investments:** Portfolio start-ups are not subsidiaries. The possibilities of influencing their operations are few. VC investing is

about offering advice and helping to boost the start-ups to success, not about taking control of them.

IV. **Blank Slate:** Don't try to bring corporate legacies into the start-up culture. While some start-ups might be happy to cooperate on infrastructure aspects like HR or accounting, refrain from trying to put structures into place that stem from the corporate environment – this is especially true for reporting formats or IT solutions.

V. **Flexibility:** Accept that the start-up landscape is always changing. This needs a dynamic and agile approach. Sometimes business models need to change ("pivoting") and in the inconstant world of start-ups, it might not always be good to follow a predetermined plan. Concepts like "Minimum Viable Product (MVP)" and "Lean Development" have to be understood in a similar way: At the beginning, it often isn't clear what the final product should and will look like without having tested the market.

VI. **Casual Mentality:** Enable a "sneakers and t-shirt" culture. This not only quite literally means to leave ties and suits at home, but also to cultivate a friendly, communicative atmosphere. Start-ups and investor colleagues should like speaking to your CVC staff. The start-up landscape is a networking culture, so make sure to build healthy grounds for that.

4.2 STRATEGY

4.2.1 Corporate Investment Objectives: Financial vs Strategic VC

One of the most important decisions to be elaborated well before setting up a CVC is that of the corporate investment objective: Will the CVC be positioned as a strategic or a financial VC – or a combination of both? This decision has far-reaching consequences for how the CVC will be perceived on the market, its modus operandi, its performance KPIs and also the team make-up.

Although this decision is so consequential, many corporates don't think it through properly before implementing their CVCs. The result: Market perception is diluted, the start-ups don't see the CVC as an attractive investor, the CVC team is frustrated because their direction isn't clear and because they get blocked and worn out at the corporate interface time and again – in short: The CVC's potential goes up in smoke.

So the decisive question is: What should be prioritized? The financial or the strategic aspect?

From a start-up perspective, taking the market position as a strategic (C)VC can bring disadvantages: The best founders might not want a purely strategic partner who's seen as working toward their own goals and possibly taking away lucrative exit channels if it benefits them, rather than focusing on the best possible development for the start-up. So, for instance, trying to negotiate call options with start-ups to gain a majority share (or even 100%) could backfire very fast as the best start-ups want to be free in their exit options.

Here, a financial VC can appear as more objective and therefore more attractive to founders.
But, as seen in chapter 3 ("WHY: The Advantages of a CVC"), a CVC with strategic corporate backing can also bring advantages to both sides. Giving those up might materially reduce the benefit a CVC unit could bring to the corporate and to the start-up – so ideally, the strategic approach shouldn't simply be discarded.
What does this mean for market positioning? A good solution would often be to present yourself as a financial VC that offers the benefits of a strategic VC without having its disadvantages: for example, by offering the start-up to use only those strategic corporate resources and benefits that it wants to use, without pressure or obligation.

Example

Sapphire Ventures receives its funds solely from one LP, German software corporation SAP. Recently Sapphire secured a 1 billion check to invest across two funds. While having a single LP-structure, Sapphire does not consider itself a corporate unit which often implicates elements of a more strategic approach towards a more coherent investment focus with the funding LP. While being able to benefit from strong ties with SAP and their network and set-up as a major international player, Sapphire operates like a traditional venture capital firm.[10]

In general, though, the question of market positioning needs to be answered based on the parent company and the business and market factors. There certainly are sectors in which excellent start-ups might mainly be interested in working with strategic rather than financial partners. One example could be the industrial

[10] https://techcrunch.com/2016/09/14/sapphire-ventures-has-1-billion-in-fresh-funding-to-invest/

engineering area, where the infrastructure (e.g. plants) a big industry player can offer to engineers makes it more attractive than a VC that can only offer funding.

Example

3M New Ventures is the strategically oriented CVC of 3M, a globally leading producer of adhesives, abrasives, laminates, passive fire protection, dental and orthodontic products, electronic materials, medical products, car-care products, electronic circuits, and optical films.

"3M New Ventures was created to strengthen 3M's position at the leading edge of global innovation by complementing 3M's holistic innovation strategy with a focus on disruptive, early stage innovations outside of the company's existing portfolio. 3M New Ventures identifies and invests in the most promising new-to-3M technologies, services and business models with long term strategic relevance to 3M."[11]

The CVC's market positioning, in turn, naturally influences both the CVC's goals and how its success should be measured. Therefore it's important to ask: What are the KPIs? Is success determined purely by financial returns or does it also include strategic goals? And how can these strategic goals be evaluated and benchmarked?

For many CVCs, the set of goals to be determined includes both financial and strategic goals. Undoubtedly the main financial aim is always to generate a maximum return on investments, but to this end, there are some points to be considered ahead of time. Therefore, the financial goals should include thoughts about capital allocation and investment performance. What are the return expectations (IRR/Investment-Multiple)? What are the key assumptions: How many of the final number of investments will be non-performing deals? How many of them will be cash cows and how many will be stars? How much capital will be allocated for these at which point – for initial investments and follow-ups? How long will this capital be tied up in investments?

Strategic goals, on the other hand, are defined in accordance with the CVC's corporate parent and usually line up with its development aims. Depending on these, the strategic objectives for a CVC may include such aspects as digitilization of the core business, gaining market know-how and exploring new market opportunities, business development, the utilization of unused capacities, and synergies with M&A. Since such goals depend much on the corporate's core business and future plans, there's no one-fits-all solution to determining them.

[11] https://www.crunchbase.com/organization/3m-new-ventures

However, it must be crystal clear that the more strategically a CVC is positioned, the less purely financial investment returns can be taken as primary performance indicators. CVCs often fall into the unrealistic trap of expecting that they can meet exceptional financial VC performance with a massive strategic impact for the core business. If financial returns are the main goal for a CVC, it must position itself and act as a purely financial VC. But if a CVC positions itself as a strong strategic investor and its main goal is to strategically boost the core business, financial KPIs are not the main indicators to evaluate the performance of the CVC.

> "At the end of the day, financial objectives are necessary to maintain internal support, while CVC's ability in meeting strategic objectives will be vital to long-term success. Each fund decides how they want to balance these strategic and financial outcomes. Although financial metrics are usually well-established, companies recognize there are 'intangible' returns that the business captures at a strategic level, which are difficult — and in some cases impossible — to quantify in the short- and medium-term."[12]

[12] "Investing in Breakthrough Corporate Venture Capital." Volans / MacArthur Foundation / The Social Investment Business / Global Corporate Venturing, http://breakthroughcapitalism.com/files/volans-investing-breakthrough-report.pdf, p. 9.

4.2.2 Investment Criteria and Focus

Once your goals have been determined, what's necessary as a next step is to define clear criteria for investing. Decide which segments you'll scout for targets, which (geographical) markets you'll focus on, which phases of a start-up's life cycle you'll invest in, the risk profile acceptable to you, investment sums for both intial and follow-up investments, the duration of portfolio investments, as well as whether to fund as a lead or co-investor.

Segment Focus

A clear-cut focus, especially in terms of investment segments and topics, has multiple advantages:

It allows building **expertise** in a specific field. This is essential for evaluating potential investment cases within their market environment.

I. **Scouting** becomes easier. By clearly defining the areas of interest, you can more effectively observe market developments and pro-actively discover new targets.

Example

At Bauer Venture Partners (BVP), the focal areas of investment are split up among its team members for active scouting. This allows to generate in-depth expertise, market knowledge and to be on top of changing market conditions and movements. Market insights, like exciting new start-ups and developments at leading companies in a speficic market segment, are shared by the responsible CVC team member in weekly team meetings and discussed within the group. Moreover, having a clear focus helps to establish automated alert systems. For this, BVP uses Feedly(.com) to monitor blogs and media sources on a relevant set of sector specific keywords that are defined by each team member for their focus segments. Feedly informs the team via alerts about news related to the defined keyword set and enables a broad, automated news coverage.

II. Thanks to the acquired expertise and scouting, it's possible to better compare business models and start-ups and in this way build a repository of **benchmarks**.

Example

Giving the CVC access to a corporate's datasets and cumulated experience will add massive value to its ability to make use of such insights generated on a day-to-day basis to evaluate and compare crucial KPIs in start-ups. Bauer Venture Partners (BVP) therefore utilizes the vast background of the Bauer Media Group as one of Europe's leading media and publishing houses. BVP has built an extensive benchmark database covering crucial KPIs for online publishers in terms of monetizing content portals and acquiring users – accessing Bauer Media's international KPIs as extensive base bechnmarks. The KPIs are complemented with best-practices in the selection and utilization of adservers, mobile advertising providers, SSPs, yield management and other adtech tools.
The benchmarks not only help BVP to evaluate business cases from media start-ups, they also provide value for the start-ups themselves.

III. By building a reputation as a field expert, you'll generate a more specific and better-quality **dealflow**.

Example

Commerz Ventures, the venture capital entity of German Commerzbank, is known for its focus on FinTech business models. Positioned as financial VC, Commerz Ventures invests solely in start-ups covering areas of financial products and services. Through investments in InsurTech company GetSafe or cloud-based digital banking platform Mambu, Commerz Ventures can be expected to receive numerous inquiries from a multitude of start-ups operating in that field who want to benefit from the investor´s deep knowledge and extensive experience.

Example

Vito Ventures, the CVC of leading heating system manufacturer Viessmann, defines itself as the "German engineering capital" and focuses on industry 4.0, big data, internet of things and cleantech among others. By displaying a profound knowledge in its focal areas, Vito Ventures has been able to close rounds with companies such as Wirepas, a provider of advanced low power wireless communication solution to connect things to the internet and will likely be able to continue its path of grouping with smart founders in these industries.

IV. Establishing the CVC as an expert in a field helps to build a **brand**, which works to uphold the aspect of generating dealflow.

Example

Having deep expert knowledge, a VC can position itself as a leading authority in its focal areas. Berlin-based VC Point Nine Capital is an excellent example of how a young VC can establish itself as brand and authority in a specific segment: Point Nine was able to position itself as a leading seed and early stage VC in the Software-as-a-Service (SaaS) market. Having made numerous well-received investments in SaaS companies like Zendesk and Unbounce and continously sharing SaaS expert knowledge in (social) media, Point Nine has built an excellent reputation and has become the first go-to-VC for young SaaS start-ups.

V. On top of that, expert knowledge in a specific field makes it easier to **support portfolio start-ups** and thus offers them an added benefit.

VI. If the focus is aligned with the corporate's development goals, then there can also be a **strategic fit** to the corporate parent. Ideally, this link gives an added authenticity to the CVC unit's defined area of interest.

Stage Focus

The company stages a CVC wants to focus on are a very crucial part of a CVCs positioning.
Many strategically-oriented CVCs tend to focus on later stage start-ups (Series A or B and upwards) that have already shown a commercial proof with a certain revenue runrate. Often this is due to the risk profile of their corporate parent: corporates tend to lower risk profiles, accepting a lower upside potential for a lower downside risk.
With some cases this can make sense, but a CVC should always ask critically if it truly is able to get its hands on top-notch later stage deals.

Frequently, later stage companies tend to accelerate their growth with top tier financial VCs to steer their company towards an exit as quickly as possible.
Strategically positioned CVCs often only get access to later stage deals if top tier financial VCs don't want to make the deal – which can quickly lead to a point where a CVC only gets second-rate deals.
The biggest demand for a strategic partner and support that exceeds the purely financial mostly lies with seed and early stage start-ups. This is the point where a strategist often can make good deals if it's able to position itself as authority in its area of focus and to build an excellent dealflow of companies in its focal segment.

Especially with a drive to deeply understand the focal segment and to help start-ups via the corporate parents, a good CVC can scout very young start-ups early on, evaluate them most efficiently, and through synergies with the corporate parent help them so much that the CVC is able to minimize the otherwise high risk of an early stage investment and therefore able to capitalize on the exponentially higher return potentials of this phase.

In principle, the decision about focal stages should be well-aligned with the corporate's profile; but it's important to critically question ahead of time how realistic it is that the CVC will have access to the best deals with certain focal stages and where it's possible to most efficiently leverage its potential through market focus and the corporate parent.

Co-Investments

Moreover, a CVC, just like any other VC, should ask if investments are best closed a) alone, b) as lead investor, or c) as co-investor next to other investors. Investment syndicates generally have important advantages: They materially strengthen one's own network, the (future) financing needs and risks rest on a number of shoulders, and different competences the VCs bring in can be used to the start-up's – and therefore all the shareholders' – advantage.

Working together with other investors is also an important source for scouting new deals: If the CVC is able to clearly and advantageously position itself on the market and to convince other investors of its benefit for the start-ups, other investors will begin sharing deals of this focal area with the CVC.

Especially in its initial phase it often makes sense for a CVC to focus on co-investments led by other CVs and then use them specifically to learn, before later ons starting to lead funding rounds itself.

> "Co-Investment Partnerships Investing in a syndicate can bring greater market leverage to the table — CVCs can share deals (and in some cases expensive sourcing and diligence costs) as well as share the risks and jointly attract additional funding. A key advantage of co-investment was seen to be internal learning. By working with other investors, especially local ones in new markets, CVC funds have a chance to better understand how to make these complex investments, and ultimately take lead roles in future deal development."[13]

[13] "Investing in Breakthrough Corporate Venture Capital." Volans / MacArthur Foundation / The Social Investment Business / Global Corporate Venturing, http://breakthroughcapitalism.com/files/volans-investing-breakthrough-report.pdf, p. 47.

4.3 SET-UP

When it comes to actually setting up the CVC, apart from the strategic questions detailed above, there are decisions to be made about the basic framework of the fund that influence the way it operates.

4.3.1 Term-Limited Fund vs Evergreen Structure

The term-limited fund is an autonomous company, a classical dedicated VC fund with a Limited Partner (LP) construct that requires a clear structure:

- committed capital,
- a fixed life span (usually 10 years),
- a defined investment and disinvestment period (usually 5/5 or 4/6 years),
- a management fee (usually 2%) and a carried interest (usually 20%) as performance component,
- a provision stating whether a portion of already realized returns can be re-invested ("recycling") and
- a provision defining whether carried interest of realized returns are distributed to fund managers (General Partners) before the end of the fund's lifespan. If yes, there should be a "clawback" defining that General Partners have to return distributed payouts after the closing of the fund in case of an overall non-satisfactory fund performance.

An evergreen structure, on the other hand, has no fixed life span or committed capital, so that investment decisions are made directly and deal-by-deal from the corporate's balance sheet.

Both models have upsides and downsides, specifically:

I. Term-Limited Fund

- **Upsides:** There is a clear commitment from the corporate to invest money based on a fixed investment plan and period. This means that there is an immediate urgency to invest and exit.
  In addition a classical fund structure provides a proven model to incentivize the fund managers for good investment performance (see "carried interest" above).
- **Downsides:** The investment plan is inflexible, therefore unable to react quickly to shifts in the market and economic environment. So the structure forces the fund managers to make investments in the first

years (usually 4-5) of the fund life cycle and to exit the portfolio companies in the last years (usually 6-10) of the fund – even if that is financially and strategically not the best option. So fund managers may be forced to invest in less attractive vintages.

Example

Robert Bosch Venture Capital, the venture fund of German multinational engineering and electronics company Robert Bosch Group, is currently running its third fund with a volume of EUR 150 million, resulting in a total of EUR 420 million allocated across the three funds of Bosch's investment arm.

II. Evergreen Structure

- **Upsides:** Investments can be done flexibly, which may be an advantage over multi-LP term-limited funds. There's no urgency to make a certain amount of investments in a given period of time with a fixed sum of capital or to sell portfolio companies, just because the fund runtime nears its end. The CVC can use this strategically to stop investing for a while when there are no attractive deals on the market. Economically weaker years can be used to allocate more capital and economically stronger years to deinvest.
- **Downsides:** The deal-by-deal attitude without a fixed commitment to invest a predetermined sum into a set number of start-ups in a given period of time can quickly lead to a lack of urgency with regards to CVC matters inside the corporation – if CVC falls behind core business and M&A in immediate importance and is put on the backburner, the CVC managers can't do the deals they want and the CVC soon loses motivation.

Example

Examples for evergreen fund structures can be found at Tengelmann Ventures, the venture capital arm of German holding group Tengelmann and Holtzbrinck Digital, the investment entity of major publishing house Georg von Holtzbrinck.

4.3.2 Corporate-Led Model vs Business-Unit-Led Model

The corporate-led CVC model and the business-unit-led model present different ways of structuring decision making processes for the CVC.[14]

As the name already suggests, in the corporate-led model the basic framework for investments is fixed by the corporate center. This means that the investment focus, especially the segments of interest, are determined by the corporate and usually chosen for their proximity to core business, to scout for start-ups that offer innovation either in existing lines of core business or adjacent ones, sometimes also in terms of improving the corporate ecosystem. Consequently, this model is useful for finding trends and developments in the market which may impact corporate business and help improve the network of suppliers and customers surrounding the corporate.

Example

> Bauer Venture Partners (BVP) is a typical corporate-led CVC. Strategic decisions as well as investment decisions are aligned with the top management executives of the Bauer Media Group (BMG). BVP's investment focus segments are decided within this group in accordance with BMG's strategic priorities and future plans.

In the business-unit-led model, on the other hand, decision power is given to the business unit. According to BCG, this model is often characterized by operational cooperation that is supported by the CVC team and members of the business unit, leading to a close relationship with the start-up. In such cooperations, this model makes use of corporate resources as well as the start-up's capabilities, and thereby giving the CVC an added lever for scaling investments.

4.3.3 Team

Staffing decisions are vital to ensure the CVC performs at the upper range of its potential. For that to happen, it's necessary to hire team leaders with broad, in-depth VC and start-up knowledge, but who at the same time offer experience with corporate structures and processes. Only with a combination of both aspects the CVC leadership will be successful, since CVCs with their corporate backing operate differently from independent VCs. They need both the flexibility and the quick

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[14] "Corporate Venturing Shifts Gears." Michael Brigl, Max Hong, Alexander Roos, Florian Schmieg, Xinyi Wu; The Boston Consulting Group; 2016; https://www.bcgperspectives.com/content/articles/innovation-growth-corporate-venturing-shifts-gears-how-largest-companies-apply-tools-innovation/

thinking the start-up world demands of VCs as well as an awareness of corporate workings to ensure smooth sailing for the CVC team.[15]
But these are by far not the only skills a CVC requires from its team members:

> "**Building the right team is the most critical success factor for a corporate venture group and it is rarely a simple task.** Creating a strong unit is dependent on acquiring a multiplicity of skills and aptitudes – in technology, finance, investing, corporate strategy, and in networking. This range of expertise is seldom found in one person alone, instead, a blend of experience across the team is often required – a strategy of appointing individuals that complement and work well together."[16]

Another main skillset required especially from the CVC's managers is a strong entrepreneurial DNA. In order to attract top talent, the CVC's top managers should be incentivized appropriately and be rewarded with an attractive upside.
In a study conducted by INTRAMEZZO, over 100 corporate venturing professionals from around the world were asked what they consider to be their venture unit's biggest obstacle to attracting and retaining talent. The top response to this question (with 56.6%) clearly unveiled "Remuneration, incentives and / or lack of carry" as their main problem.[17] And even more:

> "Portfolio companies want to know that the people who are backing them and sitting on their boards are incentivised by the success of that company and the investment. That's fundamental."[18]

However, an entrepreneurial incentive structure doesn't have to mean a classical fund carry. On the contrary, the more important the strategic goals and corporate part in a CVC are, the more incentives that are not based only on exit proceeds need to be considered. There are many examples of CVC managers who are not motivated to support corporate development with strategic deals as they are incentivized (e.g. via a classical carry) only for financial returns.
So one way or the other – it's crucial to design a compensation and bonus that offers entrepreneurial incentives for generated strategic and financial value to the

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[15] "Corporate Venture Capital: Avoid the Risk, Miss the Rewards.", The Boston Consulting Group. October 2012, http://www.bcgsea.com/documents/file120517.pdf, p. 15.
[16] "Corporate Venture Capital & Talent Report 2016." INTRAMEZZO ,p. 3.
[17] "Corporate Venture Capital & Talent Report 2016." INTRAMEZZO, p. 16.
[18] "Corporate Venture Capital & Talent Report 2016." INTRAMEZZO, p. 20.

CVC manager and that is tailored to the strategic and/or financial goals behind the CVC.

An attractive long-term incentive for the key roles of a CVC is an important measure to ensure continuity as well. And exactly that – continuity with the key team members – is an important success criterium for every VC. Venturing is a person-driven business; for successful founders with multiple offers on the table, chemistry and sympathy are often important drivers for deciding on an investor. Accordingly, the founders want to work with those same investment people and their board members until their exit and don't want to cope with team changes at their VC. Venture capital is a long-term business, changing contact persons can harm the reputation of (C)VCs directly and the CVC's performance indirectly.

Additionally, responsibilities inside the team and leadership should be clearly distributed so that hiring decisions can be made accordingly. This means that for each area that needs to be covered within the corporate and CVC unit – M&A/Corporate Development, VC, incubation, etc. – there should be designated team members. While in some specific cases it might not be necessary to have different heads for each of those areas instead of a single Chief Investment Officer, the rest of the respective teams should be staffed with their responsibilities in mind since each of those fields needs specific profiles and experiences. Within CVCs that combine financial and strategic interests even separating the teams for financial and strategic VC investments might be considered.

Example

Telekom Capital Partners (DTCP), the 500 million EUR investment management fund of Europe's biggest telecommunications corporation Telekom, covers areas from venture capital to private equity and strategic advisory. To be able to face the challenges arising from the wide focus, it put together a team consisting of managers formerly working at Telekom, other (C)VCs and tech corporations, entrepreneurs, and financial experts. Strategic and financial VC investments as well as private equity investments are separated within DCTP and have separate heads/partners with dedicated teams. In this way, DCTP ensures a well-balanced composition of talent and clearly focused team members to consistently meet the expectations of Telekom Capital Partners as well as those of its parent company Telekom in each investment category.

4.3.4 Processes

As the CVC is bound into corporate structures in most cases, it's important to set up fixed processes that structure communication and decision making and incorporate them into daily business.

Possibly the biggest role in terms of decision making falls on the Investment Committee (IC). Therefore, basic questions regarding the IC should be considered ahead of time when setting up a CVC. Next to the question of who will be part of the IC, decisions must be made with regards to aspects such as meeting schedules, reporting, presentation of new deals, and final investment decisions. Thereby, setting clear parameters and expectations for the CVC helps to make the process efficient and saves time and effort for everyone involved. Questions to be considered in this process include:

IC Meeting Schedules

- How often will the IC meet?
- Who will take part in these meetings? Just the CVC's management level or analysts as well?
- What are the topics? How much of the meeting should be dedicated to existing investments and how much to possible new deals? How detailed should the respective presentations be?

Reportings

- How often should the CVC report (e.g. once per quarter)?
- In which format? Only as a written report or should it be presented in person as well? Which format should the written report have?
- What are the IC's expectations towards the fund manager? How much of the reporting should the manager present himself? How detailed is his knowledge about the start-up's finances and progress supposed to be? The latter is an important question of expectations management and focus since it determines how the fund manager's time will be allocated: Should he spend a lot of time to become deeply familiar with each startup and its day-to-day operations? Or should he rather take an advisory bird's eye view to help the start-up by offering tips and networking support, leaving more time to source new deals?

Presentation of New Deals

- At which point in the evaluation will possible deals be presented to the IC?
- What is the format in which they'll be presented? Orally or in writing? If written, then in which format?
- Who will present the case to the IC? The investment manager/analyst who evaluated it in detail or the fund manager?

Final Decisions

- At which point in the negotiation process will the final decision about an investment be made?
- Who presents the case to the IC in the final decision meeting? (This might be the fund manager, a fund associate, or even the start-up founder(s) themselves.)

The reliability of the CVC manager's statements and the timing of final decisions may be aspects that influence the CVC's reputation on the market and therefore the quality of its dealflow, so they should be handled with care.

CVCs often have the problem that their managers are unable to make reliable statements to start-ups because they themselves are dependent on their Investment Committee's approval. This doesn't just have an impact on the CVC manager's reputation, but also on the way the CVC is perceived in the market.

Accordingly, it's critical for success that there is regular, institutionalized communication and the possibility of ad hoc appointments with the IC or the circle of decision makers whose approval is necessary for investment. The key IC members should always be involved in the investment processes on an early stage. Final decisions need to be made in a timely manner.

A good way could be to get a deal approval from the IC before a term sheet is signed, so as to have assurance that the deal will be made if there's no deal-breaker discovered during Due Diligence. Backing out of negotiations after the term sheet is signed while Due Diligence revealed nothing unexpected is a sure-fire way to get marked as an unreliable investor.

Decision-making not only influences the reputation and competitiveness of CVC on the capital and start-up market, but it is also key to acquire and retain talent. Here, the corporate itself can be a serious hindrance. In the above-mentioned INTRAMEZZO study, the parent company and/or decision-making at group level was named as one of the biggest obstacles of CVCs to attract talent:

"Dealing with corporate bureaucracy, delayed and/or misinformed decision-making (especially at the BU level) is by far the biggest hindrance to driving our mandate."[19]

Example

When setting up Ringier Digital Ventures (RDV), a main goal was to build an investment vehicle that was highly agile and fast in order to be able to compete with classical VCs. So RDV established an IC, consisting of four Ringier executives. The IC has a routine meeting every month with clear rules: In the meetings, new deals selected by RDV are discussed and the team decides together if next steps in the deals shall be pursued or not. Besides the physicial meeting, the IC gets a monthly report from RDV covering the main developments at the portfolio companies and the status of deal pipeline. For RDV, it's a main goal that all IC members are always informed about latest developments so that important decisions can be made very fast. The IC can decide on current topics on short term through a physcial meeting, a phone call or email. Due to this flexible IC structure, RDV was in the past even able to realize a new deal in just two weeks in total (a pace normally unthinkable for CVCs).

4.3.5 Cooperation between CVC and Corporate

In respect to the corporate and its business units, it's essential to establish processes for working together with the CVC - especially for strategically ortientated CVCs. Exchanging information and comparing experiences helps to align all units' activities to build a cohesive strategy. Ideally, this should be done by holding productive meetings at regular intervals to make sure the communication doesn't fall by the wayside of daily operations.

Another advantage of working closely together is the possibility for cooperation between the business units themselves or between the business units and portfolio start-ups, as detailed in chapter 3 ("WHY: The Advantages of a CVC"). But while making use of this kind of benefit may be great, there should be base rules in place about how to settle the costs generated by such processes. If one unit makes use of another unit's unused capacities, resources etc. – does it need to pay for that? If yes: what are the intercompany prices? The answers to these questions probably depend very heavily on the economic environment and the kind of corporate structures already in place, so there's no single solution.

[19] "Corporate Venture Capital & Talent Report 2016." INTRAMEZZO, p. 16.

A final point concerns stakeholder management. It's important to extend lines of communication up into the corporate's top management wherever possible, for example in the form of regular *jour fixe* meetings. This helps to keep VC visible and at the top of the priorities list – not always a given with the many other concerns of the corporate leadership. Additionally, it maximizes the learnings top management will take away from the CVC.

In general, however, the crucial factor remains to thoroughly set up all the processes in the interface between the CVC and the corporate structures. Here is where a lot of the CVC's potential for the corporate gets lost.

5. MAKING DEALS

5.1 DEAL SOURCES

Many corporates with a new CVC vehicle think that it's enough to dangle the prospect of money in front of start-ups to get good deals. But even the pull of a corporate brand in combination with investment capital usually isn't enough to rely on the most exciting market cases popping up in your inbox.

Nowadays, there's enough VC money readily accessible on the market for good founders, so that nobody is waiting for a corporate with the most recent CVC fund.

Therefore it's important that the CVC enters the relevant market actively, markets itself – yes, even pitches for founders to show them why this CVC in particular is attractive and which concrete benefits it can offer compared to a classical VC.

The CVC has to take action to be perceived as an attractive investor on the market. Undoubtedly the best method for this would be a track record of high performing deals – but that's something that only be built with time.
In the first 6-12 months, a CVC should ideally plan to use plenty of time and budget for the market launch. The CVC should be present at relevant events of the sector, construct and broaden its network, and possibly flank its market positioning with PR and content marketing.

Inbound requests by founders are rarely a good deal source. A look at the statistics of established VCs shows that only a tiny number of deals emerge from direct inquiries by start-ups. The most important sources for interesting deals are:

I. Own network of companies, entrepreneurs and multiplicators.
II. Other investors/co-investors. Dealsharing is very common and popular among well-acquainted investors.
III. Proactive scouting and approaching of existing start-ups.
IV. Fund of Fund investments (see chapter 5.2)
V. The corporate (synergy effects created by an investment focus close to the corporate's area of business)
VI. Relevant start-up events

5.2 FUND-OF-FUNDS INVESTMENTS

While it's useful to narrow the CVC's investment focus down to unlock the advantages mentioned in the sections above, it might also be beneficial to consider investing in other VC funds. Possible upsides include:

I. **Deal Sourcing:** Investing in another fund will make you a Limited Partner (LP), ideally (if negotiated right!) giving you **access** to the fund's **dealflow and to follow-up investments** with their best portfolio start-ups. This means: you can make direct investments with your CVC vehicle into existing portfolio companies of the fund you are invested in, or can directly invest in great deals that don't fit into the investment focus of the related VC fund.

II. **Network:** Gaining access to other funds in this manner expands your **network** of investors and start-ups. In a network-driven environment like the start-up world, this may well be essential to get access to good deals.

III. **Learning:** Additionally, communication and exhange of information with the other funds' managers can bring with it a boost in **investment, market and start-up knowledge,** especially about areas adjacent to your own investment focus.

IV. **Diversification:** By distributing your fund capital across multiple investment channels, you **minimize the financial risk** inherent to venture capital assets. This is much easier done by spending a portion of your capital on other funds than by trying to achieve this alone. Accordingly, investing in VC funds with a different investment focus from your own will lead to more effective diversification.

But despite these benefits to fund-of-funds investing, making start-up investments with your own CVC unit is crucial as well. Only with own investments you can maximize learnings, by getting the chance to closely observe market developments but also by being closer to the start-ups themselves. Moreover, done right, return potentials can be much better with own investments, as you can leverage your corporate's platform and your expertise in specific industries much better with a direct shareholding relationship.

Because any other rivaling fund can also easily gain access to the funds of your choosing, true competitive advantage has to stem from the investments you make and the expertise you build with your own CVC.

As so often, it's the combination that makes fund-of-funds investments powerful. They offer the possibility of finding and tracking startups in early stages to invest in them later directly and of easily keeping an eye on segments which aren't part of an active focus area, thereby effectively filling information gaps and canceling out weaknesses of a narrow investment focus.
On top of that, fund-of-funds investments offer a good option for corporates who want to gain some initial VC experience with little effort before they set up their own fully powered CVC.

Example

Siemens Venture Capital, as the investment arm of the leading technology corporation Siemens, has invested in more than 40 funds all around the globe, including renowned investment firms such as Menlo Park-based Lightspeed Venture Partners. In this way, Siemens Venture Capital is able to source deals and broaden its network at the nucleus of its investment horizon on a global scale and thereby avoid missing out on attractive deals.

Example

German media giant Axel Springer SE was quite unknown in the digital US market just a few years ago. "People used to say 'Axel who?,'" Axel Springer's Chief Executive Mathias Döpfner said.[20] To enter the US market, Axel Springer Digital Ventures (ASDV) started with very well-chosen fund investment: in 2014, ASDV invested in SV Angel, a leading San Francisco-based seed-stage venture firm, and Lerer Hippeau Ventures, a leading early-stage VC from New York with a strong focus on digital media. These fund investments were the foundation of Axel Springer's US activities as they were the key to build a relevant network in this new market, resulting in exciting opportunities for direct deals by ASDV. Now, ASDV has directly invested in exciting US-based startups like AirBnB, the video publisher NowThis, the online magazine for news and culture Ozy Media and the photo platform Pixlee.

[20] http://www.wsj.com/articles/axel-springer-looks-to-u-s-for-digital-growth-1462973407

Example

Evonik Corporate Venturing is another of many corporate-led investment firms to invest in disruptive business models through other VC funds. As Evonik, a leading player in the chemicals and energy industry, aims to expand its portfolio above the recent range in terms of technologies and geographical areas, it realized fund-of-funds investments with German High-Tech Gruenderfonds, Swiss Emerald Technology Ventures as well as North-American Pangaea Ventures.

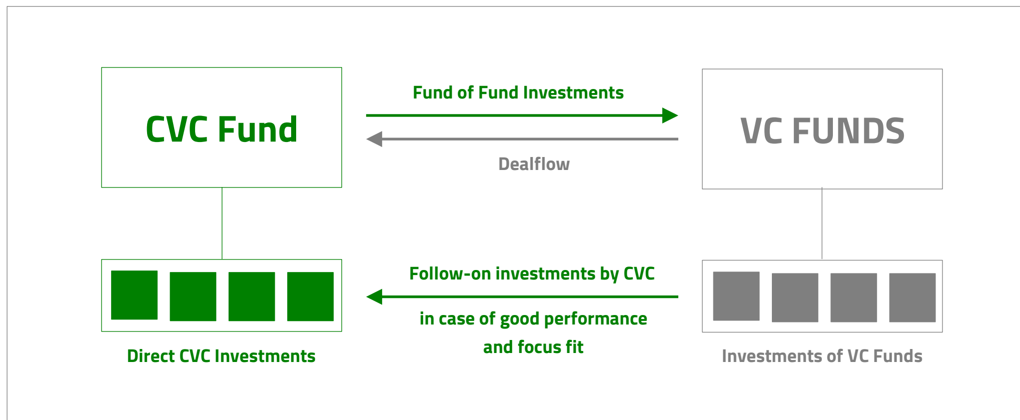

Figure 3: Combining Direct Invests with (Fund of) Fund Invests

5.3 DEAL OBJECTIVES: INTRODUCING THE CVC INVESTMENT CANVAS

As described in chapter 4.2.1, it's elementary to decide before setting up a CVC which financial and/or strategic goals you want to pursue with the CVC vehicle. To implement and follow up on the strategy afterwards, however, it's not enough to fix the strategic goals for the CVC on a meta-level. As simple as it sounds, before signing a deal, many strategically-oriented CVCs on the market fail to give enough thought to concrete strategic goals that the investment should strive to achieve in order to be aligned with the CVC's positioning.

Particularly in a corporate environment there's a lot of talk about synergies which finally never go beyond a theoretical level. CVCs with a strong strategic approach should therefore define concrete strategic and financial goals before each investment. An investment decision should be made on the basis of these goals and the potential connected to them. On top of that, it's a good idea to decide on a deal-by-deal basis whether a deal is to be considered strategic or financial, or how weighty each of these components is respectively. This will determine the KPIs with which a deal's success will be measured.

It sounds trivial, but many CVCs also neglect to sufficiently talk to start-ups about the strategic goals the corporate/CVC might have with their investment. Transparent communication right from the start is essential to align both sides' expectations for working together and to achieve the set goals.
Another point, often lost sight of before a deal is closed, is to outline what advantages the corporate could leverage for the start-up.

To accordingly discipline yourself to clearly define the corporate's strategic goals and seek potential ways of how the start-up might be able to benefit from the corporate parent ahead of closing a deal, the "Corporate Venture Capital Investment Canvas" (cf. below) was developed.
This canvas is meant as a decision template and guide for the definition of strategic investment goals per deal opportunity and their translation into specific measures. This latter aspect is emphasized because experience shows ideas about synergies can only be turned into practice if they're directly furnished with clear actions. It's recommended to directly assign those actions to members of the teams in order to be able to track the measures.
Weighting the goals (in the template based on Harvey Balls) helps to derive strategic priorities from the canvas.
The canvas serves as a framework which can be adapted to individual CVC's requirements.

Corporate Venture Capital Canvas for Investment in Startup „NewUnicorn“

CORPORATE GOALS

Learning/R&D	Business Development	Utilizing Unused Capacities	M&A
Learning about developments in core, adjacent & new markets, business models, technologies, marketing strategies, product development, cost optimization, etc.	Winning the startups as client or cooperation partner, selling the startup's products, pushing an ecosystem and stimulating demand for own products, etc.	Utilizing unused and available capacities, resources, reach, infrastructure, plants, technologies etc.	Monitoring startup as potential acquisition target, reducing risks, gaining access and information about other potential targets in market segment
Goal / O / Action	Goal / O / Action	Goal / O / Action	Goal / O / Action

STARTUP GOALS

Expert Knowledge	Business Development	Utilizing Corporate Platform	
Utilizing corporate's industry know-how, best-practices, benchmarks etc.	Winning corporate as cooperation partner or client, gaining access to corporate's network to get intros to potential clients and partners,	Using corporate's infrastructure, sales team and reach, internationality, getting better buying conditions with corporate and external suppliers etc.	STRATEGIC / FINANCIAL
Goal / O / Action	Goal / O / Action	Goal / O / Action	

Figure 4: The Corporate Venture Capital Canvas. Download under:

.pptx → http://www.alphalist.cc/cvc-investment-canvas.pptx

.pdf → http://www.alphalist.cc/cvc-investment-canvas.pdf

A barometer indicates the weighting between the strategic and financial goals of the investment. One can't expect the same return rate from a highly strategic deal as from a purely financial investment. So a strategic vs. financial consideration is at the same time a decision about the KPIs that will determine at a later stage whether the deal was successful or not: the achievement of strategic goals vs. financial (exit) returns.

5.4 CONTINUOUS REVIEWS

Strategic goals are often forgotten very quickly after making an investment. A corporate is often tempted to soon after judge the success of an investment solely on the basis of financial KPIs – even when there has been a clear strategic rationale for the investment decision. The financial KPIs are easiest to measure after all as cash is king.

Here as well the CVC Investment Canvas helps. It's a pre-destined foundation to regularly check and track the original strategic goals of an investment. Ideally, a review of the goals and the status quo of target achievements should be made each quarter, but at the very least each half year. At that point, both the strategic and the financial goals should be assessed. The latter also includes an evaluation of the start-up's valuation and an update on expected revenue returns.

Example

Bauer Venture Partners does a quarterly review of its portfolio companies: It checks the target achievements of possible strategic goals for Bauer Media Group as well as the synergies that should be leveraged for the portfolio companies, and if needed, new measures are devised and priorities adjusted. At the same time each start-up's valuation is assessed: Does the company valuation seems realistic on the basis of the latest developments? Is it necessary to adjust prognoses about the return-on-investment? The evaluation thus serves as an important decision template about follow-up and bridge financing. An additional comprehensive Excel model enables a clear and central documentation of the assumptions and prognoses for each portfolio company.

5. 360 DEGREES EXAMPLE: MICROSOFT

This paper focuses on Corporate Venturing and fades out other corporate innovation and startup initiatives like accelerators, incubators and innovation hubs.
However, as a wrap up, Microsoft provides an excellent example for a 360 degree startup strategy and a seamless integration of a CVC, Accelerator and Startup Evangelism motion ("motion" is a term often used at Microsoft).

There are currently only a few corporates on such a scale that are more serious about digital transformation than Microsoft (see "Microsoft's successful transformation: From Microsoft to Microcloud").

The cloud is Microsoft's number one priority going forward. The whole organization and product roadmap is designed to shift the core business to cloud offerings.
Under Satya Nadella, Microsoft succeeded in positioning its Microsoft Azure Cloud as the most important Amazon AWS competitor (see "Sorry, Amazon, But Microsoft Is The World's #1 Cloud Vendor - Here's Why").

Microsoft's three main startup motions are finely tuned to contribute to this digital transformation:

I. **Microsoft BizSpark & BizSpark Plus**
   BizSpark is a startup program, addressing seed/early stage companies and providing them with credits for the Microsoft Azure Cloud. BizSpark is open for every startup that meets certain criteria (like age and revenue). BizSpark Plus on the other hand is a program where Microsoft partners with over 200 leading startup accelerators around the world to provide their cohorts up to $120k of Azure cloud over two years.

II. **Microsoft (Growth) Accelerator**
   Seven Growth Accelerator programs worldwide (Seattle, London, Berlin, Tel-Aviv, Bengaluru, Beijing, Shanghai) help Series A stage B2B tech companies to scale their business. The Accelerator doesn't invest money and doesn't take any shares. It provides access to Microsoft's enterprise customers and partners, tech support, executive coaching in topics like pricing, sales and negotiation strategy and talent development and a significant amount in Azure cloud credits on top.
   The Microsoft Global Startup Roadshow 2017 Mashup video conveys a good impression about the activites of the Accelerator and its interaction with the Microsoft organization.

"(...) here is a partial list of things MS accelerator helped us with:
- Connections with MS customers
- Introductions to known investors, one of which invested in the company
- Connections to departments inside MS which might become customers
- Introductions to other alumni startups with similar difficulties and challenges
- Provided Go-to-Market experts which helped us sell our product and convey our value proposition
- Provided us with $500K (!) in Azure credits for zero equity
- Helped us close our $3M round (!) with leading investors
- Exposed us to hundreds of potential customers on a demo day which was live streamed to thousands of people via TechCrunch."

Guy Kroupp, Founder & CEO at Coralogix, Microsoft Accelerator Tel Aviv Alumni focused on the power of machine learning and artificial intelligence to power log analytics; see "MICROSOFT, what have you done for me lately?" for more.

III. Microsoft Ventures

Microsoft Ventures, Microsoft's CVC, is an active, strategic, investing partner at key stages of a startup's growth, typically investing between Series A and C/D. Microsoft Ventures currently invests in startups located in North America, Israel and Europe.

"When I came to Microsoft in 2016, I was driven by the opportunity to establish a corporate venture group that would create an additional channel to engage the start-up ecosystem. It would support not just company objectives, but our customers, partners and the ecosystem more broadly. The idea was that we would take an approach which would augment our own product and technology efforts, and enable us to place both strategic and financial bets with early stage companies."

Nagraj Kashyap, Corporate Vice President and Global Head of Microsoft Ventures

And here is how the three different motions contribute to Microsoft's core business and each other

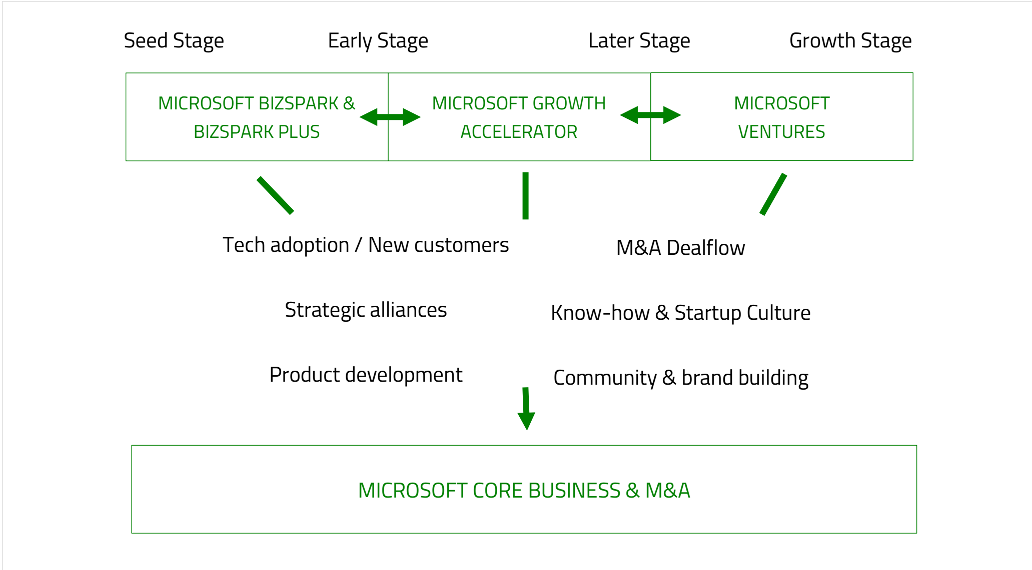

Figure 5: How Microsoft's startup programs support it's core business.

I. **Microsoft BizSpark & BizSpark Plus** (offering seed/early stage companies Azure credits)

Contribution to Core Business:

- **Tech-Adoption**: Increasing adoption of Azure cloud and other Microsoft technologies; winning the successful businesses of tomorrow at very early stages.
- **Community**: Community building in the early stage startup ecosystem.
- **Brand**: Helping Microsoft to be perceived as an innovative, disruptive, fresh brand.

Contribution to Microsoft Growth Accelerator:

- **Dealsource**: Referring later stage companies to the Accelerator programs.

Contribution to Microsoft Ventures:

- No direct link, stage-wise the targeted companies are too far from the focus areas of both entities.

II. Microsoft (Growth) Accelerator (helping later stage startups to scale)

Contribution to Core Business:

- **Tech-Adoption & new customers**: Increasing adoption of Azure cloud and other Microsoft technologies in mature startups; winning the successful businesses of tomorrow as customers.
- **Strategic alliances**: Finding complementing startups as cooperation and co-selling partners:
  A) Offering startup products to enterprise customers to drive own revenues directly.
  B) Leveraging startups to position Microsoft products at the startup's customers (like Accelerator Startups that advise their clients to implement Microsoft Dynamics as CRM) .
- **Community**: Positioning as a platform for startups and VCs, Community building in the startup ecosystem and in stages where real businesses start to evolve.
- **Brand**: Helping Microsoft to be perceived as an innovative, disruptive, fresh brand.
- **Product Development**: Identifying product and feature needs of mature startups, collecting their feedback to improve the core (cloud) products and increase their competitive edge.
- **M&A**: Feeding Microsoft's corporate M&A with interesting strategic acquisition cases.
- **Know-how**: Being at the core of innovation, learning from the markets (trends, best-practices, startup culture etc.) and leveraging the learnings for the core business.

Contribution to Microsoft Ventures:

- **Dealsource**: Referring the best later stage companies to Microsoft Ventures:
  A) Accelerator startups and alumni
  B) "External" startups seen during the Accelerator team's deal-sourcing activities.

Contribution to Microsoft BizSpark (Plus):

- **Dealsource**: Referring seed/early stage companies that they come across to the BizSpark team.

III. Microsoft Ventures (providing money for later/growth stage startups)

Contribution to Core Business (besides financial returns):

- **Tech-Adoption & new customers**: Increasing adoption of Azure cloud and other Microsoft technologies in growth stage startups.

In 2017 Microsoft invested directly (and not via the Microsoft Ventures unit) in Flipkart, an Indian unicorn[21]. Flipkart is a great example for a financial investment that comes along with a strong strategic component related to the core business of the corporate parent:
"Microsoft Corp. and Flipkart, India's leading marketplace, on Monday announced a strategic partnership to provide consumers in India with the best online shopping service. As a first step in the broad collaboration between the two companies, Flipkart will adopt Microsoft Azure as its exclusive public cloud platform. (…) Starting with computing infrastructure, Microsoft Azure will ultimately add a layer of advanced cloud technologies and analytics to Flipkart's existing datacenters. Microsoft's strong presence in India, along with its global scale, allows for continued growth and expansion, setting the stage for the long-term partnership. "[22]

- **Strategic alliances**: Finding complementing startups as cooperation and co-selling partners.
- **Brand**: Helping the Microsoft to be perceived as an innovative, disruptive, fresh brand.
- **Product Development**: Identifying product and feature need of startups in the growth stages.
- **M&A**: Feeding Microsoft's corporate M&A with interesting strategic acquisition cases.
- **Knowhow**: Being at the core of innovation, learning from the markets and leveraging the learning for the core business.

Contribution to Microsoft Accelerator:

- **Deal-source**: Referring relevant companies that they came across during their own deal-sourcing activities to the Accelerator teams.
- **Know-how**: Providing knowledge, experience and network in selecting and scaling the Accelerator startups.

[21] https://techcrunch.com/2017/04/10/flipkart-1-4-billion/

[22] https://news.microsoft.com/2017/02/19/flipkart-and-microsoft-forge-cloud-partnership-to-expand-e-commerce-in-india/

Contribution to Microsoft BizSpark (Plus):

- No direct link, stage-wise the targeted companies are too far from the focus areas of both entities.

IV. Core Business & M&A

Contribution to startup motions, especially Microsoft Ventures & Accelerator:

- **Deal-flow**: Referring interesting startups that business development executives and sales people in the field identify during their work.
- **Know-how**: Helping to evaluate tech cases with expert know-how in tech, markets, products, enterprise sales etc.
- **Business Development**: Supporting portfolio companies to scale their businesses (strategic alliances, co-selling etc.).
- **Tech & Tools**: Providing tools and deep tech support for portfolio startups.

Microsoft Ventures invested in Element.ai, a platform for companies to build AI solutions (within a 102 Million USD Series A round).
Being able to leverage Microsoft's core business capacities was an important added value for Microsoft Ventures and Element.ai:
"It sounds like Microsoft is approaching this investment not just as financial backing, but also as more pragmatic operational backing. It is providing software, cloud storage via Azure and more of Microsoft's existing tools. This ensures that whatever does get built, it has some degree of Microsoft baked into it.
"We all know 'You're only as good as your tools' and now Element AI is getting supercharged with Microsoft Ventures," said Gagne, who is leading the effort, in a statement. "Along with a strategic investment that is a real vote of confidence for Element AI, Microsoft is giving us the tools and services which will help our AI network achieve scale, which will undoubtedly create new technologies that help tackle some of the world's biggest problems."[23]

[23] https://techcrunch.com/2016/12/12/microsoft-ventures-launches-new-fund-for-ai-startups-and-backs-element-ai-incubator/

To reduce complexity, Microsoft's other existing startup and growth programs like "Success Management", "Corporate Access Program" (CAP), "Independent Software Vendor" (ISV) program and tech engagement with startups in 3rd party accelerators are faded out.

Bottom line: Microsoft covers all startup stages and uses its different startup motions to feed and support its core business and each other in a very structured way.

6. CONCLUSION

The possibilities of a CVC as an inherent element of a corporate's digital strategy are mighty and manifold. Even so, many CVCs fall short of this potential because their set-up isn't ideal. This leads to the current market situation where CVCs are seen as inferior to independent VCs.

Before setting up a CVC one should therefore put enough effort into deliberating about the different forms a CVC can take, competitively positioning the CVC at the capital market, drafting a set-up with a clear strategy and explicit goals that do justice to the corporate, and into implementing structures that help to utilize the potential of the interplay between the corporate's core business, M&A and CVC.

After the homework is done and a promising set-up is realized, the CVC must scout and execute on deals that fit into the strategy. Many CVCs neglect to define clear strategic and financial goals for each deal as a base for an investment decision. The "Corporate Venture Capital Canvas" helps to avoid this pitfall and provides strategically-oriented CVCs a framework that ensures satisfying the CVC's strategic objectives, leveraging synergies in favor of the portfolio start-ups and continuously tracking their performance.

7. READING LIST

Highly recommended papers about CVC:

I. "Corporate Venture Capital: Avoid the Risk, Miss the Rewards." TFalk Bielsch, Michael Brigl, Dinesh Khanna, Alexander Roos, Florian Schmieg; The Boston Consulting Group; 2012; http://www.bcgsea.com/documents/file120517.pdf

II. "Corporate Venturing Shifts Gears." Michael Brigl, Max Hong, Alexander Roos, Florian Schmieg, Xinyi Wu; The Boston Consulting Group; 2016; https://www.bcgperspectives.com/content/articles/innovation-growth-corporate-venturing-shifts-gears-how-largest-companies-apply-tools-innovation/

III. "Investing in Breakthrough Corporate Venture Capital." Volans, MacArthur Foundation, The Social Investment Business, Global Corporate Venturing; 2014; http://breakthroughcapitalism.com/files/volans-investing-breakthrough-report.pdf

IV. "Making Sense of Corporate Venture Capital." Henry W. Chesbrough; Harvard Business Review; 2002; http://www.signallake.com/innovation/032002HBR_making_sense_of_corporate_venture_capital.pdf

V. "Corporate Venture Capital & Talent Report 2016." INTRAMEZZO; 2016.

VI. "Global Corporate Venturing" Website, http://www.globalcorporateventuring.com

VII. "Strategic growth investing. The next evolution of corporate venture capital", TELSTRA, https://www.telstra.com.au/content/dam/tcom/personal/ventures/Telstra%20CVC%20paper_FINAL.pdf

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