The Resilience Mandate

In a world dominated by change, how can a large company stay relevant and evergreen? And update its products, services, and business models before it gets disrupted by a startup?

The answer lies in leveraging its foundational assets, and combining them with the enterprise of a startup. This paper proposes a new growth vehicle — a Purpose-built Startup. It was presented by Ajay Madhok, at the mediaX Innovation Workshop on October 22, 2019 held at Playground Global, Palo Alto.

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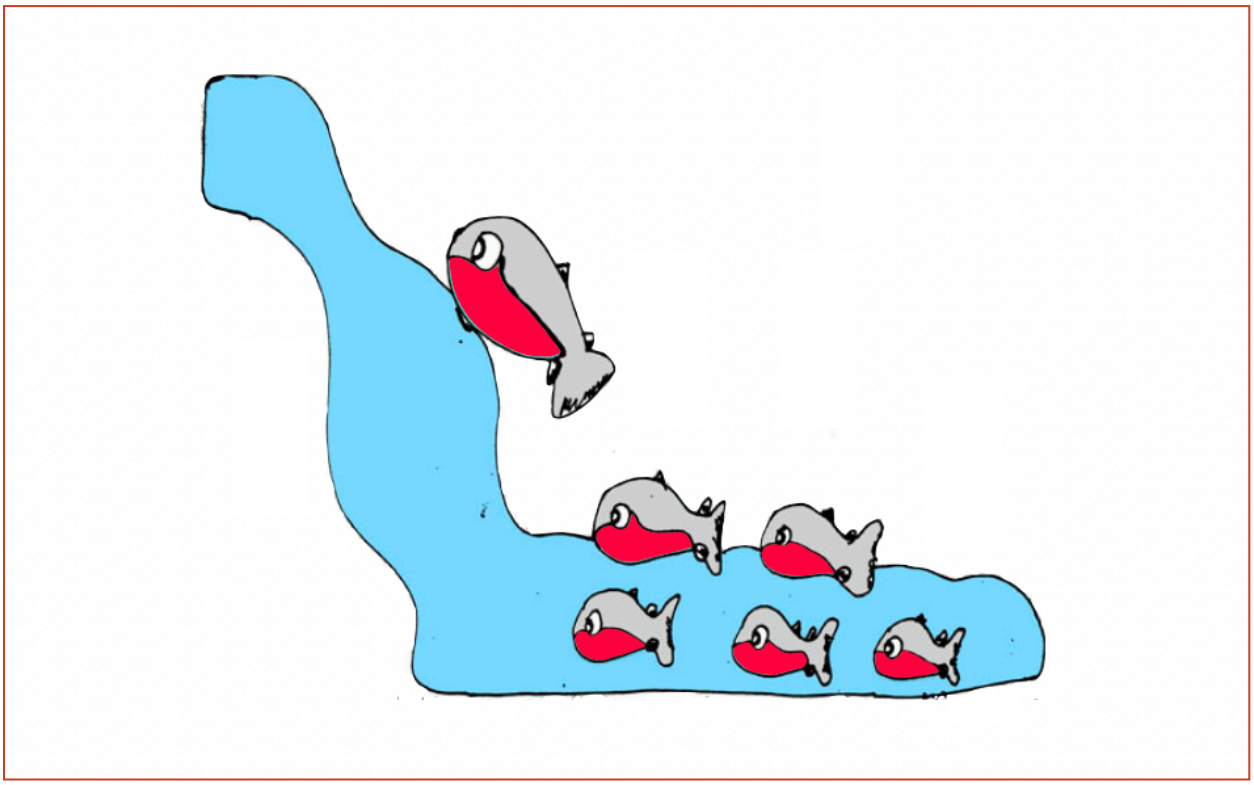
It's harder than ever to stay on top.

Unless you are a technology company, it is hard to be a big company today. We see confirmation in the longevity of S&P 500 companies. Their lifespan that averaged 33 years in 1964, contracted to 24 years by 2016, and is forecast to shrink to just 12 years by 2027. In fact, a S&P 500 company drops-off the index every few weeks. For example, Kohl's, Staples and Foot Locker were dropped earlier this year, and it is widely speculated that Coty's, Macy's and Occidental Petroleum will not make the list this quarter. On Dow Jones, General Electric was the last surviving member from the original constituents, but it finally lost its membership last year.



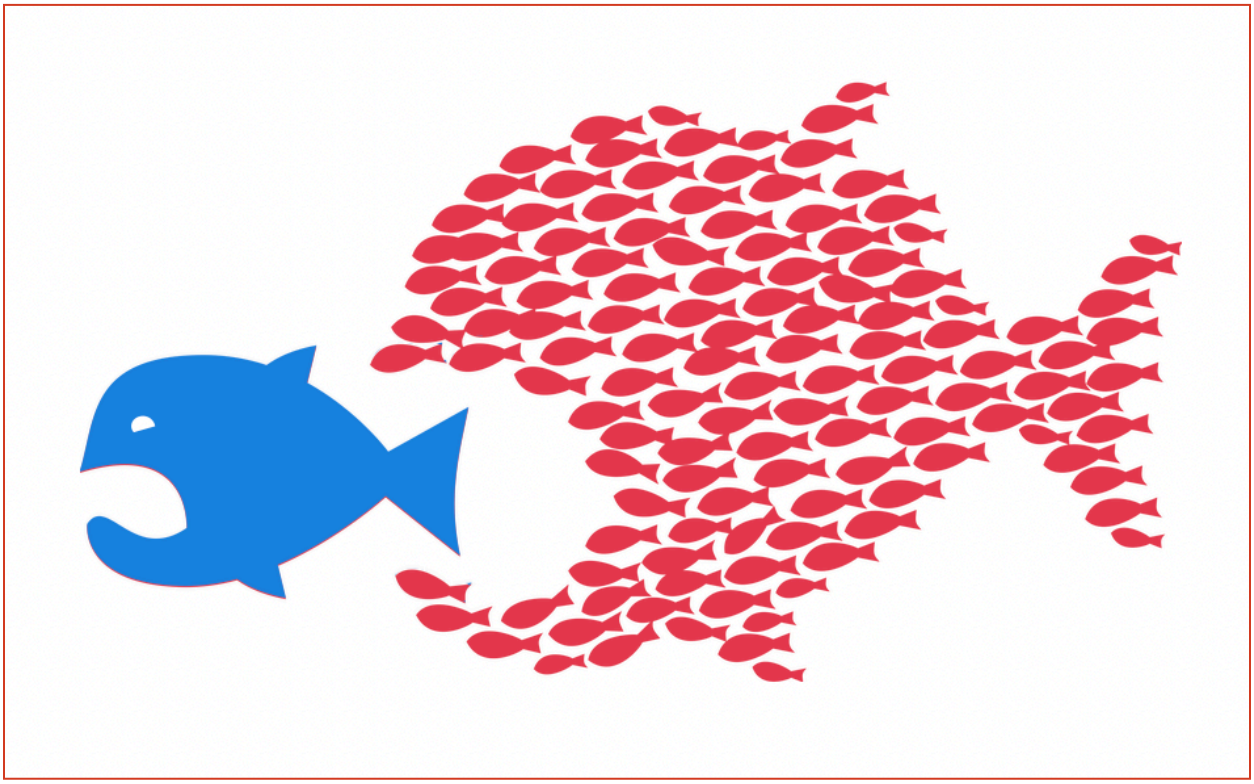
The other piece of evidence is from the stock markets — the number of publicly-traded companies in the U.S. has declined 46%, from its peak of 8090 during the DotCom era in 1996, down to 4331 companies in 2016. Put another way, there were 23 listed companies for every million U.S. citizens in 1976, and today, it is down to 11 listed companies per million.

But for a technology company, these are good times. Just look at Amazon, its ambitions know no bounds. It took off like a rocket ship and hasn't slowed down since. It got into many verticals, constantly redrawing competitive lines by leveraging its key assets such as customers, data, and its distribution reach. We will explore why technology companies are eating the world, and what lessons they offer to other large companies.

Why? Its death by a thousand cuts.

Growth, across industry verticals, is led by technology startups engaging the next generation of customers. They are funded by liberal venture capital to break things that can be done better, and rewarded for disruptive innovation.

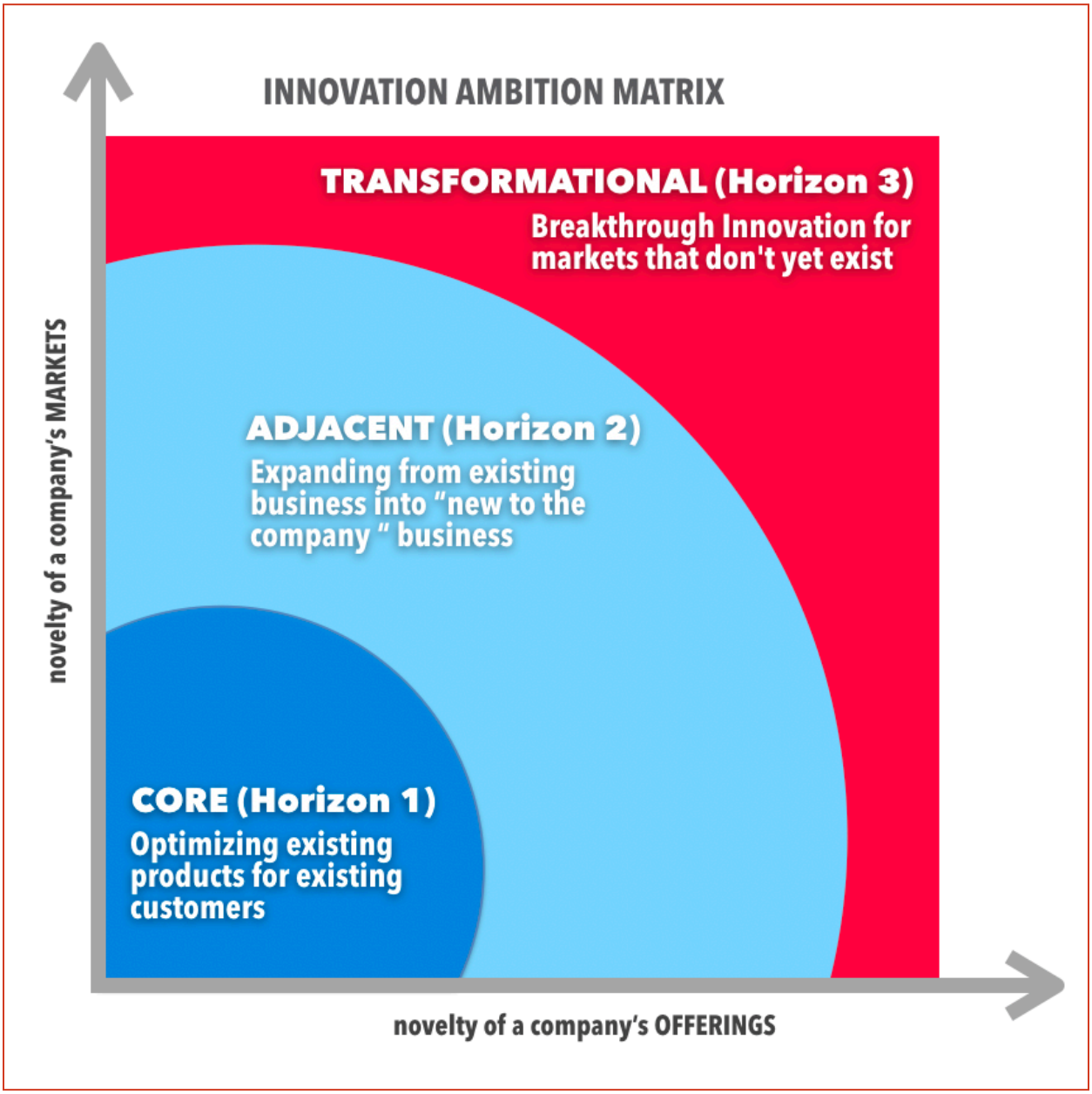
These startups don't attack incumbents head-on, instead they focus on re-imagining specific features of a product. They acquire customers by creating better experiences, cutting margins, and connecting customers better with an unbundled feature. Let's take the Banking vertical to illustrate unbundling of core banking products and service offerings from Loans to Investments to Insurance and Financing. For each of these offerings, an incumbent bank faces startup challengers focussed on just that one offering. For example, Robinhood, Betterment, Acorns, and Wealthfront offer Investments, while SoFi, tution.io and CollegeAve offer student loans.



It is this army of emerging players that strike at legacy players at an individual products and services level. Large corporations, thus, lose their edge not to their competitive peers, but to technology startups who inflict death by a thousand cuts. What is really interesting is that these startups are not trying to disrupt big companies, the big companies just become collateral damage.

The 3 Horizons model no longer applies.

A turn-of-the century framework presented in the Alchemy of Growth, was popularized as Three Horizons of Growth by Steve Coley at McKinsey, to manage for current performance while maximizing future opportunities for growth. One representation of this model is the Innovation Ambition Matrix to help companies allocate funds among growth initiatives.



Horizon 1 provide continuous innovation to a company's existing business model and Core capabilities in the short-term by upgrading them. Such innovations draw on assets the company

already has in place. Coke's Diet Coke reformulation, or Tide's single-serve pallets are familiar examples.

Horizon 2 encompasses Adjacent opportunities, to extend a company's existing business model and core capabilities to new customers, markets, or targets. A wireless charger for a smartphone is an adjacent product for Samsung, and the Retail Store from Apple is another example. In fact, it is also an example of economics of complements where allowing third parties to compete on accessories, only adds value as the accessories can only be used with Apple's core product . Adjacent innovations require fresh insights into customer needs, technology trends, and market structure to leverage existing capabilities to new uses.

Horizon 3 is the transformational creation of new capabilities and new business to take advantage of, or respond to disruptive opportunities or to counter disruption. They require that the company to call upon unfamiliar assets, and capabilities. The favorite examples of transformational innovations from a big company are Apple's iPhone, and iTunes that sold unbundled songs in packages of one.

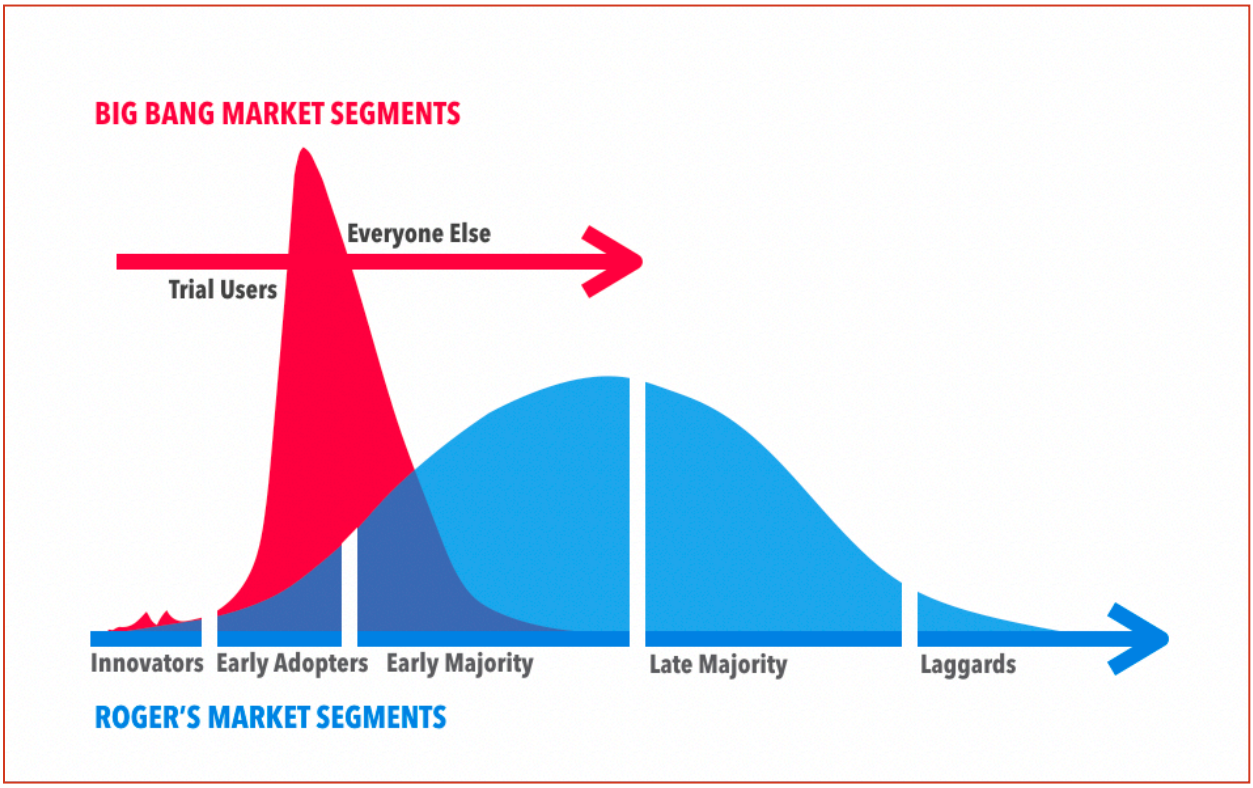
Three Horizons model suggested that to remain competitive, a company allocate its resources across all three horizons. It assigned relative delivery time to each of the Horizons — Horizon 1 as new features that could be delivered in the short term of 3 to 12 months, Horizon 2 as business model extensions that will be ready 24 to 36 months out, and Horizon 3 as creating new disruptive products or business models 36 to 72 months out.

Steve Blank argues in a recent HBR article, that this time-based definition made sense when new disruptive ideas took years to research, engineer, and deliver. But the world has changed, and the three horizons are no longer bounded by time. Today, disruptive Horizon 3 ideas can be delivered as fast as new ideas for Horizon 1. For example, Uber and Airbnb were rolled out extremely quickly. Tesla, and SpaceX are similar where it's the speed of deployment of Horizon 3 products, and express adoption by consumers, that disrupt the status quo. Likewise, many disruptions can be implemented by re-imagining existing Horizon 1 products into new business models such as Software-as-a-Service, and many Horizon 2 disruptions can be absorbed, licensed or co-developed

This time-horizon perspective is still valuable for a company to ensure that its franchise will endure and grow over the long term. Ironically, what gives attacking disruptors the advantage is that established companies invest most of their resources in existing products, or Horizon 1.

Why? because time is not on your side.

The consumer adoption curve for technology-powered products and services has become closer to a straight line that shoots up, and then falls rapidly when saturation is reached, or a new disruptor appears. Accenture calls this Big Bang Adoption, which collapses Everett Rogers' classic bell curve of five distinct customer segments—innovators, early adopters, early majority, late majority, and laggards into only two groups: trial users, and everybody else.



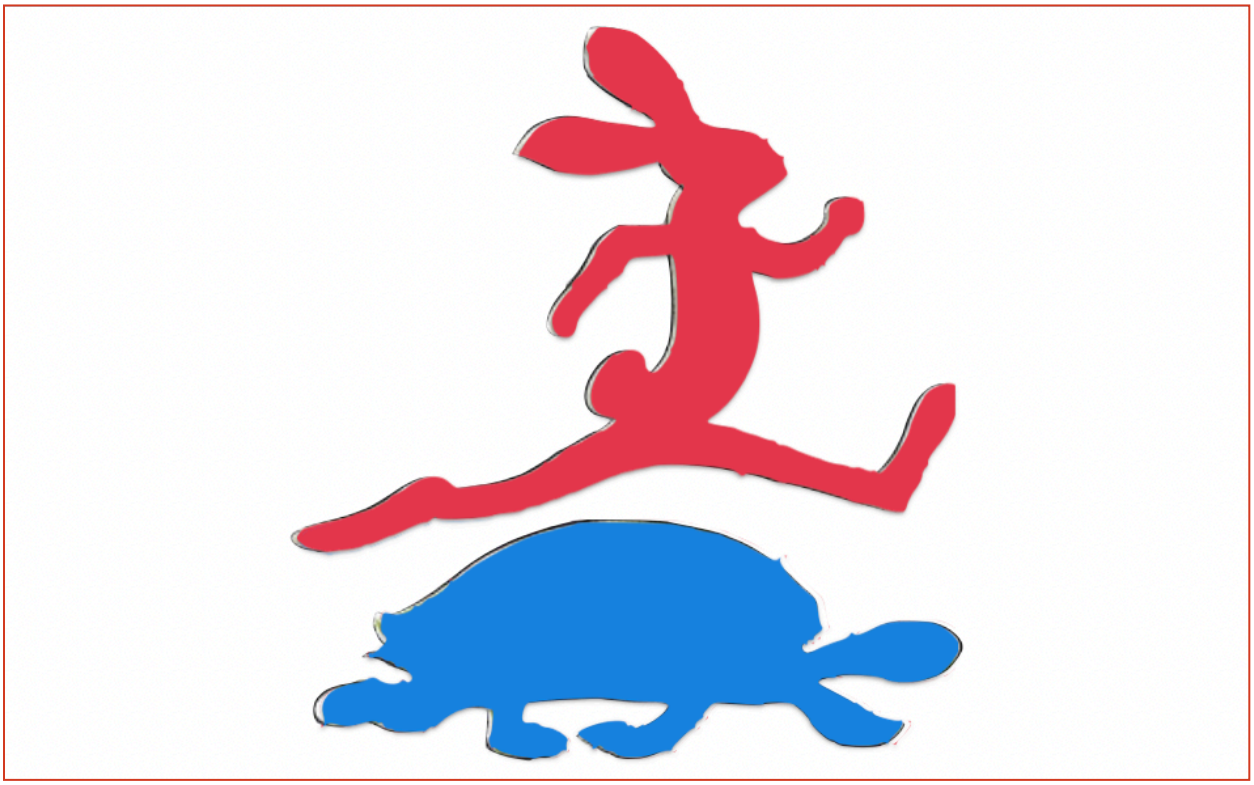
Big Bang Disruption begins with a series of seemingly random experiments, as innovators work with different combinations of component technologies and business models. Most experiments fail, giving incumbents the false sense that disruption is still far off. Yet, when the right combination of technologies is combined with the right business model, take-off is immediate. Customers adopted Skype, Gmail, Facebook, and Whatsapp as quickly as its producers supplied it, and each made the adoption curve steeper than before.

Likewise, consider the adoption of Yelp, Square, AirBnB, and Uber. Neither followed the classic disruption model, entering as a cheap substitute to a high-end product, and then gradually improving quality to move up the customer chain. Instead, they beat incumbents on both price and quality right from the start and quickly swept through every customer segment. Once launched, these innovations don't adhere to conventional paths or normal patterns of market adoption, and that makes them incredibly hard to combat.

Internal R&D can't keep up with startups.

Most large corporates can't compete with startups when it comes to speed and efficiency of breakthrough innovation. Current corporate organization structures, and innovation strategies cannot keep up with the rapid innovation pace that startups dictate.

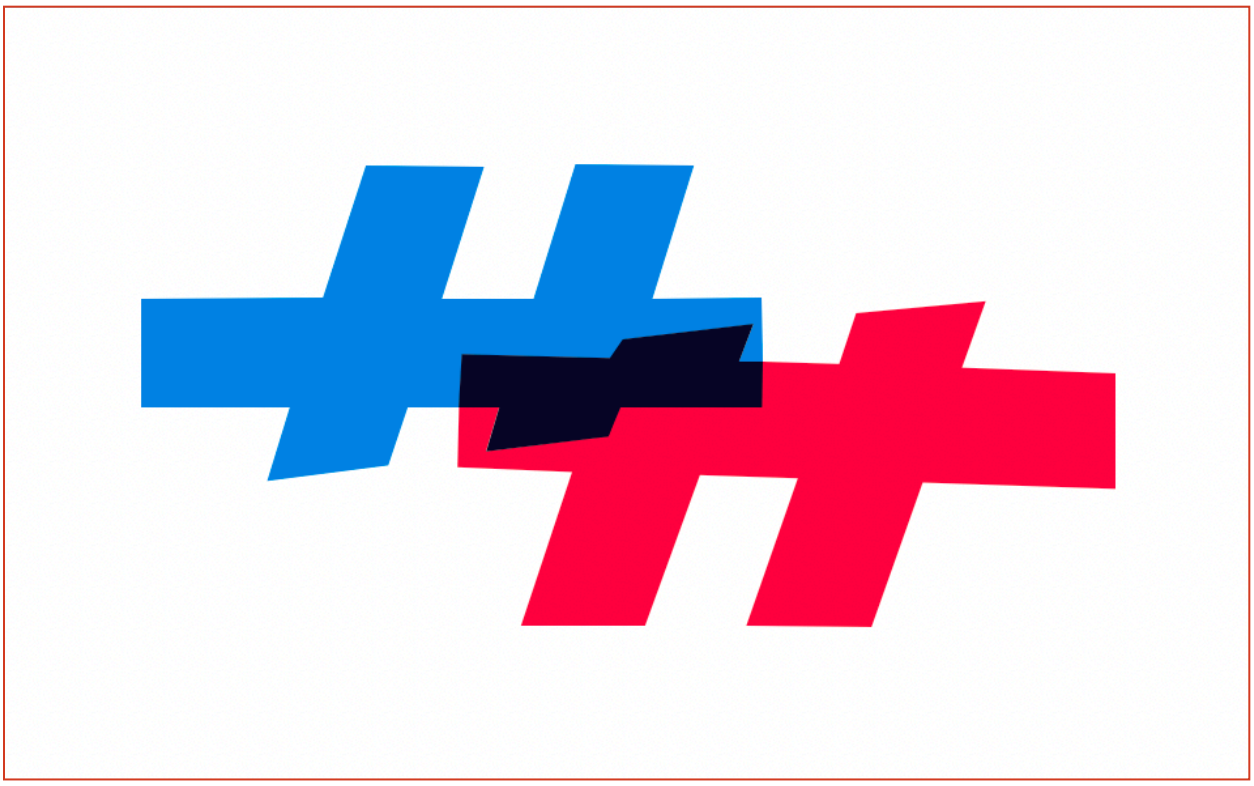
This is because big companies are typically not good at adapting to new circumstances and changing themselves, but rather big machines optimized for the efficient execution of processes, and delivering quarterly results. And that comes with rules and regulations that make it hard to innovate in a true startup spirit, which needs flexibility, an attitude for experimentation, and an environment that supports it.



Traditionally, big companies had two ways to stay relevant and competitive: internal development and acquisitions. Internal development can leverage its strengths, but struggles to keep up with the pace of startups because of the process overhead, for compliance and governance. Startups are the exact opposite. They can operate in garages, pay engineers in dreams, and move at software speeds. Further, internal R&D teams often can't keep up with the speed of exponential technologies such as AI, ML, Nanotech and 3D printing. The venture-funded startups simply outrun them by launching new products faster than a corporate committee can agree on the business case.

Traditional M&A faces many challenges.

Acquisitions can bring the incumbents the innovations and the innovators. Limited due diligence by a large corporate cannot separate the spinners a from the winners, and by the time market exposes potential winners, sky-high valuations make accretive deals difficult. Few, who end up acquiring these fast moving startups, are often unable to fluidly integrate and align them. This delays scale and market outcomes.

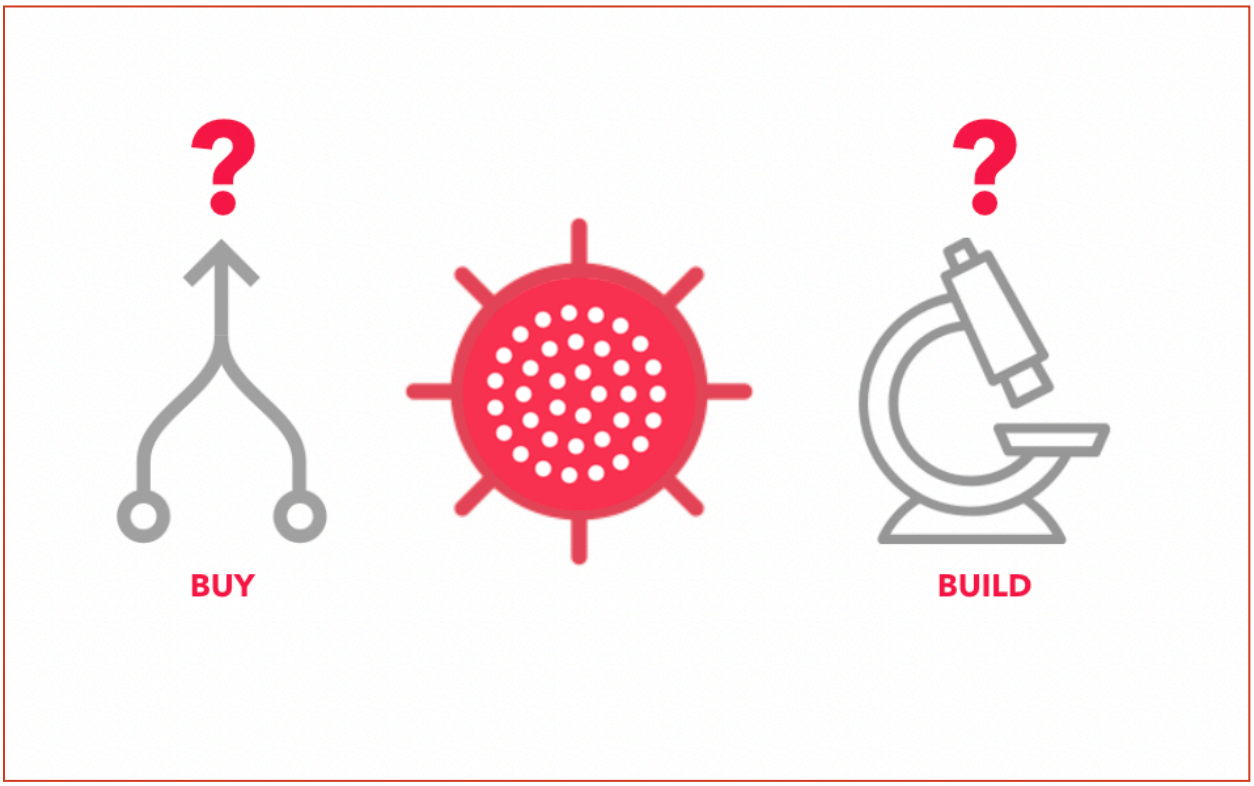


More recently, big companies have tried to resolve these internal conflicts with Corporate Incubators, or Innovation Centers. They create a new division, and place them in a separate building, where their employees can work on innovation projects. This is all nice and shiny, but unfortunately it doesn't solve the innovation challenge. Because, even in these corporate innovation centers, there is no escape from the corporate culture and immutable policies. It is hard to persuade their best people to commit to high-risk projects. And harder to get buy-in for initiatives that might cannibalize existing, profitable products. Thus, just by putting employees into a different organization unit and building, doesn't suddenly give them an entrepreneurial attitude that's needed for disruptive innovation.

In summary, Internal R&D, Acquisitions, and adopting startup techniques, have not delivered much effect. And across industry verticals, it is easy to find new, small, and agile players that are outcompeting the large, but slow incumbents.

Can a big corporation remain resilient?

Innovation, at its core, is about solving problems, and there are as many ways to innovate as there are different types of problems to solve. Innovation is also, at its heart, a resource-allocation problem. A portfolio of innovation strategies and investments is needed but retooling for innovation with multiple tools and methods can be extremely challenging. Individually each piece — the crowdsourced idea contest, the internal venture fund, the idea accelerator, internal R&D — makes sense, but the whole is less than the parts. These can't be isolated initiatives; they must work in harmony.

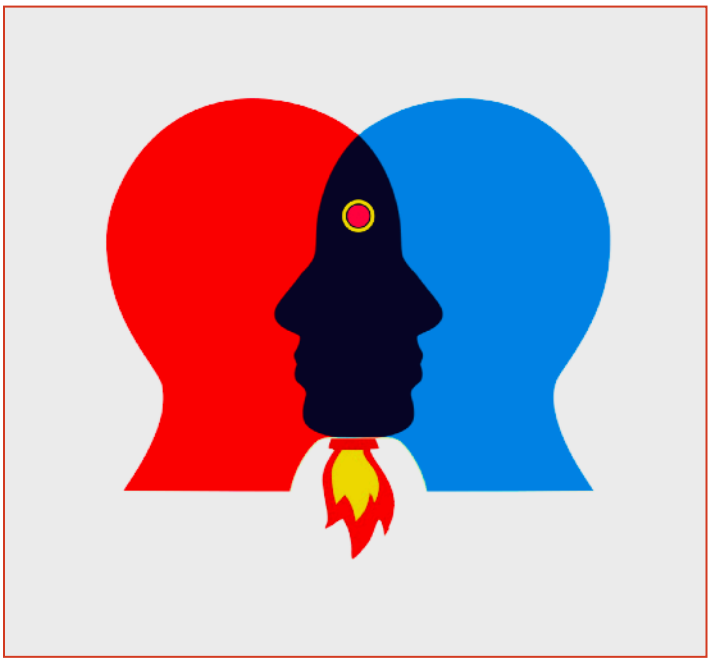


For example, Digital technologies fuel new business growth because they can change the sources of customer value and the cost of delivering it. Is there a way to innovate that is also a means to transform, and not just to grow.

In other words, can a startup with a new product, technology or a business model be both a platform for growth and transformation? Can it provide new models to capture value and monetize, and inform new ways to create and distribute value? We think this is possible through a purpose-built Startup.

There is a better interface possible between the corporate and startup worlds to iterate for innovation-led growth. And improve the chances of success, relative to the success of traditionally modeled startups, or corporate innovation efforts based on Three Horizons.

The Purpose-built Startup



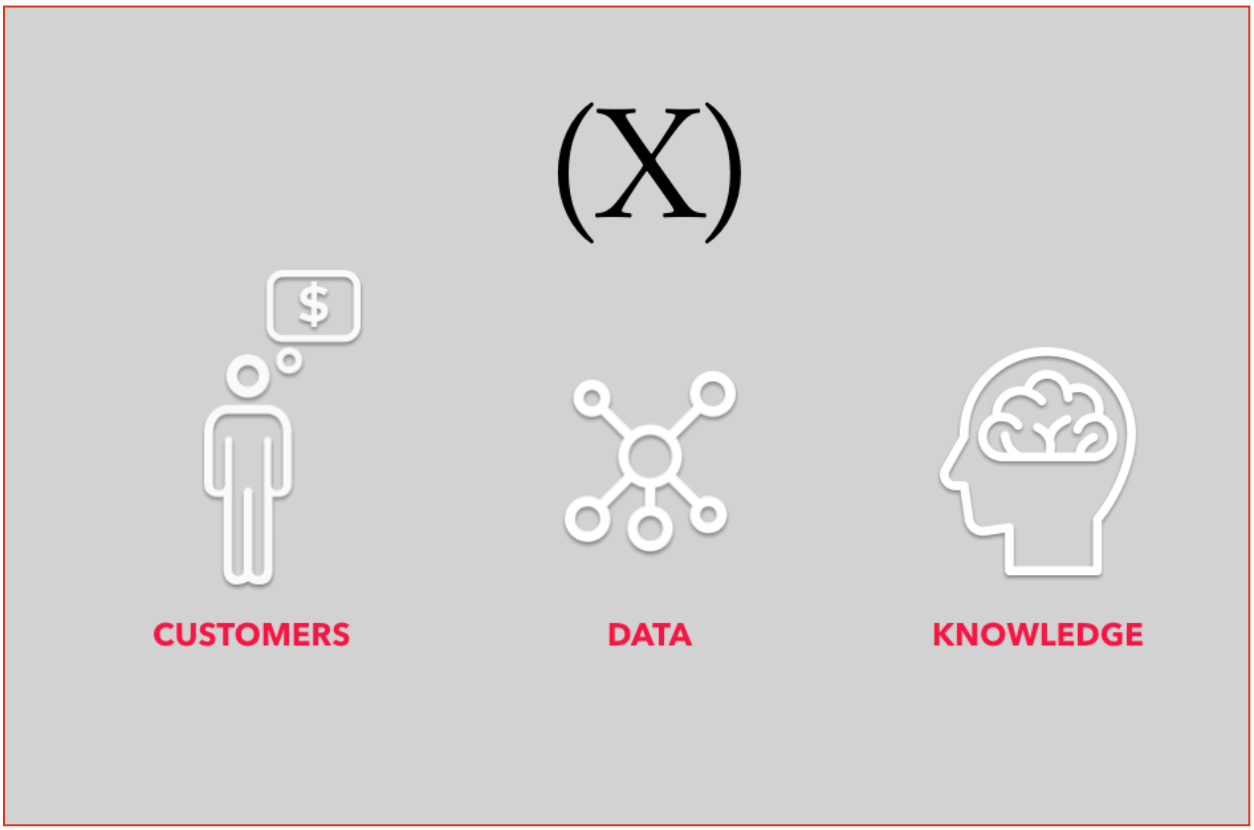
A large company and a Startup can enjoy a synergistic relationship. A Startup excels at going from Zero to One, and the BigCo is adept at scaling it from One to Hundred. Together, they can operate in a Keiretsu, to create new value in a highly cost and time-efficient manner by harnessing each other's core strengths.

It results in a new business that takes the agility and creativity of a Startup, and enables it to leverage the foundational assets of a big company — its Customers, Data, Knowhow, APIs, Talent, and Best practices. This combination of startup talent and big company assets is what we call a purpose-built startup. A configuration that is designed to be integration-ready in terms of business, technology and culture.

Might we look at the components of a Purpose-built Startup?

1. Start with the Foundational Assets

Before creating a new startup, the first strategic question to be answered is strategy in terms of costs, and differentiation. What will give the startup an unfair advantage relative to other startups in the running. For example, consider the success of Amazon in creating new businesses. It is a large corporation that has consistently leveraged its three foundational assets to provide an inimitable differentiation to its new ventures from Cloud Computing(AWS) to Logistics, to Food and Drinks, and now Pharma.

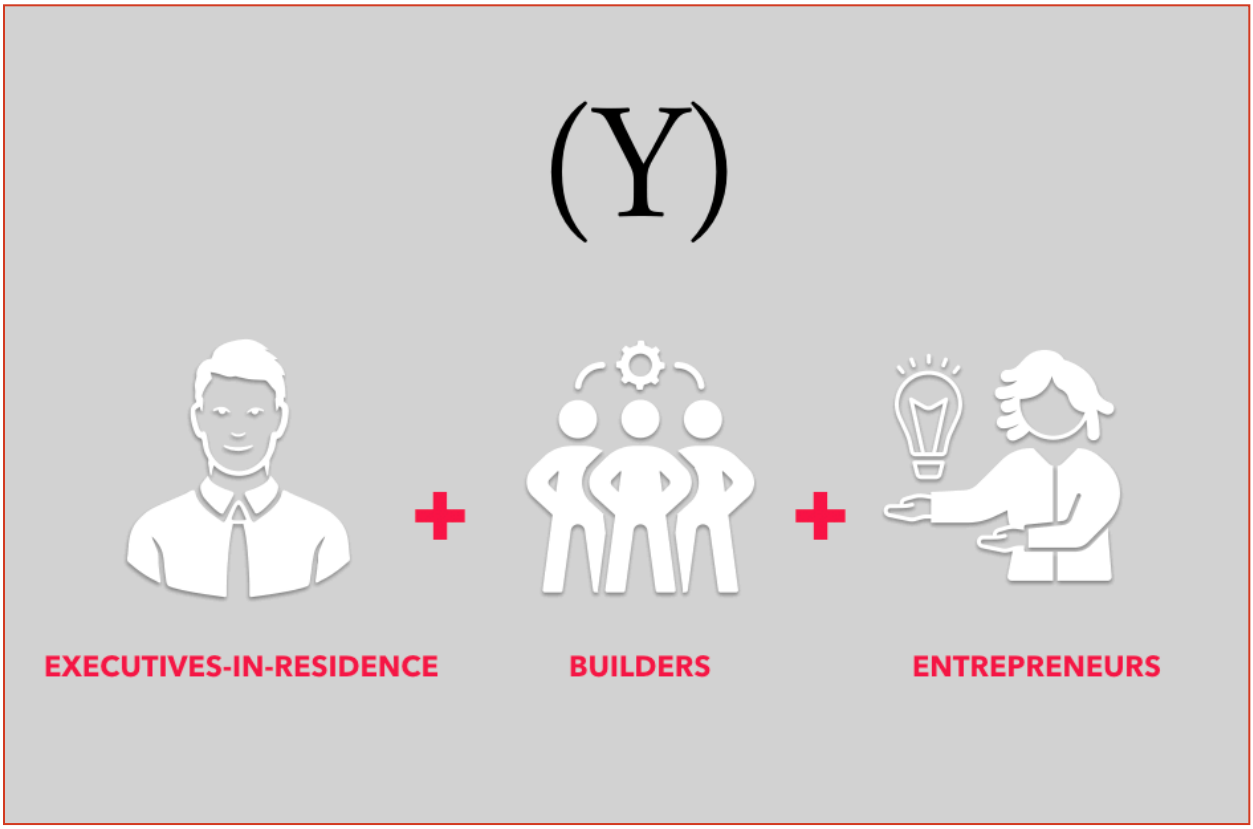


They include Customers, Data and the Distribution Network of Amazon. Let's look at Amazon Prime, as the core driver of its Distribution Network. Amazon has about one hundred million Prime customers globally who tend to buy three to four times more than non-Prime customers because they are less price sensitive. Knowing these customers in terms of their viewing, and buying history, their brand preferences, etc. gives Amazon deep insights that can be used to distribute any new product to them, from Shoes to Food to Medicines, and jump start any new service from Streaming Media to Cards and Payments.

In summary, foundational assets of a big company can provide an inimitable differentiation to a purpose-built startup. These assets include Customers, Data Insights, Know-How and IP, Distribution Capabilities, Brand strength, Buying Power, and Negotiating leverage.

2. Combine Startup and Corporate Talent

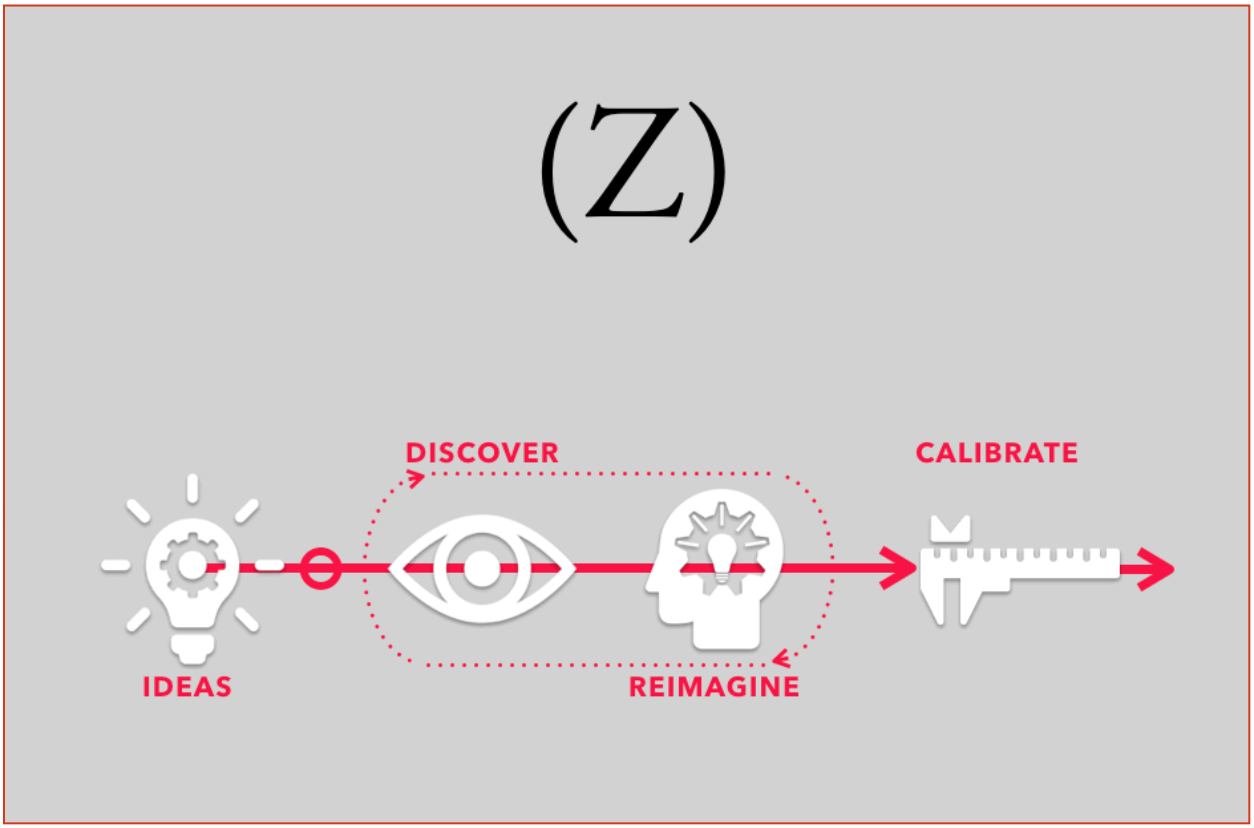
The next component in the Purpose-built Startup is the talent pool to make the venture successful by design. It includes Startup Talent, the builders who are willing and able to build startups, and the Executives-in-residence from the big company who understand the needs of their potential acquirers. These EIRs are the hackers, troublemakers, the ones who don't want to see the box. The Startup talent is typically sourced from the outside and it includes the entrepreneurs, designers, the product and the engineering resources.



Together, they have the ability to quickly innovate, build and test new products, and that gives the purpose-built Startup more flexibility than a traditional startup model. And the EIRs bring the ability to consume and integrate the startup with the mothership post M&A.

3. Calibrate the Right Opportunity

The combined team works together without the constraints of the parent company to come up with dozens of ideas. The ideas are iterated with agility for new value. Together, they discover, reimagine and calibrate opportunities with a future acquisition in mind.



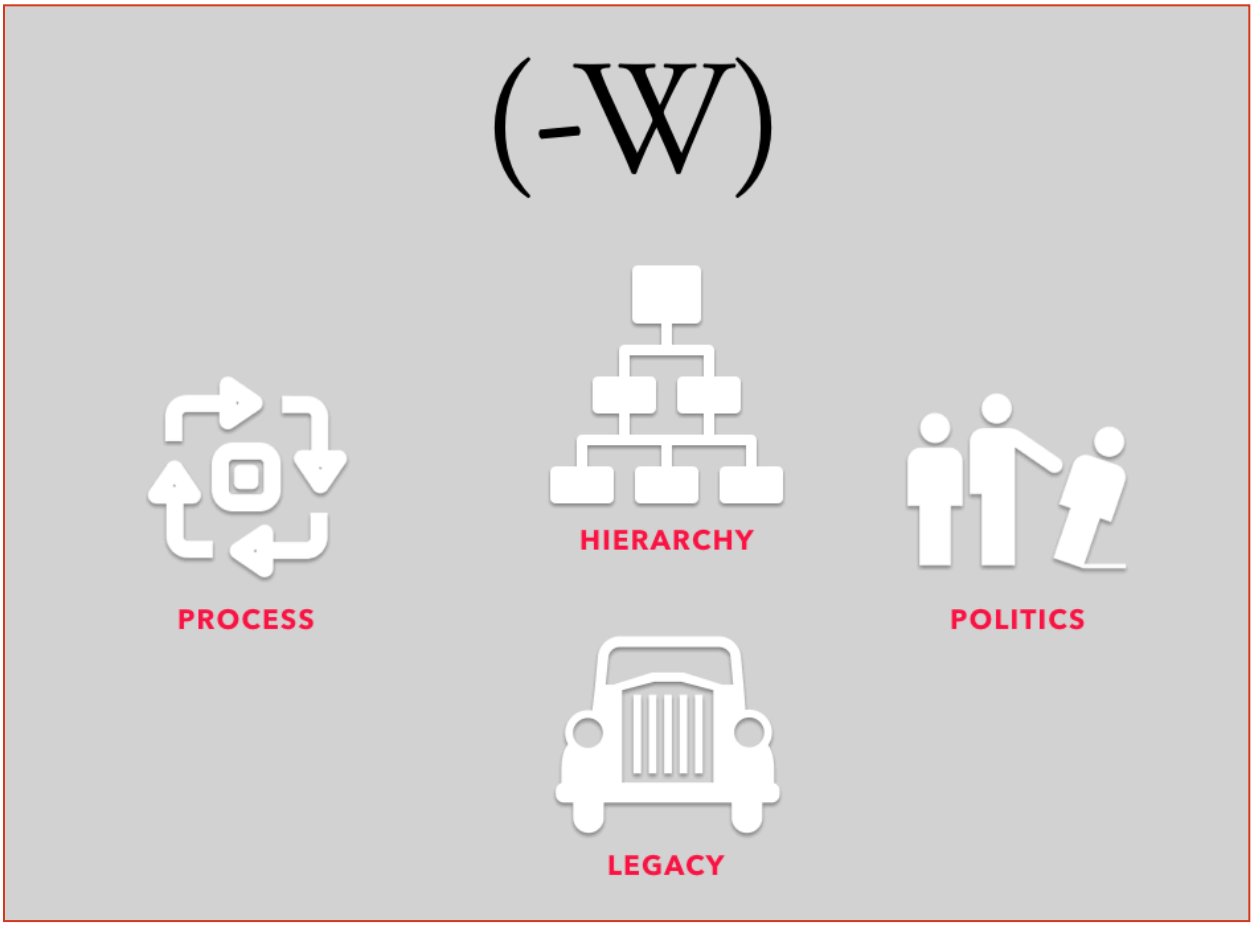
Discovery targets opportunities at the intersection of a new market that can be unlocked in incremental steps, a technology model that can take advantage of the foundational assets, and a path towards monetization. It includes exploring the solution space by analyzing incumbents and challengers that are focused on the target opportunity and market segment. The analysis is often done using a market map to develop a considered view of the problem and solution space observed through the lens of customers, their current providers, emerging startups, and the relationships in the ecosystem.

The business, technology, and experience architecture is re-imagined and informed by the foundational assets. The process unifies all constituents and audiences around the common set of goals by iterating on concepts and designs to improve the experience of getting to the desired outcomes.

This new "company within the company" is then calibrated by doing a proof-of-concept to validate all assumptions including those related to its integration into the parent organization.

4. Remove the unnecessary burdens

Most large corporates can't compete with startups when it comes to speed and efficiency of breakthrough innovation. This is because they are typically not good at adapting to new circumstances and changing themselves, but rather big machines optimized for the efficient execution of processes, and delivering quarterly results. And the big machine comes with rules and regulations that make it hard to innovate in a true startup spirit, which needs flexibility, an attitude for experimentation, and an environment that supports it.



It easy to create these conditions within a startup, but not in a big corporation. Why? A startup is created to break things that can be done better. In contrast, a big company is optimized for stable operations and fulfilling shareholder expectations. The same factors that allow it to run an efficient operation, can also suffocate its innovation attempts. Thus removing the overhead of processes designed for governance and compliances, the immutable corporate policies, and the hierarchy are critical success factors for the Purpose-built Startup. This does not mean avoiding regulatory challenges. On the contrary, a Purpose-built Startup enables the big company to conduct experiments in a controlled manner, that might be too risky to run otherwise, where even a total failure won't harm them but bring in new learnings fast.

5. Operate at the speed of software

Given that Software is transforming the way business is done, it makes sense to internalize that all businesses are now in the "software business", regardless the products, services or customers they serve. Much like a software product, a company's ability to stay fresh and evergreen requires it be more like a startup — modular, adaptable, agile and reconfigurable. Therefore, Purpose-built Startups are structured as agile software teams working towards continuous delivery. It creates and deploys products, observes, measures, learns, and optimizes at the speed of software.

To support this rapid iterative optimization, teams are aligned, and rewarded for agility and continuous iteration for value. They are tasked to solve a business problem, with an objective, and a measurable goal that determines its success. This includes the mindset of the team, the processes and tooling that make it easy to be acquired and integrated into the larger organization.

An outcome-driven, Purpose-built Startup establishes a cadenced resilience into the way it makes decisions, allowing it to make short commitments and then further those commitments or not, based on real-time market-based realities as opposed to lofty predictions of a future state that may never come. The result is a more efficient way of creating new value, achieving high levels of cost-efficiency and shortening cycle time.

6. Resilience through new Growth Vehicles

Businesses and work-systems are becoming more open and decentralized, more startup-like. The resilience mandate depends on a company's ability to innovate, and presents an opportunity for it be more like a startup — modular, adaptable, agile and reconfigurable. Therefore, a big company needs to update its products, services and business model like a startup.

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Purpose-built model is a new way of building new products and services. It improves the chances of success because Purpose-built Startups are acquisition-ready by design to enable business, technology and cultural integration. They enable corporations to keep their products, services and business models up-to-date the same way as SaaS keeps software up to date.

This framework provides a better interface between the corporate and startup worlds. It brings decision makers on the corporate side who understand how entrepreneurship and startups work as well as the assets of the corporation.Partnering with startups in this new configuration empowers established companies to maintain their core while innovating like a Startup.