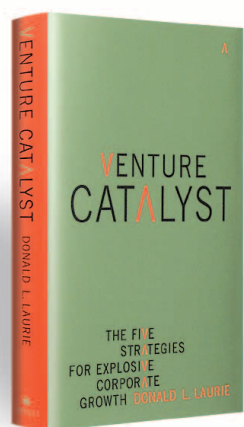


SOUNDVIEW Executive Book Summaries®



By Donald L. Laurie

The Five Strategies for Explosive Corporate Growth

VENTURE CATALYST

THE SUMMARY IN BRIEF

Business leaders have two missions: first, meet or beat Wall Street expectations on a quarterly basis; second, roll out the new technologies and products that will ensure continuous double-digit growth (as measured by market capitalization and the creation of shareholder wealth) over the next three to five years. Internal organic growth or traditional acquisitions and mergers cannot yield the kind of double-digit growth now being sought by investors. According to author Donald L. Laurie, only those companies that include ventures as an integral part of their strategies can achieve exceptional and sustainable growth. By ventures, Laurie is referring specifically to “new business enterprises that entail a certain amount of risk.” After extensive interviews with corporate leaders of both high-growth companies and venture capital firms, and drawing on his own experience as a high-level corporate advisor, Laurie identified the five key strategies for developing the next great business: invent, invest, venture, partner and integrate.

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What You'll Learn In This Summary

- ✓ **Inventing New Businesses:** Close to 90 percent of Corning's revenues come from products invented within the past five years. You'll learn the step-by-step process that Corning uses to create these new products.
- ✓ **Investing in New Businesses:** Investing in new businesses offers a short-cut to new technologies and processes.
- ✓ **Building a Venture Division within Your Company:** You'll learn how to develop a strategy to use when working with venture capital firms.
- ✓ **Creating Partnerships to Build New Businesses:** Take your latest technology developments to an experienced “business builder” and you both can win.
- ✓ **Acquiring and Integrating New Businesses:** Pairing up with another company pursuing similar product developments will create powerful synergies.
- ✓ **Case Studies in Venturing.** Five case-study companies will illustrate the five venture strategies: invent, invest, venture, partner and integrate. The case studies cover business models, value-added activities and preconditions for success.

VENTURE CATALYST

by Donald L. Laurie

— THE COMPLETE SUMMARY

Five Paths to Sustainable Corporate Growth

Explosive yet sustainable growth depends on a “venture” mentality — the desire to boldly build the next great business. Based on his research and experience, author Donald Laurie found five distinct routes to using ventures as a means of fueling corporate growth:

- 1. Invent the next great business.** In this strategy, a new business is “born and grows under the corporate roof,” according to Laurie.
- 2. Invest in the next great business.** A number of companies are establishing in-house corporate venture groups that commit the company’s money and resources to entrepreneurial ventures.
- 3. Venture the next great business.** Companies that follow this path collaborate with venture capital firms on new businesses.
- 4. Partner the next great business.** Independent and distinct companies can establish partnerships that create new businesses.
- 5. Acquire and integrate.** Acquisitions can help companies integrate new capabilities, know-how and technology.

Critical Factors

In each of these five venture strategies, three factors are crucial.

First, the company must have a clear **business model** of how it will build a new business and how it will generate revenues.

Second, the company must have unique **value-added activities** that make its business model work.

Finally, each company must recognize that certain **preconditions for success** must be in place. For instance, every venture strategy requires capital and a forward-looking leader, as well as space for innovation and compensation that encourages risk-taking.

Each of the firms researched followed a well-developed, step-by-step process for creating growth.

The Rewards of Entrepreneurship

Through ventures, both large and mid-sized companies can develop the strategies needed to maintain a

Laying the Groundwork

Large corporations who want to move from their traditional, cautious strategies to growth strategies built around ventures must be ready to:

- **Change their corporate mindset.**
- **Redefine their concept of organization.**
- **Alter their need for control.**
- **Expand their capacity for speed.**
- **Broaden their tolerance for mistakes.**
- **Modify their risk potential.**
- **Shift a portion of their investment capital from incremental R&D to internal and external ventures.**

By partnering with entrepreneurs, who have experience with quickly moving a product concept to market, a large corporation can leverage its distribution, marketing and research capabilities, for a synergistic effect that can lead to phenomenal success.

high level of innovation and growth. The process is daunting, since it requires adoption of an entrepreneurial spirit among all levels of management (see above). But the rewards are clear. Johnson & Johnson has seen its annual revenues increase from \$11 billion in 1989 to almost \$29 billion by 1999 since dedicating corporate resources to venture activity. ■

The author: Donald L. Laurie is founder and chairman of Laurie International and of Oyster International LLC. The author of *The Real Work of Leaders*, Laurie is an advisor to industry leaders and an investor in early-stage ventures.

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Invent the Next Great Business

Companies that know how to leverage their expertise in technology, marketing and manufacturing capabilities are the ones who can succeed at regularly inventing the “next new thing.” For example, 84 percent of Corning’s revenue comes from products that did not exist five years ago.

In this article, we will study Corning as an example of how to invent the next great business.

Corning’s Business Model

Corning’s corporate motto, “Discovering Beyond Imagination,” captures the belief that the highest ROI on new products will result from those that directly address unmet, unserved customer needs. In focusing on this motto, Corning is not afraid to get rid of divisions that are no longer performing or have begun to decline, including its one-time flagship Corningware division.

Corning uses five steps in nurturing an idea into a product:

1. Building Knowledge. By participating in cross-functional “roadmap” teams of technicians and managers that meet regularly, employees develop a common view of trends, discontinuities and other events that are shaping the future. Each member relates these trends to customer needs, and identifies what each of their products brings in relation to those needs.

Road-mapping helps Corning identify the product specifications for next year’s products — as well as the technologies it will need to build or acquire within the next five-year period in order to develop the products of the future.

2. Determining Feasibility. Once the idea and technology are selected, Corning involves its customers and in-house staff in experimenting with proposed applications that could evolve from the combination of the two.

At this stage of the venture process, Corning addresses these questions:

- Will the technology achieve the intended objective?
- Can the idea be developed into a product with significant market potential?
- Can we achieve proof of concept?
- Can we build a working prototype?

3. Testing Practicality. When this stage is reached, cross-functional teams in marketing and manufacturing, as well as research, test a prototype product to decide whether there is a substantial market, whether the price-to-value is acceptable to the customer, if it can be manufactured in volume — and ultimately, whether Corning should continue to pursue the development of the product.

Is Your Company Ready to Invent the Next Great Business?

If you want to invent the next great business, you must do the following:

- ✓ **Assess your company’s history of innovation, its experience and its culture.**
- ✓ **Define the company’s ambition for internal ventures.**
- ✓ **Rethink organization and control models.**
- ✓ **Commit capital and define the investment decision process.**
- ✓ **Create infrastructure and support.**
- ✓ **Understand the venture process.**
- ✓ **Let the entrepreneurial team members select themselves.**

4. Proving Profitability. Just because a new product idea is possible doesn’t mean that Corning will develop it. Corning must first determine the profitability of the idea. For example, teams study whether the company will have any advantages in either technical competencies or cost leadership.

5. Commercializing. Almost as soon as a new product is launched, Corning takes it back to the drawing board. The product’s manager takes responsibility for extending the line and looking for new breakthrough businesses.

Corning’s Value-Added Activities

Corning’s dedication to a culture of innovation and attracting and keeping top talent are central to its enviable track record of creating successful new products and businesses.

The company uses — and supports — the accumulated wisdom and experience of its highly talented work force. For example, it periodically holds informal “Growth Day” exhibitions. At these events, the company’s entrepreneur-managers present their products and businesses. The goal is to support their efforts, not review them. Rather than scrutinizing their budgets, top management asks them what they need.

Corning also understands the value of keeping smart people; in addition to its state-of-the-art facilities and resources, it offers an attractive compensation plan.

Corning’s Preconditions for Success

A top-down belief in creating conditions that allow its employees to be entrepreneurs is one of the preconditions for Corning’s success in creating new products and spinning off new businesses. As well as its culture of

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Invent the Next Great Business

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innovation, Corning holds its employees accountable: Bonuses are tied to performance.

Another fact that cannot be overlooked is the relative health and growth of the telecommunications industry, the members of which make up a significant portion of Corning's customer base. ■

Invest in the Next Great Business

After inventing, the second strategy for explosive corporate growth is investing in the next great business.

Venture capital spending, in which companies commit capital and other resources to independent, external ventures, is experiencing rapid growth. In the period from 1996 to 1999, for instance, the number of companies investing in external ideas jumped from 30 to 330, as the amount corporations spent on these investments soared from \$100 million to \$17 billion annually.

There are strategic and financial advantages to taking this path — for both the corporate investor and the entrepreneurial companies. The corporation can gain new technologies and related applications, as well as exposure to new markets; the entrepreneurial company can gain status and acceptance by aligning itself with a larger company.

Case Study: GE Equity

GE Equity, one of 28 business units within GE Capital, invested almost \$4 billion in 300 businesses in 2000, only five years after it was created. Forty percent of those 300 businesses grew out of opportunities within GE itself: Individual GE employees, or divisions, brought their ideas to GE Equity.

GE Equity's purpose is to help GE businesses grow, and to provide a buffer for GE should its earnings slip. If that happens, GE Equity would be able to liquidate selected holdings and "fill the gap."

GE's Business Model

As seen with Corning in its invention strategy, developing and adhering to a strict, step-by-step process is central to GE Equity's success in venture activity. Called the Business Management System, or BMS, GE Equity's process begins with a thorough due diligence procedure, which includes an investment overview (covering investment rationale and considerations), an industry and company overview, and a description of the target company's marketing strategy and value proposition. This thorough process reveals each invest-

Is Your Company Ready to Invest in External Ventures?

If you want to invest in external ventures as a strategy for corporate growth, you must do the following:

- ✓ **Assess your company's readiness and ambition for corporate venturing.**
- ✓ **Define your ambition and priorities.**
- ✓ **Determine the role of operating units in your investments.**
- ✓ **Develop management capabilities and systems.**
- ✓ **Be explicit about strategic benefits.**

ment prospect's top two or three risks, and evaluates its management team.

After the due diligence process is completed, the next step in the BMS is a portfolio management system to track the expectations and performance of each investment prospect.

Each prospect is coded according to performance level. Red is the most underperforming classification; companies that are coded red undergo more rigorous monthly reviews by the general manager, risk manager and investment manager.

At the same time, a financial management system is instituted so that management can allocate investments across industries and stages of investment. This financial team focuses on anticipating liquidity events so that GE Equity is able to deliver specific quarterly results.

GE Equity's Value-Added Activities

What are GE Equity's value-added activities that have made its investment strategy a success?

GE Equity's excellent analytical process is based on both decision and probability theories, and is applied systematically to its investment strategies and decisions. The company is committed to working with "the most knowledgeable people in the industry and the company — people who can provide their probability assessments on certain key variables," according to a company spokesperson.

And it parlays this analysis to managing investment portfolios as well.

GE Equity's Preconditions for Success

GE Equity's preconditions for success include an unambiguous commitment and genuine "fondness" for entrepreneurial ventures — from the top down. Furthermore, GE Equity does not dominate the companies in which it invests — instead, it supports and respects these smaller companies consistently. ■

Venture the Next Great Business

If your company is not prepared to become an investor, another approach is to build strategic partnerships with experienced venture capital firms.

There are two dominant routes to pursue. In the first, you become a passive investor and will either make or lose money as the fund is liquidated over its 7- to 10-year lifecycle. As a limited investor, the corporation has limited exposure to deal flow and does not participate in investment decisions.

In the second route, corporations can become limited partners in industry-specific ventures funds (i.e., health care, information technology). Using special rights agreements, some companies have been able to gain early access to venture capitalists' deal flow, which opens up opportunities to invest either independently or alongside the venture firm. The advantage with this second route is the ability to locate new emerging technologies sooner.

Many venture capitalists are the first to spot innovative, early-stage ventures that large corporations would otherwise rarely discover on their own. In addition, venture capital firms have expertise in matching deals with each corporation's strategic goals and have access to a continuous deal flow. Corporate scientists' deep understanding of technology and science is a good match with venture firms, who are well-versed in creating deals and building businesses with speed.

Nortel Networks invests with a select group of venture capitalists in the telecommunications industry, and is used here as an example of how to pursue this strategy to corporate growth.

Nortel's Business Model

Since it became independent of AT&T and Bell Canada in 1976, Nortel's core competency has been its ability to continuously seek out "discontinuities" in either markets or technologies. Because its executives realized that the most disruptive, cutting-edge technologies were at small start-ups and venture capital funds, it chose to target this type of firm. Additionally, Nortel was uniquely poised to reap immense benefits by matching its knowledge and know-how in data transmission with innovative ideas from telecom start-ups.

Nortel's strategy involves seeking companies that it can eventually acquire, partner with or develop as customers or original equipment manufacturers (OEMs).

Nortel's Relationship Network

To maximize its venturing strategy, the company formed a two-person team to create a systemized method for approaching investments.

Is Your Company Ready to Invest with Venture Capital Firms?

If your venture strategy includes investing through venture capital firms, you must do the following:

- ✓ **Clarify your investment strategy and your purpose in investing.**
- ✓ **Determine the level of capital and the venture leader in whom you are willing to invest over the next five years.**
- ✓ **Define the characteristics of attractive venture partners and your value added.**
- ✓ **Leverage your learning.**

The team first devised a filtering method to gain access to the greatest number of deals through the least number of venture capital firms.

Starting with the 100 or so venture capital firms in the telecommunications field, the team identified the venture capital keiretsus, loosely formed groups that invest together. It then narrowed the 20 top venture capital firms in its industry down to less than 10 firms that appeared most able to match Nortel's goals. Each of these was a leading venture capital firm in its keiretsu. Today, these firms are the basis for the company's "relationship network" that allows it access to close to 95 percent of the innovations in its industry.

From this initial strategy the company has formalized its venture investment policy, naming 11 directors of business development to work with the venture capitalists. In a four-page letter of agreement with each firm, Nortel's expectations are clearly defined, including any preferential treatment the company requires, the services the VC firm will get in return, and the information in the VC firm's deal flow that Nortel will be able to access.

Nortel's Value-Added Activities

Nortel's side-by-side collaboration — through its relationship management, screening and selection process and its emphasis on acquiring entrepreneurial firms — are the back up to its business plan. Its business unit directors, with specialized skills in both technical and financial areas, offer a good balance to the VC's ability to take risks.

Nortel's Preconditions for Success

Nortel shares its know-how in technology. The VC firms, in turn, act as the eyes and ears for any companies that might make a strategic match for Nortel. In addition, Nortel allows any of its VCs 30 days exclusive consideration for any company that Nortel spins out from its internal venture program. ■

Partner the Next Great Business

Because of the need to manage current operations and budgets, many executives often overlook the vast potential of their companies' intellectual property and technology. As a result of this oversight, exacerbated by an unwillingness to share proprietary information with other companies, company leaders miss opportunities to use partnerships to create new, disruptive businesses — either profitable spin-off businesses or businesses in their competency — that have the potential for explosive growth.

By partnering technology or know-how with experienced business builders, companies can stake a claim in next-generation platforms, products, systems and services.

For example, a consumer products company with cleaning technology contributed its knowledge and capital to a start-up that was managed by experienced business builders, who received a 20 percent of the new business as well as a business-building fee.

To illustrate how partnering can help achieve corporate growth, this article will look at XL Vision, Inc.

XL Vision: Creating an Enterprise Factory

Within four years of its founding, XL Vision had created \$3 billion in new wealth and five companies, two of which had gone public. Unlike most “incubator” models, XL Vision considers itself a long-term holder in the companies it creates. Its business model is based on the relationships it creates with Fortune 100 companies, and on its ability to leverage technology from these large global companies.

Like the other companies detailed in this summary, XL Vision has developed a systematic approach to building new businesses. There are six “imperatives” to XL Vision's business model:

- 1. Bat 100 percent in business creation.** Unlike VC firms, which factor in a 30 to 40 percent failure rate, XL Vision's thorough screening process and due diligence is driven by the goal of hitting 10 out of 10.
- 2. Imbue each new company with a long-term growth strategy based on a solution to a subtle or not-yet-identified customer need.**
- 3. Go for an IPO within three years.**
- 4. Produce at least one new public company every year.**
- 5. Create one new company every year.** Keep the pipeline full; every time one company goes public, start a new one.
- 6. Achieve a \$1 billion market capitalization for each new company within a year of its IPO.** The founders of XL Vision are convinced that it takes

Is Your Company Ready to Partner the Next Great Business?

If you want to partner the next great business, you must do the following:

- ✓ **Make sure that the business idea is unique and disruptive.**
- ✓ **Explore the advantages and disadvantages of going it alone and maintaining total control versus partnering with experienced venture managers.**
- ✓ **Understand what you do well and where you need help.**
- ✓ **Agree on principles and terms that will govern the business relationship.**

just as much effort to build a company with a \$50 million market cap as it does to create one with a \$500 million cap, so they believe in aiming high, building products or companies that will fit within large and growing markets.

XL Vision's Business Model

XL Vision's business model consists of four building blocks: Discovery, Down Select, Strategic Positioning, and Execution of the Plan.

Discovery. XL Vision's expertise is in electro-optics and electro-optical devices for different industries. When a company approaches XL Vision with a need for a new product that XL has the technology to create, they build the product and then turn over all the “discoveries” made in the process of developing the product (i.e., the technologies, intellectual property) to the outside company. XL Vision retains the rights to the intellectual property for other, noncompeting applications. Because it is in constant close contact with customers, XL Vision is able to anticipate unmet service needs that its technology can be used to meet.

Down Select. Because XL selects only one project each year, most projects are rejected. The founders admit it took some time getting used to throwing out so many ideas, but they have come to believe that this is what's necessary to achieve their 100 percent hit rate.

Over the years they have developed the capacity to spot winners by focusing on market size, market growth rate, competition and strength of intellectual property. They also examine not-so-obvious criteria, including technical experiments, alpha product test reports, customer focus groups, partner focus groups and distribution channel analysis studies.

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Partner the Next Great Business

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XL Vision's founders have come up with a 3-to-1 rule. Basically, entrepreneurs must be able to prove to them that the product or service they are proposing will either save three dollars or add three dollars to the bottom line, and that it will only cost one dollar to do so.

Strategic Positioning. An internal start-up team at XL Vision is assigned to the "incubie" while it is still undergoing experimentation with its technology and market position. The team stays with the project for an average of 18 months, during which time it is planning strategy and meeting with customers, and then adapting the product and reframing the strategy as needed.

Execution of the Plan. Now XL Vision names a new director, or "CEO" for the project and the start-up team passes on the project to this person. Different skills are needed for this stage of the process: someone who is focused, driven and execution-oriented.

At the same time, ownership of the new company is being transferred to shareholders via a process that allows for tax-efficiency as well as setting the stage for a long-term relationship. By selling the shares as cheaply as possible, XL Vision provides a very low-risk option with a high-gain potential to the shareholders. By allowing its corporate partners to buy a share of the venture, it is motivated to continue with other productive business relationships.

XL Vision's Value-Added Activities

Being market-oriented has allowed XL Vision's founders to continually leverage their technology to create new products that fill unmet needs. That, and a disciplined process for integrating the skills of technologists and entrepreneurs, is unique to XL Vision.

XL Vision's Preconditions for Success

A combination of process, analysis and entrepreneurial talent, as well as constant cultivation of its business relationships and its own internal culture, has given XL Vision an edge in building new businesses. Part of building its own internal culture includes monthly meetings of its three-person Innovation Council. At these meetings, members evaluate the company's processes and its results to see if any adjustments need to be made, and implement any that are needed. Attitude and personal drive have also contributed to XL Vision's success. As founder John Scott often says, the company's only competition "is the old way of doing things." ■

Acquire and Integrate the Next Great Business

It is important to distinguish between standard mergers and acquisitions — in which acquirers buy a customer base and established product lines — and the acquisition of cutting-edge ventures to build growth.

Cisco Systems, Inc., recognized early on the benefit of acquiring ventures that could give its own internal research and product development teams a mach-force jump start and yield continual growth for the firm. Almost as an aside, the company's rapid rate of acquisitions also enabled it to find a steady source of talent to support its expansion.

Cisco's Business Model

To achieve its goals of becoming the one-stop shopping source for network connections for the telecommunications industry, as well as becoming the builders of the Internet infrastructure, Cisco looks for companies with engineering talent that is working on cutting-edge solutions. It can then combine the acquired innovation with its impressive sales network.

Cisco clearly defines three overlapping market segments that it targets, and hones in on companies that are offering unique innovative solutions to these markets. The targeted market segments are: large corporations, educational institutions, government agencies and utilities with complex networking needs involving multiple locations and different computer systems; small- and mid-sized companies that need their own intranet data networks, connections to the Internet, and secure data links with business partners; and information service companies (such as telecommunications carriers, Internet service providers, cable companies, and wireless communication providers).

Cisco's Value-Added Activities

Cisco employs its sales force to be its eyes and ears for new opportunities. Internally, it is constantly rewriting software that eases integration of acquired products into the Cisco Systems portfolio, a capability for which it is well known. Attitude also plays an important role in the company's acquisition strategy. Besides believing that it is simply cheaper, quicker and easier to acquire companies that are further along in the research chain with new solutions, Cisco has developed a highly structured procedure for integrating its acquisitions.

Cisco's Preconditions for Success

"Shared chemistry" between Cisco and its acquired company is essential, and a simple exercise for determining a fit is carried out early in the negotiations

For another short example of a partnership venture, go to:
<http://my.summary.com>

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Is Your Company Ready to Acquire and Integrate?

If you want to acquire and integrate the next great business, you must do the following:

- ✓ **Develop technology and product maps.**
- ✓ **Assess the quality, focus and payback of research and product development.**
- ✓ **Define your venture acquisition strategy.**
- ✓ **Build the team to acquire and integrate.**

Acquire and Integrate the Next Great Business

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process. Executives from both companies are asked to write down what they consider to be the three most important benefits that the other will receive from the proposed merger. Another basic premise is that both companies must have a business need that neither can meet on their own. ■

For a case study that applies all five venture strategies, go to: <http://my.summary.com>

Basic Steps in Venturing

There is, of course, no such thing as a fail-safe 10-step process for creating a successful venture. Any success will need the right mix of an attractive market, a committed entrepreneur, a unique idea and so on. However, it is possible to identify five fundamental phases that will occur in a typical, successful business-building process:

1. **Mining opportunities.**
2. **Refining and strengthening the business model.**
3. **Developing the product, platform and business.**
4. **Executing the business-building process.**
5. **Growth.**

Each of these five phases calls for different leaders, priorities, and goals and milestones.

Mining Opportunities

The first step in mining opportunities is to generate ideas. External ideas will come from a variety of sources, including entrepreneurs, investors and other venture capitalists. Internal ideas will come from a company's managers and employees, who can be on the lookout for venture opportunities around the world.

The next step is to screen and rigorously evaluate ideas.

Be sure that you have clear criteria for your new ventures, for example the minimum size of a new market.

Refine and Strengthen the Business Model

Once you believe that you have an idea that might work, you need to refine and strengthen the business model of the new venture.

The first step is to clearly define the problem that the new venture will solve — in other words the strategic logic that underpins the business model.

The next step is to conduct a due diligence of the new venture's market, technology, competition and economics. To put it bluntly: Are you going to make money?

The third step is to look closely at the technology involved. How long, realistically, will it take to get a product ready for prototype and beta testing?

This phase requires a mix of people, including strategic thinkers, venture managers, technologists and people with market and manufacturing knowledge.

Developing the Product, Platform and Business

Early entrepreneurs can guide the initial strategic thinking, development, initial experimentation and beta-testing activities of a new venture. Now, however, is the time to bring in an execution CEO to begin the operations and implementation phases of the process.

The original processes designed to shape the business model and develop and test the initial product must now be replaced with brand, sales cycle, manufacturing and logistics management processes. Recruiting key management, developing the go-to-market strategy, establishing pre-production runs and securing operating capital are just some of the issues that need to be addressed at this stage.

Executing the Business-Building Process.

The business is now operating. Sales, marketing, engineering, manufacturing, finance and planning are in place and working. Sales and marketing people, for example, are getting feedback from the field. Engineering and product development are working with sales and marketing to refine the product based on this customer feedback.

Production people are applying product development and engineering modifications to the manufacturing process. Finally, the finance people should be tracking actual versus projected costs, revenues and return on investment.

Growth

In this phase, you will want to emphasize productivity, efficiency and improvement at all stages in the business cycle: manufacturing, logistics, sales and delivery. In addition to improving processes, leaders need to focus on serving strategic customers, building the brand, supporting acquisition efforts and expanding globally. ■