Executive Summary

Beyond 2001: A Framework for Investing in Internet and Early Stage Technology Companies

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Beyond 2001: The Investment Environment

- The volatility in the 1996-2001 investment climate for early stage technology companies (ESTC) was remarkable. Although it would be easy to write it off as a boom/bust pattern, in reality the volatility reflects some much more interesting trends
    - The unfolding of the electronic communications revolution
    - The broadening of investor participation in Internet and ESTCs
    - The complexity of the value propositions represented by ESTCs
- The correction in the financial markets in 2000-2001 reflects some useful realizations
    - There are many unknowns about the electronic communications revolution as well as the technology and business models that underlie it
    - Investors have not yet understood it well enough to maintain investments under intense scrutiny and adversity
    - The environment is much more complex than most investors appreciate
- Creating sustainable wealth through investments in early stage technology and Internet companies will require unprecedented, rigorous analysis by investors
    - The framework presented here can serve as a preliminary model

Beyond 2001: Takeaways for Corporations

- Technology "investment" has permeated the economy
  - Corporate development invests its finite attention in a limited number of alliances and initiatives
  - Corporate managers prioritize e-business technology and change initiatives
  - Employees "invest" time working at some employers and not others
  - Financiers invest in technology ventures
- Corporate managers must develop a core competency in applying early stage technology to their businesses
  - An increasing portion of products' total value is information about how to use the products to create value from customers' points of view
    - Technology broadly governs how well a product can deliver the right information to the right person at the right time to maximize that product's value
  - The value of the technology is often determined by the uniqueness of its business application: the higher the differentiation, the more value delivered to the market
  - Early stage technology carries both high potential for differentiation (reward) and high risk
  - Generally, corporate managers have had little exposure to making early stage technology investments

E-Business: Significance and Challenges for BAMs

- "E-Business" describes the strategic, process and technology activities that "bricks and mortar" (BAM) organizations undertake to digitize communications

- E-Business represents a compelling value proposition coupled with complex technology choices, increasing change within organizations and inherent challenges in measuring economic benefit delivered
  - Complexity requires BAMs to make investments carefully

- BAM executives recognize they must use technology to drive their competitive advantage
  - They will benefit by knowing how to understand ESTCs' potential value in the context of their companies so that they can be "smart buyers" and users of technology

- Collectively, the transformation of the BAM world is the ultimate context for creating value with all kinds of technology

- Investors in ESTCs will be well served by having an in-depth understanding of both e-business from the BAM perspective and the dynamics that govern ESTC life cycles

E-Business: Significance and Challenges for ESTCs

- Most ESTCs and Internet companies will be selling their solutions to B2B companies for the foreseeable future
    - Many of their customers will be BAMs
- The BAM undergoing e-business transformation represents the "selling environment" for ESTCs
    - The BAM e-business adoption curve is the "Rosetta Stone" for understanding the corporate technology buyer
- The ESTC is likely only one of hundreds of technology vendors with whom the BAM works
    - Applying myriad components of technology solutions to achieve a measurable result is a very complex proposition for buyer and seller
    - The ESTC will not control, or even influence, many of the factors that determine economic success
- BAM-ESTC relationships have enormous strategic value if each party knows how to exploit it
    - The key barrier is a two-way knowledge gap: ESTC leaders know little about the BAM world and BAM executives are unfamiliar with the realities of the ESTC life cycle
    - Each party needs in-depth insight into the other's strategy and financial drivers

Analytical Framework for Early Stage Technology and Internet Investments

- A robust analytical discipline that draws on strategy will enable investors to grow beyond a "short-term return mentality"
    - The rigorous strategy discipline identifies risks and unknowns in light of financial goals, and it specifies the intention to act given conditions
    - It will give investors insight into ESTCs' business drivers, which will increase their ability to utilize early stage technology effectively
- The framework presented here is comprised of several "lenses" through which investments can be viewed
    - The lenses' three subgroups are arranged from the broadest strategic viewpoint and get progressively more focused on the company
    - Not all lenses are required to evaluate each investment
    - Using all lenses will provide a rich view of the investment as well as a robust body of knowledge to use when discussing it with others
    - The lenses are also used to evaluate the progress of existing investments
- Regarding the Company lenses, typically two or three lenses must be extremely compelling
    - If they are not, either the ESTC leaders are not articulating them well, or there's not much there
    - It is unusual for an ESTC to have standout showings in all six

The Framework: Industry Lenses

Industry		
Transformation	Identifies industry forces and how the electronic communications revolution interacts with them; sets context for market opportunity	Research the bricks and mortar process and focus on supply and demand sides of the equation of the good or service. Where is the pain in the transaction between the supplier and customer? How many elements must act in concert in order for the e-business solution to produce value?
Discontinuous Change	Specifically views the innovation's impact on the industry and segment	In transformation, who feels the pain? What can you learn about these parties? Have they worked in industries or functions that have experienced significant change in the recent past? If so, was the change continuous, incremental or discontinuous? Have they been proactive in participating in industry or function changes?

The Framework: Industry Segment Lenses

Industry Segment		
Adoption	Maps how the innovation will be adopted by various customer segments over time	Study the origin of the company's product or service and its market, including competitors and substitutes. Note the core competencies of the founders as well as advisors. Try to pinpoint where the company's innovation is in the adoption curve. Pay close attention to the vision for how the innovation will "change the world."
Network Vision	Defines the ESTC's solar system and explains how major bodies interact	Recognizes companies as networked entities, not self-standing. The unique value of a company boils down to two things: 1) the company uses its core resources to create hard-to-reproduce, unique value; 2) the company must use the network to deliver the value. Executives must have a strong sense of what business they are in so that they can build their company quickly, and on solid ground.

The Framework: Company Lenses

Company

Technology — Quintessential to the ESTC's product or service offering

Look at network vision findings with pure technology eyes. If the offering represents a niche within a complex environment, does the leadership have past experience with complex technology environments? Are they involved with beta programs for closely related technologies? What are barriers to entry? Has the CTO had experience with building a highly scalable, robust, complex application, especially if the company is a B2B?

Marketing — Describes the company's interaction with the market and its management of that interaction

It is critical for the ESTC to have a vision for continuously managing its value proposition. If the ESTC is a B2B, try to determine the CMO's and VP Sales' insight into BAM e-business dynamics for the targeted industries because e-business will dominate the context for BAMs' use of technology for the foreseeable future. What kind of relationship assets do the CMO and VP Sales bring with them?

People — The core of the ESTC; at the beginning, the most important constant on which success is predicated

Look at the management team as well as their services providers and advisors, including the ventures they have been involved with previously and their stated motivations for giving their time to the venture. Founders have often invested extensive time and are loath to abandon the venture; they are more permanent than management who are brought in later.

The Framework: Company Lenses

Company, continued		
Knowledge	Defines the knowledge the company needs to grow and increase its value proposition	Roll up analysis thus far, identify success factors and ask yourself what the company needs to know to reach its goals. Think about other companies that have faced similar challenges: why and how did they succeed or fail? What insight or knowledge was key in achieving success?
Finance	Is it realistic for the company and the market in which it's operating?	Does the financial strategy fit the business strategy? If the company's product is to enter into a market that is dominated by major players, it probably won't make sense to bootstrap. Alternatively, if the market is fragmented, bootstrapping might be best.
Operations	Defines how the company will execute and deliver	If the company handles logistics, does the knowledge gained contribute significantly to its value proposition? Regarding service, is the offering complex, and does it require an education and training program? Will the company's products have short life cycles that depend on customer input?

For Additional Information on Applying the Framework

- Access the full white paper
    - http://www.virtualstrategist.net/issue1/1-5-1.html
- Read other research and white papers on related topics
    - http://www.rollyson.net/public/dossier/dossier.php4
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