DRAMA-FREE CEO EXITS
PAGE 10

FIXING JOINT VENTURE GOVERNANCE
PAGE 49

WIN-WIN INNOVATION PARTNERSHIPS
PAGE 38

THE POWER OF THE OUTLIER
PAGE 88

sloanreview.mit.edu
FALL 2022 • VOL. 64 • NO. 1

MIT Sloan Management Review

UNLOCK CUSTOMER VALUE

Building Relationships That Fuel Innovation and Growth

$12.95US
24>
0 74851 08784 8

Strategically Engaging With Innovation Ecosystems

Where startups, researchers, and investors cluster, opportunities to accelerate corporate innovation abound.

BY PHILIP BUDDEN AND FIONA MURRAY

Competitive pressure to innovate is driving companies to seek new ideas well beyond their own walls. But sponsoring the occasional hackathon or having one-off, uncoordinated interactions with a startup accelerator won't contribute much to boosting an organization's innovation capabilities. Many companies are missing an opportunity that's close to home by overlooking or failing to effectively tap innovation ecosystems in their regions.

These ecosystems occur where innovation and entrepreneurship activity are highly concentrated. As we define them, ecosystems are places that engage five stakeholder types — research institutions, entrepreneurs, corporations, investors, and governments — linked by a strong social fabric of mutual interest, complementary needs and resources, and trust. (See "Complementary Stakeholders in Innovation Ecosystems," p. 40.)

Our research shows that new innovation ecosystems are emerging globally, beyond well-known hubs. While often smaller or more specialized than, say, Silicon Valley, these clusters of activity are expanding the regional opportunities for corporate engagement in new locations. Meanwhile, digital interactions enable wider participation across geographic boundaries.

To achieve their goals for innovation, companies need to take a systematic approach to identifying and securing competitive advantage from working with these innovation communities.

The framework we present here, developed from our global work with hundreds of corporate leaders, provides a practical approach to such strategic engagement.[1] It helps leaders avoid the common pitfalls of deciding how and where to engage before they have identified what they need, and of deciding with whom to engage before they have determined which ecosystem players are essential for relationship-building.

Flawed Approaches to Tapping Ecosystems

Many corporations seeking to reap the benefits of innovation ecosystems fall into a series of traps and end up having little to show for their efforts. Besides causing considerable internal frustration, the following

MELINDA BECK/THEISPOT.COM

missteps — which typically arise because executives haven't established clear goals for their interactions — often mean reduced benefits for corporations and lost opportunities for the ecosystem as a whole.

First, we find that corporate leaders spread their efforts too thinly — across not only different locations but also different activities. They engage in a flurry of superficial activities that often feel transactional and performative to startups and providers of risk capital.

Second, corporations often engage in a fragmented and uncoordinated fashion: Their HR engagements for spotting talent are disconnected from the work undertaken by innovation units looking for new ideas or early-stage startup teams. In turn, corporate development and corporate venture capital (CVC) teams exploring new deals for M&A or investment may be unaware of the early-stage startup relationships established by their colleagues in the R&D group. This creates unnecessary noise in the system and often comes about because there is little clarity on whom to engage and for what purpose.

Our research has found that leaders get better results with a more structured and focused approach to getting involved with these ecosystems. This does not rule out serendipity or threaten the creativity of the innovation process. Rather, it speaks to the old adage that "chance favors the prepared mind" — it helps companies to be ready when the right encounters happen with innovators, entrepreneurs, and risk capital providers.

Alongside thoughtful planning, companies must commit to credible and sustained interaction; other stakeholders in the innovation ecosystem will be watching to see whether they will become trusted partners or merely engage sporadically or superficially. This commitment to relationship-building includes senior management and extends to relevant managers in different units as well as entrepreneurial leaders throughout the organization.

In this article, we focus on what can be the most challenging relationship among the five key ecosystem stakeholders: that between corporations and entrepreneurs. However, our framework can be applied to direct engagement with other stakeholders, including universities where many entrepreneurs begin their venture-building journey and the risk capital providers who work closely with entrepreneurs, particularly VCs and angel investors. We have also found the framework to be useful for governments looking to engage with entrepreneurs in their most pressing delivery challenges.

Start With 'What'

Our systematic approach to developing a strategy for engagement with innovation ecosystems requires that leaders consider and answer three critical questions in turn:

1. **WHAT** do you want to acquire from (and offer through) your ecosystem engagement?
2. **WHOM** do you wish to engage with, and who will engage from your side?
3. **HOW** will you engage, and will the approach ensure effective interactions?

Identifying what innovation resources an organization hopes to gain should follow from leaders' high-level strategic innovation priorities and a clear-eyed assessment of internal innovation capabilities. This analysis will also inform an understanding of the assets and capabilities the organization might offer to ecosystem players.

Asking what innovation resources your organization wishes to access might yield additional questions before it produces answers. Do you need technical talent for your hiring priorities, or perhaps entrepreneurs with new and novel projects who can contribute cutting-edge solutions to your innovation portfolio and open up new customer segments? Or do you seek the opportunity to engage with and be part of a more innovative culture to help retain talent or reenergize your internal corporate culture? Where are your internal gaps and weaknesses most acute? Each of the potential resources above may resonate differently with different parts of the organization. That is why this is a top-level strategic issue: Effective ecosystem engagement means answering the "what" question for diverse parts of the organization while also prioritizing the benefits to the enterprise as a whole.

The varied answers to the question can be combined into a unified strategy for engagement (albeit one that might be executed by individual departments). However, in order to present a coherent and welcoming face to the innovation ecosystem, it is important to at least map out the whole landscape of the corporation's needs from, and engagement with, the ecosystem. Our experience suggests that having well-articulated needs and a shared awareness of what each part of the organization seeks increases the likelihood that multiple channels of engagement will benefit the whole organization.

A good case in point is MassMutual, an insurance company based in Springfield, Massachusetts, whose leaders wished to explore how they might more effectively engage with the growing startup community in the Greater Boston area. While the company had experienced success with internal innovation, it wanted to expand its visibility into startup activity in both fintech and insurance technology.

A traditional corporate play might have been to dispatch an M&A team to buy a few fintech startups in Boston, but the leadership of MassMutual determined that the company needed sustained engagement that would inform and accelerate its strategy for internal innovation as much as it sourced externally. The leaders recognized that these resource needs would require them to engage with a large number of early-stage startups so that they could assess a range of different segments, business models, and startup approaches. What they wished to understand was how startup entrepreneurs approached the innovation process. They also hoped to gain a new perspective on the market opportunities in fintech and to observe and better understand startup cultures in order to build a more entrepreneurial culture at MassMutual.

To that end, MassMutual partnered with the sector-agnostic MassChallenge accelerator in downtown Boston to get an overview of the startups in its programs. Although this did not provide near-term deal flow (a typical CVC or M&A benchmark), that was not the company's target metric. MassMutual executives' strategic engagement provided opportunities for them to spend meaningful time with a curated group of startup teams.

By providing space in its new Boston seaport building for the MassChallenge accelerator, MassMutual bought itself a ringside seat to a huge slice of the local ecosystem, and its team was able to simply get to know entrepreneurs and interact informally with them day to day.

Working with MassChallenge as a trusted intermediary also helped MassMutual overcome the sorts of missteps we laid out above, and the challenges that often come with large corporations engaging agile entrepreneurs within an ecosystem. Building on this, the company has started to work with a wider set of ecosystem partners to establish a shared understanding of the opportunities and challenges facing Massachusetts in becoming a world-class fintech ecosystem.

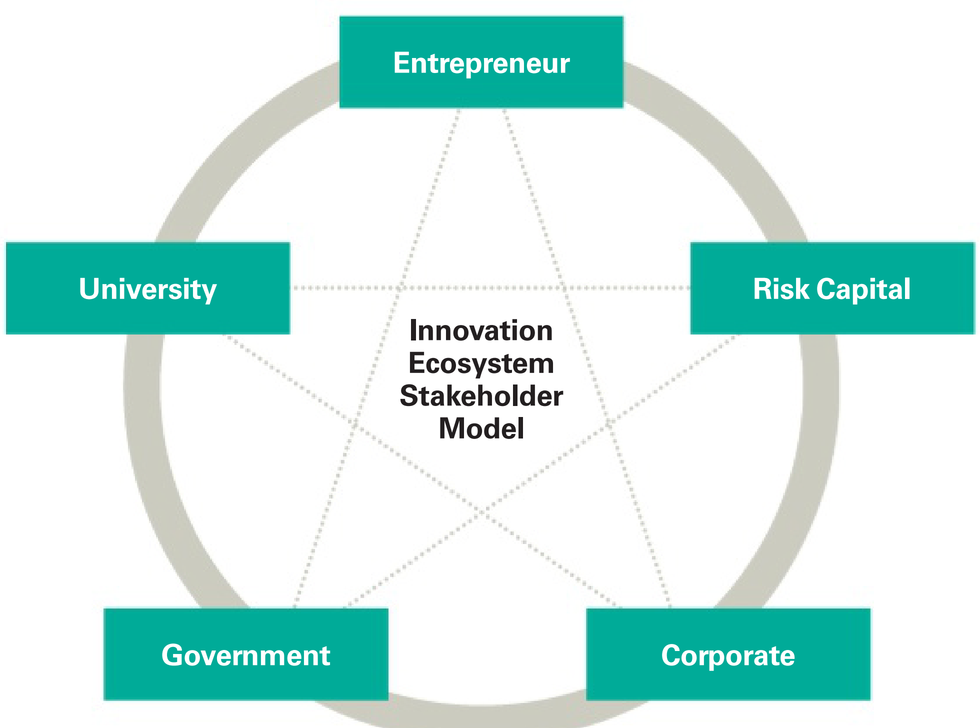
Once the question of what they wish to acquire from the ecosystem has been addressed, organizations need to turn the tables and ask what they have to offer in return. Ecosystem engagement is about reciprocal interaction and mutual exchange. Engagement is not a one-way street.

Our experience shows that funding is often part of the offer from a corporation but not always — and not at the level companies might expect. While risk capital is often a top priority for entrepreneurs, teams building new ventures often want corporations to provide them with a window into customer needs as much as they want funding. They also seek expertise in navigating complex regulatory and supply chain pathways to reach an end user, and access to infrastructure to support testing, customer access, scaling up, and supply chains.

When corporations fail to understand the needs of others — whether entrepreneurs, risk capital providers, or universities — they can fail in their engagement and in meeting expectations, even when

COMPLEMENTARY STAKEHOLDERS IN INNOVATION ECOSYSTEMS

A healthy innovation ecosystem draws value from — and delivers value to — five different kinds of stakeholders.



they have many of the resources their ecosystem partners might find useful and complementary.

Build the Right Relationships

Defining what the organization seeks to gain helps focus the question of who the right partners among the stakeholders in the ecosystem are likely to be.

If a company needs to engage teams of diverse individuals to build novel solutions for critical market opportunities, then it will likely seek to work with startups. However, it is important to understand how innovative entrepreneurial ventures develop and the stage at which engagement will be most productive.

We characterize startups exploring new and uncharted solution spaces or providing solutions to emerging problems as innovation-driven enterprises (IDEs).[2] These are the entrepreneurial ventures that large organizations will be most likely to target as potential partners rather than the more traditional small and medium-sized enterprise startups. IDEs work in milestone-driven cycles of funding, experimentation, and learning that we call innovation loops, to gain information about possible paths forward and determine which ones to explore more deeply and which to close off. Over time, they reduce uncertainty and increase their readiness. At each stage, innovators strive to improve product/market fit, the maturity of their solution, and its readiness to be scaled.

Against this backdrop, large organizations must consider not only who among startups is working on particular innovations or technologies of interest but also their stage of innovation readiness.

Is the corporation really interested in very early-stage ventures that are not yet incorporated — often a university team with a deep understanding of the solution and a working prototype but limited experimental evidence? Or, is the company interested in startups that have formed a legal corporation and have limited risk capital but demonstrated evidence of meeting critical milestones? Or, is it looking for a late-stage, plug-and-play startup with a solution to a well-defined problem and market traction as a possible CVC or M&A target or partner?

The answer depends on whether the corporation has a clear sense of what it needs from the innovation ecosystem. Organizations that see a strategic gap in their insights into future innovations and truly novel ideas will likely seek links to very early-stage ventures. Those that have a particular gap in their near-term portfolio will be looking to engage with a handful of late-stage startups that have the potential to fill that gap.

A good example of a company taking this systematic approach comes from Philips, the Dutch electronics conglomerate that successfully transitioned to a strategic focus on health care technology over the past decade. Its U.S. operations — especially those in Greater Boston — became critical to its global innovation efforts as it pursued that end. Leaders realized that Philips's internal innovation pipeline was not likely to deliver on a sufficiently wide variety of health care opportunities, and they were concerned that the company would not identify investment, acquisition, and partnership targets early enough. They decided to engage early-stage startups and founders who could bring more creative innovations and perspectives into health care and complement the digital strategy being pursued by Philips's business units and corporate labs.

Philips understood that such ventures would not yet be fully formed startups backed by extensive venture capital, but this was its sweet spot in the ecosystem — where it could explore a large number of startup ideas, especially those generated by emerging talent with alternative perspectives on health care and wellness. Key Philips executives got involved with the then-new MIT Sandbox, which supports early-stage student-initiated entrepreneurship ideas. They not only contributed to MIT Sandbox's seed funding but also made themselves available for mentoring and networking with the entrepreneurs.[3]

Through this activity, Philips was able to identify and assist the startups likely to help it in its pivot to health care. Moreover, it earned a reputation within the ecosystem for being a corporation that early-stage startups — sometimes wary of corporate venture capital and M&A teams — could trust. In each of its engagements with startup teams, the exchange was relatively modest for Philips but meaningful for the startup. That included useful but not overwhelming resources at each stage and, most important, executive engagement and mentoring that enlightened startup entrepreneurs about markets, regulatory challenges, or supply chains.

Realizing that such entrepreneurs then needed follow-on support for innovation, Philips built on these relationships by establishing its Philips HealthWorks

Too often, leaders launch into the ecosystem with a shiny new space or a single massive event but gain little from these efforts other than publicity.

accelerator program, which supports particular startups beyond the seed stage. Its clear focus on whom it wanted to engage with among early-stage entrepreneurs created a pipeline to its more focused corporate accelerator. That accelerator provided a clear second stage for engagement with, and more resources for, a hand-curated group of startups. It also allowed Philips to deepen its relationships with the startups and provide them with more mentoring.

The flip side of the question about whom to engage in the ecosystem is whom the corporation should choose from among its staff to lead its engagement with the ecosystem. Executives who are placed in this type of role but lack deep knowledge of the company and its resources often fail because they cannot navigate the choppy waters where external innovators and entrepreneurs meet internal systems and processes.

Philips assigned this role to one of its innovation executives, Brian Rosnov. Rosnov had just earned an executive MBA at MIT and was serving as an entrepreneur in residence in the Philips Digital Accelerator in Cambridge, Massachusetts, after having spent more than 10 years working on a range of product lines at the company. Rosnov led Philips HealthWorks's involvement with MIT and the rollout of its accelerator program. His long experience within the company enabled him to select effective mentors from within the corporation for each project team and ensure that they had a reasonably smooth journey accessing internal resources.

Develop Productive Ways to Engage

We can't overstate how vital it is to plan your engagement with innovation ecosystems only after considering what your organization needs and with whom it wants to work. Too often, leaders put the cart before the horse — for example, by launching their organization into the ecosystem with a shiny new space or a single massive event while gaining little from these efforts other than publicity. We've also seen government agencies and corporations enter an ecosystem by funding a large number of disparate hackathons, accelerators, university competitions, challenges, and the like. This scattershot approach fails to deliver because it is unfocused, creates confusion among ecosystem stakeholders, and occurs without an eye toward whether the significant time and energy invested will align with what the organization needs and with whom it should be engaging.

We have seen many corporations express surprise and disappointment when they sponsor hackathons and early-stage business plan programs and find that the pitch days at the end yield nothing with the sort of robust financial models and technology road maps they are used to seeing internally. That mismatch in expectations typically reflects the sponsor's insufficient clarity on goals and appropriate types of partners.

This is not to say that a hackathon is a waste of time — it can be an effective way of engaging, when the sponsor is clear that its goals are to uncover inspiring ideas and new talent, and the event is well designed. Similarly, getting involved with early-stage competitions and accelerators is a good approach when organizations are looking for very young venture teams that they can learn from and mentor. Later-stage accelerators will address the needs of companies that seek robust solutions on an already well-charted path to readiness. The challenge is to determine which mode of engagement matches the "what" and "who" answers that have been carefully developed.

As a starting point, companies should leverage existing communities where entrepreneurs already gather. Even with ongoing COVID-19 disruptions, communities of startups tend to colocate in shared workspaces, communities, and ecosystem programs. By interacting with such communities, large organizations can more easily develop a broad array of relationships than they could by targeting startups on an individual basis. Engagement designed around immersion in a particular region also helps ensure that structure and serendipity coexist.

There are, of course, numerous choices for how to structure engagement, and we've discussed how some of these tactics have been employed by MassMutual and Philips. The U.S. subsidiary of U.K. defense contractor BAE Systems provides another good example of a thoughtful engagement strategy that draws on several different ways of working with innovation ecosystems.

As BAE's leaders sought to build relationships with the Greater Boston ecosystem, they were clear on their goals: They wanted to engage with startup teams whose innovations promised to bring new functionality to BAE's innovation portfolio — especially to projects in its advanced technology and defense R&D labs that focused on next-generation emerging technology.

Rather than simply setting up shop in Cambridge's Kendall Square and hoping that entrepreneurs would find their way there, BAE rented space in the Cambridge Innovation Center (CIC), a coworking space that boasts the most densely populated startup community on the planet. By running programs at CIC's Thursday night Venture Café community events and fielding a diverse and entrepreneur-friendly team of managers led by MIT alumni, BAE was able to connect with the right startups and founders to learn about technologies that might align with the company's R&D priorities.

Beyond engaging in a visible and regular way with the entrepreneurial community, BAE leaders also recognized the role of key programs — hackathons, competitions, and accelerators — in the ecosystem. They realized that initiating their own programs would be an unnecessary challenge and might be seen as undermining existing ecosystem activities. Instead, much like Philips's leaders, they made a commitment to connect with and support local accelerators whose missions and startups were aligned with what the company sought from the ecosystem and with whom it wanted to engage.

Working with accelerators such as Techstars, BAE could seek out startups whose technology might have military and intelligence applications as well as civilian ones, and that had an interest in partnering with and learning from an experienced defense contractor. BAE created opportunities for these startups to benefit from its close relationships with the U.S. Department of Defense. Because BAE's success in ecosystem engagement is a source of its competitive advantage, the details are of course commercially sensitive, but its continued engagement shows that it judges these efforts to have paid off.

WHEN ORGANIZATIONS PUT in the work to define their ecosystem strategy, they are best positioned to reap the benefits of working with innovation communities. Using our "what," "who," and "how" questions is a systematic and practical way to secure competitive advantage through the strategic engagement of innovation ecosystems.

Companies' disappointment when their efforts fall flat is often mirrored by entrepreneurs and innovators who engage with them. When they look to large corporations and government agencies for access to experts, or even for critical venture capital, they are often confronted by lawyers, human resource experts, and accounting departments. Each of these corporate functions might create value for ambitious startups, but, absent meaningful engagement with key players at the company, the potential for deep and productive collaboration will likely go unrealized.

While simple in their formulation, our three questions can be challenging to answer, especially for large organizations that may have many answers and thus wish for many modes of engagement. Our advice is simply to work across your organization and take the time to seek internal alignment on what resources you want, what you can offer, and who the most appropriate partners are. This will ensure that how you engage your ecosystem yields results that advance your innovation goals.

Philip Budden *is a senior lecturer on technological innovation, entrepreneurship, and strategic management at the MIT Sloan School of Management.* ***Fiona Murray*** *is associate dean for innovation and inclusion at the MIT Sloan School of Management, the William Porter (1967) Professor of Entrepreneurship at MIT Sloan, an associate of the National Bureau of Economic Research, and director of MIT's new Innovation HQ (iHQ).*

REFERENCES

1. We have taught, and gratefully learned from, corporate leaders in MIT Sloan's Executive MBA program, MIT's global Regional Entrepreneurship Acceleration Program, and MIT Sloan Executive Education.

2. B. Aulet and F. Murray, "A Tale of Two Entrepreneurs: Understanding Differences in the Types of Entrepreneurship in the Economy," PDF file (Kansas City, Missouri: Ewing Marion Kauffman Foundation, 2013), www.issuelab.org; and P. Budden, F. Murray, and O. Ukuku, "Differentiating Small Enterprises in the Innovation Economy: Start-Ups, New SMEs & Other Growth Ventures," MIT Lab for Innovation Science and Policy working paper (Cambridge, Massachusetts: MIT Sloan School of Management, January 2021), https://innovation.mit.edu.

3. The MIT Sandbox Innovation Fund Program is based with similar units in MIT's new InnovationHQ.

Reprint 64101. *For ordering information, see page 4.*