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Teaching old firms new tricks

Those who follow the business news often come across stories on how firms are going to start doing new things in order to improve customer service, strategic position, profitability, or some other reason. Maybe it is a merchant bank that wants to add investment banking or private banking services, a ferry operator that wants to add cruise tours, or a music distributor that wants to add an airline. How hard can it be? Notable successes notwithstanding, the firms often end up proving the same point as the "Top Gear" program hosts do when they try to answer the question; How hard can it be? It can be really hard.

There are many reasons why it is hard, but I want to focus on one part of the answer that is often overlooked. The old firm that tries something new gets caught out because it is not doing enough of the new. Let me give an example based on research done by Gina Dokko of UC Davis and Vibha Gaba at INSEAD. Corporate Venture Capital (CVC) is when established firms create units that are made to behave more or less like regular Venture Capital firms, so they identify promising new firms, invest in them and provide advice to help them grow, and then (usually) seek to spin them off for substantial profits. In addition, some firms view these CVC units as sources of strategic strength because they get the first pick to acquire new firms with strategically important technologies or markets.

CVC units are not held in high regard by regular venture capitalists, who see them as less skilled and more prone to mis-invest than they are, but are nonetheless willing to partner with them if the price is right. But Dokko and Gaba find that something else is going on too. CVC units are not stable in their strategy. If they are staffed with managers with regular venture capital experience, they may be able to maintain a focus on spinning off successful firms, as the usual strategy is. But if they are staffed with managers from inside the firms they will increasingly end up buying the firms under their wing. Put simply, they forget what it is like to be in venture capital because they have too little experience in it, and too much experience doing their regular business. This is not special for CVCs. Investment banking or private banking units of merchant banks can end up looking more like merchant banks, and I bet you will notice the difference between a cruise ship operated by a ferry company and one operated by a cruise line. The bottom line is that firms are good at doing their usual activity, and it takes special effort to become good at something new. Hiring management with the right experience and giving them freedom to do things the way they are used to is a good start.

Dokko Gina, and Gaba, Vibha. 2011. Venturing into new territory: Career experiences of corporate venture capital managers and practice variation. Academy of Management Journal, forthcoming.

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