

XONNA PARTNERS

A Foothold in Silicon Valley One (Good) Way to Get There

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Summary

This whitepaper should be of interest to any company or government entity that wishes to tap into the Silicon Valley model of innovation and technology disruption. We describe the different models, benefits, and pitfalls of planting a foothold in Silicon Valley. We conclude by describing various execution models to help in this endeavor and maximize the chances of success while avoiding the pitfalls others have experienced.

Introduction

Silicon Valley has become a world-unique and proven birthing ground for disruptive technology startups. This is due to the complex ecosystem at the confluence of University Research, Innovation Spirit, and Venture Capital. This ecosystem is further supported by a large number of businesses and institutions that feed into this ecosystem.

Various players around the world, being corporations, governments, or investment houses have been looking at ways to benefit from the Silicon Valley ecosystem by plugging into it. This is likely to remain the case, and probably, even accelerate. The benefits range from learning and adopting the innovation force of this unique ecosystem, to leveraging it by acquiring new technologies of strategic interest, or to seek exposure to Silicon Valley Venture Capital investment returns.

In this paper, we highlight our learnings and experiences from operating in this ecosystem for several decades, and how this might be applied to benefit other companies desiring a level of exposure to the Silicon Valley ecosystem. The aim is to facilitate a low risk, strategically aligned, presence in Silicon Valley and build an adequate evolution strategy from there.

Our team at Xona Partners can be the gateway platform that would provide a cost-effective foothold in Silicon Valley that best matches the strategic objectives of the parties desiring to benefit from it.

The Drive to Plug Into the Silicon Valley Eco-System

The story of Silicon Valley has been well documented. It started with the defense industry in the 50s and 60s, followed by Integrated Circuits, Personal Computers, the Internet, etc. However another, less visible but significant transformation occurred. Since the 1980s, the US industry has witnessed a shift from in-house innovation (eg: Bell Labs) to inorganic technology acquisition (Venture Capital ecosystem and M&A) as the better model for technology and new business development.

The early decades of Silicon Valley were characterized by waves of innovation in specific industries. Today in Silicon Valley, we see overlapping innovation waves in many industries. These waves of innovation often create synergies that further accelerate innovation and disruption. A good example is the collision of Internet and automotive innovation behind Tesla and the Google self-driving cars. This trend is likely to continue, and put even further pressure on the various global stakeholders in the innovation eco-system to tightly work, integrate and synergize with what's happening in Silicon Valley.

It is our belief that this model of technology and business innovation in Silicon Valley is here to stay despite periodic turmoil in financial markets and the broader economy. Most leading companies will sooner or later have a desire to establish a presence in Silicon Valley in order to tap into this source of innovation and disruption.

Many other parts of the US and the world are trying to emulate Silicon Valley. The numbers speak for themselves. Silicon Valley remains by far the leader in the number of startups and the capital invested in them. In our view, replicating this model in a different geography is not the optimal approach (as evidenced by the many attempts over the years, and we still have one Silicon Valley), and we would argue more for a learn and adapt to context, based on specifics of the local environment, which is a model being successfully pursued by various technology hubs around the world. In that context, we propose that a “bridge to Silicon Valley” is still needed to ensure cross-fertilization of ideas, de-duplication of effort, and adequate access to venture capital.

External Innovation Model

In the US, Venture capitalists invested \$58.6 billion in 4,520 deals in 2016, according to the MoneyTree Report by PricewaterhouseCoopers LLP and the National Venture Capital Association. Although 2016 saw a decline in deals it still represents growth of VC funding when averaged over a few years. Silicon Valley accounts for about half of all US VC deals.

This level of capital fueling innovation ensures a strong supply of talent eager to develop their own ventures. Large corporations find it hard to retain and motivate top young talent. Silicon Valley is full of serial entrepreneurs. In fact, these are typically free-spirited individuals who excel in startups and do not wish to settle in a corporate environment.

This and other factors have changed the old in-house innovation model to one where most disruptive innovation is created outside of large corporations. Corporations are forced to acquire new technologies and new businesses through M&A and partnerships.

With so much activity in Silicon Valley most leading companies are opening offices there to tap into the flow of innovation. This gives them much valued insight and early warning of changes on the radar. There are many examples where companies failed to see the emergence of a significant competitor, especially in industries that Silicon Valley was not known for: BMW was blindsided by Tesla, and Honeywell by Nest. More towards the traditional core of Silicon Valley is the transformation of Cloud Computing, Genetic Engineering, and the Internet of Things. All of these new waves have incumbents scrambling to ride those waves of change rather than be swept by them.

Many corporates have opted to join the Silicon Valley innovation model by opening Startup Incubators, R&D outposts, Corporate venture Funds, and scouting for technologies for acquisition. Some corporates have opted to Spin-Out internal R&D projects into Silicon Valley so they can develop unhindered by the mothership but with an option to be re-acquired at a later time.

Changing Innovation Vehicles

The startup innovation model is rapidly changing. The biggest changes are at the early stages of the startup lifecycle. The startup exit, IPO and M&A, are mostly unchanged (with the exception of the IPO changes caused by the Sarbanes–Oxley Act of 2002). The mid stage VC funding is also relatively stable and well understood. However, the early stages have seen significant changes due to an increasing focus on this early stage by institutional and corporate investors, online versions of syndicate of angel investors, incubators and accelerators, as well as regulatory changes such as Crowdfunding.

Not so many years ago, the life of a startup before VC funding was a very opaque endeavor. There were very little formal statistics gathering or institutional attention. As it came to the forefront, that startups are driving innovation and major business disruptions, investors and corporations have increasingly focused on the earlier stages of startups formation. More recently, the US regulator has made changes that allow for new funding models such as crowd funding for startups. These changes have created a number of early-stage vehicles to stimulate startup creation and early-stage growth.

On the investor side, we have several types of Angel investors from individuals to professionally run angel groups, as well as many early stage boutique VC firms. Most universities have established spin-out centers to facilitate commercialization of the IP generated by their research. There are an increasing number of Incubators, from for-profit, via corporate incubators, to sponsored, and local government supported incubators. There are many startup competitions where winners often get funding and other support. There is an increasing on-line activity that blends social networking with investing to create crowd funding for startups. In addition, there are a number of loosely defined often sponsor supported spaces/venues where entrepreneurs meet, socialize, and work to create startups.

It can be a daunting exercise to understand, track, and engage with this dynamic ecosystem. Inevitably there are many cases of ineffective engagements with Silicon Valley, failed investments, and cost overruns. However, there are also many examples of highly successful engagements, rewarding investments, and lifesaving business transformations.

Planting a foothold in Silicon Valley

A detailed look at the Silicon Valley offices of the many companies present there reveals significant variations in function, mandate, scope, size, and structure. Furthermore, these factors often change within each company over time. This is strong evidence that the winning formula for an effective engagement with Silicon Valley is elusive.

The functions performed by these outposts, is based on various models, depending on goals and strategies. It would include some or all of the aspects below:

- Technology scouting
- Partnerships
- Startup investments from seed stage to mezzanine financing

- R&D
- Incubation
- Due diligence
- VC fund management
- Spin-out & spin-in
- M&A support
- PR & Branding
- Executive education through immersion in Silicon Valley activities

How We Are Approaching the “Silicon Valley Foothold”

Xona Partners has a long experience in Silicon Valley. Our partners have held roles in successful startups, Venture Capital and M&A firms, major tech companies, and led the Silicon Valley offices of global multinationals. Xona has rich relationships and deep networks in Silicon Valley that span decades.

Depending on the strategic needs of our partner, we typically craft a white-labeled presence in Silicon Valley. If the partner wishes to have its own longer term presence in Silicon Valley, we can design an “instant start” Silicon Valley Office for the partner by transitioning from white-labeled Xona staff to partner’s staff through hiring and training in a smooth transparent process without business disruption.

Our aim is to provide the most expedient and efficient way for our partner to establish a foothold in Silicon Valley and reap the benefits that can provide.

In our experience, we have seen the tremendous power of participating at the leading edge of technological and business disruptions. We can confidently predict that, when executed correctly, the investment into a presence in Silicon Valley will have a much higher ROI than the company’s own business. Furthermore, the reduction of the probability of being blindsided, and/or the incubation of a new area of business could have lifesaving consequences. Finally, the executive who has the wisdom to plant a successful foothold in Silicon Valley for their company often receives long-lasting praise

Executing on the “Silicon Valley Foothold” - Partnership Model

A two-phase analysis approach is typically considered:

Phase 1: Scope, Develop, and Deliver a Ready-to-Execute Proposal for the partner’s presence in Silicon Valley

Tasks:

1. Understand the partner’s business objectives, long term strategic drivers, and any existing ideas on how a presence in Silicon Valley can benefit the partner
2. Develop the Strategic Benefits statement and get the partner buy-in

3. Develop the Modus Operandi for the partner's Silicon Valley activities
4. Identify a senior champion for this project within the partner's organization
5. Develop and deliver to the partner the Ready-to-Execute Proposal for their initial foothold in Silicon Valley and evolution thereof

Phase2: Develop the partner's Silicon Valley presence and local engagement model

This phase will be the implementation of the Modus Operandi defined in the design phase. Some examples of the Modus Operandi might be as follows. We shall note that this is very customizable to the partner and may include some mixture of all the examples below including any additional activities defined prior:

1. Scouting

Scout for startups and activities of strategic interest to the partner. Develop "landscape analysis" and deliver to the partner. Facilitate direct-engagement of ecosystem players with the partner.

2. Stimulate Innovation

Depending on the partner needs, organize workshops, events, hackathons, etc. Engage with and stimulate University research groups. Develop "innovation training" seminars for partner's business units.

3. Take equity for option value

Making an equity investment in a startup can give a partner valuable options down the road. These include (a) unique intelligence and visibility into that ecosystem, (b) an option to steer the direction of the startup and technology development, (c) an option to acquire the startup and/or prevent it from being acquired by a competitor.

4. Take equity for investment returns

The returns from Venture Capital can be very attractive. Many investment firms choose to allocate a portion of their portfolio to Venture Capital. We can provide access to a large and diverse early-stage deal flow and tailor the investments to the partner's objectives.

5. Spin-out

Many R&D projects get stifled in a corporate environment spinning them out into the startup ecosystem could significantly improve their chances of success and adding value to the partner. We can facilitate the spin-out process to ensure successful launch of the entity. Spin-outs can also be used to divest the partner from product lines or businesses that are no longer strategic for the partner. This is a way to extract value from an activity that would otherwise just die or distract from the core strategic direction. We can assist in finding a buyer and/or launching the activity as a standalone company with potentially adding external investments if needed.

Select Illustrative Completed Case Studies:

Three distinct use cases, out of the various the Xona Partners team has conducted, have been selected to illustrate the “foothold in Silicon Valley” execution model

Case Study 1: a proxy innovation and venture capital arm in Silicon Valley

A worldwide Internet and Telecom Technology leader decided to place a foothold in Silicon Valley. The objective was three-fold:

1. To tap into and absorb emerging innovative technologies that have significant disruptive potential in telecoms and IT.
2. To strengthen the engagement with startups with a venture capital component that creates additional leverage and de-risks the future.
3. To act as an early warning radar to changes in macro business models caused by technology disruptions.

The Silicon Valley office was structured to best accomplish those objectives. It had very strong executive and working level relationships with HQ in Europe. It was mission critical to maintain a good connection with the core business units and engage them in Silicon Valley activities.

The focus of technology scouting was in two areas: (a) based on a deep understanding of existing products and services, we scouted for technologies that could result in significant improvement of those, and (b) scout for technologies that are adjacent to the core business and could create new business opportunities. The latter also has the potential to enter new areas that could eventually replace the existing “cash cows”.

The benefit of equity investments via venture capital are to enhance the relationship with a startup and its ecosystem, to improve the startup’s probability of success, while at the same time leaving the startup to develop naturally without suffocation by the large corporate entity. The equity investment is structured in way that gives certain preferential rights that can be exercised down the road, such as the right of first refusal, and others.

Silicon Valley is a microcosm of bigger changes that will occur later. Having first hand insight from research topics at local universities and research institutions, startup activities, venture capital flows, and industry conferences and gatherings allowed us to build an understanding of where things are going. This perspective was delivered to C-level company executives and was instrumental in shaping the strategic direction of the corporation.

Specifically, the Silicon Valley office recommended concrete strategies for integrating WiFi into a mobile service, avoiding WiMax and Fast-tracking LTE, embracing mobile advertising and accelerating entry into that business through VC investments, etc. These are just a small number of specific deliverables that had a major strategic and business benefit to the company.

Case Study 2: Contributions to the development of a tech innovation eco-system

In this case, the project included working with a country based innovation eco-system, including their venture capital arms, government R&D arms and academic and technology innovation institutions, to bridge them into the Silicon Valley eco-system, and define the best strategy for short, mid and long term cross-fertilization.

Taking into account this country aim to evolve towards becoming a Tier 1 R&D innovation technology hub, there was an opportunity to contribute to this evolution, strategically and tactically, based on the past experiences we have in the Silicon Valley innovation hub. Specifically, the goal was to assist with the development of a technology incubation initiative, from ideas inception to an early stage go to market strategy of select R&D initiatives. This did include:

- Work with select set entrepreneurs and soon to launch technology startups academics on a way to optimally jumpstart their ideas-to-startup process, and jointly build a path towards leveraging innovation towards commercialization success
- Work with them to analyze and review select R&D proposals, with market innovation in mind, based on the various goals and target markets
- Work with the potential early stage incubation fund and/or investors on the due diligence side.
- Work with the various actors of the overall innovation eco-system on putting the right elements in place for success
- Bridge in Silicon Valley venture capital process as part of the value chain engagement
- Develop relationships and explore synergies with the Silicon Valley ecosystem

The following approach has been taken to achieve this

- Spend some significant amount of time with the various stakeholders, working with them on building a path towards developing early stage ideas, with a path towards a startup venture.
- Develop a good remote working model to achieve optimal collaboration with the various stakeholders, with a focus on mentoring some of the new ventures, working with the venture capitalists to bring in high value funding, and bridging in into some key technology players that would be potential partners, channels to markets or in some cases, acquirers of such ventures
- Experiment with the above and refine based on progress, as far as model and engagement, tactically and strategically.
- The final outcome included very positive developments on various fronts, as stated by the initial objectives. Specifically, it did open other synergetic relationships with the Silicon Valley for various stakeholders, including the entrepreneurs, venture capitalists and government funding groups.

Case Study 3: Building a bridge to Silicon Valley

In this case, the partner was a hybrid public/private supported entity, that wanted to enhance technology innovation in their geography and act as a nucleus for entrepreneurship and startups. This included the layout of an innovation stimulus Fund. The stated goals included:

- Fast track plug into the Ecosystem: Access to ecosystem of startups, other Silicon Valley incubators, accelerators, angels, and solutions developers.
- Scout for high end technical and business development resources: Identifying and enrolling subject matter experts in specialized field areas, including subject matter experts and network of what would potentially become a Global Entrepreneurs in Residence (G-EIR)
- Designing Enablers: Custom pitch events and strategy consulting/trends. Answering the partner's specific needs around identifying and engaging with startups.
- Design of experimentation Sandboxes: A sandbox for innovation enablement based on the specific needs of the partner for technology experimentation (e.g. Fintech for regulators)
- Access to talent pool of knowledge worker in emerging technologies, on a global scale, with a strong Silicon Valley tie up

In addition to the local in-country structure, we added an integral "bridge to Silicon Valley" plan. This constituted an office in Silicon Valley operated by Xona Partners under the brand of the partner, with models of reverse white labeling over time.

The functions performed in the Silicon Valley Office included:

- Help review startups that apply to the in-country Program by providing a Silicon Valley perspective and evaluation methodology.
- Assess the technology in the proposal and any prior art in Silicon Valley and if needed advise on modification to the business plan.
- Assess market traction potential of the proposal, any possible partnerships, and if needed advise on modification to the business plan.
- Help with the investment recommendation to the Fund.
- Suggest possible additional co-investors from US ecosystem.
- Source guest speakers from Silicon Valley and the US to visit the Program HQ.
- Host visitors from Program HQ and organize educational tours of Silicon Valley for Startups and executives from the Program, the Fund, and other related executives and government officials.
- Create and manage an entrepreneurship syllabus for startups in the Program.
- Advise Program startups on goals and objectives as they evolve.

- Assist with business opportunities in the US.
- Assist with follow-on funding from the US and the Fund.
- Help Program startups open office or virtual office in Silicon Valley.
- Help Program startups incorporate in the US when that is beneficial.
- Assist in M&A when opportunity arises.
- Use extensive connections with Silicon Valley startups and established companies to promote using in-country resources and the startups supported by the Fund to partner with and to do trials in country or open branches in country.

Conclusion

Silicon Valley is here to stay for the foreseeable future. It will remain a constant draw for inspiration to a continuous flow of innovators from around the globe. Yet, for the corporations, governments as well as incubators and accelerators wanting to have a valley presence, this is not easy task. Finding the right model is fundamentally important, prior to diving into execution. We, as a Xona Partners team, aim at easing this process and having it tailored based on the specific innovation needs. This paper described the rationale for such approach. Real world illustrations were provided, highlighting successful recent engagements, where the end goal was to not only set foot in the valley, but do so in a way that ended up providing the most optimal results over the shortest amount of time, and in the most economical manner, as highlighted from the experiences of our partners.

Xona Partners (Xona) is a boutique advisory services firm specialized in technology, media and telecommunications. Xona was founded in 2012 by a team of seasoned technologists and startup founders, managing directors in global ventures, and investment advisors. Drawing on its founders' cross-functional expertise, Xona offers a unique multi-disciplinary integrative technology and investment advisory service to private equity and venture funds, technology corporations, as well as regulators and public sector organizations. We help our clients in pre-investment due diligence, post investment life-cycle management, and strategic technology management to develop new sources of revenue. The firm operates out of four regional hubs which include San Francisco, Paris, Dubai, and Singapore.

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