

# Corporate incubators: nurturing **innovation** **potential**

Innovation does not come naturally to most companies, especially the kind of innovation that requires thinking outside the core business focus, as well as its culture and processes. However, as sectors are disrupted by new players and new approaches, this is exactly what many businesses need. To that end, corporate incubators are proving to be a successful strategy for organizations to develop new ideas, products and services – and ensuring long-term profitable growth.



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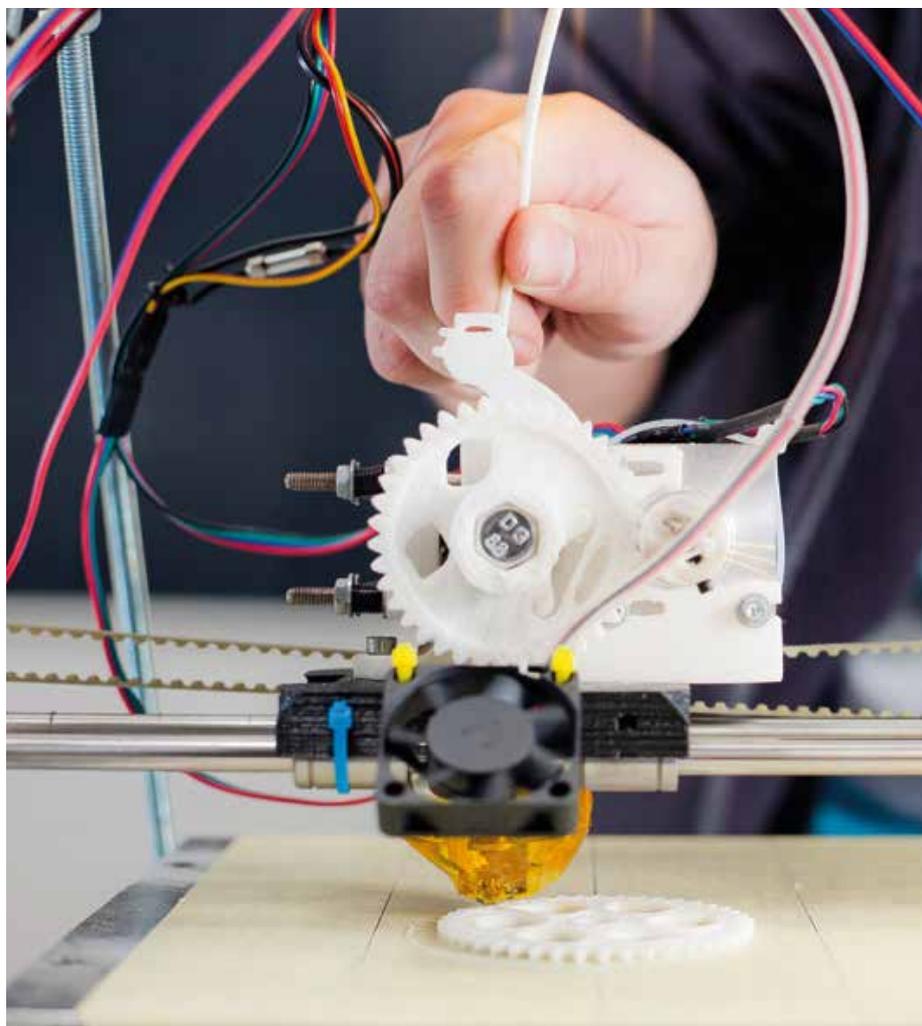
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**T**oday's fast-changing business environment aggravates the challenge for organizations to keep ahead and sustain their competitive advantage. Companies are confronted with a more complex situation than ever before – just think of escalating globalization processes and fast technological development, such as ever-increasing digitization. These give rise to new market players and market offerings, or shorter product life cycles and consumers who are better aware of their needs and market power. All of this demands excellent solutions to be delivered quickly.

In this environment, innovation becomes ever more crucial for companies to secure long-term competitive success. Most companies acknowledge the importance of innovation, yet often they struggle to put it into practice. Companies are confronted with an "innovation dilemma": choosing between maintaining and developing the existing business, or venturing into new areas.<sup>1</sup> While dealing with their daily challenges and operations, they miss out on the innovative opportunities in new fields.

How can companies really combine maintaining the existing business with developing an entirely new one? Management science suggests establishing an ambidextrous organization, which can operate with "two hands" and pursue exploitation and exploration at the same time.<sup>2</sup> One approach to realizing an ambidextrous organization is to set up units mandated to engage in exploratory innovation activities as entities distinct

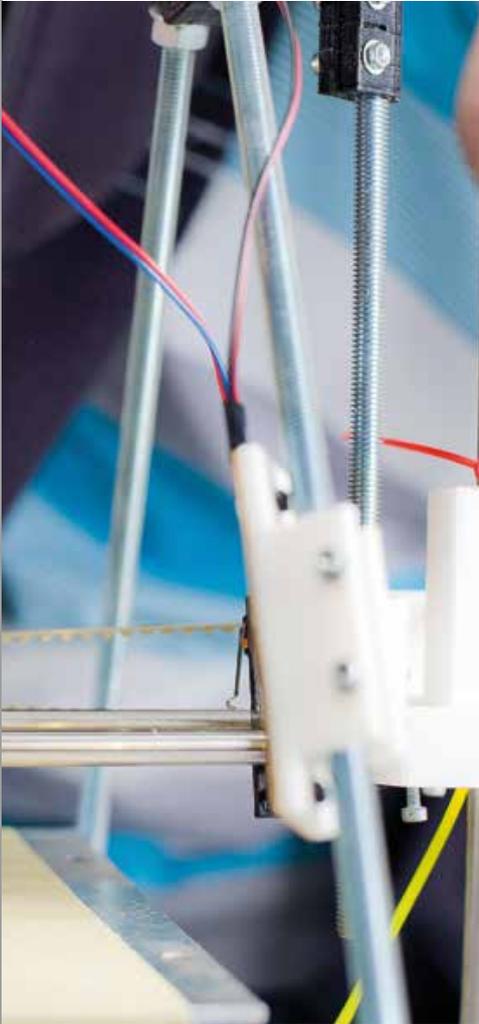


and separate from the core organization.<sup>3</sup> This idea has recently attracted attention from larger established companies as they open dedicated innovation units, or corporate incubators. Deutsche Telekom and hub:raum,<sup>4</sup> Bayer and CoLaborator,<sup>5</sup> Commerzbank and Main Incubator<sup>6</sup> or Deutsche Lufthansa and Innovation Hub<sup>7</sup> are just a few recent examples of incubation ventures.

The implementation of a corporate incubator helps companies to identify and engage with new fields and opportunities by operating in innovation spaces that are significantly different from the existing business, and in which possible solution approaches and necessary business capabilities and models are usually only

little understood or mastered. A corporate incubator serves as a platform to support the development and success of internally generated ideas or enter into an exchange with external start-ups. It provides a protected space for ideas and topics that may otherwise be sacrificed to the core business's demands.

1. C. M. Christensen, *The innovator's dilemma: when new technologies cause great firms to fail*, Harvard Business School Press, 1997.
2. M. L. Tushman and C. A. O'Reilly, "Ambidextrous Organizations: Managing Evolutionary and Revolutionary Change," *California Management Review*, No. 4, 8-30, 1996.
3. C. M. Christensen, *The innovator's solution: creating and sustaining successful growth*, Harvard Business Press, 2003.
4. <https://www.hubraum.com/profile>, accessed October 2015.
5. <http://www.colaborator.bayer.com/en/index.php>, accessed October 2015.
6. <https://www.main-incubator.com/en/>, accessed October 2015.
7. <http://hub.lh.com/#>, accessed October 2015.



### Resolving the innovation dilemma

Though most companies are well aware of the importance of innovation and expend significant effort into becoming more innovative, they often fall short of attaining truly new innovations and business activities. One major reason for this is the innovation dilemma, especially if the innovation aimed for is not solely incremental but strives for leaps of a more fundamental kind. These usually entail a higher degree of unfamiliarity, greater deviance from existing knowledge and capabilities (often, companies lack the necessary skills altogether) and thus there is higher risk and less certainty of

success. The dilemma arises because the core business and its operational logic often do not support innovative endeavors that stray far from the norm of what the company does. Indeed, they can frequently obstruct such activities.

So, while companies do the right thing and focus on managing and developing their core business, they forgo the opportunities and potential provided by innovation fields that are far from their core business activities. Yet, these are often the areas where most potential lies, from where the biggest threats for the existing business emerge and, likewise, from where the greatest opportunities for successful future development stem.

The obstructive effect of existing structures and procedures is most apparent in the case of more radical innovation, but non-radical innovation initiatives may also have a hard time gaining speed within existing structures. Nascent ideas for innovation of any kind need to be imagined as rather weak and not yet able to survive alone in the harsh reality of the outside world.

A corporate incubator is an organizational structure companies build outside their existing operational structures to facilitate innovation. It is a strategic investment a company commits to, intended to deliver innovation initiatives that have the possibility to emerge and gain traction in a protected environment, freed from the strategic and operational constraints of the core business. The intention is to provide room for the development of new technology

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applications, new product or service offerings and new business models which, if successful, will eventually benefit the core business as well – whether as another single-standing business or as a new feature integrated with, or added to, the existing business offerings.

A corporate incubator is an entity that supports entrepreneurship and the development of promising, but risky, early-stage ideas and ventures. As such, the goals of corporate incubators are not just financial (they are not financial investment vehicles) but primarily driven by strategic motivations that focus on securing long-term profitable growth through innovation activities. They aim to boost innovation performance.

While corporate incubators all follow the same intentions, they differ with regard to the actual setup – strategic and operational. Most often, one can

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find incubators institutionalized as stand-alone, structurally – sometimes even spatially – separate units characterized by different procedural and cultural arrangements exhibiting a strong spirit of entrepreneurial attitude.

**Internal and open corporate incubators**

One significant distinctive aspect in the realm of corporate incubators is the degree of openness, hence the integration of, and collaboration with, external parties. Corporate incubators can be categorized as internal or open.

**Internal corporate incubators**, such as the Audi Production Lab,<sup>8</sup> aim to support and facilitate internal idea generators, providing company staff with the space and resources to proceed with the ideas they have, with the ultimate goal of successfully developing new ventures. They rely only on internally generated ideas or concepts and do not, for the most part, engage in any partnerships or with external sources of knowledge for the creation of business ideas. The primary goal is to increase the generation and utilization of internally developed ideas by taking them and their owners out of the usual business procedures and demands, and providing them with the necessary resources for focused and speedy development.

**Open corporate incubators**, such as hub:raum by Deutsche Telekom,<sup>9</sup> aim to improve innovation performance just as internal corporate incubators do. However, they focus on external ideas

and innovators – such as single inventors or start-ups. They screen the environment for promising ideas and high-potential start-up companies with the intention of forging cooperation. An open corporate incubator provides external innovators with space and resources, as well as access to the host organization's capabilities and experience, in order to speed up business development. Cooperation can have different intensity and formal settings but the general aim is to identify and facilitate external innovators, to join forces, learn and eventually build a successful new business that can, at a later date, be jointly commercialized or integrated into the host organization.

Whether internal or open, a corporate incubator's primary goal is to support both intrapreneurs or entrepreneurs in their efforts to create innovation and new ventures in a mutually beneficial arrangement.

**What are the benefits of a corporate incubator?**

The main advantage for companies establishing a corporate incubator is the facilitation of their innovation potential and performance. An incubator increases the chances for internal ideas to be developed into new businesses or to gain access to new external ideas and technologies. The independent and innovation-conducive setup stimulates a spirit of innovation and eventually facilitates a culture of innovation across the organization.

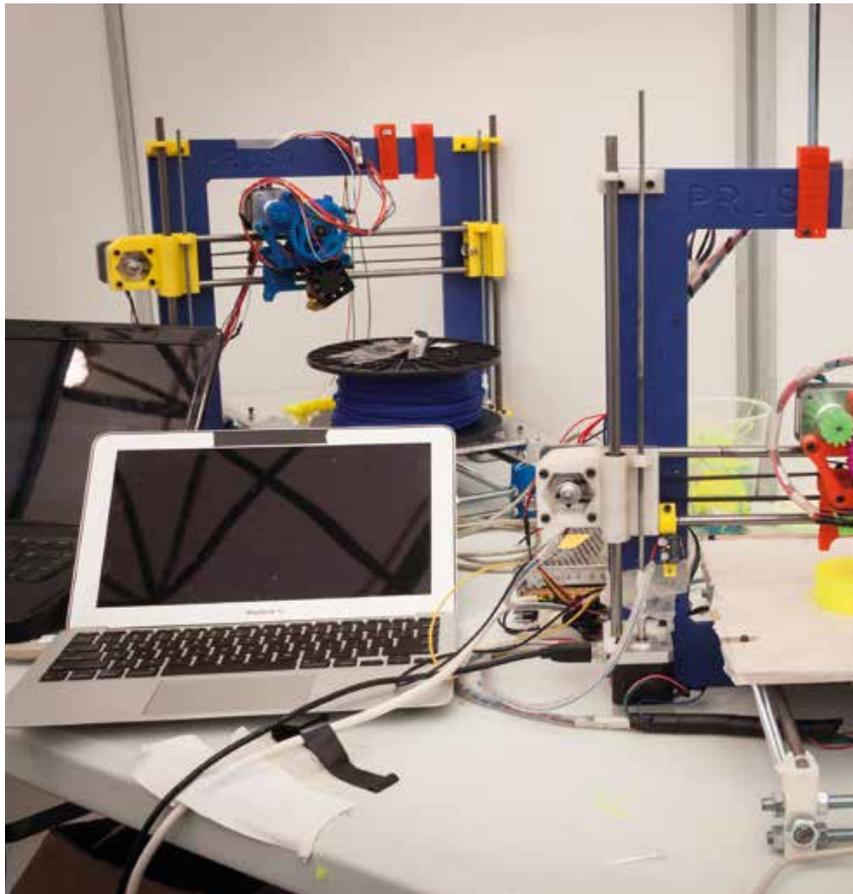
**Benefits of corporate incubators for established companies**

- ▶ Increased potential for innovation
- ▶ Generation of new business activities and competitive advantages
- ▶ Facilitation of internal innovation activities and success
- ▶ Identification of relevant external innovation developments
- ▶ Access to new ideas, technologies and competencies
- ▶ Cooperative development of innovation in a protected environment
- ▶ Facilitation of creativity and innovativeness
- ▶ Promotion of entrepreneurial spirit and innovative culture

In return, the affiliated external innovators (as well as internal idea provider) or start-ups benefit from the different kinds of support an incubator provides:

- ▶ **Infrastructure:** e.g., office space, IT tools and administrative business support services
- ▶ **Mentorship and training:** e.g., individual coaching, courses on methodologies for venture building and presentation and negotiation skills

8. <https://www.audi-mediacycenter.com/en/press-releases/audi-production-lab-journey-into-the-future-4419>, accessed October 2015.  
9. <https://www.hubraum.com/profile>, accessed October 2015.



A corporate incubator provides a protected space for ideas and topics that may otherwise be sacrificed to the core business's demands.

a corporate incubator. Overall, a corporate incubator needs a strategy, a clear organizational setup and an operating model.

#### **Aligning the incubator's strategy to the corporate strategy**

This is regarded as very important and enables the long-term success of the incubator. Involving the top management team in the corporate incubator ensures exactly this alignment and is critical for securing funding and resources, facilitating decision-making and generally providing legitimacy for the setup and operation of a somewhat extra-organizational facility. For these reasons, a dedicated incubator strategy is needed with direct involvement from top management.

#### **Communication**

Beyond strategy, an incubator also needs a specific and dedicated communication concept, as its existence can sometimes be contested. The incubator's importance, ambitions, objectives and its range of activities need to be communicated to the rest of the organization to gain crucial commitment and alignment.

- ▶ **Advice:** e.g., business essentials, management, technological assistance, legal advice and staffing
- ▶ **Network:** e.g., relationship building within the incubator, the host company and its extended network
- ▶ **Resources:** e.g., funding (such as seed investment), skills and capabilities (including technology or production and marketing), experience and business or R&D aptitude of the host company.

#### **Building and running a corporate incubator**

As every incubator should be well fitted to the objectives, organizational arrangements and business environment of the initiating company, it is advisable to design an individual and specific corporate incubator concept aligned with the company's purposes and possibilities.

EY has identified the critical pillars that need to be considered in order to successfully establish and operate

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**Organizational setup**

A corporate incubator needs a decision body, a core team and support functions. It also needs to define roles and responsibilities precisely. Finding the appropriate people for the incubator differs for each company. Their characteristics, however, can mostly be defined as entrepreneurial, visionary and reliable. Incentivizing people in an appropriate manner is essential for motivation and should not be underestimated.

**Operating model**

Processes need to be defined and governance established. Successful incubator implementation requires the definition of dedicated operational procedures while being appropriately aligned with the existing operational arrangements. It is essential that a dedicated end-to-end incubation process is established and that this process, and hence people, are supported by appropriate methods and tools. However, this process also needs to be well integrated with the core organization to avoid frictions that may arise from possible communication gaps between the incubator team and the corporate scouting or product and technology development units, or from the demands of elaborate and diverse process steps already practiced in the organization.



**Funding**

A dedicated budget for the appropriate and sustainable operation of an incubator is vital to guarantee long-term success. It is also very important to implement a performance measurement approach adjusted to the respective incubator approach. The existing accounting and reporting systems are also challenged by the implementation of a corporate incubator. Thus, appropriate support functions need to be ensured and the extent of shared functions utilization should be clarified before an incubator is established.



EY has identified the critical pillars that need to be considered in order to establish and operate a corporate incubator successfully.

## Conclusion

The setup and implementation of a corporate incubator is an extensive and complex challenge. A multitude of strategic, organizational and procedural questions arise and need to be aligned with the way the company normally operates. This is why EY takes a holistic approach when assisting companies to build corporate incubators that are fit for purpose.

Setting aside this complexity however, incubators can deliver a raft of benefits. If you are seeing new technologies, business models and players making their way into your industry, and you are aware that your competitors have already started seeking new business opportunities while your company lacks the innovation performance it could have, it may well be worth establishing a corporate incubator.<sup>10,11,12</sup> ■

10. C. M. Christensen, *The innovator's solution: creating and sustaining successful growth*, Harvard Business Press, 2003.
11. A. Hoffmann, „Die „Corporates“ entdecken die deutsche Startupszene,“ *Gruenderszene*, 2015, <http://www.gruenderszene.de/allgemein/trends-2014-corporates>, accessed October 2015.
12. J. G. March, "Exploration and Exploitation in Organizational Learning," *Organization Science*, Vol.2, No.1, 71-87, 1991.