

# *Scouting of Early-Stage Start-Ups*

## *Development and initial test of a conceptual framework*

**Roland Heinz**

*Munich University of Applied Science  
Lothstrasse 34, D-80335 Munich, Germany*

**Herbert Gillig**

*Strascheg Center for Entrepreneurship,  
Heßstrasse 89, D-80797 Munich, Germany*

**Yannic Stephan**

*FERCHAU Engineering GmbH  
Steinmüllerallee 2, D-51643 Gummersbach, Germany*

*Abstract* — For accelerators, investors and innovative companies, scouting of early-stage start-ups is a most important activity to initiate business deals as investments and partnerships. We therefore executed eight semi-structured expert interviews and an online-survey (n=31) to allow us to propose a new conceptual scouting framework. The framework consists of seven activity fields which can be grouped into three levels – execution level, management level and ambassador level. To prove the functionality of the conceptual scouting framework, we tested the management level in practice by applying it to a partnership programme. In this programme, a start-up accelerator and a corporate venture capitalist from the field of additive manufacturing/3D-printing closely collaborate in order to qualify new ways of deal sourcing.

*Keywords* — *entrepreneurship, conceptual scouting framework, early-stage start-ups, acceleration, venture capital, business angels, deal-sourcing, additive manufacturing.*

### I. INTRODUCTION

The market success of start-ups can be leveraged by precisely timing their ‘triangle of innovation successes’, the quality of the founder team, its underlying business idea, as well as by external start-up enablers [1]. The latter are incubators, accelerators, business angels, venture capitalist and innovative companies. They all wish to create business relations with early-stage start-ups.

In Europe, from 2015 to 2016, venture capital investment increased by 16% to 6.4 billion €. 23% of this amount was early-stage start-up financing [2]. In the same period of time, the number of German accelerators increased from 26 (2015) to 42 (2016) [3, 4].

From these numbers, it can be deduced that deal-making with start-ups is a growing and competitive business field. It forces enablers to identify and approach start-ups right at the beginning of their early-stage phase in order to bypass competitors. However, early-phase start-ups – especially in their seed phase – are very difficult to identify and address. They often have no registered office, no internet pages and/or do not actively communicate with the outside business world. For this reason, it is most important for enablers to understand, and to apply, processes that are well-suited to generating a promising deal-flow.

Consequently, in this paper, we shed a light on German enablers and try to analyse how they approach early-stage start-ups. We furthermore propose a conceptual framework that provides enablers with new systematic insight in the field of early-stage start-up scouting.

### II. STATUS-QUO

Scouting of early-stage technologies has been already investigated in the realm of open innovation [5-8]. In the innovation model by O’Connor and DeMartino (2006), the discovery phase combines all the activities which generate, identify, elaborate and visualise opportunities [9]. In this context, Tartarczyk (2009) develops a first model of technology-scouting [10]. Hossain et al. (2016) give an overview of the most important publications in the field of open innovation [11]. Moreover, in their innovation radar, Tikhvinskiy et al. (2016) describe structured pathways for the systematic scouting of technologies [12].

In their review article, Suman et al. (2012) analyse the behaviour of venture capitalists by reviewing 284 articles from 2005 to 2012 [13]. In his study, the authors came to the conclusion that “The major focus of research on operations has been on value-creation, acquisitions, and deal-structuring. Further research on financial engineering, relationships between general and limited partners, and deal-sourcing is missing.”

However, for accelerators and incubators, no significant research has been able to be identified so far. In 2016, the EU|BIC Network published the results of a survey form 2014, which they had executed within the pool of their members (innovation centres/incubators/business centres, n=128). The study differentiates several lead-generation activities, but gives no recommendation for how scouting in a business organisation shall be executed or structured [14].

### III. RESEARCH APPROACH

To overcome the very limited number of studies in this field of research, we chose an exploratory research design that consists of two parts, semi-structured interviews and an online-survey.

### A. Semi-structured interviews

In a first step, we interviewed eight leading managers of selected German enablers (accelerators, VC/BAs, established companies). The semi-structured interviews were analysed and categorised by MAXQDA [15]. The software gives a keyword histogram and reveals how these keywords are linked with main facts of the interview. From the analysis, we can summarise our principal findings as follows:

- No enabler was able to describe a structured scouting process that he or she applies. However, most of them combine different fields of action to identify early-stage start-ups. These fields of action were, in most cases, adopted from colleagues or network partners.
- Desk research is perceived to be the most important method, followed by network and event activities, as well as their organisation's marketing activities.
- In most cases, marketing activities are passive instruments, such as their internet pages, in order to promote the corporate brand or the scouting message.
- Branch or business-field specific investments need the higher internal qualification of employees, in order to deal with start-ups on 'eye-level' or to be integrated into branch-specific networks.
- The tracking or pre-development of potential future deals, for a period of several months before a deal becomes attractive, are not applied or not applied in a structured way.

These findings provide an initial insight into how enablers understand and execute the scouting of early-stage start-ups.

### B. Online-survey (n=31)

The online-survey was designed to shed a closer light on the following four fields, *networks*, *events*, *own search* and *marketing*. We asked the participants to answer seven questions by making use of an anchored rating-scale (1 to 5), or asking for frequency indications in specific categories. 75% of the respondents were investors, 15% belonged to accelerators, and 10% to start-ups services, such as banks and law firms.

From Fig. 1a, it can be deduced that individual searching is felt to account for only one-third of all the scouting activities (32%). The most important activity is scouting by making use of networks and events (43%). 90% of the interviewed enablers make use of events (Fig. 1b). Branch-specific networks are most often mentioned (35%), followed by pitch events (30%) and jury membership for start-up awards (19%).

As indicated in Fig. 1c, the most important network partners for deal-flow generation are other investors, such as venture capitalists and business angels (36%), followed by accelerator agents (16%) and entrepreneurs (16%). This can be traced back to the fact that venture capitalists often create

syndicates with other venture capitalists. For several German public capital funds, co-investment by private investors is even a prerequisite to invest in start-ups. Institutions which organise business plan competitions for start-ups (7%) and scouting services (6%) obviously still only play a minor role for enablers.

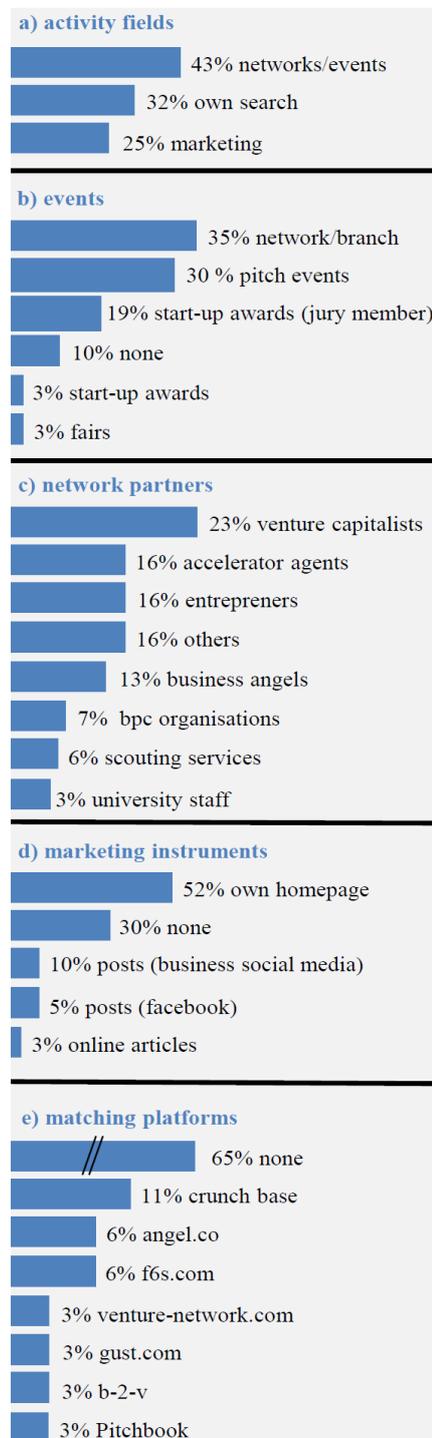


Fig. 1. Online-survey on scouting of early-stage start-ups (n=31), a) activity fields, b) events, c) network partners, d) marketing instruments, e) matching platforms.

Marketing instruments are not applied by all enablers. One-third of the enablers feel that marketing methods have almost no significance when approaching promising deals with start-ups (Fig. 1d, 30%). 52% rely on rather passive digital marketing instruments, like corporate internet pages. Only 18% of the interviewed enablers execute social media marketing or use social media networks (LinkedIn/Xing) or online tools as start-up newsletters; online matching platforms are not standard tools for start-up scouting either. Only one-third of the interviewed enablers make active use of this scouting instrument (Fig. 1e, 35%). The best known online platforms are crunch-base (11%), angel.co (6%) and f6s.com (6%).

The semi-structured interviews and the online survey reveal that scouting of early-stage start-ups is a multi-field matter which is still dominated by offline activities, such as people-based physical networks and personal visits of events. Active online tools, such as social media marketing (posts/blogs/articles) and the use of digital matching platforms, still play a subordinate role. This correlates well with the field of classic M&A activities, where online deal-sourcing has grown from 2013 to 2015, although it is still of minor importance [16]. This interlinks study (n=700) proves that, in 2015, 50% of people asked made at least one online deal, 28% made more than five deals per year.

#### IV. CONCEPTUAL SCOUTING FRAMEWORK

Based upon existing scouting literature, especially in the field of technologies, and the results of our interviews and surveys, we can propose the following conceptual framework for the scouting of early-stage start-ups (fig. 2). It consists of seven activity fields and is structured in three hierarchical levels.

The execution level indicated in Fig. 2 is the basic operational level of a start-up scouting agent. We have separated this level into four main activity fields: *desk research*, *events*, *networks* and *(social media) marketing*. Desk research helps scouting agents to identify the appropriate information and literature, to look for networks, network-partners and events and to sign up for newsletters. Moreover, desk research includes active searches on matchmaking platforms, cold-calls of identified start-ups, competitor analysis and mapping of the underlying market.

Events, such as fairs, summits, conferences, pitch-days and business plan competitions, help the scouting agent to both build-up branch-specific knowledge and to find people that he or she can integrate into his or her personal network. Events are important marketing and communication platforms to broadcast scouting messages. We therefore believe that participation in events should be executed as actively as possible. Talks with a scouting focus, participation in a jury or

at podium discussions will certainly help to boost the organisation's visibility.

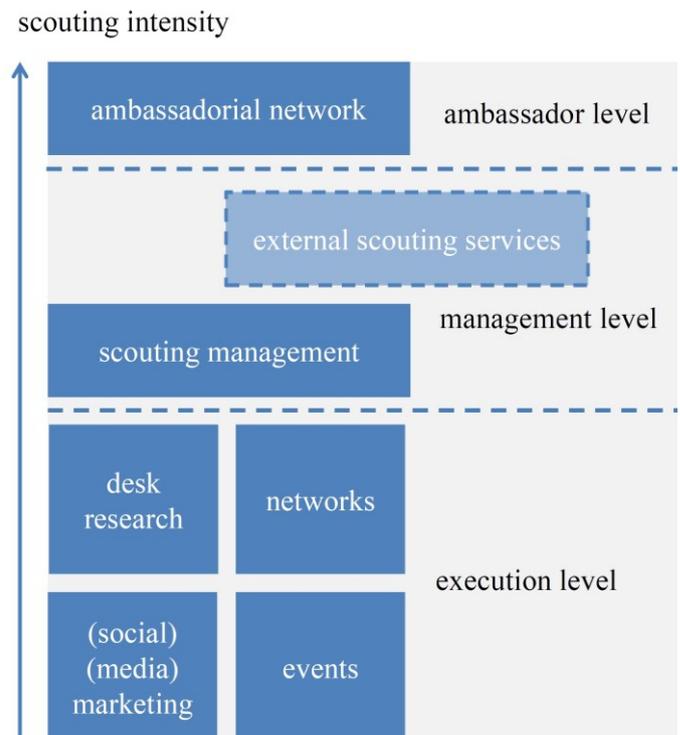


Fig. 2. Conceptual framework for early-stage start-up scouting. The framework consists of seven action fields and is vertically structured in three hierarchical levels.

Successful scouting agents have to rely on a personal network that leverages their deal-sourcing activities. The network nodes should stem from other enablers, such as business angels, investors and accelerators, but should also include experts in different branches, universities and research centres. Furthermore, we recommend the integration of entrepreneurs and successful founders and becoming a mentor for start-ups in order to develop a good sense for the start-up culture and to transfer and exchange information and knowledge.

Most enablers we interviewed were not experts in marketing and social media activities – they rely more on networks and participation in events to fulfil their deal-sourcing targets. Today, almost all enablers have homepages and most of the scouting agents have an account on LinkedIn, Xing and Facebook. However, they have almost no skills related to broadcasting their scouting message in the respective target group; these skills are often not even present within the organisation they work for.

The management level in Fig. 2 adds a professional scouting manager and optional external scouting services, which are available from scouting agencies, to the execution level. The latter shall overcome the hindrance of insufficient marketing and social media skills. On the execution level,

scouting is often a part-time activity. Business angels or investment managers also spend significant time on deal-qualification, contractual work and deal-tracking. The position of a scouting manager, however, we understand to be a full-time activity. Scouting managers co-ordinate their organisation's scouting agents and have great expertise in the activity fields of the execution level that they themselves apply. They are aware of the necessity of marketing and social media for an effective and efficient scouting approach and often integrate external scouting agencies in their activities. The latter support them in professionalising their marketing campaigns, with their media planning and also with helping them to establish and moderate social media groups. Additionally, the scouting agencies provide the scouting managers with extended online and social media reach.

The ambassador level in Fig. 2 is the most advanced level of start-up scouting. Ambassadorial scouting should be applied by enablers who have a very large deal-flow with a multi-branch or a multi-national scope. It adds a network of scouting ambassadors to the organisation. Scouting ambassadors are on the pay-roll of the enabler organisation and report to the scouting manager. This makes them different from other network nodes at the execution level. Paid ambassadors can be expected to generate more reliable scouting results and therefore to provide a stronger contribution to the organisation. Often, next to scouting skills, they have sound branch-specific knowledge which assists the scouting manager in his decision-making process.

#### V. INITIAL FRAMEWORK TEST

In order to test the functionality of the conceptual framework, we applied the management level to an existing scouting challenge. One employee of the Strascheg Center for Entrepreneurship in Munich was assigned the role of the scouting manager in order to identify early-stage start-ups in the field of additive manufacturing/3D-printing. When he started, he was neither experienced in the field of scouting, nor in the field of 3D-printing. This test project was part of a partnership between an accelerator and a corporate investor. It aimed to identify new ways of deal-sourcing.

The scouting manager started at the execution level by creating a new landing-page that made the scouting call public and he integrated himself into branch-specific networks (MUST 3D, 3D Druck Solingen, 3D Netzwerk Berlin). Moreover, he identified a scouting agency (startus.cc) that could deliver sufficient reach for a social media campaign. In only three months, he was able to identify 11 start-ups. Six start-ups were found by help of the agencies' social media call, which proved that the campaign was effective. Out of the 11 start-ups, five were invited to a pitch presentation. Finally, two start-ups were identified as promising candidates for pre-investment coaching and invited to the acceleration programme.

From this test, we deduce that the conceptual scouting framework we propose is suited to identifying early-stage start-ups. Moreover, the test shows that an intense collaboration with scouting agencies, which provide significant social media reach, can leverage the organisation's scouting results.

#### VI. LIMITATIONS AND FURTHER RESEARCH

Although this study is only based on a limited number of interviews/participants, it opens-up a new field of research and already helps to better understand the scouting of early-stage start-ups. Nevertheless, we think that further studies should be executed to deepen understanding of the conceptual scouting framework. We recommend a better analysis of the affected start-up teams' perspective. Moreover, we propose the setting-up of quantitative research design to fine-tune the framework and to develop a scouting model that provides start-up enablers with a precise understanding and monitoring of the overall scouting process.

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