5 reasons why open innovation teams use startup ratings

The use of [startup ratings] is still not commonplace in the innovation world. In fact, until recently the only rating agencies in the market were those that focused on assessing the default risk of listed companies. Standard & Poor and Fitch being the main agencies of reference for such traditional company ratings. But now, **more and more corporates are looking into startup ratings to support their open innovation initiatives**.

For the most part, large companies recognise the value in collaborating with innovative startups and actively seek emerging players with strong growth potential. Already in 2014, research by Brunswicker and Chesbrough showed 78 percent of businesses **globally practiced open innovation** in some capacity. Be it to bring cutting edge solutions to the end user, or to optimise internal capabilities, joining forces with external players can boost a corporate's ability to stay ahead of the curve.

Even so, working with external partners, not to mention young companies, always entails risks. **So how can startup ratings empower open innovation teams?** Let's look at some of the key ways in which they benefit from this type of decision-making tool.

1. Complement traditional due diligence processes

One of the key responsibilities of an open innovation team is to select great companies to partner with. In the case of startups, they not only need to check the fit with their company needs but also make sure that the startup has the potential to grow in the short-term. **Bankruptcy rate is naturally high among young companies**, hence due diligence is a crucial step. Yet, the traditional due diligence process, designed for typical partners or suppliers, is generally ill-suited to innovative companies.

By default, startups lack the history and financial records to demonstrate their stability. It's therefore important to take into account **both qualitative and quantitative factors**. Impactful criteria include:

- the complementarity and experience of the founders
- the legal barriers in the market
- the speed of execution of the technical and commercial roadmap
- the level of innovation of the product…

Open innovation leaders are usually aware of these qualitative aspects but they might not have a standardised approach to assessing them. So startup ratings are a tool to complement the due diligence process. By scoring non-financial growth factors in a statistically proven manner, corporate decision-makers can have **a more comprehensive picture of the startup's risk profile**.

2. Benchmark innovative partners

Some innovation segments are denser and more mature than others. This means that **open innovation teams might struggle to compare and choose the right startup partner** for a specific use case. In more mature markets, such as fintech or adtech, they might be overwhelmed with options. Whilst for very new markets, lack of offer and market data can be significant hurdles in the benchmarking process.

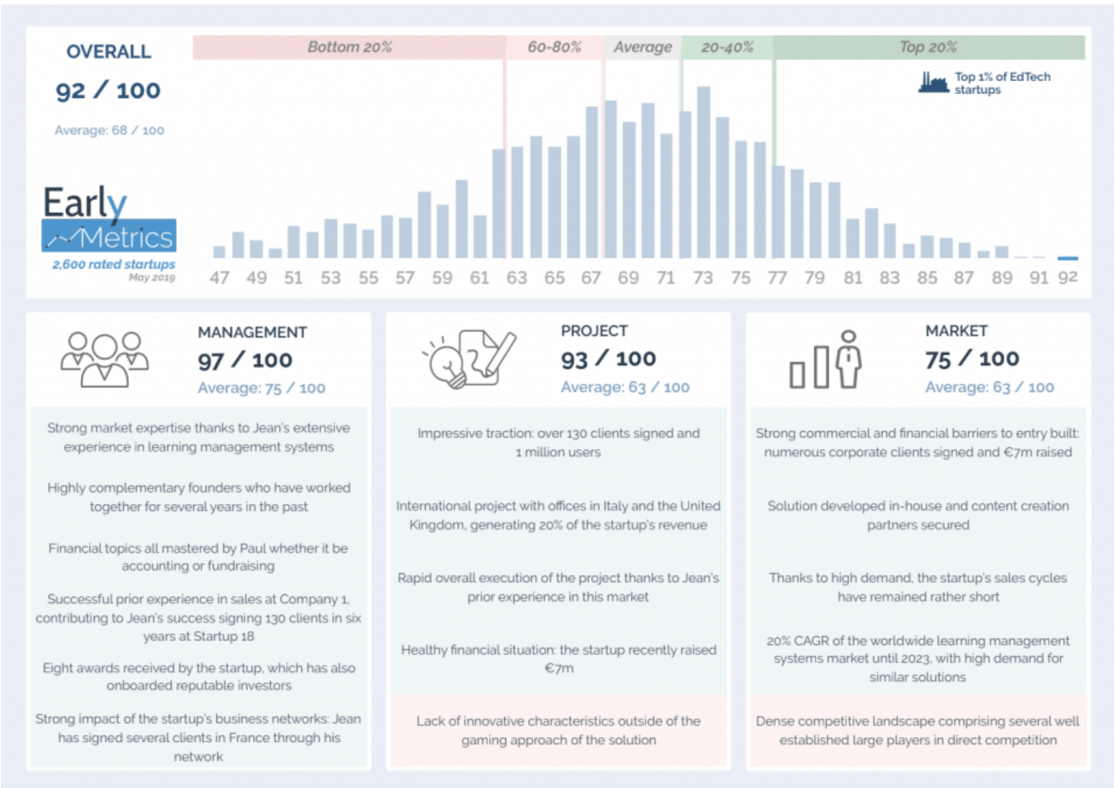
By getting partnership candidates rated, open innovation leaders can have a fair and standardised basis to compare their options on. **The overall growth potential score can help weed out riskier startups** (with a score lower than 68/100). Then, the score by pillar and criteria of assessment can help further refine the selection.

Early Metrics' methodology, for instance, looks at 30 criteria covering the management team, the project, and the market. The algorithms and scoring methods used are backed by academic research and data analysis on over 3000 startups, in a variety of innovative markets. So thanks to the rating, one can see how the startup fairs in terms of growth potential compared to companies of the same maturity and in the same market within Early Metrics' database.

3. Identify weaknesses for the startup to improve on

Some open innovation projects are more oriented towards supporting the growth of promising startups rather than working directly with them. This might be the case in corporate innovation labs, accelerators or even corporate venture capital (CVC) funds. **Knowing where a startup's weaknesses lie is therefore essential to provide the right support.**

A rating can **flag early risks and problems** that could impede a startup's growth, and in turn, its survival. This could be a lack of financial commitment from key managers within a startup. This could threaten the integrity of its team and the ability to execute the development roadmap. Another common example is a lack of barriers to entry built by the startup, which could be solved by registering patents or securing strategic partners. Startup ratings therefore provide an independent audit of a young company, **making it easier to identify key areas of improvement**.



Sample of a startup rating which shows how a startup's score compares to the rest of the startup database as well as key strengths and weaknesses identified in three pillars.

4. Assess the evolution of startup partners

If an open innovation team invests time and resources in startups, they'll want to measure the impact of their support. This is particularly important in times of uncertainty where budgets dedicated to non-core departments, including innovation, are more severely scrutinized.

Being able to clearly demonstrate which startups have developed the most can help select which ones are worth going further with (through pilots, investment…). Moreover, it can help **rationalise the resource allocation for open innovation initiatives** involving startups.

Rating a startup twice in a six month period (or at recurring intervals) provides this tangible indication of progress or lack thereof. By re-rating a cohort of startups, a corporate is also able to **evaluate the efficacy of their open innovation processes** – whether that be in the selection, mentoring or investment phase of the relationship with the startups.

5. Discover the potential of new technologies

The overarching goal of an open innovation strategy is to **discover new ways to address existing needs**, internally for the corporate's teams or externally for its clients. But open innovation can be leveraged for **explorative research** too.

What will be the needs of tomorrow's consumer? Which markets hold most potential for the future? What tools do corporate departments need to be resilient to disruptive trends? The answers can lie within emerging technologies and new companies. Indeed, most tech startups are at the forefront of emerging trends and they are actively shaping the future of all markets.

A startup rating gives an overview of the level of innovativeness of a product or service, as well as an outlook on the potential of the market the startup operates in. Hence, open innovation leaders can use this information to **explore opportunities outside the corporate's core activities and markets**. Early Metrics' rating reports include indicators on the maturity, complexity and depth of an innovative market, which in turn is helpful to assess the fit with a corporate's development strategy.

To sum it up, startup ratings facilitate and accelerate decision-making for open innovation leaders. They provide an independent analysis of potential innovative collaborators, based on comprehensive data and proven scientific methods. That's why corporations such as Barclays, AstraZeneca, LVMH and many others have integrated startup ratings within their open innovation toolkit. Ultimately, they can enable meaningful collaboration between innovative startups and corporates.