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Dear readers

In our recent newsletters we have provided you with different insights into our current thematic focal point: **"Controlling of Start-Ups and Start-Up Initiatives"**. The work on the Dream Car report is about to finish.

In this newsletter we would like to focus your perspective once again on a young Controlling discipline that has not received much attention from us so far: objectives and key results (OKRs). This management discipline, which has become known through its application in Silicon Valley and has now made the leap to Germany, refers primarily to a form of performance measurement from a management perspective.

We also want to delve into the valuation of start-ups. Finally, we return to our primary focus by reviewing the example of the Internehmertum programme from TRUMPF's Open Innovation Initiative.

We hope you enjoy this issue.

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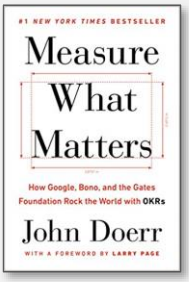
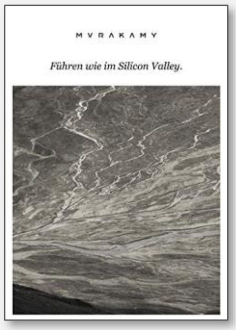
Reading tips

Measure What Matters from J. Doerr is a management system based on objectives and key results (OKRs). The objectives show us the direction we want to go. "The colonisation of Mars" could have been a good objective for SpaceX. The aim is to make results measurable and plannable: "What do I want to accomplish and what must I do to achieve it?" Setting an objective determines the direction. J. Doerr has written a book that establishes a foundation for performance measurement using OKRs. In doing so, he has created a basis on which both numerous start-ups and established companies have been built since then.



F. Alberti in his book **Führen wie im Silicon Valley** ("Manage like in Silicon Valley") not only provides the first foundations for OKRs, but also offers helpful hints for implementing them in the reader's own company. The reader can obtain a quick overview of the benefits of this management approach. At the same time, the book draws attention to the typical errors companies make when implementing this technique.



The leap of OKRs into the German start-up scene | Thematic foundations for OKRs

In 1999, when John Doerr made a presentation at Google on the new way of thinking about objectives and the closer link with strategies, he probably could not imagine how widespread his ideas would become in the future. Today, the California start-up and high-tech scene cannot get by without objectives and key results (OKRs) – the concept is increasingly popular in Germany, too.

Objectives and key results – or in short: OKRs. A very result-oriented framework lies at the heart of this technique. The core idea of this management discipline, which became well known through its application in Silicon Valley, differs from traditional performance measurement concepts because it allows objectives to be defined for individual team members. By doing so, the performance of individual members becomes more transparent and accurate. After all, it is very easy for supervisors to lose the overview, especially as the number of team members increases in growing start-ups: "Who is currently working on which topics? Does he/she have problems?" Although OKRs are very similar to the Balanced Scorecard (BSC) concept, OKRs place particular emphasis on shorter-term actual/target comparisons and integration with project management. In other words, a change in thinking has taken place, away from measuring the success of the project towards measuring the performance of employees. While the trend has been ongoing for years in the US, observers have the feeling that OKRs have meanwhile also become more popular in German companies (Handelsblatt, 30/08/2018). Besides Google, companies such as Amazon, Twitter, LinkedIn and Adobe rely on the use of OKRs as well. OKRs are becoming particularly popular in the German start-up and grown-up scene. For example, Zalando, Flixbus, Emma, Trivago and MyMüsli use OKRs to measure the performance of their teams and members.

In the case of Google, a **higher-level objective** is first predefined, which is then broken down into smaller sub-objectives. A so-called **score** is normally set – usually 100%. This is the maximum that the employee can achieve, otherwise the objective has been **formulated** incorrectly. In addition, an anticipated score is determined (depending on the case, but expected to be around 70-80%) in order to motivate employees and to push them to their own **limits**. In practice, these limits also lead to errors and failures – as a **learning organisation**, these experiences are then included in the **next quarterly meeting**.

Amid all the commotion around OKRs, their **success factors** must be taken into account when implementing them. First, the core idea of the whole organisation should be presented so that every member of the team **clearly understands** that the introduction of OKRs will not result in extra work for the traditional employee. Instead, employees should understand that this approach makes it possible for them to track their own individual performance in terms of details and results. In addition to this appropriate communication, a certain degree of transparency must be created: everyone can see the success. Furthermore, OKRs should **not measure via dichotomous objectives**, but rather in a targeted manner through KPIs. The question is whether OKRs will stay longer in companies than the BSC method, but in that regard only time will tell.

OKRs are not limited to just start-ups and tech companies. Adequate preparation and implementation are all that is needed to put this discipline into action. If appropriate objectives have been formulated, the next step is to assign to them measurable key results that can be achieved in the subsequent period (usually the next quarter). Experience has shown that ambitious objectives are usually set, which means that achieving a score of 70% is outstanding. Figure 1 provides a further overview.

BRIEFING ON OKRs

Summary	Success factors
➢ Objectives should be specified using **milestones**. ➢ An overall objective can be broken down into **subobjectives** in a second step in order to address different departments and members. ➢ **Responsibilities** must be assigned to the subobjectives so that the **success** of individual teams and members can be assessed accurately.	✓ Creation of **transparency** for individualised performance measurement. ✓ **Granular** assessment of objectives and requirements. ✓ At least one review per **quarter.** ✓ Measurement via **KPIs** and not through "yes/no" results. ✓ Autonomous teams that are easily disbanded, tasks are highly formalised through objectives (and thus also responsibilities).

Figure 1: Overview of OKRs

Valuation of start-ups | Selected methods to value start-ups

How do you value start-ups in early stages of development, or when their ideas are not yet mature? The following section presents selected valuation methods and, in particular, the calculation methods that business angels prefer.

Fundamentally, the valuation of start-ups and business ideas is not always trivial. If you imagine a start-up in its establishment phase, it is very difficult to match the value of an investment with shares in the company: either the business idea functions and financial income is highly likely, or not. This view is also shared by Darryl Wash, a famous venture capitalist.

For that reason, the following section presents **valuation methods** that deal with this challenge. It should be noted, though, that the valuation methods which refer to ideas in their early stages rarely determine an actual equivalent value. In addition, there is no such thing as *the* best valuation method; each approach has its strengths and weaknesses. Often the methods do not even attempt to calculate the company value precisely, rather they seek to specify a **range**.
Investors frequently rely on simple and quick-to-perform calculations. These include **multiples**, for example, which are used to calculate a relative market value based on the value of comparable companies. Comparable companies are benchmarked to derive metrics that can be applied to the new business idea or start-up. Investors can use multiples for companies that are traded on the stock exchange (**trading multiples**), and for companies which have just been sold (**transaction multiples)**. Here, however, investors must take into account that companies often pay a premium of up to 50% on the multiple in order to purchase the company. Although the use of multiples is primarily a static approach that does not consider the future development of the company, it is probably the **best known and most commonly used method** to value start-ups. Multiples are based on publicly available data. A method that stands in contrast to multiples is the **discounted cash flow method**, which involves **forecasting** expected cash flows and discounting them to their present value. In addition, this approach includes a final value, called a **terminal value**, which is likewise discounted. The application of this method is very complex and frequently requires the use of comprehensive internal company information.

Additional simple methods include the **Berkus Method** and the **1/3 Rule**. Dave Berkus developed a standard formula that uses the following considerations to calculate the valuation of start-ups: a good idea (USD 1 million), a successful prototype (USD 1 million), the management team (USD 1-2 million), the board quality (USD 1 million) and already successful sales (USD 1 million). The valuations refer to an “up to” value. This calculation is quite simple and understandable.
Many other business angels rely on the 1/3 Rule, which assumes that 1/3 of the investment goes to the founders, 1/3 to the investor and 1/3 to the management, which must be decoupled from the founders. This differentiation is not always easy, which makes this valuation approach significantly more difficult.

In **Germany**, investors rely on a rule of thumb that assesses valuation and investment rounds. **Investment amounts between EUR 500,000 and EUR 1 million are particularly popular** in this regard. The analysis assumes that founders who want to collect less than EUR 500,000 are thinking too small, whereas those seeking a sum over EUR 1 million appear too greedy for the beginning.

Besides these traditional valuation methods, other factors affecting the company’s value must also be kept in mind. For instance, unique products, low dependencies on employees and customers, and good customer relationships tend to increase value, while value is diminished by low market entry barriers (and thus potential imitators), as well as individual dependencies on suppliers and on major customers that account for a high proportion of revenue.

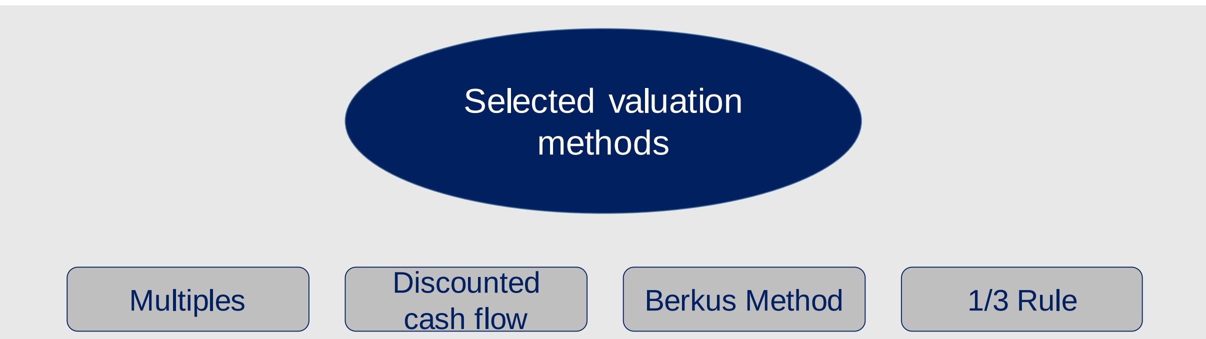


Figure 2: Selected methods to value start-ups

Focus on incubators | Showing the possibilities based on TRUMPF's Internehmertum

TRUMPF uses its Internehmertum incubator programme not only to encourage its own employees to deal with new, innovative business ideas, but also to reach business areas that are outside its core business but within the strategic vicinity of the company. Controlling pays a significant role in this regard.

Innovations are an integral component of TRUMPF's corporate strategy. The Ditzingen-based high-tech company, which has manufacturing solutions in the fields of machine tools, laser technology and electronics, also develops solutions with start-ups. Under its **Internehmertum** in-house programme, employees can validate their own business ideas. To do that, they are initially released from their regular work responsibilities for up to three months and are given a budget of EUR 30,000. What is behind the idea?

TRUMPF regularly analyses new lines of business and markets. Its focus is primarily on business models that are outside the existing business but which nevertheless have a high strategic fit with the company and should therefore be developed and implemented **internally**. To achieve that, TRUMPF gives its employees the freedom necessary to pursue new ideas and then to validate them. In addition, it coaches these employees separately again; they should be able to think entrepreneurially outside their areas of responsibility. Besides this incubator activity, TRUMPF also acts as a corporate venture capitalist (CVC) by acquiring a minority interest in (external) start-ups that already exist.

In the first three months of development, the potential founders develop a rough business model and business plan. A **minimum viable product (MVP)** should be developed as well. After these three months, TRUMPF reviews whether the idea can be continued as an independent business model. If the idea passes this check, the employees have time over the next 6-18 months to develop a **prototype** and a mature business plan. In addition, they analyse the product-market fit. If the employees are able to convince the programme's decision-makers at this check, they then consider how to proceed with the idea. Fundamentally, the business idea can be pursued either in the form of an internal start-up or as a spin-off (internal projects are not the target or focus, rather they are a by-product of the process). Business ideas are also terminated in a targeted manner if, for example, they do not have sufficient market potential or growth opportunities. TRUMPF Internehmertum currently measures the success and valuation of the ideas via **key figures**, e.g. "number of trained employees" or "number of rounds per year". The ideas cannot be evaluated according to traditional in-house procedures in Controlling, however. Instead, they must be assessed as separate, detached business plans. TRUMPF has separated the Internehmertum project spatially from the other locations in Ditzingen. The company has also put in place a top-management committee that monitors the ideas currently being pursued and decides which new business ideas to foster.

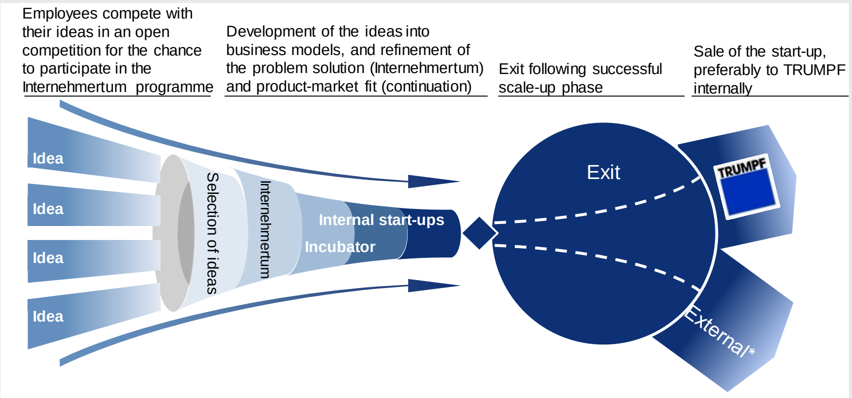


Figure 3: Example process of the evolution of an idea into a product in TRUMPF's Internehmertum's process

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