Navigating Early-Stage Ideas: Certain Strategies for Uncertain Terrains

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Many types of organizations face the challenge of evaluating, selecting, and cultivating early-stage ideas. Companies may strive to nurture innovation and entrepreneurial projects. Venture capital firms may seek an edge in earlier stages of a startup's lifecycle. Universities may desire to commercialize their inventions. Governments and other organizations may aim to improve local entrepreneurial ecosystems. The value of new ideas is extremely difficult to predict, yet investment decisions often need to be made under substantial uncertainty.

Strategies that cost-effectively reduce the uncertainty of ideas in their nascent stages can create immense value, either for individual companies or for an ecosystem. Such strategies need to address two questions. First, how to effectively select ideas based on the signals about their potential already collected by consulting with experts, conducting experiments, or testing consumers. Second, perhaps more importantly, how best to collect these signals in the first place.

The framework developed in the attached article is based on four unique strategies in a wide variety of settings that I teach in my second-year elective course at the Harvard Business School (see a brief description below):

- *Flagship Pioneering*, an integrated life sciences innovator that, while financially structured as a conventional venture capital fund, creates two thirds of its portfolio startups in-house "from scratch." (It is the parent company that created and spun off *Moderna*, one of the two companies that have developed the MRNA Covid vaccines.)
- *The Black List*, a highly anticipated annual publication in Hollywood that ranks the year's unproduced scripts based on nominations from hundreds of film executives;
- *Y Combinator* (YC) and *Creative Destruction Lab* (CDL), two accelerators that focus on consumer-tech and deep-tech (engineering- and science-based) startups, respectively.

These organizations make strikingly different choices regarding the two questions described above—some are (or enable the relevant decision makers to be) very choosy about advancing ideas based on the collected signals, while others are more relaxed; some develop structures and processes that aim to make each signal more accurate, while others focus on collecting a large number of signals and tolerate their low accuracy—yet each has achieved success in its respective area.

The framework provides a useful lens to understand these very different strategies based on three types of factors: i) costs of failure relative to success; ii) the cost and accuracy of signals; and iii) the fundamental market imperfections associated with the production and exchange of intangible knowledge (ideas, information, and judgments).

<u>A brief description of the elective course "Good Strategies in Flawed Markets."</u> Based on economic theories of market imperfections, the course is designed to help students better tailor a firm's strategy to its environment, which requires an understanding of both the competitive landscape and how it is shaped by laws, regulations, and norms. It consists of two modules: Module 1 deep-dives into private responses to market imperfections (competitive strategy); and Module 2 focuses on public responses to market imperfections (non-market strategies). The framework and the four strategies that I describe above form one sub-module in Module 1 of this course.