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ROCKET INTERNET: RISE OF THE GERMAN SILICON VALLEY?[1]

> There is a romantic concept of what tech innovation is . . . there's always an Einstein, a pioneer who defines the first category. But take the first car — it looked horrible, you would never want to use it, and you would never make a market for it. It took someone like Toyota to work harder, make it cheaper and bring it faster around the world.
>
> — Oliver Samwer, CEO and co-founder of Rocket Internet[2]

INTRODUCTION

It was the evening of October 2, 2014, and the co-founder and chief executive officer (CEO) of Rocket Internet (Rocket), Oliver Samwer, was sitting quietly in his firm's head office in Berlin, wondering what the next move should be for his company. Earlier that day, Rocket had completed an initial public offering on the Frankfurt Stock Exchange, but the share price had fallen 13 per cent by the market close, suggesting that investors may not have been as confident about Rocket's future as he had hoped.[3] Despite Rocket's early successes in building and selling startups, its business model had been questioned by numerous industry analysts and high-profile Silicon Valley investors, including Peter Thiel.[4] Considering the recent events, Samwer wondered whether it was the right time to continue Rocket's rapid global expansion, or whether any changes to the operating model were needed to build confidence with Rocket's new shareholders.

COMPANY BACKGROUND

Founded in 2007 by Oliver and his two brothers, Marc and Alexander Samwer, Rocket was designed to be a "United Nations of entrepreneurs."[5] The company invested in Internet startups and proactively managed the growth of each investment, with much greater involvement than many typical angel investors and venture capital firms.[6] Oliver and his brothers sought to "build a global galaxy of firms with Rocket at the center."[7] As of 2014, Rocket's businesses had collectively targeted 5.4 billion consumers around the world and 74 per cent of global mobile phone users.[8]

Evolution of Rocket's Operating Model

Rocket originally developed its reputation as a "copycat" of businesses — taking high-growth, proven business models in Internet e-commerce, and launching adapted versions of these businesses in other parts of the world. The proven business models often originated in the United States, and Rocket had historically focused on launching its copycat businesses in Europe and other global markets outside of North America. In its early days, Rocket built functional businesses rapidly before selling them relatively quickly, often to the same firms that had developed the original idea behind the business model.[9] However, as the firm evolved, Rocket shifted its strategy to act instead as a hybrid between a consultancy and a venture capital firm for startups with the potential to be imitated successfully across global markets.[10]

Fundamentally, Rocket invested in technology startups in their rapid-growth stage, improved their business performance and ultimately divested control, either through an equity offering or by selling to an acquiring firm. For example, Rocket successfully developed CityDeal, a German version of Groupon, which launched in 2010, and was subsequently sold to Groupon for $170 million.[11] To differentiate its company, Rocket employed highly unconventional tactics, from the choice of startups it worked with to its preferred promotional marketing strategies. Rocket targeted opportunities in e-commerce, financial services technology and computing hardware, areas that many entrepreneurs tended to avoid because of the complexity involved in launching a product or service in these industries.[12]

Startups generally approached Rocket in their high-growth stage with the goal of increasing both the speed and scale of their growth. Rocket rarely needed to search for investments.[13] Rocket typically took a majority stake in the company, often upward of 80 to 90 per cent of shares outstanding, and would seek future external funding as needed.[14] Affiliated companies were generally attracted to Rocket because of three reasons: 1) the firm's global network of relationships, which made subsequent external funding more accessible; 2) the firm's management expertise, which provided companies the opportunity to learn to build businesses "the Rocket way" and 3) the firm's coordination of the execution between global headquarters and local market levels, which facilitated global expansion.[15] Rocket offered a platform for e-commerce startups to reach markets around the world, and provided human capital to assist in expansion by sending individual Rocket employees who worked across all divisions of the business, ranging from human resources to business intelligence.[16] By affiliating themselves with Rocket, these startups gained access to untapped markets around the world, and Rocket benefitted from being able to expand its umbrella of products and services for mobile and e-commerce platforms to emerging markets and Europe.[17]

Rocket executives looked at companies pragmatically, evaluating whether firms had the necessary economies of scale that could be transferrable through geographic expansion.[18] Once partnerships were established, Rocket sent in teams of entrepreneurs-in-residence to run the firms as business managers; all team members were Rocket employees who had been trained to execute Rocket's business practices and achieve operational excellence.[19] These entrepreneur teams were entrepreneurial only by title and generally did not consist of actual entrepreneurs, but were given decision-making authority as long as they operated within Rocket's defined operating processes. Rocket had developed standardized processes for improving its businesses, employing both "centralized" and "local" improvements.[20] The entrepreneur teams began by deploying centralized improvements, such as streamlining financial reporting processes and business intelligence analytics. As the teams gained a thorough understanding of the business and its local environment, improvements became more optimized and local improvements were then phased in, including the implementation of processes developed for internal operations such as sales and customer care.

Of these operating improvements, 80 per cent were completed within the first 100 days of partnership, and the affiliated startup's performance was assessed on the basis of key performance indicators, such as contribution margin targets. If the business was unable to meet its targets within six months, the business was shut down completely.[21] However, if the business met these short-term goals, then Rocket would hold the startup in its portfolio for up to nine years, with the goal of achieving, within that period, breakeven earnings before interest and taxes.[22] Rocket also considered its involvement to have been a failure if an affiliated business was sold at a loss of €50,000 ($64,000)[23] or more relative to Rocket's initial investment.[24]

By partnering only with companies that fulfilled Rocket's stringent requirements, Rocket aimed to quickly replicate the success of its affiliated companies abroad in foreign markets and overcome its competition through superior efficiency.[25] Rocket's involvement in startups generally followed one of two trajectories: 1) businesses were improved and subsequently sold, or 2) Rocket expanded the business geographically and increased its commitment to building the business globally. In either scenario, Rocket was able to use the startup's original business model and adapt it to other global markets that had a similar need for the product or service. As Rocket operated according to the principle of scaling quickly and rarely accepting failure, it preferred to hire ambitious individuals who had strong analytical skills, often choosing to hire individuals who had previously worked at consulting firms and investment banks as opposed to individuals whose previous work experience was more creative or technical (see Exhibit 1).[26] To incentivize employees, Rocket offered not only a salary comparable with the offerings at professional service firms but also stock options.[27] As of 2014, Rocket had more than 20,000 employees operating across 104 countries as part of the businesses within its portfolio, of which 1,902 were considered core employees of Rocket.[28]

Company History

The Samwer brothers spent their childhood in Cologne, Germany, and were born within four years of each other.[29] Marc, the eldest brother, had a master's degree in law from the University of Cologne and had graduated top of his class.[30] Oliver noted that Marc was the best of the brothers at executing strategies on behalf of Rocket. Alexander, the youngest brother, had a master's degree from Oxford and an MBA from Harvard Business School; he was deemed the most intelligent of the three and the brains behind Rocket.[31] Oliver, a business graduate from the WHU Otto Beisheim School of Management in Germany, was viewed as the driving force behind Rocket and was described as "1000% intense, 0% nonsense, and 100% rational."[32]

All three Samwer brothers had been close since childhood, and were inspired to start a business together after having observed their parents, who were lawyers. "You learn very early on about hard work, about the good years, the bad years, serving clients. . . . It's like attending a mini business school for entrepreneurship," recalled Oliver.[33] Inspired by the low-cost airline revolution of the 1980s, the brothers originally wanted to start their own airline company, but were deterred by the significant upfront capital investment and experience needed to succeed.[34]

During the 1990s, the brothers moved to Silicon Valley, attracted by the allure of the Internet Revolution.[35] At the time, Oliver had started his first company, Ego International Trading Company, which produced and distributed shoes in South America.[36] Fascinated by the success of the web browser firm Netscape and the rise of technology gurus such as Steve Jobs and Bill Gates, the Samwer brothers attended as many talks as they could to learn about the global connectedness of the World Wide Web.[37] They became inspired after hearing one of Steve Jobs's speeches in the mid-1990s at Stanford University, when he told students to "forget investment banking, forget consulting, go to Europe and find love."[38] The brothers interpreted Jobs's statement to mean they should find inspiration in Silicon Valley for a business that they would love to start in Europe.[39]

While working as interns in Silicon Valley in 1998, the Samwer brothers learned about the online marketplace eBay and were surprised by its popularity.[40] Knowing that Germany had restrictive