

Case Study:
**CICSO Systems - A Novel Approach to Structuring
Entrepreneurial Ventures**

Group G

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CISCO Systems:

- Leonard Bosack and Sandy Lerner, husband and wife computer scientists at Stanford University who invented a technology to link their disparate computer systems together founded Cisco Systems in 1984.
- Cisco began by offering high-end routers primarily in the LAN (local-area network) market. The devices were the traffic cops of cyberspace – they directed network traffic to its final destination via the most efficient, least congested network path.
- By 1997, Cisco made approximately 80% of the large-scale routers that powered the Internet.
- Then entered in the market of global Internet and Corporate Intranets.
- **Core Products:** Routers, LAN switches, (WAN) switches, Web site management tools, Dial-up and other remote access solutions, Internet appliances, Network management software, Internetwork Operating System, etc.

Keys to Successful Mergers:

- The focus of any acquisition is a clear identification of specific technology or product needs as determined in their strategic matrix. So, Cisco knows why it is doing what it is doing; it is not doing deals just for the sake of making investment bankers money.
- The vision of the leader of the company being acquired and the direction the company is headed must be compatible with Cisco's. So if the visions of both the companies are dramatically different it is not advisable to acquire the firm.
- Cisco's acquisition identification process emphasizes cultural compatibility. Cisco acquisitions are typically entrepreneurial, fast-growing Silicon Valley companies that thrive in dynamic markets, with an excellent fit of cultures, values, and chemistry. The fact that Cisco is a player in all the hot network technology areas makes it attractive to the employees of acquired firms.
- Cisco sets very clear expectations as to how the merged entity will function. For instance, specifying who the leader of the combined operation will be and to whom this person will report.
- Cisco manages the change process that accompanies an acquisition quickly. Leaving acquisitions alone doesn't work. Finally, Cisco ensures that there are short- and long-term wins for the stakeholders in both companies. The short term is typically defined in financial terms. In the long term all constituencies, shareholders, employees, customers, and business partners must also benefit. Part of the benefit is ensuring that employees in the acquired company can have a future at Cisco.
- Instead of acquiring large, established, public companies, Cisco typically acquired “small” private companies, for \$200 million or less.⁶ The smaller acquisitions made

integration easier –large, established companies with strong corporate cultures were more difficult to integrate.

Problem Area:

Cisco wants to pursue new networking opportunity of Multi-service networks by entering into market for “Optical Routers”.

Alternatives available:

1. Develop the product internally within Cisco
2. Acquire some existing firm which is making the desired product
3. Start its own external venture and then acquire it using spin-in model.

Pros and Cons of each alternative:

| | Alternative 1 | Alternative 2 | Alternative 3 |
|------|--|--|---|
| Pros | <ul style="list-style-type: none"> • No need to integrate any new company with Cisco. | <ul style="list-style-type: none"> • Minimum time to market • No need to build product as it is already available | <ul style="list-style-type: none"> • Minimum time to market • Can utilize the best talent available in the market • The startup firm can use existing Cisco's assets. • Better incentives to the founders and employees of startup firm via ESOP for retaining them after merger with Cisco |
| Cons | <ul style="list-style-type: none"> • Lack of technological / engineering capability to make the product. • Building the product in-house would take too long – competition made time to market a priority. | <ul style="list-style-type: none"> • Difficult and time-consuming to search for target firm which could meet Cisco's requirements • Retaining key employees of acquired company is difficult | <ul style="list-style-type: none"> • Need to integrate the newly acquired company with Cisco • Failure of startup firm to build the desired product on time could bring loss to Cisco. • Too much interference from Cisco could quash the entrepreneur feel & creativity of the startup firm. |

Flaws in Ardent Acquisition

- Cisco's equity stake in the firm was mere 32%. Considering that they would be helping the Ardent by granting them free access to its assets and intellectual property, it should have got some free equity stake and become a majority holder of Ardent. Thus they would have to pay less money at the time of acquiring Ardent.
- The founders and engineering team of Ardent received huge incentives compared to the Cisco employees helping the Ardent team in integrating the product with other Cisco products. So there were chances these existing Cisco employees might get offended and leave the organization.
- Cisco provided lots of facilities to Ardent like engineering talent, free testing n certificate, business unit expert, software, etc. Licensing IOS software to Ardent for free was contentious as it upset Cisco personnel who felt that the company was giving away Cisco's valuable intellectual property and then paying to buy it back.
- There were no clauses/ guidelines in the deal about how Ardent should market the new product. Thus Cisco had to use the option to acquire Ardent earlier so as to control the marketing strategy of the product.

Improvements possible in PipeLinks Acquisition:

Cisco can avoid the above-said flaws in Ardent acquisition while finalizing the deal for PipeLinks acquisition.

The following are the list of improvements possible in the PipeLinks deal:

- The capital structure of PipeLinks should be such that it would have majority stake in the company. Thus at the time of acquisition, Cisco need not pay exorbitant sum of money to acquire PipeLinks.
- The incentives to the founders and employees of PipeLinks should be such that the key employees are retained as well as the existing Cisco employees are not offended.
- Cisco should license out key assets and products to the startup for a fee rather than free.
- The deal should contain clauses which should prevent PipeLinks from marketing the product without permission from Cisco.