



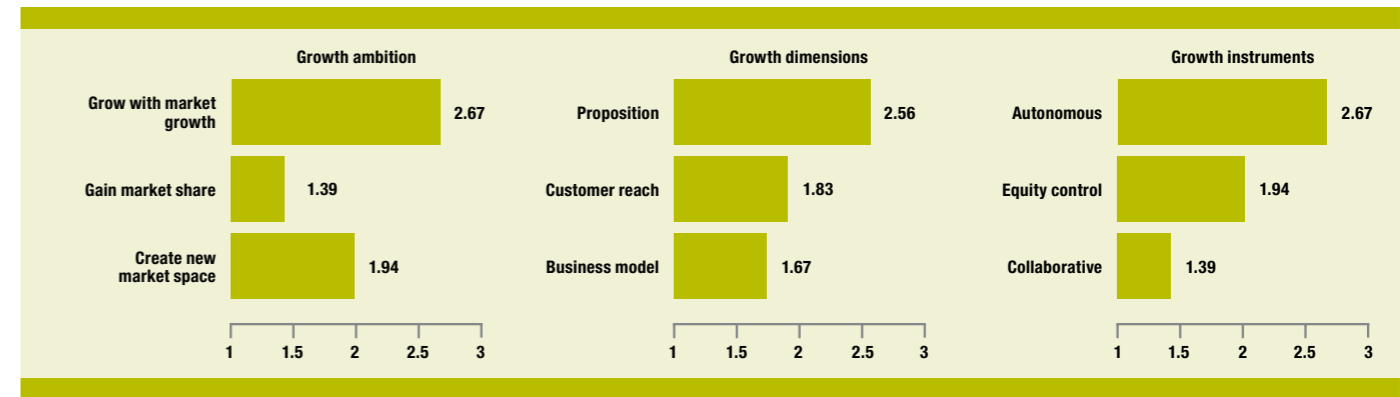
# COLLABORATIVE CREATION: INNOVATING THROUGH ALLIANCES

**A**lliances are important as instruments for realising growth through innovation. Nevertheless, some managers continue to see alliances as a last resort because of the high complexity of alliance governance. This article shows two examples of innovative alliances that have used tailor-made governance structures. It concludes that the fear of using alliances for innovation is unfounded because the risks of collaborative innovation can be mitigated by implementing best practices in alliance governance. Therefore, alliances should not be seen as a second-best option.

## ALLIANCES, POPULAR BUT UNKNOWN

Although growth has returned to the top of many corporate agendas, management is confronted with the task of selecting the best potential growth opportunity and matching it with the best possible growth instrument: i.e. (i) autonomous product and market development within the safe corporate boundaries, (ii) acquiring growth via M&A or (iii) via collaboration in alliances, JVs or networks. A 2005 study<sup>1</sup> revealed that, although alliances are popular and potentially even hyped, corporates remain reluctant to pursue growth via collaboration. They treat it as their 'last resort'. Behind the fully controlled, yet expensive, autonomous business development and the even more expensive growth through acquisition, the relatively cheap instrument of collaboration remains a promising yet under utilised instrument.

The main reason for this underutilisation seems to stem from the reluctance of the current generation of executive managers to operate in an environment outside of their complete control. In addition, the best practices, with respect to setting up and managing an alliance, are not yet widely disseminated.



**Figure 1: Corporate priorities on growth ambitions, dimensions and instruments**  
Note. Number indicates relative priority (on a scale of 1-3, with 3 being the highest priority; n=18)  
Source: Marks et al. (2005)

Nevertheless, an increasing number of innovations are created by collaborating companies. Alliances have become a hotbed of innovation.

The emergence of alliances as enablers of innovation seems closely related to rapid technological developments and ever-increasing competitive pressures. The increasing pace of technology advances inevitably raises the need for flexibility in times of uncertainty. Mounting competitive pressures lead to higher R&D costs, in relation to the business life-cycle and an associated lower return on R&D investments.

Compared to mergers & acquisitions, alliances are a relatively young organisational instrument. Whereas M&A can be traced back to the 1920s and earlier, alliances only took off in the 1970s<sup>2</sup>. Although both instruments can pursue the same goal (growth through innovation), the success rate of alliances has already surpassed that of M&A and is still increasing as companies continue to improve their alliance management skills.

However, organising alliances is not an easy thing to do. The following two cases show how companies can organise innovative alliances. The conclusion will be that innovative alliances require companies to build on their intrinsic motivations, while simultaneously paying attention to the right governance structures for the alliance.

## CASE 1 – SENSEO, THE NEW PHILIPS & SARA LEE/DE COFFEE AT HOME EXPERIENCE

Before the Senseo coffeemaker was introduced in the Netherlands in 2001, its inventors, Philips Electronics and Sara Lee/DE, had met informally on several occasions. Both parties were facing the need to come up with new products to target their relatively mature coffee and coffee-making markets. Serious negotiations between the companies, who had not previously co-operated on innovation, started in 1998. In a joint effort, Philips and Sara Lee developed an innovative concept of coffee-making, targeted at changing the coffee-drinking habits of consumers. With the introduction of a brand new coffeemaker in combination with fixed quantities of various flavours of coffee (coffee pads) ensuring a high and consistent quality of coffee, consumers were stimulated to make coffee-drinking part of their daily routines. To ensure first-mover advantages and market coverage, the Senseo coffeemaker, with a recognisable design, was quickly launched at a relatively low price. In 2005, around three million Senseo coffeemakers had been sold in the Netherlands and worldwide sales had reached 10 million. This was above expectations. In 2006, the two partners extended their partnership to include tea as well.

The companies participating in the Senseo alliance had not previously co-operated with each other and could not draw from past experience of how their partner was likely to behave. Furthermore, Philips and Sara Lee had an entirely different industrial background, which also added to the relational risk as neither company had information regarding the common ways of behaviour in their partner's industry sector. As the Senseo alliance was targeted at joint innovation in a new market creation and had a high chance of failure, the performance risk could be described as high as well. Various other innovative coffee machines were introduced into the market subsequently and the market became increasingly dynamic as coffee chains, like Starbuck's, rejuvenated the industry.

**“Alliances have become a hotbed of innovation.”**

The co-operation between Philips and Sara Lee is based on a formal contract stipulating the role played by each of the partners, as well as a division of revenues from the alliance. Philips receives a percentage of the sale of coffee pads by Sara Lee to compensate for the low price of the coffee machine. The contract is specifically drawn up for the portioned coffee market. The formal allocation of revenues from the alliance aims to maximise profits for the alliance as a whole. The governance model underlying the daily operations of the Senseo co-operation is the 'multiple points of contact' model where formal contacts for the alliance are appointed at every hierarchical layer within both organisations. Figure 2 on page 12 depicts the governance structure of the Senseo alliance.

At the top of this formal decision structure is the International Steering Committee, consisting of three managers from each partner. This committee is responsible for approving the Senseo business plan and the product roadmap. Next to being in charge of the long-term development of Senseo, this committee also has a controlling function as it provides leadership to committees in lower layers of the hierarchy. Below the International Steering Committee in the hierarchy there are National Steering Committees that are responsible for country-level sales of Senseo. These committees consist of employees from the National Sales Organisations of Philips and the National Operating Companies of Sara Lee. A third hierarchical layer is the joint sales teams, consisting of sales representatives from both partners who jointly visit retailers. In addition, the Marketing & Equity Meeting is in charge of all issues related to the marketing of Senseo coffee makers and pads, including the creation and development of brand equity. Although Philips decides which models of the Senseo coffee maker »

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Figure 4



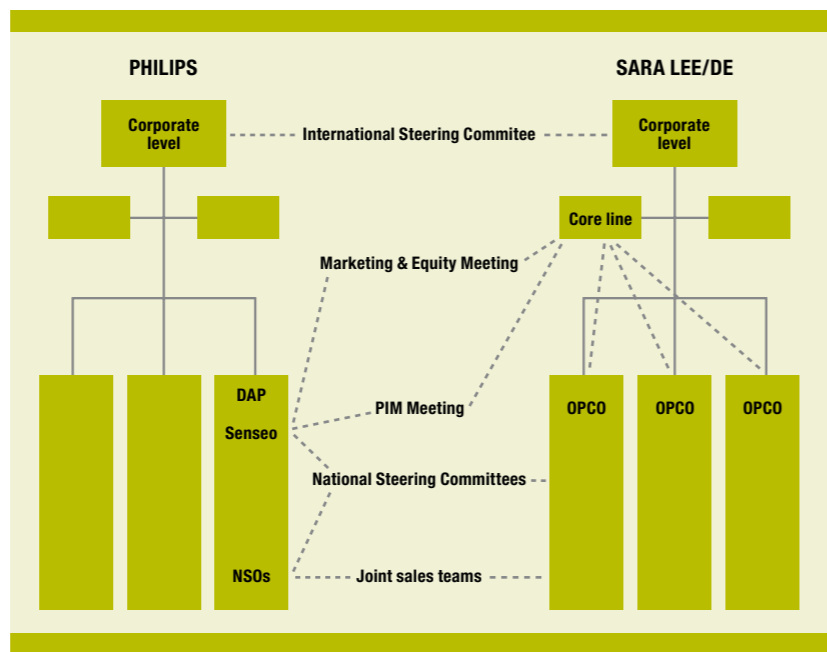
» it brings to market and Sara Lee determines which blends of coffee it introduces to its coffee market, both partners co-ordinate their product development efforts in the Product & Innovation Meeting (PIM). This decision and communication structure also provides for conflict resolution through formal escalation procedures, which state when and how an issue should be moved to the next hierarchical level.

over fifty partners joined. Each partner had to make a financial contribution to the alliance and was asked to contribute staff and resources as they deemed necessary. The benefits for the partners would be in learning about the effect of new technologies in a real-life situation, as METRO would implement the technologies in an existing supermarket. In addition, the creation of retail standards would open up new markets for the partners. The final benefit was the extensive publicity the store would get. METRO has an outstanding reputation when it comes to generating this.

**“These two elements created a sense of community: working for the Future Store alliance felt like belonging to a club.”**

To participate in this initiative, METRO invited partners it already knew. Many participating companies are suppliers to METRO and interpersonal relationships had developed with numerous executives of other companies. For technologies in areas where METRO did not have prior relationships, METRO asked existing partners whether they had partners that could be interesting for the Future Store. In this way, friends of friends were brought on board.

Figure 2: Governance structure of the Senseo alliance. There are multiple points of contact between the partners



**CASE 2 – THE METRO FUTURE STORE INITIATIVE, EXPLORING AND EXPERIENCING 21<sup>ST</sup> CENTURY SHOPPING**

METRO, the third-largest supermarket chain in the world, aims to distinguish itself from competitors by being at the forefront of technology. One of the most eye-catching ways of implementing that strategy was to build a store of the future, brimming with the latest technologies: RFID, automatic weighing scales, automatic check-out, information pillars, automated personal shopping assistants etc.

METRO realised it would not be able to create the store of the future by itself, as it lacked technological knowledge and experience. It therefore set up an alliance, the Future Store Initiative (FSI), and invited leading technology firms, like Intel, Cisco and SAP, to contribute to developing the Future Store. In total,

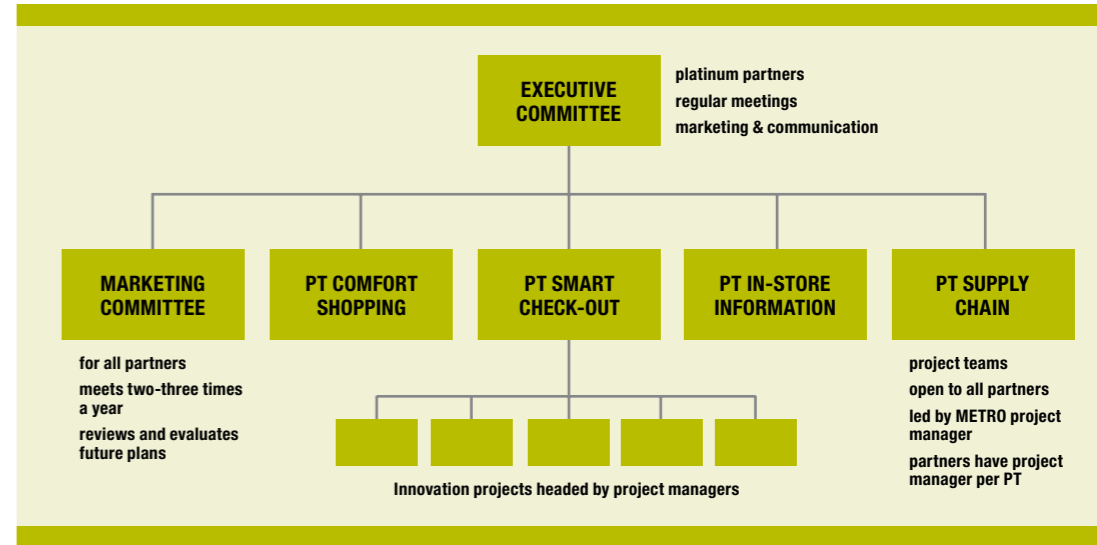


Figure 3: Governance structure of the Future Store Initiative. The executive committee oversees the projects in the Future Store

This tactic limited relational risk. Performance risk, however, was high: as with all innovation, the risk of failure loomed large. As FSI aimed at introducing a whole variety of innovations into retail, the complexity was quite high. By inviting Claudia Schiffer to open the store, enormous publicity was ensured. Combined with a very tight deadline, the risk of an enormous publicity failure was not imaginary.

The FSI was governed by simple rules. Figure 3 shows the governance structure of the FSI. METRO Group and the three top partners meet regularly in the Executive Committee. It is responsible for admitting new partners and ending relationships. It also approves cash outlays from the Initiative's fund (in which the cash contributions from partners are deposited), after consensus has been achieved about specific investments; the rest of the partners are responsible for their own expenses and investments. All partners are invited to the two-three annual meetings of the Marketing Committee. This Committee reviews progress and METRO Group shares its future plans with partners there as well. Next, there are four project teams, each dedicated to one of the four areas of innovation in the Future Store: comfort shopping, smart check-out, in-store information and supply chain. Each project team is headed by a METRO Group project manager. The different projects are set up to be run as independently as possible.

There is no elaborate contract. There is a Memorandum of Understanding between the partners that is only a handful of pages long and covers a few specific issues, among which are:

- the vision of the collaboration;
- the resource commitments that need to be made;
- non-exclusivity of the alliance;
- non-disclosure agreement, to protect all proprietary knowledge that companies bring;
- freedom to use all knowledge developed in the alliance.

For the rest, the FSI counted on a number of aspects to ensure that the FSI would progress. The first one is the fun aspect of the work. The vision of creating a store of the future created enthusiasm among the people working on the store. This ensured co-ordination<sup>3</sup>: the goals of the partners were aligned. Second, the time pressure and the risk of high-profile failure made partners mutually dependent on each other. Failure of the store to open on time would harm the reputation of all partners. These two elements created a sense of

community: working for the Future Store alliance felt like belonging to a club. The macro culture<sup>4</sup>, or network identity<sup>5</sup>, became a success factor in the alliance.

The role of METRO in organising the alliance was pivotal. METRO, however, did not force decisions on the partners but mainly acted as the first among equals, understanding that, for the alliance to be successful, benefits should accrue to all participants.

There was not much planning upfront. In fact, the speed of the project was very high. First, preliminary ideas were discussed in September 2001. By July 2002, the outline of the idea was clear and the partner base could be recruited. In April 2003, the store was opened. The lack of an overall plan, however, was compensated for by thorough attention to detail in the implementation.

The vast majority of the partners were satisfied with the benefits participation in the Future Store had generated for them. Research into the satisfaction of customers with the new technologies was carried out some time after the store was opened. The results differed per technology but, overall, most new features were evaluated as valuable by a third to half of the shoppers, whereas only between ten and twenty percent of the shoppers rated the value as low.

**CONCLUSION**

Alliances have proven to be a useful tool for growth via innovation, provided that the right governance structure is chosen. Innovation via alliances and networks requires companies to pay attention to a strong governance structure. This does not only involve paying attention to the structural side of partnering, like making contracts, decision-making structures and value-sharing agreements. It also involves the relational aspect of partnering, like building on the intrinsic motivation of people, creating trust between partners and ensuring the right alliance atmosphere.

In addition, the cases show that building alliances is precision work. Alliance governance structures need to be tailored to specific situations, depending on the innovative objectives an alliance has. Companies have different tools at their disposal to create such tailored structures: from meetings and contracts to creating the right environment conducive to innovation.

The more companies that use best practices for innovation in alliances, the better they will be able to profit from the creative potential of collaboration. Not using alliances will rob a company of an important source of renewal. Alliances should, therefore, not be seen as a second-best option but as an important weapon for harnessing innovation.



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