# OPEN INNOVATION FOR EUROPE

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REPORT



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# ABOUT

Open innovation is a business management model for innovation that promotes collaboration with people and organizations outside a company. Encouraging such practices across European firms can be a driver for innovation and competitiveness.

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FOR A COMPETITIVE AND DIVERSE EUROPE

#### OPEN INNOVATION CAN ACCELERATE ORGANIZATIONAL LEARNING AND INNOVATION



For years, the stock price of Tesla has been soaring. Although they compete with powerful incumbents, they seem to have gained investor's trust and regularly introduce innovations that push the entire industry forward. How do they scale and grow so fast? Part of the answer roots back to the year 2014 when Tesla decided to open-source its patents and encourage other companies to use its intellectual property.

In hindsight, that strategic move shows that Tesla's management team was aware of the power of an open and holistic perspective. The car manufacturer recognized the need for an enabling environment to scale their electric cars, something they couldn't do alone. They needed partners that would build charging stations and offer services to create the infrastructure to support electric vehicles. By putting itself at the center of an ecosystem of partners and by actively seeking collaborators, Tesla laid the groundwork for its explosive growth.

Even though engaging with their surroundings is not particularly novel for organizations, most activities outside a firm's boundaries happen in a sporadic and unstructured manner. Tesla's incumbent competitors traditionally focused on economies of scale, strong internal R&D activity, and control over their supply chain. This has changed and organizations have shifted their focus from purely internal R&D activities, towards opening up and exploring outside innovation more thoroughly. This can be summarized as 'Open Innovation (OI)'. Put simply, instead of doing everything inside the four walls of the business, innovation is generated by accessing, harnessing, and absorbing external knowledge across the firm, both flowing in and going out.

Future-proof organizations recognize that the traditional understanding of what an organization is and where its boundaries lie have changed. Many companies, predominately from the digital space, have shifted their emphasis on leveraging networks where partners share data, code, and skills. They recognize that there are more capabilities for innovation in the marketplace than what they can create on their own. Following the understanding that "not all the smart people work for us", these companies actively seek collaboration and partnerships to scale innovations.

Scholars emphasize that future-fit companies embrace (and that laggards are slow to accept) the fact that sources of value are increasingly and constantly changing. Leading organizations are blurring their boundaries and embracing agility over a mechanical waterfall approach. It is important to note that open innovation should not be confused with "freely available" as in "no ownership" and "no constraints on IP." Organizations find themselves confronted with a broad toolbox of open innovation methods. These entail constant interaction with stakeholders, technology, and employees.

Open Innovation describes the integration of external knowledge into an organization by using a variety of tools and methods, like accelerators, incubators, IP licensing, joint ventures, partnerships, innovation consortia, innovation hubs, open-source platforms, or corporate venture capital investments.

The open innovation paradigm goes beyond the sole externalization of R&D activity but rather reflects a fundamental change in how organizations acquire, use, and manage their knowledge. New mindsets and business models emerge such as opensource software like the Linux operating system, which was created through close collaboration of established organizations, suppliers, start-ups, users, individuals, and producers of related products.

Organizations that successfully implemented open innovation practices are characterized by a growth mindset, curiosity, and a cultural environment that encourages experimentation and even failure. The CEO of Microsoft, Satya Nadella, describes this mindset by the way his employees think about innovating. Instead of suggesting ideas, he states, "what if you said, 'I have a new hypothesis, let's go test it, see if it's valid, ask how quickly can we validate it.' And if it's not valid, move on to the next one." This kind of mindset fosters creativity and takes away the fear of failure. After all, the worst thing that can happen is that a hypothesis is not valid.

However, these open innovation practices are easier said than done. The organizational structure and decisionmaking processes need to enable experimentation and collaboration in simple and fast ways, while avoiding internal bureaucracy which produces friction. Such structures, and Microsoft's cultural shift from "know it all" to "learn it all," is exemplary of an open and learning organization that looks beyond its boundaries



Digital technologies bring constant and everincreasing speed and change to most industries, demanding incumbents to innovate. Ultimately, the combination of borderless connectivity, lower transaction costs, unprecedented automation, network effects, and shifting demographics has given rise to digital upstarts in the US and China. Amazon, Facebook, Tesla, Google, Alibaba, and Tencent to name just a few, are all examples of companies that continue to innovate, and win, in bold new ways.

Notably, most of these companies are platform business models. Such platforms are undoubtedly a key disruptor of the business world by bringing together different actors (different sides of a platform) and enabling them to work together. Apple's AppStore and iPhone, for example, enable independent developers to create applications and reach a large number of users. Platforms connect actors that were unconnected before and make it easier to divide work. Some actors might provide data, while others build additional services on the platforms or offer unique insights.

Besides all these promising advantages of open innovation, corporations still hesitate as they fear the exploitation of their resources (most notably data) by others and mention that the protection of their proprietary intellectual property is challenging. Moreover, managing such open innovation practices is characterized by complex and fragmented activities, as well as increasingly heterogeneous and interdependent actors. Employees and managers struggle with this kind of distributed, decentralized, and participatory way of innovating.

Despite this, there is also good news for incumbents. The emergency reaction and vaccination development to the Covid-19 pandemic illustrated the power of collaboration. Even the most traditional companies began to reconsider collaboration and came together to work openly at an unprecedented level, putting the ability to create value before the opportunity to make a profit in the short-term. Siemens, for example, opened up its Additive Manufacturing Network to other companies that wanted to produce medical devices. Researchers worldwide shared best practices about developing a vaccine, which resulted in multiple vaccines getting to the market in record time. Covid-19 could be a turning point towards a more collaborative and open business world.

Taking all this together, three themes emerge. First, the knowledge that is required to introduce successful innovations often resides outside a firm's boundaries. Future-fit companies engage with and integrate external partners and view them as an extension of themselves. Second, to successfully innovate openly, companies need to establish an enabling environment for their employees reinforced by the company culture, decision-making processes, and organizational structures. Lastly, the Covid-19 pandemic has illustrated the potential benefits of open innovation and (hopefully) marks a potential turning point to our economic systems.

#### OPEN INNOVATION IS MORE WIDELY USED IN THE US, WHEREAS MOST EUROPEAN ACTORS ARE JUST STARTING TO TURN INTENTION INTO ACTION.

A hundred years ago, Europe was the global powerhouse of innovation. We invented the car, transistors, and antibiotics. However, Europe lost its edge: today, despite some notable exceptions, many innovative companies are found elsewhere. We still have many profitable companies in the area of industrial manufacturing, automotive, or pharmaceuticals, but over the last decades, disruptive innovations emerged elsewhere. Europe is falling behind the United States and China in growing sectors as well as in areas of the future such as digital platforms, genomics, quantum computing, and artificial intelligence.

Notably, digitalization has also been significantly slower in Europe than in competing regions. Everyone who has traveled by train in Germany knows about the lack of phone coverage or the inability to pay with credit cards in many shops. The number of digital startups that successfully enter the market, as well as the share of the revenue from digital offerings of incumbents are significantly smaller than in the United States. In addition, China and South Korea have also been leapfrogging ahead of western economies.

European companies spend less on innovation than their global competitors and their innovation systems appear to be less dynamic. Despite growing awareness of the need to innovate and a gradual upwards trend in innovation performance, further efforts are needed to ensure Europe's global competitiveness in the future. Much of the American resurgence came from their ability to invent new industries, to test new disruptive business models, and to successfully establish them. This ability came hand in hand with a more fundamental change in how the American innovation systems function.

Compared to European companies, their American counterparts shifted focus from internal R&D within large businesses and gave way to external sourcing of technology – open innovation. The extensive emergence and utilization of platform business models in US companies demonstrates this point.

Despite the challenges to change the innovation systems of European companies and the difficulties to manage open innovation processes, there are an increasing number of European managers who seem to understand the long-term benefits of doing so.



### LEVERAGING EUROPE'S DIVERSITY AND INDUSTRIAL EXPERIENCE IN COLLABORATIVE WAYS TO COMPETE IN FUTURE MARKETS.

Innovation is far from dead in Europe. Growth is recovering and there is an optimistic, vibrant momentum in the region that is fostering a renewed sense of ambition. In recent years, many incumbents established start-up accelerators that exemplify a move towards open innovation and towards collaboration with startups. Many Corporate Venture Capital Funds emerged recently that aim to connect innovative startups with the corporation's core business.

The European ecosystem is characterized by many high-tech industries where the rate of innovation is rapid and where knowledge is distributed across multiple organizations, making it difficult to innovate alone. Which in theory, is the perfect environment for open innovation approaches. The mindset shift to open innovation approaches can already be observed in these industries today.

There are a few key recommendations for how European companies could become more innovative again.



•Open Innovation. As described above, a key to innovation lies in continuing to pursue collaboration and open innovation practices. European regulators and innovators can collaborate to build an enabling environment to make such open innovation activities easier. Currently, there are many different initiatives being developed. For example, to better connect different stakeholders and leverage the strengths of networking, the European Strategic Cluster Partnerships (ESCP) developed a "triple helix model" of innovation. This model describes how intermediaries connect and organize universities, companies, and governments to collaborate. However, these initiatives have not yet received enough attention and resources. We need more dedicated, coordinated testing areas, or sandboxes, where stakeholders of key technologies can come together and co-create.

#### Avoid the trap of focusing on technology

alone. European companies need to understand that successfully utilizing open innovation requires a cultural and mindset change. Companies ought to rethink their decision-making processes and encourage a culture that is open and experimental – understanding failure as a source of learning and not blame or shame.

•Building on existing academic strengths and skills. European universities have always had particularly strong researchers that work on fundamental research. Translating these insights into commercially viable business models by collaborating with diverse actors would help Europe to emerge as the leader in future technologies. Good examples are initiatives like the SPRIN-D in Germany, the federal agency for disruptive innovation, that brings together thinkers from science and business and provides a sandbox to translate advanced research insights into business models. There are also more and more university accelerators like the UnternehmerTUM in Munich which support their students and researchers with capital and assistance.

**Focusing on B2B**. The next playing field of innovation will likely be more oriented to business-to-business (B2B) than business-toconsumer (B2C) enterprises, with many technological applications centered on diffusion across industries and supply chains. Europe historically has a strong standing around industrial manufacturing and B2B applications. Driving collaboration and open innovation in this area seems advantageous.

Sustainability Tech and wicked problems. Corporates are pledging billions of euros to achieve net-zero emissions, governments are putting ambitious climate policies in place and an ever-growing number of consumers are putting environmental concerns first. Put simply, sustainability and in particular, climate performance will become a core value creator of our economy. Climate change is a highly complex and interconnected challenge, often described as a wicked problem. Due to their complex nature, wicked problems should be approached collaboratively as no individual actor can solve them independently. Therefore, open innovation for climate change is a huge opportunity and European institutions like the platform Climate-KIC can guide the way.

**Leverage Diversity**. Europe can compensate for its fragmentation with openness and connectedness. Diversity is a driver for innovation and Europe has much of it. But there is a need for more effort, coordination, and communication in industry and politics.

In simple words, Europe relied too much on their existing industries and missed out on many opportunities to disrupt themselves. However, it's not too late and there are good reasons to believe that Europe's businesses can thrive again. But we must act now - by being more decisive and more ambitious, building on our strengths and the European spirit of collaboration and unity.





#### **OPEN INNOVATION**

## GOT ANY QUESTIONS?

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## RESOURCES

https://www.mckinsey.com/business-functions/organization/our-insights/organizing-for-the-future-nine-keys-to-becoming-a-future-ready-company

https://hbr.org/2020/06/why-now-is-the-time-for-open-innovation

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https://sifted.eu/articles/sustainability-metrics-vc/

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