BOOKS

Ideas for the Taking

By LAWRENCE J. SISKIND
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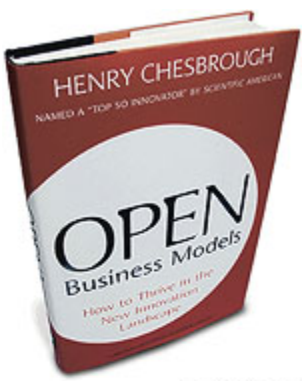
DETAILS

OPEN BUSINESS MODELS
By Henry Chesbrough
(Harvard Business School Press, 256 pages, $35)

When Francisco D'Anconia in "Atlas Shrugged" decided that enough was enough, he engineered the destruction of his mining empire. In a marvel of synchronization, every mine, dock and ship was blown up at the very moment that the government was voting to nationalize his business. If Bill Gates decided to emulate Ayn Rand's hero, he would face a tougher challenge. If he blew up every plant, warehouse and office building of the world's greatest software company, Microsoft would then be…the world's greatest software company.

The difference is that D'Anconia Copper was based on tangible property, while Microsoft is based on intangible intellectual property (IP). Destroy every single Windows CD in inventory and Microsoft would remain the only company that could legally make and market new ones.



Patrick Conlon

Intellectual property often has more value than the tangible kind. How to put it to best use?

Henry Chesbrough, the director of the Center for Open Innovation at the University of California, Berkeley, is not the first academic to grasp the superior economic value of intellectual over tangible property in today's economy. But he may be the one who has thought most deeply about its consequences for business.

In "**Open Business Models**," Mr. Chesbrough has developed a useful dichotomy of old innovation and new. Traditional enterprises, he notes, innovated and commercialized internally. A company's research-and-development department worked on inventions that, if promising, were manufactured and marketed by the company itself. Operating with the "not invented here" syndrome, companies avoided innovations developed by outsiders. With the "not sold here" syndrome, companies kept bottled up inside those ideas that they developed but couldn't use. This led to enormous waste. Mr. Chesbrough notes that Procter & Gamble surveyed its IP and found that only 10% of its patents were in use; the other 90% had no value to the company. In the pharmaceutical industry, researchers, over a 30-year career span, might never see a project ship to market.

Mr. Chesbrough's ideal businesses resist the "not invented here" and "not sold here" syndromes in favor of "open innovation." They search outside their companies for the best ideas, soliciting input from other companies (including competitors) as well as from customers, suppliers and vendors. They take their unused IP and put it on the market, through sales and licenses. (Today, Qualcomm, with a work force of 8,000, generates revenue of $4.9 billion, an amazing $612,000 per employee, mainly through its technology licenses.) Sometimes companies even give it away, if it will promote their other products. (IBM, for example, recently donated 500 software patents to the open-source community, to encourage the use of the Linux operating system.) These forward-looking companies use "innovation intermediaries"—such as InnoCentive, Big Ideas Group and Ocean Tomo—to find IP, originating with others, that is worth acquiring and to market their own.

Some of these ideas appeared in Mr. Chesbrough's "Open Innovation" (2003). In "Open Business Models," he has gone further and explored how companies can transform themselves in order to take advantage of these trends. The heart of the book is a kind of taxonomy of business types—six business models that manage innovation with steadily greater acumen and efficiency. Imagine the famous portraits of the human evolution sequence (from monkey to Neanderthal to Cro-Magnon to Modern Man) and you'll catch his drift.

Type 1 companies, the most primitive, sell the same commodities as others in their industry, and they compete on the basis of price and availability. Unequipped (or not inclined) to develop or acquire innovative intellectual property, they are swept into extinction as improvements come into their field. Type 2 companies can differentiate their products from their competitors', but innovation is ad hoc and their strategies are more reactive than planned.

And so on up the evolutionary ladder. In Type 3, innovation is planned rather than random. In Type 4, companies have evolved to open themselves up to external technologies, selectively incorporating such ideas into their internal operations. Type 5 companies, more advanced still, integrate suppliers and customers into their creative process. They study their supply chains all the way back to basic raw materials, seeking technological opportunities to lower costs. They study their customers, searching for unmet needs.

What a piece of work is a Type 6 business model! How noble in its ability to innovate even its own business model through the use of spin-offs and joint ventures. New ideas move freely in and out of its infinite faculties. Mr. Chesbrough cites Dell as one such paragon of businesses. It works closely with suppliers, such as Intel, to test the next generation of chips. It works with its customers to create and install customized products, sometimes ensuring that each employee at the customer level receives a new PC every three years loaded with tailor-made software.

This six-step evolutionary construct is useful, as are the many case studies sprinkled throughout the book. But the work also has its shortcomings. Although Mr. Chesbrough refers broadly to "intellectual property," he nearly always means patents—an important IP element, but only one element. Microsoft's market power (and the reason it has been investigated for antitrust violations here and in the European Union) rests on its copyrights. Coca-Cola leads the soft-drink industry because of its storied formula, perhaps the most closely guarded trade secret in history. Don't try to sell "open innovation" to Coke! And celebrities have been marketing their unused IP for years, in the form of trademark licenses. Paris Hilton didn't need Henry Chesbrough to teach her the value of licensing her brand to outsiders.

Still, Mr. Chesbrough's book is one that B-school students and lay readers alike will enjoy: His writing style is entirely user-friendly. Like a popular lecturer, he begins each chapter telling you what he is going to say, then he says it. If you overslept and missed a class, never fear. Mr. Chesbrough pauses at the start of each chapter to summarize what he taught in the one that preceded it. So refreshed, the reader is prepared to be taken in hand to the next interesting and provocative lesson.

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