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Stop Competing Yourself to Death

There are times when bitter rivals should team up

By Adrian Slywotzky and Charlie Hoban

Most companies compete too much and cooperate too little on activities that hold little value to customers. As a result, they're hurting their margins and putting their future at risk. It's time to rethink basic assumptions about competition and collaboration.

Earlier this year, the business press eagerly reported a surprising story: General Motors and Toyota had begun exchanging information about the development of hydrogen fuel cells. News of the talks came just months after GM and DaimlerChrysler had announced plans to work together to design a hybrid power train for large cars and sport-utility vehicles. And it followed earlier agreements by Ford and Nissan to use Toyota's hybrid technology in their own engines. Five of the world's largest automakers, in other words, had begun collaborating on the technological underpinnings of next-generation vehicles.

If this multi-party collaboration does happen, we hope it is the first of many such moves for the auto makers. Ever since California tightened restrictions on car emissions in 1990, many of the major car companies have been investing aggressively to develop successors to the traditional internal combustion engine. Technologically complex, the R&D efforts have been extraordinarily expensive and risky, with each company having to duplicate much of the research of its rivals. If the auto makers had collaborated from the outset, instead of waiting 15 years, they could literally have saved billions of dollars in redundant investments and expenses. The entire industry would have been considerably more profitable, and GM and Ford might not find themselves in such dire straits

today. More than that, by collaborating on basic engine technology, which is, after all, invisible to most car buyers, the auto makers would have been able to focus their innovation efforts on areas that have real impact on the decisions of customers, such as product design or the dealership experience. They would have been able to compete where it counts.

Vigorous competition is, of course, the lifeblood of modern economies. It spurs creativity, rejuvenates markets, keeps companies agile, and guarantees consumers better products and lower prices. But as the experience of the auto makers reveals, competition can be bad as well as good. In dynamic economies, value is constantly migrating from outmoded business models to those that are better calibrated to satisfy critical customer priorities. As the game changes, certain aspects of competition become outdated and irrelevant, and companies have to revisit the scope of activities they engage in. When companies fight over things that hold little value to customers or offer little potential for competitive differentiation, they are engaging in competition that's destructive rather than constructive. They are throwing away shareholders' money, wasting valuable time and energy, and reducing resources available for innovation, thereby reducing the chance for profitability tomorrow—not only their own profitability but that of their entire industry.

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Much of the competition in business today has become outmoded. Indeed, the prevalence of destructive competition is one reason why a wide array of industries, from music to airlines to consumer electronics, have experienced a steady and seemingly inexorable erosion in profitability.

Globalization is already putting pressure on corporate profits. Even in industries that enjoy comfortable margins today, like pharmaceuticals and movies, the persistence of misdirected competition raises the odds of severe margin compression in the future. Global sources of supply contribute to overcapacity in industries such as plastics and automotive. New competitors with structurally lower costs become more commonplace in every industry; new competitors that have not only lower costs but also innovative business models proliferate as well. And as companies outsource more product development activities to third-party providers in Taiwan and other development centers, the role of new science becomes even more prominent as a way to differentiate oneself from competitors. Science, with its long odds and high costs, is exactly the type of activity that lends itself to industry-wide collaboration.

Strategic Collaboration

By joining forces to carry out common and largely undifferentiated functions or processes, companies can avoid redundant expenditures and capitalize on economies of scale and shared expertise. Strategic collaboration can take place at any stage of an industry's value chain. Some companies may find it in their best interest to cooperate in producing a standard input required to manufacture their products or deliver their services. Others may set up a joint center for basic research, partner to produce a software application, set up a distribution channel, jointly collect and sell information, operate a repair or returns facility, or set up a factory and sales force in a new geography.

There have been examples of these types of strategic collaboration among companies in the past. But they've been rare, and they've tended to be launched too late, usually in the face of impending disaster or under government pressure. Most firms shun opportunities for collaboration, if they even recognize them in the first place. Think about your own company. What percentage of its effort and investment goes toward trouncing its rivals, and what percentage goes toward cooperating with them? What, in other words, is your firm's compete/collaborate ratio? If

“All-out warfare” is a dangerously simplistic view of business.

your business is typical, you may do a little collaboration here and there—in lobbying government regulators, say—but your compete/collaborate ratio is probably somewhere

between 90:10 and 100:0. You compete pretty much everywhere, all the time.

Mutually Assured Destruction

All-out warfare can make sense in rapidly growing industries with buoyant profits. If companies are competing for slices of an ever expanding pie, they can prosper by matching one another's investments across the entire value chain. The greater capacity—in supply, in production, in distribution, in marketing—can be put to productive use in fulfilling increasing demand. And broad competition can also boost productivity in every function, while providing different competitors with new opportunities for differentiation. But at some point, the economic logic reaches a crossover point. When an industry matures or its margins otherwise get squeezed, undisciplined competition becomes a form of mutually assured destruction. It leads to overcapacity, high costs, weak capital efficiency, a lower innovation rate, and precious little competitive differentiation.

Why do managers persist in destructive competition? Because that's what they're trained and expected to do. The idea of setting aside the sword and working shoulder to shoulder with rivals on some part of the busi-

ness is anathema to most executives.

Just look at the music business. For years, it's been clear that the digitization of songs would shake up the traditional distribution model. When Shawn Fanning invented Napster in 1999 and turned the illegal downloading of music into a mass hobby, the threat to the big music labels could hardly have been clearer or more dire. Yet instead of joining together to pioneer a legal alternative to digital distribution, the labels continued to bicker and battle. They ended up launching separate, competing services. Universal and Sony organized a joint venture called Pressplay, while Time Warner, Bertelsmann, and EMI set up MusicNet. Because the two services refused to license their songs to each other, they were shunned by customers, who wanted one-stop shopping. That provided an opening for Apple Computer to launch its comprehensive iTunes store and bring a new form of value to the customer.

That's not to say that companies haven't tried to temper the ill effects of undisciplined competition in other ways. Three methods are, in fact, commonplace. The first is acquisition—merging businesses to reduce duplicate functions and combine customer bases. The second is outsourcing—offloading non-strategic activities to third-party specialists that can achieve greater scale, lower costs, or deeper expertise. The third is standards-setting—agreeing on shared technologies or protocols to avoid a proliferation of incompatible products or components. All of these approaches can provide great value under the right circumstances, although some have shortcomings as well.

M&A, for example, is a blunt instrument. It forces companies to combine all aspects of their operations, not just those that will benefit from consolidation. Such broad integration is devilishly difficult to pull off, which is why mergers destroy value more often than create it. M&A also perpetuates the destructive type of competitive behavior, just with

larger stakes among consolidated players.

Strategic collaboration avoids these problems. Unlike M&A, it's precise. Companies only have to join forces in well-defined activities or processes—those that offer the greatest immediate payoffs from consolidation and rationalization. Unlike outsourcing, it doesn't entail a loss of control. Existing competitors are able to share directly in the benefits of economies of scale and pooled talent. And in contrast to standards-setting, it can take place throughout the value chain, in all areas except those, like pricing, that might lead to unfair competition and raise antitrust concerns. Strategic collaboration also tends to promote, rather than dampen, constructive competition, which inevitably leads to greater innovation in those fields most valued by customers.

There have, of course, been calls for greater business cooperation before. But most of the existing literature on cooperation, such as the book *Co-opetition* by Adam Brandenburger and Barry Nalebuff, focuses on complementary efforts—on businesses doing *different things* that complement each other in a way that creates added value. Strategic collaboration involves working together on the *same things*—on key shared activities within an industry's value chain. It's about collaborating in exactly those places where competition has been the rule. As such, it offers the possibility of fundamentally changing the economics of an existing industry in a way that benefits all players.

Given the harsh realities of business today, it's time for managers to rid themselves of their anti-collaboration bias. Companies need to take a fresh, objective look at their compete/collaborate ratios and begin shifting them toward a more productive balance—before it's too late. We'll examine some compelling examples of how strategic collaboration has strengthened, or even saved, entire industries while boosting the profits of individual firms. We'll describe opportunities that may be available to

*Strategic collaboration
changes the economics
to benefit all players.*

third parties in creating a collaboration platform, as Apple did with iTunes, or in serving as a collaboration catalyst for an industry. And we'll provide some practical advice for sorting through collaboration options and targeting the right ones for your business. The success of your company is too important to be competed away.

Save Money, Then Reinvest to Create New Value

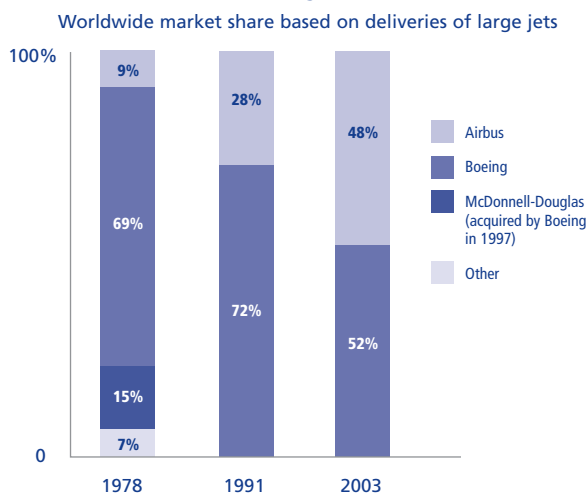
In the 1960s, airplane manufacturing in Europe appeared doomed. U.S. companies, particularly Boeing and McDonnell-Douglas, had become the dominant players in the increasingly capital-intensive industry. The smaller European manufacturers, scattered across the continent and fighting fiercely with one another as well as with their international rivals, lacked the scale and the capital to compete effectively against their U.S. counterparts in building big, modern passenger jets. By the end of the 1960s, the Europeans' combined share of the global aircraft market had dwindled to just 10%, despite the fact that 25% of planes were being purchased by European airlines.

Then, in 1970, four of the leading European manufacturers—France's *Aerospatiale*, Germany's *Daimler-Benz Aerospace*, Spain's *Casa*, and the U.K.'s *British Aerospace*—did something radical. They formed the joint venture Airbus, pooling their resources to design, produce, and sell jet aircraft. Not only did the venture provide operating economies and temper financial risks, but the combination of capital and talent also led to a surge of innovation. Despite early managerial conflicts, Airbus successfully pioneered new approaches to aircraft design, including fly-by-wire control technology and the introduction of a common cockpit across the entire fleet. Between 1984 and 1994, the joint venture launched three technologically advanced, highly efficient planes that proved attractive to a large number of airlines.

The collaboration didn't just provide temporary life support for the aircraft makers; it has allowed them to thrive. Although Airbus's

first customers were European airlines, the venture began penetrating the American market by 1980, and in the 1990s its clientele expanded to include such U.S. giants as United Airlines, US Airways, and Northwest Airlines. Not only had European aircraft manufacturing survived, but Airbus had become in essence the only rival to Boeing (which in 1997 had acquired McDonnell-Douglas). As shown in Exhibit 1, Airbus has grown rapidly over the

Exhibit 1 Airbus ascending



Source: 1973-1994, Investext. 2000-2003, Market Forecast, www.eads.net

past two decades, to the point where it now often beats its American archrival in annual deliveries of new jets. In 2000, the European partners strengthened and extended their collaboration, consolidating Airbus's management and operations at a centralized facility in Toulouse, France. While charges of unfair government subsidies from both sides surface periodically, the important business lesson is the greater efficiency and innovation made possible by the Airbus partnership.

In a similar way, collaboration set the stage for a turnaround in the once-beleaguered U.S. semiconductor industry. During the 1980s, American chip manufacturers were being trounced by low-cost Japanese rivals. Between 1980 and 1986, the U.S. semiconductor industry saw its profits shrink by more than \$2 billion and its payrolls contract by more than 27,000 workers. The sector's ongoing collapse caused grave concerns among U.S. policymakers, for national secu-

rity as well as economic reasons. Half the chips used in the country's F16 fighter jet, for example, were being supplied by Japanese manufacturers.

In response, the U.S. Department of Defense spearheaded an effort to create a research consortium to stem the industry's losses. Fourteen semiconductor manufacturers, representing 85% of the industry, joined together in 1987 to form SEMATECH in order "to solve common manufacturing problems by leveraging resources and sharing risks." Each of the participants, along with the U.S. government, invested \$100 million in the effort, and in return they were all granted the right to share in the resulting technologies. SEMATECH's research initiative, launched from dedicated facilities in Austin, Texas, succeeded in strengthening the entire U.S. semiconductor supply chain while spurring rapid advances in chip miniaturization and speed. The joint effort played a crucial role in the industry's resurgence during the ensuing decade.

These two stories show that close collaboration among competitors is not only possible—and legal (see sidebar, "Is Collaboration Legal?")—but also that it can dramatically improve the profitability of industries and individual companies, particularly in maturing businesses that are undergoing

margin erosion. Collaboration allows firms to capture the benefits of superior scale, rationalized assets, and combined talent in those areas of the value chain that offer little potential for strategic differentiation. And it frees up cash to invest in those areas that do offer the potential to generate competitive advantage.

Proactive Moves

The examples also reveal something else: Collaboration usually takes place too late. The European aircraft manufacturers and the U.S. chip makers began to collaborate only after their businesses had deteriorated severely, and in both cases governmental encouragement and financial assistance were required to get the cooperative ventures off the ground.

There have been some notable exceptions to the collaboration-as-last-resort rule. A group of 25 small hardware stores banded together to form a cooperative for joint purchasing and advertising back in 1948—well before they were threatened by big-box retailers such as Home Depot. The cooperative, now called True Value, has grown to encompass more than 6,200 hardware, gardening, and equipment-rental stores in 54 countries, with total sales of more than \$2 billion. The organization allows its members, mainly entrepreneur-owners, to enjoy big-

■ Is Collaboration Legal?

"We can't team up with competitors—it will get us into antitrust trouble." That may be a convenient excuse, but it's usually not true. Companies must, of course, think through the legal ramifications of any cooperative venture. They have to avoid working together in areas that would involve the sharing of pricing information or entail other actions that might harm customers. And they can't team up in a way that gives them cartel-like power over a critical distribution system or other component of a market's shared infrastructure.

But the goal of antitrust laws is not to prevent cooperation. Rather, it's to block business activities that damage the public interest by reducing

the efficiency of markets, slowing innovation, or obstructing productive competition. Because strategic collaboration actually enhances market efficiency, spurs innovation, and intensifies productive competition, it benefits the public and thus is unlikely to be a target of government action. (Indeed, past examples of industry collaboration often involved direct governmental encouragement and assistance.) Companies launching a collaboration initiative may need to educate policymakers and the general public about the scope and benefits of the effort, but that shouldn't be a deterrent to cooperation. The potential gains—for customers as well as companies—are too great. ❖

company scale economies without sacrificing their independence.

On the product side, True Value provides members a wide selection of private-label merchandise under such popular brand names as True Value, Master Mechanic, Green Thumb, and Master Plumber. Goods are shipped from the cooperative's 12 regional distribution centers, assuring fast replenishment and responsive service. On the marketing front, in addition to shared advertising campaigns and sales flyers, True Value allows members to tap into a joint cus-

tomers loyalty program, True Value Rewards, that not only strengthens local customer relationships but provides in-depth market data that would be prohibitively expensive for stores to assemble on their own. The cooperative also allows members to share best practices through "marketing toolkits" that include detailed instructions and templates for proven promotional and public relations activities.

Big companies, too, have on occasion launched proactive collaboration initiatives. Early in the history of the credit card busi-

■ Collaboration Platforms, Collaboration Catalysts

In addition to improving their performance by collaborating with competitors, some companies may be able to create entirely new businesses by helping spur collaboration among their customers or their suppliers.

In the automotive arena, Johnson Controls Inc. (JCI) has profited by offering to auto makers a collaboration platform—a business set up by a third party that creates the means and incentives for industry collaboration. Over the past ten years, JCI has built five state-of-the-art technology centers—two in the U.S., two in Europe, and one in Japan—to work with auto companies in researching and designing integrated, modular vehicle interiors. These labs have become, in effect, the means through which auto makers around the world can share in creating expensive but non-differentiating components, such as seats and heating systems, rather than duplicating one another's efforts as they formerly did. Acting as a collaboration platform has been extremely lucrative for JCI.

Establishing a collaboration platform can be a particularly powerful business model for two simple reasons. First, the legacy of hypercompetition often makes it difficult for competitors themselves to take the first step toward collaboration. Second, collaboration can unlock so much economic value that both the platform operator and the existing competitors can reap added profits—a collaboration platform enlarges the pie rather than just re-slicing it. For both these reasons, competitors in an industry often have strong incentives to embrace a third party's platform.

A savvy outsider may also have an opportunity

to act as a catalyst that spurs industry competitors to begin collaborating. The catalyst may, for example, be a supplier to the industry that can strengthen its existing business by helping its customers work together to solve common problems.

That's what Cardinal Health has done in the prescription drug business through its ArLight Systems venture. Cardinal convinced pharmacy competitors CVS, Albertson's, Wal-Mart, Kmart, and five regional drug store chains to form a consortium to collect and market real-time drug sales data. ArLight delivers the data and trends online to paid subscribers, such as pharmaceutical firms, that want to track the effectiveness of marketing campaigns, the impact of new product launches, and the introduction of generic drugs.

The catalyst may also be a customer of the industry. Wal-Mart, for example, is playing the role of catalyst in getting its suppliers—the world's leading consumer packaged goods companies—to collaborate in adopting radio-frequency identification (RFID) technology to better track products as they move through the supply chain. Wal-Mart knows that if the new technology enhances the productivity of the entire retail supply chain, a good portion of the gains will flow to its own bottom line. Without pressure from Wal-Mart, the consumer goods companies would have been much slower to invest in the risky new technology, basic research would be delayed, and a proliferation of incompatible standards would likely have raised development costs and undermined productivity gains. ❖

ness, for instance, card-issuing banks realized that cooperation would provide two critical benefits. First, it would allow them to develop a national (and later international) network of merchants that would accept their cards. Second, it would dramatically reduce their transaction-processing, technology, and brand-building costs, allowing them to focus their investments and attention on the kind of service programs that can provide real differentiation. To capture these benefits, the banks formed two member-owned agencies, which evolved into today's Visa and MasterCard organizations. There are now more than 1.5 billion Visa and MasterCard cards in circulation, accepted at more than 20 million merchant locations worldwide and used for nearly \$4 trillion worth of purchases annually.

The credit-card agencies have created value for all parties. Consumers have been given more credit and payment options—the agencies pioneered debit cards, among other innovations. The agencies themselves generate strong revenues through fees for basic and value-added services. And member banks have dramatically reduced their costs and risks. The cost savings provide members with an advantage over American Express (although American Express has other advantages) and a daunting barrier to new entrants.

Too Little, Too Late

Proactive collaboration remains, however, distressingly rare and is casting shadows on currently healthy businesses. Consider the pharmaceutical industry, where many companies continue to enjoy enviable profit margins as they reap the rewards of drugs developed years ago. But their future margins are under threat from the explosion in drug development costs. In 1975, it cost drug makers an average of \$138 million to bring a new therapy to market. By 2000, the cost had reached \$802 million. But pharmaceutical firms continue to compete broadly, each pur-

suing separate development or licensing initiatives for similar compounds. They often refuse to share even basic clinical information, such as data on liver toxicity, clinging to the belief that it will provide them with a competitive advantage. If the drug makers continue to ignore opportunities for strategic collaboration, they seem fated to endure the kind of margin erosion we've seen in the automotive, airline and other sectors.

What's particularly striking is that in all these industries there have been instances of competitors collaborating in the past and

reaping important benefits as a result. The Big Three car makers, for example, launched the U.S. Consortium for Automotive Research (USCAR) in 1992 to undertake studies in

such areas as safety and emissions. Most major pharmaceutical companies use sophisticated licensing partnerships to reduce costs and spread risks. Yet despite their own positive experiences with cooperation, they continue to shun broader opportunities for strategic collaboration. Their compete/collaborate ratios remain overwhelmingly biased toward competition.

Improving The Compete/Collaborate Ratio

Shifting those ratios requires, first and foremost, a change in managerial mindset. It also requires a practical, objective process for thinking through collaboration opportunities. In this area, few companies have in place either the expertise or the analytical frameworks required to make smart decisions. Every company will have to weigh different factors in plotting its collaboration strategy, depending on its industry's economics and structure and its own competitive positioning, but all companies need to answer four crucial questions: Where in our industry's value chain are the greatest collaboration gains likely to be found? What types of collaboration will allow us to best achieve those gains? Whom should we partner with? How do we overcome the "mortal enemies" objection?

What is your firm's compete/collaborate ratio?

Where in our industry's value chain are the greatest collaboration gains likely to be found?

Collaboration can unlock value in different ways in different areas of an industry's economic system. At the back end, for example, it can change the economics of innovation and discovery, allowing companies to reduce redundant investments in solving common problems, tackle larger problems by aggregating their resources, and find more creative solutions by tapping into a larger and more diverse pool of talent. In operations, it can change the economics of manufacturing by enhancing scale, spreading risk, aggregating purchases, and speeding the journey through the experience curve. And, at the front end of the curve, companies may have opportunities to enhance customer satisfaction by more tightly integrating the components of a solution or to reduce costs by consolidating low-value sales or service activities.

Start by assessing your industry's current performance in value creation along dimensions such as customer satisfaction, profitability, asset efficiency, and volatility. Different competitors will have different scores, but you'll be able to see the general trends and spot the bottlenecks that limit industry performance. Then move to the value chain itself.

Exhibit 2 shows the key activities of an illustrative company and lists some of the categories to gauge collaboration opportunities in each segment. In general, firms should try to identify activities that provide little opportunity for achieving competitive differentiation or influencing customers' perceptions of value, and that offer strong opportunities to enhance scale economies, asset efficiency, labor productivity, or innovation through the aggregation of resources from different companies. It is these activities that typically represent the strongest opportunities for collaboration.

What types of collaboration will allow us to best achieve those gains?

Collaboration can take many forms, ranging from informal cooperation to formal partner-

ship. And the right forms of collaboration will change over time, as you fulfill prior objectives and as customer preferences change.

In industries that have little experience with collaboration, it may be wise to begin with modest efforts, in order to build trust, learning, and momentum. You might partner on a narrowly defined project with a small number of companies with whom you have existing relationships. Timken works with competitors such as bearing manufacturer SKF to share logistics and e-business activities. In aerospace, Northrop Grumman has teamed up with BAE North America to develop an integrated microwave assembly for a joint striker fighter.

Or you might want to spearhead an industry-wide exploratory committee to evaluate collaboration opportunities and develop initial plans. For example, several mobile phone network operators in developing countries decided that the best way to promote adoption of mobile phones is to reduce the cost of the handset. So they joined together to aggregate their buying power, and Motorola has agreed to supply up to six million handsets for less than \$40 each. Such modest efforts provide a way to create a collaboration infrastructure, develop best practices, and build relevant skills.

Whom should we partner with?

Choosing the right collaboration partners is a balancing act. Linking up with many competitors through a consortium can bring greater scale advantages than collaborating with a smaller group, but operational conflicts and complexity also tend to increase as more partners are brought into an effort. And collaborating with companies that are similar to your own—in size, culture, and heritage—can reduce managerial and operational conflicts, but will also tend to decrease diversity, making it harder to think outside the box.

In choosing partners, therefore, you should carefully weigh both the project's goals and the characteristics of potential collaborators, asking such questions as:

Exhibit 2 Value chain analysis

Key activities	Channel	Service	Processing	Assembly	Component production	Procurement	R&D	
Source of differentiation	Y/N	Y/N	Y/N	Y/N	Y/N	Y/N	Y/N	
Position on scale curve								
Capital required/unit of output								
Opportunity for standardization	0% 100%	0% 100%	0% 100%	0% 100%	0% 100%	0% 100%	0% 100%	
Interface costs between value chain steps	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	
Can activity be eliminated?	Y/N	Y/N	Y/N	Y/N	Y/N	Y/N	Y/N	(e.g., inventory, distribution, warehousing steps)
What activities should be added?		<input type="checkbox"/>		<input type="checkbox"/>		<input type="checkbox"/>		(e.g., training, information provision, industry-wide promotion)
What activities should be transformed?		<input type="checkbox"/>			<input type="checkbox"/>		<input type="checkbox"/>	(e.g., Web sites instead of tech service)

- How tightly integrated will partner organizations need to be, given the project's scope, goals, and accountability arrangements?
- How similar are the potential partners' strategies and operating environments? Do they exhibit wide variations in performance on key measures related to the project goals, or is performance fairly uniform throughout the industry?
- What shared knowledge base or history exists among the potential partners? If the industry is tightly knit, will existing or past relationships help or hinder efforts?
- How much "common ground" do the potential collaborators have? Is there enough diversity in the collaborative design? Are there other potential partners, from within or outside the industry, that could inject new perspectives?
- Would there be benefits to bringing suppliers or customers into the group?

How do we overcome the "mortal enemies" objection?

There is a powerful psychological barrier to

collaboration: "We can't collaborate with our mortal enemies." But a quick look at the historical record suggests that this is not always the reality.

Hewlett-Packard (HP) and Canon are rivals in the printer business, yet they've worked very effectively in collaborative arrangements, such as HP sourcing printer engines from Canon.

WPP and Paris-based Havas are fierce rivals in the advertising business, yet they have worked closely together in media purchasing.

Sony and Samsung are global rivals in the consumer electronics world, yet both have begun collaborating on several fronts:

- Jointly investing \$2 billion in a factory in South Korea to produce liquid-crystal displays
- Sharing 24,000 basic patents that cover a range of components and production processes
- Participating in a consortium that is trying to establish the standard for the next generation of digital video discs and players

Crafting an effective collaboration is never easy, especially when the participants are intensely competitive. But the record shows that profitable collaboration can be achieved in ways that bring enormous economic benefits to the partners and their customers.

The Competition Paradox

In 1776, Adam Smith published his great defense of free market capitalism, *An Inquiry into the Nature and Causes of the Wealth of Nations*. By showing how competition lifts living standards throughout society, Smith successfully countered calls for increased regulation of commerce—and set the stage for the great gains of the Industrial Revolution. More than 150 years later, the economist Joseph Schumpeter added a memorable gloss to Smith's ideas, when he described how competition creates a cycle of “creative destruction” that continually brings new and better products into the marketplace.

Smith, Schumpeter, and the other great capitalist philosophers provide the intellectual bedrock for our faith and trust in the benefits of vigorous competition. But over the past 50 years, we have come to distort their teachings by using them to justify a blind and sometimes fanatical devotion to competition. Some business

executives and pundits have promoted a view of business as a form of warfare or sport—a game of “hardball” that can be won only through fierce and unrelenting conflict. That's a simplistic and dangerous view of business. Adam Smith and his followers understood that in certain cases unbridled competition may cause great harm—that mindless competition can bring not creative destruction but just destruction.

Given how easily global pressures can devastate the profitability of industries, we need to return to a more balanced view of competition—and a greater appreciation of the role of collaboration in engendering and sustaining healthy economies. When companies compete too broadly—battling in areas that create little value for customers—they end up wasting enormous amounts of money and weakening the very structure of their industry.

By refocusing competition on areas that really matter, strategic collaboration promotes the kinds of robust rivalry that engender better products, lower prices, and stronger industries and economies. That's the great paradox of competition: By reducing it in some areas, you strengthen it in the places that provide the most benefits to the most people. ❖