



Four ways incumbents can partner with disruptors

Turning disruption into a source of competitive advantage

Thriving on disruption series

In today's digital age, disruptors can transform, create or destroy a market altogether at pace and leave incumbent players with a burning platform. For incumbent CEOs, allying with disruptors can be the best solution and help turn disruptive pressures into a competitive advantage.

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The disruption challenge

Organizations in today's digital era have less time to ponder the challenges posed by disruptors, as new entrants and new technologies are quickly unsettling traditional business models and creating new ones.

Incumbent firms, those that currently play a leadership or top-tier role in their sector, are increasingly faced with disruptors, new organizations that upset the status quo. Such disruption is increasingly common as boundaries between industries dissolve in the digital age, allowing companies to enter new sectors with little physical infrastructure.

Partnering with disruptive firms is often the preferred choice by incumbents in meeting these challenges because partnership can import new technology, talent and expertise, enhancing an incumbent's business model by creating a compelling and more competitive new offering, while being cheaper and posing lower risk.

As Nicholas Griffin, Head of KPMG Global Strategy Group, KPMG International and Partner, KPMG in the UK notes, "Disruptive business models tend to use technologies, knowledge and strategies from more than one sector and then combine them to create new offers, dis-intermediate, and pull in new customers. It is possible for players from other sectors to enter markets and disintermediate existing relationships because they bring a different mindset, resources, approaches and offers."

Sometimes an incumbent can safely ignore a disruptor, if the threat posed is mild or transient, and in some situations an incumbent may wisely decide to nullify a disruptor through acquisition or response tactics.

Yet many organizations are reacting to disruption by striking partnerships with disruptors in order to develop new capabilities designed to benefit the incumbent's financial, business and operating models.

As Nicholas Griffin notes, "Organizations are starting to realize that they do not have the time, resources, capabilities, agility and risk appetite in-house to create and launch new models. Collaboration has several benefits. It enhances innovation and stimulates experimentation because it leverages the strengths of each party. The pace may well be faster and the costs can be lower than going it alone. Collaborations are easier to unwind and multiple collaborations create strategic and operational optionality."

A KPMG in the UK study of more than 80 incumbents faced with disruption found that partnership (sometimes coupled with investment) was by far the most commonly pursued route. Further analysis of more than 30 incumbent-disruptor partnerships since the start of 2014 found that such collaborations generally followed four patterns:

- 1 to fend off competition from new players in other sectors (three incumbents);
- 2 to improve customer service and loyalty (seven incumbents, including in the energy, banking and travel sectors);
- 3 to reach new markets or demographic groups (10 incumbents, including in retail, entertainment and healthcare); and
- 4 to develop new capabilities quickly by incorporating their distinctive technology or expertise (11 incumbents, including in finance, energy, technology and computing).

A discussion of those four partnering paths follows, along with an illustrative case example of each route.

The partnership opportunity

Four partnering paths to respond to disruption.

1 Partnering to fend off competition from new players in other sectors

With boundaries between industry sectors dissolving, incumbents can no longer be concerned only about traditional rivals. Technology has dramatically lowered barriers to entry in once well-protected sectors. So companies with no prior experience in a particular industry can quickly become major players because they bring new models that exploit the prevailing structural and behavioral characteristics and inefficiencies. CEOs of incumbent organizations should create early warning detection systems for new entrants, and be ready to act quickly should the insurgent present a significant opportunity or threat.

For more than a century automobile companies have sold cars to consumers, and to commercial enterprises including taxi drivers licensed to carry passengers. So the advent of mobile apps by the likes of Uber allow consumers to more easily hire private cars from their smartphones. Google parent Alphabet is developing self-driving cars which pose a threat to carmakers¹. Companies such as Google and Apple, as well as other technology companies have the potential to become major players in a mature market. Organizations from multiple industries including insurance, healthcare,

and energy are targeting automobiles on the basis that they are valuable real estate in which people spend significant amounts of time. Unlike a couple of decades ago drivers are now permanently connected and able to receive as well as transmit personalized data that can be used to create new business models for providers and opportunities for the driver.

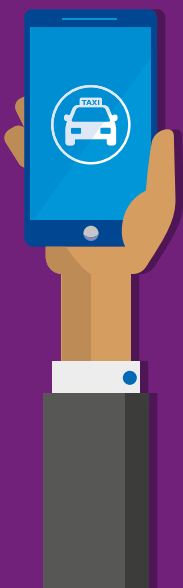
Responding to this changing landscape, General Motors in early 2016 invested US\$500million in ride-sharing firm Lyft² and acquired self-driving car company Cruise Automation³ to accelerate GM's work in autonomous vehicles. Toyota and Volkswagen have respectively struck partnerships recently with ride-sharing companies Uber and Gett^{4,5}.

"The traditional boundaries between sectors and regions have blurred," says Jaideep Prabhu, Professor of Marketing at Cambridge Judge Business School, University of Cambridge. "Incumbents can now face competition from anywhere. The threat might come from firms in their sector from emerging markets, or from start-ups in their sector in their home market, or indeed from large incumbents in seemingly unrelated sectors from both the developed and emerging world."

2 Partnering to improve customer service and loyalty

Companies with an established customer base can harness disruptors to improve the experience of those customers through added capabilities and functionality. By partnering with firms offering disruptive technology, incumbent CEOs can demonstrate that they don't take customers for granted and seek to earn their continued loyalty by offering the latest in ease, comfort or value.

Caterpillar has been known for 90 years for its tractors and other heavy equipment. Reliability is vital for its customer base that includes farmers and builders who depend on the machines for their living. So Caterpillar partnered with predictive analytics firm Uptake in order to help customers monitor and understand the state of their equipment. Together Caterpillar and Uptake are analyzing quintillions of bytes of daily data and turning that data into recommendations Caterpillar customers can use to catch maintenance issues at an earlier stage and thus reduce costly periods of downtime as well as overall ownership and operating costs⁶.



3**Partnering to reach new markets and demographics**

Many incumbents have built up a stable and loyal customer base over many years. But collaboration with disruptors to tap new geographies or age groups can protect and increase those customer numbers. Incumbent CEOs should be alert to how partnering with disruptors can help their companies keep pace with changing customer habits, needs and trends.

Telemedicine, or the provision of healthcare advice via phone or Internet, has been growing rapidly as a less costly alternative to hospital or clinic settings for minor ailments like flu or rashes. In the face of such disruption, Seattle-based telemedicine firm Carena Inc. — with investment from Cambia Health Solutions, McKesson Ventures and others — has partnered with health systems in many US states to provide virtual care partnerships which allow branded healthcare provision outside traditional settings, thus expanding their reach⁷.

“Telemedicine is a good example of disruptive innovation in healthcare,” says Stefan Scholtes, Professor of Health Management at Cambridge Judge. “This challenges the centuries-old business model of the general hospital and forces hospitals to integrate their services with care in the community.”

4**Partnering to develop new capabilities quickly by incorporating disruptors' distinctive technology or expertise**

Developing solutions in-house can be time-consuming and costly for incumbents, so partnering with disruptors which have already created valuable capabilities or filled a distinct market gap can be a very effective route. Incumbent firms which spot such valuable capabilities and know-how at an early stage can gain a valuable advantage, so incumbent CEOs should seek such partnership possibilities when they see a need to move quickly in a new direction. Collaborations tend to be less costly, less invasive and far quicker to execute than acquisitions.

Pacific Gas and Electric Company (PG&E) expanded a strategic alliance with Silicon Valley-based Picarro Inc. to reduce methane emissions from its gas system through Picarro's leak-detection technology. PG&E says that Picarro's vehicle-mounted instruments are 1,000 times more sensitive than traditional leak detection equipment, so PG&E has been able to significantly reduce minor leaks in its system. The expanded alliance is designed to integrate results from the leak detection vehicles into PG&E's information systems to speed up analysis and repair, support predictive analytics to assess the company's gas-distribution network, and improve the accuracy in measuring the volume of methane emissions⁸.

Potential partnering pitfalls

While collaboration can bring valuable new capabilities to incumbents, new partners may also import difficult issues to those incumbents.

New and disruptive firms may offer exciting opportunities for partnering, but they can also bring uncertainties related to the rapid market changes that spawned them. This in turn can present new risks, governance issues and cultural challenges to established companies, implications for reputation, brand dilution and operational excellence.

“The key thing for incumbents faced with disruptors is to engage in what I would call ‘smart partnering’ in order to build new capabilities,” says Stelios Kavadias, Professor of Enterprise Studies in Innovation & Growth,

and Director of Research at Cambridge Judge Business School.

“Partnering can be very beneficial, but it’s important for incumbents to first analyze carefully their competitive position, the complementary capabilities of the partner, and how the incumbent needs to structure its business in order to fully take advantage of the partner’s strengths. Partners are really important, but it’s also critical for the incumbent to choose carefully and figure out they can partner in the most effective way.”

Actions for CEOs

Turning disruption into competitive advantage.

Incumbents

CEOs of incumbent firms should look for the signposts of disruptive firms or capabilities threatening their business. They should consider:

- whether partnering with disruptors to create something new and compelling is the best course in responding to disruptive threats. In some cases, CEOs may instead ignore or nullify disruptors through acquisition or by developing capabilities in-house
 - which of the four principal paths for partnering with disruptors will best benefit their firm's business or operating model
 - how their business can best incorporate these new partners to create new capabilities and enhance the organization's competitive position
- ! Choose carefully: CEOs who select the wrong disruptor as partner can quickly dent an incumbent firm's hard-earned reputation.

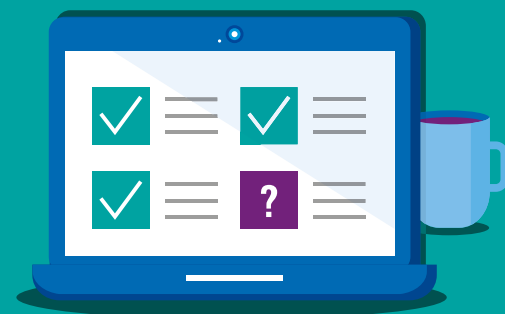
Disruptors

CEOs of disruptive firms should think about how partnering with an incumbent can help their firm grow faster and gain recognition. They should consider:

- how their firm's unique technology or expertise might be attractive to incumbents seeking an advantage.
 - which of the four principal paths of partnering with incumbents may best suit their firm.
- ! Choose carefully: Select the right incumbent for partnership, keeping in mind financial, operational and contractual implications.

Actions for both incumbents and disruptors

- Understand the implications of the collaboration on the financial, business and operating models of both parties. New relationships can bring unintended consequences that can create stress and underperformance.
- Agree how to unwind the collaboration before any contract is signed.



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Actions:

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