

Exclusive licensing deals a tool for collaboration, study says

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Exclusive licensing deals are a two-way safety net that fosters cooperation as new product ideas weave their way toward the marketplace, according to new research led by a University of Illinois business strategy expert.

Deepak Somaya says the findings reveal that granting rights to a sole partner is a tool to curb risk and leverage cooperation, not to corner the market when breakthrough innovations are ultimately launched.

"We found that exclusive licensing is very significantly about the collaboration needed to reach the marketplace and succeed, not about dominating the marketplace," he said. "Past research theorized that exclusivity was largely about creating downstream monopolies to drive sales and profits."

In short, the deals link innovators with partners who are skilled in taking new products to the marketplace, according to findings that will appear in the *Strategic Management Journal*. Those partners, in turn, develop a vested interest in success because exclusivity means no new licenses will water down earnings potential once the partner has helped the product succeed.

"Partners will be less willing to give 100 percent if they can't reap the benefits in the end, so exclusivity provides an incentive for cooperation," said Somaya, a professor of [business administration](#) in the nationally ranked U. of I. College of Business.

But exclusive deals also can be risky, according to the study, co-written by business professor Young Jun Kim, of Texas A&M International University, and Nicholas S. Vonortas, an economist at George Washington University.

Partners can turn out to be less effective than hoped or fledgling product innovations can turn out to have broader, more-profitable applications, such as a potential drug for Alzheimer's disease that later proves useful to treat Parkinson's disease, Somaya said.

Innovators can manage those risks by limiting the scope of exclusivity, according to the unique study, which analyzed more than 200 exclusive licensing deals involving publicly traded biotechnology, pharmaceutical and chemical firms.

A contract for an early-stage pharmaceutical breakthrough, for example, might grant exclusivity only for Alzheimer's treatment while the inventor retains rights for all other potential applications.

"With early-stage technologies, the licensor doesn't want to give away the store, but the licensee also wants protection because developing and commercializing the product will require a lot of investment," Somaya said. "Scope restrictions address both of those concerns."

Whether blanket or restricted, the study found that exclusive licensing is commonly used as a contractual "hostage" that innovators voluntarily give up as a sign of good faith that nurtures cooperation.

Somaya says hostages can provide incentives and safeguards for both creators of new product ideas and the sole partners signed on to commercialize them.

"There's is simple analogy in car shopping. Dealers want you to test drive

because it can close the sale. But how do they know you'll come back? Well, it's because they have your driver's license or the keys to your car," Somaya said.

"But there's a danger in giving too much of a hostage away, which is where restricted exclusivity come in," he said. "And in some cases, it may make sense to not give a hostage at all and license non-exclusively to multiple partners. If there isn't a need for close cooperation, all it does is shackle your own feet."

Somaya says giving away hostages can yield a level of cooperation that could never be spelled out in a contract, especially with early-stage product ideas that are still evolving.

"Incorporating hostages into licensing contracts is a valuable complement to detailed contractual clauses," he said. "It creates incentives for partners to cooperate willingly and automatically, even when situations arise that they did not anticipate and even if the other party can't observe the level of support being offered."

Provided by University of Illinois at Urbana-Champaign

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