

# Licensing proprietary technology



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In today's business circumstance, proprietary technology play a significant role in business, because it is considered as competitive advantage. It has recently been argued that licensing proprietary technology to foreign competitors is the damaged marketing strategy. However, the statement might not be true. Empirical results based on an example of licensing proprietary technology show that by licensing proprietary technology to other companies can also bring benefits to licensor. With several literatures, this essay argues that statement is not absolutely right.

Keywords: Licensing proprietary technology, competitive advantage, foreign competitors

## **1. Introduction**

In today's competitive marketing, it is significant for a firm to have competitive advantage, because several previous studies have shown that sometimes competitive advantage could lead to the domination in the whole market, it can bring a firm more profit. There is an issue regarding licensing proprietary technology to foreign competitors, it is probably negative related to competitive advantage. The purpose of this essay is to discuss the concept of competitive advantage and what is licensing proprietary technology, then by comparing with other technology transfer, use evidence to argue whether licensing proprietary technology is the negative method for competitive advantage. With some literature, this essay examine that licensing proprietary technology might not the best way to give up a firm's competitive advantage, because it depends on how a firm operates licensing strategy. There are several models to enter foreign countries, such as exporting, FDI and Joint ventures, all these ways should have their

shortcomings. Therefore, the opinion of licensing proprietary technology has negative relationship with competitive advantage, in some ways, might be right.

## **2. Internationalization strategies**

In global business environment, there are three strategies to expand markets widely, which are exporting, licensing and FDI. A comparison of each entry method is shown in Figure 1. (Morrison, 2011)

### **2. 1 Exporting**

Exporting is a clear entry method for a firm to offer products to foreign countries. According to Morrison (2011, p. 169), the exporter might consider costs for long distances, and face some trade barriers or law issues in several markets.

### **2. 2 Licensing (Franchising)**

Licensing is a traditional way to enter foreign markets. The concept of licensing is that the licensor permit the licensee to use its property (Morrison, 2011). As Sherman (2004, p. 361) stated ‘ Licensing is a contractual method of developing and exploiting intellectual property by transferring rights of use to third parties without the transfer of ownership.’ Licensing might include patents, inventions, formulas, processes, designs, copyright and trademarks. In addition, franchising is a specialised form of licensing. (Morrison, 2011)

## **2.3 FDI**

FDI means a firm invests directly in production or business in a foreign country. FDI has four forms, Subsidiary, Greenfield investment, Acquisition and Joint venture.

## **3. Competitive advantage**

In 1985, competitive advantage was announced to be one of the competitive strategies, which focus on firms. Competitive advantage is like the core of firms in competitive markets (Porter, 1985). Technology is regarded as firms' value chain, and innovation strategy plays an important role in both low-tech and high-tech firms (Porter, Competitive advantage: creating and sustaining superior performance, 1985). As Porter (1985, p. 1) stated 'Competitive advantage grows fundamentally out of value a firm is able to create for its buyers that exceeds the firm's cost of creating it.' Several research have shown that competitive advantage is related to a firm's opportunities and treats, as well as mentioned the strengths and weaknesses of competitive advantage (Barney, 1991). Technologies can be perceived as a vital effective tool for competitive advantage. There are four factors which are related to competitive advantage, demand conditions, factor conditions, firm strategy and supporting industries. (Porter, The competitive advantage of nations, 1990). In addition, how does a firm get competitive advantage? Porter (1985) mentioned the theory of 'industry segmentation and competitive advantage.' In this case, technology is one of them, which includes other sectors such as size, price, features, and performance.

## **4. Four types of technology transfer**

### **4. 1. Licensing proprietary technology**

Technology plays a significant role in global economy, in other words, technology might be a vital source of competitive advantage (Morrison, 2011). Many late industrializing countries have relied on licensing technology, like US and Japan (Morrison, 2011). As Morrison (2011, p. 353) stated ' the partner who owns important technology is in a stronger position to exert control through equity ownership.' Obviously, licensing proprietary technology might lose some competitive advantage. For instance, Apple Inc., which highly depends on technological inventions and innovations, like iPhone and iPad, if Apple license its rival companies the core technologies of the products, it is highly possible that Apple would lose market share to at least a certain degree and lose the competitive advantages. A licensing agreement could include the licence fee or royalty, for the technology and know-how from the licensor (Saadi, 2011). The licensor gains the value of the licensee fees and royalties from some emerging countries. (Saadi, 2011)

### **4. 2. Technology transfer of FDI**

FDI usually occurs in emerging countries. For most host counties, FDI is a convenient way to imitate and apply technologies, even management methods (Morrison, 2011). China has got such benefits from the FDI of US, for example, Appe's factories named Foxconnin in China, the employees might learn technology from assembly line.

### **4. 3. Joint ventures**

A firm has two or more owners that named joint ventures. Recently, increasingly foreign investors would like to use this type of strategy, because <https://assignbuster.com/licensing-proprietary-technology/>

in this way the company can be expanded promptly, at the meantime, costs and risks can be reduced directly (Yan, 1999). China has gained the profits from foreign partners' technology (Morrison, 2011).

#### **4. 4. Trade**

Generally, trade is a tangible licensing technology, because some labour intensive countries import foreign technological products, they might use some time to study and imitate the process of technology (Morrison, 2011).

### **5. Entering Foreign Markets & Competitive Advantages**

Although technology could lead to a firm's competitive advantage, compared with the four types technology transfer, by licensing proprietary technology to a firm does not necessarily means to give up competitive advantage.

Though it might depends on different situations. Then how to choose channels to enter foreign markets?

First of all, firms have different elements of competitive advantage.

If one company is a proprietary technological company, licensing might not be suitable for it, because Morrison (2011) summarized that technology licensing is believed as a kind of advantage strategy to the licensor. Take Microsoft's Windows and office software as an example, Suppose Microsoft licenses their technology to foreign countries' companies, it could eventually results in a lost for their large proportional market share and benefits as well. As Porter (1985, p. 166) stated ' Technology is embodied in every value activity in a firm, and technological change can affect competition through its impact on virtually any activity.'

In Porter's book (1985), he pointed out several types of technologies, named 'technologies in a firm's value chain', all of these technologies reflect in competitive advantage.

Therefore, what has been discussed above was merely one of technologies, like iPad products. On the other hand, technological leadership is another one, so if a company has succeed as being technological leader, licensing might not influence negatively on competitive advantage. (Porter, 1985).

Currently, several firms have licensed their proprietary technology to foreign countries, and they get benefits from that. IBM is a special example to support this positive opinion. IBM used licensing strategy, and on their official website there is a link that shows software license agreements (Software license agreements, 2009). Due to IBM and Microsoft's broad licencing, many developers were attracted to develop applications for them. The rapid speed of that applications appear in the market finally convinced the whole market that it is the IBM-compatible architecture the future of the market, not Apple Macs'. (Software license agreements, 2009). Moreover, IBM's annual report shows that the company's revenue has increased for the past several years and implies that there is not necessarily a negative correlation between licencing and competitive advantage.

IBM can get hundreds of millions of US dollars in annual licensing revenues, and IBM has earned profits by licensing technology (Chesbrough, 2007). Although they licensing technology, they do not give up their competitive advantage. However, as Porter (2000, p. 25) mentioned that competition and cooperation can coexist. So far, there is no sufficient evidence to support

licensing proprietary technology is the best way to abandon firms' competitive advantage.

Licensing proprietary technology to foreign competitors also might mean abandon a firm's competitive advantage. As Lichrenthaler et al. stated that 'With regard to the benefits from licensing, firms may enter new product markets because they may sell products that are complementary to the licensed technologies' (Lichtenthaler Ulrich, Ernst Holger, 2012). According to Lichrenthaler et al. (2012), firms might license a technology to a less competitive foreign competitor in order to prevent more competitive foreign competitor from entering product market. The previous research examined that the developed countries always get benefits from transferring its technology to foreign countries (Saadi, 2011).

Licensing is to be seen as an alternative way of FDI (Jiang Marshall S, Aulakh Preet S, Pan Yigang, 2009). Apart from the positive effect, licensing proprietary technology might let a firm to be in a weaker competitive position. (Fosfuri, The licensing dilemma: Understanding the determinants of the rate of technology licensing, 2006). Assuming if Apple Inc. licensing their proprietary technology to Foxconnin, obviously, Apple Inc. might lose the dominant position in high-tech field, because sometimes proprietary technology may be a monopoly in market. If firms license proprietary technology to foreign competitors, the licensor(s) could lose profit in a long run.

When a firm develops a new technological product based on a single technology, then they license a different technology to licensee to develop



complementary products, they would not give up their competitive advantage. Like Apple Inc. they permit Foxconnin to assemble iPhone or iPad, only the assembling technology is licensed to Foxconnin. Under this situation, Apple would not lose their market position or competitive advantage at all. On the other hand, a firm might develop and license the some technology to a licensee (Lichtenthaler Ulrich, Ernst Holger, 2012), like Microsoft, licensed its intellectual property to Panasonic in 2010, ' Microsoft offers flexible intellectual property licensing programs that give companies access to many of the foundational technologies in its own products, allowing those companies to build devices, applications and services that work seamlessly with each other.' Microsoft has entered into exFAT licensing agreements with Sanyo and Olympus. (News Center, 2010). If small firms which based on technology license their intellectual properties to other companies, they may lack of ' downstream manufacturing, distribution or marketing capabilities' (Fosfuri A. , 2006). However, increasingly firms would like to apply licensing proprietary technology apart from IBM and Microsoft, such as several large technology-based firms Procter & Gamble, Boeing and DuPont (Fosfuri A. , 2006). Hence, if licensing proprietary technology to foreign competitors is the best way to give up the competitive advantage, why so many firms operate this strategy for their marketing expansion? As two effects Fosfuri (2006) mentioned in 2006, which are revenue effect and profit dissipation effect, might argue against the former question. Firstly, he stated the revenue effect is about the visible profit, like the licensing payments and all possible transaction costs. The bargaining power tends to be positive to the licensor, because the licensor has intellectual property rights. While the other effect, the profit dissipation effect may decrease the

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benefits of licensor. From many contracts, the licensors impose restrictions and clauses to protect them from their competitive threaten. All in all, if the profit dissipation effect occupies dominant position which like monopoly, licensing proprietary technology to foreign competitors would give up their competitive advantage. Otherwise, licensing might be a convenient model to enter foreign market. Moreover, for most firms, they have not licensed their proprietary technology, because they may encounter pressure of competitive advantage in today's market.

## **6. Conclusions**

In this essay, it argued the opinion that licensing proprietary technology to foreign competitors might abandon the firms' competitive advantage. It actually depends on different types. Under global business environment, technology transfer is an effective method to enter foreign markets, it is an efficient tool. While some successful firms like IBM, have implemented licensing strategy in overseas market, they do not lose their competitive advantage, instead, they gain benefits from licensees. Consequently, it could be said that licensing proprietary technology to competitors might leads the firms to lose their competitive advantage, but it is not the " best way" to give up firms' competitive advantage. As this essay mentioned, the opposite result of licensing could be based on firms' types, which are the ones with different technologies or with only one technology. It is clearly shown that licensing proprietary technology is not absolutely bad market strategy, every coin has two sides, so does licensing proprietary technology.