Strategic negotiations: three essentials for successful partnerships with startups

Rudolf Freytag

Partnerships between innovative startups and large, established corporations have become increasingly common in recent years. This type of collaboration offers benefits for both sides, and the chances of success improve if both sides approach negotiations in a careful and strategic manner.[1]

In practice, there are three main questions for startups approaching collaboration with a big player. How can you properly assess the risks and opportunities? How can you systematically and efficiently negotiate without getting exploited? And how can you negotiate favorable terms of collaboration given the limited resources and short time frame typically available to startups?

A wide range of literature looks generally at the theory and practice of negotiations.[2] But there's a gap between the academic research and advice and what practitioners need to know about negotiating the partnership between startups and industry giants. To compensate, startups need a strategic process to systematically and efficiently negotiate partnerships with established players. The strategic process introduced here, based on my experience of more than a decade from the perspective of the established company, has a proven track record in the real world.

Benefits at a glance: a win-win situation

The partnership between startups and established companies can only succeed over the long term if the interests of both sides are properly taken into account. It's important that each partner have a clear concept of what the other partner hopes to gain from the partnership.

Some of the basic advantages that startups and established players might derive from a partnership are:

- Startups seek the access to customers, data, technologies and production capacities that established companies can offer – and this access is very valuable. A startup can sell its products through its established partner's sales channels, for example, or win the partner itself as a customer. Or the startup can seek to use the established company to expand its business to another country by taking advantage of the partner's global sales and production structures and its reputation in the foreign market.
- Businesses with a strong presence in a market also make promising investors for startups, since they can provide capital in both the startup phase and the subsequent growth phase. Having an established company as a strategic anchor investor can signal other investors that the new company has good prospects. The investment in a

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startup can also open the door to a subsequent full acquisition of the smaller company by the larger company, which can provide an attractive exit option for the startup.

- Startups also make attractive partners for established companies, because the startups offer an environment to test new business ideas outside of their own regular business organization. This is especially true for innovative business models in which the customer base, sales channels and value chain may not be compatible with the company's own core business. For many big industry players, this is often a valuable opportunity to test out new ideas and decide whether and how these new business activities can enhance the current portfolio or should be introduced on a disruptive parallel track.[3]
- Startups also give established companies a "crystal ball" to look into the future so that they can identify interesting trends early on and respond accordingly. Partnership here does not necessarily mean a long-term financial investment in the startup. Much more common are temporary, clearly defined partnerships on a particular project that can – but by no means must – be expanded down the road through financial investments.

Case: the FreeWire and Siemens partnership

An example of a project-based partnership without any financial investment is one, now ended, between the Silicon Valley startup FreeWire and the global player Siemens.[4] Partnering with and investing in startups like FreeWire has been an important element of the global business innovation strategy at Siemens in the areas of automation, digitization and electrification for over 25 years.

FreeWire's founders saw that more and more employees at major Silicon Valley companies were driving to work in electric vehicles, but there was a shortage of charging stations in the companies' parking lots. They recognized that it would be both expensive and inefficient for companies to increase the number of charging stations, because the vehicles would only need a short time to recharge and would then block the charging stations unnecessarily for the rest of the day.

The innovative idea of FreeWire was that, instead of having electric vehicles drive to charging stations, mobile charging station should bring the electricity to the commuters' vehicles. Drivers would use a smartphone app when they arrive to input their parking space number and desired departure time, and their vehicle then would be charged with a mobile charging station operated by a FreeWire employee before they were ready to leave work.

The decision-makers at Siemens Electromobility were intrigued by this customer-friendly approach, and this led to a partnership between FreeWire and Siemens. Siemens Electromobility provided FreeWire with the hardware and software to build its first mobile charging station, which helped the startup bring its product to market for validation much more quickly. Siemens was then on hand for the pilot test with FreeWire's initial customers in Mountain View (California) to see how the idea worked in practice and get an idea of whether it might make a good addition to the Siemens product portfolio. This yielded a partnership and a classic win-win situation.

FreeWire Technologies is now a leading manufacturer of mobile electric vehicle charging stations.

Three "Essentials" for a breakthrough: It's the concept that matters

There are three essential elements in a successful negotiation strategy that allow startups to systematically and efficiently partner with established companies:

- Essential 1: Strategic balance.
- Essential 2: Stakeholder alignment.
- Essential 3: Understanding the negotiation space.

These three essentials are not just steps that you take one after another in the course of the negotiation process; they play an important role in every phase of negotiations.

Essential 1: Strategic balance

Exhibit 1 shows some of the "strategic benefits" new and unknown companies can gain from partnerships with established players.

One strategic benefit for FreeWire, for example, was the opportunity to validate its product for customers much more quickly than would otherwise have been possible if Siemens had not provided the hardware and software. In exchange, FreeWire had to agree to share with Siemens the insights it gained from the pilot runs with its initial customers. This information-sharing represented the "strategic costs" to FreeWire of the partnership with Siemens. FreeWire had to decide whether the strategic benefits and strategic costs of its partnership with Siemens were balanced.

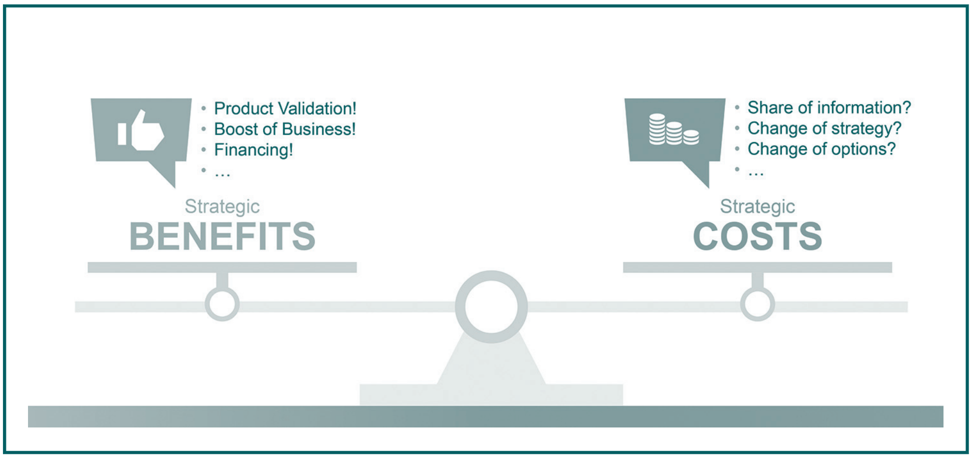
The primary objective of a startup in negotiating a partnership with an established company must be to preserve the strategic balance – an equilibrium between strategic benefits and strategic costs.

Typically, the strategic benefits for startups are relatively clear, but the strategic costs are often much more difficult to discern, as they are usually less obvious, manifest themselves at some vague point in the future or are hard to assess in monetary terms. But that in no way changes their tremendous importance, as the following two examples illustrate.

Change of strategy. One category of strategic costs is shown as "change of strategy" in Exhibit 1. Beginning a partnership with an established company can induce a startup to change its basic strategy for the purpose of optimizing the benefit it derives from the partnership. A startup might focus on a particular market segment in which the established company is active, for example, because this maximizes sales of its innovative solutions to the partner itself or to other companies through the partner's sales channels. If this limits the startup's options in favor of the larger partner, this change of strategy is a strategic cost. It might also be the case, however, that the discussions with the established partner gave the junior partner new insights into the market and that this change of strategy was just what it needed to flourish. In that case,

> **"Startups need a strategic process to systematically and efficiently negotiate partnerships with established players."**

Exhibit 1 Essential 1: Strategic balance



this change of strategy is more of a strategic benefit than a strategic cost. This example illustrates nicely that the strategic costs are not easy to assess.

Change of options. Another category of strategic costs illustrated in Exhibit 1 is the change of options. This happens when a startup's partnership with an established company results in a narrower or broader range of future options for the new company.

For example, recruiting an industry giant as an investor through a partnership may offer a strategic benefit for a newcomer. But it can limit the startup's future options to find other investors such as direct competitors of the established company. Or venture capitalists might decline to invest in the new business if they suspect that the larger company will prioritize its strategic interests causing the startup to have limited autonomy to maximize the return on investment.

Another example of a change of options is a partnership between a startup and an established company with the aim of selling the junior partner's products through the sales channels of the senior partner. Although this is a strategic benefit, the result can be to limit the startup's options for eventually selling the company. This is because the startup's revenues would be linked to its senior partner. Therefore direct competitors of the senior partner may not be suitable buyers, thus the value of the startup could be jeopardized.

The startup must carefully analyze the potential strategic balance even before negotiations begin. At the outset it's not always clear whether a particular circumstance is a strategic cost or a strategic benefit. But considering both possibilities provides greater insight during the negotiating process.

The strategic balance is the guiding strategic negotiating principle from which the startup defines its priorities, demands and the circumstances under which it may have to walk away from negotiations. That's why the startup must continuously re-assess the strategic balance and adapt its negotiating strategy based on the progress of the negotiations and any new insights it gains.

Essential 2: Stakeholder alignment

Stakeholder alignment (Exhibit 2) considers who the startup's negotiating partners at the established company are and how they need to be addressed.

Exhibit 2 Essential 2: Stakeholder alignment

They include everyone who is a stakeholder in a potential partnership. Exhibit 2 shows some of the key stakeholder groups. The startup must identify these people, contact them personally if possible and understand and address their interests and priorities in the potential partnership.

Typically, the established company will appoint a chief negotiator, who is empowered to negotiate with the startup. The chief negotiator serves as the company's point of contact in negotiations with the startup and above all is solely responsible for coordination among the stakeholders throughout the established company's hierarchy. This is very helpful for the startup. At the same time, however, it carries the risk that the negotiator will limit contact with the other stakeholder groups, making it very difficult for the potential junior partner to identify the stakeholder interests and priorities and steer the negotiating strategy accordingly.

For the startup FreeWire, the two primary stakeholders in the Siemens Electromobility unit were the Product Management and R&D organizations. Product Management actively drove the potential partnership with FreeWire from the start and saw it as a good opportunity to seize the market opportunities of the mobile electric vehicle charging stations. For R&D, the partnership initially meant a significant addition to its workload, since it had to provide FreeWire with the hardware and software needed to build the proof of concept prototype and show FreeWire how to use it. But this was, in fact, less work than developing a commercial prototype for Siemens Product Management, and so R&D supported the partnership.

This example illustrates why it's necessary to understand the precise interests and priorities of all stakeholders and address them before and during negotiations.

The sales organization in the senior partner is often a key stakeholder, and the junior partner needs to fully understand its goals. In many partnerships the plan is to sell the startup's products through the established company's sales channels. This can only work with the support of the senior partner's sales organization. Sales will want the startup's product to be easy to sell, easy for customers to understand, and equal in quality to the company's other products. It should also come with a long-term service commitment and a realistic sales incentive system. All this needs to be taken into account in the partnership between the startup and the established company to achieve a genuine alignment with Sales. One path might be to proceed incrementally, starting with a limited pilot project in one region to gather experience and build up trust before expanding the project in stages.

For a startup, a good alignment with the established company's stakeholder groups is important for successful negotiations. What's more, it builds a foundation for a close and trusting working relationship in the day-to-day process of managing the partnership. Experience shows that many of the problems in the implementation phase of a partnership have their origins in an inadequate stakeholder alignment during the negotiation phase. So investing the necessary time and energy here pays off.

Essential 3: Understanding the negotiation space

In addition to the questions of strategic balance (Essential 1) and stakeholder alignment (Essential 2), there is a third key question that startups should consider as they map out their negotiations with established firms. It's the question of negotiation space (Essential 3) – which points are negotiable and which are difficult or impossible to negotiate? Exhibit 3 illustrates some of these points.

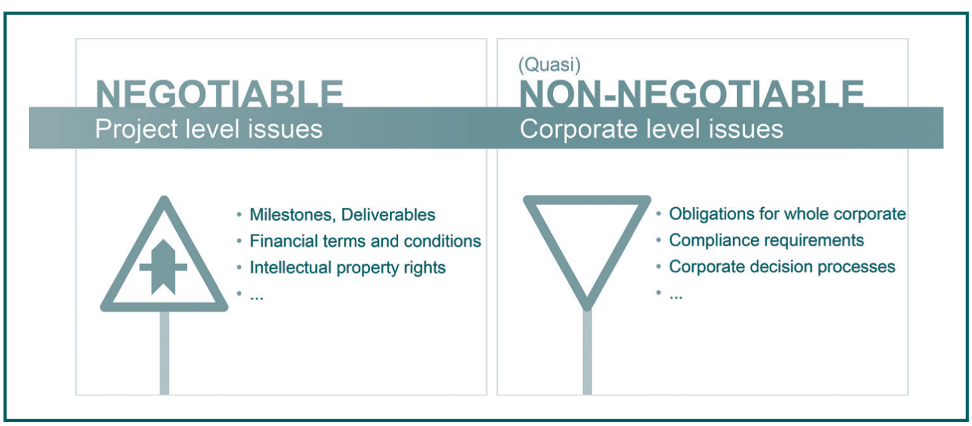
Typically, all the issues specifically relating to the project at the center of the proposed partnership are entirely negotiable. This includes the essence of the partnership: timelines, work packages, sales objectives, prices, payment dates and so on. The use of intellectual property rights and licenses relating directly to the partnership are also clearly negotiable points. So the negotiation opportunities are quite numerous and should be fully understood.

Those matters in the partnership that affect corporate level issues of the established firm, however, are difficult or impossible for a startup to negotiate. This includes language in the partnership agreement spelling out general obligations for the established company, such as non-compete or non-assert clauses. Requests by the junior partner for the senior partner to amend its general rules and regulations, such as the corporate compliance guidelines, are also practically non-negotiable in a partnership agreement. The negotiation topics that can be successfully addressed by individual stakeholders, including the corporate negotiator, typically are limited to the specific partnership, not to corporate-level issues. Changing corporate-level issues would require an exception to be made by the corporate management, and this is very difficult to obtain. Keep in mind that even a mutual understanding that something is "negotiable" simply means that it can be negotiated – not that the negotiations will be easy.

Enjoying the benefits of a partnership: this strategy makes it possible

The strategy of the three "Essentials" should make preparations easier and the actual negotiations more systematic and efficient – key prerequisites for a long-term and, above all, successful partnership.

Exhibit 3 Essential 3: Understanding the negotiation space



> **"There are three essential elements in a successful negotiation strategy that allow startups to systematically and efficiently partner with established companies: strategic balance, stakeholder alignment and understanding the negotiation space."**

This doesn't mean, of course, that negotiations cannot fail. But it ensures that a startup is professional in how it negotiates with an established company and can recognize quickly if the two companies even have enough in common for a partnership to succeed. This helps avoid long and exhausting negotiations that will ultimately fail and compromises that will turn out to be detrimental to both parties.

The strategy introduced here for how a startup can negotiate successfully with an established company can also easily be applied to the perspective of an established company negotiating with a startup. The strategic balance is critical in that case as well, and the importance of stakeholder alignment should never be underestimated. A startup may not have many employees, but these employees live and breathe their idea and must be convinced of the value of the potential partnership. That's why this strategy can also serve as a general guideline for an industry giant in negotiating a successful partnership with a small newcomer.

Notes

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