And the winner is – acquired.
Entrepreneurship as a contest yielding radical innovations

Abstract:
New entrants to a market tend to be superior to incumbents in originating radical innovations. We provide a new explanation for this phenomenon, based on markets for technology. It applies in industries where successful entrepreneurial firms, or their technologies, are acquired by incumbents that then commercialize the innovation. To this end we analyze an innovation game between one incumbent and a large number of entrants. In the first stage, firms compete to develop innovations of high quality. They do so by choosing, at equal cost, the success probability of their R&D; approach, where a lower probability accompanies higher value in case of success—that is, a more radical innovation. In the second stage, successful entrants bid to be acquired by the incumbent. We assume that entrants cannot survive on their own, so being acquired amounts to a prize in a contest. We identify an equilibrium in which the incumbent performs the least radical project. Entrants pick pairwise different projects; the bigger the number of entrants, the more radical the most radical project. Generally, entrants tend to choose more radical R&D;
approaches and generate the highest value innovation in case of success. We illustrate our theoretical findings by a qualitative empirical study of the Electronic Design Automation industry, and derive implications for research and management.

Stichworte: Radical innovation; Entrant; Incumbent; Acquisition; Markets for technology; Game theory

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