

Organisational capital, exploration and exploitation: Econometric evidence for UK services firms Research Paper 65

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Across all sectors, firms face escalating pressure to serve their customers better by innovating in the delivery of goods and services. Successful innovation requires effective exploration and exploitation, however, each requires different resources and capabilities. For example, technical or creative staff may play a key role in the exploratory stage of an innovation project, but marketing staff are likely to be more important in exploitation. Organisational practices may also be specific to different innovation activities.

Here, we draw on new survey data for five UK service sectors which separately identifies firms' exploratory and exploitative activities, to identify those organisational practices which are associated with effective exploration and effective exploitation. Strong contrasts emerge, with more 'organic' practices associated with exploration and more 'mechanistic' practices better supporting exploration.

Key findings

Based on survey data from around 900 professional services firms in the UK we find clear evidence that different types of organisational practices are associated with exploration (organic) and exploitation (mechanistic) innovation activities. More specifically:

- The adoption of organic Culture & Leadership practices (e.g. work variety, culture and leadership open to new ideas) is strongly associated with successful exploration but has no detrimental effect on firms' exploitation activities.
- More mechanistic Strategy & Information practices (e.g. formal communication processes, ISO 9000, written innovation strategy) are strongly associated with exploitation success, but again are associated with no detrimental effect on firms' exploration activities.

We also find a strong association between exploration outcomes and exploitation success, reflecting the complementary relationship between the two activities.

Exploration, exploitation and innovation

March (1991) explains: 'Exploration includes things captured by terms such as search, variation, risk taking, experimentation, play, flexibility, discovery, innovation. Exploitation includes such things as refinement, choice, production, efficiency, selection, implementation, execution' (March 1991, p.71). The strategic and managerial challenge for innovating organisations is then to balance the short-term benefits of exploitation with the longer-term gains from exploration (see Figure 1).

Authors



Stephen Roper

Warwick University
stephen.roper@wbs.ac.uk



Jane Bourke

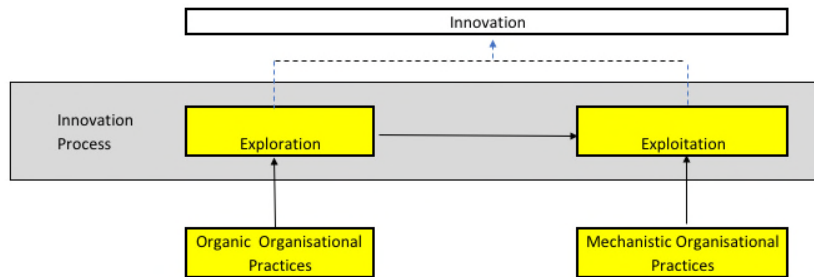
University College Cork
Jane.Bourke@ucc.ie



James H Love

Leeds University Business
School
j.h.love@leeds.ac.uk

Figure 1: From organisational practices to innovation



The lack of any trade-off between the organisational practices enabling exploration and exploitation may be linked to the focus of our analysis on services firms. In manufacturing exploration and exploitation may be more distinct activities involving very different investment priorities, external relationships and occupational groups within the firm. In services, where innovation may be less capital intensive, less technologically oriented, and more strongly linked to human interaction and creativity, the functional distinction between exploration and exploitation activities may be less marked.

Policy and practice implications

Our analysis has clear managerial implications for services firms seeking to innovate effectively. Where firms' business model dictates a focus on a single innovation activity, e.g. ideation, commercialisation, our analysis suggests the adoption of *either* an organic set of organisational practices associated with Culture & Leadership or a broader mechanistic set of organisational practices reflecting information sharing.

Currently, among our survey respondents, while around nine-tenths reported having a culture and leadership team which supports the introduction of new ideas, only around half have implemented structured processes or incentives to support the development of new ideas and information. There is clearly scope for policy intervention to encourage more widespread adoption of such practices and drive more effective exploration and exploitation.

Full paper link:

<https://www.enterpriseresearch.ac.uk/our-work/publications/>