Strategic Technology Institute

From the Archives –

Strategic Alliance Framework & Best Practices

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Approach:

Our first step in discussing strategic alliance frameworks has been to review literature on the subject in various business publications and management journals. The literature covered ranged from very general commentary on alliances (*Business Week* articles) to detailed mathematical approaches to selecting a partner or selecting an alliance tool (*Managerial and Decision Economics* publications). Though the initial focus of our efforts was to focus on selection criteria and processes, commentary on managing the alliances was more plentiful than descriptions of partner selection techniques. We were able to summarize the written perspectives in four major areas, around which this document is structured:

1) Definition and scope of strategic alliances, including reasons for alliances,
2) Company / environmental conditions for alliances
3) Selection criteria and questions
4) Management of alliances

1) Definition and scope of "strategic alliances:"

In its broadest interpretation, "strategic alliance" implies an association between two or more partners designed to achieve the objectives of the partners. In varying ways, the definition was made more specific in the literature. These definitions to varying degrees include the alliance structure, its objectives, and *timelines*, as highlighted below.

. Proactive steps to minimize the reliance on a firm's internalcapabilities to achieve sustained competitiveness and expansion.

. Joining of forces and resources *for a specified or indefinite period of* time to achieve a common objective.

. Management of an agreement between parties to work jointly on a project(s) that is designed to achieve a strategic objective (which can be offensive or defensive in nature)

. Long-term commitment between two or more organizations for the purpose of achieving specific business objectives by maximizing the effectiveness of each participant's resources.

. Kyosei, an approach, implying mutually rewarding coexistence

Implications of the term "strategic"

As implied by the definitions above, the term "strategic" is interpreted to have several implications.
First, "strategic" is built on a vision of the environment in the future, as it is:
based on a vision of the future resulting from anticipation, forecasts, or scenarios.
based on consideration of factors in the firm's external environment

"Strategic" is also defined in terms of the outcome of the alliance, meaning:
resulting in a significant shift in the business outcomes
. having an impact on more than one function or business
. resulting in a long-term relationship (otherwise the effort is not justified).

Popularity of and trends in usage of "alliances"

The literature consistently indicates that "alliances" or "partnering," however defined, are growing in popularity, and that we are now past the days when a company's business was defined only by what it owns and directly manages. A few statistics from the Ernst &Young *Electronic Business survey* (3/92) and the *Research Policy* article by Hagerdoorn and Schakenraad (5/91) indicate the popularity of the terms:

. 85% of all CEO's are involved in alliances .42% of all worldwide alliances are in IT
. Software companies rely on alliances the most
. 64% of electronics companies partner with foreign companies .45% of computer companies partner with a competitor

Forms of alliances

Alliances or partnerships are described in many forms, and, though not discussed in detail here, a follow-on project is to evaluate the set of alliance tools available, and decision criteria between these tools. The literature gives us some brief but not comprehensive views of the parameters and process for choosing the correct alliance structure.

Probably the simplest form of alliance is a direct supplier contract, and we are cautioned against the complexity of more complex arrangements unless they are merited by the situation or benefits. The range of possibilities includes:

. Long-term supplier contract.
Joint marketing agreement
. License/franchise
. Joint development agreement
. Non-equity cooperative venture. Joint venture
. Equity investment/ merger / acquisition

Objectives of alliances

Alliances are driven by many possible objectives; based on the perspectives of various authors describing alliances in different industries, industry dynamics seem to influence the objectives. We will need to apply a critical perspective to the various objectives given for alliances, which include:

a) Defensive
. Partner to ward off common enemies
. Reduce the differentiation advantages of competitors

b) Offensive / optimization
. Vendor / supplier relationship for cost or scale efficiencies
. Share responsibilities equally or in relation to relative strengths. Share information or skills

c) Cost-sharing
. Share costs of R&D when certain technology investments are too capital-intensive for one firm alone
. Partner to achieve certain goals when limited cash (internally or via public markets) does not allow acquisitions
. Some projects are too large for anyone organization to manage (ex: aerospace)

d) Expand beyond current business
. Get around internal barriers to development -resistance, resources, and risk
. Grow markets and/or enter new markets (distribution alliances / market entry strategies, for example)

Operational Definition of a "Strategic Alliance"

Given the above summary and range of opinions on alliances, what would be a goodoperational definition of a strategic alliance? Also, given the effort involved in arranging strategic alliances, a strategic alliance should be significant enough to have an impact on the following:"
. core competencies
. product/ technology positioning
. revenue stream
. market share
. relationship with customers and suppliers for the long-term

In order to justify the setup costs, the alliance would be longer-term than the life-cycle of anyone product; therefore the alliance should have a long-term impact on the "value chain." A strategic alliance for could involve a conscious decision to forego developing a required capability. Such an alliance could involve a conscious decision to collaborate with a direct competitor. (And might even involve a licensing of a core technology?)

To the extent that our core competencies and critical success factors cut across the entire organization, a strategic alliance would cut across : multiple organizations, multiple products and technologies., multiple geographies and channels, and may involve partnership with a global partner .

In managing alliances, the literature strongly suggests that the alliance be supported at multiple levels of the organization, including top management. A strategic alliance would require corporate-level coordination, internally and externally, and mayor may not involve a financial commitment. Note that several forms of alliances require financial commitment (acquisition, joint venture, minority equity stake, loan etc.) --a robust alliance program should have a full set of tools at its disposal.

General Industry Insights on the Alliance Process

The literature provides some interesting reference points and "quotable" statements on selection of an alliance, as well as the ongoing management of the alliance and the partnership spirit.

On selection of the alliance:

. Strike an alliance at the core of the company's interests to maintain top management and line interest, but, control of a firm's core activities is never shared. The firm must protect its core strengths, those hard-to-duplicate abilities that bring unique value to customers and sustain the enterprise. Careful attention must be paid to how certain of the company's strengths may be leaked unnoticed to its partner.

On management of the alliance:

. Agreements should be thorough, but also flexible. It is much more important for managers to work according to the spirit of the alliance, not the letter of the agreement. (It is interesting to note that this is very much in the spirit of Japanese negotiating skills .)

. When a partnership works, the only losers are the lawyers.

On the partnership spirit:

. Successful partnerships are those that replace "we vs. them" with "us against a common enemy," or, more broadly, with "in our respective interests "

. Partnerships cannot succeed when one party tries to gain the upper hand.
. Alliances must be viewed as "win-win", not "win-lose" situations.

2. Company / Environmental Conditions for Alliances (company attitude and readiness}

The literature on alliance management provides a number of descriptions and examples of company attitudes and approaches that are necessary for successful management of alliances.

Since alliances must be supported at multiple levels within the partners, there must be agreement within the organization regarding core competencies, core strategy, and critical success factors. Line organization objectives must be aligned with corporate objectives. Alliances must be seen as allowing the firm to concentrate on its core strengths (this is specifically a cost reduction argument).

Attitudes and conditions that must be present at the outset of the alliance include:

. Senior management must be personally committed to any alliance and to open communication with their counterparts.

. Senior managers at all participating companies must have a shared vision of how the partnership will function and understanding of how the partnership benefits each company.

. Internal reward structures must not inhibit a partnering attitude. Attitudes that must be fostered

during the alliance include the following:

. Employees are focused on the success of the enterprise in addition to personal gain.

Line managers need to see their interests in the alliance and they need to be committed to it. *Implication: Internal reward structures must be set appropriately.*

. R&D managers are judged on their ability to get the right products to market quickly, not to develop them internally unless that is required. Implication: Performance reviews should stress effective use of both internal and external resources.

. All levels in the organization are open to a partnering attitude.

3) Selection Criteria and Questions

A primary concern is the decision process for entering the strategic alliance and selection of a partner. The literature offers us some insights into some decision criteria for entering into alliances.

Objectives:

As mentioned earlier, rationale for partnering can include the following:

. To learn or enhance core competencies from competitors or other industry leaders. Partnering is a " chance to rent someone else's competitiveness, not a solution to long-term decline". (offensive / optimization)

. To acquire new skills (expansion)

. To reduce the cost and risk of market entry, for example, using agreements to learn the customer / market requirements of a new market, or distributor arrangements to enter international markets (expansion / optimization)

. To maintain or gain competitiveness quickly with minimum effort; (expansion) for example, partnering to provide a low-cost route for new competitors to gain technology and market access (cost-sharing):
-outsourcing arrangements to meet manufacturing demand or lower costs of development (expansion)
-developing strategic JIT supplier and distributor arrangements, reducing time to market and improving quality (optimization)

. To integrate horizontally to spread the cost 0f "pre-competitive" basic research, which would be duplicated and can be shared with competitors (cost-sharing)

. To integrate vertically to take advantage 0f cost efficiencies in supply and distribution chains (offensive / optimization)

. To partner against a stronger competitor to counter market domination (defensive)

. To assess competitor strengths, and learn how they will react to your moves (offensive / optimization)

. To disarm competitors (0ffensive)

. To adapt to local government regulations and provide || good citizenship"

Evaluation of the partnering relationship

A partnering relationship must be compared against the alternative of internal development. Elements for comparing partnering with internal development include costs, benefits, risks, speed of execution, among others.

If an alliance strategy is chosen, it is critical to think through the relationship from beginning to end, including the exit, if possible.

Tie to corporate goals: At the outset, the alliance must be linked to the achievement of corporate objectives and strengthening of core competencies.

The literature provides few frameworks for this process; one that was discussed is the Analytic Hierarchy Process, which can be used to align divisional and corporate objectives and choose alliance candidates based on fit. Though fairly technical, the principles developed in the discussion can potentially be applied to most situations in some modified form.

Fit with financial objectives: Financial objectives must be evaluated, and affect the decision on the type of funding vehicle desired, if any. The financial structure should maintain the independence that was the key to attractiveness in the first place.

Consider the exit path: The partnering company should emerge from the alliance more competitive than when it was entered. In setting up the partnership, the partnering company should look for ways to outpace the competition (and the partner, if it is a competitor) in building new sources of competitive advantage. To sustain the benefit of the partnership, the company must enhance internal skills and core competencies that spawn new generations of products and services. The key is to avoid DEPENDENCE; work to become more self-sufficient. Unless restricted, exploit the partner's organization, skills, and competencies. Protect what should be protected in your own organization. Clearly identify a technology transfer receptor team.
IF there is a conscious decision to transfer a core competence, consider the consequences of surrendering control on this, and plan to replenish core competencies, otherwise the organization becomes "hollow.'

Form of the alliance/partnership and dependence on industry/product status

Alliances have different objectives based on the position in the lifecycle of the technology:

Objectives needed
Development
Technology and product components
Growth
Market access
Shakeout
Cost/process efficiency

The examples given in the literature demonstrate how the objectives and environment support different rationales for partnering and different types 0f partners. Biotechnology is driven by a technology push and rapid shifts in technology leadership. Banking alliances are driven by consolidation (retail branches) and cost reduction (sharing the costs of new systems). Some automotive partnerships are driven by localization requirements (trade, safety, emissions, driving style, local road and speed conditions). We can use direction statements and business plan guidelines, in conjunction with an assessment of competitive dynamics to help us in determining the major factors to consider in setting our objectives.

Evaluation / negotiation process with the partner

If we assume the decision on the partnering structure has been made, then given a set 0£ objectives, how do we evaluate the pool of partners? As in most negotiation situations, alternative approaches should be pursued; preliminary discussions should be started with a few potential partners before settling on one.

Since the relationship will grow and change as conditions change, a partnership relies on a great deal of trust of the partner team. Compatible chemistry and culture are critical to alliance success, and should be assessed in the due diligence process on the partner.

As part of the alliance, each member of the alliance must understand each other's business, and each must understand what the other partner really desires from the alliance. Each should anticipate areas of potential conflict and be prepared for hidden agendas.

Alliance structure and approach

If the alliance is structured to allow each partner access to the other's market, technology, or capacity, the extent of exposure of each of these areas should be carefully considered and limited. The more closely a relationship is tied to a core competency, the more tightly controlled should be the relationship structure.

What specific projects should be undertaken and on what basis? A relationship can start small and build as trust builds. In the agreement itself, specific performance requirements should be established as a condition of entry into new phases of the agreement. The partners can gradually move forward in the development of markets, technologies, or products.

What are the success criteria? They will be tied to the objectives of the alliance -for example, did it bring about a more efficient deployment of capital, technology, or people? Other objectives? Given the need for top management involvement and attention, it is important that there be a great deal at stake.

Again, the exit path should be considered. Before the partnership is established, the lifetime of the partnership should be assessed, and
dependence should be avoided, especially if it blocks long-term investments in needed skills and capabilities.

4.) Management of Alliances

The literature provides a great deal of fairly consistent advice regarding the way in which the relationship is managed, which we will summarize here.

Whether alliances are managed by committee, one of the partners, or external managers, the objective should be to create an effective leadership structure agreed to by all parties. This cannot be a purely "top-down" structure. It is important that all levels of the organization have consistent goals, yet also have enough autonomy to resolve issues between the companies without a senior management approval at every step. Units “close to the action” who are in the best position to evaluate, understand, and respond must make many of the decisions. Both parties must continue to appreciate each party's objectives and expectations.

Proposals must be evaluated with an understanding that there are two or more parties' sets of goals that they must satisfy . Do they benefit both parties' markets / technologies and do they offer the potential to open new markets for both parties?

Relationship management

Continuity is extremely important in ongoing relationship management. Flexibility and patience are key. New parties to the alliance must accept their predecessor' commitments.

Personal relationships are critical to alliances, since they are driven by agreement on philosophy and overall goals, but operational procedures will continue to evolve and the personalities at various organizational levels in the partners must work together to deal with the day-to-day issues. Some pointers for maintaining the "personal" approach are:

. Hold regular top management status meetings

. Establish milestones to show progress and reenergize internal teams.

Deal face-to-face.

Meet informally

. Maintain close relationships at more than one level to ensure overlap and to secure long-term commitments.

. As in most management situations, avoid surprises

. Accommodate cultural differences (national, stylistic, industry, decision processes)

Even with a high level of cooperation, it has limits. As mentioned earlier, it is important to guard against unwanted information transfer, especially around the company's core competencies. The partner's opportunity to learn can be circumscribed by:

. inform employees at all levels what skills and technologies are off- limits to partners

. limit the scope of the agreement

. monitor information flows to the partners. Transfer is greatest when the information is easily transported (engineering drawings, floppies, a few experts), easily interpreted (common base of knowledge), easily absorbed, and skills are independent of cultural context.

. isolate joint operations from regular operations. If learning is important, locate the joint effort's facilities near the competitor's facilities.

5. Alliance Experts

The literature pointed repeatedly to certain companies and personalities in the field with extensive experience or extensive study of partnering. Corning was mentioned as a company built on an alliance philosophy, and IBM was mentioned as having over 400 alliances. General Electric has been extremely active in acquisition and divestiture activity in the 1980s. Pharmaceutical firms such as Eli Lilly and Merck are also mentioned. Other companies, even young companies such as Genentech have formalized venture and corporate development programs and technology "shopping lists". Joel Bleeke and David Ernst of McKinsey were mentioned as authors in this area, as well as Collins and Doorley of Deloitte-Touche.

Summary

The literature has given us a "first pass" look at the many ways in which partnerships are viewed. We have seen that the definitions vary in scope, but there are common impressions of the approaches needed in the management of the alliances. The objectives of alliances can vary widely, and the thrust of an alliance strategy for a particular firm is often focused by its industry / environmental situation. Managers need to review these with a critical and analytical eye to come up with a structured set of objectives for alliances for their respective companies.

Though documentation on frameworks for evaluating alliance partners is scarce, there are some tools, or at least general principles behind those tools, that we can attempt to apply for evaluating alliance partners in your corporatecontext.

We have seen that attitudinal aspects are critical to the success of not only the management of the alliance, but also to the selection process. This may be the greatest challenge in instituting an alliance process once it is generated. As mentioned in the case of General Electric: Cooperation helps or hurts depending on how a firm learns compared with its partners; the outward- looking, participative, learning organization will be open to alliances.

Blake White is the Founder & President of the Strategic Technology Institute, a San Francisco Bay Area network of management consultants and futurists. STI provides technology assessment consulting, corporate development services, and online publishing with a focus on the business and societal implications of emerging technologies. He is also the publisher of **Quantum Leap**, *the journal and newsletter of the Strategic Technology Institute and is the author of* ***The Technology Assessment Process: A Strategic Framework for Managing Technical Innovation***, published *by Greenwood Press.*