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Alliances
The secrets of successful co-operation

Professor Benjamin Gomes-Casseres

Alliances between companies have become crucial to business success, particularly in high-tech industries. But, as leading alliance expert Professor Benjamin Gomes-Casseres argues, too much emphasis is still placed on the deal itself rather than the underlying strategy.

Your company may have a strategic alliance or two, but does it have a coherent 'alliance strategy'? The two terms are not the same, and the difference is more than semantic - an alliance without a clear strategy behind it is doomed to fail. Take the tale of vehicle manufacturers Mitsubishi and Daimler-Benz, who in 1988 launched their strategic alliance with much fanfare. The leaders of the companies signed a deal in principle to collaborate in various areas, but no concrete projects followed. The alliance was stillborn. Recently the same two companies struck another major deal, and time will tell if lessons have been learned.

Too often alliances fail to deliver real benefits to the partners. Indeed research suggests that between 30 percent and 40 percent of alliances fail to meet the partners' expectations. Different analysts have different opinions on why alliances fail, blaming everything from a clash of cultures or egos, to business conflicts and ruthless competition. Yet most failures share one common factor: the creation of the alliance is seen as an end in itself rather than a means toward a strategic goal.

The lesson is clear. It is the strategy behind the deal that matters, not the deal itself. Companies that heed this lesson are more successful in their alliances than those that ignore it. Computer chip manufacturer Intel used a portfolio of alliances to test both the technology and the market. Its first generation of X86 microprocessors were licensed to several allies, while later generations were licensed to progressively fewer firms. Today, Intel is the sole producer of its high-end chips. The X86 alliances were simply tools, or steps on the ladder - the real goal was creating the microprocessor standard and dominating the field.

How to maximize success

Experience has shown that four key elements must be in place for a company to have a coherent alliance strategy:

- An underlying business policy shaping the logic of individual alliances
- A dynamic view guiding the evolution of each alliance
- A portfolio approach enabling coordination among alliances
- An internal infrastructure striving to maximize the value of external collaboration.

Taken together, these will determine whether a firm is successful in alliances. Managed well, alliances can create tremendous value. Managed poorly, they can be very costly distractions.

The underlying business strategy

Most managers would agree that an alliance must be backed by a business strategy that dictates why this partner and structure are better than the alternatives, what the firm expects to get out of the partnership, and so on. Yet, time and again, firms enter into alliances without a clear sense of their underlying strategy. Why? The reason lies partly in

the tendency of the deal's champions and negotiators to see the alliance itself as a goal. Often, the opportunity for an alliance arises suddenly - prompted by an inquiry, a competitor's move, or an executive's conversations with a counterpart. Before you know it, you are 'doing the deal,' rather than determining whether you need a deal, and, if so, what kind of deal you need.

Alliance goals vary by business strategy. A 'supply alliance' takes advantage of economies of scale and specialization by having one partner supply the other with products or services; a 'positioning alliance' helps partners enter new markets or expand existing markets; a 'learning alliance' develops new technologies through collaborative research or transfer skills between partners. Many alliances exhibit combinations of these goals.

FACTS AND FIGURES

- An alliance is an open-ended arrangement governing co-operation between two or more companies. It can come in many forms - from a technology licensing arrangement to a production joint venture
- Every major company, especially in high-tech fields, has alliances that are key to its strategy and performance. Almost all companies have increased their use of alliances in the last few years
- In healthcare, the most common drivers of alliance formation are the rising costs of R&D and new biotechnology, and the increasing integration of health services
- Over half of all alliances are dissolved within three to five years. This does not necessarily mean these alliances 'failed' - they may have been intended to be transitional or were followed by other alliances between the same partners

Success, not survival

Alliances are always open-ended and ever-changing. If all the terms of an exchange between two firms can be completely specified and agreed upon at the outset, they need not form an alliance - a simple vendor contract would do. Because in every alliance the initial agreement is in some sense incomplete, success will depend on the governance of future joint decisions. So, the ongoing relationship between the firms is critical.

The tendency of alliances to change over time is often misinterpreted as a weakness. Managers complain about the high 'divorce rate' in alliances, and academics conduct statistical studies of the 'instability' of these structures. This misses the point - the goal should not be the survival of the alliance, but the success of the alliance strategy.

Sometimes, the strategy will call for using alliances as transitory mechanisms on the way to a full acquisition or divestment. At other times, particularly when market or technological uncertainty is high, the strategy may involve launching several alliances at the same time, and determining over time which ones are worthy of further investment and which ones should be terminated. The flexibility - and instability - of alliances is often their strength, not their weakness.

The early history of the personal digital assistant (PDA) industry offers a fine illustration of the dynamic nature of alliances. In the early 1990s, leading firms in computers and telecommunications formed alliances to develop and market these handheld devices. By 1994, several 'constellations' of firms had launched products: Apple's Newton, AT&T's EO, and Hewlett-Packard's LX series. Six years later, few of these PDAs are still on the market and few of the alliances are still in force - but this does not mean that they 'failed'.

The business was inherently uncertain and many of the products were bound to fail, whether created by alliances or by single firms. The alliances simply allowed firms to conduct market experiments quickly and at relatively low cost. This was their underlying strategy and the dynamic logic behind their use of alliances.

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Portfolio management

Cultivating and coordinating a portfolio of partners is especially important for firms in industries driven by innovation. Healthcare companies, for example, are increasingly using multiple external alliances to complement internal research and development. They may invest in several small biotechnology firms and fund several university laboratories, all while also conducting internal R&D. Because the chance of success of any single project is relatively low and unpredictable, the portfolio allows a company to place multiple bets and hope for a jackpot somewhere.

But the challenge of managing a portfolio is substantial. A poorly designed, mismanaged network can entangle a firm and waste scarce managerial resources. Good coordination, on the other hand, can save resources and diversify options for growth. Many firms are experimenting with procedures for portfolio management. None stands out yet as a definite benchmark, but pharmaceutical firm Eli Lilly has developed an impressive system. Its Office of Alliance Management (OAM) has formalized the entire process, from identification of candidates through to management and evaluation, and provides alliance training for managers new to the field. This should lead to the company having a higher proportion of successful alliances, compared with firms adopting a more informal approach.

Strategy begins at home

All too often, alliances are seen by some as peripheral to a company's core operations and not deserving of the resources granted to internal projects. This syndrome is particularly common in foreign-market joint ventures. For example, some US companies have rushed to form joint ventures in China, only to starve them of resources later because they did not fit into the firms' standard ways of doing business. A good alliance strategy starts at home. You must align your organization and invest resources to support your strategy, or else it will fail. This means making alliances part of the everyday functioning of the company – not special deals relegated to a group of experts.

SUCCESSFUL ALLIANCES
Prof. Benjamin Gomes-Casseres's personal favorites

- Xerox & Fuji Film (1962-present): the most successful US-Japanese joint venture on record started as a simple market-entry venture, but has grown to become essential to Xerox' global strategy, providing technology, manufacturing capability, and new ideas
- Siemens & Corning (1973-1999): their 50/50 joint venture combined Corning Glass's optical waveguide technology with Siemens's cabling expertise to become the most successful producer of optical fibers for telecommunications. Corning's purchase of Siemens's share in 1999 was not a sign of failure, but a move to bring this success 'in house'
- Microsoft & Intel (1981-present): an alliance that reshaped the micro-computer industry by establishing a dominant standard for hardware and software
- Northwest & KLM (1989-present): the oldest and arguably the most successful of the cross-Atlantic airline alliances. It combines the complementary route structures of the two airlines into a seamless and co-branded global service

Crafting your alliance strategy

It should now be clear that an alliance strategy is so much more than a strategic alliance, in that it creates the very context for successful partnerships. The success of any given alliance typically depends on 10 key factors (see box at end).

But a successful alliance strategy requires much more. You need to establish an internal culture that views alliances as simply another business option, not as a panacea; they have risks and rewards, and they will work for some things but not for others. Effective management of alliances also relies on the ability to cope

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with change. Do for your alliances what you would do for any other aspect of business - recognize that change demands flexibility. If the market changes, would your production schedule not change? The same for alliances. It is unlikely that a company will get everything it wants out of an alliance, but it can also obtain much that it did not expect. The secret is to grab opportunities for change, not ignore them.

With such elements in place, the number of deals in which your company is engaged can be expected to grow and will need to be managed. This means prioritizing alliances and creating an organizational hierarchy responsible for optimizing the portfolio. This will call for making trade-offs among partners or even among the goals of different business units. Remember that ad hoc growth of your alliance portfolio is costly to your alliance strategy.

As your alliances grow in numbers, the importance of a supportive internal infrastructure will also become evident. Suddenly, tending to alliances will begin to place substantial demands on scarce resources. When the organization is taxed, it will either resist change or find new ways to accommodate and support the alliance strategy. Only the latter route offers a hope of success.

The companies of today and tomorrow will not survive if they try to do everything themselves, nor will they be saved by a strategic alliance here or there. But having a real alliance strategy will at the very least give them a strong fighting chance.

10 STEPS TO A SUCCESSFUL ALLIANCE

1. Have a clear strategic purpose - alliances are never an end in themselves, they are tools in service of a business strategy
2. Find a fitting partner - a partner with compatible goals and complementary capabilities
3. Specialize - allocate tasks and responsibilities in the alliances in a way that enables each party to do what they do best
4. Create incentives for cooperation - working together never happens automatically, particularly when partners were formerly rivals
5. Minimize conflicts between partners - the scope of the alliance and of partners' roles should avoid pitting one against the other in the market
6. Share information – continual communication develops trust and keeps joint projects on target
7. Exchange personnel - regardless of the form of the alliance, personal contact and site visits are essential for maintaining communication and trust
8. Operate with long time-horizons - mutual forbearance in solving short-run conflicts is enhanced by the expectation of long-term gains
9. Develop multiple joint projects - successful cooperation on one project can help partners weather the storm in less successful joint projects
10. Be flexible - alliances are open-ended and dynamic relationships that need to evolve in pace with their environment and in pursuit of new opportunities

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