

The Corporation is Dead. Long Live the Constellation.

By Benjamin Gomes-Casseres

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LAST YEAR, Cable & Wireless ran a series of glossy advertisements proclaiming that, "The firm is dead. Long live the federation." Great slogan. Too bad the sloganeer is in the process of getting splayed by the marketplace for never having figured out how to operate an alliance constellation. The lesson of Cable & Wireless is not that firms should abandon the idea of competing in groups, thereby dismissing the whole concept as faddish, freakish, or just too complex for the workings of a simple human head. That would be reactive and wrong. A better answer is that design matters. And that it is here, on the drafter's easel, where one will find sources of future comparative advantage.

Many have tried their hand at alliance constellation design. Delta Air Lines, for instance, is designing a constellation of more than a dozen global partners around a small core of cross-equity investments. Oracle has no such attachment to direct investments. To create momentum for its new network computer—and thus displace the constellation around the personal computer—Oracle is racing to line up as many supporters as it can. At last count, more than fifty firms, including computer makers, software developers, and telecoms, have lent their support, but not equity, to the firm. AT&T, on the other hand, has grown concerned that building size for its own sake is dangerous to its global telecom constellation, WorldPartners. Rather than bring in more partners, it is choosing to deepen the communication and web of commitments among the existing members (Exhibit 1).

The design choices are mind-boggling. This is partly because decisions are shaped by industry environments, firm goals, and firm capabilities, all of which exhibit high degrees of variation. Competing in constellations is also a new

style of strategy—and the pioneers are still experimenting. Like it or not, group versus group competition is here to stay, and firms need to understand the dynamics of constellation design. Early evidence suggests that design revolves around four broad choices:

- Size
- Composition
- Internal competition
- Collective governance

And it is here where designers should focus their creative juices.

Size

The total market reach of the group will have a bearing on the success of the group. This is particularly true on two occasions: when seeking a standard or economies of scale.

But choosing an appropriate definition of size is tricky—and will turn on the precise strategy of the constellation. When trying to establish a standard, for instance, the sheer number or the total marketshare of the partners is the best way to measure size. When shooting for scale advantages, however, total production capacity of the group or average production capacity per member may be better to aim at.

Cable & Wireless missed this distinction. The firm's strategy in designing its global telecommunications constellation was to assemble as many partners from as many countries as possible. Yet neither of these mattered much to global customers, except perhaps its stake in Hongkong Telecom. Concert, the joint venture between British Telecom and MCI, was an instant market leader with just two partners. MCI and BT understood that in this arena—providing voice, video, and data services to multinational corporations—competitive advantage

hinged on the size and reputation of the lead firms, as well as the nimbleness of the alliance itself.

Composition

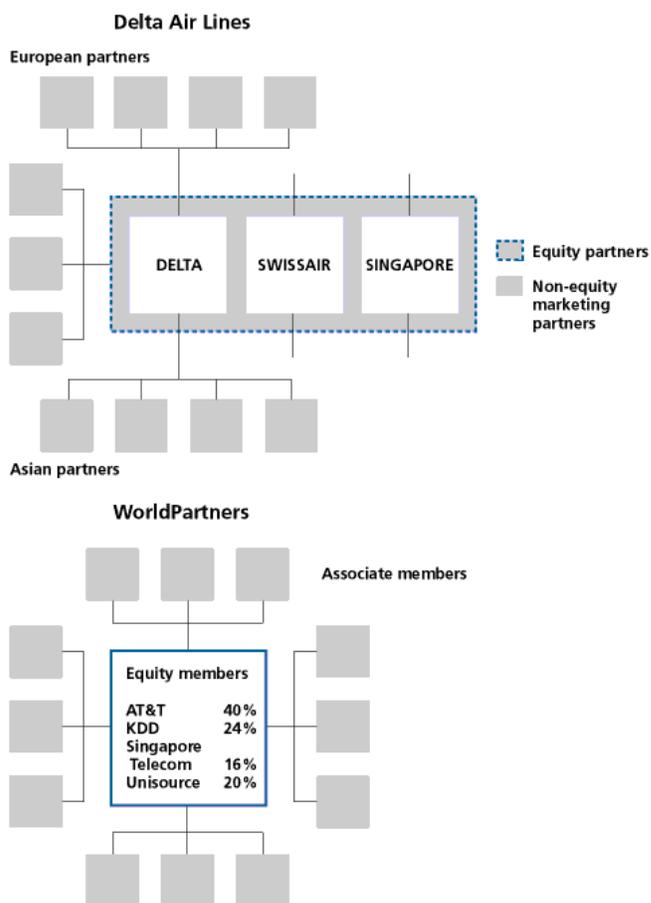
At times, advantage comes from the ability to assemble a diverse set of capabilities. What matters is not the size of the pieces but, rather, that the right pieces are assembled snugly together.

Composition has been a key to designing constellations in the market for personal digital assistants, the little hand-held device which promised the computing power of a simple PC, the communications capability of a cellular phone, and the size, styling, and durability of consumer electronics. One manufacturer's ad idealized the product: a relaxed businessman, lounging on a Caribbean beach, receives a fax from one office, sends a reply to another, and then returns to his favorite computer game.

To compete in this environment, firms had to deal with the convergence of at least four industries—computer hardware, computer software, telecommunications, and consumer electronics. Major companies in each of these industries entered the field, each arriving with particular strengths. IBM, Apple, and Hewlett-Packard approached the business from their experience in computer hardware; Microsoft and Lotus, from computer software; AT&T, Motorola, and BellSouth, from telecommunications; and Sharp, Casio, Tandy, and Amstrad, from consumer electronics. They each assembled firms into constellations which gave them access to the technical capabilities they lacked.

Constellations can also demand geographic diversity. Consider the case of Asia Link, a constellation in the Asian advertising business. Asia Link is composed of firms with very similar sets of capabilities: each has a diverse range of industry experience, \$10-\$80 million in annual revenue, and a staff of 50-100

Design choices—two samples among the infinite variations



professionals. Yet in terms of geographies, the members are intentionally distinct. Each is the leading local firm in one of eleven national markets stretching from Japan to India. By designing for such geographic diversity, the constellation believes it can defend itself against such encroaching global giants as Ogilvy & Mather and Saatchi & Saatchi.

Internal competition

Asia Link is also designed to restrict competition among member firms. Each member is the constellation's only representative in a given national market. One member will make a referral across boundaries, receiving a royalty fee while continuing to retain that portion of the business left back home. This is not dissimilar to the practice of Japanese keiretsu, where an "exclusion rule" says

there should be no duplication of activities among members.

But is exclusion always best? Rarely. Some internal rivalry is, after all, likely to encourage innovation, increase flexibility, and provide a security of supply. And given that member firms remain separate entities, internal competition is inevitable at some level. Therefore, virtually all constellations contain elements of both conflict and collaboration.

The microprocessor industry offers an interesting case. By the early 1990s, four constellations had appeared to challenge the preeminence of Intel. The groups were led by HP, IBM, Sun, and Mips, and each was betting that Intel could be challenged by group momentum and a more advanced processing technology, called RISC. That similar group goal, however, did not lead to similar choices about competition. HP explicitly limited it, choosing members for their unique capabilities or markets.

Sun Microsystems, on the other hand, promoted competition within its group, allowing members to clone its proprietary technology, even encouraging them to compete for the design of next generation chips. By creating clones, Sun believed it would facilitate the spread of its architecture. By pitting chip designers against one another, it would spur innovation.

Mips chose a line somewhere between HP and Sun. Mips encouraged competition, but also contained and isolated it. Its constellation was designed with rings around a core, with internal rivalry intensifying as one moved outward (Exhibit 2). That core was Mips, who vowed not to compete with its allies, and prevented any from competing with it. Mips would be the constellation's only chip designer, and nothing more. The chip manufacturers—the next ring of the constellation—would be limited to a maximum of six licensed firms.

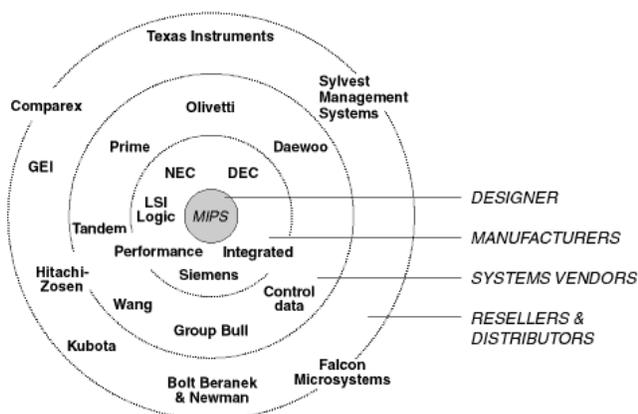
Yet even this competition was compartmentalized, since the semiconductor partners were chosen according to their geographic market strengths. According to Mips president Robert Miller, the aim was to sign on "one of the three semiconductor firms in the United States, one of the top three in Japan, and one of the top three in Europe." The final rings of the constellation were sales and marketing. Here competition flourished. Mips developed relationships with OEMs, distributors, value-added resellers, and systems integrators, and let them create and divide the market.

Which one of these three approaches worked best? While any answer is influenced by the forces external to constellation design, the Sun model appeared to have real problems. Sun benefited from having many potential chip vendors, even though it used only one for each product generation. But competition among Sun's semiconductor partners tended to benefit only Sun, not the group as a whole. Also, Sun found the competition from the clone makers too much to handle. Fearing that they would undercut its own hardware business, Sun ordered its value-added resellers to stop selling Sun clones.

Mips, in one sense, also failed. Having a small firm like Mips at the center of massive constellation created real coordination problems and led to a partial

Exhibit 2

The Mips constellation



disintegration of the group. Mips was acquired by Silicon Graphics, one of its early partners, who had grown dependent on the Mips-designed chips for its workstations.

Thus, the most effective constellations seem to create an organizational structure which promotes collaboration rather than competition. But this is not to suggest squashing all internal competition. Internal rivalry can usually be managed during sales and marketing, while it is highly problematic during research and development. Also, competition works best when it does not involve the lead firm: there is a certain clarity of purpose gained from having the leader above the fray, able to arbitrate in the best interests of the group.

Collective governance

A constellation doesn't have to have a governing body with voting rights for every member. Boeing has no such mechanism for its vast supplier network, nor does IBM for its network of software developers. However, a formal structure is useful when a constellation is large and when it has a high degree of internal competition. A forum allows partners to establish common goals and rules of behavior—something virtually impossible to do informally.

Broadly, there are three types of governance structures for alliance constellations:

- **The General Assembly.** This is the United Nations approach to member management. It is preferred when the number of partners is large, when multiple capabilities are being assembled, when there is no clear dominant firm, or when the dominant firm wants to downplay its leadership role. The first and last of these were the primary reasons behind the construction of the AT&T global alliance. WorldPartners has emerged as an intricate web of staff, committees, and meetings all of which encourage information exchange

among members. Despite these advantages, the general assembly can be slow-moving, lack an aggressive, differentiated edge, and require immense amounts of energy to manage.

- **The Equity Core.** Here, equity has the key constellation members together, and leaves the rest floating in a rather unstructured orbit. Such an approach is favored when there is a defined core group, and when these partners are similar types of firms (but not direct competitors). Delta Air Lines built an equity core for its global marketing alliance, taking small but important cross-equity stakes with its two main partners, Swissair and Singapore Airlines. These three integrate strategy at each board meeting. On the periphery, each firm maintains its own network of partners.

There are drawbacks. First, the equity core provides very little coordination among the total network membership. In other words, a Delta partner such as Virgin Atlantic has no real relationship with Singapore Airlines, much less one of Singapore's partners. Second, the equity core model may also pose real limits to growth. If entry into the center of the constellation requires an equity ante, there are simply a limited number of firms which can participate.

- **The Dominant Firm.** This is most common constellation structure, if only because it requires the least amount of conscious organization. Typically, some large firm like GM, Boeing, or IBM will stand up, lay out its direction, and invite anyone interested to trot along behind. This was the design advocated by Bank of America back in the 1960s for its BankAmericard credit card association.

The dominant firm provides the other members with some important advantages: perhaps large and guaranteed volumes, adjudication of disputes, discipline of unwieldy members. Of course, it can lead to excesses. As the members of the BankAmericard

association discovered, the lead firm can make decisions which enrich it at the expense of the others. Also, the dominant firm model simply cannot be applied in many instances. Delta simply could not dominate its global alliance the way Bank of America sought to: its size and reach are not large enough.

Whatever the formal governance structure, the collective has to have some way of coordinating actions. Without leadership or an agreed-upon formula for making joint decisions, a constellation cannot be

expected to formulate and execute a consistent strategy. Instead, internal divisions and differences in perspectives among members will most likely pull the constellation in different directions. An analogy from American Wild West is apt: out in the barren plains, cowboys would tie their horses to each other at night, knowing that each horse would pull in a different direction and the group would go nowhere. An alliance group without leadership and collective governance will be no different.

Benjamin Gomes-Casseres is the author of *The Alliance Revolution: The New Shape of Business Rivalry*, recently published by Harvard University Press. He is a professor of international business at Brandeis University, a frequent speaker and consultant to US and international companies, and a member of the Analyst's advisory board.