Strategy must lie at the heart of alliances

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Companies go into alliances for many reasons, but the results are often not what they expect. ***Benjamin Gomes-Casseres*** *explains why*

A decade ago, IBM and Apple launched a much-touted strategic alliance, including investments in joint ventures and research. Together, they would take on Intel and Microsoft. It didn't happen. Eight years later the alliance faded away, leaving unfulfilled hopes, frayed relationships and wasted effort.

Other alliances formed at high levels, often blessed with the designation "strategic", have also failed to deliver. Analysts argue over what caused each link-up to fail. Some blame egos and clashing cultures, others cite business conflicts and ruthless competition. Yet these cases often share one factor: amid the hype, the alliance came to be seen as an end in itself, rather than as a means toward a broader goal. The failures teach one clear lesson: what matters is the strategy behind the deal, not the deal itself.

For the same reason, many of today's digital alliances will fail. In many quarters, the new economy race to "get big fast" has been reinterpreted as "get hitched fast". If companies cannot gain market share and strategic dominance rapidly, the argument goes, they must find partners. For dotcom business development managers, this means: sign as many deals as you can, as soon as you can. In doing so, they forget the saying "Marry in haste, repent at leisure."

Companies that succeed with alliances put strategy first and deal-making second. For example, Sun Microsystems has leveraged its capabilities impressively through a multitude of alliances. Some alliances survived for a long time, others were short-lived; some were narrowly focused and a few broader. Sun's partners included Fujitsu, Toshiba, Oracle, Netscape/AOL and IBM. But none of these partners or individual alliances accounts for Sun's success. Rather, the way Sun integrated alliances into a coherent strategy and managed them over time allowed it to get the most from partnerships.

A coherent alliance strategy also lay behind Intel's rise. Intel made its breakthrough in the alliance with IBM to develop the PC in 1980. Plus, Intel used astute licensing to build its dominance. Its first generation of microprocessors was licensed to several allies; later generations were licensed to fewer companies; today Intel is the sole producer of its high-end processors. Intel's alliances were steps on a ladder. The real goal was creating and dominating processor standards.

Alliance strategy

So while companies announce "strategic alliances" daily, many lack "alliance strategies". The difference is more than semantic: an alliance lacking strategy is doomed. A coherent alliance strategy has four elements:

- a business strategy to shape the logic and design of alliances;
- a dynamic view to guide the management of each alliance;
- a portfolio approach to enable co-ordination among alliances;

- an internal infrastructure to maximise the value of collaboration.

At the right time and when managed well, alliances create tremendous value; at the wrong time and when managed poorly, they can be costly.

Underlying logic

In principle, most managers would agree an alliance needs to be backed by business strategy. Signing up as many partners as possible is not a strategy - worse, it can sap the company of energy.

Ideally, strategy dictates why each partner and structure is better than any option, what the company expects, how risks will be managed and how the new alliance will be co-ordinated with others. Even knowing this, companies make alliances without a clear strategy. Why?

The reason lies partly in the tendency of the deal's champions 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 a chief executive's conversations with a counterpart. Before they know it, companies are "doing the deal" rather than determining what kind of deal is best. Time to think can seem a luxury, but it is precisely because of the tendency to focus on the transaction that it is essential to examine how the alliance fits the business strategy.

Alliances have many goals, depending on the strategy.

Being clear on how the alliance fits business strategy is also important for measuring its performance. The true value of any alliance is usually not evident from the narrow costs and revenues of the collaboration, even when the alliance is a stand-alone joint venture. Because the alliance is part of a broader strategy, its effect must be measured in terms of its contribution to that strategy. Thus, we must also account for the opportunity costs of options foreclosed and for qualitative benefits the alliance brings to the company.

Take the case of Fuji Xerox. This venture between Xerox and Fuji Photo Film was created to help Xerox sell copiers in Japan. Over time, Xerox's strategy and Fuji Xerox's capabilities evolved so the venture became a supplier of products to Xerox globally and a partner in developing technologies. The joint venture was profitable, grew in size and issued modest dividends to Xerox. But its true value lay in how it helped Xerox beat back Japanese competition in the 1980s, halt its previous decline and launch initiatives worldwide. The alliance's role in corporate strategy is much bigger than the partnership itself.

A dynamic approach

The example of Fuji Xerox also shows the value of a dynamic approach to managing alliances. Just as the broader strategy is more important than the individual deal, so too the evolution of the relationship over time is more important than the initial deal.

Alliances by their very nature are open-ended and ever-changing. If all the terms between two companies can be specified and agreed at the outset, there is no need for an alliance; a contract will do. In that sense, many digital "partnerships" are not that at all, but simply agreements to exchange links and so on. A true alliance is an organisational structure that enables control over future decisions to be shared and governs continual negotiations - it is a recognition that the initial agreement is incomplete. That is why success in alliances depends so much on governance structures and on the relationship between companies, including personal relationships between managers.

This 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 their "instability". This misses the point: the goal of an alliance is not its survival, but the success of the alliance strategy. Sometimes, strategy will call for using alliances as transitory mechanisms. At other times, the strategy may involve launching several alliances at once to see which ones are worthy of further investment and which should be terminated. Such a strategy is no different from companies hedging their bets or pursuing parallel projects to develop products. The flexibility of alliances is often a strength, not a weakness.

The early history of personal digital assistants (PDAs) offers an illustration. In the early 1990s, many computer and telecommunications companies formed alliances to develop and market these hand-held devices. By 1994, Apple sold the Newton; AT&T offered the EO; and Lotus and HP made the LX series. Less than a decade later, none of these PDAs was still in the market and most of the alliances had ended. Does this signify failure? I think not. The field in which these companies were entering was uncertain and fluid. The alliances allowed participants to conduct market experiments quickly and at relatively low cost. This was their underlying strategy.

Alliance portfolios

The PDA strategies also show the value of careful design and management of a portfolio of alliances. The PDAs were produced using components from several companies and selling through many channels, so alliances could reinforce each other. Again, the effectiveness of an alliance strategy depends on a strategy that transcends the individual deal.

Some types of companies recognise the importance of a portfolio of allies. Business units that use multiple components will depend on many supply alliances and business units that sell in multiple markets will use several allies to reach different customers. Alliances among national airlines are examples of this. Similarly, a portfolio of alliances is useful when a critical mass of "sponsors" is key to market acceptance, such as in establishing software standards.

But being involved in multiple alliances is not sufficient; the company must manage the portfolio as a whole also. Two alliances of a company, with two different partners, may either complement each other or they may conflict. The same is true, in spades, of a portfolio of many alliances. A poorly designed and managed network can entangle the company and waste managers' time. Good co-ordination, on the other hand, can save resources and diversify options for growth. How are companies facing the challenges? Pharmaceutical company Eli Lilly has an office of alliance management which helps identify alliance candidates, evaluate deals and train managers new to the field. This should lead to the company having a higher proportion of successful alliances, compared with companies adopting a more informal approach.

Internal support

Eli Lilly's system is not only important for co-ordinating a portfolio of allies, but also for upgrading its ability to manage alliances. In case after case, it has become clear that the internal organisation of a company is critical to successful partnerships. Without a supportive infrastructure, every alliance will fail, no matter how ingenious the external deals.

All too often, however, alliances are seen as outside "core" operations and therefore less deserving of resources. In fact, relying on someone else to implement a piece of your strategy may require more, not less, management effort. Although companies typically choose to relegate to allies those functions they cannot do, or have no time to develop internally, forging and managing the relationship demands resources. Companies may overlook this and fail to provide the resources required for success.

A good alliance strategy therefore starts at home. The company must define a business logic for its alliances, keep an eye on the future and manage the group of partners well.

Moreover, it must align its organisation and invest resources in the strategy.

Companies that are doing this (such as Corning, Xerox, Hewlett Packard, Oracle and Sun) are frequently cited for their "alliance capability". The essence of this capability is that alliances are made part of the everyday functioning of the company. They are not special deals relegated to a group of alliance experts.

Build capability

An alliance strategy is thus more than a strategic alliance. Managers need to construct processes that root alliances in strategy and recognise that alliances will work for some things but not others. Next, they need a way to manage change. The history of alliances shows you will not get everything you wanted; but you may well get much you didn't expect. The key is to grasp change, not ignore it.

With these elements in place, the number of deals will grow and need managing. This requires prioritising among alliances and creating an organisation to optimise the portfolio. And the importance of a supportive internal infrastructure will also become evident. Suddenly, alliances will begin to place substantial demands on resources, not least the attention of senior managers.

Companies will not survive if they try to do everything themselves. But they will not be served well by a headlong rush into multiple deals. Only a real alliance strategy will give them a fighting chance.

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Further reading

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