IDEAS

STRATEGIC ALLIANCES

UNEQUAL PARTNERS

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Alliances are one way for startups to leverage their scarce resources and increase their chances of success, but many entrepreneurs lack experience in how to manage these alliances.

ENTREPRENEURSHIP • ALLIANCES • STRATEGY
HYBRID ORGANIZATIONS

The past decade has witnessed a change in how many entrepreneurs organize. Where earlier, small companies may have been likely to try to go it alone in creating a market when offering a product or service, increasingly they have turned to setting up alliances with other organizations. Many entrepreneurs are motivated to form an alliance because it may help their startup company leverage its scarce resources and increase the likelihood of economic success.

While the practice has become more widespread, the knowledge of how best to form and manage these alliances has not kept pace. Many entrepreneurs do not have any experience in managing alliances. Those that do, have likely discovered that there is no single model for when to use or how to structure an alliance.

Many firms share the conviction that you can't go it alone in today's business environment. As alliances have come to represent a substantial percentage of some firm's revenues and profits, their failure rates appear to be just as considerable. Defining what is meant by collaborative success or failure is difficult, however. Nevertheless, numerous studies have shown that between 30 and 70 percent of all alliances fail.

Alliances pose many questions and challenges for firms. When should they be used rather than alternative investments and how should they be designed and structured? How can firms navigate complex alliance processes more effectively and how can they best manage their involvement in extended networks? What are the organizational and managerial requirements of effective alliance implementation and how can partners gauge the performance of their alliances and make improvements?

Alliances are often collectively referred to as hybrid organizations, and this description is apt. They blend features of organizations and markets, cooperation and competition, flexibility and commitment, trust and formal contracts.

Alliances themselves can be seen as sources of entrepreneurial opportunities that are well defined at the outset. But they can also be seen as a means of discovering or creating completely new opportunities that are not well known prior to the formation of the collaboration. They are also one of several "modes of action" by which individuals or firms exploit the opportunities they recognize or create.

Why enter into an alliance in the first place? When entrepreneurs are asked to enumerate the reasons why their firms might take on a partner, they often list reasons such as the following: 1. to improve their chances of survival; 2. to obtain critical resources; 3. to tap into others' financial capital; 4. to create new businesses; 5. to accelerate growth in certain product markets; 6. to achieve rapid internationalization and; 7. to cope with various uncertainties.

New ventures have to overcome the "liability of newness." Often they lack relationships, or have an undeveloped set of relationships, with key stakeholders such as investors, suppliers, employees and customers. Alliances can begin to counter a firm's liability of newness by addressing the new venture's resource shortfalls by teaming up with a larger or more

ALLIANCES CAN COUNTER A NEW FIRM'S LACK OF RELATIONSHIPS BY TEAMING UP WITH A LARGER OR MORE ESTABLISHED COMPANY.

established firm. Secondly, relationships with reputable partners can have beneficial effects on the new venture's ability to secure resources from other sources as well.

Certain questions must be answered before deciding what type of alliance governance is required. The partners should consider what are the primary commercial objectives of the alliance. What are their anticipated resource contributions and what will be the alliance's product market scope and geographical scope? What are the key hazards and risks the parties face and what are their interests in the collaboration? And in what specific ways will the policies obtain financial or non-financial returns from the alliance?

Although alliances can be broadly broken down into equity and non-equity governance structures, in fact, the incentives, control rights, monitoring mechanisms, safeguards and other aspects of alliance governance can vary a great deal within each of these two categories. An equity alliance offers greater incentive alignment and control than a non-equity one, but involves greater governance costs as well. The question of whether an equity or non-equity alliance is more attractive therefore involves consideration of whether the incentive alignment control features of equity alliances are needed, such as when the firm faces a serious risk of opportunistic action.

Getting the right partner is of particular importance to alliance success. This involves a process of partner search and selection. Readily available information about potential partners is often insufficient. Determining who might be the right partner takes much time and effort from senior management due to the lack of information. When it comes to partner selection, it is necessary to make sure that the partner and the firm are compatible. Two main groups of selection criteria emerge in this respect: task- and cooperation-related. Task-related selection criteria are associated with the strategic resources and skills that a firm requires for its competitive success, while cooperation-related criteria are associated with ascertaining how partnering firms can work together effectively.

It comes down to a question of whether or not it is a good fit. Assessing the fit, be it strategic, organizational, operational or human, is an ongoing process throughout partner search, partner selection and negotiations, which entails exploration and discovery. If the company has a good knowledge of the potential partner from past relationships, the process is greatly simplified. This is why, in general, strategic and organizational fit are

KEY QUESTIONS AND CHALLENGES POSED BY ALLIANCES

- **When should you use alliances rather than alternative investments? Or avoid them?**
- **How should alliances be designed and structured? How can alliances be governed appropriately to achieve collaborative objectives?**
- **How can firms navigate complex alliance processes more effectively (e.g. partner selection, negotiations and relationship management)?**
- **How can firms best manage their involvement in extended networks?**
- **What are the organizational and managerial requirements of effective alliance implementation (e.g. capabilities, teamwork)?**
- **How can partners gauge the performance of their alliances and make improvements?**

PREPARING FOR PARTNERSHIPS

Strategic issues
- Does the firm have a clear vision and strategy?
- Does the firm understand where to form alliances, and where not to?
- Are partner selection criteria clear?
- Are potential partners being monitored?
- Are the alliance activities of rivals being benchmarked?

Organizational issues
- Does the firm have a culture of cooperation?
- Is there strong teamwork in the firm?
- Does communication flow freely?
- Is responsibility decentralized in the firm?

Managerial issues
- Are employees comfortable in situations requiring responsibility without control?
- Do employees work well with others from different cultural backgrounds?
- Do employees possess general management skills?
- Do top managers display commitment to new initiatives?

considered during partner search and selection, while most likely operational and human fit will be evaluated during negotiations as they are more difficult to assess from a distance.

When preparing to negotiate with the preferred potential partner, managers of entrepreneurial companies should keep in mind three considerations of a general nature before getting down to the details of the negotiation. The first is to keep in mind that the purpose is to use the alliance to co-create value along with the partner. Secondly, analyze both the company's needs and those of the preferred potential partner, that is, carry out a two-sided analysis. And thirdly, remember that they still have to confirm the fit with the preferred potential partner. The next step is to go ahead and sign the deal. But even then, entrepreneurs should ask themselves the killer question, "when the time arrives for my company's exit from this alliance, will the company be stronger and more powerful than when we entered?" If the answer is yes, then the time has arrived to take the pen and sign the contract.

Alliance execution is an important element of the alliance implementation challenge. Of course, the better the job that entrepreneurial managers have done selecting their partner and negotiating and designing the alliance, the better position they'll be in to address this challenge. However, sooner or later entrepreneurial managers will face one or another type of conflict. While a certain level of conflict may be healthy, it may become harmful if not properly managed. Two main avenues open up here. The first relates to setting up formal mechanisms that establish the rules of the game for decision making. The second avenue involves nurturing the right relational quality between the partners.

It is wise to periodically reassess the desirability of keeping the alliance alive in order to avoid the error of maintaining it simply out of inertia. Terminating an alliance does not mean it has failed. Alliance termination may have been planned from the beginning. Entrepreneurial managers may decide to terminate an alliance once the goals for which it was created have been achieved. In such cases, putting an end to the alliance is a sign of success.

THE END OF THE AFFAIR

Two situations may call for terminating an alliance. First, if the alliance no longer helps meet the goals for which it was created; and second, if the costs it entails surpass the benefits it yields. The first situation may arise once the firm is capable of carrying out the alliance activity on its own. The second, where costs surpass benefits, may happen when differences between the partners emerge as a relationship develops, such as incompatible goals, different philosophies and decision making, design of non-cooperative compensation systems, asymmetry in the power held by each partner and so on.

Sometimes it is not easy for the partners to agree about when and how to end a strategic alliance, particularly if the termination is due to an impasse between the partners. This is why it is highly advisable to specify the circumstances in which the alliance will be ended.

Eventually, all partnerships come to an end, whether planned or not, but planning that end may avoid major problems at the final stages and reduce the costs of termination. The more an entrepreneurial company depends on the alliance, the harder it should try to make it for the partner to leave.

MORE INFORMATION

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