Alliances: Achieving Long-Term Value And Short-Term Goals

Will Mitchell
Jack D. Sparks/Whirlpool Corporation Research Professor, Professor of Corporate Strategy and International Business, University of Michigan Business School.

Financial Times "Mastering Strategy" series, October 1999

Summary

Alliances are risky but they are a fundamental necessity of both short- and long-term strategy, says Will Mitchell. Here he urges companies to undertake a systematic approach to pre-alliance planning, to introduce effective education systems and incentives, and to develop corporate capabilities for managing alliances by setting up a dedicated alliance management unit. The author draws a distinction between contracts and contacts in successful alliances – both are important but people and the knowledge they gain are ultimately the key. Unlike good marriages alliances are not for ever and companies should be prepared to exchange partners if a better one emerges.

Alliances: achieving long-term value and short-term goals

What do the alliance strategies of a faltering electronics manufacturer in Japan, a failed software developer in the US, and an out-of-business pharmaceutical company in France have in common? Answer: each company went into decline after forming an alliance with another company. Each decline occurred because the other company learned enough about their business to be able to compete directly, while the three in question failed to learn enough to counter this competition.

What do the alliance strategies of an insolvent hospital information systems company in Britain, a dissolved auto components supplier in Germany, and a failed telecommunications company in the US have in common? Answer: Each tried to operate independently, avoiding
alliances, but had to exit their industry because they could not develop a strong enough set of internal capabilities to continue successfully.

The simple message from these cases is that alliances are both risky and necessary.

In a recent book, Cooperative Strategy, Pierre Dussauge and Bernard Garrette show that alliances provide the access to other companies' capabilities that are needed in order to enter new markets, introduce new products, acquire new components, learn new methods of producing goods and services, and learn new ways of organising.

Many readers of the FT Mastering series spend part of their daily working life in activities that intertwine with those of corporate partners and other organisational allies. Yet poorly managed alliances are also killing companies.

Some large-scale research studies reinforce this message. For example, Kulwant Singh and I (see further reading) have shown that hospital information system companies using alliances as part of development and marketing strategy are more likely to survive than competitors trying to operate independently.

However, companies that use alliances are at high risk during industry shocks that strike at the core purpose of an alliance and are susceptible to losing key partners. In addition, Pierre Dussauge, Bernard Garrette, and I (further reading) show that link alliances (ones in which the parents contribute different types of resources) commonly lead to takeover or reorganisation in favour of one of the partners -- the result of partners learning from each other.

This article outlines ways of managing alliances effectively, to gain strategic advantage while reducing risk. It focuses on how to achieve both short-term and long-term alliance goals. An alliance’s primary short-term goal is to obtain immediate access to the capabilities of ones’ partners. The primary long-term goal is to learn as much as possible about a partner’s capabilities and competitive environments.
Successful alliance management strategy depends on three elements: pre-alliance planning, post-alliance education, and corporate alliance management capabilities.

**Pre-Alliance Planning**

Too often, we rush into alliances as if they were risk-free short-term relationships. This is the **ignorance-is-not-bliss** mistake. Even the briefest business liaison can have a long-term impact on corporate life. A company must undertake a systematic approach to alliance planning that addresses several key questions.

The questions include the following.

*What do you want to achieve in the short run?* Identify the customer-oriented strategic position you want to occupy in your market. Identify the competitive context for the goods and services you will offer your customers. Determine what capabilities you will bring to the alliance and what capabilities you will need from an alliance partner to achieve your desired position and products.

*Who can best help you achieve the goal and what do they want to achieve?* Identify potential partners. Identify the functional capabilities the alliance must develop and/or that each partner must contribute for the alliance to achieve its strategic position. These functional capabilities may include development, production, marketing, distribution, financial, information, proprietary protection, managerial, and others. Assess the goals of the alliance from each partner’s point of view. The ideal partner is one with all the capabilities you need, but nothing unnecessary. Such companies are best placed to help, while least likely to evolve quickly into direct competitors.

*What can you learn from your partner for the long run?* Identify as many long-term learning opportunities as possible. Because many learning opportunities emerge only as an alliance evolves, you must scan continually to identify new learning opportunities.

*What do you want to keep your partner from learning?* Identify capabilities you want to shield from your partner and develop protection
strategies. It is particularly important to ensure people who participate in alliance activities know what capabilities you do not want to share.

*Who needs to know about the alliance?* Communicate key information about the alliance to all people and units who will be involved in alliance activities. Too often, corporate staff negotiate an alliance and then leave business unit people who are lower down the managerial hierarchy to carry out the day-to-day activities, without telling their subordinates why the alliance was formed and how it fits within a broader set of objectives. Almost always such cases either end in complete failure or, at best, realise only a small proportion of potential value.

*How should you organise to attain short-term and long-term goals?* Develop an initial organisation for the alliance. The contractual terms, structural units, management systems, and people must meet both your corporate needs and those of the alliance. An alliance organisation needs to be simple so it does not trap you within it. Too many companies attempt to reproduce subsidiary-like structures and systems for the alliance. They then become snared by the complexity of a failing or unnecessary alliance over which they cannot exercise independent control.

*In summary* - knowledge is the basis of alliance strength. You need to determine what you want from an alliance; which will be the most appropriate partner; what you can gain from your partner both short and long-term; and how you should organise your relationship. Diving into an alliance assuming you will figure it out as you go, is the fastest way to drown.

**Post-Alliance Education**

It is a mistake to think that a good alliance, like a good marriage, is forever, and that we can grow into our capabilities together with our partners. This is the *tomorrow-may-not-come* mistake. It causes us to under-emphasise the immediate need to learn from our partners. I must stress alliances between companies are fundamentally different from marriages between people. Even the best alliances will end and you must manage them accordingly, through effective education. Alliance
education involves learning from your partner and teaching people in your own business. The approach to alliance education needs to address the following questions.

*Who will be responsible for learning from your partner?* Assign people from your company to be responsible for learning from your partner. Explicitly identify your learning goals to those people who will be involved in the alliance. In addition, provide people with enough information about your long-term strategies and objectives so they can take advantage of unexpected opportunities for learning from the partners that will help your company advance.

Be prepared to take advantage of unexpected opportunities to learn from a partner. For example, I was recently involved with a project where students were the first onsite visitors to a key plant of a company with which their sponsor had just formed an alliance. We gave the students clear directions concerning what they might learn from the new partner while also, of course, informing the new partner about the students' goals. The student team then provided a detailed assessment of the new partner's skills in a business system that the manufacturer was developing and planned to implement in its global manufacturing operations.

*Who will be responsible for teaching people in your own business?* Teaching what your employees learn from an alliance is at least as important as the process of learning from your partner. Set up explicit teaching opportunities, such as job rotation, cross-disciplinary seminars, and extensive communication systems. Teach the skills to a critical mass of people, rather than hope the new information will diffuse implicitly via discussions among a few individuals. Press your people to learn both expected and unexpected skills from your partner, while they meet the day-to-day demands of the alliance. Then press them even harder to teach what they have learned to other people within the company.

*How will you reward alliance education?* Simply telling people to undertake alliance education will almost always fail. Instead explicitly set up job evaluations and personal incentives to take into account your
employees' success with alliance learning and teaching. Then expressly review and reward job performance in terms of both current activities and alliance education results.

How is the alliance changing? Alliances change even before the partners begin to work together, often in completely unforeseen ways. Constantly assess changes in the strategic position of the alliance, capabilities of the alliance and your partner, and the alliance organisation. Then identify how to modify your education goals to respond to these changes.

What is your partner learning from you? Too often, we ignore the potential for our partner to learn from us and become our strong competitor as it learns. Just as you need to assess what you are gaining from an alliance, you need to assess what your partner is learning and whether the competitive losses are worth what you are gaining. As part of this assessment, determine whether there are ways in which you can block the partner's access to your key capabilities without unduly hampering the activities of the alliance. However, do not forget to intensify your efforts to learn from your partners. Blocking tactics almost inevitably provide only short-term solutions to competitive losses. While blocking tactics are necessary, it is much more important to become good at alliance education.

Can you get out if you have to? Your company can fail if it becomes trapped in a floundering alliance or snared by a dominant partner. During the course of an alliance, you will inevitably develop business routines and systems that intertwine with your partner's capabilities. If you lose access to key systems, either because your partner disappears or because a dominant partner blocks access to capabilities that have become critical for you, your business performance will suffer. As a result, even as you use alliances as key parts of your strategy, you need to develop and maintain sufficient autonomous capability to operate independently or, at least, be strong enough to attract a desirable new partner. Developing such independent capabilities in parallel with alliance activities often requires additional investment. These may seem expensive in the short-term but evaluation should measure both long-term value and short-term cost. Inevitably, assessment of long-term
value involves greater ambiguity and requires greater judgement than identification of short-term cost.

Who is the best partner now? Although your current partner may have been the most appropriate one when you formed an alliance, a new company may now have capabilities better suited to your current needs. Although you can sometimes help a current partner improve, you need to be prepared to switch partners if a better one emerges. Otherwise you risk losing ground to a competitor that may gain access to superior capabilities. Constantly be on the look out for a new partner who might put your current partner out of business. If we mistakenly think business alliances bear a resemblance to marriages between people, this prescription may sound cruel and unethical. However, once we recognise business alliances are part of dynamic corporate strategy rather than stable family relationships, the fairness of the advice becomes clear. Your corporate partner has ways of protecting itself. In part, an initial alliance agreement can restrain partners from taking unfair advantage of each other. In greater part, companies have the responsibility to maintain and develop skills so they continue bringing value to the alliance.

In summary - education creates alliance strength. You need to learn from your partner and teach yourself as quickly as possible, from the moment you begin to interact with the other company. Alliance education requires both personal action and business systems. At their contact points, learning and teaching are individual activities, as people interact in daily jobs and responsibilities. Many companies stop at individual learning and fail to create channels for teaching the new skills throughout their business organisation. The learning and teaching processes require thoughtful business systems that identify education goals, create education incentives, and provide education channels.

**Corporate alliance management capabilities**

Finally a successful alliance strategy requires the corporate capability to manage alliances coherently. Alliance management
capabilities involve two major functions: managing alliance portfolios and distinguishing alliances from subsidiaries.

Too often, we treat each alliance as if it were our only relationship. This is the *kaleidoscope* mistake. Fragmentation among our alliances creates a fragmented view of the competitive world. The kaleidoscope mistake generates two types of problems. First, we often create conflicting business systems to manage different alliances, risking conflicts among different alliances as they compete for resources and markets. Second, we miss opportunities to share alliance education throughout the company. Therefore, it is critically important to create a dedicated alliance management unit, with corporate and business staff involvement. The alliance management unit must take the lead in assessing the composite needs and opportunities that arise from a portfolio of alliances, as well as the needs and value of each alliance.

A second mistake in managing alliances is to place alliance management in a business development function focused on mergers and acquisitions. This is the *alliances-aren't-subsidiaries* mistake, because it treats alliance partners as if they had no more strategic autonomy than a corporate subsidiary. Far too often in my conversations with corporate managers, they will say, "we recognise how important the alliance has become to the company and, therefore treat it as though it is one of our subsidiaries". This issue is particularly acute with middle managers who carry out daily activities involving the alliances, but even the most senior managers can fall into the alliances-aren't-subsidiaries trap. The common result of this of course, is that an alliance partner does something that harms you but which you cannot prohibit, such as beginning to compete in a new market or withdrawing from the relationship before you are ready. Thus, it is critical to create a dedicated alliance management unit, rather than simply treat alliance management as a minor part of a corporate development unit. Acquisitions and alliances staff must communicate and interact in a way that recognises the different challenges of acquiring subsidiaries and managing partnerships.
The key point in managing alliances is that alliance strength requires specialised corporate muscle. A company must develop a corporate alliance mindset, which all individual members of the company must share, and that recognises the strengths and risks of the full set of its alliances. A corporate alliance management unit plays a key role in developing such a mindset.

Conclusion

As a concluding point, I draw an important distinction between contracts and contacts in successful alliances. Good contracts are essential parts of all alliances, whether they are formal and detailed descriptions of responsibilities and rights, or informal ones providing a shared understanding of the alliance purpose and operation. However, no contract can fully define all of the current world, let alone anticipate all future opportunities. In addition to contracts and, in my view, far more important, the personal contacts your people develop with the people at your alliance partner and with others throughout your company will determine the success of an alliance. These contacts are the primary channel for gaining access to your partner's capabilities, using those capabilities to serve your current customers better, and learning from your partner so you can serve customers better in the future.

Further Reading


