Understanding Strategic Alliances: An Integrated Framework

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This paper will examine the literature on strategic alliances and propose an integrated framework of strategic alliances based on the reviewed material. The paper will examine two theoretical models of strategic alliances, suggested by Vyas et al. (1995) and Osland and Yaprak (1993), respectively. This paper will also investigate literature concerning advantages and disadvantages of entering into a strategic alliance. Finally, the author will suggest an integrated framework of strategic alliances, which includes the motives for forming, the process of forming, and the result of forming a strategic alliance.

INTRODUCTION

Due to increased globalization of businesses strategic alliances are gaining importance worldwide for various reasons which range from market access to reduction of risk. Strategic alliances can be placed on a continuum where contractual agreements lie on one end of the continuum, representing low control and low resource commitment, whereas joint ventures lie on the other end of the continuum, representing high control and high resource commitment (Hill et al. 1990). The decision to enter a strategic alliance should be taken seriously by management because history has shown that alliances tend to be unstable and prone to failure (Berquist et al. 1995). Firms that enter into strategic alliances often focus on the benefits that the alliances will provide without considering costs involved in the formation and maintenance of the alliance. Despite the clear identification of the potential benefits, the costs incurred are often both substantial and often difficult to predict (Das and Rahman, 2010; Morris and Hergert 1987).

Strategic alliances can cause major problems if not handled properly, for example, the failure of the merger between the French firm Carnaud and British Metalbox Packaging. This merger failed primarily due to different decision making styles and competing subsidiaries (Lorange and Roos 1993). The airline mergers between Air France-KLM and Lufthansa-Swiss Air also offered examples of problems mergers and alliances face (Iatrou and Mason, 2009). Failures in strategic alliances, in addition to the increase in the number of alliances in the 80s and 90s, have necessitated research in this area. Researchers as well as practitioners have conducted research in hopes of discerning relationships and linkages, which will facilitate successful interfirm and international strategic alliances.

The purpose of this paper is to examine the literature in strategic alliances in order to identify models that specify relationships between strategic alliance formation and success. This paper intends to examine the motives for formation of strategic alliances as mentioned by different management and marketing academicians. Two conceptual models of strategic alliances will be presented and discussed. An integrated model of strategic alliance process will be presented followed by a discussion of the benefits and limitations of entering into strategic alliances.

LITERATURE REVIEW

Before reviewing the literature in strategic alliances it is important to define strategic alliances. Parkhe (1993) defines strategic alliances as "relatively enduring interfirm cooperative arrangements, involving flows and linkages that use resources and/or governance structures from autonomous organizations, for the joint accomplishment of individual goals linked to the corporate mission of each sponsoring firm" (p. 794). Strategic alliances represent a continuous scale between free market on one hand and total internalization on the other (Lorange and Roos 1993). Varadarajan and Cunningham (1995) define strategic alliances as "the pooling of specific resources and skills by the cooperating organizations in order to achieve common goals, as well as goals specific to the individual partners" (p. 282).

There has been a significant growth in the number of strategic alliances since 1985 (Das and Rahman, 2010, Iatrou and Mason, 2009, Vissi 1997, Dussage and Garrette 1995) which has resulted in a proliferation of research articles in this field. The following sections will attempt to examine the literature and integrate the findings of researchers.

Motives for Strategic Alliance Formation

Three principal theories used to explain strategic alliances, especially joint ventures, are transaction cost economics, organization theory and business strategy (Kogut 1988). Transaction cost economists have argued that alliances are intermediate hybrid forms (Borys and Jemison 1989) between the extremes of markets and hierarchy (Gulati 1995). Transaction cost economics was developed by Williamson (1975), who suggested that firms chose alternative arrangements that minimize the sum of production and transaction costs. According to Kogut (1988), "transaction costs refer to the expenses incurred for writing and enforcing contracts, for haggling over terms and contingent claims, for deviating from optimal kinds of investments in order to increase dependence on party or stabilize a relationship, and for administering a transaction" (p. 320). Transaction cost theory predicts that strategic alliances are designed to achieve such a minimum cost arrangement (Garcia-Canal 1996). Horaguchi and Toyne (1990) theorize that "the strategy to form an alliance is not just reactive (cost reducing internalization markets), it is also proactive in that it creates new products, new markets, new organizations, new management techniques, and new technology" (p. 491).

The second approach suggested by Kogut (1988) was the organization theory approach, specifically the resource dependency approach (Kogut 1988; Gulati 1995; Varadarajan and Cunningham 1995). The resource dependence approach posits that organizations depend on other organizations within their environment to acquire needed sources (Pfeffer and Salancik 1978). The formation of joint ventures is a means for stabilizing the flow of resources that a company needs and for reducing the uncertainty confronted by the company (Pfeffer and Nowak 1976).

The third approach to strategic alliances deals with competitive strategies of firms. Porter (1986) stated that the formation of strategic alliances depends on the five forces; the threat of new entrants, the bargaining power of suppliers, the bargaining power of buyers, the threat of substitute products, and rivalry among firms. The three generic strategies provided by Porter (1985), cost leadership, product differentiation, and focus, are used in conjunction with the five forces in order to outperform competitors. The competitive strategies approach states that alliances are formed also as a defensive mechanism in order to hedge against strategic uncertainty (Wittmann, 2007, Kogut 1988). Varadarajan and Cunningham (1995) suggest that the three conceptual frameworks (transaction cost approach, the organization theory approach, and the competitive strategy approach) mentioned above should be considered as complements, rather than as rivals. Varadarajan and Cunningham (1995), in their article, summarize the motives for alliance formation. The reasons for getting into an alliance have been mainly for market growth and/or profit growth. Varadarajan and Cunningham (1995) approach the formation process from the competitive approach viewpoint. The authors mentioned the following motives for formation:

International market entry: Global competition has necessitated the need for firms to enter foreign markets in order to improve their profitability as well as their market share. Firms that

enter foreign markets via a strategic alliance benefit from the pooling of complementary resources with a foreign partner (Van Marrewijk, 2004).

Circumventing barriers to entering new international markets: New international markets, especially developing country markets, are often difficult to enter due to government regulations regarding full ownership of a subsidiary. Strategic alliances can be helpful in circumventing these barriers to enter new international markets.

Home market position protection: By entering international markets through alliances, firms force foreign competitors at home divert their resources away from expansion into the international markets, thus protecting the home market.

Expand product line/fill product line gaps: Firms often enter alliances to increase the product line or fill gaps in the existing product line. Lack of technology or high cost of production may force a firm to seek a foreign partner to fill their product lines.

Enter new-product market domains: Firms that operate in stagnant or mature industries often enter alliances to gain a foothold in emerging industries.

Reduction of potential competition: By entering into an alliance with another organization, firms tend to reduce future competition potential with that organization.

Raise entry barriers: Raising entry barriers by joining forces with other organizations are a powerful motive to enter into alliances. However, firms have to be careful not to violate the anti-trust laws of any other nation or the US.

Improve resource use efficiency: Alliances allow firms to lower their manufacturing costs, achieve efficiencies in the production process, and allow them to gain experience effects.

Resource extension: Firms that lack the resources to grow enter into strategic alliances. Small firms often enter into alliances in order to acquire R&D resources, which could be capital or equipment.

Acquiring/learning new skills: Knowledge acquisition is an important element in formation of alliances. Partners in an alliance often attempt to learn as much as possible from the other partner while guarding their distinctive skills.

The motives discussed above can be classified under the three approaches defined by Kogut (1988). Table 1 lists the motives and their classification in one of the three approaches.

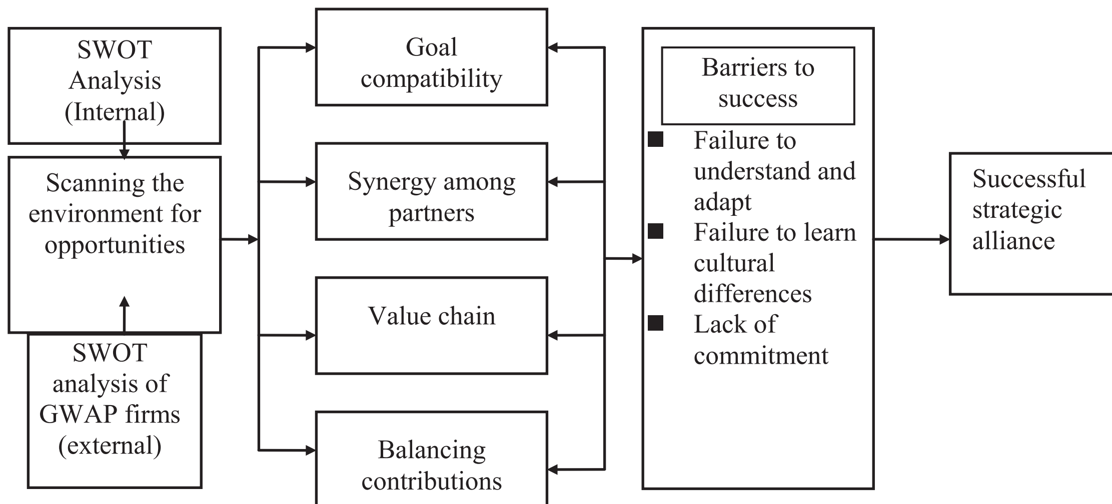
TABLE 1
CLASSIFICATION OF MOTIVES FOR FORMATION

Transaction Cost Approach	Organization Theory Approach	Competitive Position Approach
• Enhance resource use efficiency • Resource extension	• Acquire new skills • Entry into new product market domains	• Entry into new markets • Circumvent barriers to enter new markets • Protect competitive position in home market • Broaden product lines/fill gaps • Entry into new markets • Reduce threat of future competition • Raise entry barriers

According to Vyas et al. (1995), there are two forms of strategic alliances; market related and technology related. For firms in a mature industry, market related strategic alliances tend to be more profitable (Vyas et al. 1995; Varadarajan and Cunningham 1995), whereas technology related strategic

alliances tend to benefit firms in high technology industries relatively more than firms in mature industries (Vyas et al. 1995; Rai et al. 1996). The need to innovate is more immediate in the high-tech industries (Celeste, 1996) and therefore the need to form an alliance in order to create innovative products and services is evident (Schoenmakers and Duysters, 2006, Zeffane 1995, Zeffane 1994). Vyas et al. (1995) proposed a model of strategic alliances. The model states that a SWOT (Strengths, Weaknesses, Opportunities, and Threats) analysis of the parent company should be conducted first in order to assess the need to form a strategic alliance. If a need is established, then a SWOT analysis of the group with alliance potential (GWAP) has to be conducted in order to examine the possibility of an alliance. Figure 1 (Vyas et al. 1995) depicts the Strategic Alliance model.

FIGURE 1
DIMENSIONS OF STRATEGIC ALLIANCES



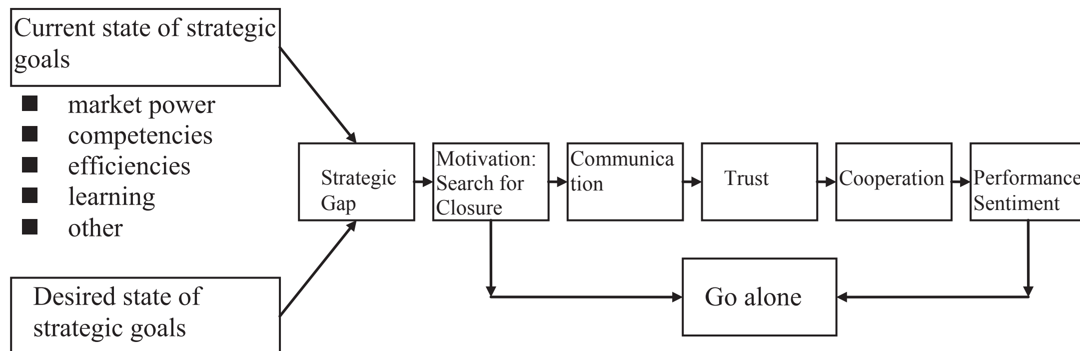
Vyas et al. (1995) posited that the four issues identified in the model are critical for the success of the alliance. The authors state that without goal compatibility the partners will eventually pull in different directions and cause the alliance to fail. Synergy among the partners is necessary in order to achieve the tasks efficiently and effectively (Wu et al., 2009). A clear understanding of the value that a particular firm brings to the alliance along with a balanced contribution to the alliance will ensure the success of the alliance. Alliances in which one partner contributes more than the other tend to end as takeovers by the dominant partner (Tser-Yieth et al., 2009).

The second model of strategic alliances to be discussed in this paper is proposed by Osland and Yaprak (1993). This model suggested that organizations have strategic goals, which at times are not realistic by the organization's standards. The perceived "desired" state of goals and actual goals has a strategic gap, which can be closed by forming an alliance with other companies. The strategic gap can be expressed as "a gap between what they (companies) would like to achieve and what they are able to achieve" (Osland and Yaprak 1993 p. 86). In this case, the motive for forming the strategic alliance is to reduce the perceived gap. Figure 2 represents the process model of strategic alliance formation.

The size of the strategic gap imposes pressure on the firm to take action in order to reduce the gap. "The greater the size of the gap and the perceived importance of filling it, the more likely the firm will desire to form an alliance with another firm" (Osland and Yaprak 1993 p. 86). The authors classify the needs of the firm using the resource dependency model:

1. Market power: market access and economies of scope
2. Efficiency: financial resources and economies of scale
3. Competencies: Knowledge and skills in value added activities of the firm

FIGURE 2
A PROCESS MODEL OF STRATEGIC ALLIANCE FORMATION



Market power can be achieved by developing new markets for present products, developing new products for present markets, and entering new product-market domains (Varadarajan and Cunningham 1995). Alliance formation allows companies to achieve market power, in case they do not possess the capability to achieve those results. Efficiency, important to achieve market power, is important, especially for the high-technology industries (Rai et al. 1996). Forming alliances allows firms to gain access to resources that make them more efficient. Alliances with large firms are particularly beneficial to smaller firms that lack resources to invest in R&D and new product development (Varadarajan and Cunningham 1995; Slowinski et al. 1996). Competencies, the third need in the strategic gap framework, relate to the organizational learning process. Firms use alliances to gain access to other firms' capabilities (Mowery et al. 1996) and attempt to build their knowledge base with their partner's information (Inkpen and Beamish 1997). Organizational knowledge provides firms with a competitive advantage and is therefore critical to the survival of the firm (Osland and Yaprak 1994; Inkpen 1996). Such knowledge creation often results in increasing the longevity of such alliances (Parkhe 1991; Inkpen 1996). However, organizational climate plays a big role in the creation of knowledge. The organizational climate of the firms in the alliance should facilitate the effective implementation and utilization of the knowledge (Inkpen 1996).

The model suggested by Osland and Yaprak (1993) states that firms need to form alliances when they realize that there is a gap between their strategic goals and current goals. Alliance with other firms will allow an organization to enhance their market power, increase their efficiency, or lower their costs. As the organizations work with each other, they develop trust in one another and strengthen the relationship which leads to the achievement of their goals. So far this paper has discussed the theoretical aspects of strategic alliance formation. The section will examine the benefits and limitations of forming a strategic alliance.

Benefits and Limitations of Strategic Alliances

In the previous section we have discussed the motives for formation of strategic alliances. Firms experience the benefits of the alliance when the alliance succeeds in achieving the goals or fulfilling the needs of the partners. The benefits of strategic alliances are derived from the motives for formation of strategic alliances. Lower cost of technology, sharing of risk in high-risk projects (Rai et al. 1996; Slowinski et al. 1996; Celeste 1996), ability to accrue economies of scale and scope in value-added activities (Varadarajan and Cunningham 1995; Day 1995), access to partner's technology, knowledge, and proprietary processes (Parkhe 1991; Chan and Wong 1994; James 1995), and basis for future competition in the industry involved in terms of sustained competitive advantage (Varadarajan and Cunningham 1995) are all benefits of strategic alliances which were previously mentioned as motives for alliance formation. Successful alliances are between firms that achieve their goals and the motives for formation of the alliance (Pateli and Giaglis, 2007). Management decides to enter into an alliance after

conducting an environmental analysis (internal and external) and finding discrepancies in their goals. These discrepancies are filled with capabilities of other firms by forming an alliance. These capabilities are termed as motives before the alliance is formed and benefits after the alliance is successful.

Several limitations and drawbacks of alliance formation, however, may accompany the benefits of forming a strategic alliance. Day (1995) posited that one of the greatest costs to a firm is the liquidation cost of the alliance, if the partners do not agree. Losing proprietary know-how is also considered to be a high impact drawback of forming alliances. Other potential drawbacks of forming strategic alliances are:

Control related problems: Strategy implementation usually goes beyond the control of one party, and thus is likely to bother some companies. Dependence on partners for skills is a potential drawback to one who is dependent (Wu et al., 2009, Lei and Slocum 1991).

- Unequal gains: Some partners in the alliance may gain more than other which can cause problems for the partner getting less out of the alliance (Harrigan 1988; Slowinski et al. 1996).
- Differences in cultural values: Corporations encompassing different cultures may experience culture clashes after the formation of the alliance. There is an increase in the formation of joint ventures between partners of different cultures (Harrigan 1988; Harrigan 1987). These alliances often suffer due to the cultural differences between the partners (Fedor and Werther 1996; Vyas et al. 1995). Different corporate cultures between firms of the same nationality also cause failure of strategic alliances (Vyas et al. 1995).
- Role ambiguity: Uncertainty about specific roles may limit organizations from fulfilling their obligations to the alliance.
- Partner's alliance with competing firms: A partner may establish cooperative linkages with competing firms (Singh and Mitchell 1996). This situation may hamper the present alliance.
- Facing antitrust charges: Antitrust regulations can restrict the benefits of an alliance with a major partner and invite governmental intervention.

These disadvantages contribute to the failure of strategic alliances. Although the disadvantages seem to outnumber the advantages mentioned in this section, mutual gains from alliances can outweigh disadvantages. For the alliance to be successful, firms should possess a change-oriented corporate culture (Vyas et al. 1995), along with continuous mutual commitment and support (Kogut 1988). Firms that possess culture that allows and encourages change are usually successful in forming strategic alliances. The change-oriented culture allows the worker to handle the barriers to success effectively in order to reduce failure of the alliance. In order to better understand the formation process of strategic alliances, the author will suggest an integrated model of strategic alliances based on the two models (Vyas et al. 1995; Osland and Yaprak 1993) reviewed in this paper. The model, which utilizes variables from both the models discussed previously, will be discussed in the next section.

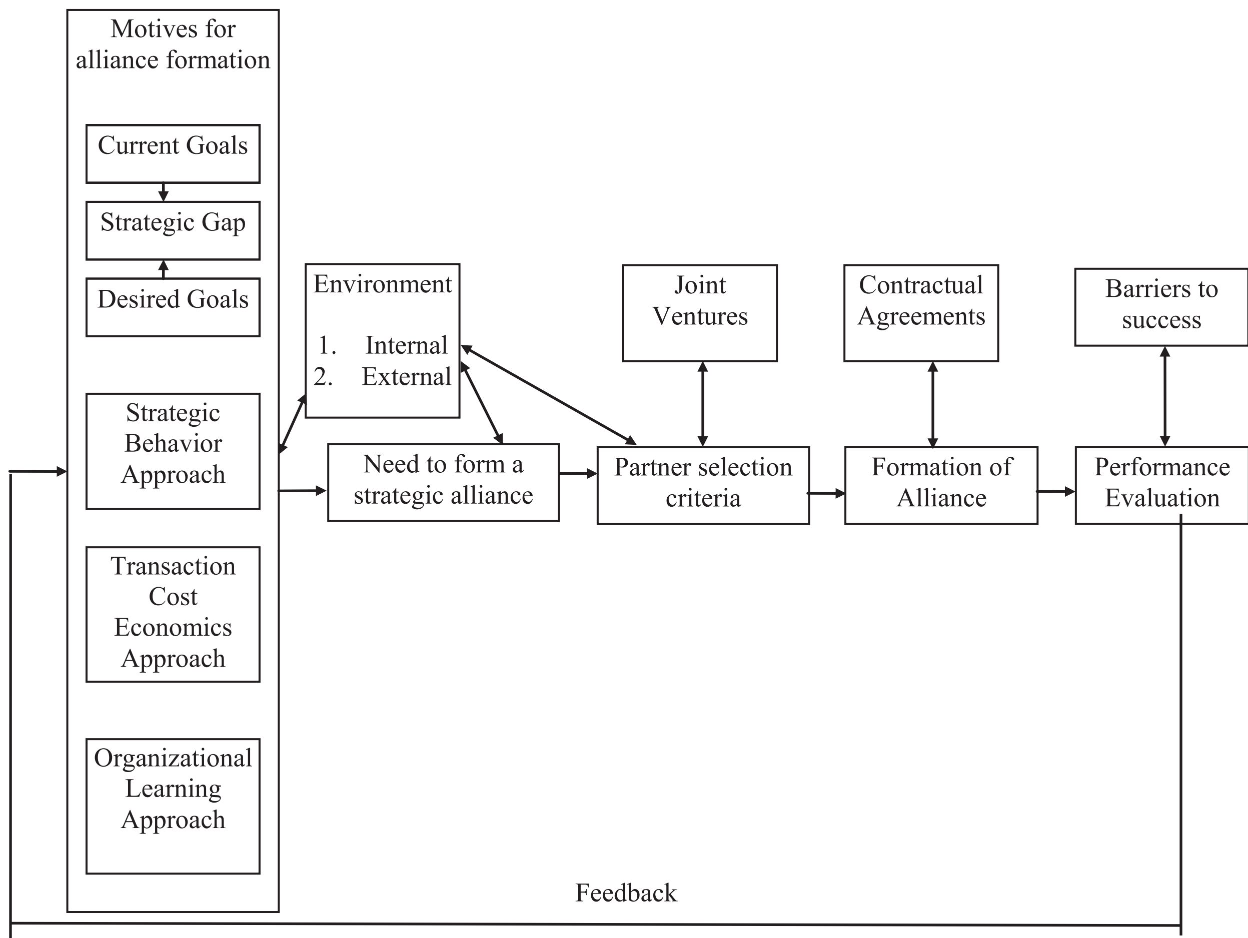
AN INTEGRATED FRAMEWORK FOR STRATEGIC ALLIANCES

Vyas et al. (1995) as well as Osland and Yaprak (1993) began their model with the environmental analysis. The need to change is perceived after the firm scans the internal and the external environment in order to assess the current performance of the firm. The model suggested by the author (see Figure 3) posits that the alliance formation process begins with the motives for formation of alliance. The motives for forming the alliance are considered to be the antecedent variables, which are derived from the literature (Vyas et al. 1995; Osland and Yaprak 1993; Kogut 1988). The internal and external environment plays an important role in the assessment of the motives for alliance formation. The need to form an alliance is perceived by management after the environmental analysis and identifying the needs of the firm that are not being fulfilled with current capabilities.

Selecting the right partner is very important to the success of the alliance. We have already discussed the importance of mutual commitment, change-oriented management on both sides, and ability to manage contrast cultures (corporate or national). The proposed model divides strategic alliances into two parts:

joint ventures and contractual agreements, which include licensing, technology agreements, and supplier arrangements. The partner selection process for joint ventures and for contractual agreements includes a careful assessment of the bargaining power of each partner, control issues, trust and commitment issues, knowledge transfer issues, stability of the alliance, conflict resolution, and experience (in alliances) of the partners (Inkpen and Beamish 1997; Hill et al. 1990; Borys and Jemison 1989; Kogut 1988).

FIGURE 3
STRATEGIC ALLIANCES: AN INTEGRATED FRAMEWORK



After carefully selecting a partner, the firm enters into the alliance. The performance evaluation of the alliance is conducted in order to assess the success of the alliance. Barriers to success, discussed in the benefits and limitations section, play a direct role in the determination of the performance of the alliance. The success of the alliance depends on how the barriers to success are handled by the partners. Firms that handle the barriers effectively are the ones that succeed in sustaining their alliance. Firms that do not succeed based on the performance evaluation have to assess the motives for alliance formation with an environmental analysis in order to detect any problems that went unnoticed the first time during the alliance formation.

The model described above adds to the current literature on strategic alliances by integrating the three

approaches suggested by Kogut (1988), the process model suggested by Osland and Yaprak (1993), and the dimensions of strategic alliances model by Vyas et al. (1995). The two models and Kogut's (1988) approaches are complementary to each other and therefore can be used in an integrated model like the one suggested above. The addition of the partner selection criteria also adds a new dimension to the new model. Although the literature in strategic alliances does not pay enough attention to the selection criteria, it is one of the most important elements of forming a successful strategic alliance. It is important to note that performance is not described in this model in terms of specific variables because alliances define performance in different terms (financial performance or market performance).

FUTURE RESEARCH DIRECTIONS

This research examined the literature in strategic alliances in order to form an integrated model. The author of this paper did propose a model of strategic alliance formation. However, this model is based on theoretical approaches and frameworks. It is important to test this model empirically in order to assess its validity and reliability.

Research in strategic alliances has been mostly using secondary data. Researchers should also make extensive use of primary data, through surveys and questionnaires, in order to understand managerial perceptions of strategic alliances. Managerial perceptions have a very powerful impact on the decision making process (Einhorn and Hogarth 1981).

CONCLUSION

Strategic alliances represent a medium that can create scale and scope advantages necessary to be competitive on a global basis. Alliances allow firms to conserve their resources as compared to forming a wholly owned subsidiary. Strategic alliances also allow firms to gain local identity giving them an advantage over wholly owned subsidiaries when dealing with local governments and businesses. The above statements discuss the gains of forming an alliance. Yet there are disadvantages to forming alliances rather than wholly owned subsidiaries. The advantages and disadvantages of alliances have to be carefully weighed by each organization before making a decision to enter an alliance.

The theoretical model proposed in this paper will allow practitioners to examine the important issues in the formation of the alliance and will also allow them to understand the process of strategic alliance formation. Researchers can examine this model and attempt to expand on it by adding more components to the model through empirical investigations. Strategic alliances will keep on increasing over the next few years, thus making it necessary to understand them more through increase in research.

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