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## **STRATEGIC ALLIANCE AND COMPETITIVENESS: THEORETICAL FRAMEWORK**

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### **ABSTRACT**

Strategic alliances, which are cooperative strategies in which firms combine some of their resources to create competitive advantages, are the primary form of cooperative strategies. Research on strategic alliance in the past few decades has suggested that strategic alliance can enhance competitiveness. Whatever forms joint venture, equity based or nonequity based, strategic alliance assist in ensuring the economic value addition, multidimensional inter-firm network, and inter-organizational coordination. In this paper we have tried to identify how strategic alliances enhance competitiveness and some factors which foster strategic alliances. Finally, we have identified some research gap that will help in conducting future research regarding strategic alliance issues.

**Keywords:** Strategic Alliance, Competitiveness, Joint Venture, Equity Strategic Alliance, and Nonequity Strategic Alliance.

### **INTRODUCTION**

Strategic alliances are increasingly becoming popular day by day. To achieve competitive advantages firms combine their assets and capabilities in a cooperative policy that is termed as strategic alliance. Strategic alliance is considered as an essential source of resource-sharing, learning, and thereby competitive advantage in the competitive business world. Management of alliance and value creation to attain competitive advantage is very important in strategic alliance (Ireland et al, 2002).

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Formation of relational capital demands an integrative approach to manage the contemporary conflict, and firms get the opportunity of both at the same time. Thus, as linkages between them strategic alliance involve firms with some degree of exchange and sharing of resources and capabilities to co-develop or distribute goods or services (Kale et al, 2000). The achievement of competitive advantages is not possible by one firm itself because it does not possess required all resources and knowledge to be entrepreneurial and innovative in dynamic competitive markets. Interorganizational relationships create the opportunity to share the resources and capabilities of firms while working with partners to develop additional resources and capabilities as the function for new competitive advantages (Kuratko et al, 2001). “Unprecedented numbers of strategic alliances between firms are being formed each year. (These) strategic alliances are a logical and timely response to intense and rapid changes in economic activity, technology and globalization, all of which have cast many co operations into two competitive races: one for the world and another for the future” (Doz and Hamel, 1998). Many firms, especially large global competitors establish multiple strategic alliances. General Motors’ alliances, for example, “..... include a collaboration with Honda and internal combustion energies, with Toyota on advanced propulsion, with Renault on medium- and heavy-duty vans for Europe and, in U.S., with AM general on the brand and distribution rights for the incomparable Hummer” (Dallas Morning News, 2002). Lockheed Martin has forms more than 250 alliances with firms concentrating on the defense modernization by providing special attention on developing advanced technologies (Martin, 2002). In general, strategic alliance success requires cooperative behavior from all partners. Alliance success depends on several factors such as, actively involvement in problem solution, being trustworthy; to create value combining partners resources and capabilities, and persuasion among the partners for cooperation and coordination of activities in the cooperative organizational behavior. Conflict management practice and desire of achievement of competitive advantages in market also foster the alliance success (Tiessen and Linton, 2000). To identify an appropriate alliance structure requires more attention in the decision making process of alliance formation. Performance risk and relational risk are involved in choosing the partners to develop alliances. Overall objective is to minimize total risk and ensuring competitive advantages. A competitive advantages developed through a cooperative strategy often is called a collaborative or rational advantage (Das and Teng, 2001). Competitive advantages significantly influence the firm’s market place success. By using technological capabilities firms can ensure customer value and competitive advantage. (Afuah, 2002). Functional and educational experience provide an important dimension in competitive advantage. Rapid technological changes and the global economy are example of factors challenging firms to constantly upgrade current competitive advantages while they develop new ones to maintain strategic competitiveness (Geletkanycz, 2001).

The objectives of this paper are, firstly, to review the strategic alliance literatures relating to competitiveness in the different forms of linkage networks. Secondly, identify the factors fostering the formation of alliances and empirical evidences. Finally, provide hypotheses and scope for future research regarding this issue. This paper, in the next section, discusses the strategic alliance and competitiveness in different form of alliances. A brief review of factors and empirical evidence regarding strategic alliance is provided in the third and fourth section respectively. The fifth section briefly discusses the hypotheses and research questions. The paper ends with concluding remarks.

## **Strategic Alliances and Competitiveness**

Evidence suggests that complementary business level strategic alliance, especially vertical ones, have the greatest probability of creating a sustainable competitive advantage. More and more companies are entering into alliances to gain competitive advantages (Gari, 1999). Strategic alliance designed to respond to competition and to reduce uncertainty can also create competitive advantages. However, these advantages tend to be more temporary those developed through complementary (both

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vertical and horizontal) strategic alliances. The primary reason is that complementary alliances have a stronger focus on the creation of value compared to competition reducing and uncertainty reducing alliances, which tend to be formed to be respond to competitors' actions rather than to attack competitors. The participants of corporate-level of strategies also can use the strategies to develop collaborate the knowledge for future success. Knowledge management is crucial for the firms to gain maximum value from this knowledge; firms should organize it and verify that it is always properly distributed to those involved with the formation and use of alliances. To successfully commercialize inventions, firms may therefore choose to cooperate with other organizations and integrate their knowledge and resources (Simonin, 1997).

Firms also use cross-border alliances to help transform themselves or to better use their competitive advantages to take advantages of opportunities surfacing in the rapidly changing global economy. For example, GEC, a U.K. based company seeks to move from "a broadly focused group deriving much of its revenues from the defense budget to full range telecommunications and information system manufacturer." Networks have more than two components in relationships and they characterize the association of components in close relationships also in existing market-based relationship. Participants' role playing, performance evaluation, profit-sharing and risk management become more complex because of high concentration of trust in network (Tomkins, 2001). A network cooperative strategy is particularly effective when it is formed by firms clustered together, as with Silicon Valley in California and Singapore's Silicon Island (Cohen and Fields, 1999). The strategic alliances can be mostly summarized into three dimensions: joint venture, equity strategic alliance, and nonequity strategic alliance. This section reviews the literature on how the three dimensions of strategic alliance may contribute to competitiveness.

## **Joint Venture**

When two or more firms form a legally independent firm to share their collaborative capabilities and resources to achieve competitive advantages in the market is termed as joint venture in the form of strategic alliance. Joint ventures are effecting in establishing long-term relationship and in transferring tacit knowledge. Because it cannot be codified, tacit knowledge is learned through experiences (Berman et al, 2002) such as those taking place when people from partner firms work together in joint venture. Expertise and experience in particular field foster the sustainable competitive advantage. Tacit knowledge is an important source of competitive advantage for many firms (Tiessen and Linton, 2000).

In a joint venture endeavor generally participating firms share resources and participate in the operations management equally. "Sprint and Virgin group's joint venture, called Virgin Mobile USA, targets 15-to-30 years-olds as customers for pay-as-you-go wireless phone service. Brand (from Virgin) and service (from Sprint) are the primary capabilities the firms contribute this joint venture"-

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Dallas Morning News (2001). In another example, Sony Pictures Entertainment, Warner Bros., Universal Pictures, Paramount Pictures, and Metro-Goldwyn-Mayer Inc. each have a 20 percent share in joint venture to use the internet to deliver feature films on demand to customers (Orwall, 2001). Joint ventures are optimal form of alliances and different from any firm that independently does in the competitive market with own resources by creating competitive advantages through sharing and combining resources and capabilities of firms, and overall evidences support this statement. The coordination of manufacturing and marketing allows ready access to new markets, intelligence data, and reciprocal flows of technical information (Hoskinson and Busenitz, 2002).

## **Equity Strategic Alliance**

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Ownership percentage in equity strategic alliance is not equal. Two or more firms own the shares of newly formed company differently according to their contribution in resources and capability sharing with ultimate goal of developing competitive advantages. Internationalization of strategic alliances focuses on the linkages between two or more different firms' management capabilities and operations activities. The different corporate cultures are matched into one goal in the strategic alliances when it crosses the boundaries of the country. Many foreign direct investments such as those made by Japanese and U.S. companies in China are completed through equity strategic alliances (Harzing, 2002).

In another example, Cott Corporation, the world's largest retailer brand soft drink supplier, formed an equity strategic alliance with J.D. Iroquois Enterprise Ltd. to strengthen its reach into the spring water segment of its markets. With a 49 percent stake in the new venture, Cott gained exclusive supply rights for Iroquois' private label spring water products. Iroquois president Dan Villeneuve believes that the alliance "... Will expand the Iroquois branded business in the west and far east," (Business Wire, 2002) which is the benefit of his gains its equity strategic alliance with Cott.

## **Nonequity Strategic Alliance**

A nonequity strategic alliance is less formal than a joint venture. To ensure competitive advantages two or more companies form an alliance in a contract basis rather a separate company and therefore don't take equity shares. They share their unique capabilities and resources to create competitive advantages. Because of this, there is an informal relationship is built among the partners. Consequently, requires less formal relationship and partner commitments than other forms of strategic alliances. So, the implementation process of nonequity alliance is simple than the others (Das et al, 1998). Since it is less formal relationship in nonequity alliances, does not need that much of experience likes others. In a complex venture where success necessitates transfer of implied knowledge and expertise, nonequity strategic alliances are unsuitable because of their relative informality and lower commitment (Bierly and Kessler).

However, firms today increasingly use this type of alliance in many different forms such as licensing agreement, distribution agreements and supply contracts (Folta and Miller, 2002). The external factors like uncertainty regarding technology and complex economic environment motivate commitment in relationships. Competition from the rivals encourages the greater commitments with partners. Strategic alliances in the form of cooperative strategies are increasing practicing by the firms because of complexity in operations and high competitive pressure. To be successful in business and survive in the long run some sort of partnership is required this age of globalization. To manage the uncertainty and external complexity formation of strategic alliance is an effective strategy (Inkpen, 2001). Partnership commitments assist to take the decision for outsourcing. Outsourcing means acquiring value-creating primary or support activity from other firms. And outsourcing decision helps to form nonequity alliances. To achieve competitive advantages and less formality this form of alliances are becoming popular (Delio, 1999). Magna International Inc., a leading global supplier of technologically advanced automotive systems, components, and modules, has formed many nonequity strategic alliances with automotive manufacturers who have outsourced by the awards honoring the quality of its work that Magna has received from many of its customers, including General Motors, Ford Motor Company, Honda, DaimlerChrysler, and Toyota (Magna, 2002).

## **Factors Fostering Strategic Alliance**

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Cooperative strategies are becoming more important to companies. Capital intensive and technology based firms are more eager to form alliance for their target success. For example, recently surveyed executives of technology companies stated that strategic alliances are central to their firms' success (Kelly et al, 2002). The affecting main factor is economic factor. Speaking directly to the issue of technology acquisition and development for these firms, a manager noted that, "you have to partner today or you will miss the next wave. You cannot possibly acquire the technology fast enough, so partnering is essential" (Inkpen and Ross, 2001). Among other benefits, strategic alliances allow partners to create value that they couldn't develop by acting independently and to enter markets more quickly.

The effects of the greater use of cooperative strategies – particularly in the form of strategic alliances – are notable. In the large firms, for example, alliances now account for more than 20 percent of revenue. This growth is not surprising because most strategic alliances are profitable. We are witnessing not quite the birth but certainly the ascent of an entity distinct from both traditional business entities and from newer entities like Limited Liability Company (Dent, 2001). Booz Allen Hamilton, Inc. predicted that by the end of 2002, alliances would account for as much as 35 percent of revenue for the one thousand largest U.S. companies (Ulfelder) Supporting this expectation is the belief of many senior-level executives that alliances are a prime vehicle for firm growth.

The entry restriction and slow-cycle market position motivates firms to develop strategic alliances to enter in new markets or establish franchises in new markets. The restricted to India's insurance market prompted American International Group (AIG) to form a joint venture – Tata AIG – with Mumbai-based Tata Group, "... which is one of the country's largest conglomerates and a trusted Indian brand name." (Kumari, 2001) AIG executives believed that the cooperative strategies were the only viable way for their firm to enter a market in which state-operated insurers had played a monopolistic role for decades.

On the other hand, the movement of first-cycle markets is unpredictable, complex, and unstable. Combined, these conditions virtually preclude the establishment of long-lasting competitive advantages, forcing firms to constantly seek sources of new competitive advantages while creating value by using current ones. To get rapid entry in a new market and successful transition from present to the future in a fast-cycle market alliances between companies with excess capabilities and resources are more appropriate because of those promising capabilities and resources. Therefore, a firm needs a comprehensive view regarding its strategy and operational capacity and efficiency. Investment in portfolio with these parameters is required to build such discipline in the cooperative strategy. Sometimes, companies establish venture capital programs to facilitate these efforts (Chesbrough, 2002).

Economies of scale and large volume orientation are the important characteristics of standard cycle markets, where strategic alliances are formed by participating firms with their complementary resources and capabilities. Lufthansa (Germany) and United Airlines (United States) initially formed the Star Alliance in 1993. Since then, 13 other airlines have joined this alliance. Star Alliance partners share some of their resources capabilities to serve almost 900 global airports. The goal of the Star Alliance is to "... combine the best routes worldwide and then offer seamless world travel through shared booking" (Berentson, 2001).

Socio-political factors also affect strategic alliance as well as international business. China's entry into the World Trade Organization (WTO) has put significant focus on this huge potential market. While more firms will enter china in coming years, many foreign firms who have entered China have found it difficult to establish legitimacy (Ahlstrom and Bruton, 2001). This is most likely due to

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China's recent history. "Collective property party" is the Chinese translation of the term communist party. Although law has established property rights, many Chinese do not share this mind-set. Their opposition to property rights is mainly of two types: ideological and practical. First many local government and communist party officials feel that private enterprise is undermining the socialist ideal. As a result, many of the local policies (such as taxes, license fees, and so on) toward private firms are punitive. Second many officials fear that foreign private domestic competitors will undermine state-owned enterprise, which provide social, educational, and medical and retirement benefits to their employees. Although China's reforms include funds for social programs, there may be uncertainty that are becoming more market oriented must work hard to establish legitimacy with local government officials, suppliers and customers.

As the economy in China increasingly adapted market mechanism, regional cluster emerged. Both market force and government supports gave birth to industrial cluster in the southeastern coast of China including Guangdong, Fujian, Zhejiang, and Jiangsu, local government were proactive in the reform (Zhao, 2002).

In the wave of internationalization of strategic alliances many firms establish facilities in the other countries to lower the cost of production. Easy access to low-cost labor, energy and other natural resources are the motivating factors behind such establishments. Sometimes location facilities foster strategic alliance. Once positioned favorably with an attractive location, firms must manage their facilities effectively to gain the full benefit of location advantage (Bernstein and Weinstein, 2002). In Eastern Europe, Hungary is a prime location for many manufactures. Flextronics, a large electronics contract manufacturer, is locating critical resources there. Hungary has good safety regulations and rapidly approves projects. In 2001, 57 percent of Hungary's exports were in electronic equipment, providing a strong and growing market for Flextronics. Furthermore, it has lower labor costs than Ireland, another important electronic components producing country on Europe (Wilson, 2001).

## **Empirical Evidence on Effectiveness of Strategic Alliance**

There is volume of literature on empirical evidences of effectiveness of strategic alliances. Strategic alliances are the result of collaborative endeavor is considered as the factor of competitive business and cooperative relationships (Varadajaran and Cunningham 1995). This study based on the especially on marketing and operations management perspective identifies several factors affecting strategic alliances and competitiveness. This section identifies several empirical experiences regarding formation and success of strategic alliances over the world.

Strategic alliances, some long-term and others for very short periods, with suppliers, partners, contractors, and other providers of world-class capabilities allow partners to the alliance to focus on what they do best, farm out every thing else, and quickly provide value to the customer. In 2004 Bierly and Coombs argued about alliances termination is relevant with product development stages.

According to their opinion the chance of termination of alliances are more if the alliances are formed at early and late-stage of product development but less chance in mid-stages of product development. Firms can adapt technological changes through interfirm cooperation and critical to commercializing the new technology when firms have complementary assets within the firms' own boundaries. To develop new products and their marketing policy formation large pharmaceutical firm and biotechnology companies are increasingly integrating the knowledge and resources. By studying 889 strategic alliances of pharmaceutical companies with new biotechnology firms Rothaerme (2001) found new product development and new technology is positively associated. An incumbent's

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alliances with new technology, new product development, and firm performance are related with each other.

Scientific capabilities, firm location, and experience of top management – the three signaling mechanisms have a considerable relationship with the amount of capital raised through international strategic alliances (Coombs and Deeds, 2000). Technological collaboration with partners and repeated interaction with new and existing partners improve new products' performance (Soh, 2003). The association between new product development and strategic alliances was tested by Dees and Hill (1996) on a sample of 132 biotechnology firms. The results indicate the relationship between rate of new product development and numbers of strategic alliances are an inverted U-shaped relationship.

Airlines industries show some evidence of strategic alliance. SAS and Swissair formed an alliance to offer connecting flight and average service frequency in airlines industry. This alliance reported increases the flights after formation of alliance between the SAS and Swissair hubs. Further, there has been an overall cost reduction in operations of flights by lowering in the layover time associated with SAS-Swissair connecting services (Youssef and Hansen, 1994). In 2001 Evans, Oum and Zhang found a positive association among productivity, pricing, profitability, and formation of alliances. By analyzing a time-series data of 56 airlines over the 1986–1993 periods Park and Cho (1997) investigated the changes of market shares of the carriers of codesharing alliances. Their empirical results indicate: (a) codesharing, in fact, increases the carriers' market shares; (b) codesharings between existing airlines increase market shares less than those between relatively new carriers; and (c) the market-share-increasing effect of codesharing alliance is higher in markets with fewer competing carriers.

Theoretical foundation analysis is also done in the formation of strategic alliances. Most of the researcher emphasized on transaction cost theory and resource-based view to analyze the alliance formation feasibility study. Initially firms focus on access to resources of partners followed by shortening of time to develop or market products. Cost reduction is the focal point for some strategic alliances in the initial stages of formation. But in high technology industries resource-based view prevails over the transaction cost theory (Yasuda, 2005). Chang (2004) examined how Internet startups' venture capital financing and strategic alliances affect these startups' ability to acquire the resources necessary for growth. The study found that three issues positively influenced a startup's time to IPO: the better the reputations of participating venture capital firms and strategic alliance partners were, the more money a startup raised, and the larger was the size of a startup's network of strategic alliances.

Japan is considered as the pioneer in the practice of SRPs (Strategic research Partnerships). Because of limited chances for mergers and acquisition, weak research wings, lack of spillover channels in Japan the formation of SRPs are motivated. In Korea, SRPs are developed to support large-scale research and development projects. In Taiwan, to assist technological transmission SRPs are developed. Consortia in the form of alliance in Japan are funded by government to sponsor R&D projects (Sakakibara and Dodgson, 2003). By studying of 114 international strategic alliances between UK firms and their European, U.S. and Japanese partners Kauser and Shaw (2001) found that to be success in international partnership endeavor require communications, commitment, mutual trust and overall coordination. So, evidences show that in different sector of the business world have strategic alliances. These alliances sometimes cross the national boundary to international arena to achieve competitive advantages.

## **Research Questions, Hypotheses, and Scope of Future Research**

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## **Research Questions**

Based on the above literature review, some questions may be asked. Does strategic alliance really increase competitiveness? Which type of strategic alliance contributes more to competitiveness? Are strategic alliance and competitiveness characteristics of a market economy? Is economic factors foster more strategic alliance than others factors? Could government policies influence the strategic alliance and competitiveness? Are the guidelines provided earlier practical?

## **Hypotheses**

Strategic alliance contributes to competitiveness. More specifically, joint venture, equity strategic alliance, and nonequity strategic alliance (including business level, corporate level, cross border, and network strategic alliance) should increase the competitiveness of firms, industries and region. The following secondary hypotheses can be tested: In a market oriented economy, some industries will be benefited from the strategic alliance. Industrial specialization and concentration will increase. New product development and technology up gradation will occur. In contrast, in a non market-oriented economy, planning may be distorted and hamper the natural process industrial alliance and development and may not generate maximum efficiency. Eventually, the strategic alliance in joint venture, equity based, and nonequity based dimensions will occur and affect firms' competitiveness.

## **Scope of Future Research**

Strategic alliances are not risk free. If a contract is not developed appropriately, or if a partner misrepresents its competencies or fails to make them available, failure is likely. Risks in strategic alliance and rate of failure can be studied. Costs not only in economic but also, in social values, environmental and ecological consequences, cultural factors should be considered in the study of strategic alliance. Again, business ethics and monopoly business issues can be studied regarding strategic alliance.

## **Conclusion**

In the competitive global economy strategic alliances are a crucial option for achievement competitive advantages. Cooperative strategy with partnering firms like customers, suppliers, creditors, service agencies etc. is important to develop alliances. By developing strategic alliances firms shares their excess and/or complementary capabilities and resources with others and create a new entity to get competitive advantages. When alliances are effectively managed, the participating firms can gain several benefits that ultimately bring profitability. Mutual trust and interdependency are increasingly becoming important for cooperation. Firms recognize the value of partnering with companies known for their trustworthiness. In a cooperative relationship, when mutual trust exist firms can use the opportunities of maximum utilization of resources. On the other hand, in a formal contractual relationship if there is no trust, extensive monitoring systems are used to controlling purposes. It increases the cost of operations that ultimately hamper the competitiveness of the alliances.



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