

International Business Strategy

Lecture Seven

International Alliances

Introduction to Lecture Seven

In our lecture six we talked about foreign direct investment (FDI) where we said this is one of the many strategies that an international business can choose to use when venturing into foreign markets. The question we have been trying to use in our previous topic is the same we will further in the current topic-**HOW**. In this topic we look at strategic alliances by international business, what they are, the forms they take, and their management.

Learning Outcomes

1. Define international alliances
2. Point out why partner selection is a crucial aspect of international alliances
3. Differentiate several management structures of international alliances

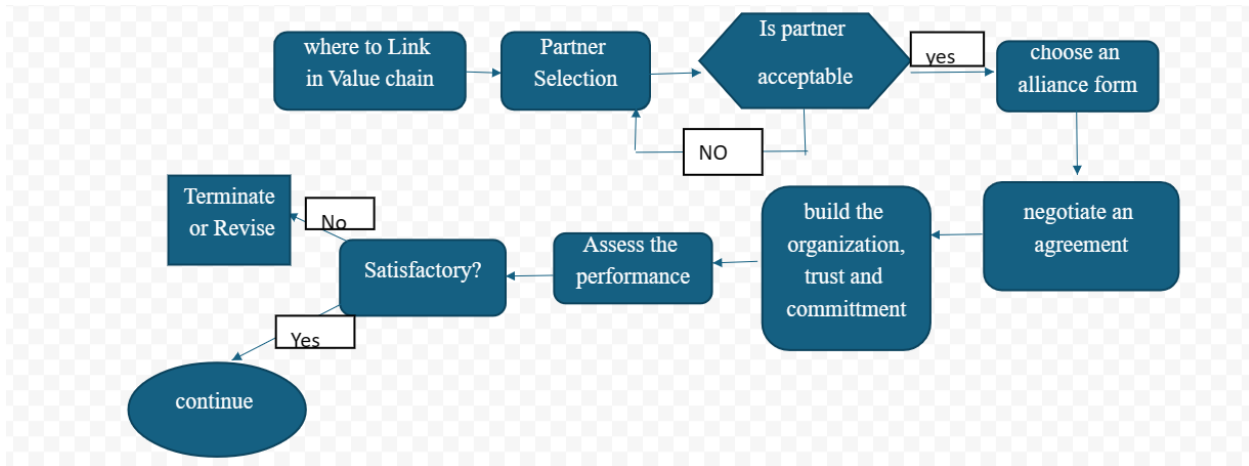
Definition

Our use of international alliance is same as strategic alliance, but to ensure that we remain within our context we will use the former. An international alliance is a relationship between two or more entities from different countries who collaborate to achieve a mutual strategic goal. The relationship often involves sharing resources, strengths, and risks. Alliances can happen between a company and its suppliers or competitors in a different country. The idea of coming together is to ride on their complementary strengths as they seek to conquer the market. In some instances, partners buy a portion of each other's share, to reduce the possibility of any taking advantage of the other. Depending on the mutual goal at hand the alliance can be short or last for years. The next section will be guided by Parboteeah and Cullen (2011) adopted framework as shown in **figure 1**.

The starting point is in determining where you want the alliance to be in your value chain. Is it in the raw materials, operation or toward the customers? As we will be able to see in the

different forms of alliance, any point makes sense, but the firm must decide on this. The next sections we will look at other aspects of the framework pertaining to international alliance.

Figure 1: Implementing an International Alliance Strategy



Adopted from Parboteeah and Cullen (2011)

Selecting a Partner for Alliance

One of the major determinants of how successful an alliance will be is partner selection. Given this, it is seldom to find two firms with the same goals or strategies, and this is where partner selection becomes very important. The issue of trust is huge in this process and the success of the alliance. Here are some guidelines for picking appropriate partners.

- **Seek strategic complementarity:** Before getting into the alliance, it is important that firms understand each other's strategic objectives, where there is complementarity, it may work. For instance, if one firm is seeking market growth and the other is seeking new technology this may be a good partnership.
- **Skills complementarity:** The partners skills should complement each other and not duplicate the skills
- **Product complementarity:** To avoid partnering with a direct competitor which could eventually lead to fights in future, choose a partner whose product complements yours, meaning your products go well together like bread and butter.
- **Compatible management styles:** Seek a firm that has similar or compatible leadership styles and philosophies. This will reduce conflicts when it comes to managing the new venture or the alliance in general.

- **Mutual dependency:** Go for a partner where contribution and dependency will be mutual. This is where the partners feel needed and their contribution is valued, there is no inferior or superior partner.
- **Sizes matters:** It is encouraged to go for a partner who equals you in term of sizes. This will reduce the possibility of one partner dominating the other merely because of their size.
- **Cross cultural communication issues:** proactively assess issues that may emanate from the fact that the partners could not be using the same language. Even in circumstances where the spoken language is the same, cultural differences have some influence in communication. This must be looked at before getting into the alliance.

Choosing the type/form of International Alliances

There are three forms of international alliances; Informal, formal and joint ventures (Parboteeah and Cullen, 2011). In the next section we briefly explore the three.

- **Informal international alliance-** this is an agreement between two or more firms from different countries that is **not legally binding**. This could be an agreement of any kind and could be about any area of their value chain, but the relationship is not legally binding. For instance, one firm can agree to market another firm's products in its market exclusively, however they are not in any way bound by such and can discontinue the agreement at any point. Mostly this form of alliance is seen as a springboard for future formal partnership.
- **Formal international alliance-** This is a **non-equity** partnership between two or more firms from different countries with a formal contract specifying what each partner must bring to the table. In this form, both parties must be willing to give away something of value to get something in return, in general we are saying there are rights and obligations.
- **International joint venture-** Here the two or more firms from different countries come together to form a separate legal entity where they have the ownership positions or control. There are instances where the two firms have equal shares, but in other countries there are legal requirements that the local firm has a dominant role/ownership.

Managing International Alliances

After choosing the partner and the form of an alliance a firm will engage in, the next question that must be addressed is the management structure that the partnership will adopt.

Managing an alliance is complex and unique, as we noted earlier the alliance could be short term or last for years. Since there is more than one party, there is need to agree on the decision-making process formally as this could avert crisis later in life of the alliance. Parboteeah and Cullen (2011), suggested five possible options that multinationals can choose from;

1. **Dominant parent:** Where there is a clear majority contribution of resources, they tend to control or dominate decision making and their managers occupy the most important positions in the alliance.
2. **Shared management:** The parties to the alliance contribute about equally to the decision-making process, shown in managers' position spread and board of directors.
3. **Split control:** This is like shared management, although when it comes to the operational level, the partners share out based on their unique skills/strengths.
4. **Independent management:** In mature alliances which are separate entities, the partners may decide to recruit managers and employees from outside their firms and give them decision-making autonomy.
5. **Rotating management:** In this structure, managers from the partners rotate through the key positions on the management ladder. The period needs to be agreed upon. This works best when technology and skill transfer is one of the mutual objectives of the members.

Commitment and Trust in International Alliance Management

We have mentioned not once, the importance of trust in alliance, indeed it is likened to the place of trust in marriage. Most alliances fail because of lack of trust; indeed, alliances start and end because of trust. Commitment in alliance means that each partner is willing to take care of each other and to do all they can to make the alliance work (this is the case in marriage). Trust on the other hand is the confidence and belief that the other partner has genuine intent and ability to meet their side of the bargain (obligations). It is therefore expected that each partner will behave with goodwill. Parboteeah and Cullen (2011), suggested that through; carefully picking your partner, knowing their strategic goals, seeking win-win approach, and investing in cross cultural trainings partners will be able to build trust and commitment in their alliance.

Assessing the Performance of International Alliance

Remember, international business is getting into an alliance to attain a certain goal. It is therefore important that an evaluation of how well the alliance is achieving its objectives.

When the objective was short term, it may not be difficult to assess such a performance, however, in some cases the benefit is long term. As we mentioned in our last lecture, financial measure may not be the only and best measure of a firm performance, it is therefore important that partners employ other ways to measure the health of the alliance and the benefits that their firm is deriving from such. For example, market knowledge may not be easily quantified but is huge and long-term. Aspects such as management process, firm competitiveness, organizational learning, marketing and financial could be employed in gauging how successful a cross border alliance has been. Where the performance is dismal, the partners need to review whether they want to continue with the alliance and where they choose to continue, a revision must be made in as far as implementation is concerned. Where the performance is satisfactory to the partners, then the alliance can continue.

Advantages or drivers of International Alliances

1. **Access to new markets-** One of the major drivers for alliance is for a multinational to gain access to a market. In countries where market imperfections such as trade barriers exist, it may be useful for such a firm to work with another (local) firm to overcome such barriers. This is common in countries where the government is so strict on foreign business. Access to China for a long time has been through alliances with Chinese firms. Walmart in 2018 acquired majority stake in Flipkart (India) to have access to India rapidly growing ecommerce market. This was the case for L'Oréal when they partnered with Alibaba in China.
2. **Cost sharing-** A serious advantage that partners in an alliance are likely to have been cost sharing in the investment that they are making. Especially, where the investment is cost intensive such as mining, research and development in pharmaceuticals industry, teaming up would help the firms to spread the cost involved. Airbus, one of the leading aircraft manufacturers, came about because of different aerospace companies in Europe joining hands to be able to reduce costs and compete better with Boeing.
3. **Tapping into competitor's/partner's strengths-** It is true that a firm may not have strengths in all areas needed to compete and succeed in each industry or market. As mentioned in internal capabilities and resources analysis, a firm needs to be honest in identifying what strengths and weaknesses they possess. When this is clear, a firm can mask its weaknesses by teaming up with a firm that complements its

weaknesses. The alliance between Google and Fiat Chrysler Automobiles (FIAT) in 2016 was mainly driven by this advantage. FIAT could integrate Android into its vehicles thereby accessing a wide range of services from Google such as Google map, Google assistant and Google play store.

4. **Gain access to partner's distribution channels-** Part of what determines success in a foreign/new market is the aspect of last miles which entail a good distribution channel. In instance where a local firm has a good established distribution channel, it may be advantageous for a multinational to try and partner with such. A good example is Coca-Cola who partnered with Swire group in China, the later have a very elaborate distribution network in China in as far as warehousing, bottling firm and retail is concerned. This allowed Coca-Cola to increase its market penetration.

5. **Reduce or share risks-** Venturing in foreign markets comes with its risk; financial, market, and political. In a bid to reduce these risks, a multinational may choose to form an alliance with a local firm(s). There are markets/countries where political risk is so high that doing foreign direct investment may not be a good strategy choice. If such a market is viable and a firm can recoup some good returns, then international alliances would be appropriate. This strategy is also common in the insurance industry especially in high value covers for instance airplane and vessels. Star Alliance brings together several international airlines who share codes, resources, and help partners to reduce risks associated with factors such as geopolitical instability, fluctuating demand, jet fuel.

6. **Access to new technology-** Sometimes alliances are formed so that a firm can access a certain technology that it does not have, which is critical for success moving forward. This driver is common in industries such as semiconductors, space exploration, automotive, and pharmaceuticals. Sometime back (2010) Tesla and Toyota partnered, with the hope that the latter would ride on the Tesla leadership in technology in as far as developing electric vehicles is concerned. In 2011, Microsoft and Nokia partnered to capitalize on each other's technology in their space, but this partnership failed.

7. **Possible economy of scale**- There is potential of cutting down on cost of production when two firms come together. Given that the production is likely to be higher than in the case where it is done for one firm, the resulting saving will be shared among the partners. The consortium of Airbus that we talked about earlier was largely to consolidate the individual production into one mega production for the manufacturers in Europe thereby being able to cut costs and allowing the alliance to compete with the US giant- Boeing. During the COVID-19 Pandemic we saw AstraZeneca, the University of Oxford, and the Serum Institute of India form an alliance to rapidly develop and distribute vaccines. The partnership allowed the vaccine to be accessible and affordable at the same time and helped in covert the pandemic.

Topic Recap

This topic has helped us to address the **how**- question. It is one of the options that a multinational can use to enter a foreign market. In the topic we have looked at what international alliance is, different forms of it, partners selection, alliance management and we concluded by looking at the drivers or the advantages that may be derived from pursuing this strategy. In our next lecture we will look at the internationalization process, which will depict the process through which firms internationalize.

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