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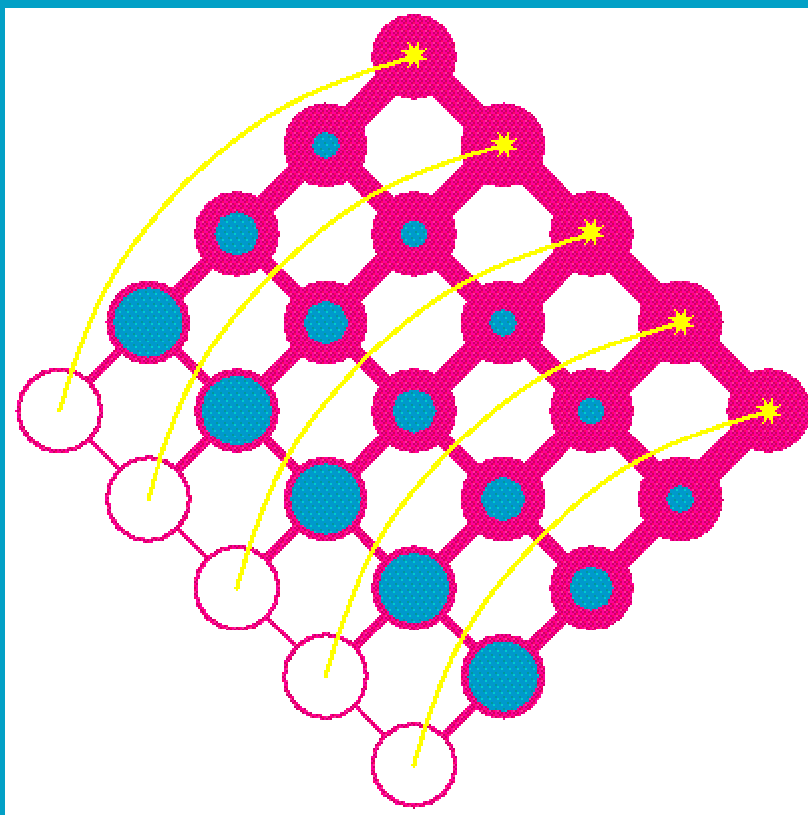
A Practical Guide to Alliances: Leapfrogging the Learning Curve

A Perspective for U.S. Companies



First in a Series of Viewpoints on Alliances

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A Practical Guide to Alliances: Leapfrogging the Learning Curve

A Perspective for U.S. Companies

by John R. Harbison
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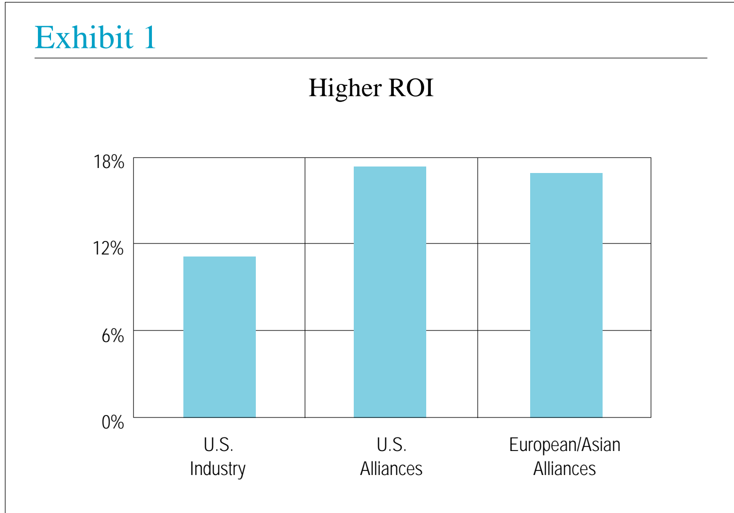
The number of alliances in the U.S. is surging — more than 20,000 new alliances were formed between 1987 and 1992, compared with 5,100 between 1980 and 1987 and 750 during the 1970s. Nearly 6 percent of the revenue generated from the top 1,000 U.S. firms now comes from alliances — a fourfold increase since 1987. However, European and Japanese firms are far more experienced in the area of alliances, and U.S. firms are at an increasing disadvantage due to this lack of experience in alliances. For example, a recent survey by Booz·Allen, the *Wall Street Journal,* and *Nihon Keizai Shimbun* revealed that 74 percent of Japanese CEOs think alliances are effective, while only 4 percent think they are dangerous; in the U.S. the respective numbers are 17 percent and 31 percent.

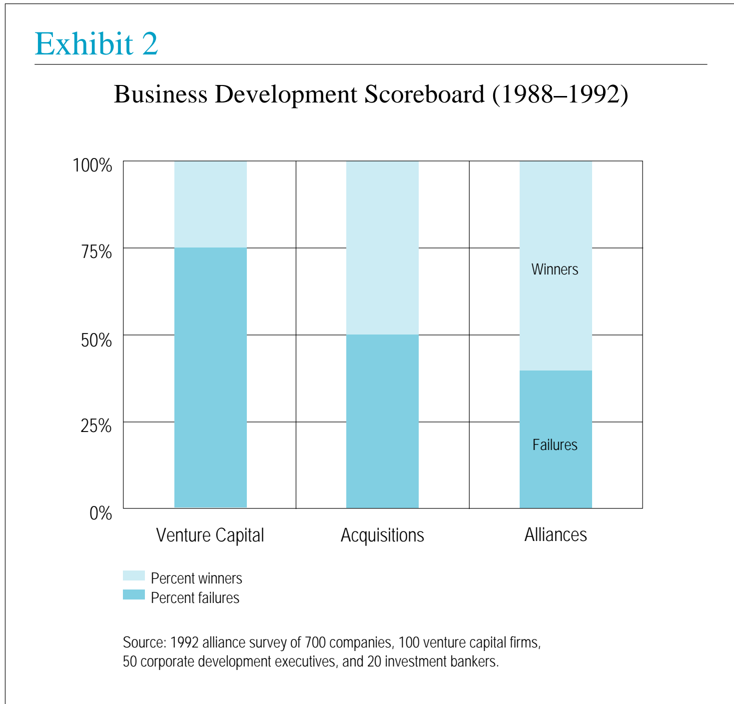
How can the U.S. catch up? Why do some alliances succeed and some fail? And how can companies learn from the mistakes of others and improve the odds for their own success? This *Viewpoint* offers practical advice to addressthese questions.

Alliances can be a powerful tool, particularly in today's world, due to the need to build differential capabilities in more areas than a company has resources or time to develop. Jack Welch, Chairman and CEO of GE, recently echoed this sentiment, "If you think you can go it alone in today's global economy, you are highly mistaken." In studying more than 700 alliances from 1988 to 1992, we learned that the average return on investment is nearly 17 percent, which is significantly higher than the average ROI experienced by the same corporations (see Exhibit 1).

Why? Because alliances typically leverage existing investments inthe partner's capabilities to access incremental opportunities. In other words, the "I" in ROI is lower from avoided investment and the "R" is often higher because incremental revenues can be realized. The catch is that alliances are inherently more complex to initiate and develop, and they require experience in the unique challenges of managing alliances.

While the success rate of U.S. alliances for companies is higher than for acquisitions and venture capital (see Exhibit 2), about 40 percent of alliances are still considered failures. Alliances are also fundamentally





different from acquisitions and require a different level of understanding. While achieving full control, acquisitions bring to the acquirer all parts of the acquired entity — both strengths and weaknesses — whereas alliances match strength to strength and balance control with collaboration.

Despite this track record, U.S. firms are less experienced with alliances and reluctant to gain further experience. European firms on average are involved in ten times as many alliances compared to U.S. firms, and Japanese alliances endure 12 years on average as compared to 7 years for U.S. firms. This relative inexperience hurts U.S. firms since our research indicates that returns improve as a company gains more experience with alliances. We will demonstrate this later in this *Viewpoint* (see Exhibit 8, page 10). However, getting better by repeating common mistakes yourself is hardly an attractive concept.

We believe there is an alternative. Based on multiple surveys and our own extensive experience helping scores of clients with alliances, we have identified a series of best practices and approaches which distinguish companies that excel at alliances. We have also identified a series of pitfalls to avoid in the process. We believe that the practical elements of these lessons learned can allow you to leapfrog the learning process and achieve superior results in your alliances. This Viewpoint *articulates some of those practical pitfalls and best practices.*

Defining the Beast: What Is an Alliance?

We define a strategic alliance as a cooperative arrangement between two or more companies where:

- A common strategy is developed in unison and a win-win attitude is adopted by all parties.
- The relationship is reciprocal, with each partner prepared to share specific strengths with each other, thus lending power to the enterprise.
- A pooling of resources, investment, and risks occurs for mutual (rather than individual) gain.

Alliances are most appropriate when there are strategic gaps in critical differential capabilities that are too expensive (or will take too long) to develop internally; they are also best when it is desirable to access a subset of the partner's capabilities (rather than the baggage of less relevant pieces included in an acquisition). Finally, they make sense when the prospective partner which controls the desired capability is too big to consider seriously as an acquisition.

Within the broad world of "Extended Enterprises," alliances fill the middle ground between strategic sourcing and acquisitions that was traditionally a legal no-man's-land in the U.S. because of antitrust laws. Not all alliances are "strategic" (see Exhibit 3, page 4).

These collaborations cover a wide spectrum of nonequity, cross-equity, and shared-equity arrangements. As one moves along this continuum, from nonequity to cross-equity, the key issue is "How does one successfully manage this unfamiliar new entity?" — and realize the potentially superior returns that are possible.

The Role of Alliances in Market Driving Capabilities

Competitive boundaries are blurring as advances in communication and the trend toward global markets link together formerly disparate products, markets, and geographical regions. Competition is no longer confined to a single nation's borders — making all firms vulnerable to threats posed by cooperative strategies. Rapid technology shifts and tailoring to accommodate rapid product innovation both put pressure on management to act faster and smarter with fewer resources. Effectively identifying, protecting, and enhancing one's core capabilities is the key challenge of our time.

In this environment, successful companies need to select, build, and deploy the critical capabilities that will enable them to gain competitive advantage, enhance customer value, and drive their markets. The emphasis should be on future differentiators, not historical ones. The competitive focus must switch from how to compete better with

current capabilities to how to select and build better future capabilities. Competition is no longer for position itself but for change in position. Positional assets such as facilities, market share, and brand franchise are transitory, while capabilities are not. The goal is to focus on the capabilities that the firm can use to constantly renew and extend its position.

Capabilities are know-how leveraged by cost-effective, responsive business processes and systems for innovation and delivery of enhanced customer value. Capabilities are intrinsically cross-functional. They are based on horizontally organized teams working according to well-designed, preengineered processes, and empowered by policy to make decisions within an established framework of rules. Competitive advantage in capabilities comes from precision tailoring and sharp focus — no company can afford to build advantaged capabilities against all aspects of both the innovation and activity streams (see Exhibit 4).

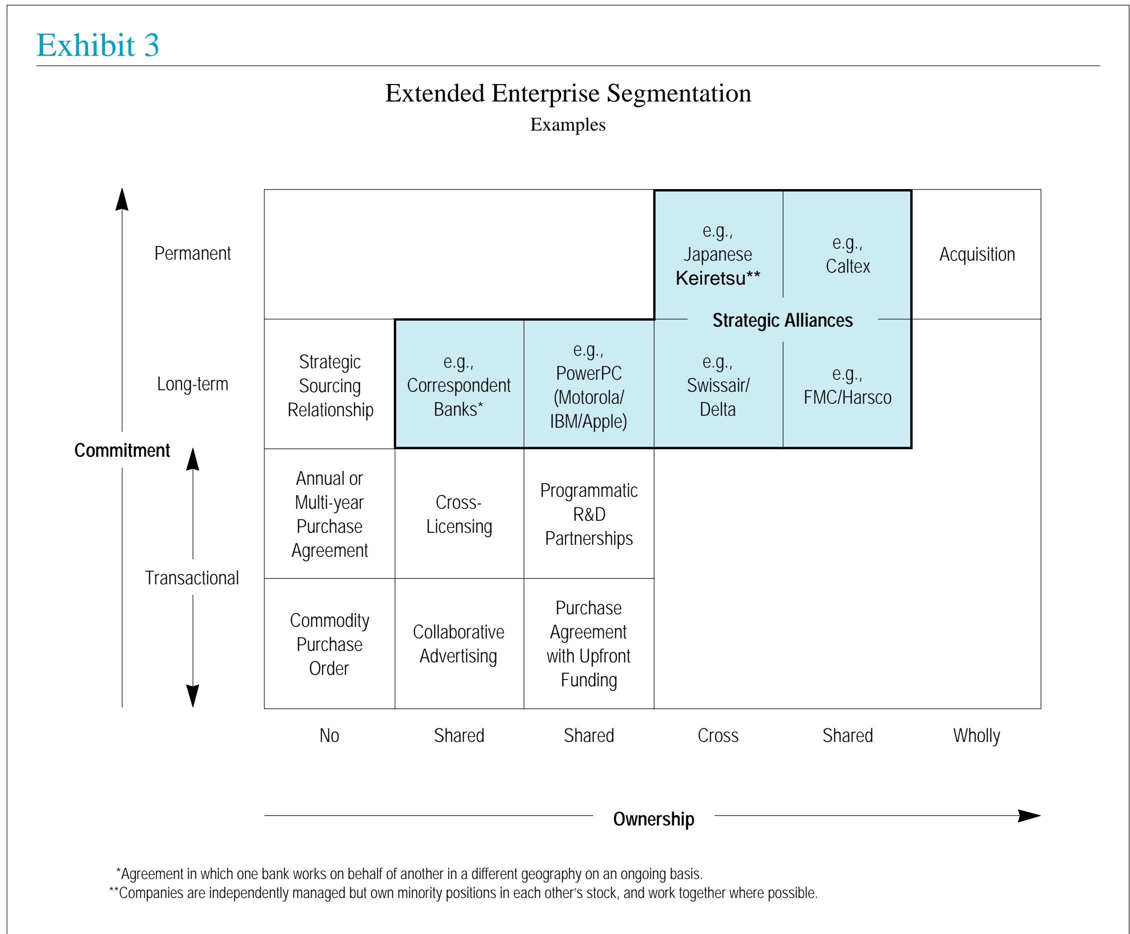
Alliances are an excellent solution to fill critical gaps where the company lacks the resources and/or the time to build its own capability to world-class levels. Alliances also should not be viewed as a static event. The strategy linkage is particularly important when thinking about the changing know-how needs and emerging critical processes that will affect the firm in the future.

The key to successfully executing this challenge lies in what we call a "tradables" analysis, whereby capabilities are differentiated based on both their importance and the company's relative advantage or disadvantage (see Exhibit 5).

Exhibit 3

Extended Enterprise Segmentation

Examples

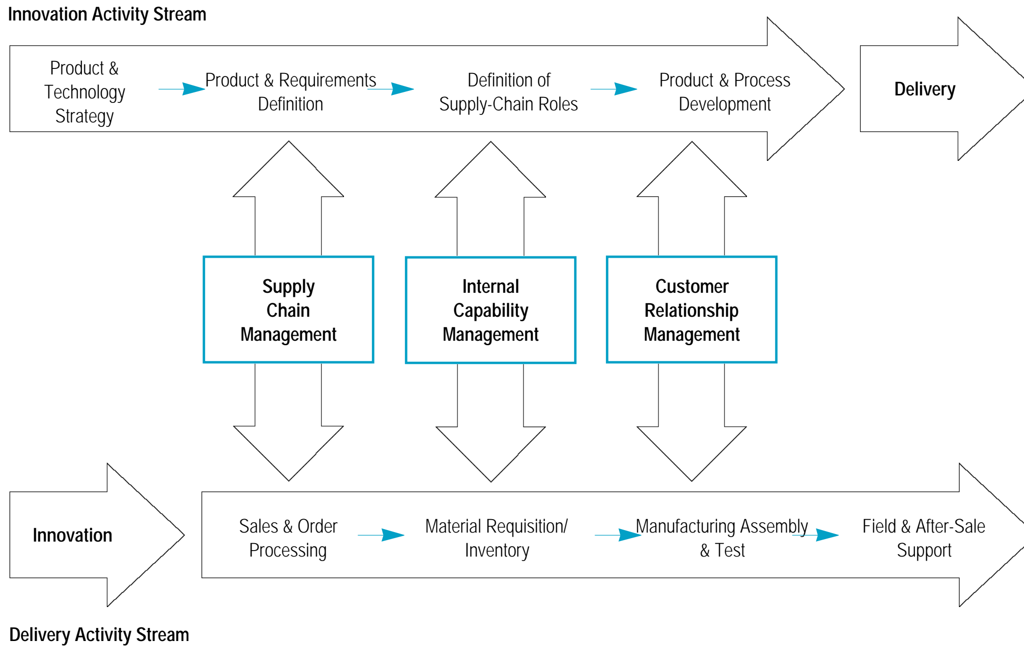


*Agreement in which one bank works on behalf of another in a different geography on an ongoing basis.

**Companies are independently managed but own minority positions in each other's stock, and work together where possible.

Exhibit 4

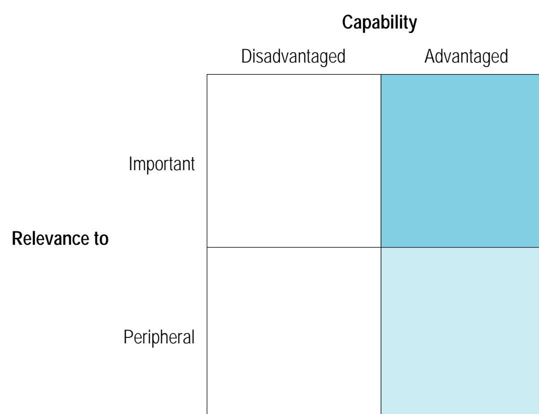
Market Driving Capabilities Framework



This type of analysis lends itself to better negotiations among the parties — through a realistic assessment of each other's true capabilities. For example, Ford and Mazda each felt it had the advantage in product development when it came to determining which company would develop a new transmission for the Ford Probe; subsequent interactions convinced Ford that Mazda was advantaged.

Exhibit 5

"Tradables" Analysis



Rationale for Alliances

There are many reasons to seek an alliance. It is important to understand these drivers from your perspective as well as your partner's:

- **Risk sharing** — you can no longer afford the risks of "bet your company" investment opportunities.
- **Economies of scale** — your industry has high fixed costs, and you need greater scale to compete globally.
- **Market segment access** — you lack a basic understanding of customers and applications, and the relationships/infrastructure to distribute your product to customers.
- **Technology access** — you face critical technology gaps, and you can't afford the time and/or resources to build it yourself.
- **Geographical access** — you are frustrated with the difficulty in penetrating a foreign market where the opportunity is attractive and you have a viable product.
- **Funding constraints** — you are confronting large and ever-increasing up-front development costs.
- **Management skills** — you need an infusion of top-quality management.
- **Value-added barriers** — you want to strengthen value-added skills and raise the level of competitive intensity for your industry.
- **Acquisition barriers** — acquisition opportunities are limited due to size, geographical restrictions, and owner reluctance regarding loss of control.

Sometimes these drivers are the same for both partners (such as risk sharing), but often

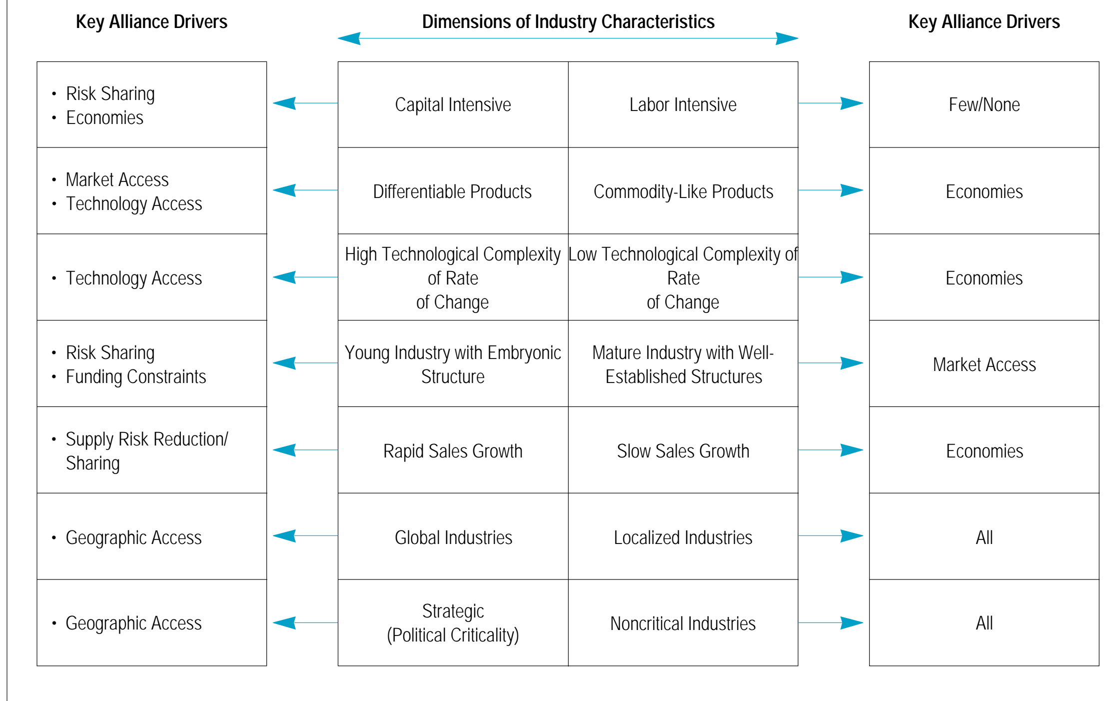


Exhibit 6

Illustrative Industry Impact on Alliance Structure

Key Alliance Drivers	Dimensions of Industry Characteristics		Key Alliance Drivers
• Risk Sharing • Economies	Capital Intensive	Labor Intensive	Few/None
• Market Access • Technology Access	Differentiable Products	Commodity-Like Products	Economies
• Technology Access	High Technological Complexity of Rate of Change	Low Technological Complexity of Rate of Change	Economies
• Risk Sharing • Funding Constraints	Young Industry with Embryonic Structure	Mature Industry with Well-Established Structures	Market Access
• Supply Risk Reduction/ Sharing	Rapid Sales Growth	Slow Sales Growth	Economies
• Geographic Access	Global Industries	Localized Industries	All
• Geographic Access	Strategic (Political Criticality)	Noncritical Industries	All

they are different (such as one partner seeking access to technology and the other access to markets). The relevance of the drivers will vary by industry (see Exhibit 6) as well as by company within an industry. Without explicitly recognizing each partner's reasons for participating, failure will surely result. While partner choice is sometimes limited, it is dangerous when the selection of a partner drives strategy rather than vice versa.

Armed with an understanding of the motivations for the alliance, it is easy for companies to plunge ahead without understanding the perils in the path ahead.

Some Commonsense Traps to Avoid

Pragmatic executives are often suspicious, and rightly so, about simple success formulas. Some executives even maintain that "seat-of-the-pants" management and pure luck play an important role in any alliance. We agree that luck always helps a business alliance succeed. However, we will show that the "luckiest" and most successful are those who learn from others.

Searching through the rubble of failed or failing alliances, we have identified seven *commonsense* traps to avoid:

1) Being a Possessive Child
2) Seeing through the Eyes of a Juvenile
3) CausingtheGenerationGap
4) Dodging the Draft
5) Picking the Wrong Spouse
6) Being Vague with the Prenuptials
7) Living with the In-laws

These hurdles should be thought of as the glue that supports the "Best Practices" that will be discussed in the next section.

1) Being a Possessive Child — *Focusing on one's slice and who controls the baker, rather than growing the pie*

The key to overcoming the possessive child syndrome is to switch emphasis from control to value creation. When addressing value creation, too many alliances fail to even materialize because there is undue emphasis up front on who owns what share, rather than how much incremental value there can be through the coupling of capabilities. Mutual benefit is critical to success.

For instance, Apple, AT&T, Motorola, Sony, Matsushita, and Philips NV are tough competitors and high-stakes players with their eyes on each other's business. Yet they have chosen to operate in unison to the benefit of the group and each member by owning equal parts of General Magic (which is developing software for the individual partners' high-growth wireless personal communicators markets). These types of alliances are becoming a looser, more American form of the Japanese *keiretsu* in which groups of corporations hold together through cross-share holdings. Some organizations like Time Warner are staking their futures on such consortiums. This inexorable drive to alliances amounts to a new chapter in the evolution of free enterprise.

2) Seeing through the Eyes of a Juvenile — *Developing the right amount of trust*

Reaching the appropriate level of consensus on the specifics of an agreement is a delicate balancing act. Some alliances fail because of a lack of trust and overly rigorous documents that degenerate into discussions among lawyers and corporate staff, resulting in stagnation and often the alliance's eventual demise. One must always be aware that circumstances can change over a long period of time and that one must remain flexible in such conditions. Others fail at the opposite extreme; companies enter into arrangements much too quickly, assuming that vague up-front agreements can be easily adjusted at a later date no matter what the state of the alliance may be at that time.

Central to this issue is understanding and articulating each other's objectives, as well as ensuring that the right amount of trust is reflected in the partnership agreement. A too short agreement frequently indicates a "caveat emptor" attitude or overenthusiasm that all problems can be worked out in an open and direct manner between partners. A complex partnership contract suggests that partners are guarded and somewhat suspicious of each other. Either way, an overly short or long agreement, typically starts a cooperative off on the wrong foot.

One must never forget that trust and understanding are the defining features of an alliance. Our advice is to keep the lawyers and corporate staff away from the negotiating table until most elements are worked out by line managers. Rather, engage middle line management early in the process. These are the people who will have to get the job done, and if they are uncomfortable with the project or the partner then the chances of success diminish accordingly.

Finally, don't be in a hurry — it usually takes about a year to put an alliance together. Remember how long it took you to realize how smart your father really was?

3) Causing the Generation Gap — *Depending on inadequate or erratic communications*

Sometimes cooperation fever grows so swiftly that it threatens to sweep away good sense. Starting an alliance without having a clear understanding of the cultural dynamics and organizational forces resistant to change is like playing Russian roulette. Without clear, open, and periodic communications, many alliances create an unbridgeable gap of talking past each other leading to tension, frustrations, and eventually suspicion.

Often the source of these problems is bureaucracy tied up in the traditional ways the partners have done business. Like the new Russia, our apparatchiks are unfamiliar and uncomfortable with their new role of fostering government-industry partnering and working in a faster-paced environment. For example, since its founding in 1991, the U.S. Advance Battery Consortium has used up only $81 million of the $264 million in government and industry funds that were allocated to be spent on the development of a battery for vehicles.

Former President Ford once said, "The most frustrating part of the job is knowing full well that many of the commands the president gives will just never be carried out." As companies get cozier, however, the issue of open communications must be addressed, not only with partners, but also within their respective organizations to foster the enthusiasm, support, and trust necessary to succeed.

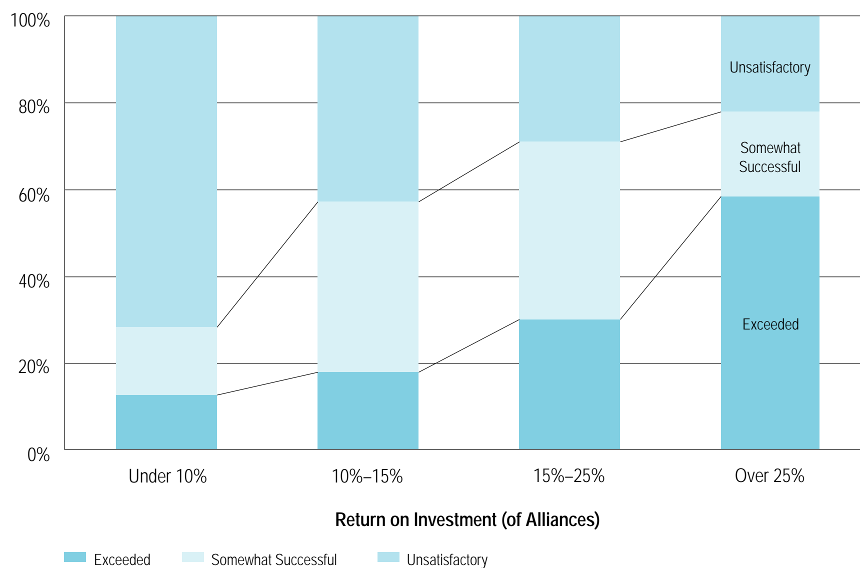
4) Dodging the Draft — *Attracting the best individuals to the alliance*

Successful alliances require personal commitments, yet they are inherently high risk from a career perspective. If the alliance fails, the individuals who cast off from the mothership to work on the alliance are often left stranded in the lifeboats. Consequently, it is not surprising to find that many alliances become viewed as a "dumping ground for misfits" and a "career graveyard," and that the best employees are reluctant to sign up. Partners also miss an opportunity to tap their managers' entrepreneurial spirit when they let the alliance be used as a parking place for executives awaiting retirement. It takes the best, most energetic people to succeed in these ventures outside the company's mainstream.

Future alliances are doomed when companies fail to recognize these tendencies early. The key is to take proactive steps to establish alliance participation as a career enhancer for the best people, and to build a track record of rescuing the best people whenever an alliance turns sour.

Exhibit 7

Success Perceptions versus ROI



Source: 1992 survey of 700 alliances.

5) Picking the Wrong Spouse — *Failing to take the time to select the right partner*

Needless to say, picking the wrong spouse or partner, in life or business, inevitably leads to disastrous consequences. But too many alliances are reactive to overtures by other companies, rather than the result of a proactive and thoughtful assessment of a company's capability gaps and a prioritization of the ideal partners. Getting to know your partner's culture and how it influences behavior, both inside and outside the business environment, is an important aspect in any alliance success.

It is important also to recognize that the selection of a partner may foreclose other options — even in unrelated areas. For example, one multi-segment company forged a promising relationship with a Korean *chaebol,* only to find that the other *chaebols* subsequently refused to discuss more optimal alliances with its other operating units. A different company found that a second coupling was precluded for antitrust reasons.

6) Being Vague with the Prenuptials — *Failing to explicitly agree on objectives and goals*

Whatever agreements are finally worked out between the parties, the provisions will give an early glimpse of the type of relationship that will develop over time. An explicit understanding of each other's mutual objectives and expectations provides the opportunity to maximize overall value and reduce the misunderstandings that will surface along the way. However, entering into a negotiation without a thorough "tradables" and "leverage analysis" of one's strengths and weaknesses tends to have one either overate or underrate one's bargaining position.

Similarly, there are many ways to judge an alliance's success — such as ROI, market share, product quality, technical knowledge, and cost improvement; failing to do so will result in the uneasy situation in which one partner heralds the success of the alliance while his partner is far less happy with the results. Although success rises with higher ROI (Exhibit 7), there

is still a significant number of companies that rate alliances unsatisfactory for not meeting their strategic goals.

Finally, having the ability to address potential irreconcilable differences early is another sign of a well-constructed alliance — successful alliances have an arbitration process and disagreement mechanisms in place at the outset. For example, Lucky Goldstar was unsuccessful in several alliances with Japanese companies because the Japanese would not provide access to vital technology that Lucky Goldstar assumed would have been accessible.

7) Living with the In-laws — *Solving the "Protective Parent Syndrome"*

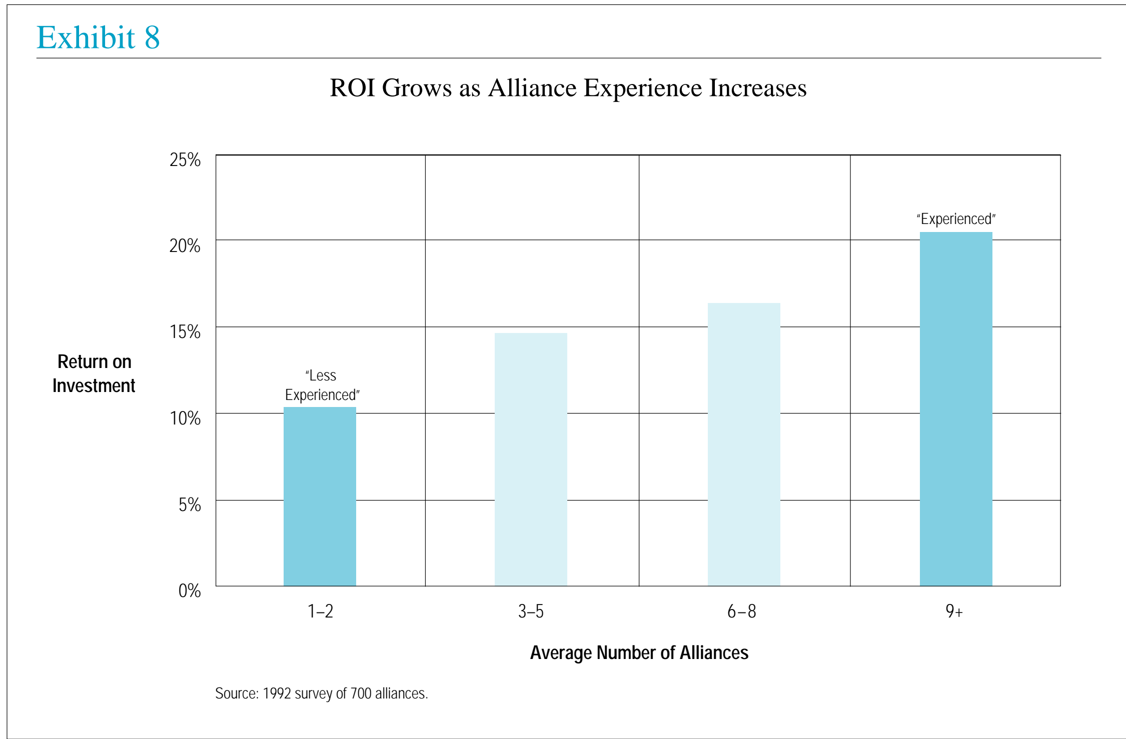
Well-meaning parents can be stifling when they impose their own culture and philosophy on their children; the same is true of corporate offspring. Managers of the new company face different challenges and usually require different cultures, processes, and structures to match the situation. The organization needs to be shaped to tailor the unique needs of the alliance.

For example, when Chevron discovered huge oil reserves in Saudi Arabia and needed a partner to help market them around the world, it chose Texaco. Texaco, another major oil company with a similar culture, had developed large marketing networks in Europe and in the Middle and Far East, and it needed the resources Chevron had discovered. Caltex, an $8 billion company, was formed in 1936 (owned 50%-50% by the two partners) and to this date is one of the best assets of Chevron and Texaco.

Offspring also need independence from their parents — anything less is to hinder the dynamics of the business and congruency of purpose. Denying your child the keys to the car doesn't compensate for failing to get the child off on the right foot in the first place.

But this is not the whole story. Although they are interesting, the Seven Traps are not sufficient to reshape management systems and processes in which strategic priorities can be translated into actions.

Exhibit 8



Alliance Best Practices: Key Success Factors

Fortunately, Booz·Allen has accumulated a body of knowledge and experience that can help you avoid repeating everyone else's mistakes. As Exhibit 8 indicates, companies experienced with the alliance process are achieving superior results over those firms that have done one or two alliances.

These best practices are used by successful alliance-building companies to achieve superior results. These practices are based upon our experience in assisting businesses in making alliances work, and are confirmed by documented results of a five-year study of more than 250 American companies that have formed nearly 1,200 alliances. This effort has led to a body of knowledge that explains the differences between businesses building successful versus unsuccessful alliances.

The principal best practices that are linked to superior results are as follows:

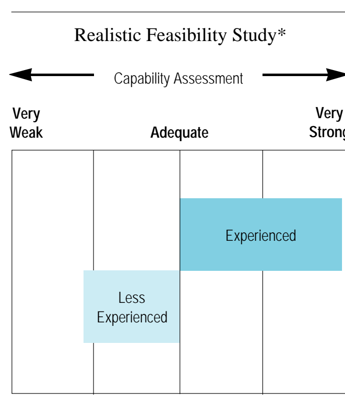
1) Preparing a Realistic Feasibility Study
2) Anticipating Business Risks and Mitigating Them
3) Linking Budgets to Resources and Priorities
4) Conducting Realistic Partner Assessment and Selection
5) Adopting Superior Resource Strategy/Planning
6) Coupling Investment and Rewards with Performance
7) Clearly Defining Roles

We will discuss each of these best practices in turn, as well as demonstrate the link with superior performance based on our survey results.

1) Preparing a Realistic Feasibility Study

Our surveys and interviews with CEOs and senior executives of both experienced and inexperienced firms show that experienced managers emphasize the assumptions, rigor, analytical depth, and consistency of alliance business plans more than inexperienced firms. They often seek the advice of objective outside experts — particularly when the alliance brings them into unfamiliar markets. They also directly translate this assessment into an explicit operating plan and budget. These experienced firms know that direction-setting is more complicated in alliances because of the difficulties in establishing and maintaining harmonious communications between the partners.

Realistic Feasibility Study*



While an alliance plan may be analytically sound, its chances of success depend on many indeterminate elements, such as competitive reactions to alliance, corporate culture, organizational structure, resource base, overall fit with the corporate long-term strategy, and the willingness of partners to dedicate high-caliber people and resources. This must be done through a process of building broad internal and external stakeholder consensus ahead of attempts to implement. Experienced firms not only prepare good alliance plans, but also calculate a probability of success after examining the effect of those exogenous variables that have a major impact on any alliance.

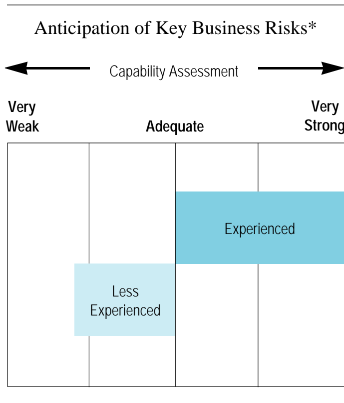
Consider IBM's experience in creating the personal computer. To get to the market quickly, it relied on key technologies from Intel (microprocessors) and Microsoft (operating software). At first everything was going according to plan, but the approach meant that IBM's system wasn't proprietary and IBM couldn't control the market. Hundreds of clone makers emerged with lower prices and better products, thus mitigating IBM's preconceived competitive edge.

*Source: Survey of 250 companies covering 1,200 alliances and 80 interviews.

2) Anticipating Business Risks and Mitigating Them

Experienced management concentrates on understanding the key risks that an alliance can create and how to deal with them.

Anticipation of Key Business Risks*



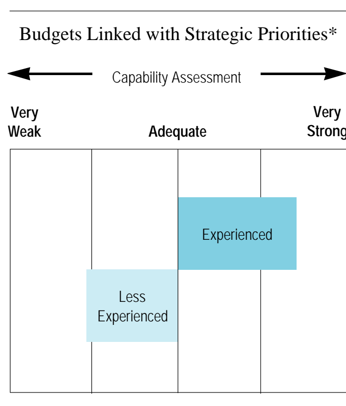
Some of the critical issues that are addressed cover: predicting the effect the alliance will have on long-term competitiveness of the parent, envisioning key obstacles (resistance and resentment to change, short- and long-term trade-off analysis), foreseeing the interchange of proprietary information and processes, preparing for possible breakdown of communications, and tailoring management systems and processes to unique alliance requirements. Plans by inexperienced management typically do not identify the major business risks that are involved when forming a partnership and suffer the consequences later.

For example, the recent alliance involving the Brooke Group strove to capitalize on a cigarette shortage so grave that riots broke out across the Soviet Union. They formed an alliance in 1991 with Ducat, one of Russia's largest manufacturers ofcigarettes, servingtheMoscow market. However, after the collapse of the central government, official organizations with whom the alliance had negotiated ceased to exist. An audit uncovered the factory loaded with debt, critical supplies were missing, and hard currency from the company's treasury was embezzled. Brooke's management moved to fire the Ducat's factory director, who immediately posted security guards to protect himself from dismissal. The alliance has yet to produce one cigarette.

3) Linking Budgets to Resources and Priorities

One of the most revealing elements of success in the survey was the strong rating given by experienced management to linking budgets to resources and strategic priorities.

Budgets Linked with Strategic Priorities*



It is evident that top management in these firms focuses more on priority development and resource concentration than on short-term financial results. They establish strategic priorities and translate them into budgets and operating plans. They also devote considerable effort to finding high-caliber personnel and carefully matching individuals to strategic priorities and objectives. In contrast, inexperienced managers often try to build alliances on the cheap, which is strategic suicide.

Primester, an alliance between Eastman Chemical and Rhone-Poulenc (France), is one of the largest construction projects ever undertaken by these companies. The venture, which was planned in 1988, came on stream in 1993. As Mike Mitchell, managing director, said, "It took a lot of planning and priority setting, but we areverypleased withtheresults."

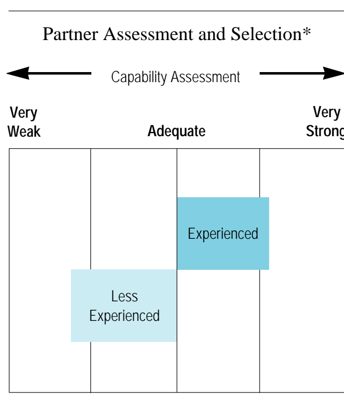
4) Conducting Realistic Partner Assessment and Selection

Partner selection is of critical importance in any alliance. Experienced firms understand that picking the wrong partner always leads to myriad problems later. Inexperienced firms appeared to emphasize objectives and rationales rather than

*Source: Survey of 250 companies covering 1,200 alliances and 80 interviews.

detailed analysis, proactive selection/in-depth understanding of potential partners.

Partner Assessment and Selection*



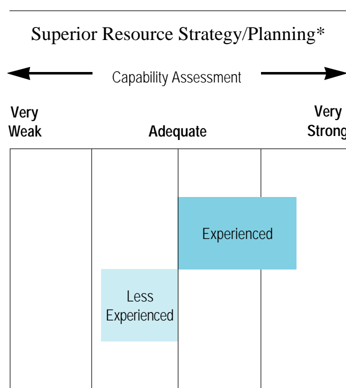
We hear over and over again that experienced players avoid forming alliances with companies unfamiliar with the process and its demands. One manager from a highly regarded Fortune 500 company told us, "I don't want to hand-hold a partner over the rough spots." He told us of an alliance with a Fortune 500 company in which their chairman had to fly to his headquarters to apologize for his company's poor performance — an embarrassing situation for both companies. He remarked, "We do our homework to determine if our potential partners know the process."

These firms have knowledge of the partner's management culture, previous alliance experience, and strategic objectives before entering into any agreement. They also make allowances to accommodate these differences. They clearly understand the partner's core strengths and fundamental weaknesses. They realize differences between a horizontal versus vertical fit. They prepare strategies to help accommodate the partner's management style to fit with their organization's style. And no matter what the time pressure, they avoid rushing into situations where the homework and preparationare not complete. And successful partners always give appropriate consideration to divorce procedures, penalties for poor performance, and arbitration.

5) Adopting Superior Resource Strategy/Planning

Resource planning is of the highest quality in successful firms. Often this is the case because of a superior planning effort.

Superior Resource Strategy/Planning*



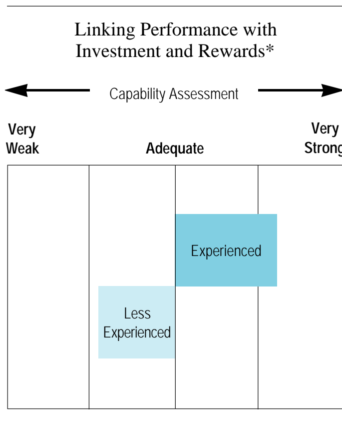
We also have found that resource planning is more effective when partners openly communicate their commitment to the alliance and the quality and level of resources to be allocated. Without this clear understanding, amicable relationships can dissolve quickly. Experienced firms clearly define each partner's contribution of people, money, and other resources and prepare precise timetables of when and how resources will be available, secured, transferred, and delivered. They also make sure resources devoted to the alliance are of the highest caliber.

Cytel's approach to alliances exemplifies the benefits that can accrue to a small biotechnology firm from superior resource planning. In 1991, Cytel negotiated a technology development agreement with Sumitomo Pharmaceutical to develop drugs based on Cytel's selectingtechnology. Inexchange for the option to license products for Pacific Rim markets, Sumitomo agreed to provide $15 million in R&D support over a five-year period. In addition, if an option is exercised, Sumitomo will pay an option fee and royalties on sales. The agreement also requires Sumitomo to make an equity investment (at Cytel's option) of $5M. The alliance, managed by a six-person steering committee, is proceeding well — Sumitomo exercised its first product option in October 1992.

*Source: Survey of 250 companies covering 1,200 alliances and 80 interviews.

6) Coupling Investment and Rewards with Performance

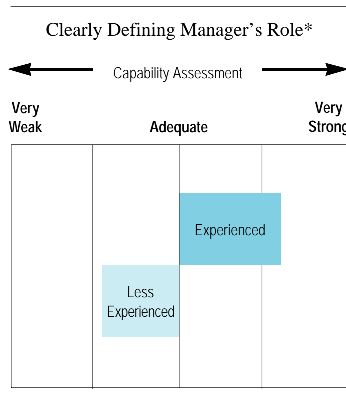
Experienced managers avoid open-ended investment posture. Yet firms have been known to stay in alliances long after the project has been proved untenable. Why? An unwillingness to face the media, stockholders, and their partners, until the situation becomes intolerable. Likewise,



experienced companies create clear strategic performance measures and link them to pay and investment. Compensation packages need to be entrepreneurial in structure and reflect the nature of the project and address the career derailment issue; this is often very different from the incentives appropriate for the parents. No one should forget the risks involved for an operating manager and his employees and their careers in joining an alliance. Lastly, alliance employees often become disgruntled if compensation rewards are not aligned with strategic performance.

7) Clearly Defining Roles

While successful companies avoid the typical committee-type decision-making process, they fix the responsibilities and authority of alliance managers and adopt a periodic struc-



tured review process. They also plan to build strong working and reporting relationships — external and internal — and foster loyalty to the alliance, not the parents.

These best practices are applicable for most types of alliances, although their relevance is greatest for shared-equity types of alliances (see Exhibit 9). Once an alliance moves beyond sharing resources to sharing ownership in some way, the importance of all these best practices becomes paramount. Equity not only makes the relationship more permanent, it makes outstanding issues more visible and more dangerous to ignore.

The Complexity Boundary and Guiding Principles

Some words of caution should be noted about what we call a "Complexity Boundary." We have found it necessary to tailor the approach to alliances based on organizational complexity — the nature and capabilities of a business. The priority of alliance skills and requirements differs across groups, and "mixed" alliances between "complex" and "simple" firms generally fail.

While all successful companies utilized the best practices discussed in this *Viewpoint,* in complex businesses, experienced management has found that it needs to further upgrade its alliance strengths and skills to achieve or maintain a high level of alliance performance. We will discuss this finding in-depth in a soon-to-be-published *Viewpoint* on "Tailoring Your Alliance Approach."

Some other "Guiding Principles" gathered from our experience and discussions with nearly eighty seasoned alliance executives:

- **Strength to Strength —** Alliances should always be formed on a "strength-to-strength" basis, not "strong-to-weak" or "weak-to-weak."

*Source: Survey of 250 companies covering 1,200 alliances and 80 interviews.

Two weak players are unlikely to pose much of a challenge to strong incumbents, and trying to improve a weak position with a strong partner most likely will result in the strong choosing the value-added part of the alliance (thereby improving its competitive strength, not the partner's).

- **Incremental Value Focus —** Making the pie big, not your slice. Do not place too much emphasis on learning your partner's skill instead of building skills incremental to combined entity. And avoid getting bogged down in how ownership will be shared until you've fully agreed on the nature and quantification of incremental value.
- **Slow Burn and Build —** We strongly recommend employing step-by-step relationship building to develop consensus and trust right from the start, thus avoiding loose and ragged partnership arrangements.
- **Structural Adaptation —** No rule is applicable across all situations. For instance, while a 50%/50% or 33%/33%/33% type of arrangement offers key advantages (such as a continued emphasis on meeting the partners' needs), it can also lead to inefficient allocation of work load on the basis of ownership share rather than advantaged capability. For example, attempts to spread production evenly across the Airbus consortium have led to the building of redundant capabilities in multiple countries rather than the rationalization of excess capacity.

Implications for Management

Management of companies in the U.S. must question the adequacy of the way it does business today. A new language of cooperation has emerged to redress the excesses of the 1980s. Many companies have already begun to position themselves in this new environment, but they need to "raise the level of their game" in the area of alliance execution by an order of magnitude. Otherwise, they will face a consortium of competitors without thebenefitof experience.

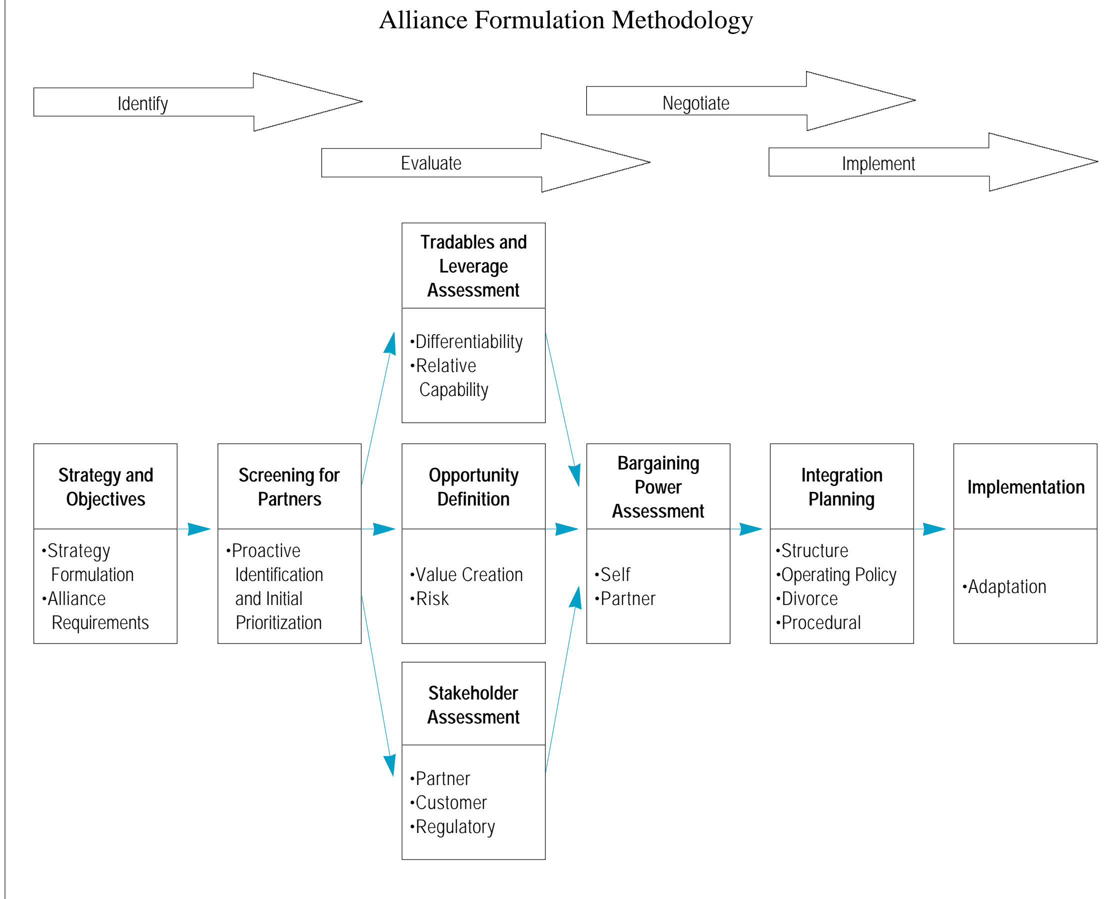
The important question is no longer, "Should we form a strategic alliance?" Now the

Exhibit 9

Relevance of Alliance Best Practices to Different Alliances

	Strategic	Alliance Continuum →				
	No Linkage	Shared Resource	Shared Funding	Cross-Equity	Shared Equity	Wholly Owned
1) Preparing a Realistic Feasibility Study	Low	Moderate	Moderate	High	High	High
2) Anticipating Business Risks and Mitigating Them	Moderate	Moderate	Moderate	High	High	High
3) Linking Budgets to Resources and Priorities	Low	Low	Moderate	Moderate	High	Low
4) Conducting Realistic Partner Assessment and Selection	Low	Moderate	Moderate	High	High	Moderate
5) Adopting Superior Resource Strategy/Planning	Low	Moderate	Moderate	High	High	Moderate
6) Coupling Investment and Rewards with Performance	Low	Low	Moderate	Moderate	High	Moderate
7) Clearly Defining Roles	Low	Moderate	Moderate	Moderate	High	Low

High Moderate Low



questions are: "What types of arrangements are most appropriate?", "How do we successfully manage these alliances?" and "Are we learning from the experience of others?"

Judging from the many recently announced partnerships in all industries, an increasing number of U.S. firms recognize that strategic alliances can provide growth at a fraction of the cost of going alone. In addition to sharing risks and investment, a well-structured, well-managed alliance can also support other goals, such as efficiency and productivity. Alliances provide a way for organizations to leverage resources. In short, alliances are a winning option available to a wide variety of industries.

We recommend a disciplined approach to alliances, to help propel your company to achieve superior results (see Exhibit 10).

In summary, we believe that less-experienced companies can accelerate their learning through actively embracing our alliance best practices, and as a result achieve the superior returns characteristic of experienced companies. Through such a disciplined approach, companies can successfully fill critical capability gaps and enhance their competitive position, while living within the realities of their resource constraints.

Booz·Allen & Hamilton is a global management and technology consulting firm, privately owned by its partners, all of whom are officers in the firm and actively engaged in client service. As world markets mature, and competition on an international scale quickens, our global perspective on business issues grows increasingly critical. In more than 75 countries, our 7,000 staff members serve the world's leading industrial, service, and government organizations. Each member of our multinational team has a single, common goal — to help every client we serve achieve and maintain success.

Our broad experience in the world's major business and industrial sectors includes aerospace, agriculture, automotive, banking, basic metals, chemicals, construction, consumer goods, defense, electronics, energy, engineering, food service, health care, heavy industry, insurance, oil and gas, pharmaceuticals, publishing, railways, steel, telecommunications, textiles, tourism, transportation and utilities.

With our in-depth understanding of industry issues and our expertise in strategy, systems, operations and technology, we assist our clients in developing the capabilities they need to compete and thrive in the global marketplace.

We judge the quality of our work just as our clients do — by the results. Their confidence in our abilities is reflected in the fact that more than 85 percent of the work we do is for clients we have served before. Since our founding in 1914, we have always considered client satisfaction our most important measure of success.

Booz·Allen & Hamilton has extensive experience assisting clients throughout the process of strategic alliance formulation, including vision definition, identification of critical capabilities, screening for partners, evaluating priority partners, negotiating and implementing alliances. We work together with our clients in three ways to help them improve their performance in alliances:

- **Process (Institutionalizing Alliance Capabilities):** Assisting clients build/improve their underlying capabilities in identifying, evaluating, negotiating, implementing and managing alliances — based on our best practices frameworks and methodology.
- **Content (Transactions):** Working together with a client on a specific alliance, at individual stages in the process or throughout the process.
- **Alliance Portfolio Renewal:** Revitalizing a client's portfolio of existing alliances by involving the client's current partners in an effort to improve performance of those alliances, by tuning them up and reinvigorating them.

We couple the understanding from our industry practices with our functional expertise in alliances and our geographical footprint to help our clients achieve superior results in their alliance efforts.

John R. Harbison, Vice President for Booz·Allen based in Los Angeles, specializes in strategic alliances, acquisitions and post-merger integration.

Peter Pekar, Jr., Ph.D., Visiting Associate Professor at the London Business School, is a recognized expert in the area of strategic alliance, with 30 years of business experience in forming and managing alliances. He has authored more than forty articles on alliances and related subjects and is Senior Advisor to Booz·Allen.

Other related *Viewpoints* in our Alliance series:

Cross-Border Alliances in the Age of Collaboration (1997)

– *An Asian Perspective on Cross-Border Alliances: Different Dreams*

– *Betting on Stability and Growth: Strategic Alliances in Latin America*

Institutionalizing Alliance Skills:

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