**9. Cooperative Strategy**

Strategic Alliances and Networks

Introduction

Cooperative forms of doing business have grown rapidly and continue to do so as firms of all sizes and nationalities in an increasing number of industries and countries perceive value in such arrangements.

The Rationale for Cooperation

1. Firms have limitations and inadequacies in coping successfully with a world of changing markets, technologies, economics and where vast investment funds are needed to supply new products with shortening life cycle.
2. Cooperative activity between firms has become a necessity in order to cope successfully with a dynamic environment characterised by high uncertainty and turbulence.
3. Different forms of cooperative strategy are used such as strategic alliances, joint ventures, dynamic networks, cooperative agreements, collective strategies and strategic networks to cope with successfully with the state of uncertainties.
4. All these forms of cooperative strategy are based on the fundamental concept of resource allocation efficiency.

Why is this revival of the popularity of cooperation coming about, since the obvious problem with cooperating with your competitor is that he may steal your secrets? How can cooperation be justified?

1. In the situation where it involves a cooperative agreement, its success depends on the existence of genuine trusting cooperation. The pay-off is only a single shot game in the sense that it is only for a certain time frame such as a certain project or work.
2. In the situation where the partners intend to work with each other over indeterminate period, the situation is different. Here it depends on building a trusting relationship and achieving synergies from cooperation. Furthermore the reputation will become an issue. If one partner decides to defect then its reputation will be questioned and it will be difficult to attract further partners in the future.
3. The dominant strategy is fundamentally cooperation among the partners. A cooperative strategy can only become successful when the competencies of multiple partners are combined to achieve a competitive strategy with competitive advantage.
4. The general features of cooperative strategy are:

* Existence of a genuine trust among the partners.
* Reputation of partners is to be guarded well.
* Forgiving cooperative strategies are found to be most effective.
* The superiority being difficult to imitate.
* Generate confidence and reduce uncertainty.
* Cooperative learning takes place e.g. in joint ventures, collaborations and consortia.
* There is skill substitution e.g. in virtual corporations, distributor agreements, networks, keiretsu.

The Motivation for Cooperation

1. To achieve with one’s partner, economies of scale and of learning.
2. To get access to the benefits of the other firm’s assets, be they technology, market access, capital, products or manpower.
3. To reduce risk by sharing it, notably in terms of capital requirements, but also often R & D.
4. To help shape the market e.g. to withdraw capacity in a mature market.
5. To enter the market speedily e.g. to be the first mover.

External Forces that stimulate the Growth of Cooperative Strategy

* Globalization of taste and markets
* The rapid spread and shortening life cycle of new technology and its products
* The development of opportunities for achieving major economies of scale, scope and learning
* Increasing turbulence in international economies
* A heightened level of uncertainty in all aspects of life
* Declining international trade barriers

The globalization of markets and technologies have demanded a sufficiently large volume productions to realise maximum economies of scale and scope and therefore to compete globally on a unit cost basis. Alliances have made this possible. Furthermore alliances help to reduce vulnerability of companies due to environmental uncertainty.

Internal Conditions

Firms will only enter into strategic alliances and networks, when their internal circumstances allow them to do so. They must have adequate resources and competencies in order to bring about satisfaction of complementary needs on the part of both partners and thereby lead to competitive advantage. There are many forms of resource dependency that provide the internal motivation for cooperation:

* Access to markets
* New technology
* Access to special skills
* Access to raw materials
* Belief that an alliance would be less costly than running and financing an integrated company or would provide strong protection against takeover predators or the best way to limit risk or to achieve a desired market position faster than by any other way.
* Achievement of speed in order to capture opportunities.

Strategic Alliances

Strategic alliances are partnerships between firms whereby their resources, capabilities and core competencies are combined to pursue mutual interests in designing, manufacturing or distributing goods or services. An important attribute of strategic alliances is that they allow firms to leverage their resources. Strategic alliances are explicit forms of relationships between firms and they come in three basic forms:

1. Joint venture - two or more firms create an independent company by combining parts of their assets. JVs are effective in establishing long-term relationships and in transferring tacit knowledge, an important source of competitive advantage. Commonly, partner firms own an equal percentage of a joint venture’s equity.
2. Equity strategic alliance - partners own different percentages of equity in a new venture. e.g many foreign direct investments.
3. Non-equity strategic alliance - formed through contractual agreements given to a company to supply, produce or distribute a firm’s goods or services without equity sharing. Other types of cooperative contractual arrangements concern marketing and information sharing.

The Consortium - a distinct form of strategic alliance in that it has a number of partners and is normally a very large-scale activity set up for a very specific purpose and usually managed in a hands-off fashion from the contributing shareholders. Con sortie are particularly common for large-scale projects in the defence or aerospace industries where massive funds and a wide range of specialist competencies are required for success.

Selecting a Partner

One of the keys to successful alliance must be to choose the right partner. This requires 3 basic factors to be taken into consideration:

1. The synergy or strategic fit between the partners in the sense that the alliance has or is capable of developing a clearly identifiable source of sustainable competitive advantage such as to attain economies of scale or scope or to reduce transaction costs.
2. The cultural fit between them in the sense able to enable cultural adaptation to take place and lead to the most successful alliance;
3. The existence of only limited competition between the partners in the sense as not to become too competitive against each other so that their stability will be affected.

The Management of Alliances

For successful management of alliances, there must be:

* Commitment by the partners.
* Cumulative trust must prevail.
* Cultural sensitivity is necessary to ensure cultural compatibility.
* A good dispute mechanism is necessary.
* An effective system for disseminating alliance information widely within the partner companies is important to ensure learning among the partners.
* Procedure for moving out of the alliances should be established at the outset of an alliance.

Alliance Evolution

An alliance must continue to evolve or else it will result in strategic decay. Important conditions for evolution are:

1. there must exist a balanced benefits between the partners;
2. strong bonding factors must be established;
3. new projects are regularly developed between the partners; and
4. constant learning is adopted by the partners.

**Strategic Networks**

Strategic networks differ from alliances in that they generally involve a lower level of interdependence between the members and the learning factor is rarely so important. Members provide their own skills, and leave other members to provide theirs.

The Nature of Strategic Networks

The network is very loosely used to describe any relationship between organisations. It generally exists for reasons stemming from resource dependency i.e. one network member provides one function, which is complementary to and synergistic with the differing contribution of other members of the network and provides other members with privileged access.

There is greater autonomy and choice among members. The relationships among firms are stable and can basically play the same coordinating and development function as intra-organisational relations. Through relations with customers, distributors and suppliers a firm can reach out to quite an extensive network. Such indirect relationships may be very important. They are not handled within the transaction cost approach.

Networks of whatever type arise for a number of distinct reasons:

* to reduce uncertainty
* to provide flexibility
* to provide capacity
* to provide speed to take advantage of opportunities that might not exist for long and may require a fast response
* to provide access to resources and skills not owned by the company itself
* to provide information

Power and Trust in Strategic Networks

Power and trust are the factors that dominate network relationships.

Power refers to 5 resources:

* economic base
* technologies
* range of expertise
* trust
* legitimacy

All network members will not have the same degree of power, and it is the linkages between the members and their respective power over each other in causing outcomes, that determine the culture of the network. Members in networks are free to enter, exit and reposition themselves. They are not static closed bodies. Their demand is dependent on the contribution other members believe they can make to their projects and that such network activity would strengthen the competitive position.

Trust and reputation are most vital in networks. Without trust the cooperation would wither away. Therefore it is the perceived quality of relationships in networks that matters but not the quantitative measures that cannot easily be applied.

Types of Strategic Networks

Three types are identified:

1. The internal network - activities are carried out within the firm and then ‘sold’ to the next stage of the value chain at market prices with the purchaser having the right to buy externally, if he can get a better deal. The activity may also in turn develop third party clients external to the firm.
2. The stable network -the film employed partial outsourcing to increase flexibility and improve performance, with a smaller base of permanent employees.
3. Dynamic networks - composed of lead firms who identify new opportunities and then assemble a network of complementary firms with the assets and capabilities to provide the business system to meet the identified market need. They are also known as ‘Hollow corporations’ in the sense that the entrepreneur lacks the capacity to carry out the range of necessary activities from its own resources.

The Equal Partner Network

In all equal networks, power relationships are varied and constantly shifting with the fortunes of members. Equal partner network can change according to changing market opportunities and often a different lead partner. It implies great flexibility and an ability to respond to changing environment but it lacks the permanent brain and central nervous system to ensure its combative ability. It is just a group of mutually aware capabilities than an actual organisation form.

An Overview of the Network

An attractive characteristic of many networks is that they help members to achieve increased global reach at low cost and with minimum time delay. They are flexible in their membership and able to respond rapidly to changing environmental situations. In an increasingly turbulent world, they reduce uncertainty for their members. They enable synergies between members to be captured and provide the conditions for the achievement of scale and scope economies through specialization. They are also good vehicles for the spreading of information and all forms of market intelligence. Under conditions of trust between members, they may also reduce traction costs, in contrast to vertically integrated companies with internally competitive cultures. Globalisation of markets and technologies have led to widespread growth of cooperative activity as a necessary strategy, if firms with limited financial strength, focused competencies and limited ‘global reach’ are to be able to compete in global markets.

Conclusion

Cooperative strategy, whether in the close form of strategic alliance or the more loosely-coupled form of networks, requires attitudes and approaches to management quite distinct from those found in hierarchies. It generally emerges when a company finds itself unable to cope with a global or other challenge, because of limitations in its resources and competencies and seeks an ally to reduce its vulnerabilities. Where this new mode of organising its business is approached, flexibly and sensitively by the partners enduring, successful and mutually beneficial relationships can be created and maintained. The future of these more flexible organisational forms as exemplified in alliances and networks is likely to be bright. Such arrangement will not survive, however, if partners play power politics with each other, show lack of commitment, distrust and lack of integrity and do not make very positive steps to deal with the cultural differences between the partners that will almost inevitably exist. It is these latter mishandled situations that have led to the reported 50% failure rate of recent alliances. The need is to understand the key factors for success in managing alliances as competently as the lessons from a management theory in handling integrated hierarchical corporations. They are as different as the contrast between giving orders from a position of authority compared with developing a consensus for action in a community of equals. Only when this difference is appreciated and translated into changed behaviour will the failure rate of cooperative arrangements begin to decline.

Source: *Cooperative Strategy* - Strategic Alliances and Networks by David Faulkner.