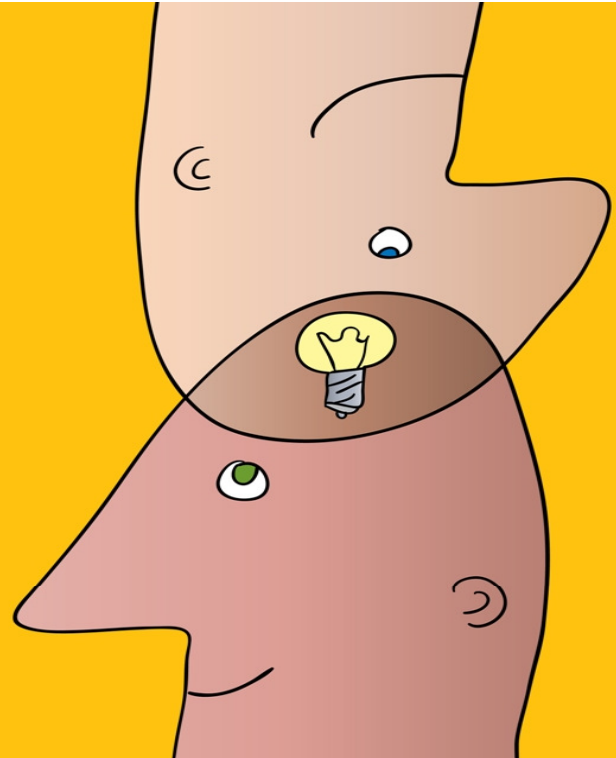


Alfred Griffioen

# The alliance effect



Six guidelines for a successful collaboration or partnership

# The alliance effect

## Foreword

Collaboration between companies is becoming increasingly important. Truly new products generally emerge through partnerships only, simply because companies, if left to their own devices, tend to stick to their available knowledge. Companies that do not join forces with complementary partners, even if their customers would prefer that they do, are letting an opportunity for additional profits slip by. Shareholders value new collaborative ventures and will reward them through stock price advances.

However, the greatest hindrances to collaboration reside within the organisation. I was personally able to contribute to fleshing out the collaboration between Douwe Egberts and Philips that resulted in the Senseo coffeemaker. The concept was originally devised by Douwe Egberts, yet it could only acquire its massive impact on household coffee

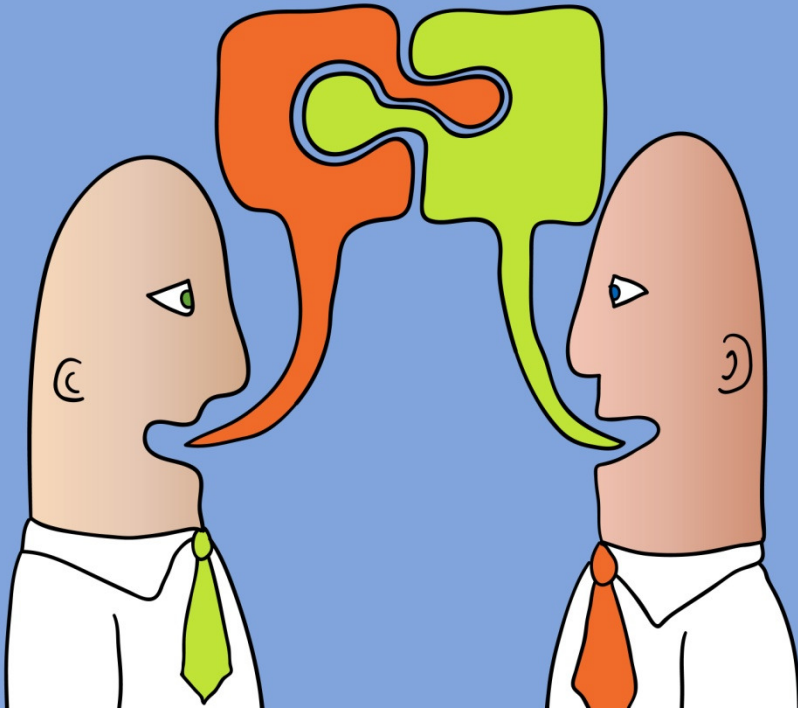
consumption thanks to the technological know-how and distribution channels offered by Philips. Even though the benefits of this alliance were clear from the start, it still took quite a bit of people management to get the personnel of the two organizations to really cooperate.

Not all collaborative ventures will achieve an impact on this scale. Nevertheless, it is important to embark on any partnership or alliance with full deliberation. How does one go about it? This booklet offers a practical guide.

Cor Boonstra

former Board of Directors Chairman  
Sara Lee/DE and Philips





## Six guidelines for a successful collaboration or partnership

1. Connect with your strategy
2. Find a win-win business model
3. Create a flexible contract structure
4. Nurture the relationship
5. Maintain and benchmark your alliances
6. Make deliberate use of networks

# 1.

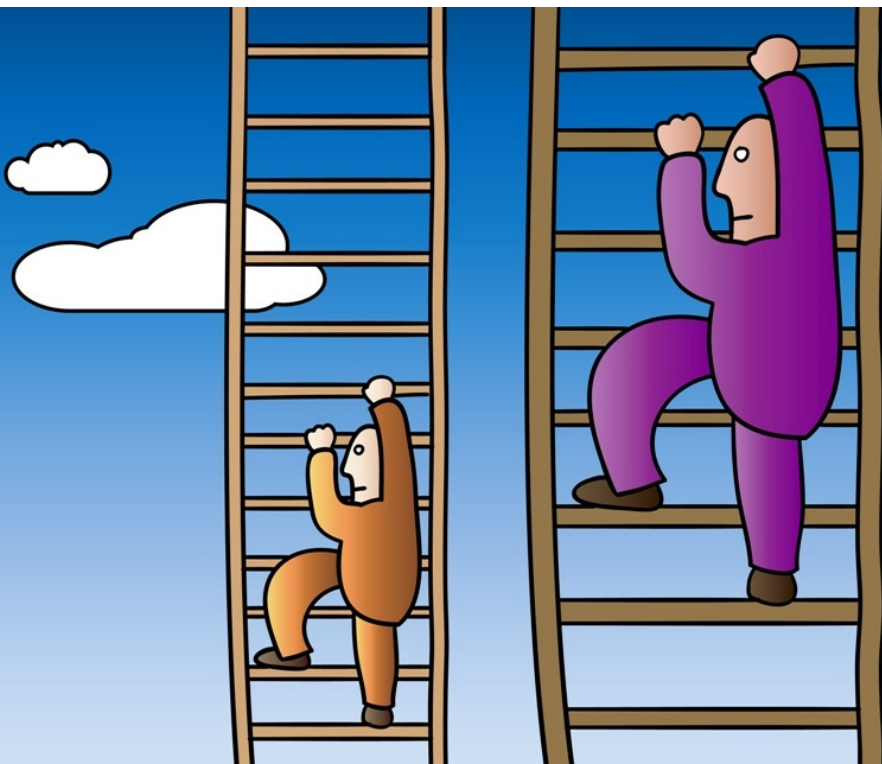
## Connect with your strategy

Distinctive quality is the foundation of every company's profit. This distinction may be owing to a unique product or service, or to the relationship that you manage to build with your customer, and can either be supported by your brand or not. Your distinctiveness means that you cannot easily be played off against your competitors, which results in higher profit margins. Alternatively, you can develop a distinctive cost structure that enables you to draw more profit from the same transactions.

The most dominant development in recent decades to affect the way consumers and enterprises do business is undoubtedly the far greater availability of information. Consumers, companies and public entities are increasingly aware of what the market offers and are finding it increasingly easy to compare products and suppliers. It takes just a few mouse clicks and telephone calls to satisfy their needs, drawing on suppliers from across the world. At the same time, it is easier than ever for your competitors to discover your plans, suppliers and work methods.

As a result, companies are forced to critically assess their own distinctive potential and to build and maintain their own specialism. Is that in product or services development, resulting in patents or exclusive know-how? Or are you relevant to your client mainly for the reach of your portfolio, distribution channels or marketing communications? In any case, cost benefits have become more transient than ever.

Since one cannot be strong on all fronts, you will need to pursue other avenues. Entering into collaboration with another company can be a way of procuring the competencies you lack, or of consolidating a set of existing competencies. This requires self-examination, market knowledge and an open mind.



Partnerships and alliances contribute to shareholder value in several ways. They first of all offer access to competencies in a much faster way than if you were to develop these yourself. This reduces the payback period of new ventures, thus reducing the risk. The required capital is moreover lower since your partner will shoulder part of the investment. This impacts the Return on Investment as well as on the risk of getting stuck with wrong investment choices. Finally, a partnership opens doors to new growth markets and hence to investment opportunities which would not emerge within the scope of a single company.

Research conducted between 2000 and 2002 into almost 900 announcements of alliances by listed companies revealed that the stock price increased by 3.8 percent on average on the day of the announcement. Two days later, this figure still stood at 2.5 percent. The price increase was largest in high-tech sectors and for smaller companies that entered into an alliance with a bigger company<sup>1</sup>.

A partnership can be viewed an intermediate form between an open market and the bundling of activities within a single company.

Organisation form	Market	Alliance	Company
Collaboration mechanism	Transaction	Agreement/ joint venture	Merger or take-over
Features	<ul style="list-style-type: none"> <li>Agreement with a clear scope</li> <li>Limited mutual dependency</li> <li>No separate operational costs</li> </ul>	<ul style="list-style-type: none"> <li>Open-ended contract</li> <li>Mutual dependence to achieve goals</li> <li>Parties remain separate companies</li> <li>Shared decision making</li> </ul>	<ul style="list-style-type: none"> <li>One single company</li> <li>Control over all resources</li> <li>Internal operational management</li> <li>Option of divestiture</li> </ul>

## 2.

# Find a win-win business model

The core of every collaboration is the business model, rooted in the question: what is the added value of the combination of these parties? In case of a partnership, this value is created by combining activities of two businesses in the chain in order to create a third, more valuable product or service. The second step is to turn (part of) that added value into revenue, to be shared between the parties.

There are two important routes towards sustainable competitive advantage. The first is to have a unique product that others cannot copy or imitate easily. This can be achieved by combining the knowledge of two companies to develop a product protected by patents, designs and model law or copyright. This occurs for example in the pharmaceutical industry in the development of medicines, as Pfizer does with biotech companies. Other examples can be found in the ICT industry for the development of new software.

The second route is to enhance your relevance for your customer base. Companies can strengthen each other by jointly offering a broader portfolio, by guaranteeing that each other's products are compatible, or by combining their networks, as for instance telecom operators and airlines often do. You can also enhance your relevance by expanding your presence in terms of shops and other sales outlets. Franchising is a form of partnership that can contribute effectively here. Joint marketing and co-branding are ways of making your brand more relevant through communication. Madonna and H&M have demonstrated the effectiveness of this strategy.



When creating value, you also need to distribute this value in a way that creates a win-win situation for both parties. This should preferably be achieved in as transparent a manner as possible, and consistent with the efforts performed by the two parties. A sound method to employ is as follows:

- First compensate the direct expenses incurred by each of the parties: purchasing, direct personnel expenses and production facility expenses, as far as possible applying the prices which would also be charged elsewhere.
- Objectify the value of sales efforts, use of patents, unique production facilities etc., and calculate a premium for the risks run by each party. Compensate this value for each party.
- If necessary, correct for financing costs and tax benefits resulting from the collaboration.

Finally, only discuss the money that subsequently remains. Share this equally, proportionate to the input, or reward the initiative taken to establish the partnership. The balance of power between the parties will become an issue here, but remember that every party must win in an alliance, or he will quit the alliance sooner or later.

Also carefully consider newly created value such as copyright, patents and goodwill. A sound arrangement for patents is that both parties can use them within certain restrictions, but this arrangement must be made properly. You should also consider what happens with a shared brand name if the collaboration should end.

# 3.

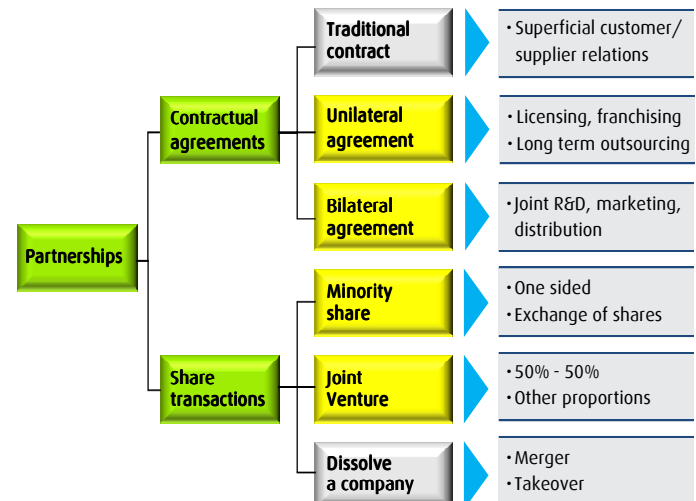
## Create a flexible contract structure

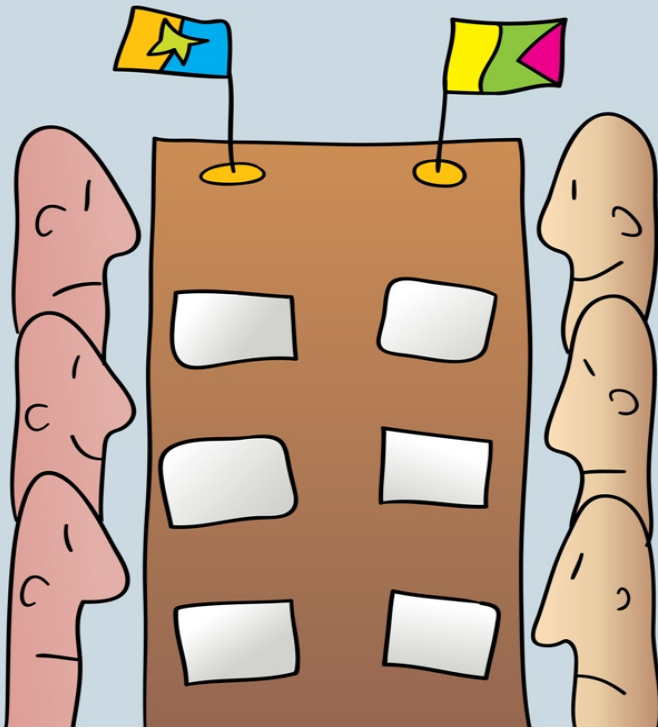
A collaboration between two or more parties will eventually be established in the form of an agreement. But even before you start talks with your partner, it is important to consider possible legal aspects.

There are three important moments at which the advice of a lawyer or other contract specialist should be enlisted:

- When formulating your own strengths, competencies and resources: in how far are the knowledge, brands or documents registered and protected? Are there proper arrangements in place to maintain the confidentiality of knowledge that cannot be protected?
- When starting talks with another party: should you draw up and sign a confidentiality agreement? What should such an agreement reasonably cover? And to what extent is such an agreement enforceable?
- When elaborating the collaboration in a contract: which legal form should you choose? What do you and don't you arrange in the contract? To what extent do you take account of new possibilities and patents?

An important choice when fleshing out an alliance is whether it is formed through a contractual agreement or as a shares transaction (as in a joint venture). And there are various options within both variants.





In all four instances (unilateral or bilateral contract, minority stake or joint venture), the goal for the companies involved is to find a way to have access to valuable resources owned by the partner, without losing control over one's own resources. The optimum choice will depend in part on the uniqueness of each party's contribution. For example, if the other party can easily copy or imitate your contribution, but you cannot use his patents or customer portfolios, then taking a minority stake is one way to nevertheless recoup part of the value that you are contributing.

In the collaboration between Philips and Douwe Egberts with regard to the Senseo coffeemaker, the parties chose the form of a (bilateral) agreement. This was an obvious choice, since both parties have their own production and sales systems. Philips' sales channels include chain stores for electrical equipment, while Douwe Egberts mainly sells through supermarkets.

In its collaboration with LG to produce LCD screens, Philips chose to establish a joint venture. Both partners contributed knowledge, and the production plants had yet to be built. Thus a new company, separate from both partners, was an ideal form. Philips and LG could continue to use their own sales channels, but this did not pose much of a risk to either party.

Be aware that the resources and goals for each party can change, as well as the external circumstances. A flexible contract structure, drafted with the desired long-term outcomes in mind, will help parties to continue the collaboration.

# 4.

## Nurture the relationship

In a contract, the parties record promises and obligations regarding the future performance of certain activities. This is complemented by the need to fulfil certain promises in a social context: the relationship. The contract and the relationship reinforce each other. Discussing the contract means building the relationship. And within that relationship it may be easier to balance out certain matters than in a contract: “Even if you don't make your top expert available, since you will solve any last hitches, then I will go along with that.” This works so long as the partner is considered trustworthy, and this trust consolidates through the parties' further interaction.

Trust is generally formed by three components: shared values, commitment, and communication.

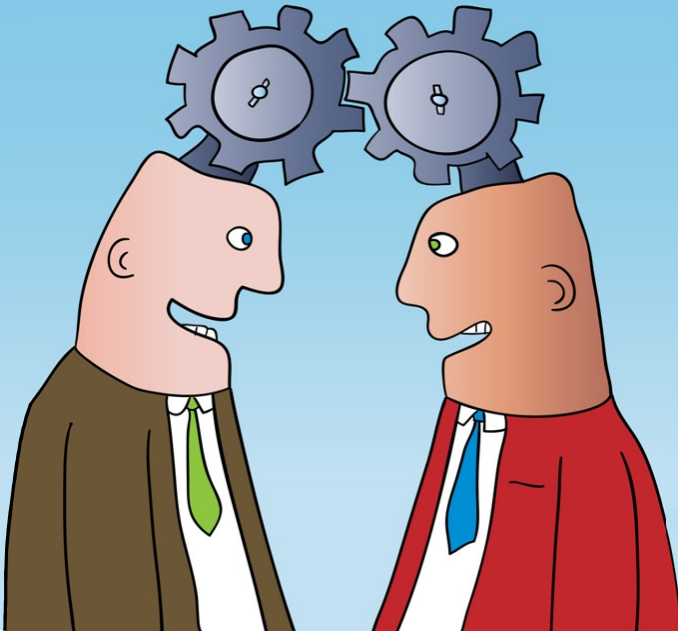
It is first of all important to assess whether values are shared, both at executive level and at work floor level.

These values pertain to matters such as:

- cooperation
- fulfilling agreements
- value of the contract
- manner of communication
- manner of supervising personnel.

Commitment to the partnership is the second component: is the managing director or CEO personally involved, and are arrangements implemented quickly? Trust is generally won through small steps at a time, for instance through the timely delivery of documents.

The third component is communication: is information shared rapidly, and is there a picture on both sides of the equation of what goes on behind the screens? Of course you needn't share all information, but it is worthwhile to also share non-public information, for instance about internal troubles, even if this is of no consequence to the other.



As soon as an alliance fails to deliver the projected results, it is important to gain an objective insight into the cause. Is the failure due to the cooperation, or to a change in external circumstances? Does it affect the value created through the partnership, or only the distribution of this value between the partners? Mapping out these factors will identify a number of possible causes, each implying various corrective measures<sup>2</sup>.

Upon entering an alliance, it is wise to make arrangements with respect to its possible termination. This creates a firm and clear framework, within which the partners can cooperate more openly.

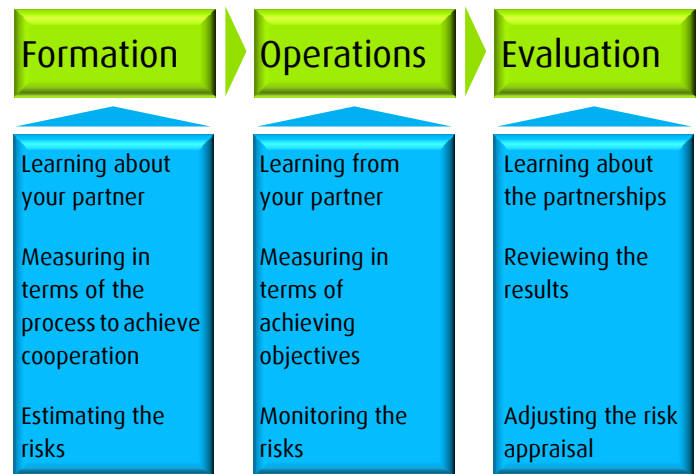
		Source of the problem	
		Internal	External
Effect on the collaboration	Efficiency (value creation)	Poor cooperation: <ul style="list-style-type: none"> <li>• Share insights</li> <li>• Consult to improve interface and management</li> <li>• Joint learning to gain better understanding of tasks and competencies</li> </ul>	Deterioration of conditions and benefits: <ul style="list-style-type: none"> <li>• Share market knowledge</li> <li>• Joint analysis of how to respond to changed situation</li> <li>• Modify JV structure or continue with other expectations</li> </ul>
	Distribution (allocation of value)	Changed insights and interests, perceived imbalance: <ul style="list-style-type: none"> <li>• Test partner's motives and behaviour</li> <li>• Stricter monitoring of results</li> <li>• Reopen negotiations or terminate alliance</li> </ul>	Change in balance between the partners: <ul style="list-style-type: none"> <li>• Joint analysis of how conditions change partners' benefits</li> <li>• Modify the profit distribution key</li> </ul>

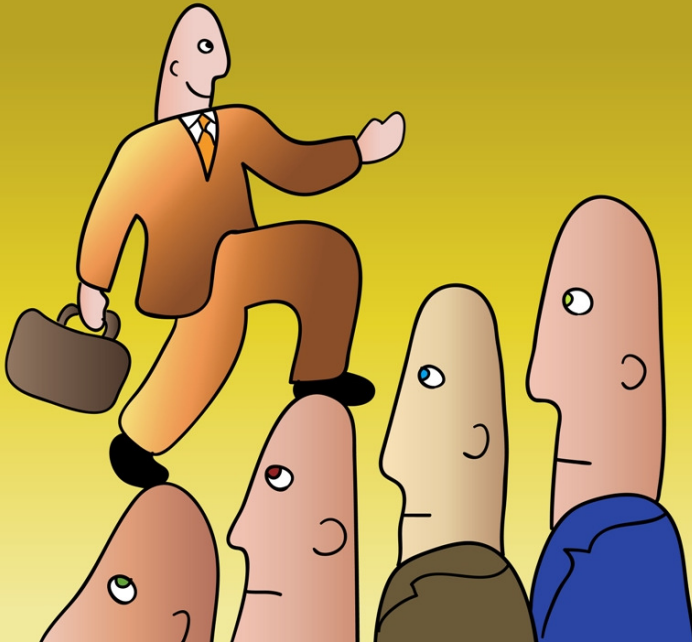
# 5.

## Maintain and benchmark your alliances

Each phase of the alliance process represents an opportunity to learn. In the formation phase you mainly want to learn about your partner. What is his strategy and what is he good at? In the operational phase it's more about learning from your partner. The evaluation phase is about learning about partnerships in general: what knowledge and skills have you acquired through the process that will help you do better in forging the next alliance? You can similarly identify a cycle for result measurements and risk management<sup>3</sup>.

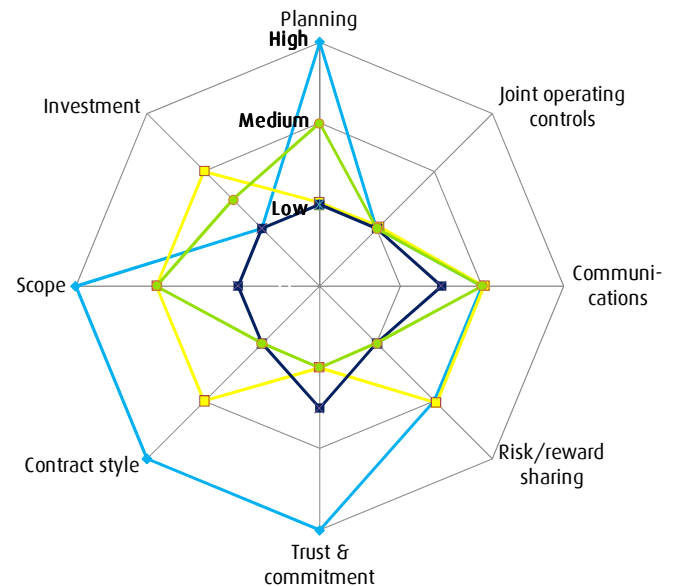
It is advisable to not see the collaboration or alliance as a fixed structure. By incorporating regular evaluation moments, internally as well as with the partner, you can introduce improvements and optimise the alliance.





A next step is to compare alliances. There are various ways to go about it; for instance, you can evaluate alliances in terms of their intensity. This can be performed with reference to eight aspects, including communication, investments, trust and risk sharing<sup>4</sup>. More intensive alliances can serve as reference example for less intensive alliances.

Category	Partnership component	Type I: Low	Type II: Medium	Type III: High
<b>Planning</b>	<ul style="list-style-type: none"> <li>• Style</li> <li>• Level</li> <li>• Content</li> </ul>	<ul style="list-style-type: none"> <li>• On ad hoc basis</li> <li>• Focus is on projects or tasks</li> <li>• Sharing of existing plans</li> </ul>	<ul style="list-style-type: none"> <li>• Regularly scheduled</li> <li>• Focus is on process</li> <li>• Performed jointly, eliminating conflicts in strategies</li> </ul>	<ul style="list-style-type: none"> <li>• Systematic: both scheduled and ad hoc</li> <li>• Focus is on relationship</li> <li>• Performed jointly and at multiple level, participation in each other's business planning</li> </ul>
<b>Joint operating controls</b>	<ul style="list-style-type: none"> <li>• Measurement</li> <li>• Ability to make change</li> </ul>	<ul style="list-style-type: none"> <li>• Performance measures are developed independently and results are shared</li> <li>• Parties may suggest changes to other's system</li> </ul>	<ul style="list-style-type: none"> <li>• Measures are jointly developed and shared; focused on individual firm's performance</li> <li>• Parties may make changes to other's system after getting approval</li> </ul>	<ul style="list-style-type: none"> <li>• Measures are jointly developed and shared; focus on relationship and joint performance</li> <li>• Parties may make changes to other's system after getting approval</li> </ul>
<b>Communications</b>	<ul style="list-style-type: none"> <li>• Non-routine</li> <li>• Day to day communication</li> <li>• Balance</li> <li>• Electronic systems</li> </ul>	<ul style="list-style-type: none"> <li>• Very limited, usually just critical issues at the task or project level</li> <li>• Conducted on ad-hoc basis, between individuals</li> <li>• Primarily one-way</li> <li>• Use of individual systems</li> </ul>	<ul style="list-style-type: none"> <li>• Conducted more regularly, done at multiple levels; generally honest and open</li> <li>• Limited number of scheduled communications; some routinisation</li> <li>• Two-way but unbalanced</li> <li>• Joint modification of individual systems</li> </ul>	<ul style="list-style-type: none"> <li>• Planned as part of the relationship; occurs at all levels; sharing of both praise and criticism</li> <li>• Systematised method of communication; communication systems are linked</li> <li>• Balanced two-way communication flows</li> <li>• Joint development of customised electronic communications</li> </ul>
<b>Risk/reward sharing</b>	<ul style="list-style-type: none"> <li>• Loss tolerance</li> <li>• Gain commitment</li> <li>• Commitment to fairness</li> </ul>	<ul style="list-style-type: none"> <li>• Very low tolerance for loss</li> <li>• Limited willingness to help the other gain</li> <li>• "Fairness" is evaluated per transaction</li> </ul>	<ul style="list-style-type: none"> <li>• Some tolerance for short-term loss</li> <li>• Willingness to help the other gain</li> <li>• "Fairness" is tracked year to year</li> </ul>	<ul style="list-style-type: none"> <li>• High tolerance for short term loss</li> <li>• Desire to help the other party gain</li> <li>• "Fairness" is measured over life of relationship</li> </ul>
<b>Trust and commitment</b>	<ul style="list-style-type: none"> <li>• Trust</li> </ul>	<ul style="list-style-type: none"> <li>• Trust is limited to belief that each party will perform</li> </ul>	<ul style="list-style-type: none"> <li>• Partner is given more trust than others, viewed as "most"</li> </ul>	<ul style="list-style-type: none"> <li>• There is implicit, total trust; trust does not have to be</li> </ul>



Comparison of the intensity of the collaboration on eight aspects and the results for four different alliance partners

# 6.

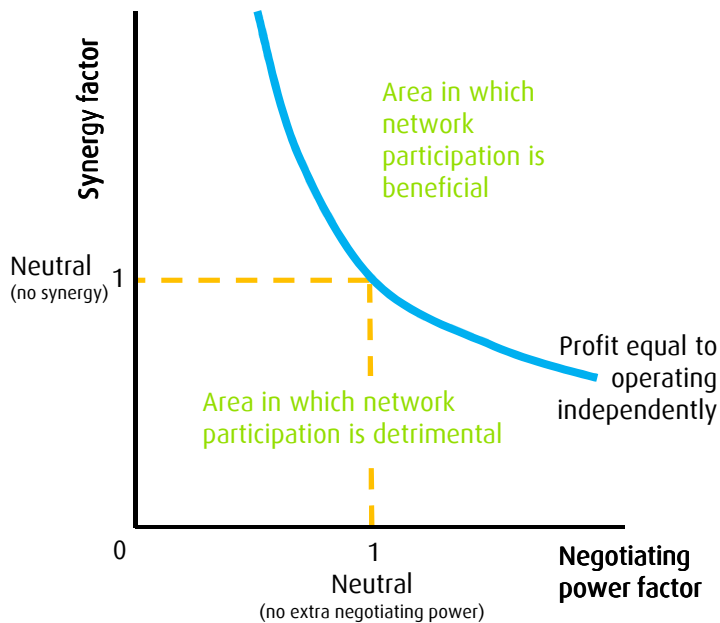
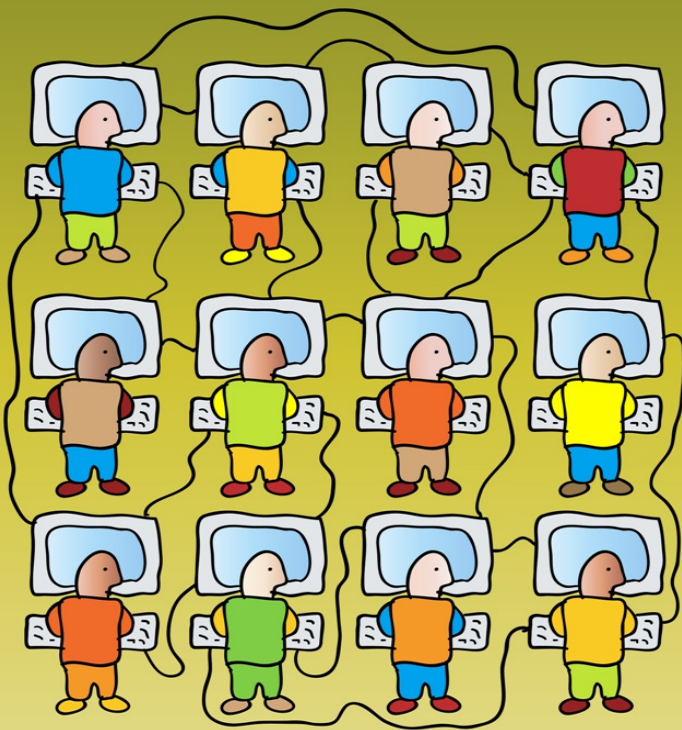
## Make deliberate use of networks

Company networks come in roughly two sorts. On the one hand you can have a group of comparable companies, sometimes even competitors, who have a common interest. That interest can be, for instance, campaigning against an amended legislation, or the collective purchasing of certain goods, or the standardisation of product specifications. Such networks are often open to every similar company, are clearly structured, and there is generally not a clearly leading party.

On the other hand you have networks of complementary companies, aiming for instance to create a new product or to achieve collaboration in the value chain. Such networks are often initiated by a single party, have a looser structure, and are only open to those that are invited to join. The networks most likely to succeed are those in which the contribution of all parties is comparable in size, but each has its own activity.

What is the value of participating in a network? That depends on the synergy that the companies manage to generate, and on the negotiating power of each individual company. The synergy of a network can sometimes be negative for the parties involved, for example if the collaboration restricts each other's possibilities. To the extent that a company's contribution is more essential to the creation of synergy, that company will be able to claim a larger share of the higher yield, as it will have greater negotiating power.

With a synergy factor of 1 (neutral) and a negotiating power factor of 1 (equivalent), the profit of operating within a network is equal to the profit that the company would make independently. At the upper right end of the curve, network participation is beneficial (high degree of synergy and/or negotiating power), and at the lower left end of the curve it is detrimental<sup>5</sup>.



Initiating a network seems to be one of the better ways of maximising one's control over that network. Recent research based on games theory has shown this to be true. Suppose that it would benefit a company to form an alliance with two other parties. The company then must choose between:

- Concluding an agreement with one of the parties, and then asking the other party to join
- Negotiating with both parties at the same time
- Waiting until the other parties jointly ask it to join.

Unless it is clear from the outset that the company is vital to the collaboration, taking the initiative with first one partner delivers the greatest amount of negotiating power<sup>6</sup>.

# About the author



## Literature:

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- <sup>4</sup> Douglas M. Lambert, Margaret A. Emmelhainz, John T. Gardner, So you think you want a partner, 1996
- <sup>5</sup> Benjamin Gomes-Casseres, Alliance strategies of small firms, 1997
- <sup>6</sup> Annelies de Ridder, The dynamics of alliances, A game theoretical approach, 2007

Illustrations by Miroslaw Piepzyk

Alfred Griffioen first acquired experience in helping companies collaborate in his role as sales manager and marketing manager with telecom company KPN, and later as business development manager with an international contracting and installation company. He has been advising companies since 2006, first as manager at a strategy consultancy and now as partner of Alliance experts, which is specialised in mediation and consultancy in the field of strategic collaboration and alliances.

For more information please visit:  
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