

# **How to build alliance capabilities**

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## HOW TO BUILD ALLIANCE CAPABILITIES

*Developing expertise through multiple alliance management practices*

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## INTRODUCTION

During the last decade or so, many firms have been forming strategic alliances at an impressive clip, and they are now faced with the coordination of scores of alliances, if not many more. Firms such as Cisco and Motorola enter into 50 to 100 new alliances each year. Large firms like Pfizer and Eli Lilly are vying to be the ‘preferred partner’ in the pharmaceutical industry.<sup>1</sup> Philips, the Dutch electronics and medical equipment firm, currently engages in over 1,000 alliances. By some forecasts, alliances will make up as much as 50% percent of company sales in the next few years.<sup>2</sup>

As firms develop more complex alliance portfolios, executives’ attention has shifted from the design and management of individual deals – always an important concern – to the broader question of how they can develop the necessary firm-wide capabilities for forming, implementing, and terminating their collaborative ventures.

Many firms have relied on learning-by-doing as their chief source of capability development. Dow Chemical and Corning, for instance, are legendary for cultivating alliance management capabilities through the informal accumulation of experience over the years. Not only have they had an enviable track record; alliances are central to their management processes, career tracks, and even cultures.

For others, it is simply not viable to develop alliance capabilities so patiently through experience. Too many companies must form a large number of relationships in very short order. Moreover, relying upon the trial-and-error learning approach that was initially found in manufacturing settings is often fraught with problems in the alliance context: compared to production activities, alliances have opaque performance metrics; the true causes of good and poor performance are hard to discern; and alliances are heterogeneous with respect to partners’ motives as well as management challenges, so the lessons learned in one alliance might not be appropriate for another.

Faced with these challenges, many firms are attempting a very different tack. They are pursuing a much more formalized process of managing alliances and developing alliance capabilities.<sup>3</sup> For instance, firms such as Hewlett-Packard and Eli Lilly have organizational units dedicated to alliances.<sup>4</sup> Other firms are devising knowledge management tools to capture and leverage best practices in a more disciplined manner by using databases or company intranets. Still others are opting for a variety of formal training programs to develop alliance managers or are turning to external experts for support.<sup>5</sup>

So how are firms actually engaging in these myriad practices? To understand the usage of these alternatives for alliance capability development and how they might

complement or substitute one another, we conducted extensive fieldwork at various companies in the US and Europe. We then did a survey of 192 firms across a broad range of industries (see sidebar).

Through this fieldwork and survey, we discovered four distinct ways that firms are seeking to build their alliance capabilities: (1) functional and staffing solutions; (2) tool-based solutions; (3) training solutions; and (4) third party solutions. We used the survey to benchmark companies' alliance practices, and we also examined how the most experienced firms and those with dedicated alliance functions were adopting these various solutions in different ways to enhance their alliance capabilities.

*\*\*\*Insert side bar about here \*\*\**

## **ALLIANCE MANAGEMENT PRACTICES**

The number and diversity of alliance practices firms were implementing was clearly evident. Take KLM Royal Dutch Airlines as an example. KLM wrote history by forming the first airline alliance when it in 1989 acquired 19.3% of Northwest Airlines. After obtaining anti-trust immunity, KLM and Northwest Airlines started to operate both companies' EU-US flights through their joint venture. Even though the initial KLM-Northwest deal was dissolved shortly after Alitalia joined in May 1999, KLM distilled lessons from this first relationship to make changes in subsequent alliances.

Like various other firms we interviewed, KLM had adopted and developed more formal practices over time to develop their alliance capabilities. To begin with, the experiences from their alliances with Northwest were shared among alliance managers in training programs.

With the growth of KLM's alliance portfolio throughout the 1990s came a need for improved coordination of their relationships, resulting in the creation of units in their Passenger and Cargo divisions specializing in alliance management reporting directly to the Board of Directors. They also implemented new practices in support of these units, ranging from in-house company courses to the development of joint business planning procedures. After KLM's merger with Air France, the combination holds a strong position on the North Atlantic markets in the Skyteam alliance.

By contrast, some firms like glass maker Corning make alliances succeed by relying on a set of principles embedded in the organizational culture; while Corning has eighty years of experience to rely on, clearly other firms have less favorable starting points to make alliances work quickly. The various practices that we observed in

our fieldwork clustered into four distinct categories (see Table 1, “Elements of Alliance Capabilities and Skill Development”):

\*\*\*Insert Table 1 about here \*\*\*

**Functional and staffing solutions** Some firms participating in our research have mandated individuals or entire business units to carry responsibility for and coordinate the firm’s alliance activities. For example, at the end of 1990s, GlaxoSmithKline’s management observed that all of their alliances were managed independently from one another. This meant GSK was unable to leverage upon its previous experiences or standardize its policies and procedures for these relationships. In order to share knowledge more effectively internally, steps were taken to consolidate skills that were available in the firm. Although alliance managers began to share knowledge informally, GSK subsequently decided to create an alliance department to disseminate experiences and stimulate the adoption of standard processes by managers throughout the firm. The Vice-President of Alliances heading the corporate group explained: *“Initially, alliances were managed individually. At that point, we primarily relied on exchanging best practices. However, as we reckoned alliances were a major contributor to the business development of our firm, we started building alliance competences; consolidating our knowledge did this. This way, we anticipated, we could develop the discipline called alliance management. ... We set up an alliance department through which institutional learning could take shape, in which knowledge could be developed and processes could be adopted more easily.”* GlaxoSmithKline was not an exception: 39% of the firms in our survey made use of an alliance department, 39% had a Vice-President of alliances, 73% had a staff specialist for alliances, and 48% employed dedicated alliance managers (see Table 2, “Knowledge Management Practices for Alliances”).

\*\*\*Insert Table 2 about here \*\*\*

**Tool-based solutions** Many of the firms in our research used a variety of tools to provide practical guidelines and encourage learning about alliances. Because these instruments often contain codified knowledge on issues in different stages of the alliance life-cycle,<sup>6</sup> the executive managing the alliance is not left alone in handling the business relationship as it evolves. Take Dow Chemical as an example. Dow consists of eight separate business units, each of which manage about 100 alliances, so the company has historically shied away from too much reliance on central coordination. However, in order to capture and disseminate their experiences more systematically, Dow has started sharing best practices. Specifically, they use the company intranet to make accessible and update best practices so employees can leverage and share insights from prior alliances. This substantially reduces the need for members in an alliance team to develop their skills from scratch. As our data suggest, many firms currently use this and other tool-based solutions: partner

selection protocols are used by 49%, joint business planning by 51%, codified best practices by 36% and intranet by 47% of survey respondents.

**Training solutions** The third category of alliance management practices consists of training programs, which can be in-house or organized externally. Back in the Fall of 1998, Eli Lilly decided to start a firm-wide program aimed at establishing itself as the preferred partner in the pharmaceutical industry. Under intensive competitive pressure and facing the need to fill gaps in its drug pipeline, Lilly defined an Alliance Management Process (LAMP) and established 'The Office of Alliance Management' (OAM) to systematize its alliance management approach. Under supervision of the OAM, the company trained over 500 of its employees in one year. Lilly had the vision that alliance management could become a key competitive strength. As in the case of Dow Chemical's programs, Lilly's partners were invited to join in the firm's alliance training programs.<sup>7</sup> Other firms such as Sun and Motorola conduct internal training programs for executives, and 20% of the firms in our survey launched such internal training initiatives. A smaller number of firms, 14%, held specific programs dedicated to nurturing cultural awareness skills, and the largest number of firms, 34%, relied on courses by external experts.

**Third party solutions** Finally, some firms in our research turned to external experts to access their specialized expertise. For instance, KLM uses external consultants to improve the alliance management skills of its employees. It has also used an outside consultancy to help derive key lessons from the alliance with Northwest. The support such external consultants provide can also complement some of the alliance practices discussed above. As one example, the lessons that KLM's consultants distilled from the alliance with Northwest were shared using in-house training sessions organized by the consultancy. As table 2 shows, external parties also provide legal advice (38.6%), financial expertise (32.5%) and, to a lesser extent, mediation services (4.8%).

## **COMPARING EXPERIENCED AND INEXPERIENCED FIRMS**

As we have emphasized above, the alliance management practices a firm pursues or chooses not to utilize are going to be a function of the experience base the firm currently has. It is also the case that these supporting decisions, rather than experience alone, will ultimately contribute to the firm's alliance capabilities and performance. In order to compare experienced and inexperienced, we separated firms that formed less than 15 alliances over a 5 year period (1997-2001) with those that formed more than 15 alliances.

Our survey results indicate that experienced firms rely more heavily on most of the knowledge management practices discussed above. Of the four categories of

solutions, experienced firms make more use of all but one, i.e. those provided by third parties (see Table 3, “Comparing Experienced and Inexperienced Firms”).

*\*\*\*Insert Table 3 about here \*\*\**

To compensate for their lack of alliance management skills, inexperienced firms in our survey made greater use of external experts. Firms seek to compress their learning by using external consultants to gather best practices and benchmark their performance, for example. A manager at Dow Chemical noted: *“Where you can jumpstart is by leveraging in and gathering knowledge from external sources in order to ease the management of the first alliances. In this way, firms with little experience can jump the alliance learning curve by adopting knowledge from other firms that already have experience; this way, it does not necessarily have to be an internally supported process.”* Similarly, inexperienced firms made greater use of mediators than their more experienced counterparts.

Yet, there is another notable difference between experienced and inexperienced firms. Inexperienced firms tend to use a staff specialist for alliances to compensate for lack of coordination and know-how rather than building an alliance department. Given the costs involved in setting up a department dedicated to alliances, only firms with extensive alliance activities are likely to find the benefits to offset incurred costs. Of the inexperienced firms in our survey, only 23% made use of an alliance department to oversee their alliance activities, while 80% relied on staff specialists to take responsibility for alliance management.

On all other counts, experienced firms can be characterized as trying to access and share knowledge via many routes other than simply learning-by-doing. For example, 67% used a partner selection protocol and 63% used the intranet as an alliance resource to share knowledge. As another example, when it comes to training solutions, as much as 30% relied on their own in-house company course, compared to 11% for inexperienced firms.

It is evident that many firms do much more than just rely on previous experience: they actively share and develop their alliance capabilities deploying a diverse set of alliance management practices.

## **COMPARING FIRMS WITH AND WITHOUT AN ALLIANCE FUNCTION**

As a final way to examine how the different alliance practices work together, we examined how the firms that had an alliance function differed from those who did not implement this structural solution (see Table 4, “Comparing Firms With and Without an Alliance Function”). Such comparisons could be made for any one of the

15 individual management practices in our survey, but we focused on this one in particular given the attention it has received in recent years.<sup>8</sup>

*\*\*\*Insert Table 4 about here \*\*\**

Three interesting patterns stand out. First, we see that certain functional and staffing solutions appear to work as substitutes and others as complements. Less than half of the firms with an alliance function had a staff specialist for alliances, but the incidence of this role increased to nearly 90% for firms without an alliance function. By contrast, firms *without* an alliance function had a VP of alliances only 15% of the time, and 26% of them had managers dedicated to alliances. These figures rose to 75% and 82%, respectively for firms that had implemented an alliance function. Hence, firms with an alliance function tend to also assign a VP and dedicated alliance managers whereas firms without an alliance function tend to rely solely on staff specialists. For the latter group of firms, the costs of coordinating alliance activities are likely to be lower than the costs of assigning an extensive office and group of dedicated managers.

Second, the data suggest that tool-based solutions and training solutions are important complements to the alliance function. In the case of tool-based solutions, the incidence of the individual tools more than doubled for three out of the four (i.e., partner selection protocol, joint business planning, and intranet for alliance resources), and for firms with an alliance function, these tools were used in the vast majority of companies. The codification of best practices similarly increased markedly for firms adopting alliance functions (i.e., from 28% to 48%). Regarding training solutions, the incidence of internal alliance management training programs increased four-fold for firms that implemented alliance functions. However, firms lacking an alliance function tended to rely fairly heavily on courses by external experts (32% vs. 39%) and were more likely to focus efforts upon intercultural management programs.

Finally, firms with an alliance function tend to rely more on internally available knowledge than firms without an alliance function. For example, the survey results show how firms without an alliance function rely heavily upon consultants, lawyers, and other experts for assistance with their alliance activities, while the usage of these third party experts drops markedly for firms that build an alliance function. For instance, the usage of consultants drops from 40% to 31%, the usage of legal experts drops from 43% to 32%, and the usage of financial experts drops from 37% to 26%. Although roughly 8% of firms without an alliance function use mediators, we observed no firm with an alliance function relying upon third parties for mediation.

A number of these patterns apply to Royal Philips Electronics. Like the other firms we interviewed, it has an 'Alliance Office' that oversees its alliance portfolio. Since

Philips established this office approximately four years ago, the need for alliance specialists at the business unit level has gradually reduced. By internally servicing business unit managers, the Alliance Office provides them with useful tools to assist them in forming and executing the alliances at hand. Having dedicated alliance managers who report to the Alliance Office and are responsible for one or a few alliances, the need for assistance from outside has also dropped.

## **MANY ROADS TO ROME: HOW TO BUILD ALLIANCE CAPABILITIES**

With the rising importance of alliances, firms increasingly turn their attention to fully exploiting the value of their alliances for good reasons. As the results of this study indicate, the way in which firms advance their alliance capabilities is quite diverse and changes over time as firms develop experience and adopt different alliance management practices such as a dedicated alliance function. There are a few final observations and recommendations to make.

**Experience isn't the only teacher** There are many other ways for companies to develop alliance capabilities than by accumulating experience and using a trial-and-error approach. External training, conferences, and third party consulting, for instance, can help firms overcome experience limitations. Moreover, firms have to decide how much to rely on informal means of developing capabilities versus more formal, deliberate means. Remember also that experienced firms make greater use of many of the knowledge management practices discussed; so rarely do firms rely purely on experience to develop capabilities. Essential is the willingness to learn, in order that the lessons from experience are captured and then shared deliberately.

**Different firms need different practices** There appears to be no such thing as a universally-optimal mix of alliance management practices. In analyzing the 192 firms involved in our study, there was no dominant or superior profile of practices used. In contrast, companies proved to use diverse sets of ways to develop alliance capabilities. For instance, small firms involved in our study were much more relying on third party solutions in contrast to large firms. Firms that adopted an alliance function added some practices and jettisoned others. The knowledge management practices we studied appeared to be tailored to companies' situations rather than 'one-size-fits all' solutions.

**Avoiding the 'superstitious learning' syndrome** Some firms can grow more confident, than competent, at managing alliances as their experience grows, particularly if their alliances are successful. Firms can fall victim to this problem of inappropriately applying lessons from one alliance to another, even if the underlying motives or management challenges of the collaborations are quite

different. The use of more deliberate learning approaches (e.g., tool-based solutions, training solutions, etc.) can help curb this problem because they help managers see how heterogeneous alliances are and how various alliances need to be managed differently.

**Alliance management practices are a means to an end** Related to the previous point, the various alliance management practices we have discussed are not designed to impose rigid standardization or corporate dictates, nor are they an objective in and of themselves. Rather, these practices are intended to be a means of improving management skills as opposed to being an end in itself. For instance, there is an analogy to strategic planning here: the mere fact that a firm has codified aspects of alliance management might not help as much as the processes of codifying and sharing knowledge inside the firm. We also have presented evidence that some of the alliance management practices work as substitutes to one another, and firms adopting certain solutions such as dedicated alliance units are able and willing to jettison other alliance management practices.

## **SIDEBAR**

### **Research Design and Methodology**

We conducted two types of research to understand what alliance management practices firms engage in to manage their alliances. We first interviewed executives at firms that were renowned for their alliance capabilities. These included such firms as GlaxoSmithKline, Oracle, Royal Philips Electronics, the Dutch flag carrier KLM, and Dow Chemical. Each of these executives reported extensively on their alliance management practices and the ways in which the firm sought to build alliance capabilities. Based upon the insights gleaned from these interviews, we designed and carried out a large-scale survey in order to gather data on the organization of firms' alliance management practices across a broad range of industries and firms in the US and Europe. In total, 192 firms were involved in the second stage of this research. Additional details on the survey items and other findings are available from the authors.

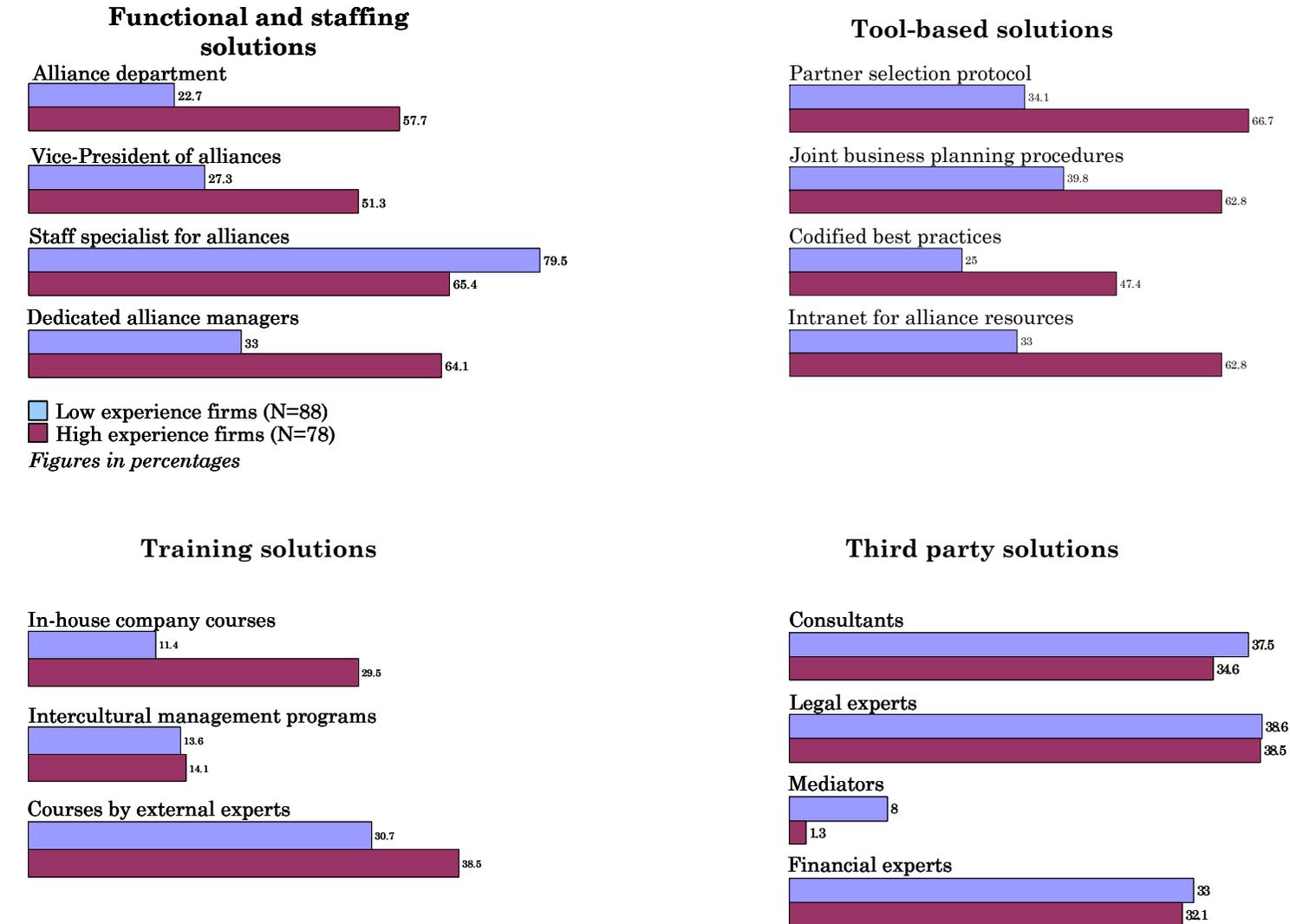
**Table 1 Elements of alliance capabilities and skill development**

<b>Types of Alliance Management Practices</b>	<b>Descriptions</b>
Functional and staffing solutions	Units or functions within units which are mandated with responsibility for managing and coordinating alliance activities within the firm
Tool based solutions	Instruments containing guidelines on alliance management issues within different stages of the alliance life-cycle
Training solutions	Training programs organized internally or externally to improve understanding of critical issues in alliance management for the employees involved
Third-party solutions	Outside experts who provide specialized content related, for instance, to conflict mediation, legal issues, financing, and alliance management

**Table 2 Knowledge management practices for alliances (average percentages)**

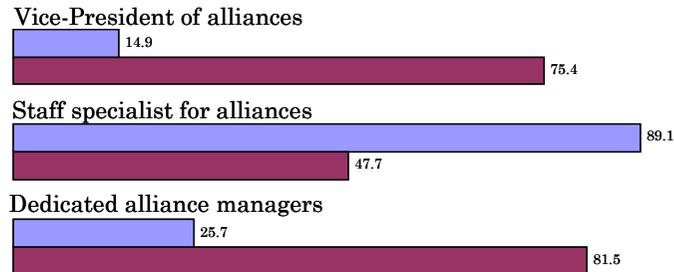
<b>Functional and staffing solutions</b>	<b>Tool based solutions</b>
Alliance department 39.2%	Partner selection protocol 49.4%
Vice-President of alliances 38.6%	Joint business planning procedures 50.6%
Staff specialist for alliances 72.9%	Codified best practices 35.5%
Dedicated alliance managers 47.6%	Intranet for alliance resources 47.0%
<b>Training solutions</b>	<b>Third party solutions</b>
In-house company courses 19.9%	Consultants 36.1%
Intercultural management programs 13.9%	Legal experts 38.6%
Courses by external experts 34.4%	Mediators 4.8%
	Financial experts 32.5%

**Table 3 Comparing Experienced and Inexperienced Firms  
(average percentages)**



**Table 4 Comparing Firms With and Without an Alliance Function  
(average percentages)**

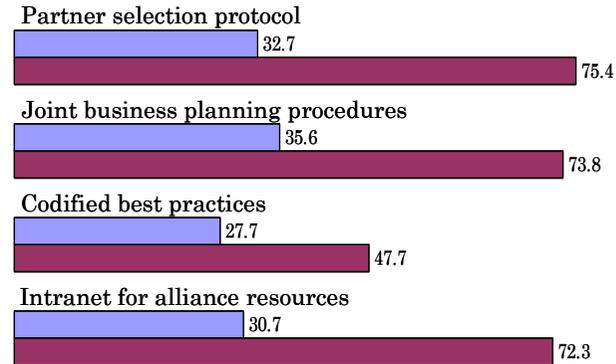
**Functional and staffing solutions**



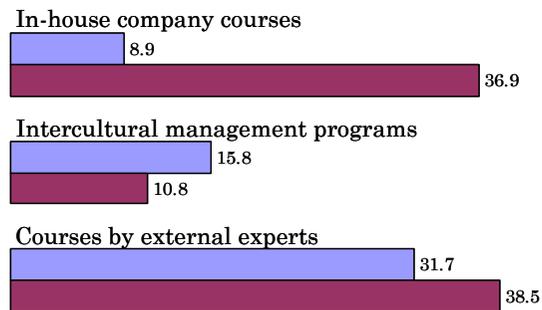
■ Firms without an alliance function (N=101)  
■ Firms with an alliance function (N=65)

*Figures in percentages*

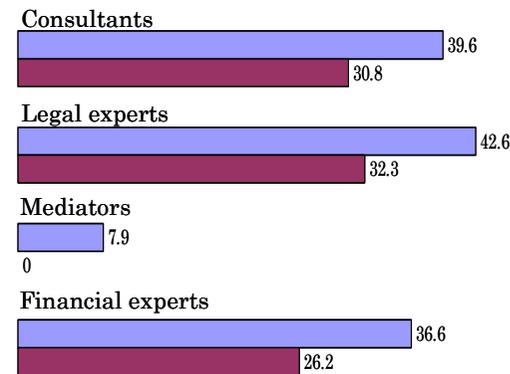
**Tool-based solutions**



**Training solutions**



**Third party solutions**



## ENDNOTES

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<sup>1</sup> PricewaterhouseCoopers. 2000. *Partnering Capabilities Survey*. PwC Canada.

<sup>2</sup> Harbison and Pekar. 1998. *Smart Alliances, A practical guide to repeatable success*. BoozAllen & Hamilton. Jossey-Bass Publishers: San Francisco; Margulis M, Pekar P. 2001. *The Next Wave of Alliance Formations: Forging Successful Partnerships with Emerging and Middle-Market Companies*. Houlhan Lokey Howard & Zukin; and Duysters G, Heimeriks K. 2005. Developing alliance capabilities in a new era. In *Advances in Applied Business Strategy, Vol. 8, Competence Perspectives on Managing Interfirm Interactions*, Sanchez R, Heene A (eds). Elsevier: Oxford: 151-167.

<sup>3</sup> Dyer JH, Kale P, Singh H. 2001. How to make strategic alliances work, Developing a dedicated alliance function is key to building the expertise needed for competitive advantage. *Sloan Management Review* 42(4): 37-43.

<sup>4</sup> *Alliance Analyst*. 1994. Two Grandmasters at the Extremes. November 1994. NewCap Communications: Philadelphia, PA; *Alliance Analyst*. 1996. New Track for Training, Parts I and II. August 1995. NewCap Communications: Philadelphia, PA.

<sup>5</sup> *Alliance Analyst*. 1996. Managing Alliances: Skills for the Modern Era. March 1996. NewCap Communications: Philadelphia, PA.; Harbison JR, Pekar P jr. 1998. *Smart Alliances, A practical guide to repeatable success*. BoozAllen & Hamilton. Jossey-Bass Publishers: San Francisco.

<sup>6</sup> For issues related to different stages of the alliance life-cycles see e.g. Bamford JD, Gomes-Casseres B, Robinson MS. 2003. *Mastering Alliance Strategy: A Comprehensive Guide to Design, Management, and Organization*. Jossey-Bass: San Francisco, CA.

<sup>7</sup> See also Gueth (2001) Entering into an alliance with big pharma. *Pharmaceutical Technology* October: 132-135.; Dhanaraj C, Lyles M (2006) for a recent case study on Eli Lilly's alliance capabilities.

<sup>8</sup> See e.g. Dyer JH, Kale P, Singh H. 2001. How to make strategic alliances work, Developing a dedicated alliance function is key to building the expertise needed for competitive advantage. *Sloan Management Review* 42(4): 37-43; and Kale P, Dyer JH, Singh H. 2002. Alliance capability, stock market response, and long term alliance success: the role of the alliance function. *Strategic Management Journal* 23(8): 747-767.

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