

CHAPTER 13

International Strategic Alliances



Francis Joseph Dean/Newscom

AFTER STUDYING THIS CHAPTER, YOU SHOULD BE ABLE TO:

1. Compare joint ventures and other forms of strategic alliances.
2. Characterize the benefits of strategic alliances.
3. Describe the scope of strategic alliances.
4. Discuss the forms of management used for strategic alliances.
5. Identify the limitations of strategic alliances.

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THE EUROPEAN CEREAL WARS

Kellogg virtually created the market for breakfast cereals in Europe. The maker of such popular brands as Kellogg's Corn Flakes, Rice Krispies, and Frosted Flakes, Kellogg began introducing its products in the United Kingdom in the 1920s and on the European continent in the 1950s. However, Europeans traditionally favored bread, fruit, eggs, and meats for breakfast, so the firm had a tough sell on its hands. Indeed, it took decades for Europeans to accept cereals as a viable breakfast choice.

Fortunately for cereal makers, during the 1980s and 1990s, demand for breakfast cereals in Europe began to accelerate as European consumers became more health-conscious and started looking for breakfast alternatives to eggs and meat. The busy schedules of the increasing number of dual-career families spurred demand for prepackaged foods. Another contributing factor has been the emergence of supermarkets in Europe. Traditionally most food products in Europe were sold at small specialty stores, which were often reluctant to stock cereals because they take up so much shelf space. In recent years, however, more full-line supermarkets have opened in Europe, and shelf space is now available for a wider array of products. Finally, the growth of commercial TV outlets in Europe has helped firms increase brand awareness and demand through advertising. Needless to say, the enormous potential of the European cereal market also attracted the interests of Kellogg's competitors.

One of Kellogg's biggest competitors in the United States is General Mills, which makes popular brands such as Cheerios and Golden Grahams. General Mills has traditionally concentrated on the North American market. But in 1989 General Mills' managers decided it was time for the company to enter the European market. However, they also recognized that taking on Kellogg, which controlled 50 percent of the worldwide cereal market and dominated the European market, would be a monumental battle.

After careful consideration, General Mills' Chief Executive Officer (CEO) Bruce Atwater decided that the firm could compete most effectively in Europe if it worked with a strategically located partner. It didn't take him long to choose one: Nestlé, the world's largest food-processing firm. Nestlé is a household

name in Europe, has a well-established distribution system, and owns manufacturing plants worldwide. One major area in which Nestlé had never succeeded, however, was the cereal market. Thus, Atwater reasoned that Nestlé would be a logical and willing partner.

When he approached his counterpart at Nestlé, he was amazed to discover that that firm had already been considering approaching General Mills about just such an arrangement. From Nestlé's perspective, General Mills could contribute its knowledge of cereal technology, its array of proven cereal products, and its expertise in marketing cereals to consumers, especially children.

Top managers of the two firms met and quickly outlined a plan of attack. Each firm contributed around \$80 million to create a new firm called Cereal Partners Worldwide (CPW). CPW's corporate offices were established in Lausanne, Switzerland. General Mills agreed to install its proprietary manufacturing systems in existing Nestlé factories, oversee the production of cereals, and help develop advertising campaigns. Nestlé, in turn, agreed to use its own globally recognized corporate name on the products and to handle sales and distribution throughout Europe. The two partners set two major goals for CPW: They wanted CPW to be generating annual sales of \$1 billion and to be a strong number 2 in market share outside North America by the year 2000.

By almost any measure, CPW has been a roaring success. Among its first triumphs was a deal struck with Disneyland Paris to supply breakfast cereals to the restaurants and hotels at the French theme park and to use Disney characters to promote the firm's cereals. The firm quickly established itself as a major player in the European cereal market, with an impressive 25 percent of the United Kingdom market. Having solidified its beachhead in Europe, CPW then expanded its operations to Latin America and Asia. With revenues of \$2 billion in 2011, it is now one of the world's largest cereal manufacturers. CPW operates in 140 countries and markets 50 brands, delivering a steady and growing stream of earnings for its parents, Nestlé and General Mills.¹ ■

Globalization can be an expensive process, particularly when a firm must perfectly coordinate research and development (R&D), production, distribution, marketing, and financial decisions throughout the world to succeed. A firm may discover that it lacks all the necessary internal resources to effectively compete against its rivals internationally. The high costs of researching and developing new products alone may stretch its corporate budget. Thus, a firm may seek partners to share these costs. Or a firm may develop a new technology but lack a distribution network or production facilities in all the national markets it wants to serve. Accordingly, the firm may seek out other firms with skills or advantages that complement its own and negotiate agreements to work together. Such factors motivated Nestlé and General Mills to team together, as the opening case indicated.

International Corporate Cooperation

Cooperation between international firms can take many forms, such as cross-licensing of proprietary technology, sharing of production facilities, cofunding of research projects, and marketing of each other's products using existing distribution networks. Such forms of cooperation are known collectively as **strategic alliances**, business arrangements whereby two or more firms choose to cooperate for their mutual benefit. The partners in a strategic alliance may agree to pool R&D activities, marketing expertise, or managerial talent. For example, in the early 1990s, Kodak and Fuji—two fierce competitors in the film market—formed a strategic alliance with camera manufacturers Canon, Minolta, and Nikon to develop a new standard for cameras and film, the Advanced Photo System, to make picture taking easier and more goof-proof.²

A **joint venture (JV)** is a special type of strategic alliance in which two or more firms join together to create a new business entity that is legally separate and distinct from its parents. JVs are normally established as corporations and are owned by the founding parents in whatever proportions they negotiate. Although unequal ownership is common, many are owned equally by the founding firms. Cereal Partners Worldwide represents this type of alliance.

A strategic alliance is only one method by which a firm can enter or expand its international operations. As Chapter 12 discussed, other alternatives exist: exporting, licensing, franchising, and foreign direct investment (FDI). In each of these alternatives, however, a firm acts alone or hires a second individual or firm—often one further down the distribution chain—to act on its behalf. In contrast, a strategic alliance results from cooperation among two or more firms. Each participant in a strategic alliance is motivated to promote its own self-interest but has determined that cooperation is the best way to achieve its goals.

Some means is required for managing any cooperative agreement. A JV, as a separate legal entity, must have its own set of managers and board of directors. It may be managed in any of three ways. First, the founding firms may jointly share management, with each appointing key personnel who report back to officers of the parent. Second, one parent may assume primary responsibility. And third, an independent team of managers may be hired to run it. The third approach is often preferred because independent managers focus on what is best for the JV rather than attempting to placate bosses from the founding firms.³ Other types of strategic alliances may be managed more informally—for example, by a coordinating committee, composed of employees of each of the partners, which oversees the alliance's progress.

A formal management organization allows a JV to be broader in purpose, scope (or range of operations), and duration than other types of strategic alliances. A non-JV strategic alliance may be formed merely to allow the partners to overcome a particular hurdle that each faces in the short run. A JV will be more helpful if the two firms plan a more extensive and long-term relationship. A typical non-JV strategic alliance has a narrow purpose and scope, such as marketing a new smartphone in Canada. A JV might be formed if firms wanted to cooperate in the design, production, and sale of a broad line of telecommunications equipment in North America. Non-JV strategic alliances are often formed for a specific purpose that may have a natural ending. For example, the agreement among the camera manufacturers Canon, Minolta, and Nikon and the film manufacturers Fuji and Kodak to jointly create the Advanced Photo System for cameras and film terminated in 1996 after the new standards were developed. Each participant then marketed the resulting products on its own: Kodak called its new film Advantix; Minolta labeled its new cameras Vectis; and Nikon chose the name Nuvis.⁴ But because JVs are separate legal entities, they generally have a longer duration. A venture such as CPW has an indefinite time horizon in that it will continue to function so long as its two owners are satisfied with its performance.

Because of their narrow mission and lack of a formal organizational structure, non-JV strategic alliances are relatively less stable than JVs. For example, in 1988 United Airlines and British Airways entered into an agreement to form a strategic marketing alliance involving their North American and European routes. At the time, United was offering limited service to Europe and was losing market share to archrivals Delta and American Airlines, both of which offered more extensive service there. To solve its problem, United agreed to coordinate its flight schedules with British Airways, thereby making it more convenient for a Europe-bound U.S. traveler to board a domestic United flight and then transfer to a transatlantic British Airways flight. United and British Airways both prominently described the arrangement in

their marketing campaigns and in the visits of their marketing reps to U.S. and European travel agencies. Within a year, however, Pan Am's routes to London were placed on the auction block. United quickly purchased those routes from Pan Am and severed relations with its strategic ally. British Airways was of little use to United once United could operate in London on its own. Needing a transatlantic partner, British Airways then entered into a similar strategic alliance with US Air in 1993. Three years later American Airlines and British Airways agreed to form a separate strategic alliance. US Air, believing that it would be the weakest partner in a three-way alliance, promptly sued British Airways and terminated their alliance.

In Practice

- Strategic alliances occur when two or more companies agree to cooperate to achieve a mutual objective.
- A joint venture (JV) is a strategic alliance in which a new firm or organization is created. JVs are often used when the proposed strategic alliance is complex and expected to be long-lived.

For further consideration: Why have JVs involving firms from two or more countries become so popular?

Benefits of Strategic Alliances

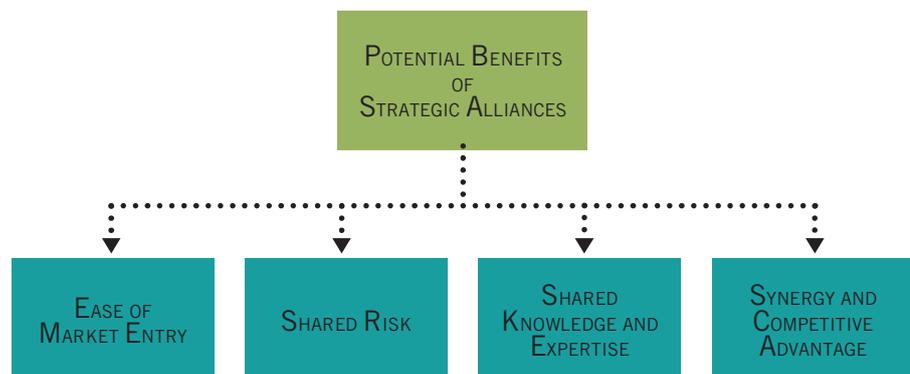
Firms that enter into strategic alliances usually expect to benefit in one or more ways.⁵ As summarized in Figure 13.1, international business may realize four benefits from strategic alliances: ease of market entry, shared risk, shared knowledge and expertise, and synergy and competitive advantage.⁶

Ease of Market Entry

A firm wishing to enter a new market often faces major obstacles, such as entrenched competition or hostile government regulations. Partnering with a local firm can often help it navigate around such barriers. In other cases, economies of scale and scope in marketing and distribution confer benefits on firms that aggressively and quickly enter numerous markets.⁷ Yet the costs of speed and boldness are often high and beyond the capabilities of a single firm. A strategic alliance may allow the firm to achieve the benefits of rapid entry while keeping costs down.

For example, IMAX recently targeted China as an important growth market for filmed entertainment. To speed its entry, it entered into a \$40 million JV with Wanda Cinema Line, the operator of China's largest theater chain, to build 75 IMAX theaters in China. IMAX will supply its specialized projection equipment, while Wanda will build the theaters.⁸ A similar meshing of strengths motivated a JV between Cigna, the U.S. insurance giant, and Banco Excel Economico, one of Brazil's largest privately owned banks, to sell personal insurance in Brazil.

FIGURE 13.1
Benefits of Strategic Alliances



Cigna provides expertise in selling life, accident, and credit insurance to consumers, while Banco Excel supplies its knowledge of the Brazilian financial services industry, as well as access to its existing retail customer base. Each partner contributed half of the \$19 million invested in the new company, Excel Cigna Seguradora.⁹

Regulations imposed by national governments also influence the formation of JVs. Many countries are so concerned about the influence of foreign firms on their economies that they require multinational corporations (MNCs) to work with a local partner if they want to operate in these countries.¹⁰ For example, the government of Namibia, an African nation, requires foreign investors operating fishing fleets off its coast to work with local partners. At other times governments strongly encourage foreign companies to participate in JVs to promote other policy goals. A case in point is China, which required foreign automobile companies to partner with local firms as a means of transferring technology to its automobile industry. A local partner may also make it easier to navigate through complex laws and customs. For instance, Rio Tinto, an Anglo-Australian mining company, formed a JV with Chinalco, China's leading aluminum company, to explore for ore deposits in China. The JV will benefit from Rio Tinto's expertise and Chinalco's knowledge of local laws and ways of doing business.¹¹

Shared Risk

Today's major industries are so competitive that no firm has a guarantee of success when it enters a new market or develops a new product. Strategic alliances can be used to either reduce or control individual firms' risks. For example, Boeing established a strategic alliance with several Japanese firms to reduce its financial risk in the development and production of the Boeing 777 jet. Researching, designing, and safety-testing a new aircraft model costs billions of dollars, much of which must be spent before the manufacturer can establish how well the airplane will be received in the marketplace. Even though Boeing has enjoyed much success as a manufacturer of commercial aircraft, it wanted to reduce its financial exposure on the 777 project. Thus, it collaborated with three Japanese partners—Fuji, Mitsubishi, and Kawasaki—agreeing to let them build 20 percent of the 777 airframe. Boeing, the controlling partner in the alliance, also hoped its allies would help sell the new aircraft to large Japanese customers such as Japan Air Lines and All Nippon Airways. The arrangement proved so successful that Boeing used it as well in designing and producing its latest jet, the 787 Dreamliner.

Or consider the strategic alliance involving Kodak and Fuji and three Japanese camera firms discussed previously. At face value, it might seem odd for Kodak to agree to collaborate with Fuji, its biggest competitor, to develop a new film that both would make and sell. Closer scrutiny, however, suggests that the arrangement reduced Kodak's risks considerably. Kodak managers realized that if they developed the film alone, Fuji would aggressively fight the innovation in the marketplace and Kodak would have to work hard to gain consumer acceptance of its new standard for film. Still worse, Fuji might have decided to develop its own new film standard, thereby jeopardizing Kodak's R&D investment should the Japanese-dominated camera-manufacturing industry adopt Fuji's approach rather than Kodak's. Mindful of the financial losses incurred by Sony when VHS rather than Betamax became the standard format for VCRs, Kodak chose to include Fuji in the deal. Through this strategic alliance, Kodak perhaps reduced its potential profits but also substantially reduced its risks. It was then free to compete on a playing field of its own choosing, able to harness its marketing clout, distribution networks, and formidable brand name against the efforts of its rivals.

Shared Knowledge and Expertise

Still another common reason for strategic alliances is the potential for the firm to gain knowledge and expertise that it lacks. A firm may want to learn more about how to produce something, how to acquire certain resources, how to deal with local governments' regulations, or how to manage in a different environment—information that a partner often can offer.¹² The firm can then use the newly acquired information for other purposes. For instance, Moody's entered into a JV with China Cheng Xin International Credit Rating Company to allow them to offer joint credit ratings for participants in cross-border financings; the Chinese company provides credit ratings for domestic firms, and Moody's provides ratings for non-Chinese companies.¹³ And, as our opening case discussed, CPW has proved to be successful, in part because it blended the knowledge and expertise of Nestlé and General Mills.

Synergy and Competitive Advantage

Firms may also enter into strategic alliances to attain synergy and competitive advantage. These related advantages reflect combinations of the other advantages discussed in this section: The idea is that through some combination of market entry, risk sharing, and learning potential, each collaborating firm will be able to achieve more and to compete more effectively than if it had attempted to enter a new market or industry alone.¹⁴

For example, creating a favorable brand image in consumers' minds is an expensive, time-consuming process, as is creating efficient distribution networks and obtaining the necessary clout with retailers to capture shelf space for one's products. These factors led PepsiCo, the world's second-largest soft drink firm, to establish a JV with Thomas J. Lipton Co., a division of Unilever, to produce and market ready-to-drink teas in the United States. Lipton, which is the global market leader in ready-to-drink teas, provided the JV with manufacturing expertise and brand recognition in teas. PepsiCo supplied its extensive and experienced U.S. distribution network.¹⁵ Alternatively, firms create synergies by establishing JVs to deepen and strengthen their global business relationships. Exxon Mobil and Qatar Petroleum International, for instance, created Golden Pass Products LLC to construct and operate liquefied natural gas (LNG) import facilities in Port Arthur, Texas. With the boom in production of shale-based natural gas in Texas (see Chapter 2's closing case, "Fracturing the Energy Market"), the two partners are planning a \$10-billion expansion of the facility to export LNG. Golden Pass is but one of the many projects the two firms collaborate on because each benefits from the financial strength, technical expertise, and political connections of the other.¹⁶

In Practice

- JVs are often created to facilitate market entry, share risk, transfer knowledge and expertise, and promote synergies and competitive advantage.
- In many JVs, one partner's strength is its partner's weakness and vice-versa.

For further consideration: Many JVs involve a host country firm and a foreign firm which possesses a superior technology. Why might this be so?

Scope of Strategic Alliances

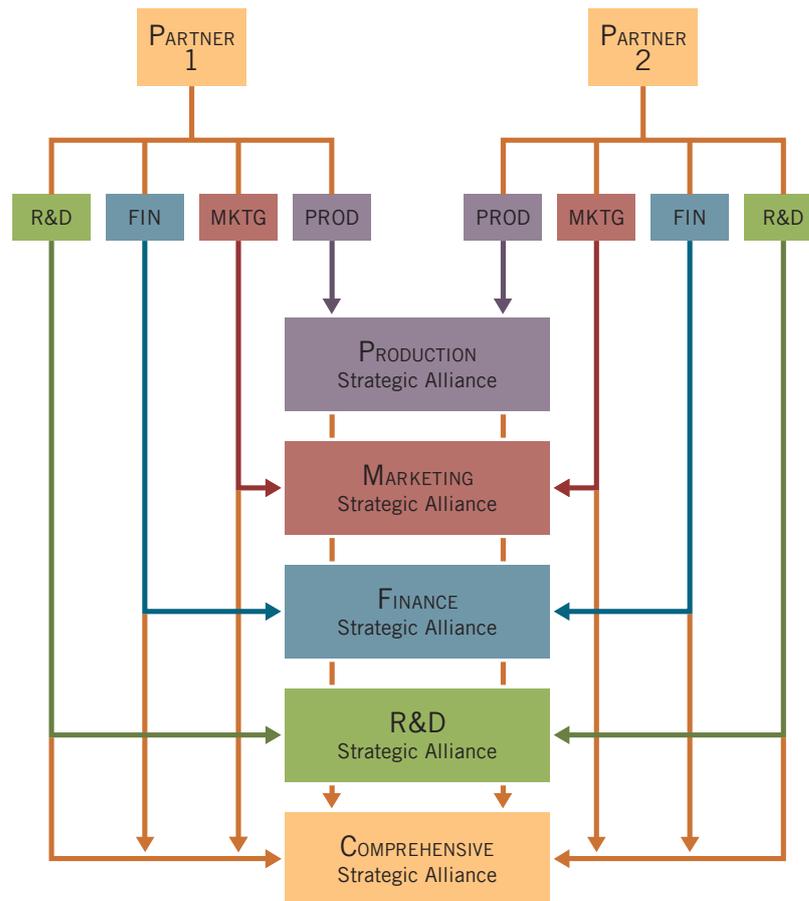
The scope of cooperation among firms may vary significantly, as Figure 13.2 illustrates. For example, it may consist of a comprehensive alliance, in which the partners participate in all facets of conducting business, ranging from product design to manufacturing to marketing. Or it may consist of a more narrowly defined alliance that focuses on only one element of the business, such as R&D. The degree of collaboration will depend on the basic goals of each partner.

Comprehensive Alliances

Comprehensive alliances arise when the participating firms agree to perform together multiple stages of the process by which goods or services are brought to the market: R&D, design, production, marketing, and distribution. Because of the broad scope of such alliances, the firms must establish procedures for meshing such functional areas as finance, production, and marketing for the alliance to succeed. Yet integrating the different operating procedures of the parents over a broad range of functional activities is difficult in the absence of a formal organizational structure. As a result, most comprehensive alliances are organized as JVs. As an independent entity, the JV can adopt operating procedures that suit its specific needs, rather than attempting to accommodate the often incompatible procedures of the parents, as might be the case with another type of strategic alliance.

Moreover, by fully integrating their efforts, participating firms in a comprehensive alliance are able to achieve greater synergy through sheer size and total resources. For instance, as the chapter's opening case discussed, General Mills and Nestlé created a comprehensive JV, CPW, to market cereal in Europe in the face of fierce, entrenched competition from Kellogg. General Mills contributed its cereal-making technology to the JV, and Nestlé added its European distribution network and name recognition. CPW would have had a major uphill battle in the

FIGURE 13.2
Scope of Strategic Alliances



European cereal market if the JV had covered only a single function, such as marketing. But a complete meshing of each firm's relative strengths resulted in a business unit that has emerged as a formidable competitor for Kellogg. Similarly, Dow Chemical and the Saudi Arabian Oil Company (Aramco) created a JV, Sadara Chemical Company, that will build and operate a \$19-billion petrochemical complex near Jubail that is scheduled to begin operation in 2015. Aramco will provide the feedstock for the plant, and Dow Chemical will contribute its technology and expertise in manufacturing petrochemicals.¹⁷

Functional Alliances

Strategic alliances may also be narrow in scope, involving only a single functional area of the business. In such cases, integrating the needs of the parent firms is less complex. Thus, functionally based alliances often do not take the form of a JV, although JVs are still the more common form of organization. Types of functional alliances include production alliances, marketing alliances, financial alliances, and R&D alliances.

PRODUCTION ALLIANCES A **production alliance** is a functional alliance in which two or more firms each manufacture products or provide services in a shared or common facility. A production alliance may use a facility one partner already owns. For example, as we discuss later in this chapter, the NUMMI joint venture between Toyota and GM was housed in a former GM assembly plant in California, which the U.S. company had previously closed down. Alternatively, the partners may choose to build a new plant, as was the case for a \$3.5-billion JV between Sony and Sharp to manufacture liquid crystal display panels for high-definition televisions in western Japan.¹⁸ At other times, the alliance may be quite narrow. Paramount Pictures, for instance, and state-owned China Movie Channel agreed to coproduce segments of the movie sequel *Transformers 4* in China.¹⁹

MARKETING ALLIANCES A **marketing alliance** is a functional alliance in which two or more firms share marketing services or expertise. In most cases, one partner introduces its products or

services into a market in which the other partner already has a presence. The established firm helps the newcomer by promoting, advertising, or distributing its products or services. The established firm may negotiate a fixed price for its assistance or may share in a percentage of the newcomer's sales or profits. Alternatively, the firms may agree to market each others' products on a reciprocal basis. For example, U.S. toymaker Mattel and its Japanese rival Bandai established a strategic marketing alliance that served their mutual interests. Bandai agreed to distribute Mattel products such as Barbie dolls, Hot Wheels, and Fisher Price toys in Japan, and Mattel agreed to market Bandai's Power Rangers and Digimon in Latin America, where Mattel's distribution network is strong but Bandai's nonexistent.²⁰ Marketing alliances are also common in the international airline industry, as "Venturing Abroad" indicates. However, when forming a marketing alliance, partners must take care to ensure that their expectations and needs are mutually understood.

FINANCIAL ALLIANCES A **financial alliance** is a functional alliance of firms that want to reduce the financial risks associated with a project. Partners may share equally in contributing financial resources to the project, or one partner may contribute the bulk of the financing while the other partner (or partners) provides special expertise or makes other kinds of contributions to partially offset its lack of financial investment. The strategic alliance between Boeing and its three Japanese partners was created primarily for financial purposes—Boeing wanted the other firms to help cover R&D and manufacturing costs. Those firms, in turn, saw a chance to gain valuable experience in commercial aircraft manufacturing as well as profits. Similarly, Marriott International and Samhi Hotels Pvt Ltd., a hotel investment fund, created a financial alliance to introduce Marriott's midtier Fairfield hotel chain into the Indian market.²¹ And 20th Century Fox and Paramount Pictures were financial allies in producing *Titanic*, one of the most successful movies in history.

VENTURING ABROAD

ALLIANCES IN THE SKY

Marketing alliances are usually ad hoc in nature, established to remedy some problem a firm has in a specific market. In the international airline industry, however, mega-marketing alliances now dominate competition within the industry. Three mega-alliances together account for a majority of the world's air revenue passenger miles. The Star Alliance, established in 1997, was the first of the mega-alliances to form and is the industry's largest. Its 27 members include United, Lufthansa, SAS, Air Canada, Air China, South African Airways, Singapore Airlines, and Turkish Airlines. The Star Alliance provides 21,900 daily departures to 1,329 airports in 194 countries. The 19-member SkyTeam alliance includes Air France, KLM, Delta, Aeromexico, Korean Air Lines, China Eastern, and Aeroflot. This alliance offers 15,000 daily flights serving 1,000 cities in 187 countries. The OneWorld alliance, whose 12 members include American Airlines, British Airways, Qantas, Cathay Pacific, and Japan Airlines, is the third-largest alliance. OneWorld carriers offer 8,800 daily departures to 841 cities in 157 countries.

Alliances have become a critical component of competition in the international airline industry because of decisions made at the International Civil Aviation Conference held in Chicago in 1944. The Chicago Conference, like the Bretton Woods Conference of 1944, was convened to structure a portion of the post-World War II economic environment—in this case, that of the civil aviation industry. The Chicago conferees decided to grant each government control over international airline service to and from its country. Most countries chose to grant commercial airline rights on a reciprocal basis: Country A would grant country B the right to designate a carrier from country B to fly between a city in B and a city in A if country B granted country A the right to designate a carrier from country A to fly between a city in A and a city in B. Moreover, few nations allowed cabotage—the carrying of passengers by a foreign carrier from one



city in the host country to another city in the host country (e.g., Delta Airlines carrying a passenger from Vancouver to Montreal).

Thus, an airline such as Delta could develop an elaborate hub-and-spoke system in Atlanta that would allow it to pick up a passenger in a U.S. city like Buffalo, transport her to Atlanta, and transfer her to a Delta flight going to Albuquerque. Using a hub-and-spoke system, Delta could provide convenient service to Buffalo-Albuquerque travelers, even though only a few passengers might wish to fly from Buffalo to Albuquerque on any given day. This advantage, however, stopped at the water's edge. Because of the Chicago Conference, Delta could not create a similar hub in Europe or Asia. However, by joining the SkyTeam Alliance, Delta can take advantage of Air France's hub in Paris, KLM's hub in Amsterdam, Aeroflot's hub in Moscow, and Korean Airlines' hub in Seoul. Thus, Delta and any other member of the SkyTeam alliance can advertise and offer service on 15,000 flights a day to 1,000 cities in 187 countries even though it physically flies only a small percentage of these flights itself.

Besides offering customers more flights and more destinations, these marketing alliances make it easier for customers to transfer between alliance members' flights and allow customers to use frequent flyer miles earned on one carrier to fly free on the flights of other members of the alliance. The alliances also strive to maintain uniformly high standards of service and to promote consistent customer service policies. The SkyTeam alliance, for instance, coordinates its in-flight video offerings so that passengers flying different SkyTeam carriers on a given day see different movies on each leg of their journey.

Sources: www.staralliance.com; www.skyteam.com; www.oneworldalliance.com, accessed July 27, 2013.

In Practice

- Strategic alliances come in all sizes and scopes. They may range from a narrow scope, involving a single business function such as marketing, to comprehensive scope, involving all aspects of designing, manufacturing, marketing, and distributing a product or service.
- Oftentimes R&D alliances are not structured as JVs so as to avoid disrupting ongoing laboratory work.

For further consideration: Consider production alliances and financial alliances. Which type is more likely to result in the creation of a JV? Why?

Implementation of Strategic Alliances

The decision to form a strategic alliance should develop from the firm's strategic planning process, discussed in Chapter 11. Having made this decision, its managers must then address several significant issues, which set the stage for how the arrangement will be managed.²⁵ Some of the most critical of these issues are the selection of partners, the form of ownership, and joint management considerations.

Selection of Partners

The success of any cooperative undertaking depends on choosing the appropriate partner(s). Research suggests that strategic alliances are more likely to be successful if the skills and resources of the partners are complementary—each must bring to the alliance some organizational strength the other lacks.²⁶ A firm contemplating a strategic alliance should consider at least four factors in selecting a partner (or partners): (1) compatibility, (2) the nature of the potential partner's products or services, (3) the relative safeness of the alliance, and (4) the learning potential of the alliance.

COMPATIBILITY The firm should select a compatible partner that it can trust and with whom it can work effectively. Without mutual trust, a strategic alliance is unlikely to succeed. But incompatibilities in corporate operating philosophies may also doom an alliance. For example, an alliance between General Electric Corporation (a UK firm unrelated to the U.S. firm of the same name) and the German firm Siemens failed because of incompatible management styles. The former firm is run by financial experts and the latter by engineers. General Electric Corporation's financial managers continually worried about bottom-line issues, short-term profitability, and related financial considerations. Siemens' managers, in contrast, paid more attention to innovation, design, and product development and less attention to financial issues.²⁷ In contrast, a key ingredient in CPW's success is the high level of compatibility between General Mills and Nestlé.

NATURE OF A POTENTIAL PARTNER'S PRODUCTS OR SERVICES Another factor to consider is the nature of a potential partner's products or services. It is often hard to cooperate with a firm in one market while doing battle with that same firm in a second market. Under such circumstances, each partner may be unwilling to reveal all of its expertise to the other partner for fear that the partner will use that knowledge against the firm in another market.

Most experts believe a firm should ally itself with a partner whose products or services are complementary to but not directly competitive with its own. The JV between General Mills and Nestlé is an example of this principle in action: Both are food-processing firms, but Nestlé does not make cereal, the product on which it is collaborating with General Mills. Similarly, PepsiCo and Lipton complement but do not compete with one another, thus raising the likelihood of success for their JV to market ready-to-drink tea in the United States.

THE RELATIVE SAFENESS OF THE ALLIANCE Given the complexities and potential costs of failed agreements, managers should gather as much information as possible about a potential partner before entering into a strategic alliance. For example, managers should assess the success or failure of previous strategic alliances formed by the potential partner. Also, it often makes sense to analyze the prospective deal from the other firm's side. What does the potential partner hope to gain from the arrangement? What are the partner's strengths and weaknesses? How

will it contribute to the venture? Does the proposed arrangement meet its strategic goals? The probability of success rises if the deal makes good business sense for both parties.²⁸

For example, Corning, Inc., created a JV venture—Asahi Video Products Company—by integrating its television glass production with the operations of Asahi Glass, a producer of large television bulbs. Corning believed this JV would be a sound one for several reasons:

- Asahi Glass' expertise in large television-bulb technology complemented Corning's strength in other bulb sizes.
- The JV would benefit from Asahi Glass' ongoing business connections with the increasing number of Japanese television manufacturers that were establishing North American facilities.
- The combined strengths of the two firms would help both keep abreast of technological innovations in the video display industry.
- Asahi Glass would benefit from Corning's technology and marketing clout in the U.S. market.
- Corning had successfully operated another JV with Asahi Glass since 1965.

In fact, Corning is so good at developing JVs that almost half its profits are generated by JVs with leading MNCs such as PPG, Dow Chemical, and Samsung.

THE LEARNING POTENTIAL OF THE ALLIANCE Before establishing a strategic alliance, partners should also assess the potential to learn from each other. Areas of learning can range from the specific—for example, how to manage inventory more efficiently or how to train employees more effectively—to the general—for example, how to modify corporate culture or how to manage more strategically. At the same time, however, each partner should carefully assess the value of its own information and not provide the other partner with any information that will result in competitive disadvantage for itself should the alliance dissolve—a point we revisit in the next section.²⁹ “Venturing Abroad” discusses a successful alliance formed for learning purposes.

Form of Ownership

Another issue in establishing a strategic alliance is the exact form of ownership that is to be used. A JV almost always takes the form of a corporation, usually incorporated in the country in which it will be doing business. In some instances, it may be incorporated in a different country, such as one that offers tax or legal advantages. The Bahamas, for example, are sometimes seen as a favorable tax haven for the incorporation of JVs.

The corporate form enables the partners to arrange a beneficial tax structure, implement novel ownership arrangements, and better protect their other assets. This form also allows the JV to create its own identity apart from those of the partners. Of course, if either or both of the

VENTURING ABROAD

LEARNING BY DOING

Toyota and GM enjoyed one of the more successful and long-lived JVs in the United States. In 1982 GM closed an old automobile manufacturing plant in Fremont, California, because it had become too costly and inefficient to run. In 1984 Toyota agreed to reopen the plant and manage it through a JV called New United Motor Manufacturing, Inc. (NUMMI). Although NUMMI was owned equally by the two partners, Toyota managed the facility and assembled automobiles for both. Each firm entered into the deal primarily to acquire knowledge. Toyota wanted to learn more about how to deal with labor and parts suppliers in the U.S. market, and GM wanted to observe Japanese management practices firsthand. Toyota used its newly acquired information when it opened its own manufacturing plant in Georgetown, Kentucky, in 1988. GM used lessons learned from NUMMI in developing and operating its experimental automotive division, Saturn, and in organizing its then newest European assembly



plant in Eisenach, Germany. As a result, productivity in this plant was double that of GM's plants in the United States. When GM entered into its \$1.6-billion JV with Shanghai Automotive Industry Corporation to make Buicks in 1997, lessons learned at NUMMI played a critical role in the overwhelming success of that JV. However, by the late 2000s, the strategic and learning benefits of NUMMI to the partners had lessened. In the midst of its financial crisis and ensuing bankruptcy, GM announced it would withdraw from the JV in 2009. Nonetheless, NUMMI must be rated a success: Both companies acquired the knowledge they sought through the creation of the JV.

Sources: “A giant falls,” *The Economist*, June 4, 2009; “The car company in front,” *The Economist*, January 27, 2005; “Testing GM's shock absorbers,” *The Economist*, April 29, 1999; “Making a global alliance work,” *Fortune*, December 17, 1990, pp. 121–126.

PEOPLE, PLANET, AND PROFITS

ALLIANCES FOR GOOD

Alliances between nongovernmental organizations (NGOs) and businesses large and small are growing in importance. Most NGOs are focused on promoting a cause, such as human rights, workers rights, or environmental protection. Often their initial approach was to organize politically and then lobby their local government to pass legislation to achieve their agendas. But many found that governments are slow to act and often inefficient in implementing and enforcing legislation once enacted. The private sector, conversely, can react faster and more efficiently if motivated to do so.

NGOs therefore have turned their attention to forming alliances with private sector organizations. For instance, the World Wildlife Fund now focuses on the largest 100 companies in the global marketplace: "We know if they change their practices, it will affect half of the markets in which they operate, and that will make a huge difference in conserving the places we care about....This is the fastest-growing part of our work, and it's the place where we see the greatest traction."

Sometimes an alliance is formed because the business partner genuinely believes in the mission of the NGO; sometimes the alliance develops after the business partner suffers adverse publicity, often triggered by the NGO it later partners with. Nike provides a useful example. In the 1990s, Nike was pilloried by NGOs for the unsafe and abusive working environments in factories of its contract manufacturers. At first, Nike argued that it had no responsibility for the conditions because the workers were not its employees. That argument proved unpersuasive in the court of public opinion. After several false starts, Nike forged a strong working relationship with leading labor rights NGOs and agreed to an active and open monitoring of conditions in the factories of its subcontractors, the results of which are available on its website, at www.nikeinc.com/pages/responsibility. Although conditions are not perfect in the factories, Nike is now viewed as a partner, not an enemy, in the promotion of workers rights by the NGO community.



Other examples abound: IKEA and Kingfisher (a leading European home improvement vendor) teamed with the Forest Stewardship Council, the Rainforest Alliance, and the World Wildlife Fund to protect Chinese forests by purchasing only lumber certified as having been cut in an environmentally sound manner. Limited Brands agreed to purchase paper for its 400 million catalogs from sustainable vendors after being pressured to do so by ForestEthics. Walmart has committed to triple its purchases of local produce for its grocery operations, thereby supporting local small farmers and reducing transportation-related greenhouse gas emissions. It forged this new sourcing strategy in consultation with experts from the National Resource Defense Council, the World Wildlife Fund, and the Environmental Defense Fund.

NGOs often work with smaller firms as well, particularly in emerging markets. For instance, the Brazilian branch of the World Wildlife Fund has partnered with the state government of Acre and local farm cooperatives to promote sustainable agricultural practices and reliance on the bounty of the rainforest. For instance, Cooperacre, a 2,000-member cooperative collects, shells, and packages Brazil nuts gathered from the wild. Natex, a 700-member cooperative, purchases latex gathered from wild rubber trees to manufacture condoms, which are then purchased by the government to combat AIDS.

Sources: "Asian paper giant agrees to stop cutting Indonesia's natural rain forests," *Washington Post*, February 5, 2013; "The new rubber boomlet," *The Economist*, December 1, 2012; "Going bananas," *The Economist*, March 31, 2012; "Wal-Mart pledges more purchases from local farmers across the world," *Washington Post*, October 14, 2010; "The long road to sustainability," *The Economist*, September 23, 2010; "Strange bedfellows," *The Economist*, May 22, 2008.

Rainforests provides critical habitat to millions of species of flora and fauna and a vital role in controlling global greenhouse gas emissions. Many NGOs and lumber retailers formed alliances to protect rainforest habitats and promote sustainable forestry practices. These alliances want to eliminate the use of clear cutting (shown here), an ecologically harmful technique.



guentermanaus/Fotolia

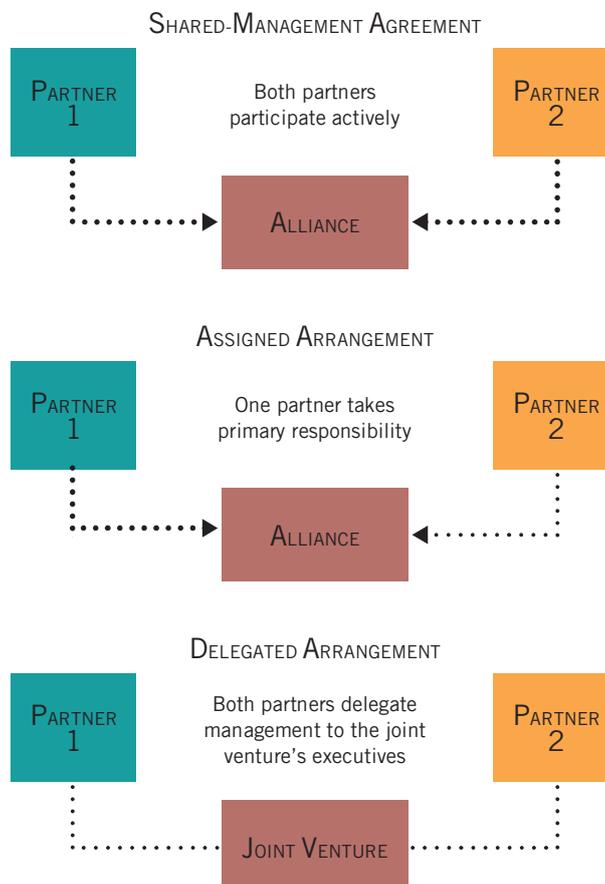
However, other Western firms have had their share of troubles with these arrangements, prompting a bitter joke among expatriates in China: “What qualities should you look for in a joint-venture partner?” “One who never comes to the office.” For instance, Daimler-Benz signed an agreement in 1995 to establish a JV with state-owned Nanfang South China Motor Corporation to build minivans. Two years later, nothing had been done because the two partners bickered over a variety of issues. Nanfang, for example, wanted to assemble the minivans at two plant sites, whereas Daimler-Benz officials fought for a single plant so as to capture economies of scale.³² Unilever had a different problem. Its JV partner in Shanghai not only continued to sell its own brand of detergent, White Cat, in competition with the Unilever product (Omo) produced by the JV, but it also began to copy Omo’s formula and packaged its detergent in a box that looked almost identical to that of Omo. New Balance executives could sympathize with Unilever’s plight. They discovered that their Chinese manufacturing partner was making counterfeit sneakers and selling them directly to discounters in England and Australia in addition to those it was legally making for New Balance itself.³³

Joint Management Considerations

Further issues and questions are associated with how a strategic alliance will be managed.³⁴ Three standard approaches are often used to jointly manage a strategic alliance (see Figure 13.3): shared management agreements, assigned arrangements, and delegated arrangements.

Under a **shared management agreement**, each partner fully and actively participates in managing the alliance. The partners run the alliance, and their managers regularly pass on instructions and details to the alliance’s managers. The alliance managers have limited authority of their own and must defer most decisions to managers from the parent firms. This type of agreement requires a high level of coordination and near-perfect agreement between the participating partners. Thus, it is the most difficult to maintain and the one most prone to conflict among the partners. An example of this type of JV management is that used by Coca-Cola and France’s Groupe Danone to distribute Coke’s Minute Maid orange juice in Europe and

FIGURE 13.3
Managing Strategic
Alliances



Latin America. This JV combines Danone's distribution network and production facilities—Danone supplies between 15 and 30 percent of the dairy products sold by supermarkets in these countries—with the Minute Maid brand name. The JV operates under a shared management arrangement: Each company supplies three members of the JV's board of directors. Danone is responsible for the JV's operations, and Coke controls its marketing and finance.³⁵

Under an **assigned arrangement**, one partner assumes primary responsibility for the operations of the strategic alliance. For example, GM, with a 67-percent stake in a JV with Raba, a Hungarian truck, engine, and tractor manufacturer, has assumed management control over the venture's operations.³⁶ Boeing controls the overall operations of its strategic alliance with Fuji, Mitsubishi, and Kawasaki for the design and production of its 777 and 787 commercial aircraft. Under an assigned arrangement, management of the alliance is greatly simplified because the dominant partner has the power to set its own agenda for the new unit, break ties among decision makers, and even overrule its partner(s). Of course, these actions may create conflict, but they keep the alliance from becoming paralyzed, which may happen if equal partners cannot agree on a decision.

Under a **delegated arrangement**, which is reserved for JVs, the partners agree not to get involved in ongoing operations and so delegate management control to the executives of the JV itself. These executives may be specifically hired to run the new operation or may be transferred from the participating firms. They are responsible for the day-to-day decision making and management of the venture and for implementing its strategy. Thus, they have real power and the autonomy to make significant decisions themselves and are much less accountable to managers in the partner firms. For example, both American Motors and the Beijing Automotive Works contributed experienced managers to the operation of Beijing Jeep so that its management team could learn both modern automobile assembly operations and operating conditions in China. Moreover, these managers were given responsibility for the JV's operations.

Although it is important that both parties to the JV agree to the formal rules by which the venture will be managed, savvy international businesspersons recognize that in some instances the informal rules are equally important. Failure to appreciate the unwritten rules can sandbag foreign JV partners, as "Emerging Opportunities" explains.

In Practice

- Partner selection is a critical issue in the success or failure of strategic alliances. Each firm should carefully analyze the learning potential of the alliance, the nature of the potential partner's products or services, and the relative safeness of the alliance.
- As in a marriage, compatibility of the prospective partners may be the most critical determinant of success or failure. An alliance may make good business sense, but if the partners can't get along, failure is likely.

For further consideration: Consider the three approaches to managing a JV: shared management agreements, assigned arrangements, and delegated arrangements. Which one requires the most trust among the JV partners?

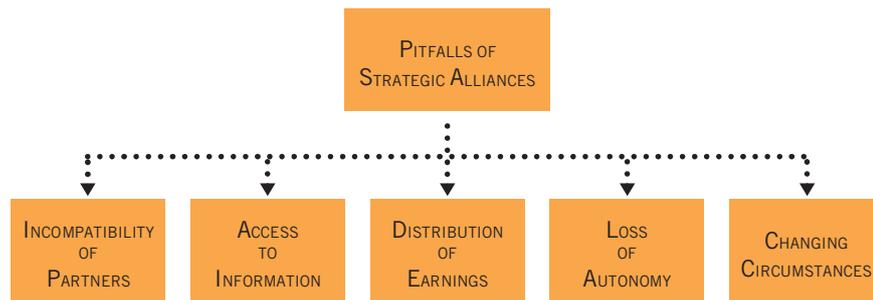
Pitfalls of Strategic Alliances

Regardless of the care and deliberation a firm puts into constructing a strategic alliance, it still must consider limitations and pitfalls. Figure 13.4 summarizes five fundamental sources of problems that often threaten the viability of strategic alliances: incompatibility of partners, access to information, conflicts over distributing earnings, loss of autonomy, and changing circumstances.

Incompatibility of Partners

Incompatibility among the partners of a strategic alliance is a primary cause of the failure of such arrangements. At times, incompatibility can lead to outright conflict, although typically it merely leads to poor performance of the alliance. We noted previously in the chapter the example of the conflict between Siemens' engineering-oriented management and General Electric Corporation's financially oriented management. Incompatibility can stem from differences in corporate culture, national culture, goals and objectives, or virtually any other fundamental dimension linking the

FIGURE 13.4
Pitfalls of Strategic Alliances



two partners. For instance, General Motors' \$340-million JV with Russian auto manufacturer OAO AvtoVAZ, which was established to build Chevrolet-branded compact SUVs designed by AvtoVAZ, has struggled as a result of disagreements between the partners over parts pricing, product design, market development, and adjustments in the JV's strategic direction.³⁷ Similarly, VW's management was disappointed with the slow start of its JV with Suzuki, which it attributed to the methodical but time-consuming decision making of its Japanese partner. It later accused Suzuki of sourcing certain diesel engines from Fiat in violation of the terms of their alliance agreement.³⁸

In many cases, compatibility problems can be anticipated if the partners carefully discuss and analyze the reasons why each is entering into the alliance in the first place. A useful starting point may be a meeting between top managers of the two partners to discuss their mutual interests, goals,

EMERGING OPPORTUNITIES

XI'S IN CHARGE

Webster's dictionary defines communism as a "social scheme which promotes the abolition of inequalities in the possession of wealth by distributing wealth equally or by holding all wealth in common for the benefit and use of all citizens." By that definition, contemporary China is not very communist. That does not mean that the Communist Party is unimportant, however, when doing business in or with China.

The most important person in the governance of any Chinese business organization of significant size is often the organization's party secretary. The party secretary is a member of the Chinese Communist Party (CCP) and is appointed by the CCP to be its representative within the organization. Although a Chinese corporation or a JV with a Chinese partner may be formally governed by a board of directors, ultimate power resides with the party secretary. Appointments of executives and senior managers or major strategic decisions must be approved by the party secretary. Often, the party secretary informs the board as to decisions that have been made by the party, which the board must then implement. One telling example was the government's decision in November 2004 to have the CEOs of the country's three largest telecommunications companies (China Telecom, China Mobile, and China Unicom) swap jobs among themselves. Although all three companies were state-owned enterprises, two of them were publicly listed with significant minority shareholders. Regardless of the formal role or wishes of their boards of directors, CCP leaders made the decision, which the three boards of directors then dutifully ratified.

Foreign companies must understand these informal, unwritten rules of governance or face the consequences, as New Zealand's Fonterra Corporation, the world's largest exporter of dairy products, learned to its chagrin. In 2005, Fonterra signed a JV agreement with Sanlu, China's premier dairy products firm. To implement the JV, Fonterra received a 43-percent ownership stake in Sanlu and was given three seats on Sanlu's board. Sanlu's rapid growth was attributable to its practice of buying milk in bulk from middlemen who in turn purchased

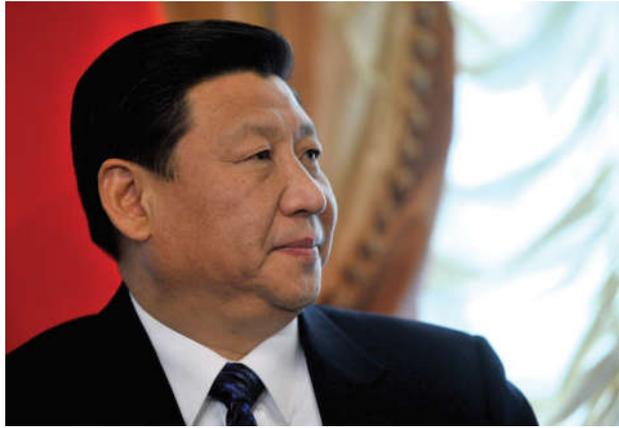


it from local farmers. Sanlu began receiving scattered reports early in 2008 that some of the purchased milk, which it used to make its market-leading infant formula, was laced with melamine. Melamine boosted the apparent protein content of the milk, which raised the price that the seller received, but it is highly toxic, causing kidney stones, bladder cancer, and damage to the reproductive system. By the end of July 2008 Sanlu's testing confirmed the problem.

Sanlu and its chairwoman Tian Wenhua—who also served as Sanlu's party secretary—faced a political as well as public health disaster. The Beijing Olympics were scheduled to begin on August 8, 2008, and the CCP made it clear it wanted no bad publicity to damage its desired triumphal staging of the summer games. When Sanlu's board met on August 2, it voted for a full product recall, according to Fonterra's minutes of the meeting. Sanlu's minutes indicate agreement on a limited product recall, the apparent result of intervention by the local vice-mayor in charge of product safety, who was mindful of the CCP's directive to suppress any food safety scandals while the eyes of the world's media and sports fans were focused on Beijing. A full product recall belatedly commenced in September, the result of New Zealand's ambassador notifying the Chinese government of the problem. Although Fonterra executives claim that they first heard of the melamine contamination at the August 2nd board meeting, the damage to the firm's reputation was not be easy to repair. Fonterra learned too late that the party secretary, not the board of directors or the company's managers, is the one in charge.

Sources: Richard McGregor, *The Party* (New York: HarperCollins, 2010); "Convicted Sanlu boss blames Fonterra," *nzherald.co.nz*, January 28, 2009 (online); Xinting, Jia, "Corporate Governance in State Controlled Enterprises," *Journal of Business Systems, Governance, and Ethics*, Vol 1., No. 3; "China bank chiefs hit at Communist party role," *Financial Times*, April 28, 2005 (online); www.webster-dictionary.org.

Regardless of his or her formal role in the organization, the party secretary, who is appointed by the Communist Party, is the most powerful decision maker in many Chinese corporations and joint ventures. The General Secretary of the Chinese Communist Party—a position held by Xi Jinping since 2012—is the party’s highest ranking official and the de facto leader of the country.



ITAR-TASS Photo Agency/Alamy

and beliefs about strategy. The manner in which the managers are able to work together during such a meeting may be a critical clue to their ability to cooperate in a strategic alliance. Obviously, if the partners cannot agree on such basic issues as how much decision-making power to delegate to the alliance’s business unit, what the alliance’s strategy should be, how it is to be organized, or how it should be staffed, compromise will probably be difficult to achieve and the alliance is unlikely to succeed. For example, a marketing alliance between AT&T and Italy’s Olivetti announced with great fanfare quickly failed after the firms could not reach agreement on a marketing strategy, what they wanted the alliance to accomplish, and how they planned to work together.

Access to Information

Limited access to information is another drawback of many strategic alliances. For a collaboration to work effectively, one partner (or both) may have to provide the other with information it would prefer to keep secret. It is often difficult to identify such needs ahead of time; thus, a firm may enter into an agreement not anticipating having to share certain information. When the reality of the situation becomes apparent, the firm may have to be forthcoming with the information or else compromise the effectiveness of the collaboration.³⁹

For example, Unisys, a U.S. computer firm, negotiated a JV with Hitachi, a Japanese electronics firm. Only after the venture was well underway did Unisys realize that it would have to provide Hitachi with most of the technical specifications it used to build computers. Although Unisys managers reluctantly gave Hitachi the information, they feared they were compromising their own firm’s competitiveness. And an alliance between Ford and Mazda to work on the design of a new Ford sedan almost stalled when Mazda officials would not allow their Ford counterparts to visit their research laboratory. After several weeks of arguing, a compromise was eventually reached whereby Ford engineers could enter the facility but only for a limited time.

Conflicts Over Distributing Earnings

An obvious limitation of strategic alliances relates to the distribution of earnings. Because the partners share risks and costs, they also share profits. For example, General Mills and Nestlé split the profits from their European JV on a 50/50 basis. Of course, this aspect of collaborative arrangements is known ahead of time and is virtually always negotiated as part of the original agreement.

However, there are other financial considerations beyond the basic distribution of earnings that can cause disagreement. The partners must also agree on the proportion of the joint earnings that will be distributed to themselves as opposed to being reinvested in the business, the accounting procedures that will be used to calculate earnings or profits, and the way transfer pricing will be handled. For example, Rubbermaid ended its JV to manufacture and distribute rubber and plastic houseware products throughout Europe, North Africa, and the Middle East because its local partner, the Dutch chemical company DSM Group NV, resisted reinvesting profits to develop new products to expand the JV’s sales as Rubbermaid preferred.⁴⁰

Loss of Autonomy

Another pitfall of a strategic alliance is the potential loss of autonomy. Just as firms share risks and profits, they also share control, thereby limiting what each can do. Most attempts to

introduce new products or services, change the way the alliance does business, or introduce any other significant organizational change first must be discussed and negotiated. To overcome such problems, FedEx chose to buy out its Chinese JV partner, Tianjin Datian W Group, for \$400 million. The purchase freed FedEx to better integrate the JV's 90 parcel-processing facilities and its 3,000 workers into FedEx's global distribution network.⁴¹ Conversely, as part of its contract with General Mills, Nestlé had to agree that if the JV is ever terminated, Nestlé cannot enter the North American cereal market for at least 10 years.

At the extreme, a strategic alliance may even be the first step toward a takeover. In the early 1980s, the Japanese firm Fujitsu negotiated a strategic alliance with International Computers, Ltd. (ICL), a British computer firm. After nine years of working together, Fujitsu bought 80 percent of ICL. One survey of 150 terminated strategic alliances found that more than three-fourths ended because a Japanese firm had taken over its non-Japanese partner.⁴² In other cases, partners may accuse each other of opportunistic behavior, that is, trying to take unfair advantage of each other. For example, a JV between the Walt Disney Company and Sky Television, a British pay-TV channel operator, broke down after Sky accused Disney of deliberately delaying the supply of promised programming. Disney, in turn, accused Sky of proceeding too hastily and without consulting it.⁴³

Changing Circumstances

Changing circumstances may also affect the viability of a strategic alliance. The economic conditions that motivated the cooperative arrangement may no longer exist, or technological advances may have rendered the agreement obsolete. For example, in late 2011 Samsung bought out Sony's interests in a seven-year-old JV to produce LCD screens for high-definition TVs. Although the venture was profitable for several years, industry overproduction led to operating losses in the 2010s.⁴⁴ Similarly, that same year, Johnson Controls sued to dissolve its JV with French battery manufacturer Saft Groupe SA to fabricate lithium-ion batteries for the automobile industry. The U.S. company claimed that rapid technological change and the investments needed to maintain market leadership rendered the JV ineffective. Its French partner disagreed.⁴⁵

In Practice

- The most important reasons why strategic alliances fail include incompatibility of partners, conflicts over access to information, disagreements over distributing earnings, loss of autonomy, and changing circumstances.
- Due diligence and discussion with prospective alliance partners can lessen the likelihood of some of these issues arising. For example, access to information and policies toward distributing earnings should be understood by all parties before an agreement is signed.

For further consideration: Consider the NUMMI JV, which dissolved after 25 years. Would you consider this JV a success or failure? Why?

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CHAPTER REVIEW

Summary

Strategic alliances, in which two or more firms agree to cooperate for their mutual benefit, are becoming increasingly popular in international business. A joint venture (JV), a common type of strategic alliance, involves two or more firms joining

together to create a new entity that is legally separate and distinct from its parents.

Strategic alliances offer several benefits to firms that use them. First, they facilitate market entry. Second, they allow

the partners to share risks. Third, they make it easier for each partner to gain new knowledge and expertise from the other partner(s). Finally, they foster synergy and competitive advantage among the partners.

The scope of strategic alliances can vary significantly. Comprehensive alliances involve a full array of business activities and operations. Functional alliances involving only one aspect of the business, such as production, marketing, finance, or research and development (R&D), are also common.

The decision to form a strategic alliance needs to be based on a number of different considerations. Selecting a partner is, of course, critically important and must take into account compatibility, the nature of the potential partner's products or services, the relative safety of the alliance, and the learning potential of the alliance. Selecting a form of organization is also important to the success of the alliance. A special form of strategic alliance involves public and private partners. The management structure of the strategic alliance must also be given careful consideration.

Partners in a strategic alliance must be aware of several pitfalls that can undermine the success of their cooperative arrangement. These include incompatibility of the partners,

access to information, conflicts over distributing earnings, loss of autonomy, and changing circumstances.

Review Questions

- 13-1. What are the basic differences between a JV and other types of strategic alliances?
- 13-2. Why have strategic alliances grown in popularity in recent years?
- 13-3. What are the basic benefits partners are likely to gain from their strategic alliance? Briefly explain each.
- 13-4. What are the basic characteristics of a comprehensive alliance? What form is it likely to take?
- 13-5. What are the four common types of functional alliances? Briefly explain each.
- 13-6. What is an R&D consortium?
- 13-7. What factors should be considered in selecting a strategic alliance partner?
- 13-8. What are the three basic ways of managing a strategic alliance?
- 13-9. Under what circumstances might a strategic alliance be undertaken by public and private partners?
- 13-10. What are the potential pitfalls of strategic alliances?

Questions for Discussion

- 13-11. Are strategic alliances common in your country? What are the current trends?
- ★ 13-12. Assume you are a manager for a large international firm, which has decided to enlist a foreign partner in a strategic alliance and has asked you to be involved in the collaboration. What effects, if any, might the decision to structure the collaboration as a JV have on you personally and on your career?
- 13-13. Identify an example of strategic alliance in your country that has not worked. Why?
- 13-14. Identify an example of a strategic alliance in your country that has worked. Why?
- 13-15. There will be some clear examples of success stories for strategic alliances. What appears to be the correct formula for successful strategic alliances in your country?
- ★ 13-16. What are some of the issues involved in a firm's trying to learn from a strategic alliance partner without giving out too much valuable information of its own?
- ★ 13-17. Why would a firm decide to enter a new market on its own rather than using a strategic alliance?
- 13-18. Identify any particular concerns or issues a global business might have to consider if they want to enter into a strategic alliance in your country.
- 13-19. Emerging markets offer great opportunities for businesses. The opportunities can be particularly advantageous if the corporation can obtain first-mover advantage by engaging a local partner. However, it can be that local partners are difficult to identify and assess. Why might this be the case?

Building Global Skills

Break into small groups of four to five people. Assume your group is the executive committee (that is, the top managers) of Resteaze, Inc. Resteaze is a large manufacturer of mattresses, box springs, and waterbeds. The publicly traded firm is among the largest in the U.S. bedding market. It operates 15 factories, employs more than 5,000 people, and last year generated \$20 million in profits on sales of \$380 million. Resteaze products are sold through department stores, furniture stores, and specialty shops and have the reputation of being of good quality and medium-priced.

Your committee is thinking about entering the European bedding market. You know little about the European market,

so you are thinking about forming a JV. Your committee has identified three possible candidates for such an arrangement.

One candidate is Bedrest. Bedrest is a French firm that also makes bedding. Unfortunately, Bedrest products have a poor reputation in Europe and most of its sales stem from the fact that its products are exceptionally cheap. However, there are possibilities for growth in Eastern Europe. The consultant who recommended Bedrest suggests that your higher-quality products would mesh well with Bedrest's cheaper ones. Bedrest is known to be having financial difficulties because of declining sales. However, the consultant thinks the firm will soon turn things around.

A second candidate is Home Furnishings, Inc., a German firm that manufactures high-quality furniture. Its line of bedroom furniture (headboards, dressers, chests, and so on) is among the most popular in Europe. The firm is also known to be interested in entering the U.S. furniture market. Home Furnishings is a privately owned concern that is assumed to have a strong financial position. Because of its prices, however, the firm is not expected to be able to compete effectively in Eastern Europe.

Finally, Pacific Enterprises, Inc., is a huge Japanese conglomerate that is just now entering the European market. The firm does not have any current operations in Europe but has enormous financial reserves to put behind any new undertaking it might decide to pursue. Its major product lines are machine

tools, auto replacement parts, communications equipment, and consumer electronics.

Your task is to assess the relative advantages and disadvantages of each of these prospective partners for Resteaze. The European market is important to you, this is your first venture abroad, and you want the highest probability for success. After assessing each candidate, rank the three in order of their relative attractiveness to your firm.

13-20. How straightforward or ambiguous was the task of evaluating and ranking the three alternatives?

13-21. Determine and discuss the degree of agreement or disagreement among the various groups in the class.

CLOSING CASE

Look Before You Leap

Groupe Danone SA, the Paris-based marketer of yogurt, nonalcoholic beverages, and baby foods, has long been a savvy international competitor. Employing 102,000 persons, its sales in 2012 totaled €20.9 billion, 90 percent of which are outside of France, its home country. It is the world's largest seller of fresh dairy products, and the second-largest vendor of bottled water and infant nutrition products. Like many other MNCs, Danone believes emerging markets—which currently produce one-third of its sales—offer it significant opportunities for growth. Danone has adopted a strategy of allying with local companies to penetrate promising emerging markets. Danone contributes its financial clout, manufacturing expertise, and sophisticated marketing skills to these JVs, and the local partner contributes its knowledge of the host country's legal system, political process, distribution channels, and the consumption habits of local consumers.

In Bangladesh, for example, Danone created a joint venture with the Grameen Group (see page 588 for a fuller discussion of Grameen). Danone viewed Bangladesh's 164 million people as an untapped market. Grameen had two different, but complementary goals. It wished to improve nutrition in that country through the provision of healthier foods. It also wanted to reduce poverty by creating new markets for Bangladeshi farmers. To accommodate Grameen's goals, Danone had to make some changes in its normal business practices. For example, its local factory uses as little automation as possible to maximize job creation, and Danone scientists tinkered with product formulas to eliminate the need for sugar, which would have had to have been imported. Grameen Danone's first product is low-priced Shoktidoi yogurt (Bengali for "yogurt that makes you strong"), which is fortified with vitamins to overcome nutritional deficiencies in the diet of rural children. Shoktidoi yogurt is made using milk provided by local farmers and is sweetened with molasses made from locally produced dates.

Danone adopted a similar strategy in entering the Chinese and Indian markets. In the former market, Danone established a partnership with Zong Qinghou, the entrepreneur who in the 1980s founded the Hangzhou Wahaha group, a drink manufacturer and owner of one of China's most famous brand names, Wahaha. Starting in 1996, Danone and the Wahaha group formed a series of JVs—a total of 38 in all—to produce soft drinks, sport drinks, tea, and bottled water. In most of these JVs, Danone had a 51-percent ownership share and Wahaha a 49-percent share.

On paper, these JVs were quite successful; most enjoyed large market shares with significant growth prospects. For example, Wahaha is the largest bottled-water marketer in China, with a 39-percent market share. Danone's JV with Hangzhou Wahaha and another small partner made Danone the country's largest soft drink seller, with an 18-percent market share. Its soft drink sales enjoyed annual growth rates between 10 and 15 percent in the past several years.

Despite the market successes of these companies, the relationship between Danone and Hangzhou fell apart. Danone argued that Zong Qinghou, the founder of Hangzhou Wahaha, set up without its permission 20 parallel soft-drink businesses, with cumulative sales of \$1.46 billion, which operated outside of the Danone-Hangzhou agreement. Zong did not deny his creation of these parallel companies. Rather, he responded he was forced to do so to protect his rights to the Wahaha brand name and because Danone was not aggressive enough in building and investing in their JV operations. Zong also argued that Danone has been unfaithful as well, investing in other Chinese companies—such as the Mengui dairies and the Hui Yuan company, a manufacturer of fruit juices—that competed with their JVs.

Besides depriving it of its share of the profits, the parallel operations, in Danone's view, made it impossible to determine if the products sold to consumers were legitimate.

Accordingly, Danone sued Zong and Hangzhou Wahaha in Chinese, Swedish, and U.S. courts, alleging they had violated the JV agreement. Danone did not fare well in Chinese courts. Danone claimed its JVs had the right to the Wahaha name. However, when Hangzhou Wahaha first submitted its request to transfer the Wahaha brand name to the JVs as was required by their contract, Chinese regulatory authorities failed to approve it. No reapplication of the request was ever made. Thus, in December 2007, the Hangzhou Arbitration Commission ruled that Danone had waited too long to demand that Wahaha transfer ownership of the Wahaha brand name to their JVs. Subsequent to this ruling, Danone suspended its lawsuits, hoping that the Chinese government would recognize the importance of protecting foreign companies' legal rights and that the Chinese and French governments would intervene to help settle the disputes. Its hopes for a political solution came to naught. Accordingly, in 2009, Danone chose to surrender: It sold its 51-percent share of the JV to Wahaha for €300 million, ending their dispute.

Danone had the opposite problem in India. Danone and the Wadia family each owned about one-quarter of their JV in India, Britannia Industries Ltd., with the remainder publicly held. Danone preferred to be more aggressive in introducing new products in India. Unfortunately, as part of its agreement with the Wadia family to market foodstuffs there, its 1995 contract stated it could only introduce new foodstuffs in the Indian market with the consent of the Wadia family, which was unwilling to do so. As was the case with its Wahaha JVs in China, in 2009 Danone sold its stake in Britannia Industries to the Wadia family for \$170 million.

Case Questions

- 13-22. Grameen Danone is a JV among two companies—the nonprofit Grameen Group and the for-profit Groupe Danone SA. What are the benefits of this JV to each of these companies? Why did each choose to participate in the JV?
- 13-23. From the perspective of each of the partners, are there any potential pitfalls to joining this JV?
- 13-24. Now consider Danone's JV in China. What were the benefits of this JV to each of these companies? Why did each choose to participate in the JV?
- 13-25. What could Danone have done to avoid the problems it encountered in China and India?

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- 13-26. What are the three primary means by which JVs can be managed? What are the advantages and disadvantages of these three approaches?
- 13-27. What factors should a firm consider in selecting a strategic alliance partner?
- 13-28. Mymanagementlab Only—comprehensive writing assignment for this chapter.

Endnotes

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