



Managing Alliances And Joint Ventures

A White Paper by Daniel Park, Associate Consultant, B2B International

E-mail info@b2binternational.com
Web www.b2binternational.com
Blog www.b2binternational.com/b2b-blog/





INTRODUCTION

The first of the two B2B International white papers on alliances and joint ventures was posted to the website in May 2008. It was concerned with scoping out and evaluating possible opportunities. This second white paper is concerned with the specific management challenges that are posed by collaborative structures. It is set out in the following way.

1. Meeting the needs of two or more partners
2. Managing the route to the deal
3. Choice of organizational form
4. Selection of managers
5. Control of the operation
6. Dealing with variance and divergence
7. Summary and general remarks

1. MEETING THE NEEDS OF TWO OR MORE PARTNERS

THE DEMANDS OF MULTIPLE OWNERSHIP

As in the scoping/evaluation phase, achieving a balance between the needs of different partners is crucial to the ultimate success of the venture once one moves into implementation and management. The first set of questions relates to the expectations of the partners and in particular the capability of each partner to sustain costs over time before revenue stream turns the operation positive. Assuming that the collaborative option is the best of the alternative options for developing two or more companies, it is usually the case that the initial discussion of the deal focuses on how to share the proceeds. What is more important is to look at costs and timing and the impact of these two phenomena on the participating companies.

Put simply, the first part of the discussion should focus on the balanced contribution of each partner; the requirements in terms of return of/on capital and the time-scale for this; the minimum performance requirements in financial and non-financial terms. Each participant needs to view each venture as if it were an independent investor with hurdle rates that reflect not only its cost of capital but also the opportunity cost of pursuing the venture plus any risk premium that the venture should be required to accept.

These issues are frequently overlooked and a premature discussion takes place that results in a laborious route to agreement on profit share, with insufficient attention to the creation of profit in the first place. It goes a long way to explaining why the instance of financial restructuring, as set out in the Harvard Business School data in our Scoping Out Alliances And Joint Ventures white paper, is so high.

Valuation of "sweat equity" or physical resource is a potential minefield, particularly when one partner is a fairly large company and the other(s) quite small or young. In these circumstances the smaller/younger partner(s) would often contribute in kind rather than in cash, particularly in units of human resource. This requires valuation and agreement early on.



Another area that is frequently neglected is the process for termination of the venture. It has been described as “planning for a possible divorce on the wedding day itself”. Given the risks quantified in Scoping Out Alliances And Joint Ventures and in the event that the venture diverges from track to an extent that its continuation makes no business sense, a cost-effective wind-up process is needed so as to avoid further unnecessary expense.

THE FORMAL REVIEW PROCESS

Each venture will have an executive management structure at the operational level. However, a supervisory group – rather along the lines of supervisory boards found in German industrial structures – is useful in representing the interests of partners and to offer guidance, particularly in the early stages.

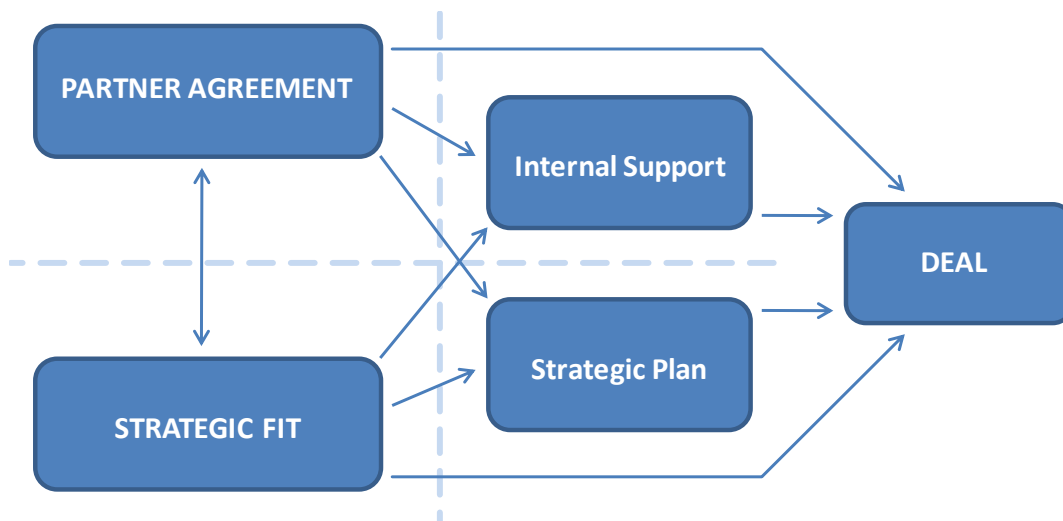
This is where the agreement of performance criteria and performance measures and the clarity of this agreement is paramount, since almost all collaborative ventures do not stick to the development path originally forecast. Review periodicity should be monthly in the initial phase, and then can gradually be reduced to a 6-monthly period. The focus should be on understanding and supporting the correction of variances rather than on directive management of the detail.

Quite simply, the role of the supervisory board is not to run the venture by “remote control” but to provide inputs and catalysis for the operating management team. Excessive parental involvement, though understandable, is a recipe for demoralizing the venture team.

2. MANAGING THE ROUTE TO THE DEAL

PROCESS IN SECURING AN AGREEMENT

The process via which a deal can be reached in setting up a collaborative project (partial alliance) or joint venture company (full alliance) can be summarized as follows.





KEY ISSUES IN SECURING AN AGREEMENT

Objective conceptual and managerial robustness in the basic venture is insufficient to guarantee its ultimate success. The other element is to neutralize internal opposition to the venture in the first instance. It is very rare to undertake a collaborative relationship without encountering some measure of internal opposition in one or more of the partner organizations. Such opposition occurs mainly because the creation of the venture is almost always a response to an opportunity that partner companies cannot undertake alone and which therefore appears unusually risky. Moreover, collaborative ventures can be viewed as a threat to established structures and beliefs simply because often they are exactly that. In these circumstances it is not a good idea to pretend otherwise. Managing internal opposition is as difficult and necessary as managing the process of creating and running the venture itself. Dealing with this at an early stage is one of the most essential elements in securing later success.

It is, therefore, essential to ensure that a collaborative venture should have the overt support of senior executives in the participating organizations. Tacit top management “approval” with an inbuilt backsliding opportunity in reserve is a widespread feature of troubled collaborations. The processes relating to analytical and political considerations should be undertaken in parallel, as shown in the diagram above.

Other key issues center on fluency in the process of gaining agreement. Successful collaborative ventures are not characterized by drawn-out discussion and protracted negotiation, with perhaps the only exception found in the case of major political involvement in very large-scale undertakings. If the idea is intrinsically robust then it ought to be obvious to the prospective partners. Lengthy wrangling over detailed minutiae of the basic agreement is almost always a predictor of trouble to come.

3. CHOICE OF ORGANIZATIONAL FORM

TYPES OF COLLABORATIVE RELATIONSHIPS

It is useful to consider the different forms of collaborative initiative that are available. The requirement is to choose the optimal organizational form not the most obvious. The main ones can be broadly summarized as follows, with an example of each.

Informal or semi-formal agreement	"Ryanair recommends Hertz."
Project-focused alliance	Very large-scale civil engineering/construction
Product-focused alliance	Roche markets "Zantac" for GSK in USA
Service-focused alliance	The three major global airline alliances
Joint design-research-development	Philips/Sony in pre-competitive phase of DVDs
Joint/parallel production	Fiat (I) and FSO (PL) "Cinquecento"
Cross-invested operations	KLM with NWA
Joint marketing	Airline/hotel/entertainment "packages"
Joint branding	Credit Suisse First Boston (before CS purchase of FB)
Subcontracting	Codeshare flying
Licensing	Anchor Malaysia brewing Guinness in Kuala Lumpur
Franchising	Holiday Inn and several other hotel chains
Supply chain linkages	"Guest engineering" in many manufacturing sectors
Informal or semi-formal agreement	"Ryanair recommends Hertz."

It will be seen from the above that it is not always necessary, or desirable, to form a joint venture **company**: there should be a clear strategic and operational rationale for so doing.

CHOICE – THE CORRECT OPTION VERSUS THE OBVIOUS ONE

The choice of relationship can be critical. It depends on the depth of relationship that is required, and this ranges from a simple "gentlemen's agreement" to a fully incorporated entity.

Why incur the cost of setting up a joint venture company when a simple franchising operation could achieve better results quicker and cheaper? Several of the larger hotel chains operate very successfully using this mechanism, attracting owner-investors into the core business. In a different dimension, the growth of airline alliances is due as much to operational cost efficiencies than to marketing benefits, such as (a) the sharing of maintenance and terminal facilities with greater uptime and resource utilization and (b) economies of scale in purchasing components for increasingly homogeneous airplane fleets.



4. SELECTION OF MANAGERS

WHAT IS SPECIAL ABOUT A COLLABORATIVE RELATIONSHIP?

There are four main points to bear in mind when selecting managers for this type of organizational structure. These are as follows:

1. Synergies do not occur automatically, even when the potential for synergies is obvious.

As with mergers and acquisitions, realizing the benefits of apparent synergies is a lot more difficult than is usually anticipated. Managers have to know how to make these happen – clearly and quickly. Many things can get in the way of achieving synergies for which the collaborative venture was set up. Managers need to be aware of possible conflicts in marketing styles, extent of financial risk that can be borne, ethical standards in pursuing business objectives in alien cultures, and a host of other dimensions. It is dangerous to assume that synergies will be realized simply because it is clear that they ought to.

2. The human resource dimension is a critical success factor.

Whether the alliance involves a national or international operating structure, the question of human resources is often the most difficult, especially in the initial stages. The critical issue here is to ensure that whoever is leading the venture is aware of the cultural dissimilarities that characterize the members of the collaborative ownership. This can be as severe in a national as in an international partnership. We turn to this in the next two points.

3. Basic “technical” competencies are relatively straightforward.

The basic technical competences are no different in an alliance than in a single-parent operation. Depending on the purpose and focus of the alliance, competencies such as marketing, finance, project management, production scheduling, etc are no different in an alliance from any other organizational structure.

4. Specific competencies relate to the “collaborative” and “joint” elements.

The specific challenges relate to the fact of multiple ownership, and these are manifest most strongly when there have been deficiencies in managing the process of creating the alliance. The main challenge is putting in place an effective system of communication and ensuring that it is implemented. It is clear that the communication channels must work for more than one parent, otherwise misunderstandings, errors and delays creep in with alarming speed and alliance managers are left spending too much time in picking up the pieces.



SPECIFIC COMPETENCIES IN THE CONTEXT OF A COLLABORATIVE VENTURE

page
6

The specific competencies that relate to management of collaborative ventures are fourfold, as follows.

1. Dealing with more than one “boss”

As Director/General Manager of a collaborative venture the leader will have to work effectively with more than one “boss”. No matter how effective is the process of delegation on the part of parents represented in the supervisory team, the fact remains that the nature of a collaborative venture is that its leader has to satisfy more than one boss. The skill required here is in ensuring that objectives, policies and performance measures are agreed on time lines that enable the venture to perform as if it were fully independent.

2. Balancing parental and local demands

As with any business strategic and operational decisions are made under conditions of (often substantial) uncertainty. It is almost certain that in any collaborative venture the participating parent companies will have differing criteria in issues such as risk levels, investment ‘hurdle rates’ and internal transfer pricing, to identify just a few potential problem areas. All these issues should, as argued earlier, be part of the decision sphere of the collaborative venture itself. However this is a utopian wish. Effectiveness in gaining commitment of parents in a situation in which does not compromise business sense for the venture is crucial.

3. Creating effective communication systems

Following naturally from the first two points above, the ability to create an effective communication system that keeps each parent ‘in the loop’ is something specific to collaborative ventures. Rather than providing every piece of minute operational data and decision to parents, the leader of a collaborative venture should communicate only (a) divergences from plan and decisions to bring the venture back on track and/or (b) advance warnings of events that could in the foreseeable future require input and guidance from parent companies.

4. Coping with two or more parent company cultures

Analysis of success and failure of collaborative ventures highlights the critical skill on the part of management in coping with differing cultures in stakeholder organizations. This issue is very often overlooked in the process of creating the collaborative venture and only surfaces at a later stage, often when difficult decisions have to be made on approaches to specific aspects of the business. Ideally the creation of a culture that is unique and appropriate to the collaborative venture itself is the proper solution to this issue.

However, that is again utopian. To take an example, how, if at all, does a collaborative venture do business with unethical companies or repressive regimes when the position and policy of parent companies diverge on the issue? Assuming, as is too often the case, that this issue does not get addressed in advance, the leader of the collaborative venture has to be able to get parents with diverging views to reach a clear and quick decision.

Avoid “sideways promotions”.

Managing a collaborative relationship is not an activity in which a “sideways promotion” is an appropriate mechanism for appointing any level of management. It is an activity for top-class executives and should be a significant career development position. Top management in each of the parent companies should acknowledge that in addition to the skills required in business management there is another set of high-level skills that are particular to collaborative relationships, especially when one of more aspects of the relationship are international. This specific skill set is most significant when the organizational form has the characteristics of the more developed mechanisms – supply chain partnerships and joint venture companies.

Analysis of collaborative ventures that run into difficulties almost always points to management selection as a prime cause. Quite simply, a collaborative venture requires top performing managers. Even then success in a single company environment might not transfer if the additional competencies specific to collaborative ventures are not found.

5. CONTROL OF THE OPERATION

CONTROL FRAMEWORK AND KEY POINTS

Collaborative operations require close but “light touch” approach to management on the part of the parent organizations. This framework can be summarized in six key points.

1. Parents should set only a few objectives that are clear and measurable.

What gets measured gets done. In the early stages the objectives and performance measures should be relatively few, unambiguous and easily measurable. Progress towards financial break-even with a time target should be a top objective. Revenue, cost reduction, time reduction, productivity, etc are examples of the type of simple, measurable objectives that necessarily should in the earlier stages take precedence over the “softer” measures such as customer satisfaction, product comparisons, customer mix. This is not to state that these issues are unimportant: it is to recognize priorities that are most likely to ensure success and stability of the venture.

2. A collaborative venture should set its own business strategy and operating plans.

Control freaks ought not to be involved in supervising a joint venture on behalf of a parent company. Successful ventures from projects up to full joint venture companies have in common a freedom to set their own plans and take full responsibility for their own destiny. Failed ventures share a characteristic - lack of “ownership” of business plans and repeated imposition of ever-changing directives from parent shareholders. Strategy and plans should always be subjected to presentation, discussion, modification and final approval by the supervisory team. This then constitutes commitment not only on the part of the venture team but also the parents.



3. Parents should review performance frequently in the early stages and then back off.

The best contribution that parents can make is to offer a “guiding hand” in the early stages and then to back off fairly quickly. Venture managers should be required to give early warning signals of variance or possible divergence from plan, but a parent company that acts like a gendarme guarantees a dead hand on initiative and potential success. Alliances and joint ventures are the ultimate form of delegation: the broad principles of delegation apply.

4. Parents should manage support not operational implementation.

The role of parents companies can be summarized as one of removing obstacles rather than getting involved in operational decisions.

Many collaborative ventures, particularly project-based ones, rely on inputs from one or more of the parent companies. Time is wasted if the management team of the collaborative venture is constantly arguing for inputs and transfers that ought to take place naturally. This and similar obstacles are the pressure points at which executives of the parent companies can make the most useful contribution to the venture.

5. Start-up usually takes longer than planned, but parents should set a maximum tolerable “sunk cost”.

Referring back to the Harvard Business School analysis in Scoping Out Alliances And Joint Ventures, we see that even satisfactory ventures sometimes require financial re-structuring before ultimate success is achieved. The sunk cost dimension is one of the most difficult to deal with – a view that “we’ve put so much into this already and it will only take a little more.....etc”. At the outset there should be a clear view as to the maximum sunk cost that the venture can be allowed to incur before a decision to terminate is considered. Then the partners should move ahead unemotionally.

6. A collaborative venture should be allowed to operate as an independent entity.

This is just about the most difficult dimension in the management of a collaborative venture. Case experience points to excessively eager “parenting” as a frequent cause of disappointing venture performance and even outright failure.

The first thing to accept is that parents should think of themselves as interested shareholders or venture capitalists not as venture managers. However, as risk takers, parents in this context have the right to influence the venture. The issue here is to identify the right type and quantity of influence that can best contribute to the venture. The answer is found in attitudes to operational management. The solution to this issue is to ensure that operational management in a collaborative venture has the confidence to seek guidance and input rather than end up needing it in a crisis. The best representatives of parents in working with a collaborative venture are executives who themselves have had prior experience in running a collaborative venture.



THE ISSUE OF SUPPORT NOT DIRIGISME

Parent companies should see their role as supportive not interventionist, unless there is a divergence from plan that looks as if it could sink the venture.

The least useful contribution that any parent can make to a collaborative enterprise, whether this is a simple agreement or a full joint venture company, is to try to micro-manage it. There are two main reasons for this: (i) it would tend to demoralize the venture team and (ii) it undermines the rationale for setting up a collaborative structure in the first place.

What experience and ideas do executives from parent companies have that they can share with management of a collaborative venture. Supporting management with ideas and shared experience rather than telling them what to do is a worthwhile contribution.

All the foregoing might give the impression that I am making out a case that management of collaborative ventures is different and more difficult than managing a single-owner operation. If so, good. That is what I hoped to do.

6. DEALING WITH VARIANCE AND DIVERGENCE

PLANS AND FORECASTS

The only certainty about plans and forecasts is that they are most unlikely to turn out as originally expected, unless you are lucky. The big issue here is to recognize variance from the desired trend line and divergence from that line. Variance is to be expected: in most instances any venture will be above or below trend line but the question is whether it is actually on trend.

Divergence, positive or negative, is a different issue.

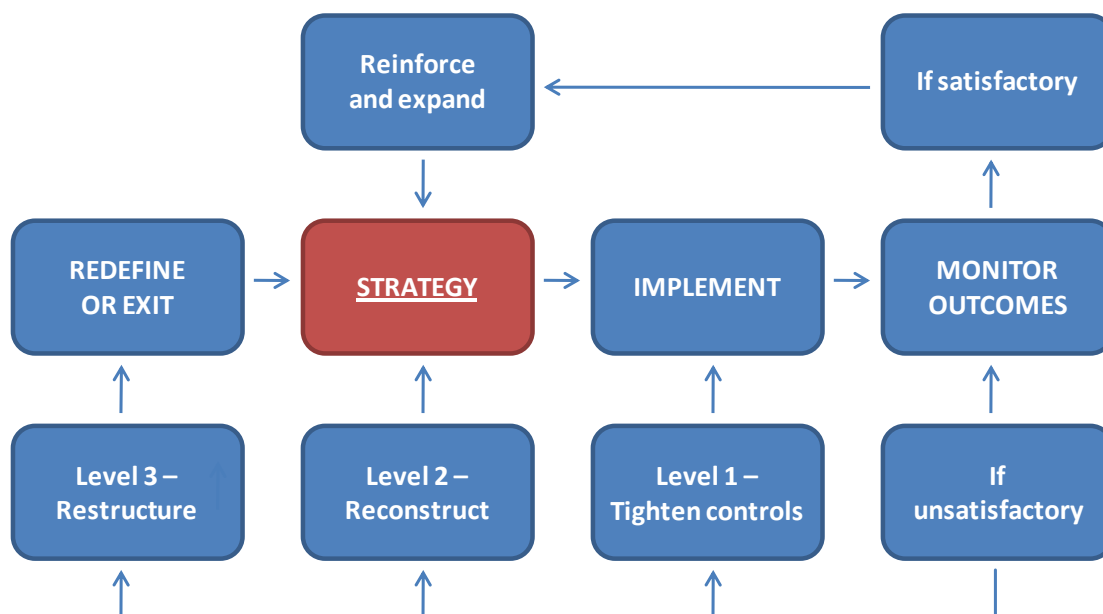
The performance of a venture may be underestimated or overestimated. The financial and operational implications are the same as for any commercial organization. Is it under-resourced – in other words ought we to allocate more resources and revise upwards the assumptions and plans on which the venture was launched?

Alternatively is the venture heading for trouble – in which case how do we get out with as little loss as possible? It is in both sets of circumstances that the position, resources, objectives and criteria of each parent company have to be considered carefully. It may be the point at which to alter the relativities in the ownership structure so as to take into account the different capacities and broader corporate objectives of the individual parents.

Hard analysis and fluent decision-making are required in the above circumstances.

THE MANAGEMENT PROCESS

The management process for a collaborative venture should not differ radically from that of any single-owner operation. It can be summarized in the following diagram.



7. SUMMARY AND GENERAL REMARKS

The key success factors in managing a collaborative relationship can be summarized as follows.

- Realistic and clearly defined objectives and performance measures.
- Contribution of sufficient resources to the venture.
- Assignment of accountability and commensurate authority.
- Design and implementation of effective “information retrieval” process.
- Transfer/recruitment of key people as a career development move.
- Close but “light touch” monitoring of progress.

Finally, as we saw in the analysis conducted by the Harvard Business School that was set out in the Scoping Out Alliances And Joint Ventures white paper, alliances and joint ventures are difficult mechanisms to manage. Taken seriously, however, they give access to business and added value that could not be gained by acting independently.

Inevitably this short paper cannot do full justice to the complexity and challenges presented by the collaborative form of organizational development and business management. Hopefully it will highlight the main issues to be faced in setting up and running a collaborative venture without putting anyone off considering this as an option. Collaboration is an approach to business and market development that is not restricted to large companies: it is relevant to SMEs also. More companies should take a look at this.



Daniel Park
25 July 2008

page
11

Dr Daniel Park is an economist, specialising in business strategy, organisational development and international marketing. He is co-founder and partner in MASS Consulting Group, Manchester, UK and has been associated with B2B International Ltd since the foundation of the company, advising on many of the company's international projects. He is the author of 48 published works on international economics and business and is a frequent conference speaker on these topics.



B2B International
Americas | EMEA | Asia-Pacific

email: info@b2binternational.com

web: www.b2binternational.com

blog: www.b2binternational.com/blog

MARKET RESEARCH WITH INTELLIGENCE