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## Appraisal of Strategic Alliances and Corporate Effectiveness

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### Abstract

*The paper appraises strategic alliances and corporate effectiveness. The findings of the study are; strategic alliance of firms leads to effectiveness, it helps in sourcing the required capital, it minimizes competition among firms in similar market and it is a tool for penetrating saturated or complex markets. The study concludes that: Strategic alliances provide opportunities for participants to tap into the resources, knowledge, and skills of their collaborators; it provides social potential for the strategic allies to significantly leverage its member's resources and capabilities, it helps*

*partners in an alliance to overcome legal, political and socio-cultural barriers to cross-national transactions. The paper recommends that firms that aim at achieving effectiveness in their operations in the face of scarce resources should take advantage of strategic alliance through which they will be able to accumulate adequate capital, penetrate saturated or complex markets, fight competition, and achieve competitive advantage.*

**Key Words:** Appraisal, Corporate, effectiveness, Strategic Alliance.

## **Introduction**

Joint venture is a popular strategy used by two or more companies to capitalize on opportunity or to minimize threat. It is a strategy that allows companies to put their resources together in order to achieve their strategic objectives. International joint venture involves two or more companies that put their stock and/or other resources together in an agreed percentage to establish a subsidiary company in a foreign country. This strategy is used when the distinctive competencies of the two or more companies concerned complement each other (Aloko, Odugbesan, Gbadamosi and Osuagwu, 1997).

On the other hand, strategic alliance is where two or more companies come together to share resources and activities together, in order to pursue a strategic objective. This option might be resorted to due to a number of reasons which include; high cost or capital requirement for the resources concerned, environmental factor, legal requirement, technical expertise required by the resources, and so forth. In Nigeria, strategic alliances have become popular as a means of surviving the ever complex environment. Its uses cuts across sectors of the Nigerian economy; banking, oil, Manufacturing, to mention but a few.

Joint venture and strategic alliances have existed in Nigeria since early 1980s. However, the two strategies became more obvious in recent years due to the effects or pressure of globalization on local firms, unfavourable rivalries among firms, global economic meltdown and lately, minimum capital requirement as demanded by regulatory authorities. For instance, the Nigerian Central Bank request for a minimum operating capital of 25 billion naira for Commercial Banks operating in Nigeria in 2005 led to a number of strategic alliances and joint venture of a number of Banks. However, while some joined their capital and formed brand new Banks, some acquired others,

while the remaining formed strategic alliances. Some international business literature argued that there are benefits for companies that engage in strategic alliances. These benefits according to them include: higher return on equity, investment and improve effectiveness of the firms in the strategic alliance.

### **The problem of the study**

A number of organizations across the world today are either dead completely or operating below their normal capacities due to some or most of the following challenges: cross border market penetration challenges; the challenges of raising adequate capital to acquire enough operational assets, competition among firms producing similar product and in the same market, while others are faced with vertical and/or horizontal integration challenges to minimize operational expenses that accrues to firms that are into strategic alliances. In Nigeria, the major problem asides competition facing most firms across the sectors of the economy is the minimum capital requirements as set by the regulating bodies. For instance, in 2005 the Central Bank of Nigeria fixed Twenty-five Billion naira (N25b) as the minimum acceptable capital for any commercial bank that must operate in Nigeria. The policy brought a number of them into forming strategic alliances, while those that could not were either acquired by others or went into liquidation.

The questions now are: Does a strategic alliance among firms improve their service and operational effectiveness? Can firm use strategic alliance to improve their capital? Does strategic alliance of firms minimizes competition and improve profitability of firm?

### **Objective of the study**

The major objective of the study is to appraise strategic alliances as experienced in the Nigerian Central Bank's banks consolidation of 2005 and the alliance in the Nigerian oil industry of five downstream oil firms. The specific objectives are to;

- i. evaluate the impact of strategic alliance on firm capital requirement.
- ii. assess the effect of strategic alliance on competition and profitability of firm.
- iii. determine whether a firm can use strategic alliance to penetrate saturated or complex markets.

### **Concept of strategic alliance**

The term Strategic alliance may be defined as collaborative agreement between or among potential competitors or non-competitors. Strategic alliances can be through a joint venture or through short-term collaboration of two or more companies to execute particular projects. The two mentioned strategies may be as a result of the need to achieve efficiency and competitive advantages and/or to avoid the pitfall of market uncertainties, and structural rigidities. Strategic alliance according to Yoshino and Rangan (1995), is alliance that involves at least two partner firms that are legally independent after the alliance; share managerial control over task; make continuous contribution to the objective of the alliance.

### **Strategic alliances through joint venture**

Joint venture between two or more companies is when companies create a jointly owned legal organization to achieve an agreed purpose such as research and development (R&D), marketing, and other objectives. Asides direct exporting, joint venture is the second method of entering a foreign market. It involves joining with foreign companies to produce or market products or services. It is different from exporting with a partner to market abroad (Kotler, Armstrong, Saunders and Wong, 1999). They stated further that there are four types of joint ventures; licensing, contract manufacturing, management contracting and joint ownership.

There are a number of Joint Ventures in Nigeria, especially, in the oil and gas industry. For instance, Total Nigeria Plc, National Oil and Chemical Marketing Company Plc, Texaco Nigeria Plc, and Mobil oil Nigeria Plc formed a joint venture in 1979. They formed a company known as Joint Users Hydrant Installation Depot. This depot was jointly financed to provide storage facility for aviation fuel (Jet A1), for hydrant fuelling operations at the Murtala Mohammed International Airport, Lagos-Nigeria. This venture was a capital intensive one that no single company as it were, was able to fund, but through the joint venture agreement they were able to fund the venture, and achieved their strategic objectives. The hydrant is still in used till date and the partners have benefited immensely in the alliance.

Furthermore, a number of joint ventures also exist in the Nigerian upstream sector. This includes the joint venture between the Nigeria National

Petroleum Corporation (NNPC) and Chevron Nigeria Limited (CNL). In this venture, NNPC own 60% and Chevron 40% of the stake respectively.

### **Motive for alliances**

There are a number of motives for strategic alliances between and among firms. However, they tend to be of three main types (Johnson, Scholes and Whittington, 2005). The motives for strategic alliance by firms include:

1. The need for critical mass: Alliances bring competitors or those producing complementary goods or services together. This leads to cost reduction and increases in customer value and satisfaction.
2. Co-specialization: It allows partners to specialize on the activities that maximize the achievement of their strategic objectives or where their capabilities are best used. For example, producer may form an alliance with distributors for the effective marketing of his goods and services by those who possess the capabilities to do so in a particular geographical region.
3. To learn from partners: This helps the allies to learn and develop distinctive competences that may be useful elsewhere. For example, partnering with those firms that are successful in the area of interest helps partners to gain knowledge that can be useful in another area of business.

### **Types of strategic alliances**

There are a number of strategic alliances in existence among firms. The type that is favoured or adopted by firms or group of firms at a time is a function of their objectives, resources, capability, top management preferences or value, and environment forces. However, some of them include:

1. Joint ventures: They are collaborative arrangements whereby independent firms setup jointly owned firms. This is the highly favoured means of collaboration in China. While the Chinese provides labour and avenue for effective market penetration, the western firms in the venture provide technology, management expertise and finance. In another perspective, joint ownership venture consist of one company joining forces with foreign investors to create a local business in which they share joint ownership and control (Kotler et al, 1999). Joint ownership of business between local and foreign firms is necessitated by a number of reasons,

which include economic and/or political reasons. A foreign government may require that certain percentage of shares be owned by local investor as a condition for entry its market by foreign investors. For example the British Telecom's joint venture with MCI, American's number two Long-distance carriers are cases in point (Kotler et al, 1999). Joint venture has a number of drawbacks which include; investment disagreement by partners, and marketing or others challenges. To benefit maximally by partners to a joint venture, the partners must clarify their expectations and objectives at the beginning and work towards ensuring that all partners equitably benefits from the outcome or profit of the venture.

2. Networks alliances: under this arrangement, two or more firms form alliance with formal relationship to exploit common opportunity. This type of alliance is increasingly being used by airline firms. It is usually to achieve strategic marketing objectives by partners. For example, Air France versus KLM, and Delta versus Swissair Lines are in strategic alliances of this type. The essence of this type of alliance is to among others minimize the rate of competition and operational/marketing costs.
3. Intermediate alliances: In this arrangement, some rights are granted to some firms (franchise) to perform specific activities like manufacturing distribution or selling, while the franchiser undertakes brand name, marketing and if possible training. Also, firms may decide to subcontract part of its activities to another firm under this arrangement.
4. Contract manufacturing: Under this arrangement, a company enters into a contract with manufacturers in a foreign market to produce its product or service. It is mostly used to enter a new market. The challenges of this alliance include lack of control of the manufacturing process and reduction in the expected profit on manufacturing. However, the benefits include; it increases the chances of start time, it is less risky to use than other mode of alliances, and it provides an opportunity for the partner to buy up local manufacturer.
5. Management contracting: In management contracting, the local firm provides managerial expertise to foreign firm or partner who supplies capital for the alliance or venture. The benefit is that profit for the provider of the expertise starts from day one. However, it

discourages self investment or reduces the chances of setting up own venture on the part of the provider of the expertise.

### **Factors influencing the types of alliances**

A number of factors influence the types of alliances to be formed between or among firms in an industry. However, some of such factors are:

1. Strategic capacity: under this, if a strategy requires the use of separate, dedicated, resources, joint venture alliance will be the best form of alliance. Contrarily, if the firm's resources require support from other partners, then, loose contractual relationships can be formed.
2. Speed of market change: Opportunistic alliance will be preferred to a joint venture, if the market situation changes frequently, coupled with increased competition.
3. Environmental risk: if the risk of doing business in an environment is high, firms in the environment will prefer strategic alliance than joint venture.

### **Advantages of strategic alliances**

Firms that involved in strategic alliances stand to gain a lot of benefits. Some of such benefits according to Hill (2000) include:

1. Cost sharing and saving: The firms that would not have been able to finance certain projects will be able to do so, when resources are pool together. Also, the savings from the alliance will be used effectively to pursue other strategic objectives.
2. Complementary skills and other resources advantages: Firms that are endowed with complementary skills and other resources form alliance to take advantage of their complementarities to tap opportunities. Through this, they are able to achieve goals/objectives with minimum cost.
3. It facilitates entry into a new market: Firms can form alliances to enable them penetrate a new market. This is especially, when either of the collaborating partners are already used to the new market. This helps to break the barriers of new entrants into the new market.
4. Minimizes the risk of competition: Strategic alliances by firm are a potent tool for coping with high degree of rivalry in an industry.

Through an alliance they are able to control price and supply to the market for mutual benefits.

5. Risk Reduction and diversification: The risk of the business is collectively shared by the partners, unlike a situation where one firm bears the risk and uncertainty of a business, the collaborating firms in an alliance bear the risk that may arise from the business.
6. Economics of Scale: Through strategic alliances, firms in the collaboration will be able to raise enough capital to benefit from bulk purchases which attracts discounts and other benefits that lower cost and selling prices of the firm's goods/services. This reduction is a competitive tool for winning rivals in competitive market.

### **Disadvantages of strategic alliances**

Despite the fact that strategic alliances has been embraced by a number of firms as easy way out of the global economic meltdown and other environmental constraints that hinders a firm effectiveness, it is however confronted with a number of challenges between or among firms in the union. Some of such challenges according to Hill (2001), include:

1. Management problem: The value of the collaborating firms differs, so also are the managers different in their preferences and culture. These differences in value and preferences structure can be a source of conflicts among managers from the collaborating firms.
2. Low- cost route to new technology and new market: Strategic alliances among firms allow some firm to have cheap access to new technology that would not have been easy to come by through research and development or imitation. However, this benefit will be achieved at the expense of the original owner of the technology. Also, at the expense of the partner(s) that is already familiar with the market.
3. A firm in the union may suffer the risk of receiving less than what it contribute to the alliance.

### **Factors that determine the success or failure of strategic alliances**

The success or failure of any strategic alliances between or among firms is dependent on a number of factors. However, they include:

1. Strategic purpose: The reason for any alliance is to achieve certain objectives. These objectives could be to penetrate a new market,

expand existing market, pursue cost advantage, minimize the rate of competition among rivals, and so forth. However, the levels of accomplishment of the predetermined objectives of the collaborating firms determine the success or failure of the alliance. That is, whether they are realized or not.

2. The level of trust among partners: Trust is the most crucial elements of success or failure of partners in a strategic alliance. Trust is of two dimensions. That is, whether or not the partners have trust on the competences of each other ability to fulfil their part in the alliance; and also on the character of partners compatibility in terms of attitude and integrity to fulfil their part of the alliance. If trust exist among partners in an alliance, then, success will be possible. Contrarily, it will be an illusion of the strategic objectives of the firms in the alliance.
3. Cultural compatibility: Alliances among firms that cut across countries of different cultural background requires extra efforts by partners to achieve a high degree of human relationships that will see the alliance through to the realization of the objectives of the allies. This requires among other things accommodation/adaptability of these cultural differences to achieve the objectives of the alliance. Contrarily, failure becomes imminent.

## **Findings**

The findings of the study from the Nigerian experience include; banks that formed alliances became more effective in their services and operations, they were able to meet up with the minimum capital as required by the Nigerian central bank, they were able to overcome excessive competition and penetrate saturated or complex markets. On the downstream oil firms, they were able to share similar facility to achieve their objective of profitability and effectiveness which would not have been possible with each operating in isolation.

## **Conclusions**

Strategic alliances provide opportunities for participants to tap into the resources, knowledge, and skills of their collaborators in a portfolio of inter-firm agreement (Todeva and Knoke, 2001). It provides social potential for the strategic allies to significantly leverage its member's resources and capabilities. Strategic alliances as option for achieving strategic objectives

through collaborative efforts and resources have proved to be more efficient and effective than the arm's length market exchange strategy. This is because it has helped partners in an alliance to overcome legal, political and socio-cultural barriers to cross-national transactions.

### **Recommendations**

The paper recommends that firms that aim at achieving effectiveness in their operations in the face of scarce resources should take advantage of strategic alliance through which they will be able to accumulate adequate capital, penetrate saturated or complex markets, fight competition, and achieve competitive advantage.

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