Alliances and Mergers

The Build-Borrow-or-Buy Framework

- Choices for Growth:
  - Organic growth
  - Internal development
  - External growth through: alliances or acquisitions
- Build Borrow and Buy Framework
  - Internal development (build)
  - Enter a contract / strategic alliance (borrow)
  - Acquire new resources, capabilities, and competencies (buy)

Recall:
Resource Based View

Resources
Capabilities
Competencies

Valuable
Rare
Difficult to imitate
Organizable

Where do we get such resources?

Strategic Gap in Resources:

- Why strategic?
  - Because closing it may lead to competitive advantage.

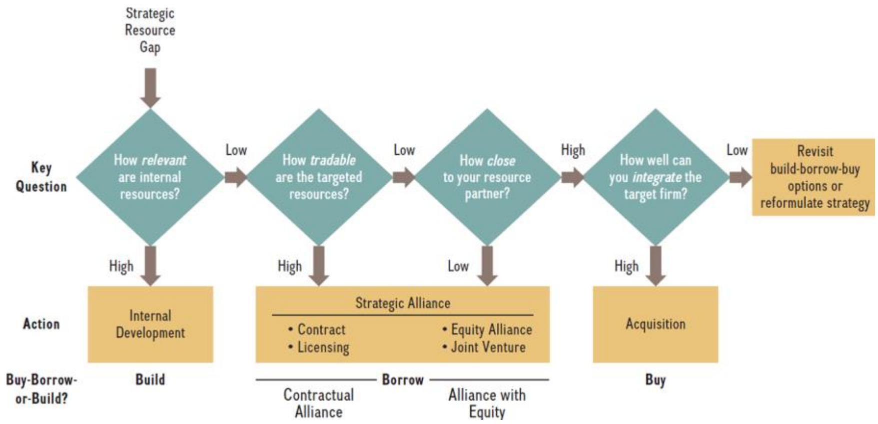
Main Decisions Points:

- Look internally
- Look externally
  - Partner
  - Control

The Main Issues in the Build-Borrow-or-Buy Framework

- Relevancy
  - How relevant are existing internal resources to solving the resource gap?
- Tradability
  - How tradable are the targeted resources that may be available externally?
- Closeness
  - How close do you need to be to your external resource partner?
- Integration
  - How well can you integrate the targeted firm should you determine you need to acquire the resource partner?

Guiding Corporate Strategy: The Build-Borrow-or-Buy Framework



Relevancy: Internal Test

- Are the firm's internal resources high or low in relevance?
  - In relation to solving the resource gap
  - If high, the firm should develop internally.
- Internal resources are relevant if:
  - They are similar to those the firm needs to develop.
  - They are superior to those of competitors in the targeted area.

Tradability: External Option

- The firm creates a contract.
  - Allows for the transfer of ownership
  - Allows for use of the resource
- Short-term and long-term contracts are a way to borrow resources from another company.
  - Licensing and franchising
- Example: biotech-pharma industry:
  - Producers use licensing agreements to transfer knowledge and technology.

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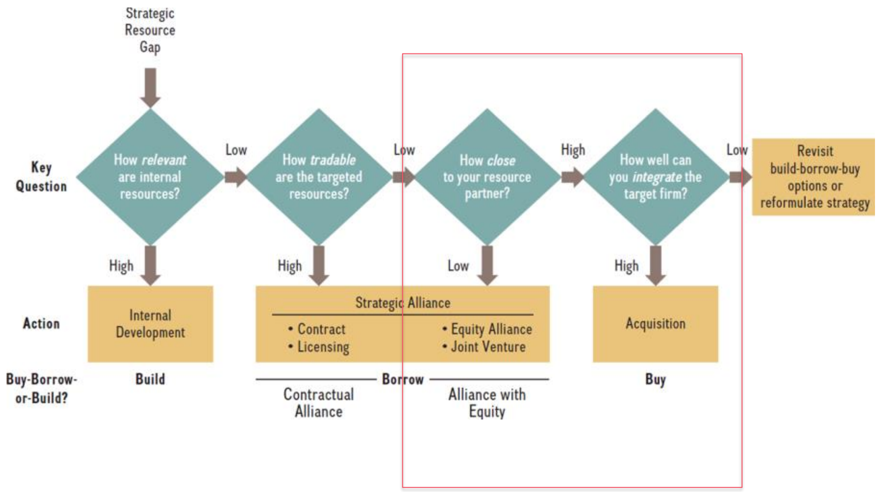


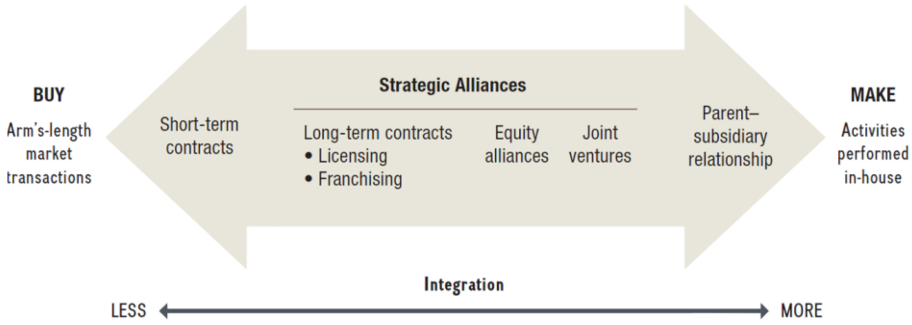
Closeness: Just how close

- Can be achieved through integrated alliances
  - Equity alliances
  - Joint ventures
- Also enables the borrowing of resources

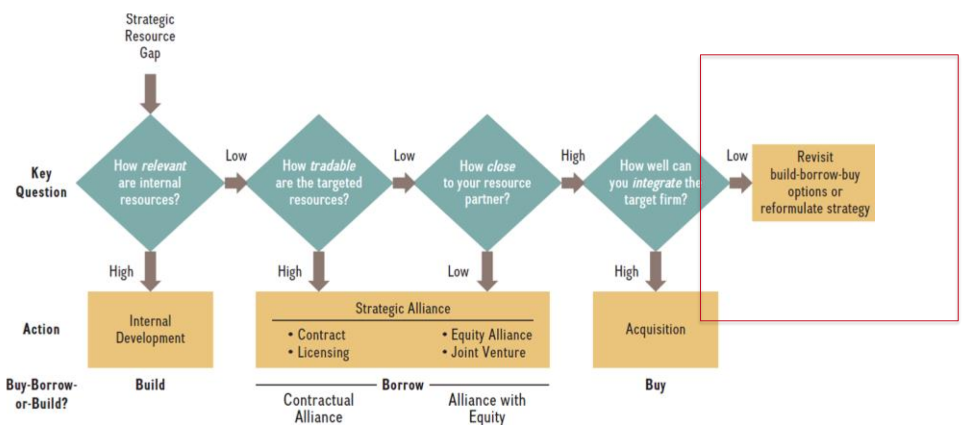
Integration: Bringing into the Fold

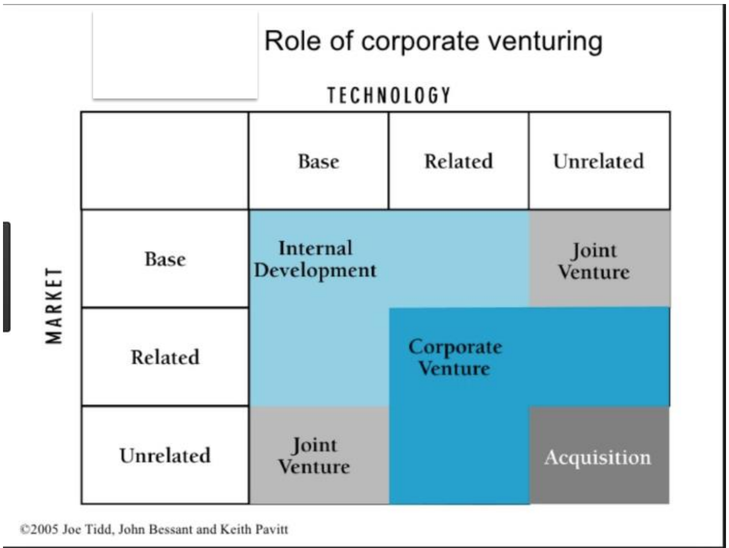
- Mergers and acquisitions are:
  - The most costly
  - The most complex
  - The most difficult to reverse strategic option
- Examples of post-integration failure:
  - Daimler-Chrysler
  - AOL and Time Warner
  - HP and Autonomy
  - Bank of America and Merrill Lynch

Exhibit 8.4 Alternatives on the Make-or-buy Continuum (2 of 2)



Guiding Corporate Strategy: The Build-Borrow-or-Buy Framework





What are Strategic Alliances?

- A voluntary arrangement between firms
- Involves the sharing of:
  - Knowledge
  - Resources
  - Capabilities with the intent of developing:
    - Processes
    - Products
    - Services

Why Do Firms Enter Strategic Alliances?

- Strengthen competitive position
  - Change industry structure or put competitive pressure on rivals
- Enter new markets
  - Products/Services/Geography
  - Geography
- Hedge against uncertainty
  - Stage investment /explore /experiment
- Access critical complementary assets
  - Marketing / R&D /
- Learn new capabilities

Governing Strategic Alliances

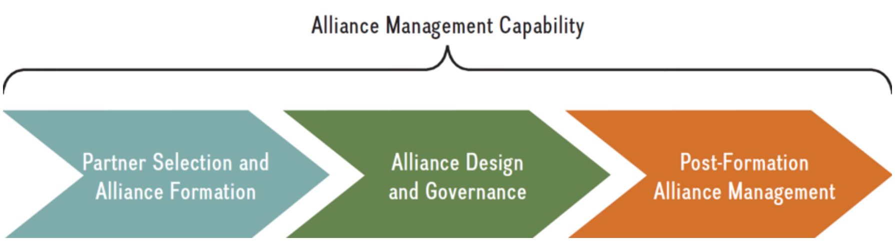
- Non-Equity Alliances
  - Partnerships based on contracts
  - Examples: supply agreements, distribution agreements, and licensing agreements
- Equity Alliances
  - One partner takes partial ownership in the other.
- Joint Ventures
  - A standalone organization created and jointly owned by two or more parent companies

Exhibit 9.2 Key Characteristics of Different Alliance Types

Alliance Type	Governance Mechanism	Frequency	Type of Knowledge Exchanged	Pros	Cons	Examples
Non-equity (supply, licensing, and distribution agreements)	Contract	Most common	Explicit	• Flexible • Fast • Easy to initiate and terminate	• Weak tie • Lack of trust and commitment	• Genentech–Lilly (exclusive) licensing agreement for Humulin • Microsoft–IBM (nonexclusive) licensing agreement for MS-DOS
Equity (purchase of an equity stake or corporate venture capital, CVC investment)	Equity investment	Less common than non-equity alliances, but more common than joint ventures	Explicit; exchange of tacit knowledge possible	• Stronger tie • Trust and commitment can emerge • Window into new technology (option value)	• Less flexible • Slower • Can entail significant investments	• Renault–Nissan alliance based on cross equity holdings, with Renault owning 44.4% in Nissan; and Nissan owning 15% in Renault • Roche's equity investment in Genentech (prior to full integration)
Joint venture (JV)	Creation of new entity by two or more parent firms	Least common	Both tacit and explicit knowledge exchanged	• Strongest tie • Trust and commitment likely to emerge • May be required by institutional setting	• Can entail long negotiations and significant investments • Long-term solution • JV managers have double reporting lines (2 bosses)	• Hulu, owned by NBC, Fox, and Disney-ABC • Dow Corning, owned by Dow Chemical and Corning

Exhibit 9.3 Alliance Management Capability

- The three phases of Alliance Management:
  1. Partner selection and alliance formation
  2. Alliance design and governance
  3. Post-formation alliance management
- Can



Partner Selection and Alliance Formation

- The benefits must exceed the costs.
- Five reasons for alliance formation:
  - To strengthen competitive position
  - To enter new markets
  - To hedge against uncertainty
  - To access critical complementary resources
  - To learn new capabilities
- Partner compatibility & commitment are necessary.

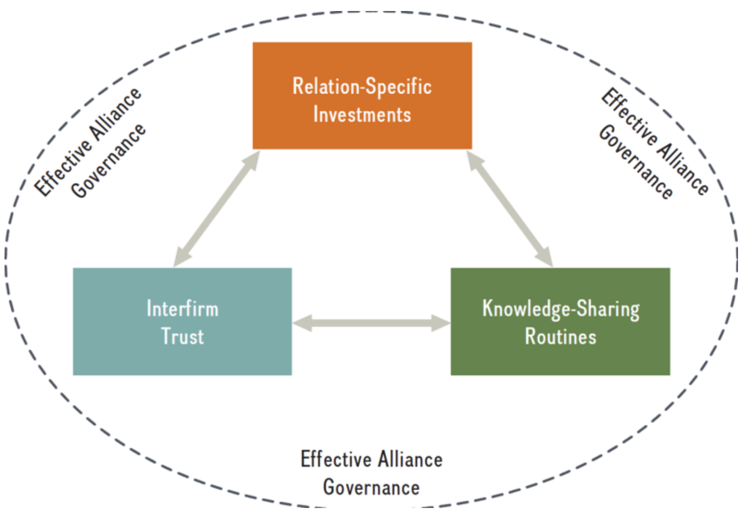
Alliance Design and Governance

- Possible governance mechanisms:
  - Non-equity contractual agreement
  - Equity alliances
  - Joint venture
- Joining specialized complementary assets increases the likelihood that the alliance is governed hierarchically.
- Inter-organization trust is critical.

Post-Formation Alliance Management

- To create VRIO resource combinations:
  - Make relation-specific investments.
  - Establish knowledge-sharing routines.
  - Build interfirm trust.
- Build capability through repeated experiences over time.
  - Repeated alliance exposure improves learning.

Exhibit 9.4 How to Make Alliances Work



Jump to Appendix 3 long image description

Mergers and Acquisitions

- Merger:
  - The joining of two independent companies
  - Forms a combined entity
- Acquisition:
  - Purchase of one company by another
  - Can be friendly or unfriendly.
  - Hostile takeover:
    - The target company does not wish to be acquired.

Why Do Firms Merge?

- Horizontal integration:
  - The process of merging with competitors
  - Leads to industry consolidation
- Three main benefits:
  1. Reduction in competitive intensity
     - Changes underlying industry structure in favor of surviving firms
  2. Lower costs
     - Economies of scale
  3. Increased differentiation
     - Fills product gaps

Exhibit 9.5 Sources of Value Creation and Costs in Horizontal Integration

Corporate Strategy	Sources of Value Creation (*V*)	Sources of Costs (*C*)
• Horizontal integration through M&A	• Reduction in competitive intensity • Lower costs • Increased differentiation	• Integration failure • Reduced flexibility • Increased potential for legal repercussions

Why Do Firms Acquire Other Firms?

- To access new markets & distribution channels
  - To overcome entry barriers
- To access new capabilities or competencies
- To preempt rivals
  - Example: Facebook acquired:
    - Instagram (photo & video sharing)
    - WhatsApp (text messaging service)
    - Oculus (virtual reality headsets)
  - Example: Google acquired:
    - YouTube (video sharing)
    - Motorola (mobile technology)
    - Waze (interactive mobile maps)

M&A and Competitive Advantage

- Benefits of mergers & acquisitions are often hard to achieve.
  - Anticipated synergies don’t materialize.
- Other reasons to merge:
  - Principal-agent problems
  - The desire to overcome competitive disadvantage
  - Superior acquisition and integration capability