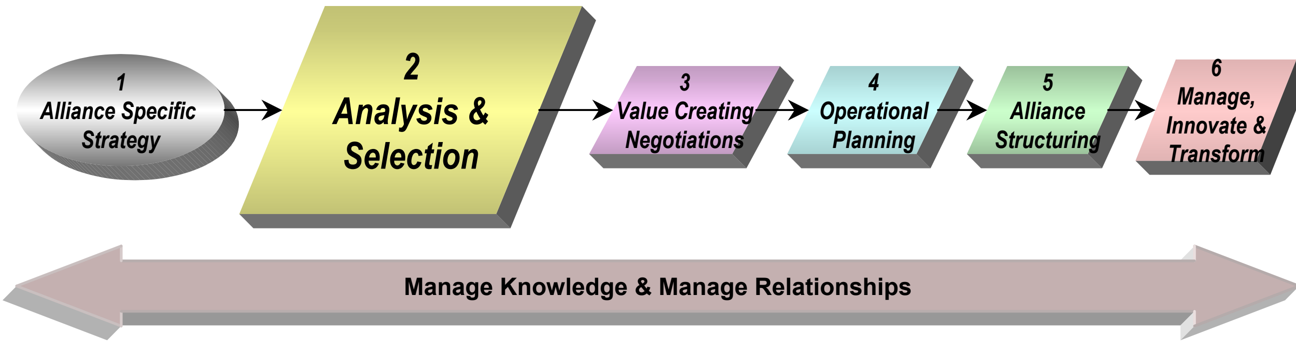
Strategic Alliance
Best Practice User Guide

-- Contents --

Alliance Framework



Analysis and Selection Overview

As its name suggests, the Analysis and Selection phase is dual in nature.

In the first part of this phase (Analysis), performance goals for the alliance relationship are established. Those goals are used to determine the broad operational capabilities that will be required, and the targeted operational results that will be used to measure performance once the relationship is in place.

In the second part of this phase (Selection), those performance goals are used as some of the criteria to identify and evaluate potential alliance partners. The selection process begins, and the list of candidates are narrowed to a short list of finalists.

The Analysis and Selection phase begins after the core alliance development team has had an opportunity to develop a broad understanding of what the organization can achieve through an alliance relationship, and how it plans to proceed with establishing this relationship. The team's work should be based on a clearly documented charter from senior management.

In the outset of this phase, the core alliance development team creates a number of sub-teams to explore specific aspects of the business requirements in question and the potential alliance partner organizations. This phase may require people with expertise in a variety of functions. Precisely which functions to involve will depend on the business requirements. For example, an IT process would require expertise in information technology, while a financial administration process would require finance expertise.

ANALYSIS & SELECTION OVERVIEW *(Continued)*

The activities for the **Analysis** portion of this phase are:

1. Outline tentative performance goals for the business requirements that are to be obtained;
2. Establish preliminary requirements and measures;
3. Gather internal and external benchmarking data; and,
4. Develop a summary of specific performance objectives, operating requirements and measurement criteria to be used.

The activities for the **Selection** portion of this phase are:

1. Develop an ideal-partner profile;
2. Create an initial list of candidates;
3. Establish and communicate the partner-selection procedure;
4. Check the references of candidates;
5. Conduct interviews with candidates;
6. Perform due diligence; and
7. Pick the alliance partner.

Purpose:

- Establish potential alliance goals
- Identification of quantitative goals
- Preparation of Market information through benchmarking
- Identify potential alliance partners
- Develop criteria by which to make partner selection

Goals, Critical Success Factors & Expected Outcomes

Goals

- Analysis Framework for Evaluating the Alliance
- Determine the Risks and Rewards
- Build Internal Support and Commitment

Critical Success Factors

- Finding the Right Alliance Prospect
- Know Your Risk and Reward Thresholds
- Be able to Communicate What You Want
- Differentiate between a Strategic Alliance and a Tactical Relationship

Expected Outcomes

- Performance Goals to be Outlined
- Preliminary Requirements and Measurements Documented
- Gather and Document Benchmarking Data to be used in Selection Process
- Document the Ideal Partner Profile for the Alliance
- List of Candidates Identified and Screened
- Select Candidate Partner based on Documented Criteria

Analysis & Selection

Step 2.1 Preconditions for Success
- **Rules of Thumb**

Step 2.2 Candidate Research and Due Diligence

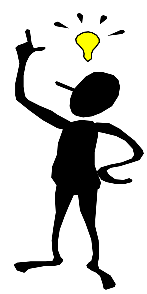
Step 2.3 Fit Analysis

Step 2.4 Risk and Business Case Analysis

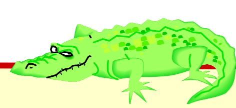
Step 2.5 Strategic Return on Investment
- **Market Growth**
- **Competitive Advantage**
- **Organizational Capability**
- **Innovative Capacity**
- **Financial Return**

Step 2.6 The Strategic Spectrum

What the Experts Say...



The two most cited reasons for success in an alliance according to CEO's in the Electronics Industry are:
- Selection of the right partner
- Commitment of Senior Management



~TRAP~

The single most cited reason for failure was:
-Overly optimistic expectation (i.e. poor planning, analysis, and coordination)

Step 2.1 Preconditions For Success

Not every alliance we engage in will achieve our level of expectations. Some alliances will fall short of our revenue goals, some will not achieve market share, customer satisfaction levels or other metrics we have established as our measure of success.

While we should never expect failure, we should be aware that it can occur. In order to reduce the number of non-performing alliances to a minimum, the following **Rules of Thumb** should be utilized.

RULES of THUMB

Rule #1: Ensure an Alliance is the Best Alternative:

Create an alliance only if it is the best alternative and would be foolish to go it alone. If in doubt, first test the waters with a single test product. If successful, consider a deeper plunge with a broader alliance.

Rule #2: Minimize Ambiguity:

The higher the future ambiguity, the higher the probability of failure. Alliances are the step-children of uncertain risks and opportunities. Uncertainty breeds ambiguity, and ambiguity is the seed of business failures. Do everything possible to limit the unexpected ruining the likelihood of success. Lower risk by building governing and decision-making processes for resolving unanticipated consequences.

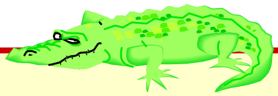
Rule #3: Conduct a Comprehensive Due Diligence:

Know your competition and your potential partners thoroughly. Due Diligence is vital to deciding whether a collaborative venture will indeed be fruitful.

Rule #4: Ensure ROI Surpasses Threshold:

The return on investment should be significant and generally should be measured over a 2-5 year period.

Step 2.1 Preconditions For Success



~TRAP~
Don't Consider an Alliance If These Conditions Exist

- Top Management of either partner in the Alliance does not *fully understand* and give *unqualified support* to the venture.
- Poor Communications and lack of Teamwork are inherent internally within the corporate structures of either of the partners.
- The critical "Driving Forces" are essentially missing. There are internal, adversarial relations between the production and design teams, characterized by comments like "assemblers are dopes", "manufacturing can't do it right," or "engineers are egg-heads with no conception of reality."

RULES of THUMB *(continued)*

Rule #5: Be Adaptable:

Business conditions are changing constantly. As the venture matures, be willing to address new risks, and transform the structure as strategic and operational conditions change. Identify alternatives and develop implementable contingency plans. As the alliance is formed, ensure mechanisms are put in place for future joint planning.

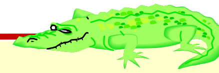
Rule #6: Ensure a Positive Impact on Market Share:

If the alliance won't enable us to, at the very least, hold existing market share, the strategy is probably wrong and the venture will not be to our advantage.

Rule #7: Take Advantage of Emerging Channels:

Global competition is changing distribution channels throughout the world. Previously exclusive channels are opening and customer service is becoming critical to establishing alliances as a competitive weapon.

Step 2.1 Preconditions For Success



~TRAP~

"Alliances established primarily for operational rather than strategic reasons, will have a far greater likelihood for failure. Too frequently, operational (tactical) issues change rapidly in the near term, placing pressures on the venture that it was never conceived to endure."

Step 2.1 Preconditions For Success

Checklist 2.1
Preconditions For Success:
A Quick Checklist

Alliances are most advisable when conditions are right both within your company, the prospective partner company and within our target industry segment. The more “yes” answers, the better the chance of success:

Company Conditions:

___1. Our company has something very valuable to offer to a prospective partner <u>and</u> our company has something valuable to gain from another company.

___2. Our company has a cooperative corporate culture.

___3. Our company has insufficient resources <u>or</u> our company has a prominent but not debilitating strategic weakness.

___4. Our company is ready to jump into a leadership position in the marketplace.

___5. Our company knows that pursuit of a particular strategic objective is too risky to undertake independently.

___6. Our company is very doubtful of its ability to complete an important project or to obtain customer acceptance of a new product without the name recognition or support of another company.

Style of Operations:

___7. The Prospective Partners have similar goals, rewards, methods of operations,and corporate cultures.

___8. Both companies have a similar style of decision-making (both are either decentralized / collaborative companies or centralized / hierarchical).

Support:

___9. The Top Executives of the partners are in full support of the alliance.

___10. There is no apparent threat of unfriendly takeover which could jeopardize trust and a cooperative working relationship. (This should not prevent discussion of a buy-out of the venture by one of the partners.)

Step 2.1 Preconditions For Success

Checklist 2.1 *(continued)*
Preconditions For Success:

Industry Conditions:

___11. High Capital Costs and/or Direct Costs result in the need to Share Financial Risks.

___12. Rapid changes occur in Technology, Customer Traits, and the need for Product Differentiation.

___13. Decline or Maturation of an industry requires consolidation to protect market share.

___14. High Entry Costs or Entry Risks make risk sharing advisable.

___15. Major Competitive Realignments (mergers, acquisitions, foreign entry into the market) occur or there is uncertainty about a response by major competitors.

___16. The Market is expected to respond positively to the "best product" which can only be produced by a superb team combining excellent resources.

___17. There is a need for Rapid Market Entry and Acceptance.

Time Perspectives:

___18. Our definition of "long-term" means the same thing to our partner.

Financial Goals:

___19. The goal of the alliance is to seek increased market share, profit and gains resulting from customer satisfaction, rather than simply quarterly earnings.

Past Working Relationship:

___20. There is a history of collaboration between the companies that enables top and middle management to build trust and communications on an existing foundation.

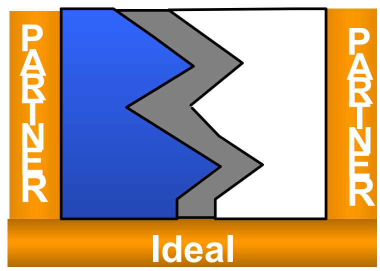
Step 2.2 Candidate Research and Due Diligence

Evaluating A Prospective Partner's Strengths And Weaknesses

Figure 2.2 a -- Sample Strengths & Weaknesses Profile

Organization A

Market Access
Management
Technology
Capital
Materials
Manufacturing



Organization B

Market Access
Management
Technology
Capital
Materials
Manufacturing

No one would ever consider hiring a corporate vice president without a clear job description. Similarly, it's vital to have a profile of a prospective partner before beginning the search.

Strategic Synergy: Figure 2.2a depicts how two organizations should compare in key functional areas of their organization. BEFORE actually courting a partner, a careful evaluation of their strengths and weaknesses is imperative. Do a value analysis, (see Step 2.2 Checklist) make a list of the value elements you can provide, and then the value you expect the potential partner to provide. Be sure your prospective partner is sufficiently different to make an exciting match, but sufficiently alike to permit a harmonious working relationship.

DUE DILIGENCE

Due Diligence is the technical term for looking into the background, capabilities, and operations of a potential ally, before beginning negotiations. It means doing more than a credit check. It maximizes the chances of a successful venture, avoiding entering into a deal that will eventually sour. Some companies perform a basic level of due diligence before even proposing the venture. That way they screen out bogus companies without expending resources on negotiations, travel, and lawyers.

Step 2.2 Candidate Research and Due Diligence

Evaluating A Prospective Partner's Strengths And Weaknesses *(continued)*

SIX TYPES OF ALLIANCE PARTNERS

Who should our partner be? A carefully selected team-mate is essential for maximizing the chances for long-term success. Several types of partners to look for are:

1) **Direct Competitor**: This ally should be chosen when the alternative is cut-throat competition. However, be cautious, because the success of one partner may come at the expense of the other. Ventures of this sort are typically more tactically oriented and short-lived, unless well thought out and the boundaries of operation are clearly delineated. This type of partner may also be chosen when attempting to introduce a new industry standard.

2) **Potential Competitor**: This is an alternative to future cut-throat competition. Unite to gain market share, and to fend off larger direct competitors. A broader alliance may result in the future.

3) **Parallel Producer/Server**: These truly complementary alliances are used to widen or integrate product lines, to capture market share, to trade on relationships, and to take mutual advantage of each partner's strengths. Many are formed when highly integrated technology is essential.

4) **Vertical (Supply) Integrator**: Rather than be bound by a rigid system of vertically integrated subsidiaries that may not be able to adapt to changing customer needs, many companies are using cooperative ventures as a better alternative. These alliances link supply, product, and market functions.

5) **Technical Developer**: Prohibitive or extremely risky development costs are the prime motivators for seeking this type of alliance partner. Generally, partners occupy parallel, but not directly competitive market niches; however, many research consortia pool direct competitors with common access to all knowledge developed.

6) **Distributor**: These can be either transitory or long-term alliances which enable parties to provide improved service and benefit from increased market performance.

Step 2.2 Candidate Research and Due Diligence

Checklist 2.2a
Due Diligence Issues

Product Line: Is it competitive or complementary to our company?

Service Offerings: Are they unique, competitive with our company, or duplicative of our line?

Corporate Ingenuity: Are their core competencies and attributes that our company would gain by if we had an association with this company?

Corporate Strategy: Is their long-term strategy likely to be aligned with ours over the foreseeable future?

Financial Condition: Are they financially stable? If not, are they profitable? Are they likely to be serious players in the future?

Industry Reputation: What do other industry leaders and customers think of this company?

Alliance Prospects: If we do not form an alliance with this company, are they likely to form one with a competitor?

Impact on Existing Alliances: If we form an alliance, what will this mean to other alliances we have? Implications for alliances the partner has? And the partner interrelationship?

Recent Sales History: What has been their sales history in the last three years?

Synergy: What are their strengths and weaknesses? How well do these match our company's? Are there any key areas of overlap? Are there any critical missing elements (especially from the customer's perspective) in this alliance?

Customer Reaction: How will customers respond to this alliance?

Step 2.2 Candidate Research and Due Diligence

Checklist 2.2.b
Sample Partner Profile

Management Style
__ Compatible Structure, Philosophy
__ Work Ethic, Operating Style
__ Strategic Planning, Culture and long-term view
__ Responsiveness to opportunities and threats
__ Values & Beliefs
__ Continuous Learning/ Organization Improvement
__ Culture

Product Development
__ Consistent High Quality Producer
__ Production Capabilities
__ Efficient State of the Art Producer
__ Technical and R & D Expertise
__ Willingness to Invest in New Product
__ Develops High Quality Long-Term Suppliers

Marketing
__ Strong Management Team
__ Consumer Marketing Expertise
__ Development & Maintenance of Competitive Advantage
__ Consumer Orientation, Market Driven
__ Innovative Market Leader
__ Understands Brand Management and Market Mix
__ Proven New Product Success
__ Track Record of Putting Strategic Thinking into Action

Finance
__ Strength
__ Solid Long-Term Growth
__ Realistic ROI
__ Pricing
__ Cost Structure

Trade & Customer Services
__ Strong Trade Relationships
__ Customer Service Driven

Joint Ventures/Alliances
__ Successful Joint Venture Experience
__ Enthusiastic about our Company
__ View Our Company as a High Priority Partner Profile
__ Past Litigation

Step 2.3 Fit Analysis

Best Practice: Three Dimensional Fit

Figure 2.3a- Three Dimensional Fit

Both strategic 'fit" and operational "fit" have long been thought of as the essential elements of good acquisitions.

However, in alliances, there is one additional "fit" that must be included in the formulation of an alliance -- the "chemistry fit." (See Figure 2.3a) Chemistry inherently measures the quality of the relationships between the people involved in operating the alliance, particularly trust and integrity. Moreover, chemistry fit is the nature of how well the two cultures will interact. According to virtually every veteran of a successful alliance, chemistry is essential. The key elements of the Three Dimensional Fit are:

Strategic Fit:

- Future Vision & Value Proposition
- Competitive Advantage
- Customer's Needs
- Long-term Strategy and Goals
- Values and Beliefs

Chemistry-Cultural Fit:

- Decision-making
- Trust, Culture & Teamwork
- Alignment of Systems, Processes
- Risk Preference
- Quality of Relationships
- Leadership & Commitment

Operational Fit:

- Systems Integration
- Performance Processes
- Integrative Mechanisms
- Fast Time Implementation
- Complementary process capability

Step 2.3 Fit Analysis

Figure 2.3b depicts companies that have a good strategic fit, but a poor operational fit.

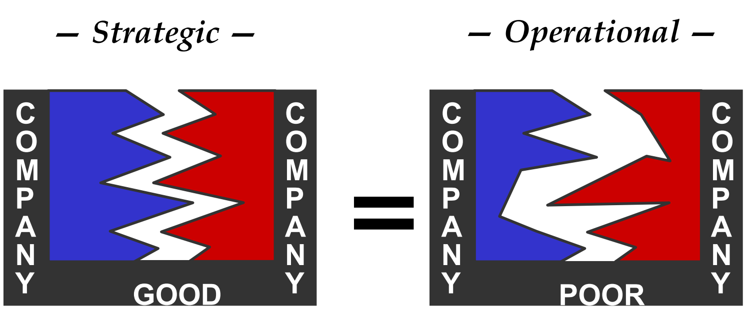
A Good Strategic Fit Does Not Imply A Good Operational Fit!

While the strategic directions of both companies should be similar, the operational strengths and weaknesses should be dissimilar.

Why?

- Mutual, quantifiable advantage must exist; potentially good partners/targets will have strengths that complement one another's weaknesses (e.g., contiguous geographic markets, products that fill gaps in a portfolio, capabilities that contribute to a customer solution, new technologies to complement more mature ones).
- Companies with identical strengths will disagree over the relative value of their contributions.
- Companies with identical weaknesses will suffer from a lack of essential resources.

Figure 2.3b

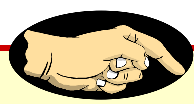


Step 2.4 Risk and Business Case Analysis

Why Risk is so Vital to Success

It should not be the intention to eliminate risk entirely from the alliance. The proper division of risk and reward serves not only the doctrine of fairness in an alliance, but it creates the proper long term motivation, an absolutely essential ingredient for success. It is important that the potential rewards are commensurate with the risks being taken.

For example, the banker, whose professional rules require the acceptance of virtually no risk, dramatically increases his chances of getting his loan repaid in full when the material possessions of the entrepreneur are at risk daily, (i.e. by requiring a second mortgage on the owner's house) and a business owner will work twice as hard to avoid losing his home and material gains. This illustrates the value of "Vested Interest Motivation," one of the vital principles which increase the chance of success of an alliance.



~TIP~
Vested Interest Motivation

Essentially, the uneven risk posture creates its own conditions for conflict. Professor Paul Lawrence of Harvard Business School advises:
"If long term motivation by top management is desired, then be sure both long-term risk thresholds and long term reward thresholds are sufficient to keep the partners engaged.."
Take away the risk from one of the partners, and the chances are great that the venture will fade away, particularly if one of the individuals who created the venture must leave the parent company. Before striking a deal, be sure both you and your partner have *vested interest motivation* sufficient to give the entire team the desire to win.

Business Case Analysis -- Examining Risks and Rewards

As alliance manager, you must determine if there is a strong business opportunity from creating a successful alliance with a prospective partner in a particular market segment. Together, with the sponsoring business unit, build a preliminary financial analysis of the alliance. A financial analysis should be built that examines:

Step 2.4 Risk and Business Case Analysis *(continued)*

- Potential Sales Forecast
- Probable Risks
- Capital Requirements & Operational Expenses
- Sensitivity Analysis on Key Assumptions & Variables
- Possible Financial Returns
- Pro Forma Financial Statements

This Business Case/Financial Model will determine to a “rough order of magnitude” whether it is advisable to move forward with negotiations. The Business Case will address key issues such as:

- Description of the business model and value proposition.
- Will the strategy translate into implementation?
- Can we make money?
- Is an alliance the best alternative?
- Is it possible to derive a powerful Win-Win-Win for our customer, company and the alliance partner?
- Determine what resources will be required and from whom.

Ultimately, the “hypothetical” case will be later compared against a more detailed business & implementation plan which is created with the other partner, once all the critical risks, requirements for performance,and resource issues can be fully analyzed.

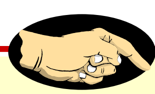
Definitions:

RISK: Variance with precise probabilities for well-defined activity.

UNCERTAINTY: Unknown probabilities for ambiguous activities.

Risk Management requires careful planning, analysis, and continuous measurement.

Uncertainty Management requires scenario analysis optional pathways, opportunity assessment, flexibility, and decentralized decision-making.



~TIP~

Distinguish Risk From Uncertainty

“Risk” is often confused with “uncertainty.” It is important to distinguish between the two, because each requires a very different management approach.

Step 2.4 Risk and Business Case Analysis

Many companies, such as Hewlett-Packard, use a business case format to better grasp the issues of the alliance. Below is an alliance process which provides a map to follow when developing an alliance business case.

Strategic Objectives
- Strategic
- Business Unit
- Driving Forces
- Value Migration
- Competitors Expected Response

Value Proposition
- Breakthrough
- Customer Orientation
- Strategic Return on Investment

Target Company
- Critical Data
- Due Diligence
- Profile
- Strengths & Weaknesses

Risk Analysis
- Alternatives
- Growth Profile of Market
- Key Factors for Success
- Legal Protections
- Contingency Plans

Fit Analysis
- Strategic Fit
- Operational Fit
- Chemistry & Culture Fit
- Business Unit Fit
- Other Alliance Fit

Financial Analysis
- Projections
- Cash Flow
- Investment Required
- Hurdle Rates
- Returns Expected
- Valuation

Planning, Implementa--tion and Integration
- Resources Required
- Critical Interfaces
- Cultural Issues
- Leadership Issues
- Organizational Structures
- Governance

Go-Forward Action Steps
- Next Steps
- Deal Breakers
- Approvals Required

Step 2.4 Risk and Business Case Analysis

Evaluate Critical Risks

Checklists 2.4 shown on the following page is used as a basis for collecting information that will be used in assessing the risks inherent in any new product introduction, technology development, or acquisition. Too often in the haste to introduce a new product or service, there is a tendency to skim over all of the risks in favor of the obvious rewards.

In an alliance relationship, we may be compounding our risks if the potential partner sees only the upside of the relationship and not any of the potential shortcomings. Especially if both organizations overlook the commitments required for a successful relationship.

Do not take on any type of alliance relationship based on the assumptions that there will be appropriate capital and human resources made available at a later date. Be sure and build all of the requirements for success into the business plan and the financial pro formas that should be developed.

The information to answer the questions in the following charts will come from our market research, our due diligence of our potential partner(s) and from our customers. Populate Task 2.3 with the appropriate information determined from our market research effort.

Step 2.4 Risk and Business Case Analysis

Checklist 2.4
Evaluate Critical Risks

There are generally dozens of excellent opportunities in the field at all times. Which ones should be chosen? The process of selection should start with a risk-reward analysis. Each of the following risks should be examined:

___ 1. **Market Risk:** Will the market continue to provide opportunities for us to sustain our growth? (Beware of entering new markets with new products utilizing new technology - the "compounded risk" - see note below.)

___ 2. **Competitive Technology Risk:** Will a competitor develop a technology that will make ours obsolete? Are margins sufficient in the event of a price war? Are technologies supporting our value proposition approaching obsolescence in the near or immediate term that may eliminate or reduce the benefits we seek from the alliance?

___ 3. **Cooperative Environment Risk:** What is the chance that someone or something (partner, government, subcontractors, transportation, etc.) will stop or slow down the venture?

___ 4. **Management Risk:** Are sufficient personnel available to carry out the venture? Can proper resources be obtained on a timely and cost effective basis?

___ 5. **Political Risk:** Are there governmental regulations, now or pending, that will interfere with success?

___ 6. **Resources Risk:** Will the supply of materials, or products remain available? Will the partners have the required financial, human, and intellectual resources?

___ 7. **Capital Risk:** Will inflation, exchange rates, or government policy change the investment's value?

___ 8. **Prospective Partner Risk**: Is the partner strong enough to withstand competitive pressures? Will they be stable and cooperative over the long haul? Will they maintain a strategic perspective?

NOTE: Insurmountable Risks: Some risks are insurmountable, regardless of the care taken in the formation of the agreement. This is one of the principle reasons for the failure of high risk alliances. Explorations into new technologies, development of new products for new markets, and introduction of unique, untested services are often insurmountable risks – unfortunately, often unrecognized until after the fact.

Step 2.4 Risk and Business Case Analysis

Task 2.4

Risk Analysis

1. Market Risks ______________________________
2. Competitive Risks ______________________________
3. Cooperative Environment Risk ______________________
4. Management Risk ______________________________
5. Political Risk ______________________________
6. Resources Risk______________________________
7. Capital Risk ______________________________
8. Prospective Partner Risk______________________

Business Analysis

1. **Marketing Study Identified**:
   Key Factors for Success________________________
   Market Characteristics__________________________
   Market Size________________________________
   Top Ten Customers:
   1.______________ 6. ______________
   2.______________ 7. ______________
   3.______________ 8. ______________
   4.______________ 9. ______________
   5.______________ 10. ______________
   Top 5 Competitors:
   1.______________
   2.______________
   3.______________
   4.______________
   5.______________

2. Sales Forecast
Units ________________________
Frequency of Sale __________________
Sales Projections __________________
____
____
to a "Rough Order of Magnitude" of (±%)______
Key Sales Forecast Assumptions ________
____

Step 2.4 Risk and Business Case Analysis

Task 2.4 *(continued)*

3. Projected Capital Expenses

____

____

4. Projected Operating Expenses:

____

____

5. Business Planning Model Completed and

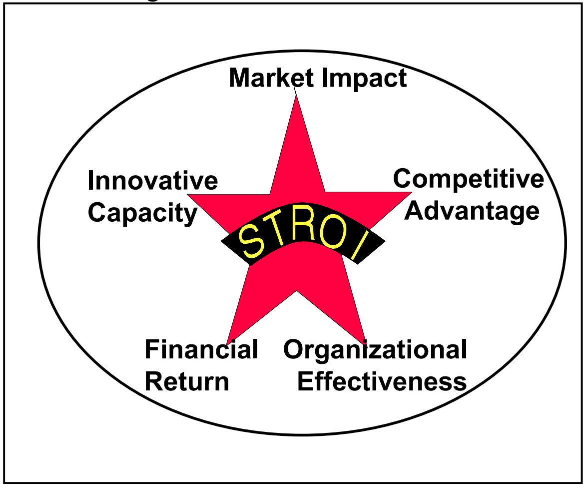
Forecasts/Projections done ___

Sensitivity Analysis done ___

Contingency Analysis done ___

Step 2.5 Metrics: Strategic Return on Investment

Figure 2.5a - STROI



STROI is a metrics tool that will determine how *our company and its partner derive value*.

The best tool for measuring the results that an alliance strategy will bring to our company is "Strategic Return On Investment" (STROI). STROI measures five basic dimensions that measure the results of a successful alliance. (see *Figure 2.5a*)

Notice that "Financial Return" is only one of the five dimensions. Because the primary purpose of an alliance is *strategic*, its rewards must be more than financial. Financial gain is not just a *result* of strategy but also a *measure* of the combined strategic success of the other four dimensions.

Describing the five dimensions enables the measurement of expected strategic results. The allies then know whether or not the alliance May be expected to achieve its strategic goals. In this way, the allies look for the key strategic benefits and can then measure these returns against their "investment," which can include time, people, technology, or money.

Using the STROI tool is a far more effective method for measuring success than simply using financial return methods. Four indicators (Market Impact, Organization- al Effectiveness, Innovative Capacity, and Competitive Advantage) are *leading* indicators, and are therefore more important than the financial element, which is a *lagging* indicator.

~Tip~
What STROI Does

1) Takes strategy from the warm, fuzzy stage to a **clear, crisp** state.
2) Checks underlying **assumptions**.
3) Build/establishes clear **common vision**.
4) Defines **results** - the end-state
5) Provides **bridge** between strategy & operations for design of an operations plan
6) Takes a holistic, **systems** perspective
7) Establishes **performance expectations and measurements**
8) Builds & measure **synergies**
9) **Quantifies** non-financial returns

Step 2.5 Metrics: Strategic Return on Investment

Market Impact:

This is a form of "top line" (versus bottom line) management. It can indicate market share growth, expansion into new markets, capturing niches that show promise of future growth, locking up key distributors, pumping more product through existing distribution channels, and becoming more responsive to the customer, to name a few. The possibilities are as broad as the driving forces and inspirations of the alliance creators.

~ Tip ~

What Are The Elements Of Victory?

•Key measures of a 'Win"
You can't construct a Win-Win alliance without defining what "win" means!
•Key units of Measure…Ask:
  •How Many?
  •How Much?
  •How Often?
  •How Soon?
•What Management Information System will measure our progress?
•OBJECTIVE: Stay out in front of potential problems!
ACT -- Don't REACT!

Organizational Effectiveness:

Ultimately, all organizational strength is based not on the money in a company's coffers nor on its technology, but on its ability to marshal its human resources. Strength is *not* measured in the *numbers* of people, but in the *effectiveness* of people.

Among the components of this element of strategy can be new knowledge, heightened loyalty and commitment, teamwork, new career opportunities, adaptability to change, and utilization of resources, among others.

Innovative Capacity:

Peter Drucker says there are two basic functions of a business -- marketing and innovation. Without innovation, there is no adaptability for the future. Innovation can take a variety of forms, ranging from new technical capabilities, development of better manufacturing processes, improved service delivery capacity, new products, better quality, higher productivity, to highlight a few. Look for opportunities where the Enterprise can leverage its innovations, and current assets or capitalize on the innovations of its alliances.

Step 2.5 Metrics: Strategic Return on Investment

Be careful not to view innovation simply from technical perspectives. Innovations occur everywhere: in marketing, in using human resources, in strategy -- virtually everywhere. Our alliance partners, if they are world class, will invariably have created innovations that could benefit our company. The corporation that does not see continuous improvement as a fundamental component of business strategy will soon not need strategy in the world of fast-advancing armies of international competitors (and should probably not be one of our alliance partners).

Competitive Advantage:

All strategy must give major consideration to enduring competitive advantage if it is to be successful. Business is a chess match; there is never a single "best move." Strategy is relative to the customer, the responses of the competitor, and the forces of the environment.

By designing an alliance to be the best at every step in the value chain, we create a substantial hurdle that becomes a barrier to entry to potential competitors. And by creating efficiencies of scale that make market entrance costs excessive, we can create further hurdles.

Financial Return:

Notice that this dimension does not necessarily measure *return*, but rather *gain*, which is a broader factor. This is because the financial results can be garnered in a variety of ways through an alliance. The typical American manufacturing corporation purchases goods and services from outside suppliers that make up nearly 60% of all final sales costs. In this case, adding value by going farther than just cutting costs can significantly improve profits, thereby securing a long-term relationship.

Both alliance partners should develop a STROI matrix similar to the one in *figure 2.4.b*. By developing the STROI analysis together, the allies become unified in their goals and the methods by which they will be gaining their return on investment.

STROI not only sets the criteria for assessing a potential alliance and evaluating its results, but also becomes the framework and underpinning for an annual audit of the alliance.

Step 2.5 Metrics: Strategic Return on Investment

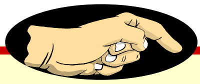
STROI Tools

Strategic Return On Investment Matrix - *Figure 2.5b and 2.5c*

Figure 2.5b reviews the five elements of the STROI concept by providing examples of the type of responses you will need to have in order to determine what are the most strategic aspects of the relationship. It also assists you in identifying whether or not your expectations are reasonable and achievable. Task 2.5should be used to develop alliance specific STROI matrix.

Strategic Return on Investment Checklist - *Figure 2.5d*

The STROI Checklist provides you with another tool to ensure that you have covered all the necessary points to ensure a successful alliance. Remember, not all of the points indicated here are required for every alliance. Use the list as a memory aid to be sure you do not miss anything of significance while evaluating the risks and returns of the potential arrangement.



~Tip~

Alliance Management Principle

"If you can't measure it,
You can't manage it"

Establish clear criteria for success, otherwise the results will be elusive.

Step 2.5 Metrics: Strategic Return on Investment

Figure 2.5b

Example
Strategic Return On Investment Matrix

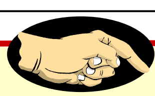
STRATEGIC ELEMENT	**MEASURABLE RETURN EXPECTED**	**RESOURCES INVESTED (Time, People, Materials, $$)**
1. MARKET IMPACT	Double Sales, Increase Share from 10% to 20%	Existing Sales Force, plus Establish base in Office Market $150,000
2.ORGANIZATIONAL EFFECTIVENESS	Increase sales with no rise in fixed costs Shorten new product development cycle to 12 months by Nov, 2001	8 individuals (100% dedicated) Assign 3 engineers & one technician
3. INNOVATIVE CAPACITY	Initiate joint product development program Introduce 3 new products in Yr. 1, and 5 in Yr. 2	6 individuals (50% dedicated) 1 design engineer
4. COMPETITIVE ADVANTAGE	Lock up key distributors before competition enters market Hold position of highest equipment, plus TQM program producer	$100,000 (variable costs) $50,000 in new quality, lowest cost
5. FINANCIAL RETURN	Double Return on Sales Lower unit-marketing-cost	Total of Above

Step 2.5 Metrics: Strategic Return on Investment

Using Checklist 2.5c as a starting point and the example in Figure 2.5b, create a clear Statement of Strategic Return.

Strategic Return On Investment Matrix

Strategic Element	Measurable Return Expected	Resources Invested (Time, Materials, People, $$)
Market Impact		
Organizational Effectiveness		
Innovative Capacity		
Competitive Advantage		
Financial Return		



~Tip~

Confidentiality

The analysis you have done is very valuable, and could be used against the enterprise if it falls into the hands of a competitor. Be sure to follow all guidelines for transfer of confidential material.

Step 2.5 Strategic Return on Investment

Checklist 2.5c
Strategic Return On Investment -- "STROI"

Rewards from an alliance may be measured in numerous dimensions. Strategic Rewards should be more than strictly financial. How each reward is evaluated will be custom tailored for each venture. Be sure to use a quantifiable metric for measuring each of these dimensions.

The following are SAMPLE STROI ISSUES: Your alliance will generate its own unique STROI.

Remember, STROI defines a "Win"

Market Impact
__ Penetrate into new market niches?
__ Expand market share?
__ Broaden product line?
__ Access best lines of distribution?
__ Respond faster to customer needs?
__ Raise customer satisfaction?
__ Increase sales closing rate/shorten sales cycle time?
__ Develop strong brand recognition?

Organizational Effectiveness (Not necessarily measured in quantities of people)
__ Organize talent more efficiently?
__ Improve productivity?
__ Shorten product development cycle?
__ Lower absenteeism?
__ Broaden or deepen core competencies or knowledge?
__ Increase capacity to convert ideas into new products?
__ Provide faster/more accurate decision- making?
__ Heighten levels of synergy between business units?
__ Improve commitment, teamwork, and vision?
__ Improve service delivery capacity?

Innovative Capacity (More than just technical)
__ Provide new or broader technical capacity?
__ Improve manufacturing processes?
__ Access financial innovations/continuous improvement?
__ Integrate systems for added value?

Competitive Advantage
__ Enable us to become "Best in Class" competitor?
__ Create new barriers to entry/exit?
__ Enlarge market to maximize production efficiencies?
__ Become Bet at Every Step in Value Chain?

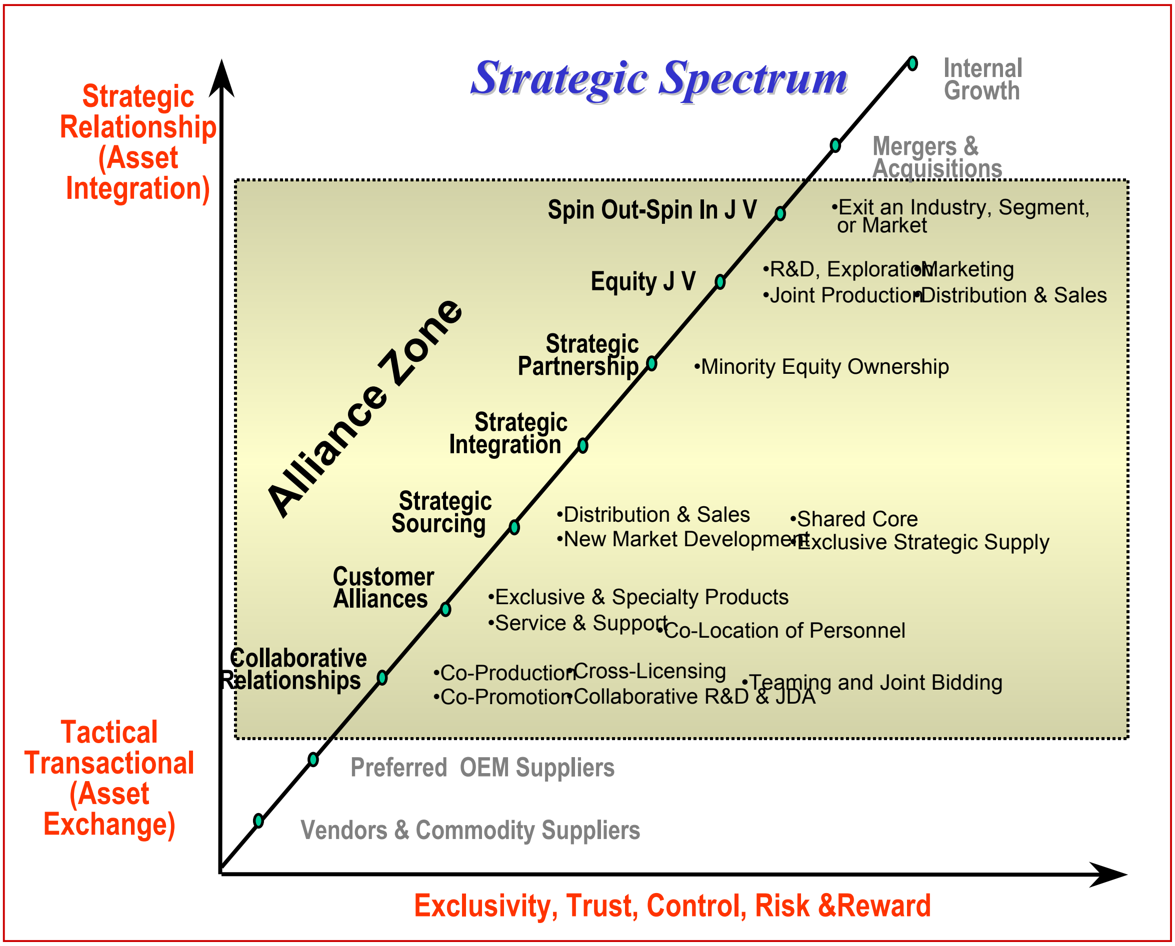
Financial Return (More than simply "profit" or "ROI")

Step 2.6 The Strategic Spectrum

Business Relationship Spectrum

Different types of business relationships can be described on a continuum representing differing degrees of collaboration, and the exchange (trading) or integration (merging) of corporate assets between participants. Strategic Alliances constitute a spectrum of business relationships within this continuum, involving more integration than a simple buy/sell transaction, but less than that of a merger or acquisition. In a merger or acquisition, only one firm remains, therefore, a merger or acquisition would not constitute an alliance. *Figure 2.6a* depicts a general view of how different business relationships might be characterized on this continuum. The examples provided are neither absolute nor evolutionary, as each business relationship is unique.

Figure 2.6a - Strategic Spectrum Continuum



Step 2.6 The Strategic Spectrum *(continued)*

Strategic Spectrum Checklist 2.6

•Critical Questions to Ask:

√ Where on the spectrum can we produce maximum value for the customer with the least acceptable risk?
√ Will the alliance migrate up or down the spectrum as value migrates in time?
√ What relationship type will produce the maximum competitive advantage?
√ What will competitors do when we form an alliance?
√ What's in it for the alliance partners?

Alliances are architected by **function**, not by **form**. What is meant by this statement is that we never structure a solution to a problem until we understand what the problem is. If we need to have timely customer response, we must first determine all the parameters of the response and then develop the solution that will meet those parameters. Not the other way around. When designing the strategic relationship, be clear about the specific factors that will define the outcomes. *Figure 2.6b* distinguishes between 1) the traditional manufacturer/distributor (vendor) arrangement, 2) a tactical (short-term) relationship, and 3) a strategic alliance. Use this chart to be sure you understand the differences in the types of relationships you can enter into, depending upon your requirements and those of the alliance partner. In reality, alliances may not fit as neatly into categories as *Figure 2.6b* describes.

Step 2.6 The Strategic Spectrum

Figure 2.6b - The Purchaser-Supplier Strategic Spectrum

	VENDOR	PREFERRED SUPPLIER	ALLIANCE
Viewed As:	Replaceable Commodity	Unique Specialty	Integrated, Customized Specialty
Level of Integration	Low/Not Integrated	Loosely Integrated	Highly Integrated or Inseparable
Number of Suppliers	Many Suppliers	Several Suppliers	Very Few Suppliers
Distinguishing Features	Mainly Price Driven within min. Quality Standards.	Price plus unique offering (i.e. technology, service, etc)	Synergistic Value Proposition (i.e. mutual growth, etc)
Style of Interaction	Tactical Transaction	Preferred and/or Tactical Relationship	Strategic Synergy
Duration of Term	Short Term	Medium Term	Long Term
Value Proposition	Price and acceptable quality	Price, superior quality, and excellent service	Strategy, Cost, Quality, Reliability, Speed, Innovation, and more
Framework for Winning	Winning is essential for me, What happens to you is your business	A Win is essential for me, and I know I should let you win too if the relationship Is to survive	A Win/Win is essential for both of us and is critical if the relationship is to thrive continually
Competitive Advantage	Low Competitive Advantage	Moderate Competitive Advantage	High Competitive Advantage
Make, Buy, or Ally Decision	Seldom produced internally (not a core competency)	Often Produced Internally (debatable core competency)	Frequently has been an integral part Of the internal value chain
Trust Level	Distrust Prevalent (caveat emptor)	Trust is important to managing the relationship	Trust is essential to generating a continuous stream of new value
Difficulty of Exit	Low Impact, Excellent Ability to Switch Vendors quickly	Moderate Impact	High Impact, Switching may have detrimental impact due to disintegration of systems
Strategic Environment	Cost Driven Low Product Differentiation TCO is non-critical Relationships not important	R&D is a Distinguish Value Applications Focus Provider of Performance	Discontinuous Change in Buyer's Industry Fast Time To Market is Essential Innovation & Integration Essential

Step 2.6 The Strategic Spectrum *(continued)*

Beginning Negotiations

Once the Business Analysis, Business Strategy and our company's Strategic Return on Investment are clear, and the internal team is in concurrence with the Analysis and Strategic Return; then, it is time to begin negotiations with prospective partners.

~Best Practices Tip~

Selection of the best partner should be based on that partner filling in the missing pieces of our organization. We would not have need for an ally if we had similar strengths and weaknesses.

WHAT IF you determined you had the…?

- •Right Partner
- •Right Attitudes
- •Right Strategies
- •Right Culture

BUT INSUFFICIENT

- •Skills
- •Quality Control
- •Alliance Experience, etc.

Effective alliance partners often CONTRIBUTE missing elements.