Strategic Alliances

LEARNING OBJECTIVES

Studying this chapter should provide you with the knowledge to:

1. Differentiate among strategic alliances, vertical integration, and arm's-length supplier relationships.
2. Explain the different types of strategic alliances, how they are governed and the conditions under which each type is preferred.
3. Describe the different ways value is created in alliances.
4. Discuss the two potential dangers of strategic alliances and three ways that firms can protect themselves against these dangers.
5. Describe the importance of building an alliance management capability.

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Tokyo Disneyland

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Excited tourists who enter Tokyo Disneyland are immediately transported into a uniquely American dream world. Nearly everything at Tokyo Disneyland is a replica of the original Disneyland in Anaheim, California, from Sleeping Beauty's castle to Disneyland's famous "Main Street" attraction. Signs are printed in English, with only small Japanese subtitles. When the park opened in 1984, only 2 of its 27 restaurants even sold Japanese foods.[1] Instead, visitors snacked on hot dogs, popcorn, and "spaceburgers" between rides. The only observable Japanese touch is an enormous roof-covering over Main Street, a symbol reminding visitors that they truly are in Japan, rainy season included.

Despite all appearances, the interesting thing about Tokyo Disneyland is that the Walt Disney Company is *not* involved in the day-to-day operations of the park. It simply collects a licensing fee from Oriental Land Company (OL), a Japanese real estate firm that financed, built, and runs both Tokyo Disneyland and its neighboring park, Tokyo DisneySea. Walt Disney and Oriental Land came together in 1979 to form a strategic alliance and make the Tokyo Disney dream a reality. OL had what Disney did not: 115 acres of open real estate on the outskirts of Tokyo, financial resources, and knowledge of Japanese and Asian culture that could make the venture a success. Disney had its brand, park design, and management capabilities, and a host of movie characters that people would pay just to stand next to and snap a photo with, as outlined in Table 8.1.

A Disney resort in Japan seemed to make sense, given that Japanese tourists flocked to Disneyland in the United States. Furthermore, since there are almost no imports or exports between foreign markets in the leisure industry, there would be none of the negative side effects typically associated with Japanese-American licensing agreements. But there were still risks involved. Would Japanese and other Asians want to go to a Disneyland that wasn't in America? Would a theme park work in Tokyo's cold, humid, rainy climate? Disney's two US parks in Florida and southern California are both "vacation destination" parks with warm weather.

Moreover, back in the late 1970s, Disney was hurting financially. It didn't have the capital to make the investment needed to build a park in Japan. Disney received more than 20 offers from

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TABLE 8.1 Disney-Oriental Land Co. Alliance

Disney Resources and Capabilities	OLC Resources and Capabilities
• Disney brand	• Land for the park near Tokyo
• Disney theme park rides and designs	• Financial resources to build the park
• Park management processes	• Relationships with construction firms to build the park
• Ongoing stream of Disney characters from movies	• Knowledge of Japanese culture and how to manage Japanese workers
• Disney consumer products to sell at the park	

Japanese firms vying for the chance to become its partner in building and running the park. So Disney did its due diligence of potential partners in Japan and eventually decided that OL would be the best partner.

Forming the partnership was not necessarily a walk in the park. Negotiating a satisfactory partnership agreement required that both sides overcome cultural barriers and major disagreements. OL wanted Disney to contribute funds to build the park, but Disney refused to contribute in any way toward the initial investment. Disney also required a 50-year contract, a time commitment that frightened OL when so many unknowns remained. Moreover, Disney demanded a high licensing fee of 10 percent of all gross revenues; OL wanted to pay 5 percent. OL initially called Disney's terms a "servile agreement,"[2] and it took more than four years of negotiating for the two to reach common ground in 1979. In the end, Disney paid a sum of less than 1 percent of the initial investment and received a license fee of 10 percent of gate receipts, but did lower its license fee to 5 percent on nongate receipt sales.[3]

Despite the difficult negotiations, Tokyo Disneyland has been a smashing success. Even though it had to pay high interest costs from the $1.53 billion upfront investment required to build the park, as well as the average 7.5 percent license fee to Disney, OL was able to make the project profitable in just four years after the park opened in 1983. The firms continued their partnership, working together to build Tokyo DisneySea in 2001. Together with Tokyo Disneyland and a number of Disney-branded hotels, the two parks make up the Tokyo Disney Resort. Disney's Imagineering unit continues to design and develop new theme concepts and attractions for the parks. In fact, in 2016 the two companies announced a large-scale expansion that will include a castle and village from "Beauty and the Beast," a new "Big Hero 6" themed attraction, and a full-scale indoor theater for live performances.

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All in all, Disney's support through providing its image, know-how, and design skills has been invaluable, and Oriental Land's management and execution is unparalleled by Disney's other international partnerships. The Tokyo Disney Resort has received more than a half billion total visitors since Tokyo Disneyland opened in 1983, with more visitors each year than either of Disney's US parks. The annual number of visitors has never dropped below 10 million, and it reached a high of 17 million visitors in 1997. OL, which runs few destinations other than the Tokyo Disney parks, is now ranked as the second-largest tourism-leisure firm in the world, just behind Disney itself.[4] In one recent year, Tokyo Disney Resort generated revenues of approximately US $4.15 billion. That translated to about US$690 million in operating profits for OL. Disney received about $300 million from its licensing fees, a sum that is basically pure profits for Disney, since it has negligible costs associated with Tokyo Disneyland and no investment in assets.

There are currently no plans for a third park in Japan, but Disney has confirmed that if another park was planned, Disney would be happy to work with Oriental Land to make it a success.[5]

What Is a Strategic Alliance?

strategic alliance A cooperative arrangement in which two or more firms combine their resources and capabilities to create new value; sometimes referred to as a partnership.

The Walt Disney–Oriental Land Company alliance illustrates how strategic alliances can be a vehicle for achieving important strategic objectives—such as lowering costs, creating new sources of differentiation or entering new markets. A **strategic alliance**—sometimes referred to

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as a partnership between firms—is a cooperative arrangement in which two or more firms combine their resources and capabilities to create new value.[6] Strategy scholars sometimes refer to these types of arrangements, in which firms cooperate to create competitive advantage through their collaboration, as *cooperative strategy* or a *relational advantage*.[7]

Strategic alliances have grown dramatically in importance during the past 25 years. Strategic alliances accounted for only about 5 percent of the revenues of Fortune 1000 companies in 1980, but by 2010 it is estimated that they accounted for almost one-third of the revenues of Fortune 1000 companies. In Walt Disney's case, Tokyo Disneyland contributed almost 20 percent of Disney's total theme park profits in 2011.[8]

Today, many companies are increasingly using alliances to achieve strategic objectives. The basic logic for alliances can be summed up in the adage, "Two heads are better than one." Sometimes it just makes sense to combine the resources and capabilities of two companies to solve certain problems or achieve particular objectives.

Companies can choose to cooperate at any stage along the value chain, from research and development to manufacturing to the marketing, sales, or service of products or services. For example, BMW and Toyota are doing R&D together to develop new fuel-cell technology to increase fuel efficiency.[9] Intel and Micron have teamed up to manufacture flash memory together.[10] Target and Neiman Marcus have partnered to sell affordable luxury brands.[11] In these instances, firms collaborate to improve their performance at common stages of the value chain. In other instances, a firm might team up with a firm at a different stage of the value chain. For example, Apple and AT&T teamed up to sell the iPhone—Apple provided the phones and AT&T provided the cellular network.[12] Although there are different ways to categorize alliances, perhaps the most common way to distinguish one type of alliance from another is by the mechanism used to govern the alliance. We explain these different types of alliances in the next section.

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Choosing an Alliance

Companies have three choices—summarized as make, buy, or ally—when it comes to conducting any particular activity that needs to be done to offer a product or service to a customer.

- First, they can *make*, or conduct the activity themselves within the firm.
- Second, they can *buy*, or purchase, the activity or input from another firm, using an "arm's-length relationship," in which the buyer purchases an input with no obligation to have a long-term relationship with the supplier. Companies that send out a "bid" to numerous suppliers and then buy from the supplier that offers the lowest price have an arm's-length relationship with those suppliers. The winner of the bid this month might lose next month.
- Finally, they can *ally*, or *access*, the activity or input from another firm, using an exclusive partnership with that firm.

As discussed in Chapter 7, companies want to conduct those activities internally that are most important to delivering the unique value they hope to offer. Disney prefers to create its own stories and characters for its movies, make its own movies, and run its own stores. These activities are most important to its success with customers, and therefore it wants to have control over those activities.

However, companies can't do everything, so they buy many inputs from other companies using an arm's-length relationship. Arm's-length relationships work just fine for purchasing commodities, inputs that aren't differentiated on anything but price. For example, Disney doesn't have a partnership with suppliers that provide fabric for its character's costumes or hot dogs and buns for its theme park restaurants. It can purchase those inputs from whatever supplier offers the lower price. Similarly, automakers need to purchase basic inputs such as nuts and bolts from suppliers to put their cars together, but they usually don't have a partnership with those suppliers.

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