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STRATEGIC ALLIANCES AND FIRM PERFORMANCE: THE ROLE OF INDUSTRY STRUCTURE: A CRITICAL REVIEW OF LITERATURE

[1] Dr. Nyaberi, Justry P. Lumumba

Senior lecturer, School of Law, Catholic University of Eastern Africa, Kenya

P.O Box 62157. 00200

Abstract: **Firms around the world cannot survive without creating alliances that bring together vital skills, resources and capabilities, that otherwise will be time and cost consuming to obtain. The current paper reviews literature on how industry structure influences the relationship between strategic alliances and performance aspect. The study is anchored on Dynamic Capabilities Theory, The Institutional Theory and the Resource Dependence Theory. Structure poses a challenge to implementation of strategic alliance because it involves restructuring of firm and work processes. Structure of alliances reflects the vision and intentions of the partners. Choosing the appropriate structure from joint ventures, equity bilateral, equity unilateral or contracts structure involves creating a fit between the structure and alliance strategy. The review of literature shows that strategic alliance challenges affects firm performance. Despite the popularity of strategic alliances in business, a considerable proportion of strategic alliances face many challenges and are unstable or performed unsatisfactorily. Further, the rates of instability and unsatisfactory performance are relatively higher in developing countries than in developed countries. The paper concludes that the underlying structure of an industry is reflected by the strength of his Five Forces model which describes the firm as facing buyers, suppliers, substitute products, potential entrants and rivalry from established players. The strength of each if the five competitive forces is a function of industry structure. The results of this study are important in influencing the government policy. This is especially because of the intervening effect of industry environment. The government should put measures to ensure that firms have favorable business environment. The Ministry of Industrialization and Enterprises Development in liaison with other ministries should ensure that there is appropriate legal framework that enhances the business environment. This is important because the government formulates and implement appropriate policies based on empirical data, the firms in strategic alliances will have more conducive environment to be competitive locally and globally.**

Keywords: **Strategic alliances, Industry structure, performance.**

1. INTRODUCTION

According Doz and Hamel (1998), strategic alliance is the response to globalization and changes in economic activities and technology. Thus firm around the world cannot survive without creating alliances that bring together vital skills, resources and capabilities, that otherwise will be time and cost consuming to obtain. Creation and management of strategic alliances are essential to one's success in modern times, when firms are engaged in a race for the world and the future. However, whether this is justifiable or not remains highly debatable. Bar Nir and Smith, (2002), argues that alliances provide the advantage of decreased dependency on supplier and make firm potentially more self-sufficient. Many horizons can be opened as a result of an excellent strategic alliance. Some of which are reduced cost of supplies, quick access to more and reliable information, exploring new markets through a confident entry, more resources and

technology advancements. According to Gray (1989), alliances offer a mechanism through which "parties who see different aspects of a problem can constructively explore their differences and search for solutions that go beyond their own limited vision of what is possible". Strategic alliances are typically voluntary, enduring relationships that involve resource sharing and joint decision making. They offer partner firms a number of otherwise unavailable assets including additional human and financial resources, new knowledge, increased flexibility and productivity, and enhanced legitimacy (Austin, 2000; Child & Faulkner, 1998; Gray, 1989; Kanter, 1994). On the other hand Bergquist, et al., (1995) argues that despite the increasing number of strategic alliances and their popularity, the rate of failure has also been remarkable. The percentage rate of failure of all alliances has been estimated to range between 30% and 70% (Bleeke and Ernst, 1991).

2. THEORETICAL REVIEW

Dynamic Capabilities Theory

The dynamic capabilities theory was defined by Teece, Pisano andShuen(1997) in their paper on dynamic capabilities and strategic management. The theory argues that the key role of strategic alliances is appropriately adapting, integrating, and reconfiguring external and internal firm's skills, resources and functional competences to much requirements of a changing environment (Pohjola& Stenholm, 2012). The theory further asserts how the responsiveness or rather the innovativeness of an firm may change and become flexible and even rapid in dynamic markets to avoid arising threats and take opportunities that may lead to improved firm performance.

The theory argues that it is important for firms to understand the changing market and come up with processes that will lead to quick strategy formulation such as entering in to strategic alliances to remain competitive on the changing and uncertain markets (Barreto, 2010). The theory therefore aims to understand a firm's growth and survival after an alliance agreement. Strategic alliances according to the theory may be driven by management fads such as culture change, business process engineering, empowerment, total quality, dramatic changes within the environment, declining firm performance, or even both.

The major critique of dynamic capability theory is that it does not explain how firm responsiveness and innovativeness become timely, rapid and flexible in dynamic markets. Further based on a review and synthesis of the strategic management literature, the theory does not clearly explain the potential to systematically solve problems formed by its propensity to sense opportunities and threats, make timely and market-oriented decisions and to change its resource base (Barreto, 2010; Di Stefano, Peteraf& Verona, 2010).

The Institutional Theory

Firm change often occurs as the result of processes that make firms more similar without necessarily making them more efficient through a process called Isomorphism (DiMaggio & Powell 1991). This theory considers the process by which structures including schemas, norms and routines become established as authoritative guidelines for social behavior (North, 1991). Institutional theorists postulate that the institutional environment can strongly from a basis upon which structures or firm level characteristics are created within the firm. Firm values which are engraved in institutions are transmitted through various mechanisms, including symbolic systems, relational systems, and routines. Institutions are structures based on more or less taken for granted, formal or informal, rules that guide social behavior (Johnson, 1999). The firm characteristics and strategy emerge out of such norms and institutional values as well as systems, meaning that this theory is relevant to the postulation of the two variables. The theory falls short of indicating which institutions or characteristics are more relevant to firm performance than others.

Institutional theory posits that the primary objective of firm change is formal legitimacy. In other words, firms adapt their internal characteristics in order to conform with the expectations of the key stakeholders in their environment. Institutional theory suggests that firms are likely to 'conform' with isomorphic pressures, the meaning of conformity has not been clearly articulated (Frumkin & Galaskiewicz, 2004). Institutional pressures may influence some firm characteristics more strongly than others. Hannan and Freeman (1984) argue that changes in the institutional and task environment may alter the firm 'periphery' while leaving the 'core' intact.

The Resource Dependence Theory

The theoretical proponents were first put forward by Emerson (1963) and then advanced by the arguments of Pfeffer and Salancik (1978) who argued that the motivation of other firms depending on another firm is the possession of the critical resources that is required for the said firms to gain competitive edge. The theory sets the argument that all firms have

heterogeneity of resources plus capabilities even if they operate within the same environmental and industrial confine (Leiblein, 2003).

It is therefore not practical to according to the theory to say that firms are self-sufficient in terms of resource possession and especially those resources that enable them to be more competitive. It is therefore argued that they have to rely on other firms that can contribute positively in terms of sharing that critical resource that brings competitive edge and market survival. Further that argument is that strategic alliances are now necessary for firms to reduce those uncertainties by acquiring that critical resource to remain on the market competition (Gray & Yan, 1992).

This theory however has shown major weaknesses and challenges. For instance it does not take into account the effect of a single resource on the firms operation if it is assumed in the bunch of other resources deemed important to a firm. The theory further does not link directly how the resources deemed necessary in a firm affects the overall performance or how it depends on the environment in question. Thus, it only makes assumptions on how environment and key actors intertwine in achieving firm objectives. The theory also does not come out clearly on the aspect of uncertainty and how firms can engage resources reduce environmental or management risks.

3. LITERATURE REVIEW

Implementation of strategic alliances involves operationalizing of partner's plans, intentions and expectations (Kale, 2009). Implementation phase reveals the antecedent outcomes which pose challenges to alliances. Strategic alliances challenges are categorized as either "hard" or "soft" (Ulijin et al, 2010). The "hard" challenges are process and firm based while the "soft" components are human based. The "hard" components include; implementation coordination, structural changes, managerial control and cultural dimensions. The "soft" challenges are; opportunistic behaviors, conflict resolutions, communication and the human resources.

Strategic alliance requires a lot of coordination to ensure institutionalization of processes, systems and learning transfer mechanisms between partnering firms (Dyer et al, 2001). There is therefore a need to have a dedicated managerial coordination function or team to coordinate the implementation process. The coordinating team that is drawn from all the partners is usually headed by an external consultant, thereby making the coordination work rigorous and expensive. Ireland et al, 2002 observes that firms with a managerial coordination function achieved 25% implementation success rate compared to firms without such a function. The managerial coordination team ensures timely availability of resources, integrates the processes and offers solution to problems before they impede the implementation.

Structure poses a challenge to implementation of strategic alliance because it involves restructuring of firm and work processes. Structure of alliances reflects the vision and intentions of the partners. Structure influences flexibility and how operational functions of marketing, production, information sharing, equipment's and logistics are operationalized (Klint et al, 2003). Choosing the appropriate structure from joint ventures, equity bilateral, equity unilateral or contracts structure involves creating a fit between the structure and alliance strategy (Colombo, 2003).

Management control and commitment challenge arises when the partners in an alliance exercise control and influence in an attempt to reduce the level of uncertainties (Ireland et al, 2002). Jostling for key positions that give power and influence is a characteristic of alliance (Das et al, 1997). Trust and commitment to the alliance is reduced where a partner exercise a disproportionate level of control. Hill et al, (2000a) has observed that willingness to share resources and to engage in risk oriented ventures is influenced by the level of trust between partners in alliances. Commitment to the alliance is the degree to which the partners involve their time, energy and resource. Das (2000) suggests that management horizon orientation influences the commitment. Managers with short-term horizon show little commitment and are likely to be involved in opportunistic tendencies and pursuit of short term goals.

Culture clash is bound to be a challenge in implementing strategic alliances because alliances are encounters between partners with different backgrounds. Holfsted (2001) categorizes culture to be national, firm, or professional. Culture determines alliances compatibility, integration and harmony (Grotehuis, 2001). National cultures that affect alliances at national or global level include power distance, uncertainty avoidance, long term orientation and long term drive. Corporate or firm culture has extremes of: rigid or flexible structure, process or result orientation in work, pragmatic or nominative attitude towards market, open or closed systems (Ulijin et al, 2001). Presence of firm cultural discrepancies results to alliance implementation challenges. Human resource skills, competences, commitment and capabilities are a challenge to strategic alliances; occurs when partners fail to commit the best of their employees to the alliance.

Uncertainties in alliances and short horizon perception held by managers make them perceive strategic alliances as temporally undertakings that requires less performing employees (Das et al, 1997).

Porter (2007) suggests that industry structure is manifested in the strength of five competitive forces which include threat of new entrants, threat of substitute goods, bargaining power of suppliers as well as customers and rivalry among existing competitors. These forces determine an industry's long-run profit potential because the forces shape the division of value among industry actors—whether profit is constrained by substitutes or new entrants, bargained away by customers or suppliers, or competed away by rivals. By studying these forces, a firm finds a position in an industry where it can influence the forces in its favor or buffer itself from the power of the forces (Hitt, Ireland, & Hoskisson, 2011).

The arena in which competition takes place is the industry in which a company and its rivals vie for business. Each industry has a distinctive structure that shapes the nature of competitive interaction that unfolds there. Understanding the underlying structure of a company's industry, now and in the future, is a core discipline in strategy formation. The quest to understand the determinants of performance have created a bifurcated view (Galbreath & Galvin, 2008). On one side of the debate is the structural characteristics of industry while on the other are the firm-specific characteristics. While the debate continues, it could be likely that firm specific influence on strategy could be impacted on by the industry structure.

Understanding the forces that shape competition in an industry is the starting point for developing strategy. It reveals the most salient aspects of the competitive environment and the crucial constraints to overall profitability. It highlights the industry changes that pose the greatest threats and opportunities. Industry structure also provides a baseline for sizing up a company's strengths and weaknesses (Ogollah et al, 2011; Brock et al, 2006): where does the company stand versus buyers, suppliers, entrants, rivals, and substitutes? Most importantly, an understanding of industry structure guides managers toward possibilities for strategic action, including positioning the company vis-à-vis the current competitive forces; anticipating shifts in the forces and exploiting them; an shaping the balance of forces to create a new more favorable structure or one that favors the company. Industry structure reveals insights for positioning. Here, strategy can be viewed as building defenses against the competitive forces or as finding a position in an industry where the forces are weakest (Porter, 2007).

Strategic alliances are formed to facilitate implementation of the firm strategy. Consequently the challenges encountered during strategic alliances implementation directly affect implementation of organisational strategy (Webster, 1999). Alliances implementation challenges include; coordination, structure, management control and commitment, culture and human resources practices. Restructuring of the firm occurs with creation of strategic alliances. An appropriate firm structure shall determine how firm strategy shall be implemented (Mockle et al, 1997). Organic structures are preferred because they provide the required flexibility that enables modification of strategic alliances (Daft, 2007).

Competencies linked to the structural, functional, and social characteristics of alliances are more likely to influence alliance performance through compilation processes. For example, the structural, functional, and social competencies of alliance managers relate to those of alliance teams and alliance firms. In other words, the skills and knowledge of an alliance manager increases the competencies of an alliance team to which he/she is assigned, and the competencies of that team contribute to the competence of an alliance firm, thereby making the latter effective in collaboration (Chen & Tjosvold, 2008). The structure, function, and social characteristics of alliances to which alliance managers are interlinked facilitate or hamper the compilation process.

Almeida, Song and Grant (2002) on superiority of firms to markets and strategies found thatknowledge building through strategic leadership enhances firm performance as a result of cross border alliances. This is argued in the sense that strategic alliances along the border are well interpreted to enhancing performance of the involved firms through strategic leadership functions. In essence therefore this study concludes that strategic alliances are key in any firms to gain competitive advantage from cross border firms as a result of transfer of resources and necessary capabilities along the firms.

4. CONCLUSIONS

The review of literature shows that strategic alliance challenges affects firm performance. Despite the popularity of strategic alliances in business, a considerable proportion of strategic alliances face many challenges and are unstable or performed unsatisfactorily. Further, the rates of instability and unsatisfactory performance are relatively higher in developing countries than in developed countries (Sim & Yunus, 1998). Nevertheless, many of the studies undertaken on strategic alliances in both the developed and developing countries only take into account a small number of factors that

may positively influence strategic alliances outcomes with the effect of strategic alliances and industry structure on firm performance far from clear. Some of the studies even reported contradictory impacts.

The paper concludes that the underlying structure of an industry is reflected by the strength of his Five Forces model which describes the firm as facing buyers, suppliers, substitute products, potential entrants and rivalry from established players. The strength of each if the five competitive forces is a function of industry structure or the underlying economic and technical characteristics of an industry. In any particular industry, not all Porters five forces will be equally important - every industry has its own unique structure. Changes in industry structure therefore have an influence on the type of strategy adopted by firms in an industry. If a firm can shape structure, it can fundamentally change an industry's attractiveness for better or for worse. He says that firms, by applying short sighted strategies, can destroy the industry structure and profitability of the industry. For example, the introduction of generic products by a firm in an industry may enhance the price sensitivity if buyers, trigger price competition among established players and erode high advertising barriers that have kept out new entrants. This therefore affects the performance of firms within the industry. The relationship among the strategic alliance challenges, industry structure and firm performance are intertwined in a conceptual model and discussed in the literature review.

Implications of the study

The finding of the study has the following implications to the theories that formed the theoretical foundation. The results of study indicated that strategic alliances challenges influence the firm performance and therefore support the RBV theory of strategy. The dynamic capabilities theory is consistent with the study because it argues that beyond a firm having resources, it is imperative to determine how to maximize on their utilization. The study will contribute to the body of knowledge; this is especially indicated by clear demonstration of combined effect of the independent variables on performance.

The study provides empirical evidence on strategic alliance challenges and provides a ground for more studies on contingency factors and firm performance. The results of the study contribute toward areas that have been having conflicting results, for example on what influences performance of strategic alliances. The concern has been whether is internal firm level factors or external factors such as industry environment that affects performance of strategic alliances.

The results of this study are important in influencing the government policy. This is especially because of the intervening effect of industry environment. The government should put measures to ensure that firms have favorable business environment. The Ministry of Industrialization and Enterprises Development in liaison with other ministries should ensure that there is appropriate legal framework that enhances the business environment. This is important because with globalization, the business environment has become more dynamic and turbulent. When the government formulates and implement appropriate policies based on empirical data, the firms in strategic alliances will have more conducive environment to be competitive locally and globally.

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