Strategic Alliances, New Challenges

Ed Hendrick

Strategic Alliances: A Relational Approach to Gaining a Competitive Edge

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Edward J. Hendrick, Jr.
Biography

Mr. Hendrick began his R&D career at Bell Laboratories in 1966 and served in a host of management positions, including the project management team responsible for the design and development of the first USA made digital switch. At the Bell System Divestiture, he joined Bell Communications Research (Bellcore). From 1989 through 1993 he was Vice-President, Industry Markets responsible for world wide marketing, sales, and licensing of intellectual property, particularly large systems software. In 1993 he joined U S WEST Technologies, Boulder, Co. where he served until 1996 as the Strategy Implementation Officer. In that role, he was responsible for competitive technology intelligence, strategic technology planning, technology alliance management, and intellectual property optimization and new business development. Mr. Hendrick is currently the Principal in Sagebrush Associates.

Mr. Hendrick is a graduate of St. Joseph's University (Philadelphia) and has his MBA from Fairleigh Dickinson University. Since 1996, he has been pursuing Juris Doctor and Masters in Intellectual Property dual degrees at Franklin Pierce Law Center in New Hampshire.

OVERVIEW

- Marketplace Realities
- Business Implications
- Economic Signals
- Views Of The Experts
- Some Industry Examples
- Model For Self Examination/Client Analysis
- Some Legal Quandaries

Marketplace Realities

- Information Age Success
  - demands total solutions that are technologically superior, timely, understandable, valuable, permissible
  - craves multi-functional capabilities integrated as solutions
  - is perceived as more dependent on customization and packaging than on technology or platforms

Marketplace Realities

- Success (cont'd)
  - is optimized by easy access to, and differential use of, knowledge
  - is increasingly dependent on multiple key players and diverse core competencies
  - requires public policy, social and cultural acceptance

Business Implications

- Isolationist "not invented here" attitudes spell doom
- Brilliant ≠ Smart
- A critical excellency vs. a suite of core competencies
- Internal and External Partnering
- Cost of "best in everything" is bankruptcy

Economic Signals

- Virtual "full employment"
- Inflation--2% (+/-)
- Corporate Profits--600+B--up 3X since'92
- Investor Expectations--14-23% ROI !!
  --78M "boomers"
- World Currencies
  -mostly tied to the dollar
  -"chaos" role of the Euro

Economic Signals

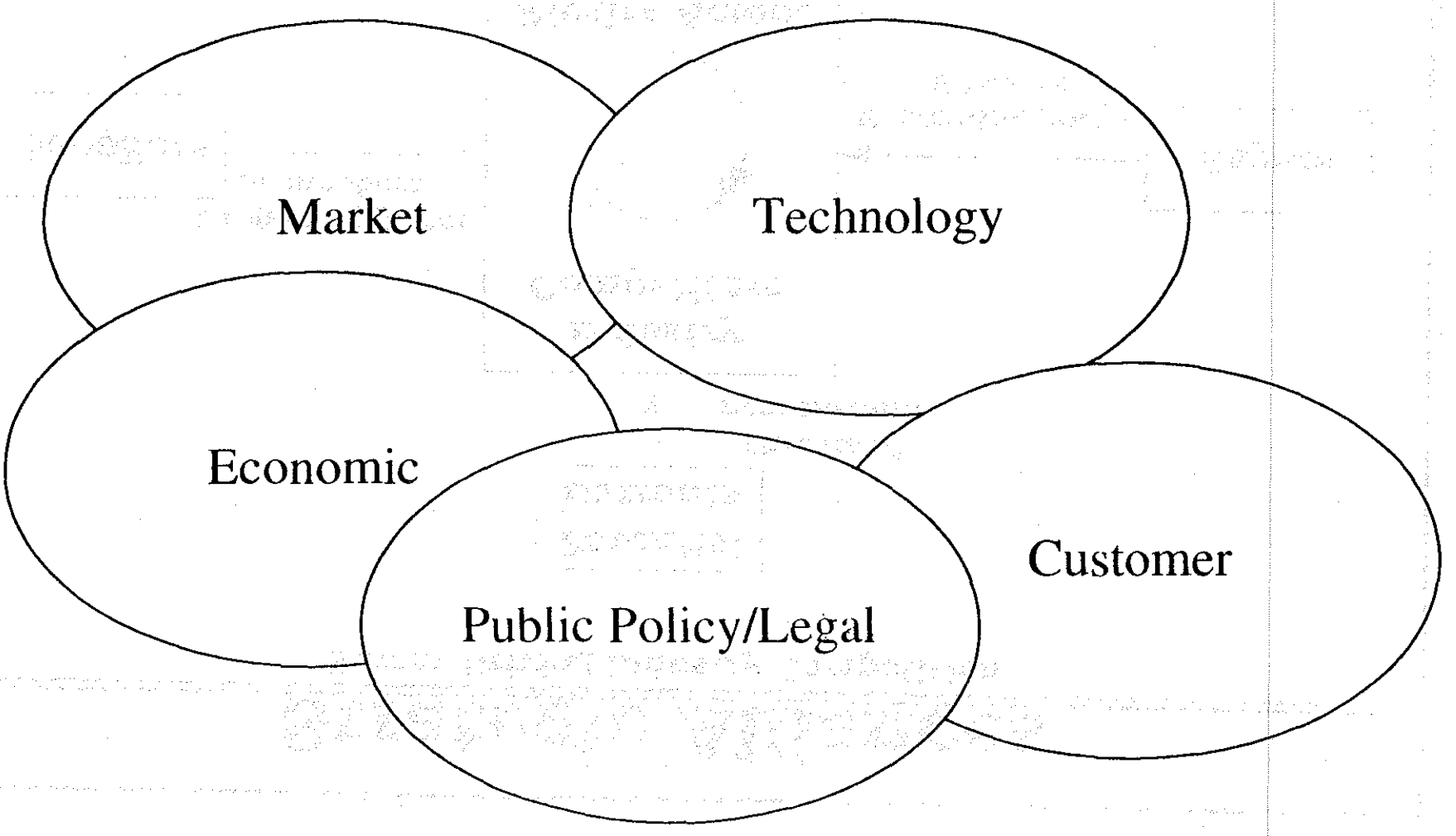
- Globalization--U.S. Exports--% of GDP

  1984 = 7.4%

  1998 = 15.0% (projected)

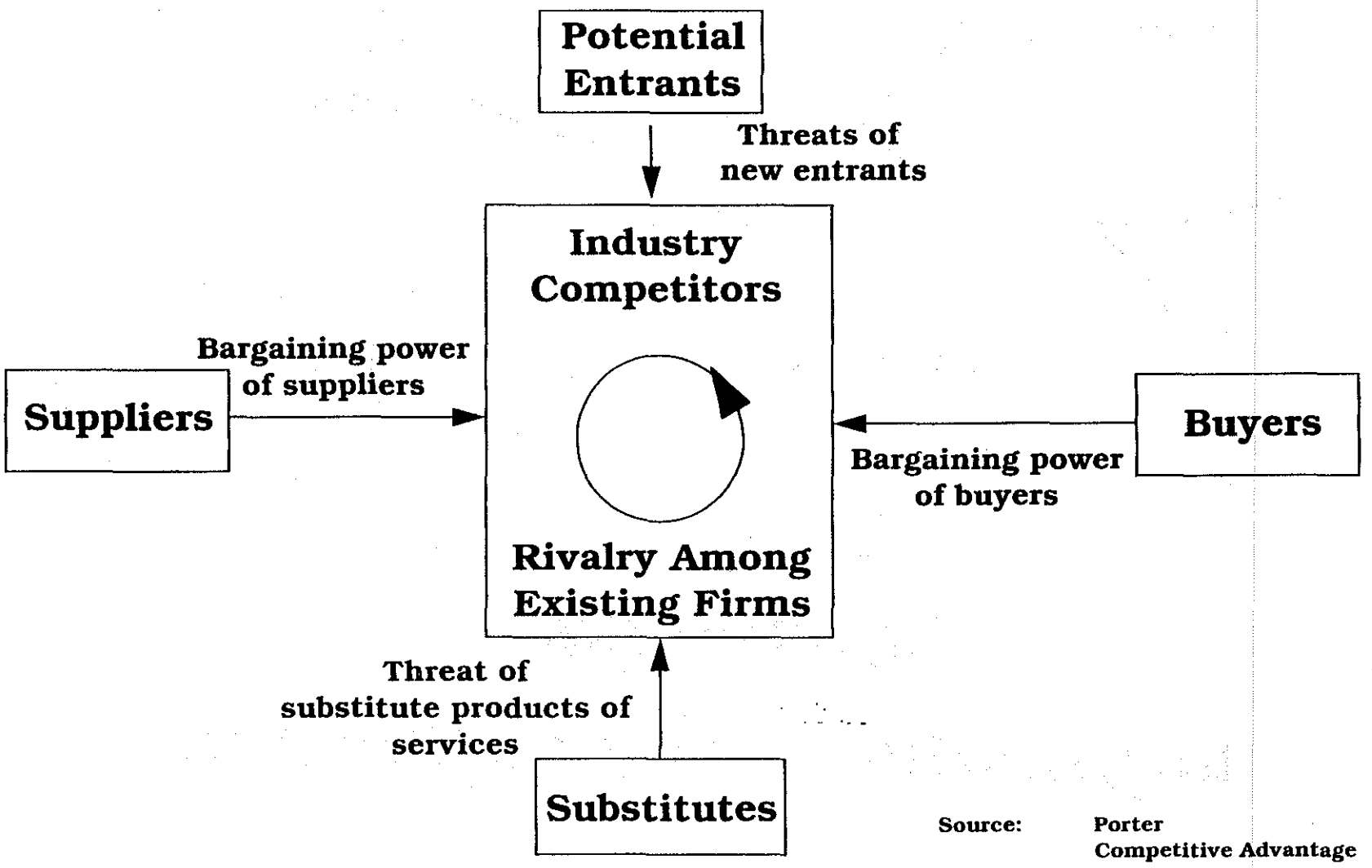
- Initial Public Offerings (IPO)-- $60 B in new money in 1997
- Mergers & Acquisitions (M&A)--1st "one trillion dollar year" in 1998

Information Age Competition Components



Strategic Alliances

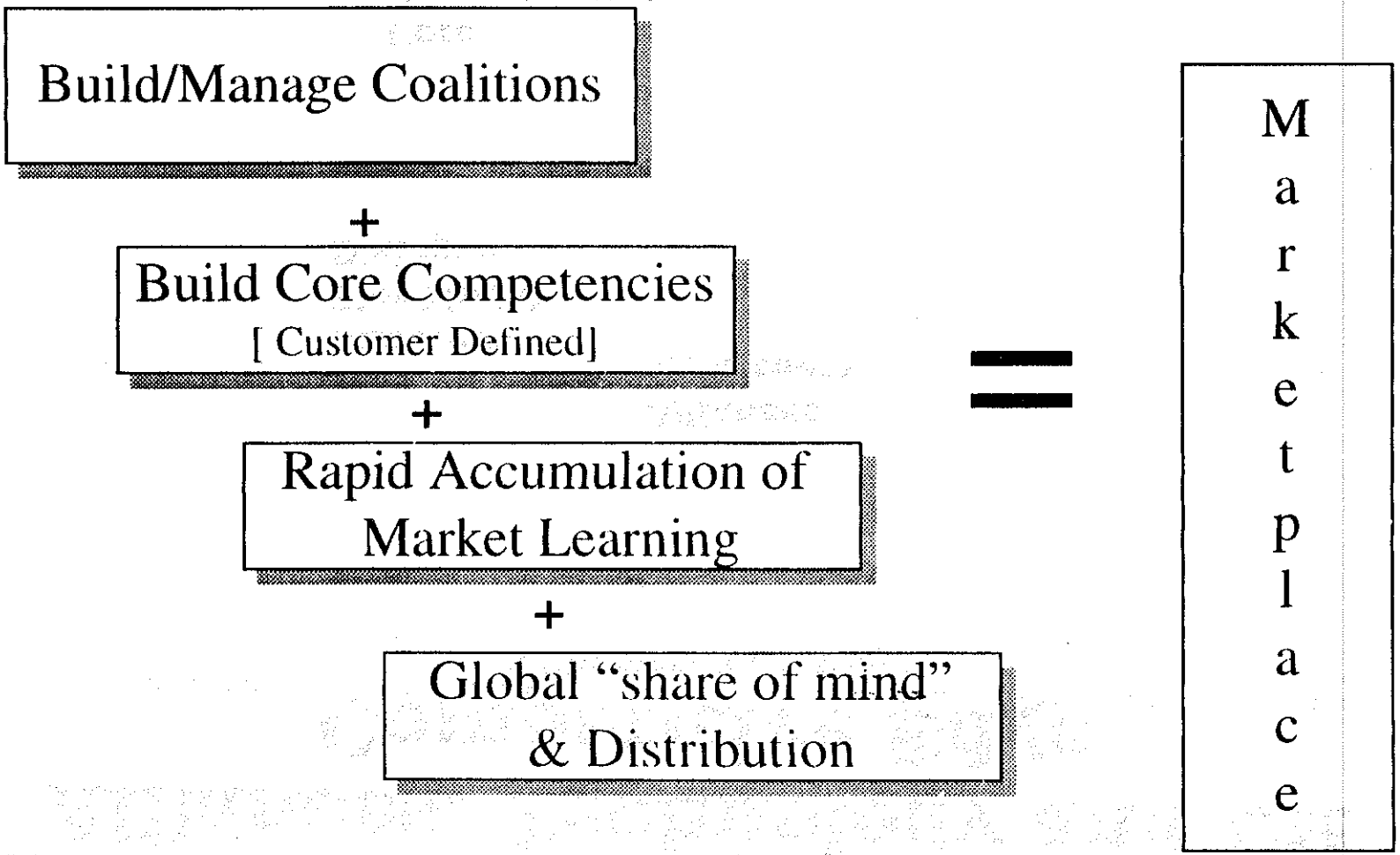
Forces Driving Industry Competition



Source: Porter
Competitive Advantage

Evolving External Focus

[Hamel & Prahalad: Competing for the Future (1990)]



Alliances, Technology and the Competitive Edge

A Shamrock Strategy

Alliances & Partners

Strategic Thinking & Dialogue

Core Competencies

Adapted from: **Handy**
Age of Unreason

Alliances, Technology and the Competitive Edge

A Shamrock Strategy

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Alliances & Partners

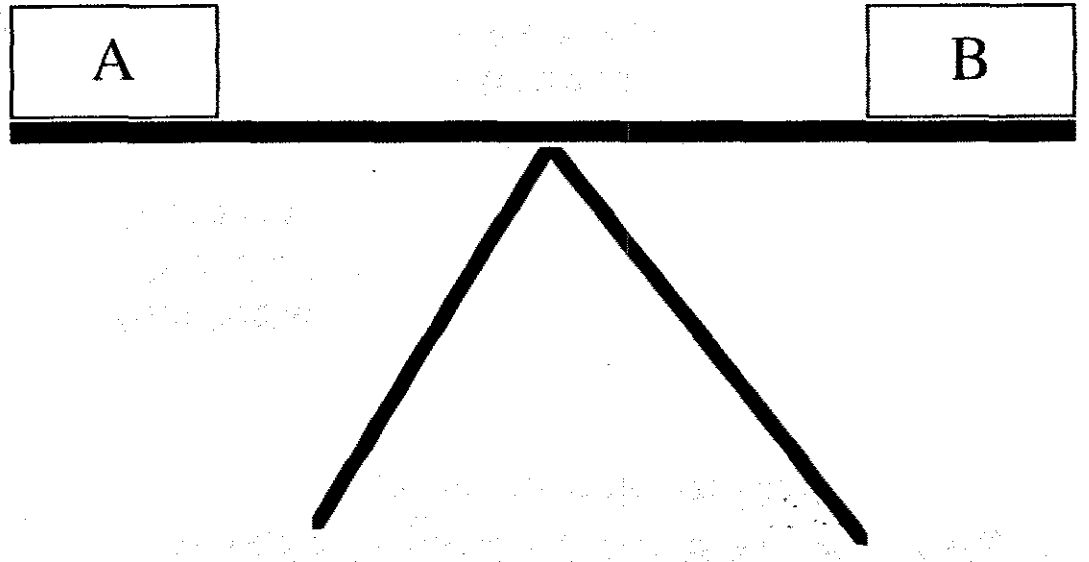
Core Competencies

Customer

Adapted from: **Handy**
Age of Unreason

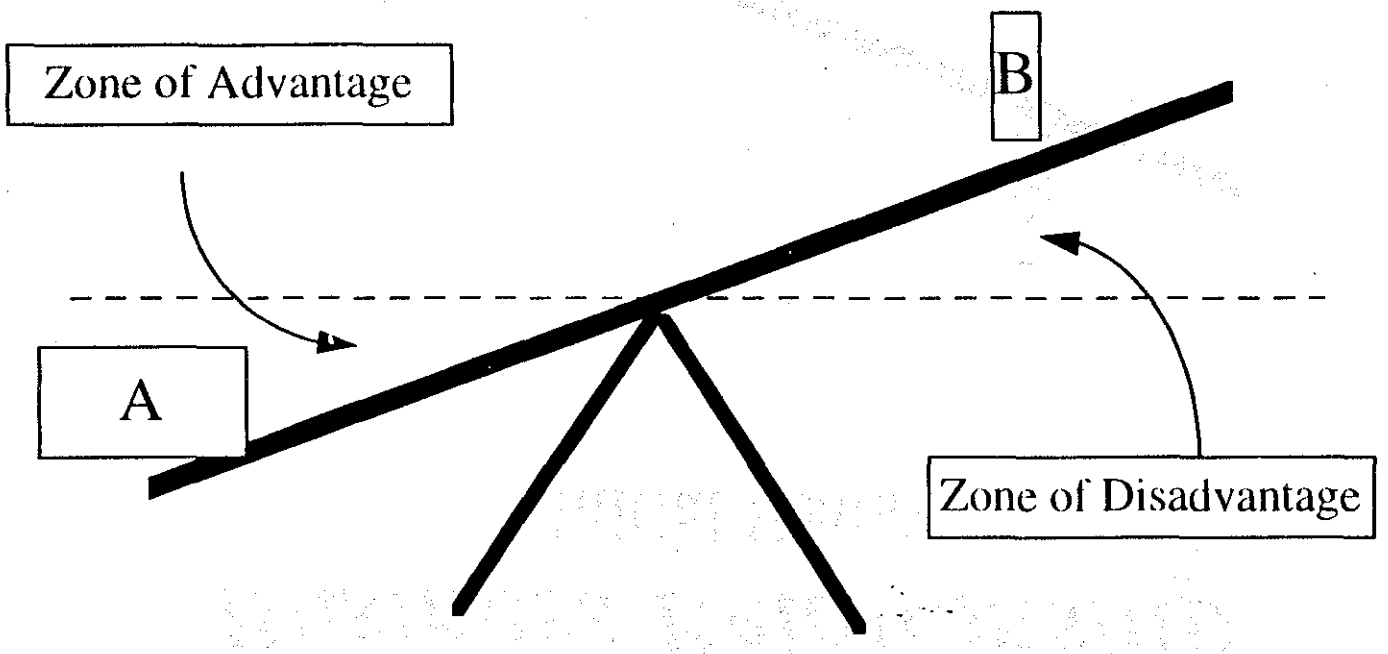
Cost Of Participation

"The Perfect Contract"



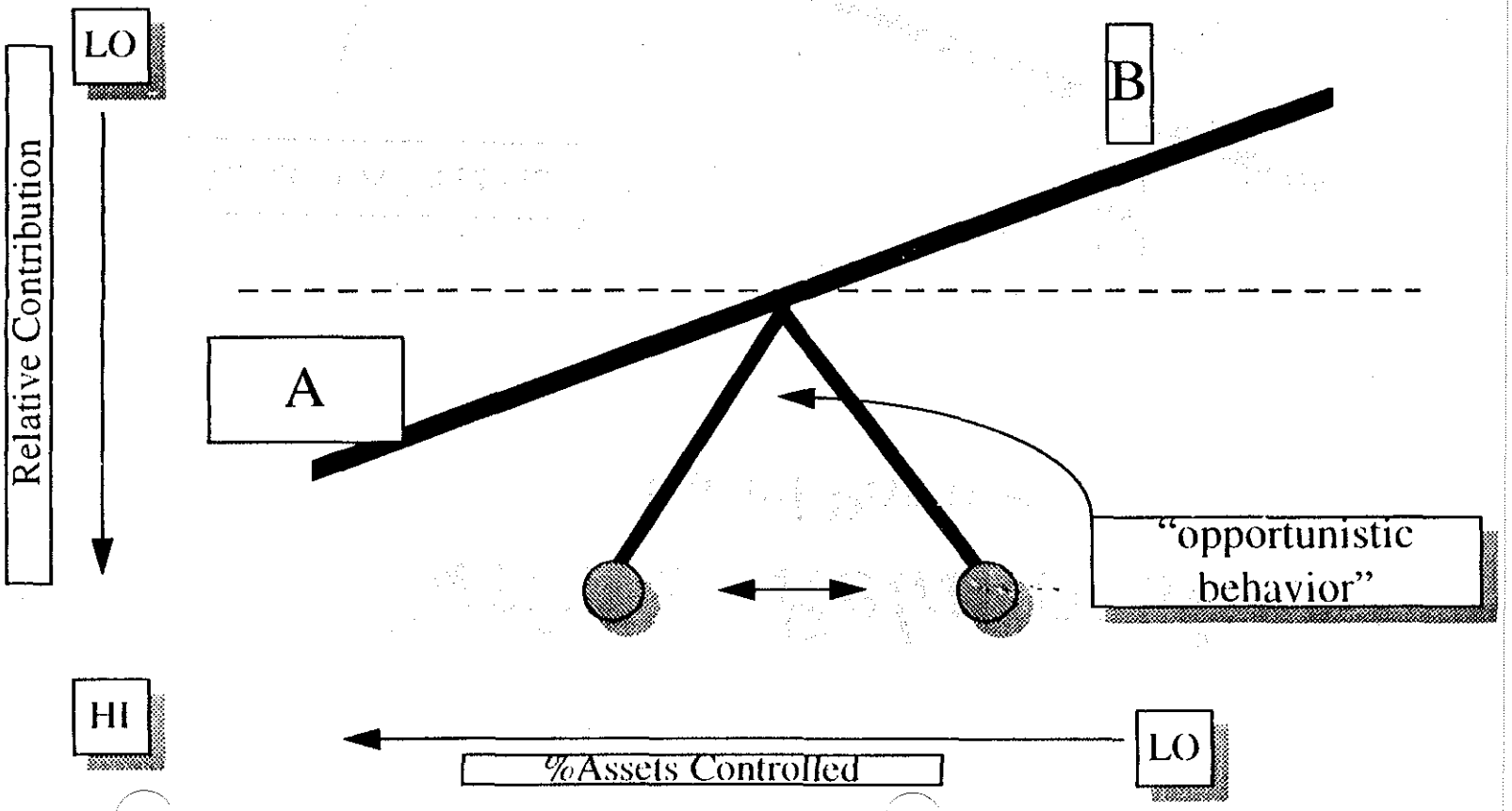
Business Relationship

-Initial Posture-



Business Relationship

-Initial Fears-



Trust

"In legal theory contract may express trust, but in social reality our fondness for contract demonstrates a degree of mistrust among people who persistently pursue their own advantage at each other's expense."

Auerbach:
Justice Without Law

Strategic Alliances

Some Definitions

"A coalition of two on more organizations to achieve strategically significant goals and objectives that are mutually beneficial. These goals and objectives can be pursued in either the economic or political arena, and can be flexible in time orientation."

Source : Murray and Mahon

Strategic Alliances : Gateway to a New Europe ?

Strategic Alliances

Some Definitions

"Non zero-sum games, enhanced by the cooperation-inducing feature of communication, in which both parties to the arrangement anticipate benefits (due to an "expanding pie")."

Source :Parkhe

Partner Nationality and Structural Performance in Alliances

Strategic Alliances

The "Endgame"

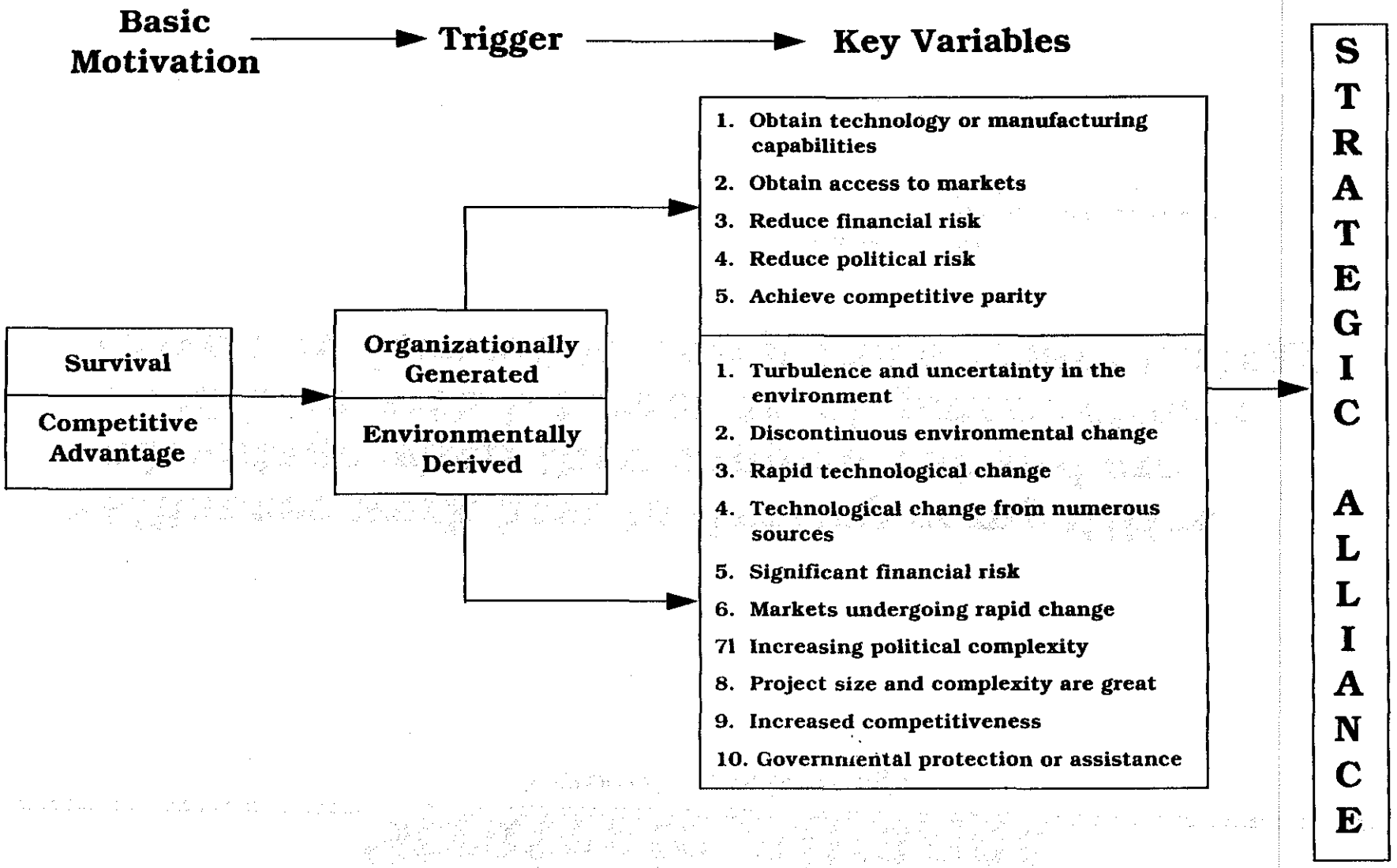
$$S \geq Q * 2$$

Where:

S = Synergy

Q = Quid Pro Quo

Reasons for Forming a Strategic Alliance



Strategic Alliance

-Competitive Advantage-

- **Alliances work best to develop competitive advantage when they supplement and are combined with internal development efforts driven by focused learning and a clear strategy.**

Source: **Lei**
Offensive and Defensive Uses of Alliances

Strategic Alliances

Required Conditions for Some Success

- **Understand your own core competencies and skills**
- **Choose partners with complementary skills and markets**
- **Match external alliances with internal strategic intent**
- **Keep alliance personnel long-term**
- **"Pre-nuptial" planning**
- **Measure alliance worth**

Source: Lei
Offensive and Defensive
Uses of Alliances

Strategic Alliances

Required Conditions for Some Success

- **Clear, strategic understanding of one's current and future required capabilities**
- **Identify and truly consider a wide range of alliances**
- **Understanding / identification with values, commitment, capabilities of potential partners**
- **Understand risks of opportunism, knowledge leaks, and obsolescence**
- **Avoiding undue dependence**
- **Structured and managed like separate companies**
- **Mutual trust**
- **Willingness to change operations and organizations to be open to learning**
- **Must be led, not managed**

Source: **Badaracco**
The Knowledge Link

Strategic Alliances

Eight I's that create Successful We's:

- **Individual Excellence**
- **Importance**
- **Interdependence**
- **Investment**
- **Information**
- **Integration**
- **Institutionalization**
- **Integrity**

Source: **Kanter**
Collaborative Advantage

Strategic Alliances

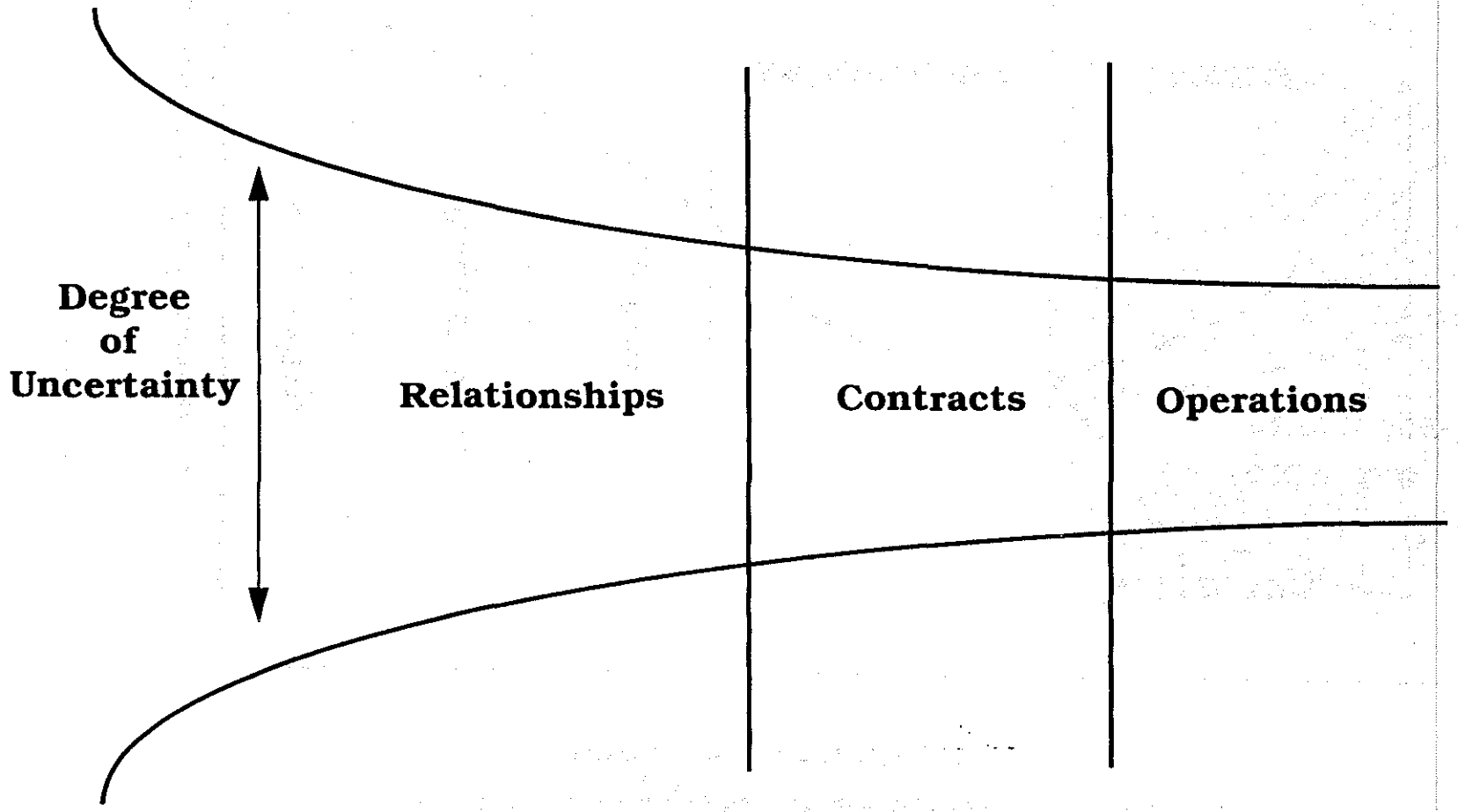
Challenge to *Integrate* the Partnership

- **Strategic - continuous contact/commitment among top leaders**
- **Tactical - Involvement of middle managers/professionals on specifics**
- **Operational - Timely, mutual access to information, resources, people**
- **Interpersonal - Foundation of people to build value**
- **Cultural - Communication skills and awareness of differences**

Source: **Kanter**
Competitive Advantage

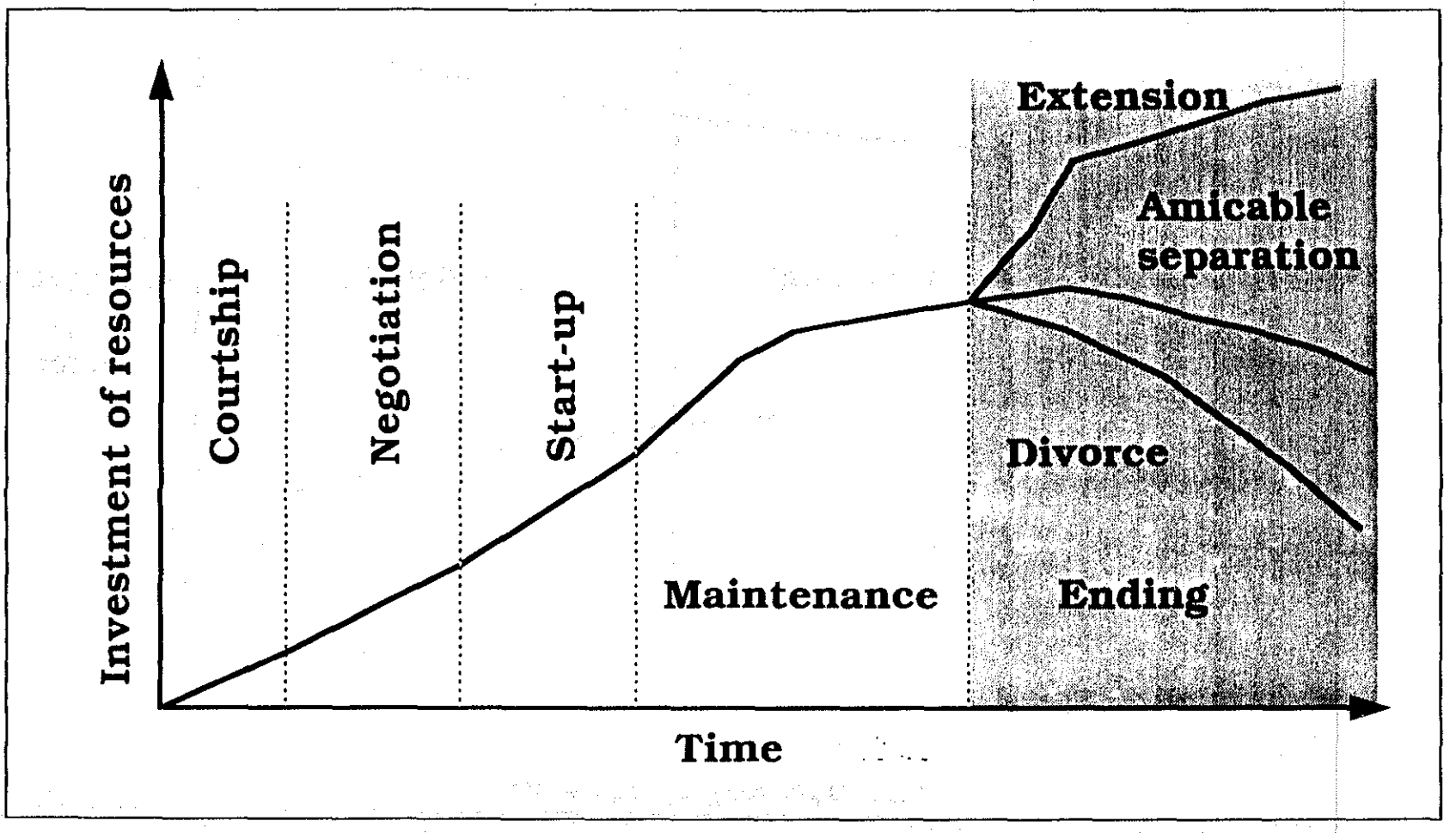
Strategic Alliances

Life Cycle Investment



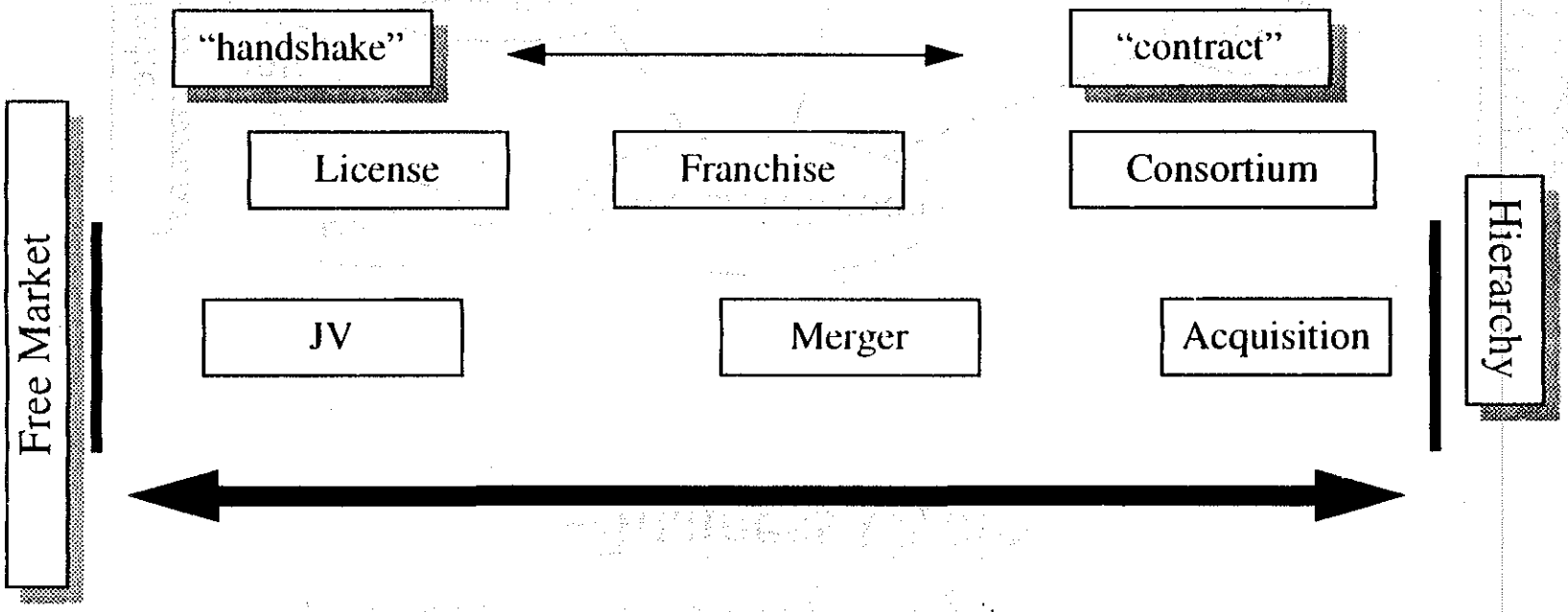
Strategic Alliances

Life Cycle Investment



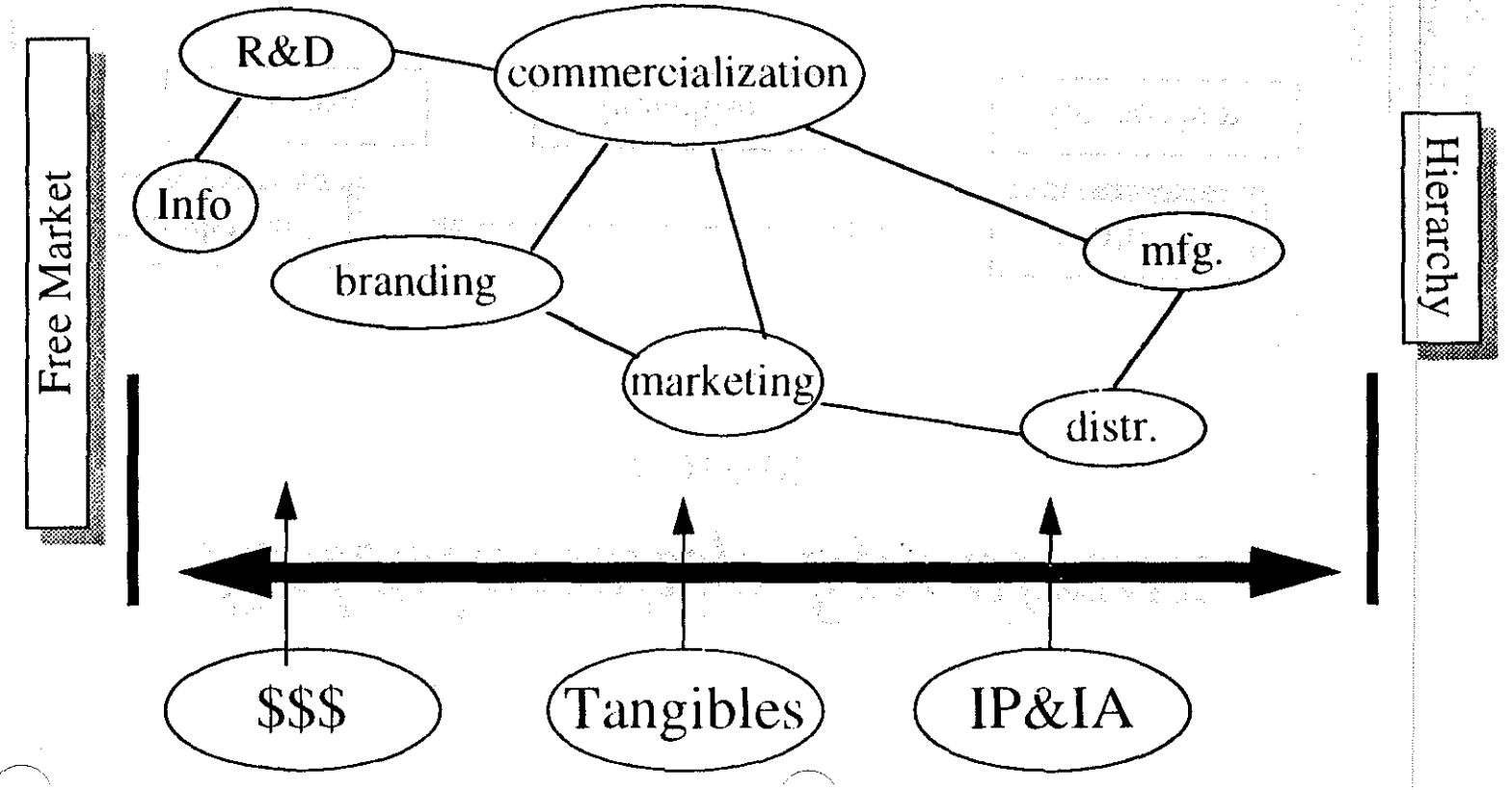
Relationship Spectrum

-Forms-



Relationship Spectrum

-Business Cycle-



Strategic Alliances

Strategic alliances in the semiconductor industry

U.S. Firm	Partner	Technology
AT&T	NEC	Custom-designed chips
	Mitsubishi	Manufacturing and design skills
Intel	NMB Semiconductor	DRAM Technology
	Samsung	DRAM Technology
	Sharp	Flash memory chips
Motorola	Hitachi	Specialized logic chips
	Toshiba	Advanced microprocessors
MIPS	Digital Equipment	RISC Technology
	NEC	
	Kubota	
	Siemens	
Sun Microsystems	Fujitsu	RISC Technology
	Texas Instruments	
	N.V. Philips	
	Cypress Semiconductor	
	Bipolar Integrated	

Strategic Alliances

AT&T's alliance strategy

Partner	Technology	Intent
NEC	Customized chips Computer-design tools	Learn new core technologies from NEC, increase sales position in Japan
	Mobile phone	Penetrate cellular phone market; compatible standards
Mitsubishi	SRAM and gallium-arsenide chips	Increased sales in Japan; learn new semiconductor technologies
N.V. Philips	Circuitboards	Market and technology access; venture purchased in 1990
Lucky-Gold Star	Fiber optics, telecommunications, circuits	Entry into Asian markets; technology sharing agreement
Telefonica	Telecommunications and integrated circuits	Expand production and marketing beachhead in Europe
Zenith	High-Definition television	Apply and learn digital compression technology to set new broadcast standards in U.S. and global markets
Intel	Personal computer networks and integrated circuits	Shared manufacturing technology and capacity. Develop UNIX compute operating system for local area networks
Go Corp.	Pen-based computers and wireless networks	Set industry standards for telecommunications power and range
Olivetti	Personal computers	Failed in 1988
Eo corp.	Personal communicator devices	Create new hand-held computers, failed 1994
McCaw Cellular	Cellular telephones	Secure downstream market in U.S.

Strategic Alliances

Corning's major alliances

Venture	Partner	Technology
Pittsburgh-Corning	PPG Industries	Shared production
Owens-Corning	Owens-Illinois	Auto, industrial fibreglass
Dow Corning	Dow Chemical	Silicone technology
Iwaki Glass	Asahi Glass	Glass Bulbs
Samsung-Corning	Samsung	TV tubes
Siecor	Siemens	Fibre optics production
Genencor	Genentech and Eastman Kodak	Industrial enzymes
Ciba Corning	Ciba-Geigy	Medical diagnostics Sold in 1989
Corning-Asahi	Asahi Glass	Colour TV tubes
NGK-Corning	NGK Insulators	Ceramics for catalytic converters
Corning-Vitro	Vitro	Household glassware

Strategic Alliances

IBM's alliance strategy

IBM

Personal computers
- Matsushita (Low-end PCs)
- Ricoh (Hand-held PCs)

Computer Hardware/Screens
- Toshiba (Display tech)
- Mitsubishi (Mainframes)
- Canon (Printers)
- Hitachi (Large Printers)

Factory Automation
- Texas Instruments
- Sumitomo Metal
- Nippon Kokan
- Nissan Motor

Telecommunications
- NTT (Value-added networks)
- Motorola (Mobile data nets)

Memory Chip Technology
- Micron Technology
- Motorola (X-ray lithography)
- Motorola (Microprocessor designs)
- Sematech (U.S. Consortium)
- Intel (Microprocessor designs)
- Siemens (16 and 64 Megabit chips)
- Perkin-Elmer (20% stake)
- Apple Computer (Operating systems and mulitmedia technology)
- SGS-Thomson (Graphics technology)
- Eteq (Electron beam technology)
- Toshiba & Siemens (256 Megabit chips)
- Toshiba (Flash memory)

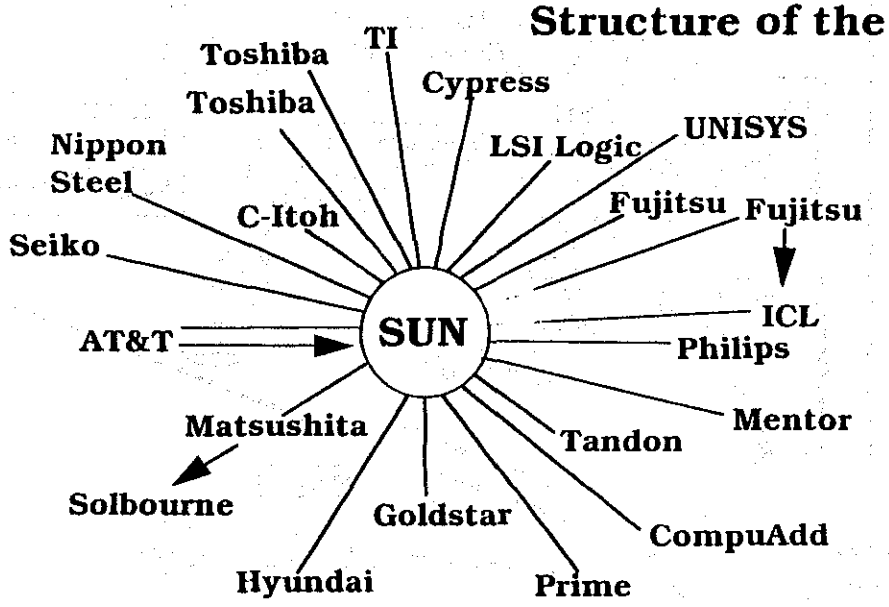
Software Processing
- Microsoft
- Lotus
- Silicon Graphics
- Metaphor
- Wang
- Sun Microsystems
- Hewlett Packard

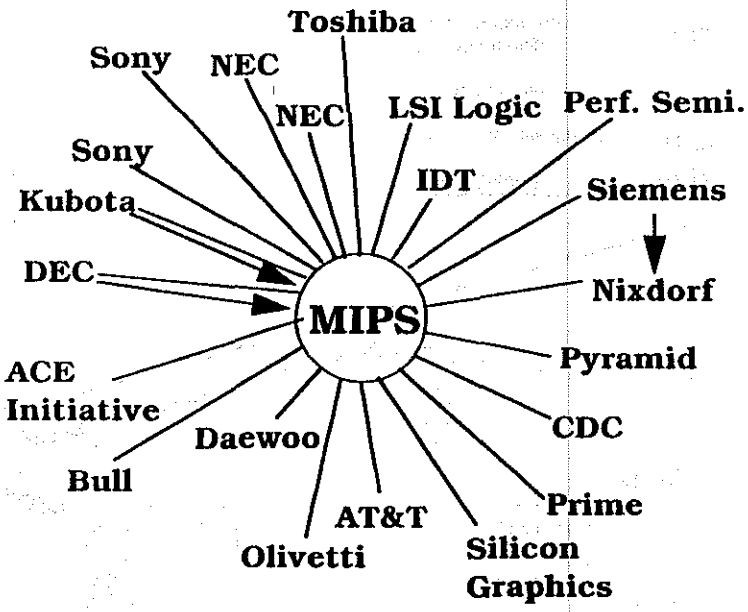
Customer Linkages
- MCI/Rolm
- Prodigy
- Sears
- Mitsubishi Bank
- Eastman Kodak
- Baxter Healthcare
- Hogan Systems

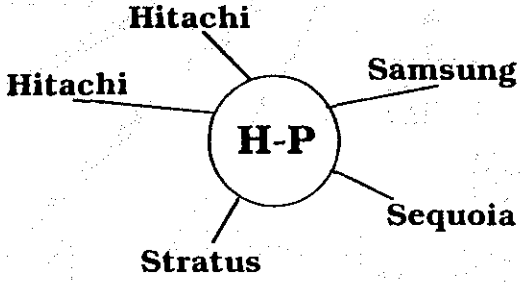
Supercomputers
- SSI
- Thinking Machines

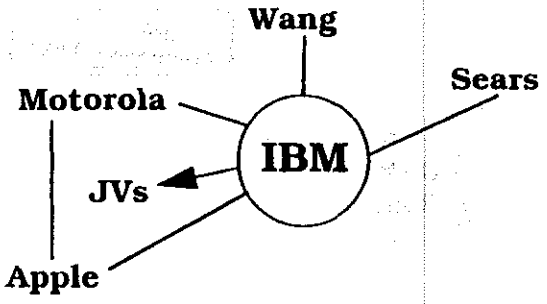
Strategic Alliances

Structure of the RISC Groups



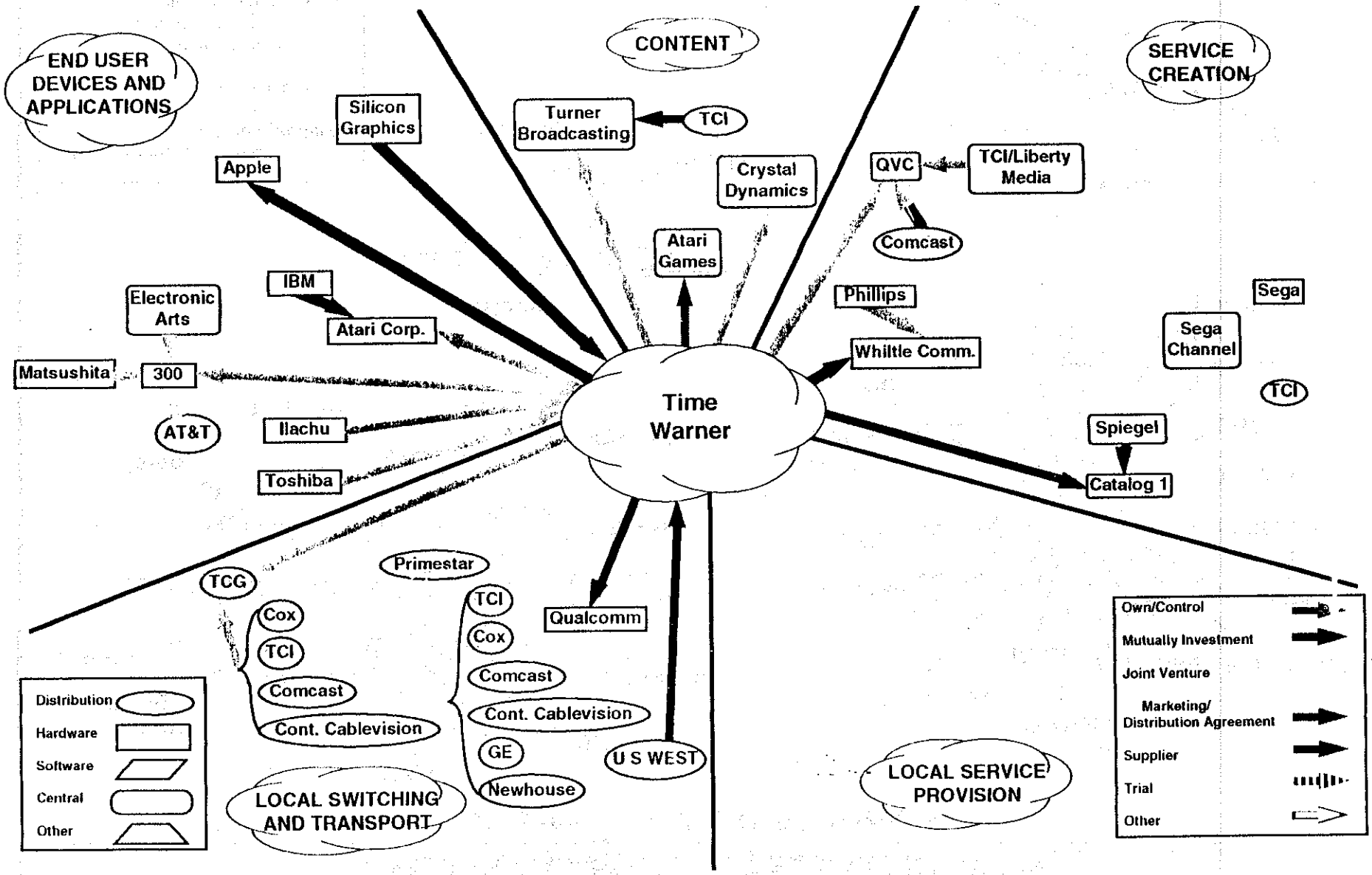






RISC Groups as of 1992
- Semiconductor producer
- System reseller
- System manufacturer

- Technology agreement
- Product supply
- Commitment to use chip
- Equity investment


END USER DEVICES AND APPLICATIONS
CONTENT
SERVICE CREATION
Silicon Graphics
Turner Broadcasting
TCI
Apple
Crystal Dynamics
QVC
TCI/Liberty Media
Comcast
Atari Games
IBM
Electronic Arts
Atari Corp.
Phillips
Sega
Sega Channel
Matsushita
300
Whiltle Comm.
TCI
Time Warner
AT&T
Ilachu
Toshiba
Spiegel
Catalog 1
Primestar
TCG
Cox
TCI
Comcast
Cont. Cablevision
TCI
Cox
Comcast
Cont. Cablevision
GE
Newhouse
Qualcomm
U S WEST
Distribution
Hardware
Software
Central
Other
LOCAL SWITCHING AND TRANSPORT
LOCAL SERVICE PROVISION
Own/Control
Mutually Investment
Joint Venture
Marketing/ Distribution Agreement
Supplier
Trial
Other

"Top 10 New Media Alliances"

When	Who	Deal	Status
May, 1993	U S WEST/ Time Warner	$2.5B buys 25.5% stake to partially find TW's Full Service Network (FSN) with initial test to 4,000 homes - 1994	FSN serving 30 homes- Summer '95
June, 1993	AT&T/Viacom	Test interactive video programs/games to 4,000 customers-Mid 1994	Hold-July '95- deployed to 250 homes
Oct., 1993	NYNEX/ Viacom	JV/strategic relationships around Viacom's talkover bid for Paramount	JV's to be announced by year end '95
Oct., 1993	Bell Atlantic/ TCI	Cable/phone merger to deliver interactive services to 9M homes by 2000	Collapsed
Dec., 1993	CBC/Cox	$4.9B cable/phone partnership	Collapsed 4/94

"Top 10 New Media Alliances" (cont.)

When	Who	Deal	Status
Oct., 1993	Comcast/ Sprint/TCI	Bid for "Personal Communications Services" (PCS) licenses to package and sell local, long-distance, wireless and entertainment services	• 29 markets • 182M potential customers-no announced plans
Nov., 1993	Bell Atlantic/ NYNEX/ Pacific Telesis/ Creative Artists	JV to commit $300M to develop/sell traditional/interactive services to 30 M homes	• 1996 introduction planned • Same as PCS • CA "dropped"
Mar., 1993	Microsoft/ Dreamworks	JV to develop interactive and multimedia products. Target="several hundred million in next 3 to 5 years	Too early
Apr., 1993	Disney/ Bell South/ Ameritech/SBC	$500M programming partnership to develop traditional/interactive services. GTE may join	Too early
May, 1993	MCI/ News Corp	$2B investment- deliver entertainment and information over MCI's digital network	Too early

SOURCE: Wall Street Journal - 9/15/95

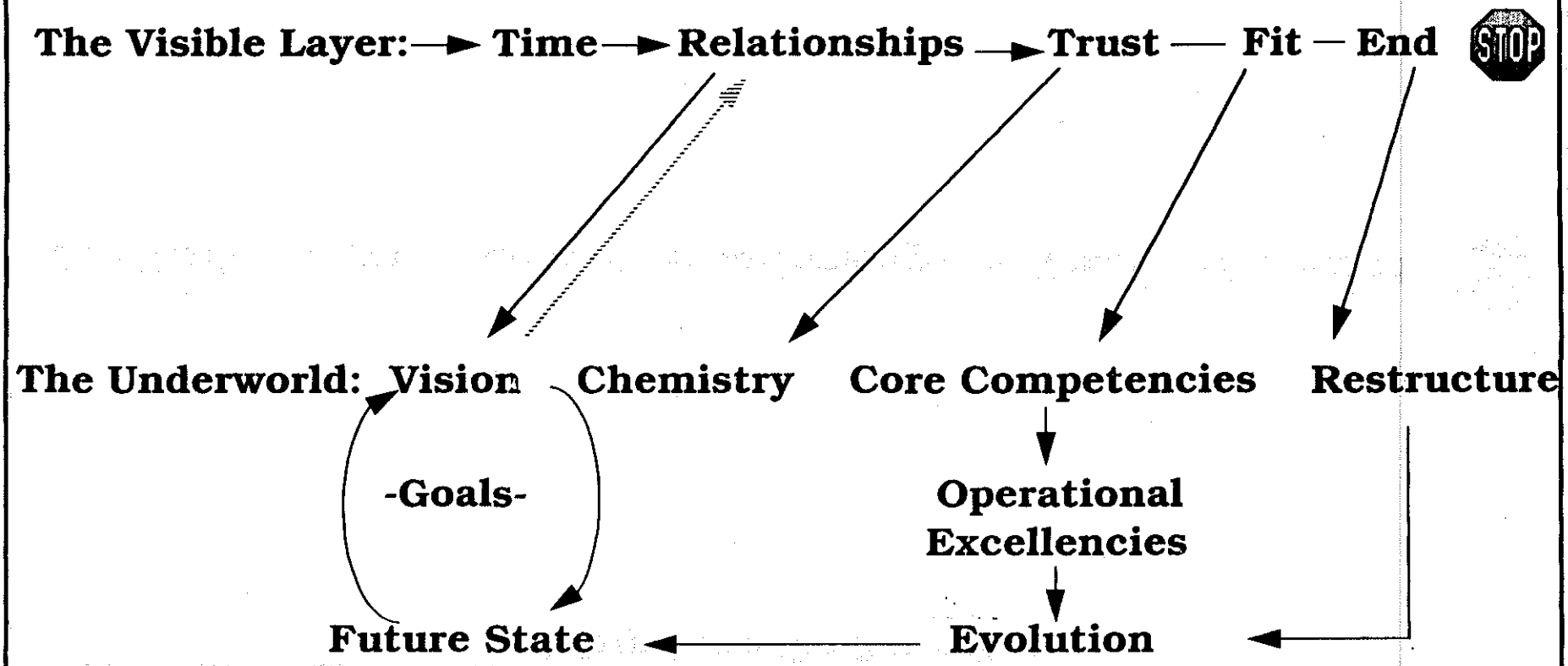
Strategic Alliances

A Trip Down the River Styx

The Visible Layer : Time → Relationships → Trust → Fit — End — 

Strategic Alliances

A Trip Down the River Styx



Legal Quandaries

- Business Goal Disclosure
- Merger related Statements
- Duty to Update
- Antitrust-- "chilling competition"
- 1st Amendment
- Lawyer "risk aversion"
- Fiduciary and Opportunity Doctrines

Moore Business Forms v. Cordant Holdings Corp
(1995 WL 662685, Del. Ch, Nov.. 2,1995)(No. Civ. A. 13911)

Facts: Dispute over termination of 3 party business relationship :

-work together to identify/develop business relationships

-mutual right of first refusal as to certain client requirements

-last a minimum of 4 1/4 years; then either party can terminate as per conditions in Purchase Agreement

Moore Business Forms v. Cordant Holdings Corp (cont'd)

Complaints :

-Breach of contract

-Breach of Implied Covenant of good faith and fair dealing

-Affirmative Misrepresentation of Intent to terminate the Strategic Alliance

Moore Business Forms v. Cordant Holdings Corp (cont'd)

Legal Issues :

-Improper concealment of intention to terminate

-Improper selection of KPMG to perform "valuation"

-Unfair exclusion of π in valuation process

-Selection of unfair valuation methodology

Moore Business Forms v. Cordant Holdings Corp (cont'd)

Business Issues :

-Ability of Entities to act independently of the strategic alliance

-Formal and informal communications

-Legal vs. fiduciary vs. operational behavior

Moore Business Forms v. Cordant Holdings Corp
(1998 WL 71836,Del. Ch. Feb. 6,1998)(No.Civ A. 13911)

Facts: π's designated representative on both Cordant's and Holdings' Boards not included in discussion/information flow associated with Δ's decision to exercise termination right.

Issues:

(1) Is π contractually entitled to same information that π's designated representative would have been entitled to receive ?--YES

(2) Does the Attorney-Client privilege, or any independent side agreement among the parties, bar π's designated representative from access to information that was disclosed to all directors ?--NO

SBC Interactive v. Corporate Media Partners
(1997 WL 7707115, Del Ch., Dec. 9,1997)(No. Civ. A. 14595

Facts : SBC entered a general partnership with the venture entities of Ameritech, Bellsouth, GTE,Disney, and SNET to :

-assemble and market video programming via an advanced broadband network

-create a unique navigator to facilitate consumer program selection

-develop new programming services

SBC Interactive v. Corporate Media Partners (cont'd)

Terms and Conditions:

-expected to last at least 5 years

-under limited, specific circumstances, withdrawal permitted before 5th anniversary

-remaining partners must redeem withdrawing partner's interest

-SBC exercised withdrawal under a permitted contract provision associated with the parent's "material change in strategic direction"

SBC Interactive v. Corporate Media Partners (cont'd)

Legal Issues :

-whether SBC's right to withdraw was arbitrable ?

-whether information compiled by the Partnership's attorneys was available to the withdrawing party ?

SBC Interactive v. Corporate Media Partners (cont'd)

Court's Observations:

-where the interests of one partner become adverse to the partnership, the expected congruency of the partnership and the partner does not hold, unless reasonable reliance to the contrary.

-so long as the Board employs appropriate governance procedures, Board is entitled to deliberate and receive legal advice, in confidence, without having to share with the director representing the adverse party.

Paramount Communications v QVC Network

(637 A.2d 34(1994))

Facts: appeal from decision preliminarily enjoining certain defensive measures designed to facilitate a "so-called strategic alliance"between Viacom and Paramount Communications and to thwart an unsolicited, more valuable, tender offer by QVC.

Paramount Communications v QVC Network (cont'd)

Details :

-sale of control--tender followed by 2nd step merger-$69/share

- "no shop" clause

-termination fee-$100M

-Stock Option Agreement

-senior subordinated note of "questionable marketability"

-cash payment = difference between purchase and market prices(uncapped)

Paramount Communications v QVC Network (cont'd)

Court's Observations:

"Irrespective of the present Paramount Board's vision of a long term strategic alliance with Viacom, the proposed sale of control would provide the new controlling stockholder (Sumner Redstone) with the power to alter that vision."

Paramount Communications v QVC Network (cont'd)

Court's Observations:

"The director's initial hope and expectation for a strategic alliance with Viacom was allowed to dominate their decision making process to the point where the arsenal of defensive measures established at the outset was perpetuated (not modified or eliminated) when the situation was dramatically altered."

Paramount Communications v QVC Network (cont'd)

Court's Observations:

"Their (Board's) view of the strategic alliance likewise became an empty realization as the opportunities for higher value for the stockholder's continued to develop."

U S West, Inc. v. Time-Warner, Inc.

(1996 WL 307445, Del. Ch.. June 6,1996)(No. Civ. A. 14555)

Facts: request for injunction to block "TWI" from acquiring through merger ownership of Turner Broadcasting System (TBS).USW(25.51%) and TWI(74.49%) were remaining limited partners in Time Warner Entertainment(TWE). Limited Partnership agreement precluded any partner from competing with the partnership in business of producing and distributing video programming and filmed entertainment products, subject to certain stated exceptions.

U S West, Inc. v. Time-Warner, Inc.
(cont'd)

Law of Corporate Opportunities :

-Partnerships have greater freedom to design "relationships" than do corporations

-Fiduciary duties may be "clearly contracted"

-Misappropriation of opportunity

(1) similar line of business ?

(2) advantageous ?

(3)means to take advantage ?

(4)officer/director conflict created ?

The Legal Horizon

-Some Observations-

- There is no law of strategic alliances
  - interdisciplinary decisions-contract & equity
  - relationships are not "bright line"
- Areas of Modern Concern
  - how to balance business judgment rule with shareholder protection
    - corporate opportunity doctrine
    - duty to "update"

The Legal Horizon

-Some Observations-

- Antitrust--how to apply principles not politics
  - rapid technology shifts
  - fluid markets
  - aggregation of competencies vs. products
  - offsetting divestitures
- 1st Amendment--merger of the "marketplace of ideas"

Some Learnings

3R's

Relationships

Reciprocity

Review