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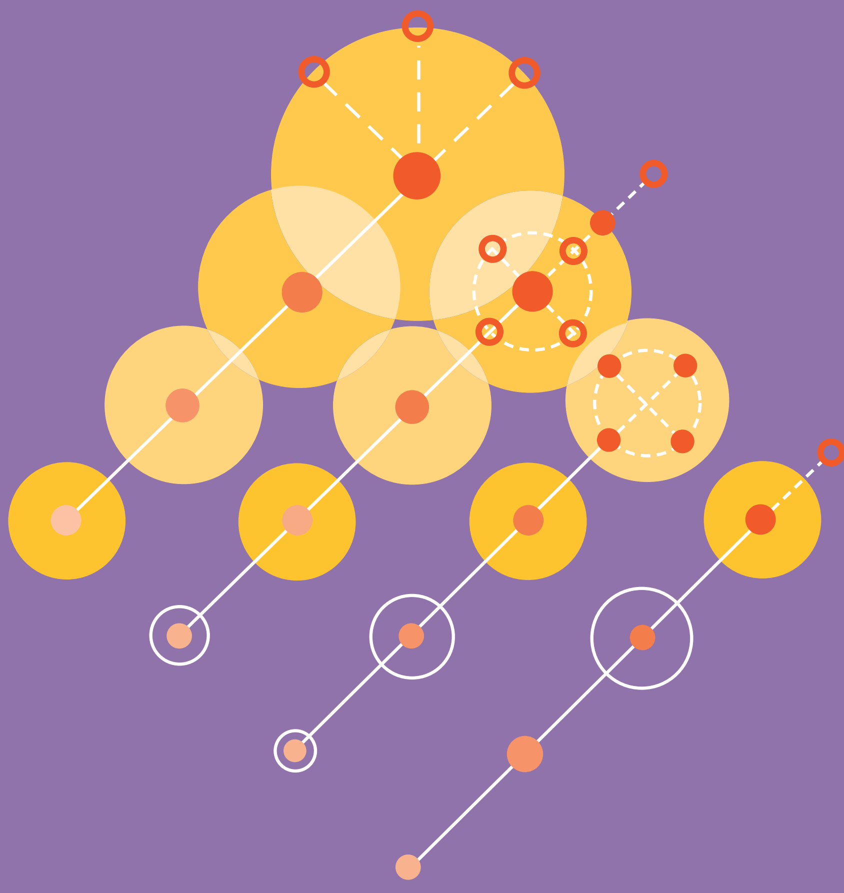
The Allianced Enterprise: Breakout Strategy for the New Millennium



Fifth in a Series of Viewpoints on Alliances

Executive Summary

Strategic alliances are sweeping through nearly every industry and are becoming an essential driver of superior growth. Within five years, the value of alliances is projected to range between $30 trillion to $50 trillion. Peter F. Drucker has said that there is not just a surge in alliances but “a worldwide restructuring” is occurring in the shape of alliances and partnerships.

Recent surveys by Booz•Allen have revealed:

- More than 20% of the revenue generated from the top 2,000 U.S. and European companies now comes from alliances, with more predicted in the near future.
- These same companies earn higher ROIs and ROEs on their alliances than from their core businesses.
- Leading edge alliance companies are creating a string of interconnected relationships which allows them to overpower the competition.
- The traditional “command and control” organizational model is inadequate to manage the complex set of relationships forming outside the direct control of the corporation.

Why is a new organizational model called for? What does it look like? How does it work? How does it differ from the traditional “command and control” organizational model, which has worked so well up to now?

This *Viewpoint* addresses these questions, and covers:

- The Five Driving Forces Behind Alliances
- The Three Alliance Modes
  — Filling Single and Multiple Gap Deficiencies
  — Creating Integrated Products and Services
  — Forming a Breakout Offering
- Four “Pure Tone” Alliance Models
  — Franchise Model: *Deep Bench Strength*
  — Portfolio Model: *Hub and Spoke*
  — Cooperative Model: *Mutual Benefit*
  — Constellation Model: *Integrated Service Offering*

The Alliance Enterprise: Breakout Strategy for the New Millennium

A Viewpoint by:

John R. Harbison
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David Moloney

Nineteen ninety-eight in Monaco. The magnified image of Bill Gates beams from a giant screen in front of 200 executives of elite technology firms in Europe during a live video conference. This leader of the most successful business start-up of the past century makes a startling admission: "Microsoft can't make it alone, but together anything is possible."

Indeed alliances have become an essential element of every successful business. They bring higher growth, higher profitability and higher market valuations. Global companies with successful alliances get more than 20% of their revenues from alliances today, and they expect that percentage to increase to 35% by 2004; the leading European companies are already averaging almost 30%. Alliance-intensive companies earn 70% higher return on equity and they are more likely to see higher market valuations. Alliance announcements routinely cause surges in the stock of both partners.

Alliances are becoming pervasive in the very fabric of how business is conducted, and companies such as Hewlett-Packard and Oracle are deciding that the ability to form successful alliances is in itself a core competency to be nurtured and developed. But something is missing. Corporations have evolved portfolios of alliances, but too often they are managed discretely, not as an extended enterprise. Yet the fundamental truth is that **the predominant "command and control" organizational model that we have known for the past century is inadequate to manage the complex set of relationships where over 50% of the activity of a company occurs outside the company.** To unleash the power of this portfolio of relationships, a new model is needed — *The Allianced Enterprise*.

What is this? How will it work? This *Viewpoint* will begin to lay out our blueprint for addressing the challenge of *The Allianced Enterprise,* and how you can apply the concept to your company.

Background

As recently as only two decades ago, competition was simpler and companies did not need to excel in all capabilities or participate across the globe — one differential capability serving one major market region was often enough. The pace of change in technologies and markets was modest compared with today's activity, and industry boundaries were well-defined and generally not global. If you lacked a capability, you either took the time to develop it or you bought it through an acquisition.

Shareholders were (relatively) patient and less demanding about profitability and returns. The hottest ideas of the day for strategic thinkers and planners were market segmentation, application of portfolio models (to categorize the companies' different businesses and determine resource allocation) and competitive strategies. The "command and control" model which had evolved over the last two centuries was still working successfully.

But there were some dissonant voices saying that things were not what they seemed to be. Individuals such as Gary Hamel (London Business School), Barry Nalebuff (Yale) and Adam Brandenburger (Harvard) noticed a pattern emerging where companies were voluntarily deciding to cooperate. This cooperation spawned a new type of business entity — a less discrete enterprise with clusters of common activities in the midst of a network of relationships. The goal of this network was to share knowledge and core capabilities in order to rapidly increase the value to customers.

These embryonic networks led others such as Michael Hammer (MIT) and Sumantra Ghoshal (London Business School) to predict that the traditional concept of management and control was at the end of its life cycle. And Ben Gomes-Casseres (Brandeis) coined the phrase "constellations" to describe this new era. Bruce Pasternack and Albert Viscio at Booz·Allen studied this emerging trend and came to the conclusion that we are moving toward a "Centerless Corporation" where competitive strength will be based more on harnessing capabilities, knowledge and the power of people in ways previously unknown (for more details see their book *The Centerless Corporation)*.

We are now in the early phases of a new era where cooperative business models will become dominant forces in the world economy.

The Allianced Enterprise as an Alternative Growth Engine

Many companies are extending their enterprises beyond internal boundaries by teaming with other companies. These relationships run from conventional transactional sourcing and servicing arrangements at one extreme to acquisitions and mergers at the other. In the middle of the spectrum are what we call strategic alliances.

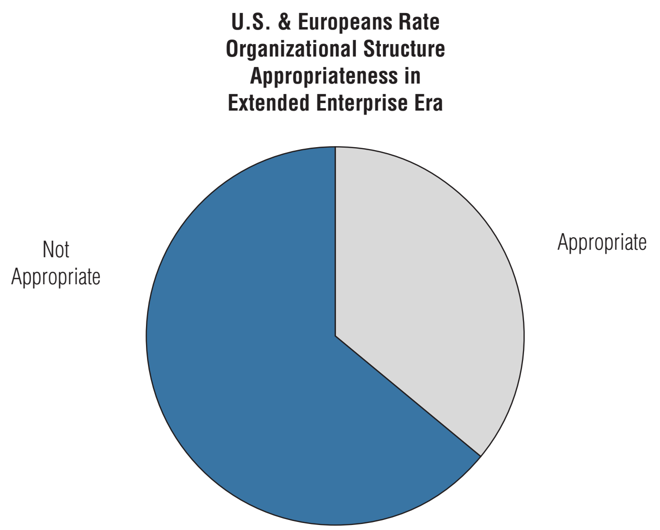
We have been studying strategic alliances for 15 years. These alliances are not transactional (arm's length) in nature but are entities where partners are willing to act in unison and share core capabilities. Let us share with you the results of our most recent survey of senior executives in the top U.S. and European firms:

- In the past two years, more than 20,000 alliances have been formed worldwide, and more than half occurred between competitors. All our participants said that alliances are increasing within their industry, with over 75% noting that alliances are effective. Acquisitions and mergers over the same period have also remained strong, with over 15,000 completed; however, a success rate of less than 50% is acknowledged.
- The percentage of revenue that the top 1,000 U.S. companies have earned from strategic alliances is now 18% (vs. Europe at almost 30%). By 2004, these same companies expect over 30% (U.S.) and nearly 40% (Europe) of their revenue to come from alliances.
- The top two reasons stated for forming alliances are (1) to accelerate the growth trajectory (75% of survey); and, (2) to gain access to external core capabilities (67%).
- For the past ten years, strategic alliances have consistently produced a return on investment of nearly 17% among the top 2,000 companies in the world. This is 50% more than the average return on investment that companies produced overall. And the 25 *Fortune* 500 companies most active in alliances earn an average return on equity of 17.2% compared to 10.1% for the 25 least active.

With over 20% of today's revenue coming from strategic alliances and with more predicted in the near future, is the current "command and control" model appropriate for managing in the Allianced Enterprise Era?

When we asked this question, nearly two-thirds of our respondents said, "No!" (see Exhibit 1).

Exhibit 1. Today's Organization Model Is Flawed



Source: 1999 BA&H survey of over 200 U.S. and European firms

If these battle-tested alliance executives believe their current business model is not appropriate, then what will work? Where are we headed? To start, let's look at the forces driving this explosion in alliances.

Dynamic Forces Driving Strategic Alliances

Environmental: There are certain environmental conditions that favor the formation of alliances and explain the increased cooperation in the last decade:

1) Competitive boundaries have blurred as technology advances have created crossover opportunities merging formerly distinct industries

2) Advances in communications (voicemail, e-mail and e-Business) and the trend toward global markets link formerly disparate products, markets and geographical regions, and facilitate the open communication essential between partners

3) Intensifying competition and increasingly demanding customers require advantaged capabilities across the board, and no company has the time or resources to either develop these themselves or acquire them

4) The insatiable drive for technology standards and compatibility in a globally linked world necessitates cooperation

5) Growing number of companies have successfully scaled the alliance learning curve and a global body of expertise to ensure successful alliance formulation and execution

Let's examine some of the facts behind these influences:

- **Defending the Ramparts "Retrenchment to the Core"—** Our studies reveal that in 1985 only 26% of the revenue of top U.S. companies was coming from their core businesses. Diversification was still the standard of the day. By 1998, all this had changed. Today we find that the core generates over 60% (U.S.) and 67% (Europe) of these companies' revenue. It is critical to effectively identify, protect and enhance one's core without giving up the key elements of the value chain where one's core is not positioned. As competition intensifies, alliances fill in capability gaps to protect the core business.
- **"Nowhere to Hide—Global Reach"—** Fifteen years ago U.S. companies produced only 14% of their revenue overseas. Most U.S. companies saw competition confined to U.S. borders. However, today 35% of U.S. revenue (and 45% of European revenue) comes from international sales — making all firms vulnerable to threats from global players, especially from experienced cooperative international partners.
- **"Holding the High Ground —Turbocharging the Development Engine"—** R&D took a back seat in the early 1980s with only about 2% of revenue spent

Exhibit 2. Growth Drives Performance

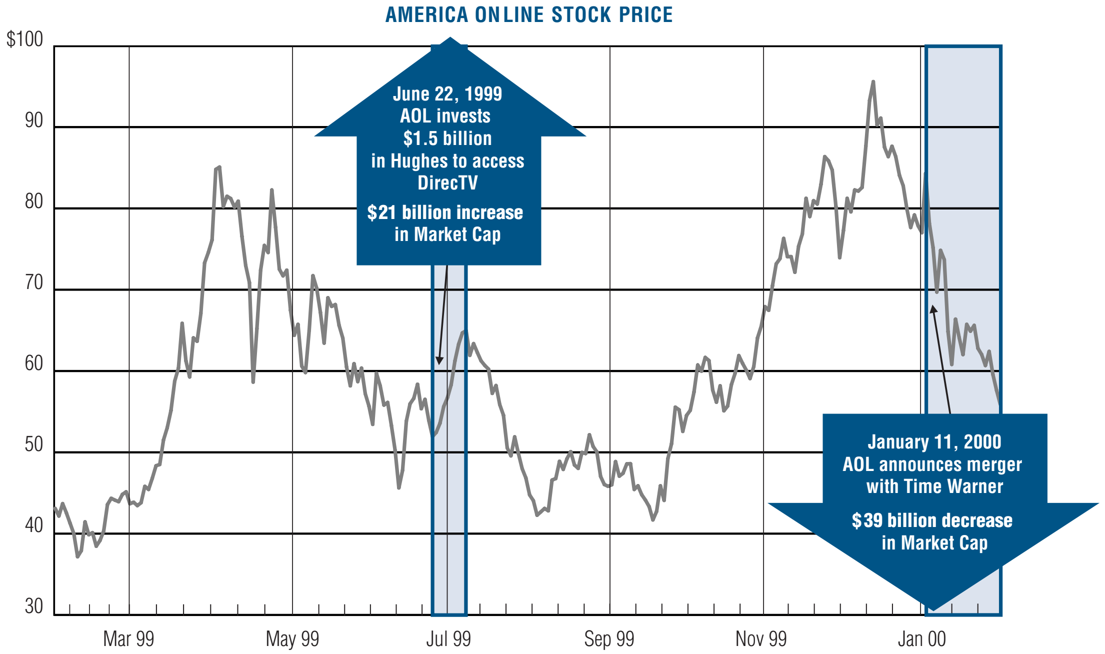
Financial Performance 1985 –1994

	ANNUAL RATES OF GROWTH			TEN-YEAR CUMULATIVE GROWTH		
	Shareholder Returns*	Earnings	Revenue	Shareholder Returns	Earnings	Revenue
90th Percentile	23.7%	25.9%	21.1%	841%	997%	678%
80th Percentile	19.1%	17.8%	13.3%	573%	516%	347%
50th Percentile	12.7%	9.6%	8.5%	331%	251%	226%

** Shareholder returns reflected stock price appreciation plus dividend reinvestment, adjusting for stock split.*

Source: Booz•Allen & Hamilton

Exhibit 3. AOL Stock Rises on Alliance News, but Falls on Merger News



Source: Booz•Allen & Hamilton

on R&D. By 1995 a dramatic change had occurred with nearly 6% of revenue allocated to R&D in the U.S. and Europe. We believe that this change was directly related to the increased importance of new product development to enhance competitive position. Since 1990, our surveys show that new products have accounted for a steady stream of over 20% of revenue every two years. Accommodating such rapid innovation has put pressure on management to act faster and smarter with fewer resources—hence the move toward alliances.

- **"Thriving Under the Watchful Eyes of Wall Street"—** Recent studies at Booz•Allen reveal the link between growth and market capitalization. Exhibit 2 illustrates what high performers achieve. Clearly they generate growth, but that growth also translates into high shareholder returns and earnings. It is not surprising that these companies have much higher PEs and market caps than their competitors or the market in general.

You are probably thinking, okay, but where do alliances fit? The majority of these top performers are some of the leading alliance companies and they experience significantly higher alliance ROIs than on their core business, gain a higher percentage of revenue from alliances and earn 70% more return on shareholder's equity than their lesser allianced competitors.

Research by Bharat Anand (Yale School of Organization and Management) and Tarun Khanna (Harvard Business School) shows that alliances outperform mergers in terms of stock market value creation. Consider the specific example of America Online in Exhibit 3. In June 1999 AOL announced a major alliance with DirecTV to provide broadband access to AOL customers, and in the ensuing weeks the market value of AOL increased by $21 billion. In contrast, when they announced their proposed merger with Time Warner in January 2000, their market cap dropped $39 billion. Alliances tend to raise both partner's market value, while acquisitions tend to raise the market cap of the acquiree and lower that of the acquirer.

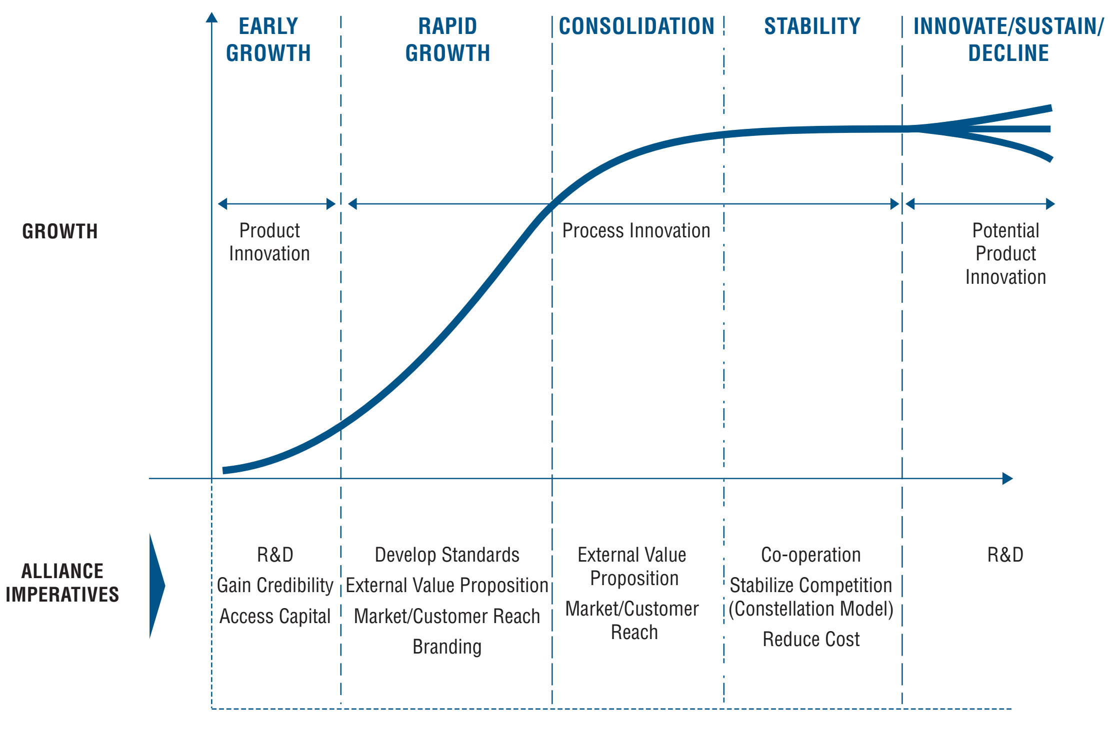
The Business Life Cycle

In the 1950's, Booz·Allen introduced the concept of the Product Life Cycle in a landmark *Harvard Business Review* article. Business life cycle phase is a key driver of alliance imperatives and suggests at least five growth engine trigger points. Exhibit 4 illustrates alliance imperatives at each life cycle phase.

In the early growth stage, product innovation and credibility are the key drivers of alliance initiatives. In the rapid growth phase, the development of standards and market reach are most important. The drivers change again in the stability phase where reduced cost, product extension and value chain strengthening are important. Organizations are increasingly embracing alliance-enabled opportunities to close these strategic gaps.

Take Microsoft as an example. From its market capitalization of $0.6 billion at the time of its IPO in 1986, the company has grown to over $500 billion in market capitalization. But many people don't understand the critical role that alliances have played in this evolution. Microsoft's first breakthrough was an alliance

Exhibit 4. Business Life Cycle Phases Influence Alliance Imperatives



Source: Booz·Allen & Hamilton

with IBM to develop DOS. It followed this alliance with its second breakthrough, the emerging dominance in operating systems through Windows and its "Wintel" alliance with Intel. The pace has never slackened. In the past two years, the company announced on average two alliances per day. Microsoft's investments in these partnerships have paid huge dividends; for example, their equity investment in Apple has risen over 800% in just two years.

Business life cycle phase is the key driver of alliance strategy imperatives. Once the linkage between these imperatives and the corporate and business strategies and objectives is clear, the next step is determining where alliances can be effective in meeting these objectives and strategies. Processes for identifying alliance opportunities encompass traditional industry analysis, brainstorming and a new breed of opportunity identifying tools we call "Forcing Techniques." Exhibit 5 illustrates a forcing technique designed to identify alliance opportunities for a retail funds manager looking to grow distribution.

Exhibit 5. Forcing Techniques to Surface Alliance Options—Example

EXAMPLES

LIFE CYCLE EVENT ANALYSIS — INDIVIDUAL INVESTMENT LIFE CYCLE

	Acquire Funds to Invest	Identify Investment Needs	Investigate Available Products	Effect Transaction	Monitor Investment Performance	Manage Tax	Sell Investment
POTENTIAL PARTNERS FOR A RETAIL FUNDS MANAGER	• Financial institutions without investment offering (e.g., credit unions, small banks) • Employers • Professional associations/ affinity groups • Real estate agents • HR consultants	• Accountants • Independent financial advisers • Investment magazines • Investment clubs • Financial planning software • Financial planning Internet sites	• Independent financial advisers • Investment magazines • Investment clubs • Investment Internet sites	• Stockbrokers • Credit unions/small banks • Financial management software (e.g., Quicken, MS Money) • Utilities • Credit card companies	• Investment magazines/ finance papers • Financial management software (e.g., Quicken, MS Money) • Investment tracking Internet sites	• Accountants • Tax return preparation agents	• Independent financial advisers • Stockbrokers

Source: Booz•Allen & Hamilton

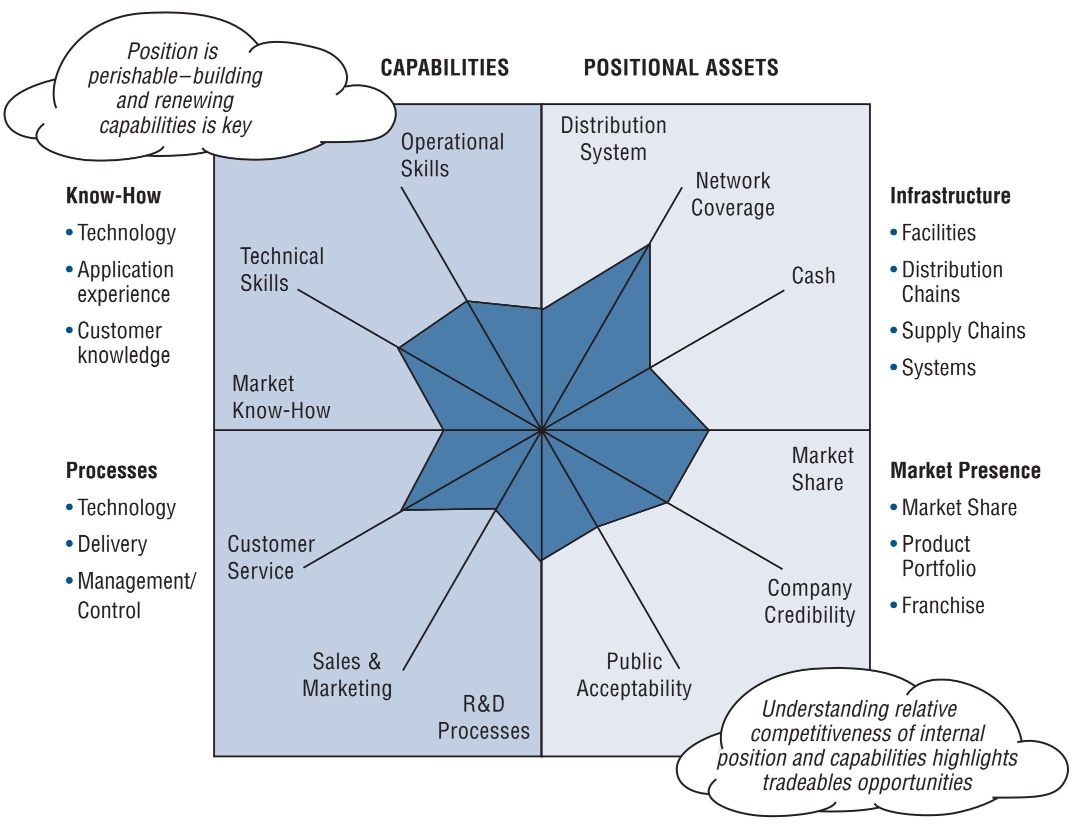
Alliance Modes: The Search for Advantaged Capabilities

Many companies see alliances only as a discrete activity—filling in a hole, here or there, primarily where one cannot purchase a capability or build it oneself. They miss the real power of this new tool to become a superior growth engine. Real alliance power comes not from discrete alliances, but from using a group of alliances in a concentrated manner, i.e., creating a string or class of interconnected alliances to rapidly overpower the competition.

In today's dynamic environment, successful companies need to select, build and deploy critical capabilities, which will enable them to gain competitive advantage, enhance customer value and drive their markets. The emphasis should be on future differentiators, not historical ones. The competitive focus must switch from "how to compete better with current capabilities" to "how to select and build better future capabilities, especially those emerging capabilities that will drive the market" (see Exhibit 6).

Competition is no longer for position itself, but for change in position. Positional assets such as facilities, market share and brand franchise are transitory, while capabilities are not. The goal is to focus on the capabilities which the company can use

Exhibit 6. Capabilities and Position Asset Analysis



Source: Booz•Allen & Hamilton

to constantly renew and extend its position. We find alliances are being used in the following ways. (We will later discuss how these modes can be grouped into *classes of interconnected alliances*, thus leveraging a vast array of capabilities to increase value to the consumer and to overwhelm the competition.)

1) Filling Single and Multiple Gap Deficiencies: Capabilities are know-how leveraged by cost-effective, responsive business processes and systems for innovation and delivery of enhanced customer value. Capabilities are intrinsically cross-functional; they are based on horizontally organized teams working according to well-designed, pre-engineered processes and empowered by policy to make decisions within an established framework of rules.

Competitive advantage in capabilities comes from precision tailoring and sharp focus — no company can afford to build advantaged capabilities against all aspects of the value-added stream.

Alliances are an excellent solution for filling critical gaps where the company lacks the resources and/or time to build its own capability to world-class levels. Alliances also should not be viewed as static events. The strategy linkage is particularly important when thinking about the changing "know-how" needs and emerging critical processes that will impact the company in the future. At a minimum, alliances should be seen as a way to fill key single or multiple gaps in a company's value-added chain.

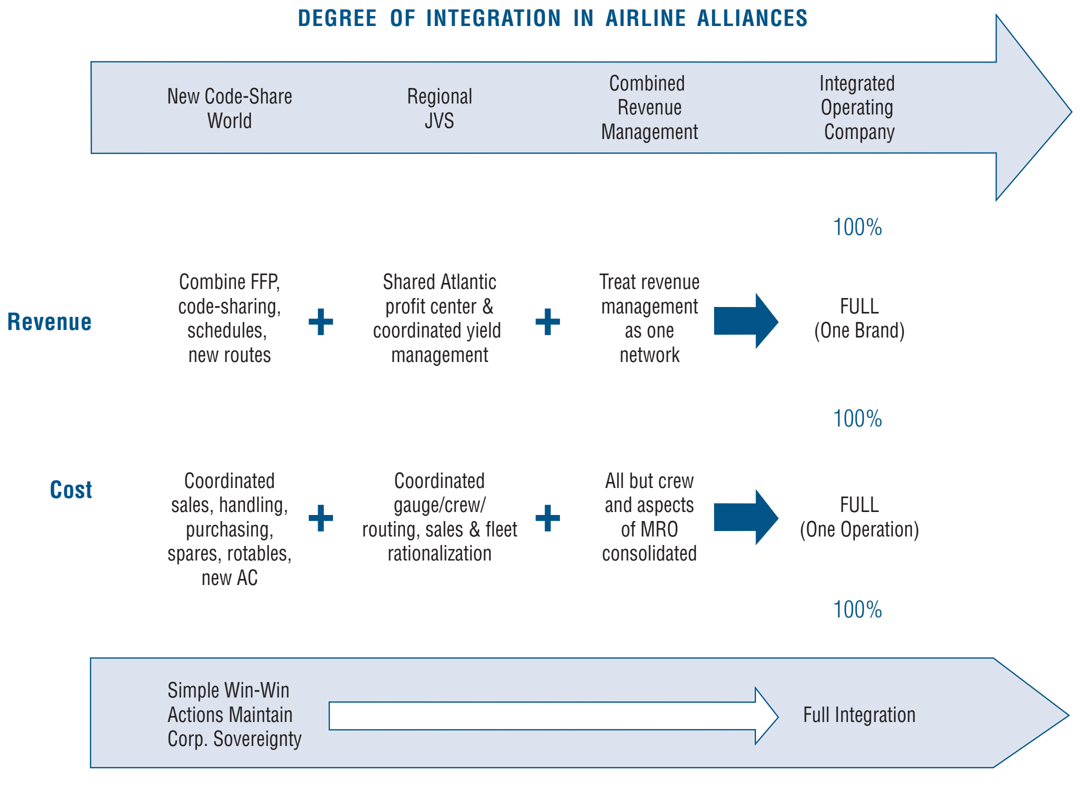
2) Creating Integrated Products and Services: The alliance approach also can be used to build integrated products or services. A team of partners can significantly raise the competitive bar whereby a single competitor will be outflanked or be forced to respond and thus place a severe strain on its internal resources.

Global airline alliances are perhaps the most obvious example of initiatives to provide an integrated product or service offering (see Exhibit 7). Member airlines coordinate schedules for rapid, more hassle-free connections; frequent travelers are provided recognition and special services even when far from home; and customers can earn and redeem miles essentially wherever they go. Alliance members have been especially successful at stimulating markets that neither carrier could serve effectively on their own—providing more competitive offerings between medium-sized cities that were not aggressively marketed and sold with the more traditional interline relationships. Member airlines are also rewarded with richer yields, attracting a higher proportion of frequent travelers.

However, significant opportunities remain untapped in the largest (new) alliances. The lack of effective cross-company compensation schemes, lack of antitrust immunity in some instances and a natural reluctance to violate corporate sovereignty may be inhibiting further integration. We expect that the winning alliance(s) will find ways of acting more effectively as one, potentially leveraging regional JVs and other mechanisms to combine revenue management fully, while integrating operations more effectively over time. The group that is most successful with these initiatives will not only further stimulate travel, but will gain share of high-yield traffic over time at the expense of other groupings.

Beyond this, airlines are developing additional alliances and relationships in related businesses such as maintenance, and

Exhibit 7. The Future of Global Airline Alliances



Source: Booz•Allen & Hamilton

the airlines are beginning to explore potential "breakout" strategies by leveraging their key capabilities and market positions in the e-commerce and loyalty management businesses.

3) Forming a Breakout Offering: Some companies are using alliances to develop a breakout strategy to leap over the competition and grab the high ground before the competition can react. Consider Exhibit 8 which shows how a constellation has been developed in the Excite@Home cable broadband Internet access market.

Since its founding in 1995, @Home has reached affiliate agreements with 23 leading cable companies worldwide. Their goal has been to create a broadband alternative to AOL (America Online) by marrying a leading graphics-intensive portal/search engine (Excite) to @Home's exclusive distribution arrangement with the cable TV companies. The service offering to customers is integrated (e.g., Cox@home, Comcast@home, etc.), and the customer is probably not aware that there are multiple companies behind the service offering.

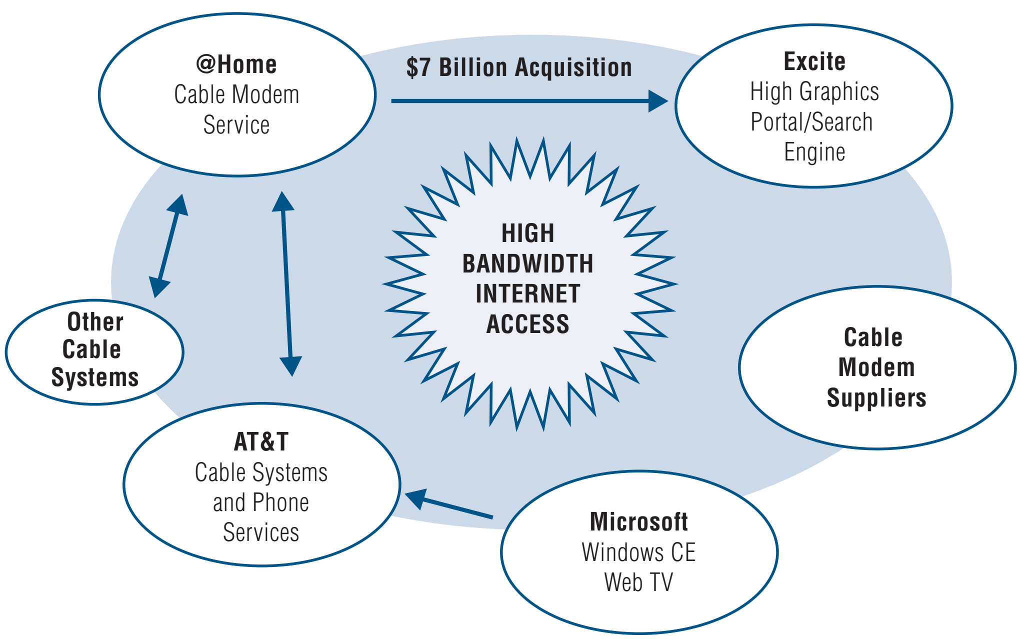
In the breakout offering, successful partners select, build and deploy critical capabilities, which will enable them to gain competitive advantage, enhance customer value and drive their markets, thus putting their competitors on the defensive.

Controlling the Battlefield—Emergence of Alliance Models

"The Command and Control Model of Organization Is Dead. Long Live the Allianced Enterprise!"

The exploding number and scope of alliances is creating challenges for executives trying to manage this complex activity—which is increasingly outside the direct control of the corporation. Companies are forming vast arrays of alliances that on the surface seem to be a collection of unconnected arrangements.

Exhibit 8. Excite@Home Cable Modems "Constellation"



Source: Booz•Allen & Hamilton

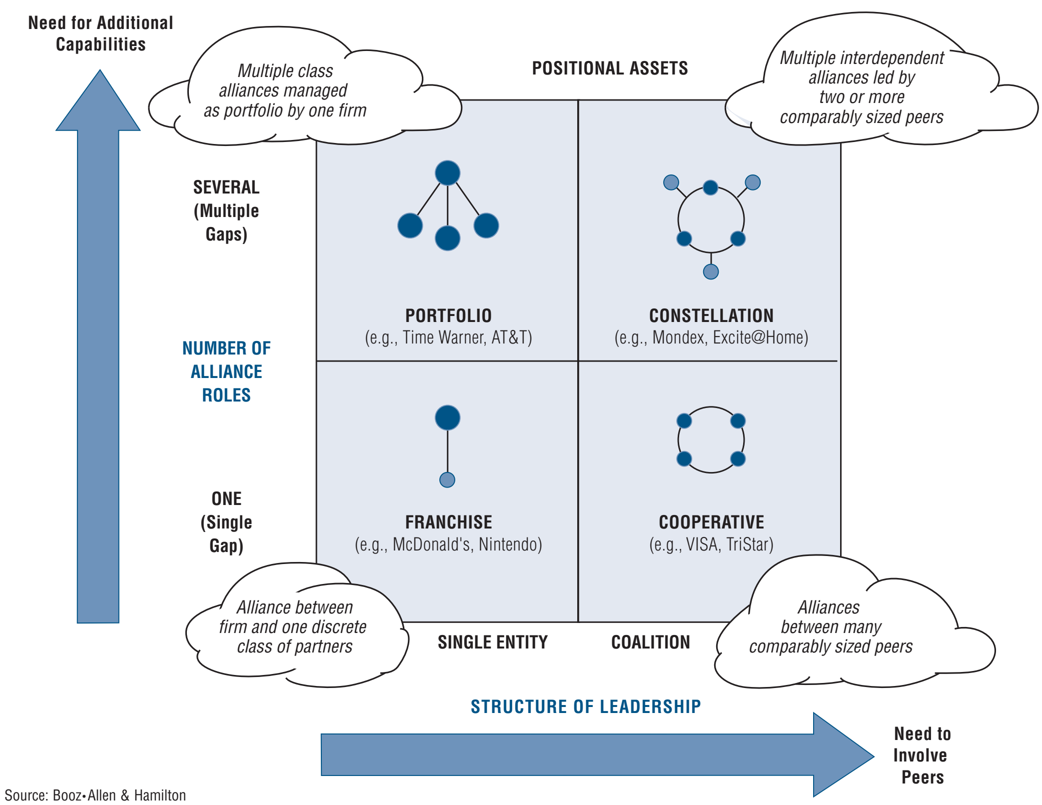
However, these alliances are increasingly becoming an inter-related tapestry of activities, linked in ways to gain competitive advantage and control the battlefield, rather than a series of discrete transactions. The need to adapt the organizational model is compelling.

Leading-edge companies are beginning to use alliance architecture models that are defined in terms of the role strategic alliances can play and their leadership structure. The key issue is how should these alliances be governed, controlled and managed? Consider this: many of these alliances could dwarf the size of any one partner. Yet today, many of these highly dynamic and competitively strong entities have no definable business model of their own.

These models cannot use a "command and control" business model to span multiple partners. Rather, they require something more flexible and dynamic to reflect the market environment and the partnership structure. We see four models emerging for companies with multiple alliances: franchise, portfolio, cooperative and constellation, and each of these "pure tones" will have a different set of implications in terms of the appropriate governance model.

These pure tone models are shown in Exhibit 9, and described on the following pages.

Exhibit 9. Alliance Architecture Models



Source: Booz•Allen & Hamilton

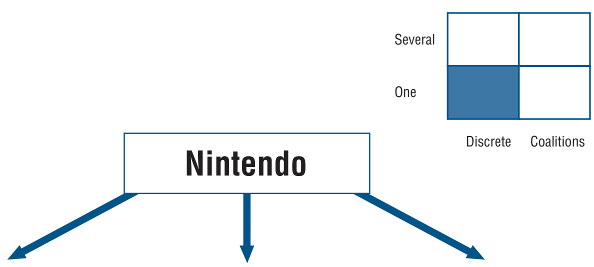
Franchise Model: Deep Bench Strength — This model is used by companies to fill a single critical gap in its value chain. But the needs in that gap area are greater than any one partner can fill. So the company develops a replicable alliance model for a class of partnerships.

For example, Nintendo is using this franchise model to fill in a key capability need — the development of games for its consoles. Nintendo is positioned in the center, closely controlling the activities of its alliance partners (see Exhibit 10). The franchise model develops a single alliance role that can be refined and quickly replicated to create scale, thereby producing an alliance growth corridor for the alliance initiator. This alliance architecture is a significant part of the business model of e-Business companies that use the franchise architecture to develop and manage referral affiliates (e.g., Next Card), content partners (AOL) or distribution partners (FirstUSA).

Portfolio Model: Hub and Spoke — The portfolio model is a major step up from the franchise approach. Companies that adopt this approach are finding that the value-added chain contains far too many elements for it to command all the capabilities necessary to compete. However, instead of forming a number of single discrete arrangements to fill each gap (thus making itself vulnerable should a partner experience difficulty or if the market changes rapidly), the company decides to create multiple class alliances managed as a portfolio. These companies are still in the center, but they are weaving together a portfolio of distinct and often unrelated partnerships. The external partners have little relationship to each other, but interact only with the company at the center.

For example, Time Warner is trying to cover multiple gaps in the key elements of the value chain — including content, applications, distribution, software and service (see Exhibit 11). In each of these areas, it has formed alliances with a variety of partners, although generally a similar class of companies. It manages these classes as a portfolio, thus directing the arrangements to meet its strategic needs. Although Time Warner acts in consort with its portfolio partners, it never loses its sense of direction or co-ops its control of its future. By adopting the portfolio approach, it can move

Exhibit 10. Franchise Model — Nintendo



Acclaim Entertainment Inc./LJN Toys Ltd.
Accolade, Inc.
Activision, Inc.
Advanced Gravis
Advanced Productions, Inc.
American Sammy Corp.
American Softworks Corp.
American Technos, Inc.
Ascii Entertainment Inc./Nexoft
Atlus Software, Inc.
Bandai America, Inc./Shinsei
BMG Entertainment
Capcom
Disney Interactive
Eidos Ineractive
Electro Brain Corp.
Electronic Arts/EA Sports
Fox Interactive
Gametek, Inc./Cybersoft, Inc.
GT Interactive Software
GTE Interactive Media
Hot-B USA Inc.

I Motion
IMN
Interact Accessories Inc.
Interplay Productions
Jaleco USA, Inc.
JVC Musical Industries, Inc.
Kemco of America, Inc.
Koei Corporation
Konami Inc./Ultra Soft
Laral Group
Left Field Entertainment
Life Fitness
Light Wave Technologies
Majesco Sales, Inc.
Microprose Software, Inc.
Midway Home Entertainment
Milton Bradley
Mindscape/Software Toolworks
Namco Hometek, Inc.
Natsume Inc.
Nuby/Curtis
Ocean of America, Inc.
Parker Brothers
Philips Media

Playmates Interactive Ent.
Psygnosis, Limited
Rare Ltd.
Raya Systems, Inc.
Seta USA, Inc.
Sharp Electronics Corp.
Sports Sciences, Inc.
Sun Corporation of America (Sunsoft)
Take-Two Interactive Software, Inc.
TecMagik, Inc.
Tecmo Inc.
T*HQ/Malibu Games/Black Pearl Software
Titus Software Corp.
Toho Co., Ltd.
Tyco
Ubi Soft Inc.
Viacom New Media
Vic Tokai Inc.
Video System
Virgin Interactive Entertainment, Inc.

Source: Booz•Allen & Hamilton

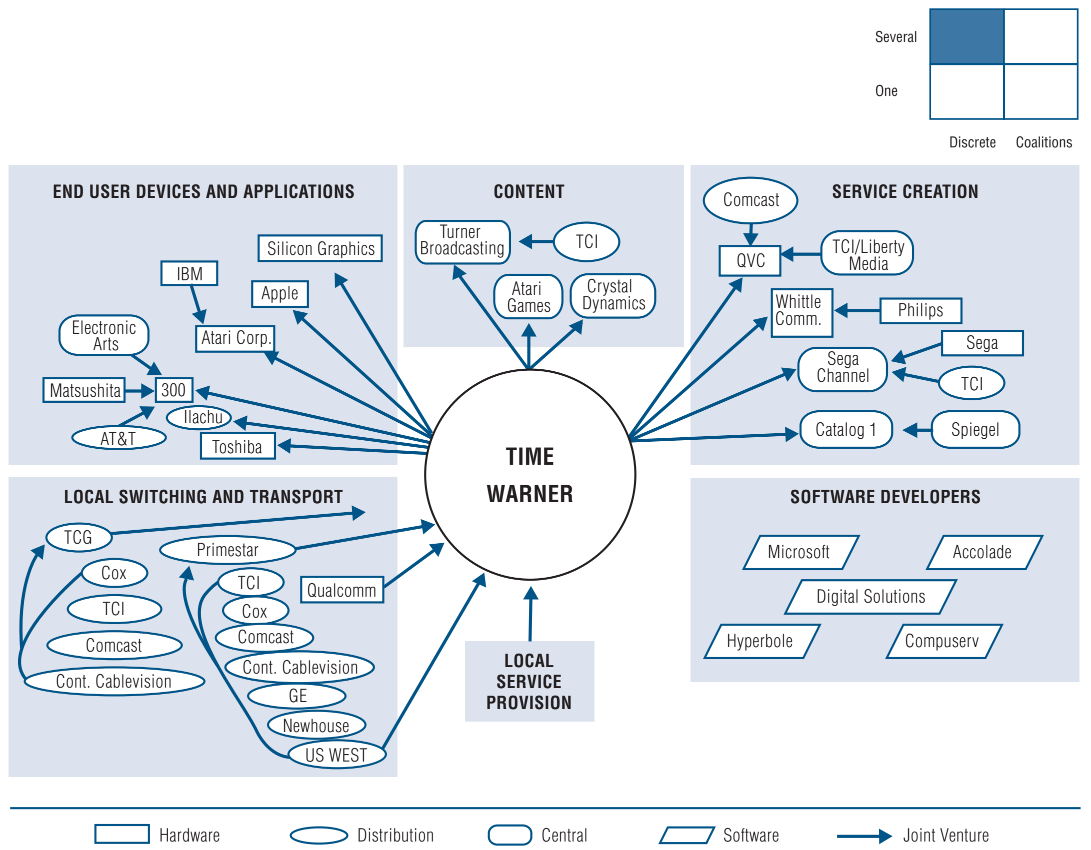
quickly within a class, adjusting its position or its partners.

The biggest advantage to the franchise and portfolio models is that the forming company sits in the control position directing and managing the interconnectedness of the arrangements. In the portfolio model, the forming company acts as the "corporate core." Through its actions it formulates strategic leadership and capability building. It manages this process by forming and dissolving its alliances as its primary control mechanism. The more dominant the position of the forming partner, the easier it is to implement this model.

Cooperative Model: Mutual Benefit — With the cooperative model, one moves from a central position to more of a cooperative role. The alliance is at the center, rather than one of the partners, and the customer relationship often shifts from the company to the alliance. Typically, we find that companies that have adopted the cooperative model do so to outflank the competition and substantially raise the competitive bar. The most distinguishing feature of the cooperative model is that no one company is in control — all work together to raise the competitive bar.

Consider TriStar, the cooperative effort between CBS, Columbia Pictures and HBO. These partners formed a film company and motion picture studio with an initial investment of $300 million in the 1980s. Through TriStar, HBO gained access to an additional source of feature films. CBS obtained a toehold in cable TV services and

Exhibit 11. Portfolio Model — Time Warner



Source: Booz•Allen & Hamilton

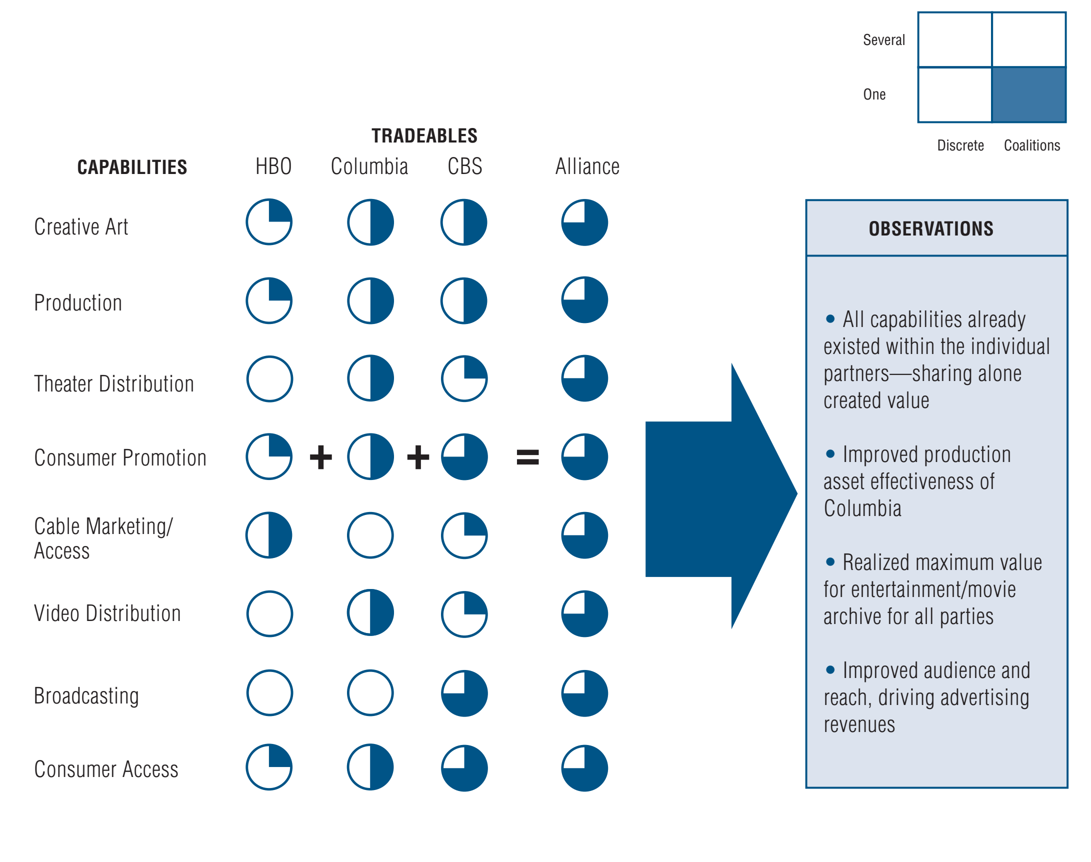
gained a source of feature films for commercial broadcasting. Columbia Pictures gained access to new distribution channels and extra studio capacity when space was scarce (see Exhibit 12).

Although TriStar operated separately from its parents, it did not have its own distribution system. Its parents distributed TriStar's films through their respective distribution systems, thus raising the effectiveness and productivity of the partners. TriStar's movies were made, sold and distributed through TV, cable and theaters in a much more seamless way, and it helped establish cable and made HBO the dominant force in the paid cable area.

The cooperative model requires a different business model. While the relative size of the partners may differ, they are equals at the point of intersection (the specific product or service provided to the marketplace). All companies are working toward the same goal; however the day-to-day running is not under direct control of any one partner.

Constellation Model: Integrated Service Offering — Companies that utilize constellations develop breakout strategies that leapfrog the competition and put industry competitors on the defensive.

Exhibit 12. Cooperative Model — TriStar



Source: Booz•Allen & Hamilton

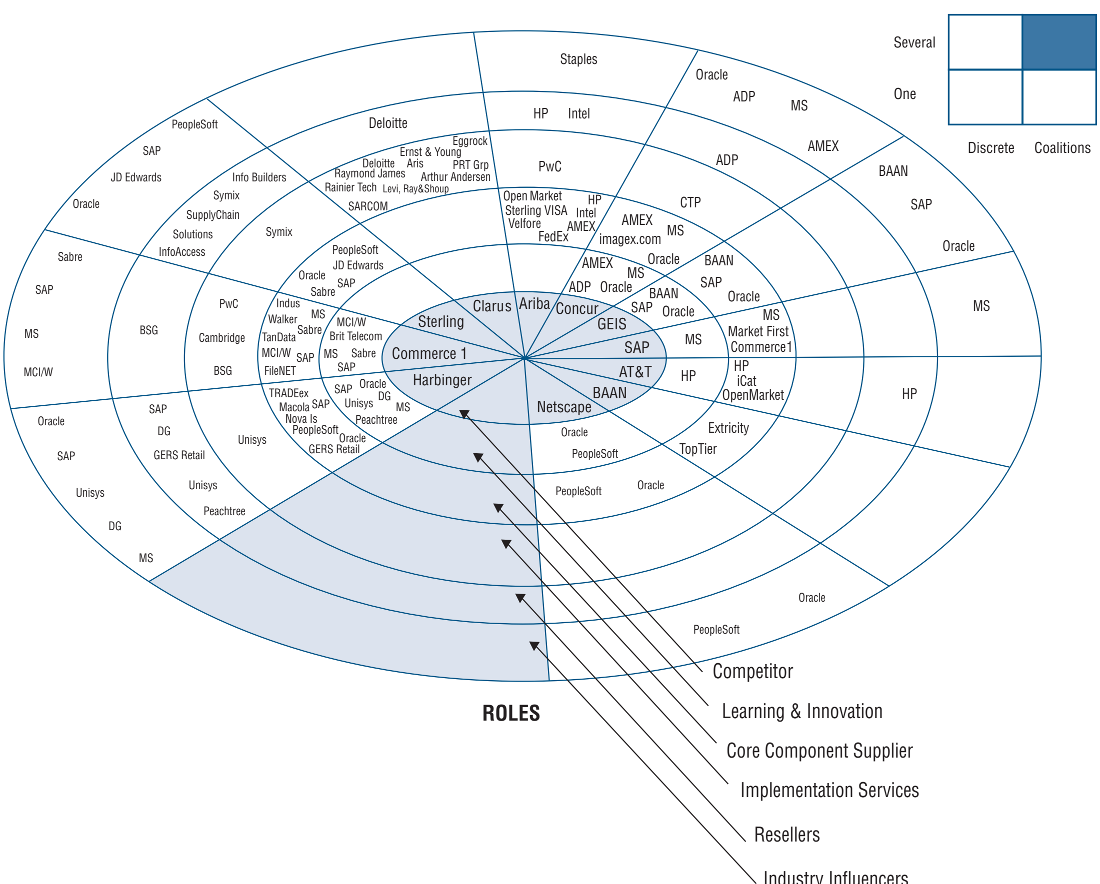
E-Procurement is a good example of an industry with emerging alliance constellations. Entering this industry requires a very substantial set of partners playing multiple alliance roles (portfolio model). However, requirements for global scale, standardization and substantial capital injections are forcing early players to share leadership and equity with selected partners through migration to a constellation model (see Exhibit 13). These constellations will mature as constellation partners discover new ways to work together to change the rules of the game.

These constellations are initially comprised of a set of equity joint ventures and should naturally evolve into independent companies. They will have all the "organization" required and be self-contained. They will be governed through board processes and create their own identity in the marketplace.

Managing Alliance Models: Art of Virtual Coherence

Each alliance model has a different set of characteristics, governance issues and strategic focus (see Exhibit 14), and this is one key reason that a new organizational model is necessary. Trying to manage these models under the old "command and control" structure inhibits the formation and management of these models. It has been our experience that companies which form and manage

Exhibit 13. E-Procurement Alliance Portfolios — Ripe for Evolution to Constellations



Source: Booz•Allen & Hamilton

Exhibit 14. Each "Pure Tone" Alliance Class Has a Unique Set of Characteristics

	Governance	Integrated Offerings	Industry Focus
Franchise	**Easiest** *(Operationally Managed)*	**Little** *(Fill Single Gap)*	**Single** *(Concentrate on Current Customer/Market Segments)*
Portfolio	**Easier – Internal** *(Oversight Committee Crosses Various Areas)*	**Little** *(Multiple Gap Focus)*	**Single** *(Concentrate on Current Customer/Market Segments)*
Cooperative	**Intricate – External** *(Shared Leadership Shared Governance)*	**High** *(Create New Value Proposition Within Industry)*	**Multiple** *(Concentrate on Creating New Value Position to Extend Reach into Customer/Market Segments)*
Constellation	**Difficult – External** *(Shared Governance Crosses Industry Boundaries)*	**High** *(Leapfrogs Current Competitive Structure)*	**Multiple** *(Rapid Expansion into New High Growth and High Value Market Areas Unobtainable Before)*

Source: Booz•Allen & Hamilton

these successfully do not want to team up with companies that have not learned this lesson.

Successful companies in the next decade will be the ones that harness the full potential of the alliance models and tailor their organizational structures to take full advantage of the "pure tone" alliance situation which most appropriately fits their strategic needs. The world will be difficult to navigate and competitors too ingenious as companies are shaken loose from traditional ways of doing business. Companies must develop "coherence" among the many seemingly disparate and far-flung pieces of the business, establish a potent binding force and sense of direction where all the pieces mutually reinforce each other, as well as provide a platform for growth. Coherence is what allows the company to de-emphasize a rigid organizational structure. One of the staggering failures of the old and dysfunctional "command and control" business model is that it "chokes" the potential of the company.

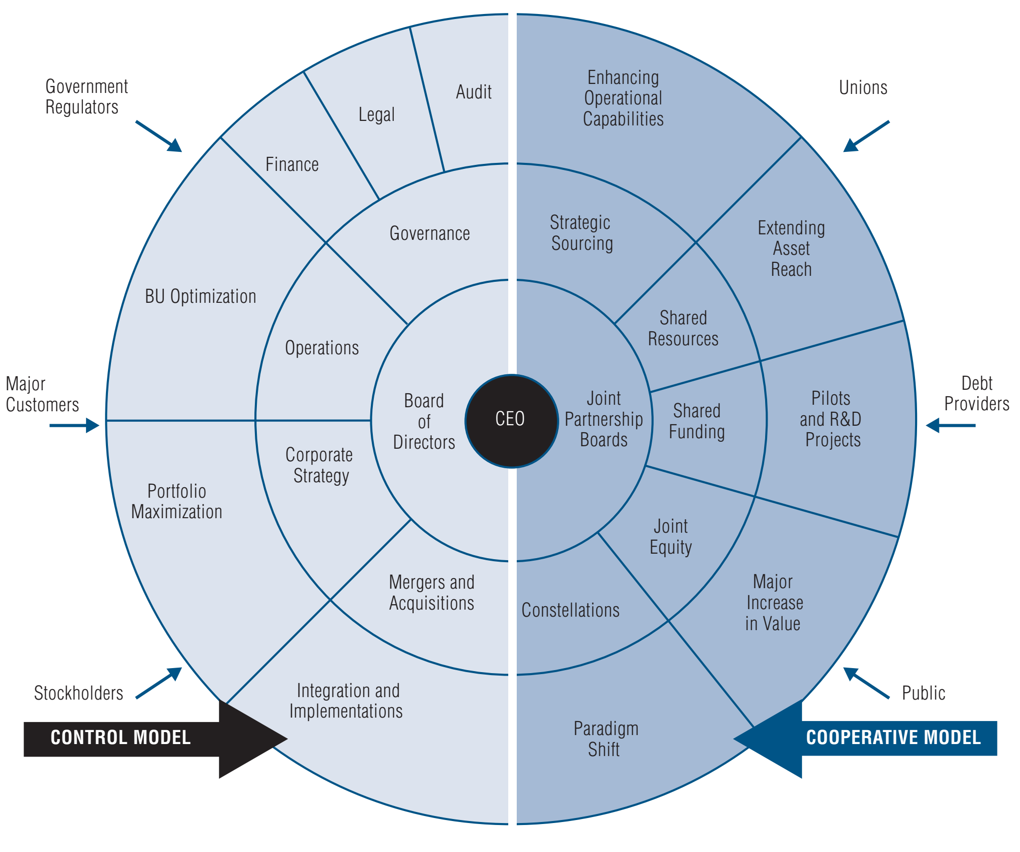
The successful company of tomorrow will develop coherence between the control model and the cooperative model of alliances (see Exhibit 15). So how does one establish coherence in an alliance? How should these alliances interact with the partners? The answers differ by kind of alliance.

Franchise alliances are operational in nature, an extension of a specific part of a company and that's where and how it should be managed.

The *portfolio* model is, de facto, a new business model. Since it usually involves more than one primary part of the dominant partner, it is managed not by an operations group but by a business center. That center acts as the "corporate center" for the alliances. It must treat its partners as a business unit within a Centerless Corporation — adding value only where the businesses cannot (see Exhibit 16). It must focus on knowledge and people and work diligently to build coherence internally and externally.

The *cooperative* model is a shared business model that needs its own leadership, but with few "owners," they need to work through some cooperative governance structure. The challenge with these models is to establish a set of operating/performance parameters. This model is very similar to what firms do when they establish a shared services organization within the corporation, or rely on an outsourcing agreement.

Exhibit 15. Emerging New Business Model Contains Elements of Control and Cooperation



Source: Booz•Allen & Hamilton

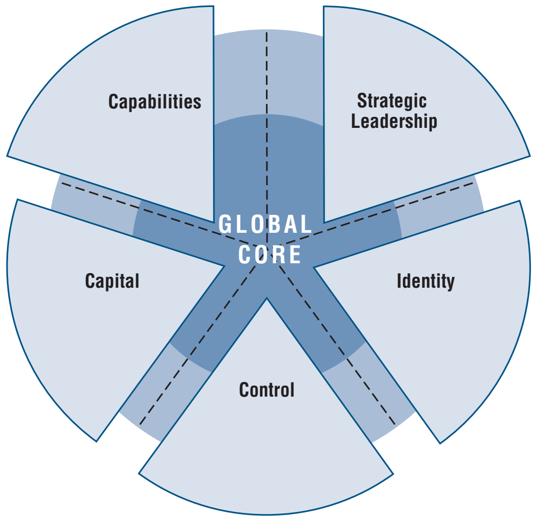
The *constellation* must be thought of as the new company. The constellation requires its own center, one that is focused on creating value for the extended entity. The only areas where a corporate center adds value are in strategic leadership, capability brokering, identity, control and capital. This holds true for a corporation and for a constellation.

The more an alliance must mirror a single business model, the more it must focus on its knowledge creation and dissemination, its people strategy and creating coherence throughout the entity. Without this kind of focus the venture is doomed from the start. This business model will have strong analogies to a single business, but it must cross corporate borders (see Exhibit 17). So while the basic principles hold, their applications will differ. These new models will be the growth engines of the future, and there is great value in being an early adopter.

To a large extent we are entering new territory. As the word spreads and more companies seek alliances as a growth vehicle, the differentiator will shift from being able to form an alliance to being able to manage one. Obviously, those in the game the longest have the most experience. However, the game is evolving and standards have yet to be set.

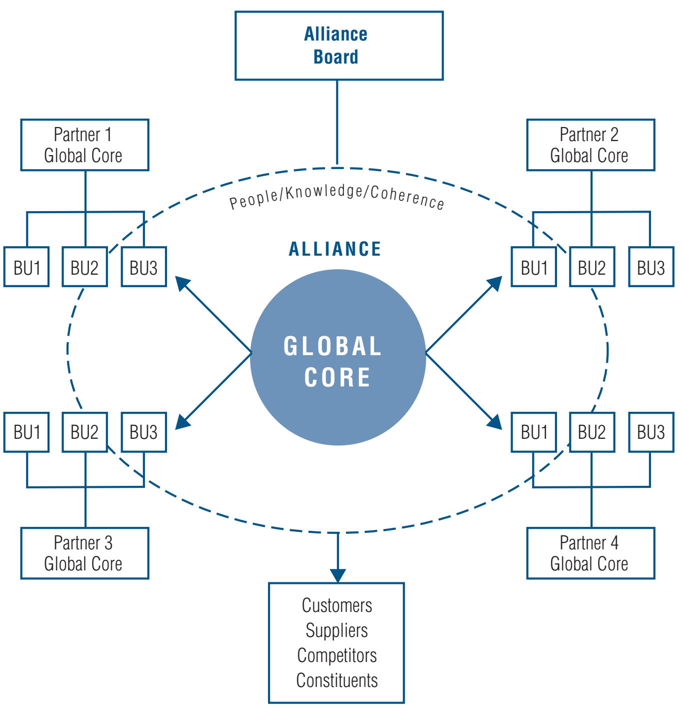
We envision a race to optimize the alliance business model over the next few years. And, as with alliance formation itself, the early adopters will win big.

Exhibit 16. Centerless Corporation Missions



Source: Booz•Allen & Hamilton

Exhibit 17. New Business Model for Alliances



Source: Booz•Allen & Hamilton

Alliances as a Core Competency

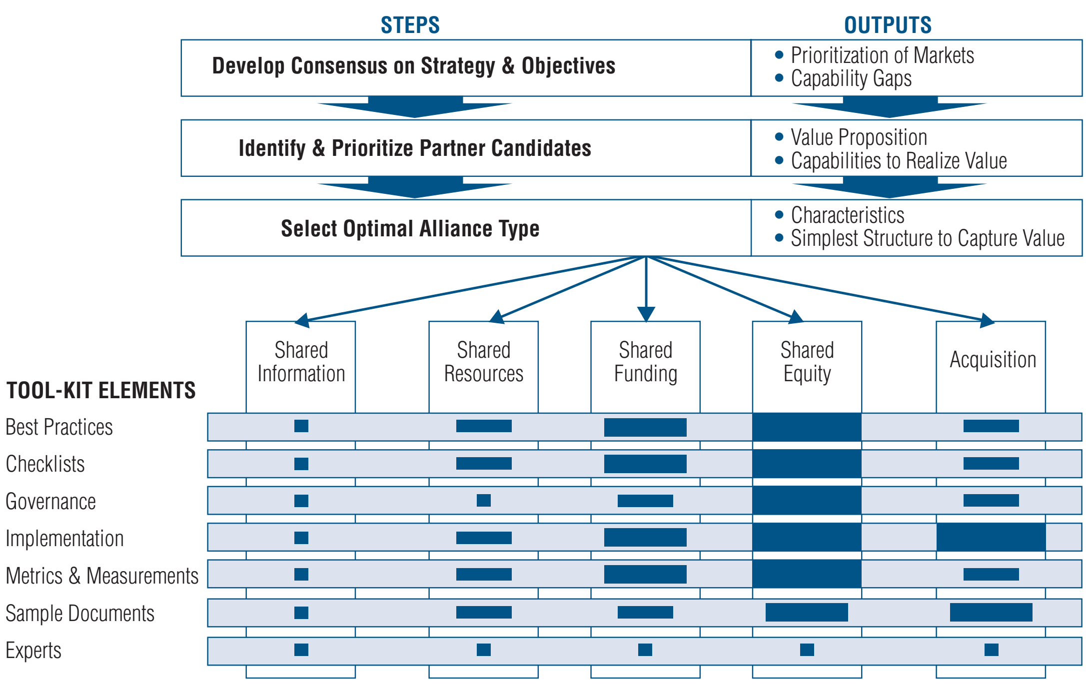
Regardless of which of the four "pure tones" is appropriate for your company, you will no doubt be compelled to form multiple kinds of alliances. You will need to have a disciplined process that helps you decide what type of alliance is optimal in a particular situation, and then adapt the process to the particular type of alliance.

Pragmatic executives are often suspicious, and rightly so, about simple formulas. Some executives even maintain that "seat-of-the-pants" management and pure luck play an important role in any alliance. We agree that luck always helps a business alliance succeed. However, our studies show, and experienced alliance practitioners will tell you, that the chances of alliance success without experience, learning and best practice adoption are, at best, only one out of five.

Alliances come in different flavors and each flavor has different characteristics. Each type of alliance needs to be treated differently for such issues as best practices, governance, success measurements, implementation, etc. Exhibit 18 outlines a proprietary alliance tool-kit approach developed at Booz·Allen.

The alliance tool-kit approach supports learning and institutionalization and thus avoids an ad-hoc approach in developing an alliance process as a core competency. Successful alliance companies are utilizing alliance tool-kits to generate an alliance transaction stream, while increasing and reinforcing their alliance proficiency (see Exhibit 19).

Exhibit 18. Tailoring the Alliance Tool-Kit

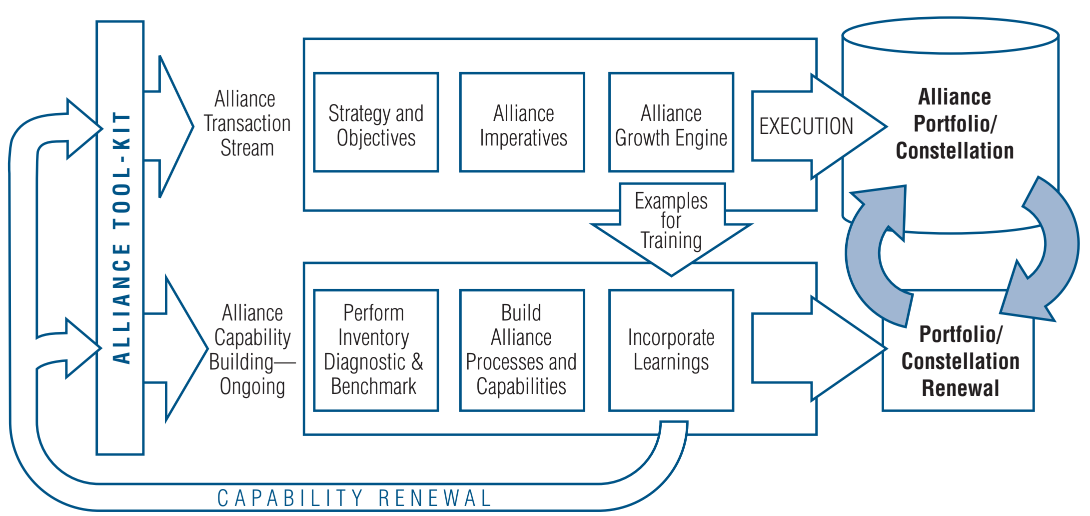


Source: Booz•Allen & Hamilton

Summary

Global industry has entered an unprecedented era of structural change. Not since the industrial revolution have new technology development and adoption, rapid market expansion and revolutionary business processes invaded managerial space with such virulence. The old "command and control" model that has worked successfully for nearly two centuries is now challenged by "The Allianced Enterprise." This new organizational ecosystem is more robust than what it replaces. This ecosystem places a high premium on growth, market leadership and capability absorption — and it delivers results. Leading edge companies are transforming their organizations and are reaping the benefits of this new business model, and so should you.

Exhibit 19. Building an Alliance Capability



Source: Booz•Allen & Hamilton

What Booz·Allen Brings

Booz·Allen & Hamilton is a global management and technology consulting firm, owned by its partners, all of whom are officers in the firm and actively engaged in client service. As world markets mature, and competition on an international scale quickens, our global perspective on business issues grows increasingly critical. In more than 90 countries, our 9,000 professionals serve the world's leading industrial, service and government organizations. Each member of our multinational team has a single, common goal — to help every client achieve and sustain success.

Our broad experience includes the world's major business and industrial sectors: aerospace, agriculture, airlines, automotive, banking, basic metals, chemicals, construction, consumer goods, defense, electronics, energy, engineering, food service, health care, heavy industry, insurance, oil and gas, pharmaceuticals, publishing, railways, steel, telecommunications, textiles, tourism, transportation and utilities.

With our in-depth understanding of industry issues and our expertise in strategy, systems, operation and technology, we assist our clients in developing the capabilities they need to compete and thrive in the global marketplace.

We judge the quality of our work just as our clients do — by the results. Their confidence in our abilities is reflected in the fact that more than 85% of the work we do is for clients we have served before. Since our founding in 1914, we have always considered client satisfaction our most important measure of success.

Booz·Allen & Hamilton has extensive experience assisting clients throughout the process of strategic alliance formulation, including vision definition, identification of critical capabilities, screening for partners, evaluating priority partners, negotiating and implementing alliances. We work together with our clients in four ways to help them improve their performance in alliances:

- **Strategy (explicit alliance strategy formulation):** Assisting clients to identify the alliance potential of their business, exploring traditional and non-traditional alliances, as well as threats posed by pre-emptive alliance plays.
- **Alliance Formulation (transactions):** Working together with a client on specific alliances, at individual stages in the process or throughout the process.
- **Process (institutionalizing alliance capabilities):** Assisting clients to build and improve their underlying capabilities in identifying, evaluating, negotiating, implementing and managing alliances — based on our best practices frameworks and methodology.
- **Alliance Portfolio Renewal:** Revitalizing a client's portfolio of existing alliances by involving the client's current partners in an effort to improve performance of those alliances — by tuning them up and reinvigorating them.

We couple the understanding from our industry practices with our functional expertise in alliances and our geographical footprint to help our clients achieve superior results in their alliance efforts.

We work with the full range of clients in terms of their alliance sophistication. We help current alliance leaders advance to the next level, as well as help companies inexperienced in alliances get established in building core capability.

Our book, *Smart Alliances*, is the top-selling alliance book, and we host the leading website on the topic (www.smartalliances.com), as well as the leading annual conference on alliances which we co-sponsor with The Conference Board.

John R. Harbison, Vice President of Booz·Allen based in Los Angeles, leads the firm's Strategic Alliances practice, and specializes in strategic alliances, acquisitions and post-merger integration. He is co-author, with Peter Pekar, of Smart Alliances: A Practical Guide to Repeatable Success*, which is the bestseller of the 110 books on alliances sold by Amazon.com.*

Peter Pekar, Jr., Ph.D., Visiting Associate Professor at the London Business School, is a recognized expert in the area of strategic alliances, with 30 years of business experience in forming and managing alliances. He has written more than 40 articles on alliances and related subjects and is a Senior Advisor to Booz·Allen.

Albert Viscio, Vice President of Booz·Allen based in San Francisco, specializes in organization and leadership, and is co-author of the book The Centerless Corporation.

David Moloney, Principal of Booz·Allen and based in Sydney, specializes in alliance-enabled strategy formulation and e-Business.

Other titles in Booz·Allen's Strategic Alliances *Viewpoint* series:

1) A Practical Guide to Alliances: Leapfrogging the Learning Curve (1993)

2) Cross-Border Alliances in the Age of Collaboration (1997)

- *An Asian Perspective on Cross-Border Alliances: Different Dreams* (1997)
- *Betting on Stability and Growth: Strategic Alliances in Latin America* (1997)

3) Institutionalizing Alliance Skills: Secrets of Repeatable Success (1997)

4) Making Acquisitions Work: Capturing Value After the Deal (1999)

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