

Strategic Management

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Lecture 8

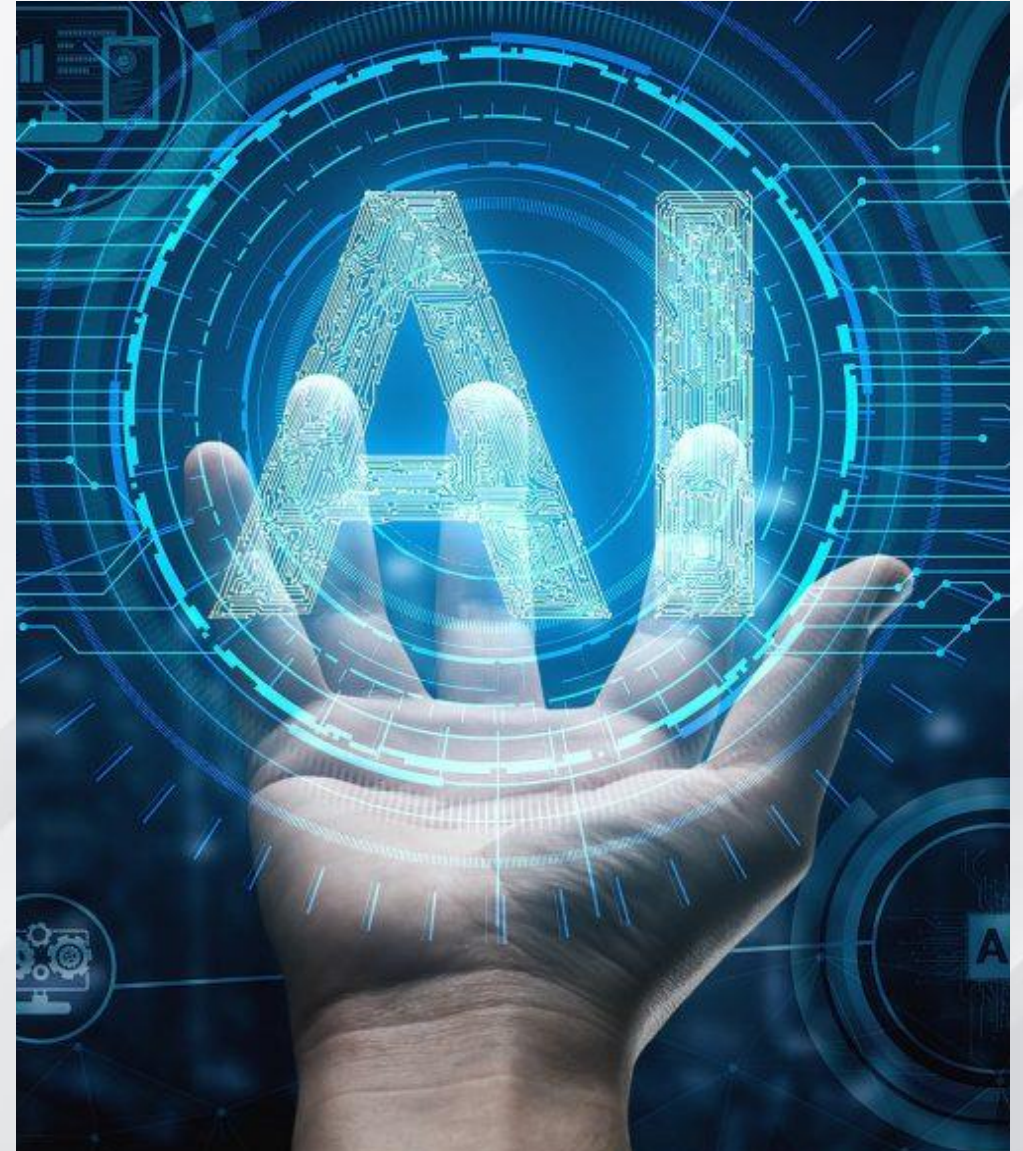
MGM414



Content

Part One / Analysis

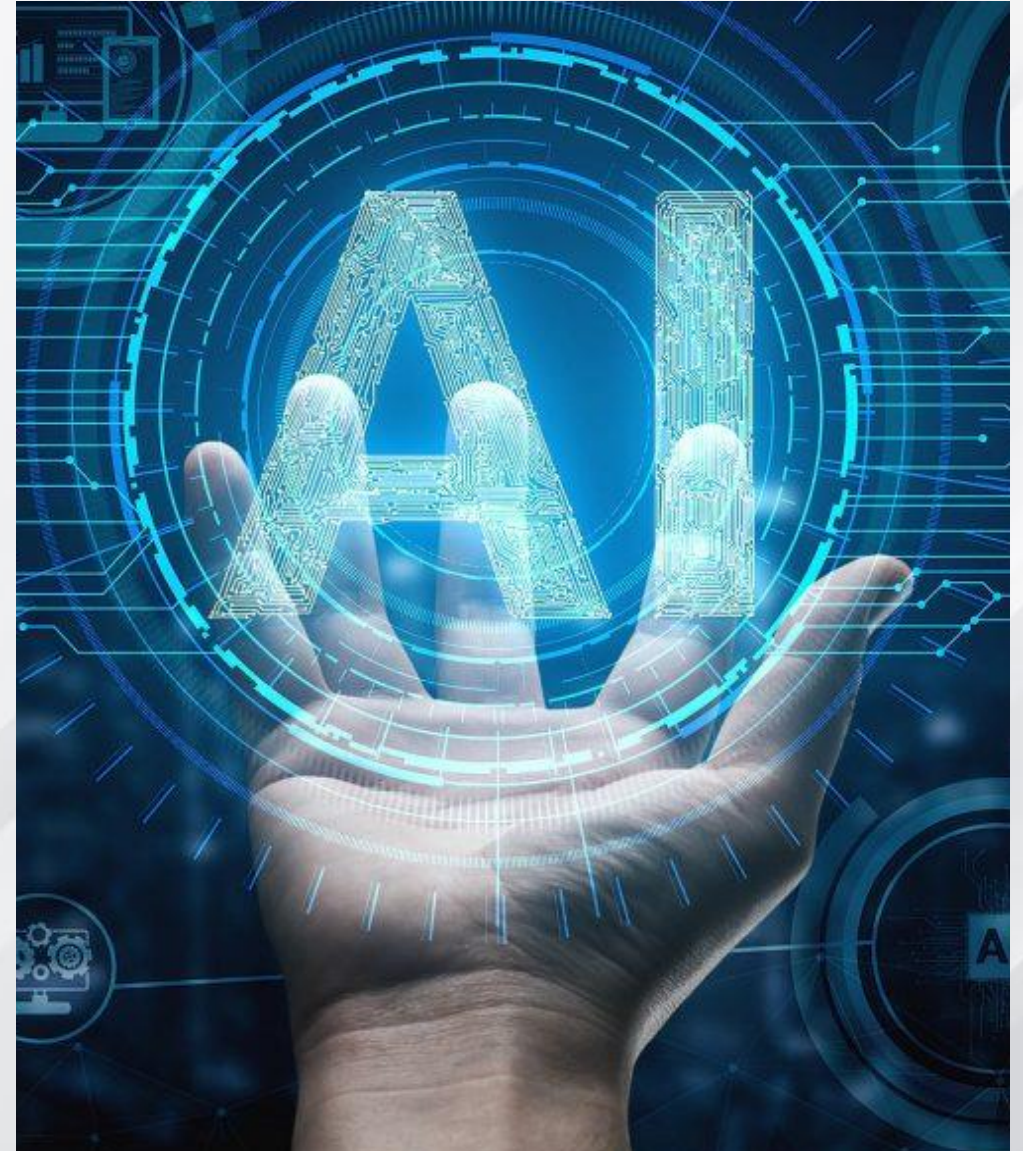
- **Chapter 1** What Is Strategy?
- **Chapter 2** Strategic Leadership: Managing the Strategy Process
- **Chapter 3** External Analysis: Industry Structure, Competitive Forces, and Strategic Groups
- **Chapter 4** Internal Analysis: Resources, Capabilities, and Core Competencies
- **Chapter 5** Competitive Advantage, Firm Performance, and Business Models



Content

Part Two/ Formulation

- **Chapter 6** Business Strategy: Differentiation, Cost Leadership, and Blue Oceans
- **Chapter 7** Business Strategy: Innovation, Entrepreneurship, and Platforms
- **Chapter 8** Corporate Strategy: Strategic Alliances, Mergers, and Acquisitions
- **Chapter 9** Global Strategy: Competing Around the World
- **Part Three/ Implementation**
- **Chapter 10** Organizational Design: Structure, Culture, and Control



Strategic Management

Strategic management involves developing and implementing plans to help an organization achieve its goals and objectives. This process can include formulating strategy, planning organizational structure and resource allocation, leading change initiatives, and controlling processes and resources.



Agenda Corporate Strategy: Strategic Alliances, Mergers and Acquisitions

- **Tesla's Secret Strategy**
- **How Firms Achieve Growth**
 - The Build-Borrow-Buy Framework
- **Strategic Alliances**
 - Why Do Firms Enter Strategic Alliances?
 - Managing strategic alliances
 - Alliance Management Capability
- **Mergers and Acquisitions**
 - Why Do Firms Merge with Competitors?
 - Why Do Firms Acquire Other Firms?

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Tesla's Secret Strategy

How Tesla Used Alliances Strategically

Since its initial public offering in 2010, the electric-car manufacturer Tesla has had tremendous impact. Indeed, by 2017 it had become the most valuable car company in the United States, ahead of GM and Ford. One critical factor in the success of the California startup is the role played by Tesla's strategy involving alliances with larger, more established companies. Two key strategic alliances in particular—one with Daimler and the other with Toyota—were crucial to Tesla's early success.



Strategic Management
Tesla Business Case



Tesla's Secret Strategy

How Tesla Used Alliances Strategically

The Daimler partnership provided a much-needed cash injection; the Toyota partnership gave Tesla access to a world-class automobile manufacturing facility located near its headquarters in Palo Alto, California.



Tesla's Secret Strategy

How Tesla Used Alliances Strategically



Initially, Tesla, which began selling its all-electric Roadster model in 2008, had neither a market nor legitimacy. Moreover, it was plagued with both thorny technical problems and cost overruns. Yet it managed to overcome these early challenges, in part by turning prospective rivals into alliance partners. In 2009, the year before its IPO, Tesla worked out the alliance with Daimler, whose roots in automobile engineering extend back to early days of the automobile powered by an internal combustion engine about 130 years ago. The deal provided Tesla with access to superior engineering expertise and a cash infusion of \$50 million, helping to save the company from potential bankruptcy.

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How Firms Achieve Growth

How do firms achieve growth? Corporate executives have three options at their disposal to drive firm growth:

- 1- organic growth through internal development.
- 2- external growth through alliances.
- 3- external growth through acquisitions.



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The build-borrow-or-buy framework

- The build-borrow-or-buy framework provides a conceptual model that aids strategists in deciding whether to pursue internal development (build), enter a contract arrangement or strategic alliance (borrow), or acquire new resources, capabilities, and competencies (buy).



The build-borrow-or-buy framework

- Firms that are able to learn how to select the right pathways to obtain new resources are more likely to gain and sustain a competitive advantage.



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Strategic Alliances

strategic alliances Voluntary arrangements between firms that involve the sharing of knowledge, resources, and capabilities with the intent of developing processes, products, or services.



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 - Why Do Firms Acquire Other Firms?

Why do companies enter into strategic alliances?

To affect a firm's competitive advantage, an alliance must promise a positive effect on the firm's economic value creation through increasing value and/or lowering costs. This logic is reflected in the common reasons firms enter alliances.

They do so to

- 1- Strengthen competitive position.**
- 2- Enter new markets.**
- 3- Hedge against uncertainty.**
- 4- Access critical complementary assets.**
- 5- Learn new capabilities.**



Why do companies enter into strategic alliances?

1- Strengthen competitive position.

Firms frequently resort to strategic alliances to strengthen their competitive position.

Firms can also use strategic alliances to change the industry structure in their favour.

Moreover, firms frequently use strategic alliances when competing in setting an industry standard.

Competitive Positioning



Why do companies enter into strategic alliances?

2- Enter new markets.

Firms may use strategic alliances to enter new markets, either in terms of products and services or geography. Using a strategic alliance, HP and DreamWorks Animation SKG created the Halo Collaboration Studio, which makes virtual communication possible around the globe. Halo's conferencing technology gives participants the vivid sense that they are in the same room.



Why do companies enter into strategic alliances?

3- Hedge against uncertainty.

In dynamic markets, strategic alliances allow firms to limit their exposure to uncertainty in the market. For instance, in the wake of the biotechnology revolution, incumbent pharmaceutical firms such as Pfizer, Novartis, and Roche entered into hundreds of strategic alliances with biotech startups. These alliances allowed the big pharma firms to make small-scale investments in many of the new biotechnology ventures that were poised to disrupt existing market economics.



Why do companies enter into strategic alliances?

4- Access critical complementary assets.

The successful commercialization of a new product or service often requires complementary assets such as marketing, manufacturing, and after-sale service. Building downstream complementary assets such as marketing and regulatory expertise or a sales force is often prohibitively expensive and time-consuming, and thus frequently not an option for new ventures.



Why do companies enter into strategic alliances?

5- Learn new capabilities.

Firms also enter strategic alliances because they are motivated by the desire to learn new capabilities from their partners. When the collaborating firms are also competitors, co-opetition ensues. Co-opetition is a portmanteau describing cooperation by competitors. They may cooperate to create a larger pie but then might compete about how the pie should be divided.



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A collage of three images. The top left shows a close-up of a hand holding a smartphone. The top right shows a person in a white lab coat. The bottom image shows a white flying robot (robotaxi) on a runway at sunset.

A large, white, multi-engine aircraft with six engines is shown on a runway at sunset. The aircraft has a high-wing configuration and a large fuselage. A smaller, similar aircraft is visible in the background on the right. The scene is set against a bright orange and yellow sunset sky.

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- A word cloud featuring various terms related to business partnerships and teamwork. The most prominent words are "strategic", "partnership", "alliance", "business", and "teamwork". Other visible words include "cooperation", "joint", "success", "collaboration", "agreement", "unity", "effort", "community", "coordination", "management", "company", "creativity", "togetherness", "collaborate", "manager", "union", "integration", "synergy", "successful", "investor", "compliance", "design", "common", "motivation", "vision", "investment", "career", "organization", "politics", "work", "goal", "join", "partner", "team", "venture", "direction", "merger", "corporate", "mutual", "consensus", "achievement", "friendship", "coalition", "relationship", "clarification", and "word". The background shows a close-up of hands shaking, symbolizing agreement or partnership.

Chapter

8

Managing strategic alliances

➤ Alliance Type

1- Non-equity (supply, licensing, and distribution agreements)

Governance Mechanism

Contract

Frequency

Most common

Type of Knowledge Exchanged

Explicit



Chapter

8

Managing strategic alliances

➤ Alliance Type

1- Non-equity (supply, licensing, and distribution agreements)

Pros

- Flexible
- Fast
- Easy to initiate and terminate

Cons

- Weak tie
- Lack of trust and commitment



Chapter

8

Managing strategic alliances

➤ Alliance Type

1- Non-equity (supply, licensing, and distribution agreements)

Examples

- Genentech-Lilly (exclusive) licensing agreement for Humulin
- Microsoft-IBM (nonexclusive) licensing agreement for MS-DOS



Chapter

8

Managing strategic alliances

➤ Alliance Type

2- Equity (purchase of an equity stake or corporate venture capital investment, or investment in kind such as a plant and equipment)

Governance Mechanism

Equity Investment

Frequency

Less common than non-equity alliances, but more common than joint Ventures

Type of Knowledge Exchanged

Explicit; exchange of tacit knowledge possible



Chapter

8

Managing strategic alliances

➤ Alliance Type

2- Equity (purchase of an equity stake or corporate venture capital investment, or investment in kind such as a plant and equipment)

Pros

- Stronger tie
- Trust and commitment can emerge
- Window into new technology (option value)

Cons

- Less flexible
- Slower
- Can entail significant investments



Managing strategic alliances

➤ Alliance Type

2- Equity (purchase of an equity stake or corporate venture capital investment, or investment in kind such as a plant and equipment)

Examples

- Renault-Nissan alliance based on cross equity holdings, with Renault owning 43.4% in Nissan; and Nissan owning 15% in Renault
- Roche's equity investment in Genentech (prior to full integration)



Chapter

8

Managing strategic alliances

➤ Alliance Type

3- Joint venture (JV)

Governance Mechanism

Creation of new entity by two or more parent Firms

Frequency

Least common

Type of Knowledge Exchanged

Both tacit and explicit knowledge exchanged



Chapter

8

Managing strategic alliances

➤ Alliance Type

3- Joint venture (JV)

Pros

- Strongest tie
- Trust and commitment likely to emerge
- May be required by institutional setting

Cons

- Can entail long negotiations And significant investments
- Long-term solution
- JV managers have double reporting lines (2 bosses)



Chapter

8

Managing strategic alliances

➤ Alliance Type

3- Joint venture (JV)

Examples

Hulu, owned by NBC (30%), Fox (30%), Disney- ABC (30%), and Turner Broadcasting System (10%)

- The A++ trans-Atlantic joint venture, owned by United Airlines, Lufthansa, and Air Canada



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- **Strategic Alliances**
 - Why Do Firms Enter Strategic Alliances?
 - Managing strategic alliances
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- **Mergers and Acquisitions**
 - Why Do Firms Merge with Competitors?
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Alliance management capabilities

Strategic alliances create a paradox for managers. Although alliances appear to be necessary to compete in many industries, between 30 and 70 per cent of all strategic alliances do not deliver the expected benefits, and are considered failures by at least one alliance partner.

Alliance management capability is a firm's ability to effectively manage three alliance-related tasks concurrently, often across a portfolio of many different alliances;

- Partner selection and alliance formation.
- Alliance design and governance.
- Post-formation alliance management.



Chapter

8

Alliance management capabilities



Alliance management capabilities

1- Partner selection and alliance formation:

When making the business case for an alliance, the expected benefits of the alliance must exceed its costs. When one or more of the five reasons for alliance formation are present—to strengthen competitive position, enter new markets, hedge against uncertainty, access critical complementary resources, or learn new capabilities—the firm must select the best possible alliance partner. Partner compatibility and partner commitment are necessary conditions for successful alliance formation.

Alliance management capabilities

2- Alliance design and governance:

Once two or more firms agree to pursue an alliance, managers must then design the alliance and choose an appropriate governance mechanism from among the three options: non-equity contractual agreement, equity alliances, or joint venture. For example, in a study of over 640 alliances, researchers found that the joining of specialized complementary assets increases the likelihood that the alliance is governed hierarchically.

Alliance management capabilities

3- Post-formation alliance management:

The third phase in a firm's alliance management capability concerns the ongoing management of the alliance. This can most likely be accomplished if the alliance partners make relation-specific investments, establish knowledge-sharing routines, and build interfirm trust.

Agenda Corporate Strategy: Strategic Alliances, Mergers and Acquisitions

- **Tesla's Secret Strategy**
- **9.1 How Firms Achieve Growth**
 - The Build-Borrow-Buy Framework
- **9.2 Strategic Alliances**
 - Why Do Firms Enter Strategic Alliances?
 - Managing strategic alliances
 - Alliance Management Capability
- **9.3 Mergers and Acquisitions**
 - Why Do Firms Merge with Competitors?
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Mergers and Acquisitions

A popular vehicle for executing corporate strategy is mergers and acquisitions (M&A). Hundreds of mergers and acquisitions occur each year, with a cumulative value in the trillions of dollars.⁵³ Although the terms are often used interchangeably, and usually in tandem, mergers and acquisitions are, by definition, distinct from each other.



Mergers and Acquisitions

- A merger describes the joining of two independent companies to form a combined entity.



Mergers and Acquisitions

A merger describes the joining of two independent companies to form a combined entity. Mergers tend to be friendly; in mergers, the two firms agree to join in order to create a combined entity. In the live event-promotion business, for example, Live Nation merged with Ticketmaster.



Mergers and Acquisitions

- An acquisition describes the purchase or takeover of one company by another. It can be friendly or unfriendly.



Mergers and Acquisitions

An acquisition describes the purchase or takeover of one company by another. Acquisitions can be friendly or unfriendly. For example, Disney's acquisition of Pixar, for example, was a friendly one, in which both management teams believed that joining the two companies was a good idea. When a target firm does not want to be acquired, the acquisition is considered a hostile takeover.



Mergers and Acquisitions

- Although there is a distinction between mergers and acquisitions, many observers simply use the umbrella term mergers and acquisitions, or M&A.
- Firms can use M&A activity for competitive advantage when they possess a superior relational capability, which is often built on superior alliance management capability.

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Why do companies merge with competitors?

In contrast to vertical integration, which concerns the number of activities a firm participates in up and down the industry value chain, horizontal integration is the process of merging with a competitor at the same stage of the industry value chain. Horizontal integration is a type of corporate strategy that can improve a firm's strategic position in a single industry.

There are three main benefits to a horizontal integration strategy:

- 1- Reduction in competitive intensity.
- 2- Lower costs.
- 3- Increased differentiation.

Why do companies merge with competitors?

1- Reduction in competitive intensity

Horizontal integration changes the underlying industry structure in favour of the surviving firms. Excess capacity is taken out of the market, and competition tends to decrease as a consequence of horizontal integration, assuming no new entrants. As a whole, the industry structure becomes more integrated and potentially more profitable.



Chapter

8

Why do companies merge with competitors?

2- Lower costs

Firms use horizontal integration to lower costs through economies of scale and to enhance their economic value creation, and in turn their performance. In industries that have high fixed costs, achieving economies of scale through large output is critical in lowering costs.



Why do companies merge with competitors?

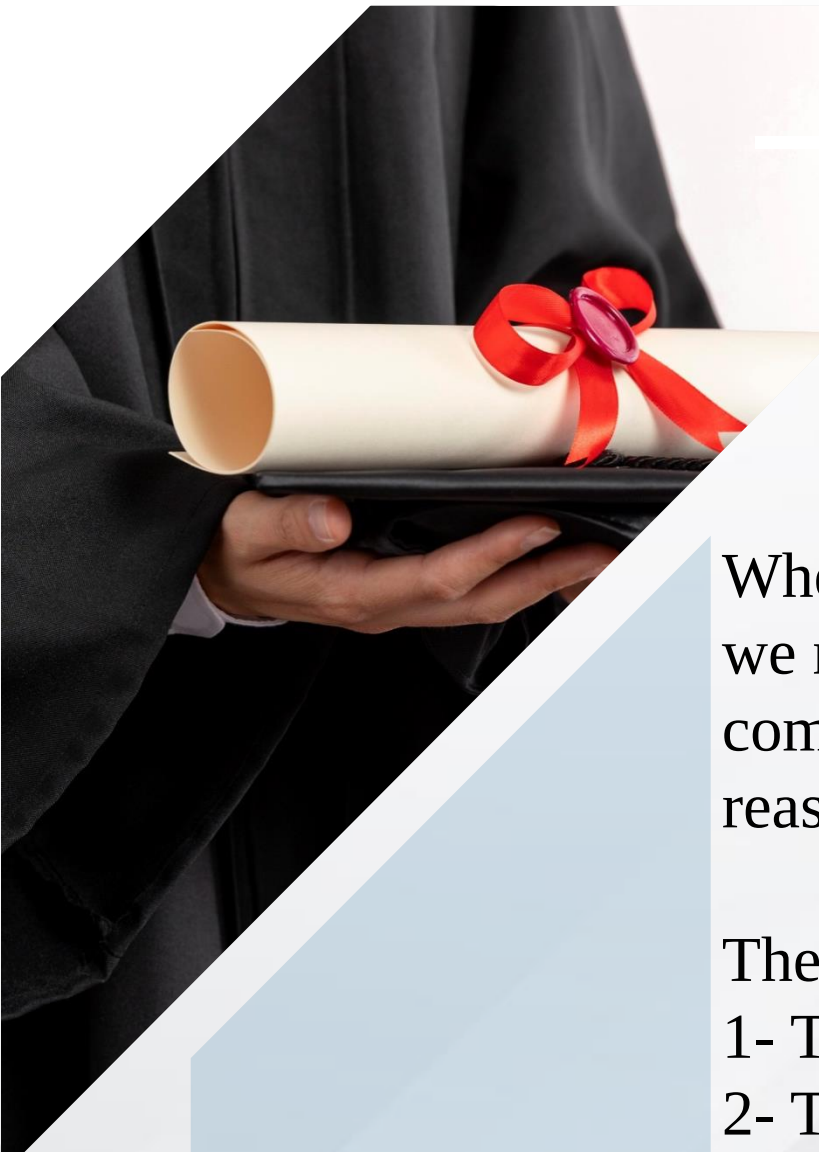
3- Increased differentiation.

Horizontal integration through M&A can help firms strengthen their competitive positions by increasing the differentiation of their product and service offerings. In particular, horizontal integration can do this by filling gaps in a firm's product offering, allowing the combined entity to offer a complete suite of products and services.



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Why do companies acquire other companies?

When first defining the terminology at the beginning of the chapter, we noted that an acquisition describes the purchase or takeover of one company by another. Why do firms make acquisitions? Three main reasons stand out:

There are two main benefits to a horizontal integration strategy:

- 1- To gain access to new markets and distribution channels.
- 2- To get ahead of its competitors.

Why do companies acquire other companies?

1- To gain access to new markets and distribution channels.

Firms may resort to acquisitions when they need to overcome entry barriers into markets they are currently not competing in or to access new distribution channels. Aggressive acquisitions, both successful and otherwise, in this regard. Firms often resort to M&A to obtain new capabilities or competencies.



Chapter

8

Why do companies acquire other companies?

2- To get ahead of its competitors.

Sometimes firms may acquire promising startups not only to gain access to a new capability or competency but also to preempt rivals from doing so. Let's look at the acquisitions made by two of the leading internet companies: Facebook and Alphabet's Google.







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