RATIONALE FOR AND BENEFITS OF STRATEGIC ALLIANCES FOR BUSINESSES IN A GLOBAL MARKET

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- rationale for and benefits of global strategic alliances
  - outsourcing
  - acquisition
  - mergers
  - joint ventures
  - franchising

WHAT WE NEED TO KNOW

Here are all the topics this PowerPoint aims to cover from the BME Y12 Syllabus.

WHAT IS A STRATEGIC ALLIANCE

A strategic alliance is designed to be a collaborative strategy between a variety of business formed over a pre determined time frame with the objective of creating mutual benefit.

Reasons why firms enter into strategic alliances

- Develop synergies (cooperation of two or more entities) to create a competitive advantage
- To acquire and export limited/unique resources, technology, skills and expertise
- Find new opportunities for growth by establishing a wider sales base
- Establish efficient entries into new markets

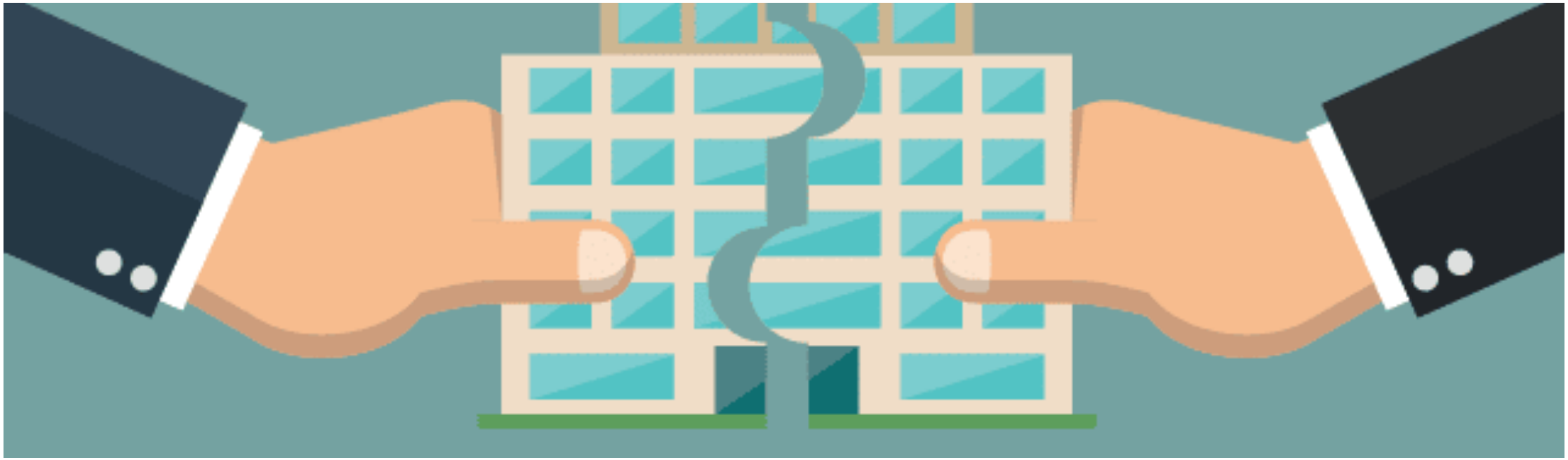
THE CASE FOR STRATEGIC ALLIANCES

Benefits	Drawbacks
• Cooperation between competitors for strategic purposes • Combine resources, capabilities, and core competencies to generate mutual interests • Gain access to a restricted market • Maintain market stability (setting product standards) • Establish a franchise in a new market • Gain market share • Pool resources for large capital projects • Establish economies of scale • Gain access to complementary resources • Speed up the development of new goods or services • Share R&D, operating and working capital expenses • Reduction of competition by forming an alliance with competitors • Quick access to a new market	• Conflicts of interest and differences in culture, values, and objectives • Loss of control and autonomy over product quality, operating costs, and employees • Difficulties in coordinating and integrating operations and systems • Legal and regulatory issues • Information sharing and intellectual property concerns • Dependence on the partner's performance and reputation • Limited strategic flexibility and potential for lock-in

OUTSOURCING

- The act of moving non-core activities of a firm away from internal operations, this allows an external specialist party (firm, agency etc.) to provide or conduct the activities instead.
- Outsourcing work and/or jobs to other firms both abroad and domestically can lead to more efficient results at often cheaper prices. Examples of outsourcing overseas would include game development, engineering, payroll, and human resources.

Rewards	Challenges
- Potentially lower labour costs through classification of workers as sub contractors not employees - Improve quality of processes by outsourcing to heavily specialised firms - Allows management to focus on core competencies (areas) of the business	- Reduces control and oversight of a firm on certain processes and functions outsourced - Creates risk of confidential information being disclosed to competitors even with NDAs (non-disclosure agreements) - Language and cultural barriers from overseas partners may restrict firm to firm communication or lead to incorrect expectations/outcomes



ACQUISITION

- The process of a business permanently buying out another firm by purchasing a majority (controlling) stake in the target firm. This is a long-term strategy with the primary focus of providing a quicker start in exploiting an overseas or new market
- Businesses acquisitions are common and frequently used as a growth strategy because it can create bigger, more competitive and cost-efficient businesses.
- Two businesses are more valuable together than apart due to combined skills, expertise, shared capital and greater market share.

ACQUSITIONS (CONTINUED)

When a firm is acquired, it ceases trading (existence) and becomes a part of the firm who purchased it. These acquisitions as such can be of hostile or friendly nature:

- **Hostile** acquisition – where a business approaches directly the shareholders of another firm to offer to buy their shares, or when the business uses its voting power (generally from shares) to place people on the Board of Directors to approve the acquisition. This is defined as hostile as the acquisition is attempted without prior approval or consent of the firm's management and directors.
- **Friendly** acquisition – when a business purchases majority shares in another firm based on an agreed negotiated process with the full consent of the board and directors and full disclosure to existing shareholders. For this purchase to proceed, **existing shareholders may have to agree to sell their shares.** This is a more accepted form of acquisitions that is likely to pass shareholders.

STRATEGIES USED IN A HOSTILE ACQUISITION

Presenting a tender offer – see the description in the previous slide for hostile acquisition, this explains what presenting a tender offer is.

Buying shares on the open market – when a firm purchases enough shares in another firm through the stock exchange to obtain a controlling stake

Using a proxy fight – the interested purchaser persuades shareholders to replace the management of a firm with one that will approve the acquisition. This minimises the financial burden of otherwise needing to buy out a firm's shares.

Bear hug approach – this is similar to a tender offer where a buyer makes an offer to a firm's board to take over the company **without approaching shareholders.** The purchase proposal and offered price to buy shares off shareholders is made public to try and 'squeeze' board of directors to accept an offer they may not like. The shareholders and media scrutiny adds pressure to the board to accept the offer.

ACQUISITIONS PROS AND CONS

Pros	Cons
- Established customer base able to be utilised - Increased market share by combining customer bases - Skip start-up process that requires expensive and time-heavy research and development - Enhances economies of scale - Opportunities to diversify a business by acquiring different brands - Reduction of training costs as the firm can use resources from the other firm acquired to reduce internal training expenses	- Administrative burden leads to job loss (accounting, IT, human resources management) - Credit issues (difficulty obtain borrowings from lenders, especially acquisition was final debt) - Cultural clashes between firms as each firm has its distinct culture that was in development since inception - Duplication of employee duties as when similar firms are acquired there may be departments and/or people which have the same responsibilities

MERGERS

- The permanent amalgamation (combination or union) of two or more firms where shareholders of two businesses become the shareholders of a new merged business. This strategy is similar to an acquisition but both companies involved are typically of similar size and **agree to form a new business**
- This is an agreement between **firms to exist as one**
- It may involve a new name, logo and slogan to launch and identify the new business

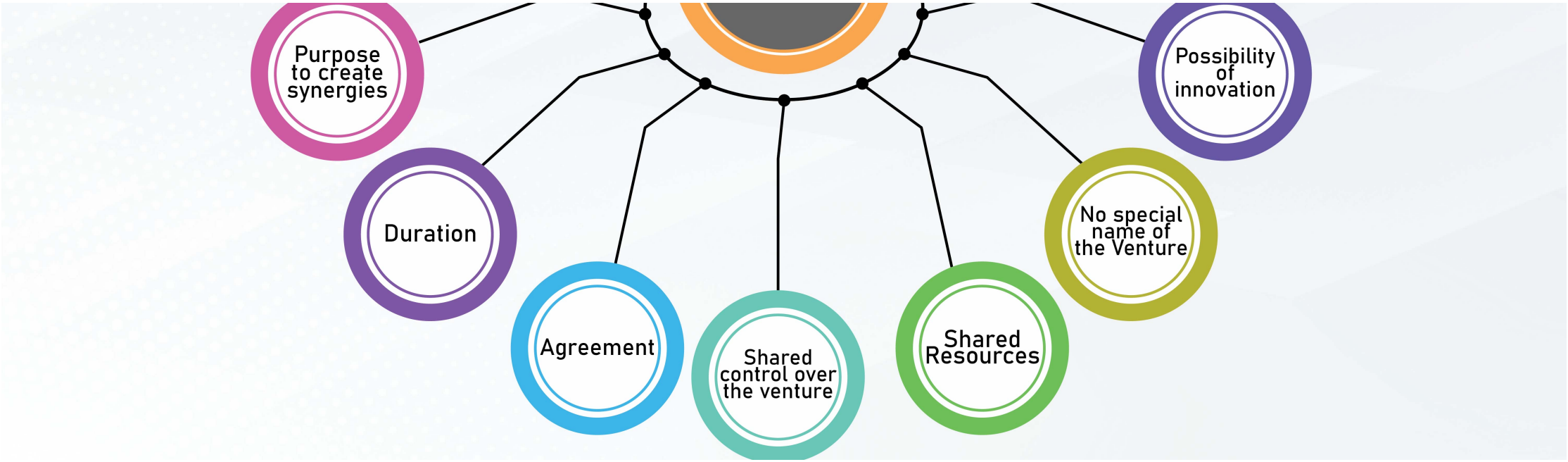
TYPES OF MERGERS

There are three main types of mergers that firms may undertake.

- **Horizontal mergers** – when two firms in the same industry that sell similar products or services in the market combine. A completed merger leaves the market with one less competitor and a larger combined firm which is more competitive at the risk of potential monopolisation of a market or sales cannibalisation (where sales of a similar product reduce the market share of another good)
- **Vertical mergers** – where two or more firms involved in different stages the supply chain process for the same/common goods or services combine under one ownership. These firms previously would have been selling to or buying from each other
- **Conglomerate mergers** – when active firms combine in completely unrelated business activities or operating in different geographical locations. Firms often do this when there is a commercial interest to expand into different industries or markets

MERGERS PROS AND CONS

Pros	Cons
- Increased Market Share, decreased competition - Wider Customer base - Access of funds/assets to facilitate business growth – economies of scale - Reduces competition for the firm by merging with its competitor - Ownership of extended intellectual property - Reduces operation costs through rationalisation (the reorganization of a company in order to increase its operating efficiency) - Less expensive to merge with a business than to expand/create another division	- Duplication of labour resources result in job losses - Internal politics can cause employee turnover - Different understanding of organizational culture - The buyer may end up with obligations they are not ready to undertake (such as class action lawsuits, complicated tax issues) should due diligence (vetting) not take place on the firm being merged with - Miscalculating synergies where the firms merging may be overly optimistic about the results and underestimate how long it takes for synergies to come to fruition



JOINT VENTURES

A form of alliance where there is a temporary and legally binding agreement between two or more businesses to collaborate and combine their resources for a certain period, to provide a service, produce a good or work on a unique project opportunity.

A **separate business entity** is created out of a joint venture, so that the firm can focus on the joint venture project and allow individual firms to focus on their own core businesses.

Employees of all joint venture initiatives must be committed to embracing change and open communication, as these are reportedly the two main factors that determine the success or failure of these ventures.

JOINT VENTURES PROS AND CONS

Pros	Cons
- High specialization in job, share skills - Same objectives which compliment each other (viability) - Access to greater resources, including specialized staff/technology (decreases costs) - Access to new markets and distribution networks - Increases production capacities - Allows risks and costs (liability) to be shared between partnering firms	- Different cultures, management styles personalities might present conflict - Differing or unclear visions regarding the objectives of the venture - Each company equally responsible for claiming level of involvement in activities that prompt claim - Work and resources may not be distributed clearly - Leadership and support may be lacking in early stages - Venture's contractual limitation could pose a risk to a partner's core business operations

FRANCHISING

- ‘[A] continuing relationship in which the franchisor provides a licensed privilege to do business, plus assistance in organising training, merchandising and management in return for a consideration from the franchisee.’ – International Franchise Association
- A franchisee in this model sells its marketing rights or a business image/model in return for a fee and/or royalty payment.
- Master franchisees are responsible for developing a franchise network in a geographical region, and may work with firms on behalf of a franchising firm to setup and fund new franchises with the intent of added security/likelihood they will succeed.

FRANCHISING PROS AND CONS

Pros	Cons
Receives goodwill consisting of - Well-established brand, reputation & product - Healthy/strong business model - Market research - Intellectual property Also, will have assistance with: - Leasing, site development, shop fitting, design/equipment purchasing, financial assistance - Education + Training for franchisee and staff	- Payments of royalties as an initial fee and fees restrict profitability - Obligations to obey rules and guidelines by franchisor - Restricted control on introducing new products which limits innovation and creativity - Potentially two many franchisors in a market that have similar or same products and services - Franchisor may select a location or fit-out (furnishings) that may not suit you or the area