You can't run from strategic alliances. So learn how to borrow.

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Collaborate with Your Competitors—and Win

by Gary Hamel, Yves L. Doz, and C.K. Prahalad

Collaboration between competitors is in fashion. General Motors and Toyota assemble automobiles, Siemens and Philips develop semiconductors, Canon supplies photocopiers to Kodak, France's Thomson and Japan's JVC manufacture videocassette recorders. But the spread of of what we call "competitive collaboration"—joint ventures, outsourcing agreements, product licensings, cooperative research—has triggered unease about the long-term consequences. A strategic alliance can strengthen both companies against outsiders even as it weakens one partner vis-à-vis the other. In particular, alliances between Asian companies and Western rivals seem to work against the Western partner. Cooperation becomes a low-cost route for new competitors to gain technology and market access.[1]

Yet the case for collaboration is stronger than ever. It takes so much money to develop new products and to penetrate new markets that few companies can go it alone in every situation. ICL, the British computer company, could not have developed its current generation of mainframes without Fujitsu. Motorola needs Toshiba's distribution capacity to break into the Japanese semiconductor market. Time is another critical factor. Alliances can provide shortcuts for Western companies racing to improve their production efficiency and quality control.

We have spent more than five years studying the inner workings of 15 strategic alliances and monitoring scores of others. Our research (see the insert "About Our Research") involves cooperative ventures between competitors from the United States and Japan, Europe and Japan, and the United States and Europe. We did not judge the success or failure of each partnership by its longevity—a common mistake when evaluating strategic alliances—but by the

1. For a vigorous warning about the perils of collaboration, see Robert B. Reich and Eric D. Mankin, "Joint Ventures with Japan Give Away Our Future," HBR March-April 1986, p.78.

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shifts in competitive strength on each side. We focused on how companies use competitive collaboration to enhance their internal skills and technologies while they guard against transferring competitive advantages to ambitious partners.

There is no immutable law that strategic alliances *must* be a windfall for Japanese or Korean partners. Many Western companies do give away more than they gain – but that's because they enter partnerships without knowing what it takes to win. Companies that benefit most from competitive collaboration adhere to a set of simple but powerful principles.

Collaboration is competition in a different form. Successful companies never forget that their new partners may be out to disarm them. They enter alliances with clear strategic objectives, and they also understand how their partners' objectives will affect their success.

Harmony is not the most important measure of success. Indeed, occasional conflict may be the best evidence of mutually beneficial collaboration. Few alliances remain win-win undertakings forever. A partner may be content even as it unknowingly surrenders core skills.

Cooperation has limits. Companies must defend against competitive compromise. A strategic alliance is a constantly evolving bargain whose real terms go beyond the legal agreement or the aims of top management. What information gets traded is determined day to day, often by engineers and operating managers. Successful companies inform employees at all levels about what skills and technologies are off-limits to the partner and monitor what the partner requests and receives.

Learning from partners is paramount. Successful companies view each alliance as a window on their partners' broad capabilities. They use the alliance to build skills in areas outside the formal agreement and systematically diffuse new knowledge throughout their organizations.

Why Collaborate?

Using an alliance with a competitor to acquire new technologies or skills is not devious. It reflects the commitment and capacity of each partner to absorb the skills of the other. We found that in every case in which a Japanese company emerged from an alliance stronger than its Western partner, the Japanese company had made a greater effort to learn.

Strategic intent is an essential ingredient in the commitment to learning. The willingness of Asian companies to enter alliances represents a change in competitive tactics, not competitive goals. NEC, for example, has used a series of collaborative ventures to enhance its technology and product competences. NEC is the only company in the world with a leading position in telecommunications, computers, and semiconductors – despite its investing less in R&D (as a percentage of revenues) than competitors like Texas Instruments, Northern Telecom, and L.M. Ericsson. Its string of partnerships, most notably with Honeywell, allowed NEC to leverage its in-house R&D over the last two decades.

Western companies, on the other hand, often enter alliances to avoid investments. They are more interested in reducing the costs and risks of entering new businesses or markets than in acquiring new skills. A senior U.S. manager offered this analysis of his company's venture with a Japanese rival: "We complement each other well – our distribution capability and their manufacturing skill. I see no reason to invest upstream if we can find a secure source of product. This is a comfortable relationship for us."

> It's not devious to absorb skills from your partner – that's the whole idea.

An executive from this company's Japanese partner offered a different perspective: "When it is necessary to collaborate, I go to my employees and say, 'This is bad, I wish we had these skills ourselves. Collaboration is second best. But I will feel worse if after four years we do not know how to do what our partner knows how to do.' We must digest their skills."

The problem here is not that the U.S. company wants to share investment risk (its Japanese partner does too) but that the U.S. company has no ambition *beyond* avoidance. When the commitment to learning is so one-sided, collaboration invariably leads to competitive compromise.

Many so-called alliances between Western companies and their Asian rivals are little more than sophisticated outsourcing arrangements (see the insert "Competition for Competence"). General Motors buys cars and components from Korea's Daewoo. Siemens buys computers from Fujitsu. Apple buys laser printer engines from Canon. The traffic is almost entirely one way. These OEM deals offer Asian partners a way to capture investment initiative from Western competitors and displace customer-competitors from value-creating activities. In many cases this goal meshes with that of the Western partner: to regain competitiveness quickly and with minimum effort.

About Our Research

We spent more than five years studying the internal workings of 15 strategic alliances around the world. We sought answers to a series of interrelated questions. What role have strategic alliances and outsourcing agreements played in the global success of Japanese and Korean companies? How do alliances change the competitive balance between partners? Does winning at collaboration mean different things to different companies? What factors determine who gains most from collaboration?

To understand who won and who lost and why, we observed the interactions of the partners firsthand and at multiple levels in each organization. Our sample included four European-U.S. alliances, two intra-European alliances, two European-Japanese alliances, and seven U.S.-Japanese alliances. We gained access to both sides of the partnerships in about half the cases and studied each alliance for an average of three years.

Confidentiality was a paramount concern. Where we did have access to both sides, we often wound up knowing more about who was doing what to whom than either of the partners. To preserve confidentiality, our article disguises many of the alliances that were part of the study.

Consider the joint venture between Rover, the British automaker, and Honda. Some 25 years ago, Rover's forerunners were world leaders in small car design. Honda had not even entered the automobile business. But in the mid-1970s, after failing to penetrate foreign markets, Rover turned to Honda for technology and product-development support. Rover has used the alliance to avoid investments to design and build new cars. Honda has cultivated skills in European styling and marketing as well as multinational manufacturing. There is little doubt which company will emerge stronger over the long term.

Troubled laggards like Rover often strike alliances with surging latecomers like Honda. Having fallen behind in a key skills area (in this case, manufacturing small cars), the laggard attempts to compensate for past failures. The latecomer uses the alliance to close a specific skills gap (in this case, learning to build cars for a regional market). But a laggard that forges a partnership for short-term gain may find itself in a dependency spiral: as it contributes fewer and fewer distinctive skills, it must reveal more and more of its internal operations to keep the partner interested. For the weaker company, the issue shifts from "Should we collaborate?" to "With whom should we collaborate?" to "How do we keep our partner interested as we lose the advantages that made us attractive to them in the first place?"

There's a certain paradox here. When both partners are equally intent on internalizing the other's skills, distrust and conflict may spoil the alliance and threaten its very survival. That's one reason joint ventures between Korean and Japanese companies have been few and tempestuous. Neither side wants to "open the kimono." Alliances seem to run most smoothly when one partner is intent on learning and the other is intent on avoidance—in essence, when one partner is willing to grow dependent on the other. But running smoothly is not the point; the point is for a company to emerge from an alliance more competitive than when it entered it.

One partner does not always have to give up more than it gains to ensure the survival of an alliance. There are certain conditions under which mutual gain is possible, at least for a time:

The partners' strategic goals converge while their competitive goals diverge. That is, each partner allows for the other's continued prosperity in the shared business. Philips and Du Pont collaborate to develop and manufacture compact discs, but neither side invades the other's market. There is a clear upstream/downstream division of effort.

The size and market power of both partners is modest compared with industry leaders. This forces each side to accept that mutual dependence may have to continue for many years. Long-term collaboration may be so critical to both partners that neither will risk antagonizing the other by an overtly competitive bid to appropriate skills or competences. Fujitsu's 1 to 5 size disadvantage with IBM means it will be a long time, if ever, before Fujitsu can break away from its foreign partners and go it alone.

Each partner believes it can learn from the other and at the same time limit access to proprietary skills. JVC and Thomson, both of whom make VCRs, know that they are trading skills. But the two companies are looking for very different things. Thomson needs product technology and manufacturing prowess; JVC needs to learn how to succeed in the fragmented European market. Both sides believe there is an equitable chance for gain.

How to Build Secure Defenses

For collaboration to succeed, each partner must contribute something distinctive: basic research, product development skills, manufacturing capacity, access to distribution. The challenge is to share enough skills to create advantage vis-à-vis compa-

nies outside the alliance while preventing a wholesale transfer of core skills to the partner. This is a very thin line to walk. Companies must carefully select what skills and technologies they pass to their partners. They must develop safeguards against unintended, informal transfers of information. The goal is to limit the transparency of their operations.

The type of skill a company contributes is an important factor in how easily its partner can internalize the skills. The potential for transfer is greatest when a partner's contribution is easily transported (in engineering drawings, on computer tapes, or in the heads of a few technical experts); easily interpreted (it can be reduced to commonly understood equations or symbols); and easily absorbed (the skill or competence is independent of any particular cultural context).

Western companies face an inherent disadvantage because their skills are generally more vulnerable to transfer. The magnet that attracts so many companies to alliances with Asian competitors is their manufacturing excellence – a competence that is less transferable than most. Just-in-time inventory systems and quality circles can be imitated, but this is like pulling a few threads out of an oriental carpet. Manufacturing excellence is a complex web of employee training, integration with suppliers, statistical process controls, employee involvement, value engineering, and design for manufacture. It is difficult to extract such a subtle competence in any way but a piecemeal fashion.

There is an important distinction between technology and competence. A discrete, stand-alone technology (for example, the design of a semiconductor chip) is more easily transferred than a process competence, which is entwined in the social fabric of a company. Asian companies often learn more from their Western partners than vice versa because they contribute difficult-to-unravel strengths, while Western partners contribute easy-to-imitate technology.

> Alliances should establish and enforce specific performance requirements. No performance, no technology transfer.

So companies must take steps to limit transparency. One approach is to limit the scope of the formal agreement. It might cover a single technology rather than an entire range of technologies; part of a product line rather than the entire line; distribution in a limited number of markets or for a limited period of time. The objective is to circumscribe a partner's opportunities to learn.

Moreover, agreements should establish specific performance requirements. Motorola, for example, takes an incremental, incentive-based approach to technology transfer in its venture with Toshiba. The agreement calls for Motorola to release its microprocessor technology incrementally as Toshiba delivers on its promise to increase Motorola's penetration in the Japanese semiconductor market. The greater Motorola's market share, the greater Toshiba's access to Motorola's technology.

Many of the skills that migrate between companies are not covered in the formal terms of collaboration. Top management puts together strategic alliances and sets the legal parameters for exchange. But what actually gets traded is determined by day-to-day interactions of engineers, marketers, and product developers: who says what to whom, who gets access to what facilities, who sits on what joint committees. The most important deals ("I'll share this with you if you share that with me") may be struck four or five organizational levels below where the deal was signed. Here lurks the greatest risk of unintended transfers of important skills.

Consider one technology-sharing alliance between European and Japanese competitors. The European company valued the partnership as a way to acquire a specific technology. The Japanese company considered it a window on its partner's entire range of competences and interacted with a broad spectrum of its partner's marketing and product-development staff. The company mined each contact for as much information as possible.

For example, every time the European company requested a new feature on a product being sourced from its partner, the Japanese company asked for detailed customer and competitor analyses to justify the request. Over time, it developed a sophisticated picture of the European market that would assist its own entry strategy. The technology acquired by the European partner through the formal agreement had a useful life of three to five years. The competitive insights acquired informally by the Japanese company will probably endure longer.

Limiting unintended transfers at the operating level requires careful attention to the role of gatekeepers, the people who control what information flows to a partner. A gatekeeper can be effective only if there are a limited number of gateways through which a partner can access people and facilities. Fujitsu's many partners all go through a single office, the "collaboration section," to request information and assistance from different divisions. This way the

Competition for Competence

In the article "Do You Really Have a Global Strategy?" (HBR July-August 1985), Gary Hamel and C.K. Prahalad examined one dimension of the global competitive battle: the race for brand dominance. This is the battle for control of distribution channels and global "share of mind." Another global battle has been much less visible and has received much less management attention. This is the battle for control over key technology-based competences that fuel new business development.

Honda has built a number of businesses, including marine engines, lawn mowers, generators, motorcycles, and cars, around its engine and power train competence. Casio draws on its expertise in semiconductors and digital display in producing calculators, small-screen televisions, musical instruments, and watches. Canon relies on its imaging and microprocessor competences in its camera, copier, and laser printer businesses.

In the short run, the quality and performance of a company's products determine its competitiveness. Over the longer term, however, what counts is the ability to build and enhance core competences – distinctive skills that spawn new generations of products. This is where many managers and commentators fear Western companies are losing. Our research helps explain why some companies may be more likely than others to surrender core skills.

Alliance or Outsourcing?

Enticing Western companies into outsourcing agreements provides several benefits to ambitious OEM partners. Serving as a manufacturing base for a Western partner is a quick route to increased manufacturing share without the risk or expense of building brand share. The Western partners' distribution capability allows Asian suppliers to focus all their resources on building absolute product advantage. Then OEMs can enter markets on their own and convert manufacturing share into brand share.

Serving as a sourcing platform yields more than just volume and process improvements. It also generates low-cost, low-risk market learning. The downstream (usually Western) partner typically provides information on how to tailor products to local markets. So every product design transferred to an OEM partner is also a research report on customer preferences and market needs. The OEM partner can use these insights to read the market accurately when it enters on its own.

A Ratchet Effect

Our research suggests that once a significant sourcing relationship has been established, the buyer becomes less willing and able to reemerge as a manufacturing competitor. Japanese and Korean companies are, with few exceptions, exemplary suppliers. If anything, the "soft option" of outsourcing becomes even softer as OEM suppliers routinely exceed delivery and quality expectations.

Outsourcing often begins a ratchetlike process. Relinquishing manufacturing control and paring back plant investment leads to sacrifices in product design, process technology, and, eventually, R&D budgets. Consequently, the OEM partner captures product-development as well as manufacturing initiative. Ambitious OEM partners are not content with the old formula of "You design it and we'll make it." The new reality is, "You design it, we'll learn from your designs, make them more manufacturable, and launch our products alongside yours."

Reversing the Verdict

This outcome is not inevitable. Western companies can retain control over their core competences by keeping a few simple principles in mind.

A competitive product is not the same thing as a competitive organization. While an Asian OEM partner may provide the former, it seldom provides the latter. In essence, outsourcing is a way of renting someone else's competitiveness rather than developing a long-term solution to competitive decline.

Rethink the make-or-buy decision. Companies often treat component manufacturing operations as cost centers and transfer their output to assembly units at an arbitrarily set price. This transfer price is an accounting fiction, and it is unlikely to yield as high a return as marketing or distribution investments, which require less research money and capital. But companies seldom consider the competitive consequences of surrendering control over a key value-creating activity.

Watch out for deepening dependence. Surrender results from a series of outsourcing decisions that individually make economic sense but collectively amount to a phased exit from the business. Different managers make outsourcing decisions at different times, unaware of the cumulative impact.

Replenish core competences. Western companies must outsource some activities; the economics are just too compelling. The real issue is whether a company is adding to its stock of technologies and competences as rapidly as it is surrendering them. The question of whether to outsource should always provoke a second question: Where can we outpace our partner and other rivals in building new sources of competitive advantage?

company can monitor and control access to critical skills and technologies.

We studied one partnership between European and U.S. competitors that involved several divisions of each company. While the U.S. company could only access its partner through a single gateway, its partner had unfettered access to all participating divisions. The European company took advantage of its free rein. If one division refused to provide certain information, the European partner made the same request of another division. No single manager in the U.S. company could tell how much information had been transferred or was in a position to piece together patterns in the requests.

Collegiality is a prerequisite for collaborative success. But *too much* collegiality should set off warning bells to senior managers. CEOs or division presidents should expect occasional complaints from their counterparts about the reluctance of lower level employees to share information. That's a sign that the gatekeepers are doing their jobs. And senior management should regularly debrief operating personnel to find out what information the partner is requesting and what requests are being granted.

Limiting unintended transfers ultimately depends on employee loyalty and self-discipline. This was a real issue for many of the Western companies we studied. In their excitement and pride over technical achievements, engineering staffs sometimes shared information that top management considered sensitive. Japanese engineers were less likely to share proprietary information.

There are a host of cultural and professional reasons for the relative openness of Western technicians. Japanese engineers and scientists are more loyal to their company than to their profession. They are less steeped in the open give-and-take of university research since they receive much of their training from employers. They consider themselves team members more than individual scientific contributors. As one Japanese manager noted, "We don't feel any need to reveal what we know. It is not an issue of pride for us. We're glad to sit and listen. If we're patient we usually learn what we want to know."

> When a foreign partner houses, feeds, and looks after your managers, there is a danger they will "go native."

Controlling unintended transfers may require restricting access to facilities as well as to people. Companies should declare sensitive laboratories and factories off-limits to their partners. Better yet, they might house the collaborative venture in an entirely new facility. IBM is building a special site in Japan where Fujitsu can review its forthcoming mainframe software before deciding whether to license it. IBM will be able to control exactly what Fujitsu sees and what information leaves the facility.

Finally, which country serves as "home" to the alliance affects transparency. If the collaborative team is located near one partner's major facilities, the other partner will have more opportunities to learn – but less control over what information gets traded. When the partner houses, feeds, and looks after engineers and operating managers, there is a danger they will "go native." Expatriate personnel need frequent visits from headquarters as well as regular furloughs home.

Enhance the Capacity to Learn

Whether collaboration leads to competitive surrender or revitalization depends foremost on what employees believe the purpose of the alliance to be. It is self-evident: to learn, one must *want* to learn. Western companies won't realize the full benefits of competitive collaboration until they overcome an arrogance borne of decades of leadership. In short, Western companies must be more receptive.

We asked a senior executive in a Japanese electronics company about the perception that Japanese companies learn more from their foreign partners than vice versa. "Our Western partners approach us with the attitude of teachers," he told us. "We are quite happy with this, because we have the attitude of students."

Learning begins at the top. Senior management must be committed to enhancing their companies' skills as well as to avoiding financial risk. But most learning takes place at the lower levels of an alliance. Operating employees not only represent the front lines in an effective defense but also play a vital role in acquiring knowledge. They must be well briefed on the partner's strengths and weaknesses and understand how acquiring particular skills will bolster their company's competitive position.

This is already standard practice among Asian companies. We accompanied a Japanese development engineer on a tour through a partner's factory. This engineer dutifully took notes on plant layout, the number of production stages, the rate at which the line was running, and the number of employees. He recorded all this despite the fact that he had no manufacturing responsibility in his own company,

and that the alliance didn't encompass joint manufacturing. Such dedication greatly enhances learning.

Collaboration doesn't always provide an opportunity to fully internalize a partner's skills. Yet just acquiring new and more precise benchmarks of a partner's performance can be of great value. A new benchmark can provoke a thorough review of internal performance levels and may spur a round of competitive innovation. Asking questions like, "Why do their semiconductor logic designs have fewer errors than ours?" and "Why are they investing in this technology and we're not?" may provide the incentive for a vigorous catch-up program.

Competitive benchmarking is a tradition in most of the Japanese companies we studied. It requires many of the same skills associated with competitor analysis: systematically calibrating performance against external targets; learning to use rough estimates to determine where a competitor (or partner) is better, faster, or cheaper; translating those estimates into new internal targets; and recalibrating to establish the rate of improvement in a competitor's performance. The great advantage of competitive collaboration is that proximity makes benchmarking easier.

Indeed, some analysts argue that one of Toyota's motivations in collaborating with GM in the much-publicized NUMMI venture is to gauge the quality of GM's manufacturing technology. GM's top manufacturing people get a close look at Toyota, but the reverse is true as well. Toyota may be learning whether its giant U.S. competitor is capable of closing the productivity gap with Japan.

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Competitive collaboration also provides a way of getting close enough to rivals to predict how they will behave when the alliance unravels or runs its course. How does the partner respond to price changes? How does it measure and reward executives? How does it prepare to launch a new product? By revealing a competitor's management orthodoxies, collaboration can increase the chances of success in future head-to-head battles.

Knowledge acquired from a competitor-partner is only valuable after it is diffused through the organization. Several companies we studied had established internal clearinghouses to collect and disseminate information. The collaborations manager at one Japanese company regularly made the rounds of all employees involved in alliances. He identified what information had been collected by whom and then passed it on to appropriate departments. Another company held regular meetings where employees shared new knowledge and determined who was best positioned to acquire additional information.

Proceed with Care – But Proceed

After World War II, Japanese and Korean companies entered alliances with Western rivals from weak positions. But they worked steadfastly toward independence. In the early 1960s, NEC's computer business was one-quarter the size of Honeywell's, its primary foreign partner. It took only two decades for NEC to grow larger than Honeywell, which eventually sold its computer operations to an alliance between NEC and Group Bull of France. The NEC experience demonstrates that dependence on a foreign partner doesn't automatically condemn a company to also-ran status. Collaboration may sometimes be unavoidable; surrender is not.

Managers are too often obsessed with the ownership structure of an alliance. Whether a company controls 51% or 49% of a joint venture may be much less important than the rate at which each partner learns from the other. Companies that are confident of their ability to learn may even prefer some ambiguity in the alliance's legal structure. Ambiguity creates more potential to acquire skills and technologies. The challenge for Western companies is not to write tighter legal agreements but to become better learners.

Running away from collaboration is no answer. Even the largest Western companies can no longer outspend their global rivals. With leadership in many industries shifting toward the East, companies in the United States and Europe must become good borrowers – much like Asian companies did in the 1960s and 1970s. Competitive renewal depends on building new process capabilities and winning new product and technology battles. Collaboration can be a low-cost strategy for doing both.

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