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Successful and sustainable business partnerships: How to select the right partners

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Abstract

In more and more industries it becomes true that value creating networks compete against each other with relatively stable relations between suppliers inside the network. Managers all over the world are searching for the most efficient and effective coordinative forms for their relations with OEM's or suppliers within such a value-creating networks. This paper gives a normative guideline to decide if or if not a partnership is the right coordinative form for OEM-supplier relations within a value-creating network. Based on the existing mainly positivistic research in this field, two aspects are highlighted as the main drivers for the suitability of a partnership as a well working governance mechanism for value-creating networks: (i) individualization vs. standardization of the delivered components combined with the potential of the end customers to identify quality differences or not and (ii) the possibilities to allocate the revenues made by the value-creating network on the several 'partners' within the network. All aspects were integrated in a decision model for managers to find out if partnership as the coordinative form is really the best choice in a given situation.

Keywords: Network competition; OEM-supplier-partnership; Governance mechanisms; Revenue distribution among the partners; Decision model

1. Introduction

The formation of partnerships with the aim of improving competitiveness for all partners is currently the subject of intense debate. In any marketing related journal, one constantly encounters "hymns" about partnerships as the ideal coordination mechanism for suppliers in a value-creating network. Two reasons above all, are likely to be responsible for the renaissance of this not necessarily new idea (e.g., Axelsson & Easton, 1992; Hakansson, 1989; Johanson & Hallen, 1989; IMP conference proceedings between 1990 and 1999):

(i) The first reason derives from an observation in the sector of goods with network effects, of which there are progressively more over time. Due to interface incompatibilities between products in different networks, the very powerful binding effect on the customer means that it is no longer products, but complete systems that compete with one another. We are experiencing increasing competition between standards and the successful implementation of such standards determines market success. For example, someone who already owns a camera with a Sony memory stick, will also consider buying a mobile phone from Sony Ericsson or a laptop from Sony in order to use the memory stick for these other appliances as well (Katz & Shapiro, 1994).

(ii) The second reason lies in the development of relationships between OEM's and their suppliers. In order to evade the rising pressure from OEM's for greater efficiency, suppliers have developed very effective strategies which, in some cases, impact negatively on the quality and reliability of future products of OEM's. Reversing this trend, while at the same time maintaining the pressure to be efficient, currently ties up substantial resources in monitoring and controlling enterprises — by both suppliers and OEM's. Against this background, a partnership among peers *without* massive monitoring activities on both sides seems to constitute an insurmountable obstacle. A value-creating network can only be mutually successful where likeminded interests prevail for all parties (Jap, 1999). That is, it is necessary

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to achieve *joint* success in competing against rival value-creating chains or networks. In such a situation, it would indeed be possible to eliminate the bulk of monitoring costs (Gadde, Huemer, & Hakansson, 2003).

In fact, in several industries, the idea of a partnership in business relationships between companies within a value-creating network is becoming progressively more important (Dietl & Royer, 2003, Hunt & Morgan, 1994). Yet, within these networks, the entire range of potential relationships can be found: trustful partnerships (with relatively low levels of transaction costs because of less monitoring etc.) on the one hand and highly governed relationships embedded in a complex of contracts and monitoring activities – the '*classical style*' – on the other.

Against the background of these developments, a number of questions arise:

1. How exactly should one understand a partnership in a value-creating network? As a very special so-called hybrid governance mechanism, how can it be differentiated from the 'ordinary' forms of coordination according to Williamson (1985): market, hierarchy, 'classical style' business relationship?
2. Is partner-based coordination suitable for any business relationship? When and under what circumstances is this special form of coordination or governance advantageous?
3. What requirements must potential partners fulfill so that a partnership based coordination mechanism functions effectively? What are the drivers of stability for this form of coordination in the long run?

In this article, we intend to focus on the third group of questions. However, before proceeding to do so, we wish to reveal the underlying basis and general understanding of partner-based coordination. In contrast to most current positivistic research papers, this should be carried out with a normative impetus. As long as we are striving towards the most efficient and effective management solutions for OEM-supplier relations, a positivistic view – what is really done in the markets – is not sufficient. What can be learned from the available empirical investigations is that the degree of specific investments on the buyer and/or supplier side, is the most important driver for the choice of appropriate governance mechanism (Cannon & Perreault, 1999; Jap & Genesan, 2000) — that is, the suitable coordinative form and viable relationship form.

Accordingly, in the following section, partnership, as a special type of relationship seen as a governance mechanism, with its responsibilities and potential benefits, is differentiated briefly from other forms of coordination with respect to the buyer–seller relationship in general and the degree of specific investments in particular. The third section then deals with the characteristics of suitable suppliers for a partnership. The issue will be addressed as to what sort of supplier is likely to provide substantial advantages for this special form of coordination. This is the second aspect which differentiates this paper from many others. The problem of coordinating OEM-supplier relations is frequently seen from only one side — that of the OEM or the supplier (Cannon & Perreault, 1999; Jap, 1999). Here, we discuss the choice of coordination mechanism as a two-sided problem. Both parties must agree. Therefore, while considering a partnership as a suitable coordination mechanism, an OEM must take into account the situation of the supplier and vice versa. The fourth section turns to the issue of how the potential profits derived from a value-creating network should to be divided internally. This is an important stability factor within coordination mechanisms and therefore of considerable significance in terms of its sustainability. This aspect has largely been ignored in the literature up to the present. One of the few papers dealing directly with this problem is from Kulmala, Paranko, and Uusi-Rauva (2002). In contrast to our argumentation here and as a representative of the opinion in the literature up to now they see the cost management as the key for the revenue or profit distribution. The final fifth section integrates and transfers the results of the analysis into a decision model which tests supplier suitability for a partnership. Thus, the theoretical considerations can be converted into a normative decision tool for managers.

2. On the fundamentals of partnership-based coordination within a value-creating network

The discussion at issue is only really justified if the phenomenon is in fact new. Therefore, the new aspects need to be extracted and analyzed. The existence of different forms of governance between market and hierarchy is certainly *not* new (Anderson & Weitz, 1992; Heide & John, 1992; Lal, 1990; Lusch & Brown, 1996). These governance structures, referred to as hybrids by Williamson (1975, 1985) and Williamson (1991), have been debated intensely. According to the various investigations, several influential factors – the degree of specific investments, symmetry of investments on the side of OEM and supplier, phase of relationship life cycle, etc. – influence the choice of a special governance mechanism. Consequently, relationships are arguably the most prominent governance mechanism (Grönroos, 1999; Hakansson & Snehota, 1995; Heide & John, 1990). However, it is also true that the term relationship subsumes many different forms of explicit coordination. Therefore, when we talk about partnership, we mean a very special type of coordinative form under the banner of a broad understanding of the term relationship, which is defined in the following section (see Fig. 1).

The reason that partnerships constitute something special, lies more in the implications associated with the notion of competition between value-creating networks, than in the novelty of the monitoring problem (Farrell, Monroe, & Saloner, 1998). Competition between different networks will only work if the suppliers integrated into such a network, always operate in one market at a time and within one network. Acting on the assumption that each partner makes a contribution to the competitive advantage of the entire network, supplying other networks simultaneously would be counterproductive. The contribution to competitive advantage would