

**Title: Expectations concerning Potential Conflicts in Alliances and Implications to Trust Building**

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**Abstract:** This article explores contrasts in the expectations of different national groups of executives concerning possible conflicts in strategic alliances. Trust building is discussed as a crucial prerequisite to a successful alliance and the paper suggests that more than operationalising conflict resolution techniques, executives should be aware of different expectations of conflict.

**Key words:** Alliances, conflicts, trust

# **Expectations concerning Potential Conflicts in Alliances and Implications to Trust Building**

This article explores contrasts in the expectations of different national groups of executives concerning possible conflicts in strategic alliances. Trust building is discussed as a crucial prerequisite to a successful alliance and the paper suggests that more than operationalising conflict resolution techniques, executives should be aware of different expectations of conflict.

## **Introduction**

Recent evidence suggests that the success rate in international alliances in general is less than 40% (Spekman 1998). In the specific area of this study, biotechnology alliances, success rates are estimated to be slightly higher (Rule 1999). The importance of improving the success rates of strategic alliances cannot be underestimated for as Pascale (1999) points out, the need “to improve the hit rate of strategic initiatives” is the major challenge for corporations.

A way of attempting to minimise failure would be to avoid, or create mechanisms to deal with conflicts as early as possible in the process of allying. The identification of potential conflicts as a means of improving success rates is the main aim of this study. Relevant research concerned with perceptions and expectations that can impact alliances is discussed together with an explanation of the nature of trust. Evidence of the different expectations from two different national groups of ‘European’ executives contemplating biotechnology alliances in Brazil is presented and discussed. Finally the article proposes that conflict resolution techniques are insufficient to ensure success. Rather a prior analysis of expectations of conflict may be more beneficial.

Conflicts or problems between partners are to be expected in a collaborative venture. These are most likely to have arisen over the division of authority and decision making (Young *et al.* 1989). A number of authors (Stopford & Wells, 1972; Dong & Buckley & Mirza, 1997) have proposed a set of dimensions of partners' conflicts or problems. (These studies are summarised in table 1 below) These authors explored the views of foreign investors rather than those of both parties to an alliance. Young *et al.* (1989) point out three further associated problems:

1. disagreements over objectives and plans
2. the need for compromised decisions
3. a slowing down in the decision making process.

### **Trust**

Notions of trust are intrinsically connected to the time duration of the relationship. Trust may be seen as the result of the mutual fulfilment of arrangements between partners, or of the observation of those actions by spectators<sup>1</sup> (which would strengthen the actors reputations). In both cases trust develops during a certain period of time. In this study it is assumed that the developed country partner firm would not have much exposure to the emerging economy in focus, i.e. the Brazilian economy. Thus, in considering the expected contributions from an emerging economy partner firm at an early stage in the partnership process (consideration of the possible strategies to enter a market and the selection of a partner), trust does not seem to be something to be expected. In fact this "a priori" expectation of trust in a partner could lead to a higher disposition to the arrangement's failure (Buckley & Casson, 1988).

Moreover, in developing trust, Buckley & Casson (1988) point out the value of providing a series of decision making opportunities where the parties could be

exposed to conflicts between their own interests and those of their partner. Additionally, joint R&D that could be seen as the expected outcome after a series of less complex arrangements within two biotechnology partners, would depend on the sharing of ideas, and could lead to the sharing of values (Buckley & Casson, 1988).

It has been noted (Buckley & Casson, 1988) that uncertainty concerning the quality of the product could result in both partners reciprocally opening up their operations “after a certain degree of trust has been attained”, and in consequence establishing a natural route for the progression of their relationship.

One way to increase the speed of this process seems to be by increasing the exchange of information, and consequent creation of an increased exposure between partners.

Moreover, Dong *et al.* (1997) suggest that good co-operation between partners over key decisions areas such as accounting, marketing, pricing policy and quality control is very important to the success of International Joint Ventures (IJV). Additionally, Lane & Beamish (1990) advise that shared decision-making control (when decisions are shared between partners based on skill, experience, and understanding of the particular issue) is to be recommended in emerging economies. Moreover issues concerning shared decision-making should be agreed upon at the formation stage of the IJV. The same authors, associating size and decision making conflicts, conclude that: large foreign parents tend to be systematic and slow in the decision-making process, whereas local partners are usually entrepreneurs managing intuitively and taking strategic decisions very quickly. Local partners would be expected to have immediate financial needs. Moreover, Bower & Whittaker (1993b) affirm that contrasts in the corporate culture between large and small companies were more conspicuous in their study than national cultural divisions.

Using Child's account of a model of trust development by stages (1998), and using concepts of calculative and cognitive trust (Lane 1998)<sup>ii</sup>, it would seem that one problem that is still open to discussion is speeding up the passage from the initial stages of trust (calculative) to cognitive trust, so that the partner behaviour becomes predictable.

**Table 1: Potential Conflicts in Alliances (From Stopford & Wells and Dong *et al*)**

POTENTIAL CONFLICTS	Stopford & Wells (1972)	Dong & Buckley & Mirza (1997)
1) Retention of earnings vs. dividends	Retention of earnings vs. dividends (1 o/10)	Dividend policy (MNC- 2 o/15) (OC- 4 o/15)
2) Export market allocation	Export market allocation (2 o/10)	Export and import (MNC- 8 o/15) (OC- 5 o/15)
3) Transfer prices for components or raw materials	Prices at which components or raw materials are sold to joint venture subsidiaries (3 o/10)	Purchasing (MNC- 7 o/15) (OC- 13 o/15) Accounting (MNC- 6 o/15) (OC- 1 o/15)
4) Marketing policies (distribution channels, customer financing, after sales service policy)	Distribution channels, customer financing, after-sales policy, or other mktg policies (4 o/10)	Marketing (MNC- 3 o/15) (OC- 7 o/15)
5) Budget for marketing and promotion	Amounts to be budget for marketing and promotion (5 o/10)	Budgeting (MNC- 13 o/15) (OC- 2 o/15)
6) Rationalisation of production among subsidiaries in a region	Rationalisation of production within a given area (6 o/10)	Production planning (MNC- 9 o/15) (OC- 12 o/15)
7) New product introduction	New product introduction (7 o/10)	product planning (MNC- 14 o/15) (OC- 11 o/15)
8) Pricing of products	Pricing of products of joint venture (8 o/10)	Pricing policy (MNC- 5 o/15) (OC- 10 o/15)
9) Product quality standards	Product quality standards (9 o/10)	Quality Control (MNC- 1 o/15) (OC- 14 o/15)
10) Brand names to be used	Brand names to be used (10 o/10)	
11) Royalty payments	Conflicts over royalty payments(*)	
12) Manufacturing facilities' expansions	Conflicts over expansion of plant(*)	Capital expenditure (MNC- 11 o/15) (OC- 3 o/15) Loan funds (MNC- 12 o/15) (OC- 6 o/15)
13) Local tax rules / concessions	Problems with local tax concessions(*)	
14) Management philosophy / practices	Differences in attitudes toward management philosophy(*)	Organisation (MNC- 15 o/15) (OC- 9 o/15) Management recruitment (MNC- 4 o/15) (OC- 8 o/15)
15) Labour relations	Differences in attitudes towards labour relations(*)	Wage / labour policy (MNC- 10 o/15) (OC- 15 o/15)

Notes: (1) The contributions (\*) were not assessed by the study, but they were suggested during the respective field work; (2) The figures in brackets represent the ranking of each of the studies of the degree of importance of each of the possible sources of conflict.

Table 2 presents a summary of differences in perception regarding conflicts in alliances based on the evidence in table 1.

<b>Table 2: Observed Differences in Perceptions of Potential Conflicts</b>		
<b>Key: ○ - similar; ✓ - different; ✓✓ - very different NA - not available</b>	<b>Differences due to timing or circumstance</b>	<b>Between Foreign Investors of Diverse Cultural Background</b>
<b>CONFLICTS BETWEEN PARTNERS</b>		
<b>1) Retention of earnings vs. dividends</b>	○	○
<b>2) Export market allocation</b>	✓	○
<b>3) Transfer prices for components or raw materials</b>	○	✓
<b>4) Marketing policies (distribution channels, customer financing, after sales service policy)</b>	○	○
<b>5) Budget for marketing and promotion</b>	✓	✓✓
<b>6) Rationalisation of production among subsidiaries in a region</b>	○	○
<b>7) New product introduction</b>	○	○
<b>8) Pricing of products</b>	✓✓	✓
<b>9) Product quality standards</b>	✓✓	✓✓
<b>10) Brand names to be used</b>	NA	NA
<b>11) Royalty payments</b>	NA	NA
<b>12) Manufacturing facilities' expansions</b>	NA	✓
<b>13) Local tax rules / concessions</b>	NA	NA
<b>14) Management philosophy / practices</b>	NA	✓
<b>15) Labour relations</b>	NA	✓

The table is the result of a comparison of the two studies. The conflicts that are perceived differently are highlighted. This was accomplished by grouping the dimensions of the differences into those that are seen to be due to cultural differences and those that may be due to differences in timing or circumstance. It was felt necessary to compare the studies in this manner as they were conducted at different times and included different cultural groups of respondents. Thus the comparison between the results of Stopford & Wells (1972) US MNC managers with the results of the interviews of MNC managers by Dong *et al.* (1997) generated the column “differences due to time or circumstance”. The comparison of the results in Dong *et al.* study between Overseas Chinese investors and MNC managers generated the other column (‘between foreign investors of diverse cultural background’).

As for the comparison, the set of results of each study was ranked, and the range of replies to each question was reconciled. If the difference was less than a third of the total range, it was classified as similar (“○”), if it was more than a third but less than two thirds it was classified as different (“✓”), and finally if the difference was more than two thirds it was classified as very different (“✓✓”). Using this simple technique for comparison, different ranges for the ranks (10 for Stopford & Wells, and 15 for Dong et al) were compensated.

For instance, the perceptions concerning the importance of potential conflicts between alliance partners was observed to be “very different” with regards to ‘pricing of products’ and ‘product quality standards’. As to the ‘pricing of products’ US MNC managers in the early seventies seem to allocate a lower importance as a source of conflict than MNC managers operating in China in the late 90's. A possible explanation could be the fact that US MNCs had a more centralised structure in the 70's, particularly regarding pricing decisions. In the 90's corporations have become more market orientated.

Considering ‘quality of products’, a similar explanation would seem to hold. In addition this could be associated with the relatively greater unwillingness to share decisions in the 70's: a joint venture partner from a developing country would be in a weaker position regarding decisions on quality standards, whilst partnerships have become more ‘democratic’ in the 90's.

Differences between foreign investors of diverse cultural background show higher differences were ‘budget for marketing and promotion’ and ‘product quality standards’ is concerned.

‘Budget for marketing and promotion’ seems to be perceived by OC managers as having a high potential to generate conflict, contrary to the view of MNC managers

form partner-firms. A possible explanation could be based on the accumulated experience of MNC managers and the use of established procedures or formulas (e.g., a percentage of the revenue is to be spent on promotion).

‘Product quality standards’ could induce even more interesting tentative explanations. The overseas Chinese managers seem in this context to share similar views as the US MNC managers of the 70’s. This could be linked to a gap of management mentality. I similar gap in business mentality was pointed out between biotech Brazilian managers and US managers of the 70’s in a previous work (see De Mattos 1997).

Thus, considering the results presented it would seem that perceptions of potential conflicts do differ among executives in at least two dimensions. It also seems plausible that the prior examination of potential conflicts could speed up the formation stage of the alliance by influencing the development of trust as shown in figure 1.

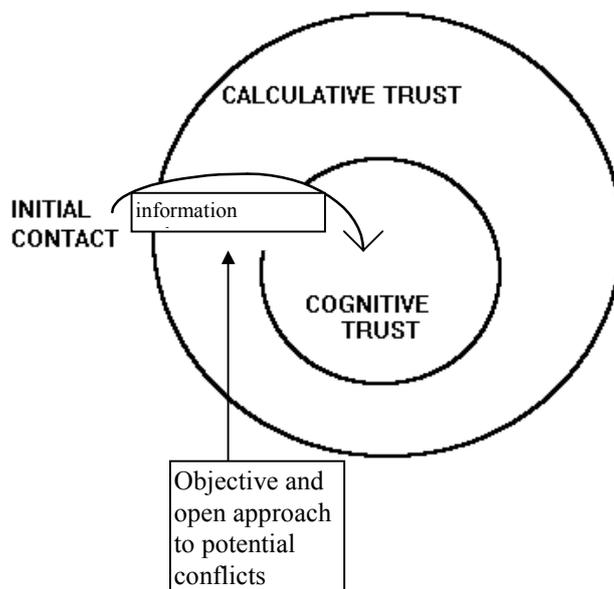


Figure 1: Trust in the formation stage of an International Strategic Alliance

## **The Environment of the Research**

Modern biotechnology as an emerging technology is part of the latest industrial revolution. Due to its enormous range of potential applications, it is believed that it can solve many of humanity's major problems: malnutrition, disease, energy and pollution (OTA, 1984)<sup>liii</sup>. It is seen as a very promising technology for sustainable development in the next century (FT<sup>iv</sup> 23.10.1997; EU White Paper 1994). Genetically engineered plants, for instance, seem to expand the possibilities for the environment to feed the increasing world population. However as a downside, this possible solution has generated a fierce opposition of some groups in developed countries (FT 17.10.1996). However, the markets for biotechnology related products, mainly chemical, pharmaceutical and agriculture, continue to attract investors of developed industrial countries due to the enormous rates of growth they are associated with.

## **The Survey and results**

### **Data Collection**

The data were collected by means of questionnaires completed in face-to-face semi-structured interviews. Respondents were then asked, by use of scaling techniques to determine of all of the potential conflicts which were the three most important.

A total of 55 interviews were carried out in 53 firms. Of the 55 interviews 29 were British executives (28 firms), and 26 German executives (25 firms)<sup>v</sup>. Most of the interviewed executives were managing directors and several of them could be classified as 'owner-managers' The UK firms were located mainly in the South of England. The German firms were contacted in three areas that are known to have a high concentration in the biotechnology sector: the Berlin area, the Dusseldorf area,

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1

and the Munich area.

Germany and the United Kingdom were selected for this study, because they are considered to be the two most active countries in the European biotechnology sector (Ernst & Young 1995). Brazil was chosen as representing emerging economies presenting large potential markets. Moreover, this choice was assisted by circumstantial knowledge of that country (the researcher has conducted previous studies of the Brazilian biotechnology sector).

Rank over frequency	European (55 exec.)	British (29 exec.)	German (26 exec.)
<b>1st</b>	Cf 14 (28) 51%	Cf 14 (18) 62%	Cf 9 (15) 58%
<b>2nd</b>	Cf 9 (23) 42%	Cf 5 (10) 34%	Cf 8 (12) 46%
<b>3rd</b>	Cf 8 (21) 38%	Cf4; Cf8 (9) 31%	Cf4; Cf 14 (10) 38%
<b>4rd</b>	Cf 4 (19) 35%	Cf 9 (8) 28%	Cf 3 (6) 23%

Key: Potential Contribution (frequency) % over respondents

Summary of the mentioned conflicts or problems:  
 cf1. Retention of earnings vs dividends; cf2.Export market allocation; cf3.Tranfer prices;  
 cf4. Marketing policies; cf5.Budget for marketing and promotion;  
 cf6. Rationalisation of production among subsidiaries; cf7. New Product Introduction;  
 cf8. Pricing of products; cf9. Products quality standard;  
 cf10.Brand names to be used; cf11. Royalty Payments;  
 cf12. Manufacturing facilities' expansions; cf13. Local tax rules concessions;  
 cf14. Management philosophy / practices; cf15. Labour relations.

Difference in Percentual Frequency  
 Less than 10 percentual point differences not always represented

### ***The four most frequent choices in each group of analysis***

This section examines the potential (future) conflicts that were selected as “of greatest importance” to the establishment of an alliance with an Emerging Economy Partner Firm (EPPF). Three (3) groups of analysis are used here, depending on which cases are grouped together. Thus the groups of analysis are: Fifty-five (55) ‘European Executives’ of which twenty-nine (29) were British executives (BE), and twenty-six (26) German Executives (GE). The analysis emphasises the responses up to the fourth rank of frequency distribution for each group as shown in Table 3. It is assumed the upper ranks portray the executives’ main worries concerning expected conflicts. The analysis tries to identify contrasts focusing on the four higher ranks in frequency.

Although table 3 displays more information, the analysis focuses on the differences between the BE and the GE.

Several differences in perceptions relative to potential conflicts in Alliances were identified. The most relevant contrasts between BE and GE (table 4) are highlighted below. Firstly the item “products quality standard” (cf9) is pointed out by 58% of GE (1st rank), whereas by contrast only 28% of BE (4th rank) indicated it. A German manager justifies his view: “we Germans always think that the highest quality (products) can be produced in Germany and other countries of EU, and quality standards in countries like Brazil...; they are bad.”

Secondly 62% of BE chose “management philosophy / practices” (cf14) as a conflict “of greatest importance” (1st rank), contrasting with only 38% of GE (3rd rank). This aspect could be illustrated by a comment from a British manager: “That could be a potential problem, couldn’t it? Because if you are thinking of an emerging country that has a completely different view (on management)...”, or the opposite view by the

pointed response of a German manager: “(No,) I don’t think... this is an important thing.”

Other differences were identified however as they were not significant, can only be contemplated as indicative: (3) Forty-six per cent of GE chose “pricing of products” (cf8), whereas only 31% of BE did so; (4) BE contrary to GE, placed among the four higher levels the item “budget for marketing and promotion” (cf5); (5) GE, contrary to BE, placed “transfer prices” (cf3) among the four higher levels of frequency. Basically the main concerns of GE seem to surround product related matters (quality, pricing), whereas BE seem to be concerned with management and marketing aspects. The former seems to corroborate the “product directed” strategy of GE.

The main results are summarised below in table 4.

**Table 4: Contrasts between BE and GE relative to conflicts “of greatest importance” in the four higher levels in frequency**

Conflicts “of greatest importance”:		% Δ
• Products quality standard	GE=58%; BE=28%	30 (p<0.05)
• management Philosophy / practice	BE=62%; GE=38%	24 (p<0.1)

**Implications and procedures for research and practice: Increasing awareness of expected conflicts:**

What this paper has attempted to show is that the potential of any trans-national alliance can be significantly influenced by the perceptions and expectations of the principal parties involved. More specifically the potential areas for mistrust and conflict can be isolated and defined and that their source is rooted in differences in national culture and business practices. National differences may be blurred when

outsiders fail to spot the subtleties that exist between countries in the same region for example, in Europe or South America.

However, the process of isolating and dealing with the various potential areas of conflict by constructing checklists from the literature may be termed a technical or calculative solution. The use of such lists can assist in trust building and in pre-emptive moves by either party. Some authors have pointed out there may be a level beyond this where trust has to be built on a more cognitive foundation through the creation of an understanding and empathy for the cultural influences on expectations and perceptions of potential partners. This, it is argued can be brought about through a deeper understanding by both parties of the cultural determinants of their perceptions and expectations and the consequent effects on developing trust. There may be a level beyond the cognitive which is more emotional but that is beyond the scope of this paper

In essence predicting likely situations with checklists of areas of potential conflict is dealing with the symptoms of mistrust whereas dealing with the cultural differences and drivers is an attempt to get at the cause.

The limitations of the research are important and should be considered when extrapolating results of this study to other situations or countries. Executives should consider that these findings represent a picture of a moment in time.

The implications for policy makers are that the existing differences in perceptions among executives suggests that these might also exist between executives in the industry, and governments keen to promote alliances. In the process of fostering co-operation between these groups, governments should accommodate the potential for conflict. For instance, one way of avoiding conflicts would be the discussion of listed general contributions each party could expect.

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## Notes:

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<sup>i</sup>Buckley & Casson (1988)

<sup>ii</sup> 'Cumulative trust' involves expectations about another, based on calculation which weigh cost and benefits of certain courses of action. The latter depending on the availability of information. 'Cognitive trust' is based on the sharing of cognition, which provides the basis for predicting the partner's line of thoughts (sharing of ideas). (Lane 1998)

<sup>iii</sup> OTA abbreviates 'Office of Technology Assessment'.

<sup>iv</sup> FT abbreviates 'Financial Times'.

<sup>v</sup> **British, and German** refer to executives operating respectively in the United Kingdom, and Germany. However the nationalities follows the respective country of operation in the United Kingdom. In Germany two firms had non-German executives who had nevertheless been living in that country for more than 15 years.