

**WORKING PAPER SERIES ON  
RESEARCH IN RELATIONSHIP MANAGEMENT**

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An Integrated Perspective**

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<b>WORKING PAPER SERIES ON RESEARCH IN RELATIONSHIP MANAGEMENT</b>	
Reference number	RRM-2004-03-STR
Publication status / version	January 2004
Email address contact author	<a href="mailto:g.ziggers@nsm.kun.nl">g.ziggers@nsm.kun.nl</a>
URL (electronic version)	<a href="http://www.nsm.kun.nl">http://www.nsm.kun.nl</a>
Address	Nijmegen School of Management University of Nijmegen Thomas van Aquinostraat 1 P.O. Box 9108 6500 HK Nijmegen, The Netherlands Phone: +31 (0)24 361 14 07 Fax: +31 (0)24 361 19 33

# **Alliance Capabilities and Relational Capital: An Integrated Perspective**

Gerrit W. Ziggers\*, Geert Duysters\*\* <sup>1</sup>

\* University of Nijmegen  
P.O. Box 9108  
6500 HK Nijmegen  
The Netherlands  
G.Ziggers@nsm.kun.nl

\*\* Eindhoven Centre for Innovation Studies (ECIS)  
P.O.Box 513  
5600 MB Eindhoven  
The Netherlands

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<sup>1</sup> The authors gratefully acknowledge the financial support from KLICT

# Alliance Capabilities and Relational Capital: An Integrated Perspective

## Abstract

Over the past decades alliance activity among companies has reached unsurpassed levels. In spite of this strong increase in alliance activity, success rates of alliances have been surprisingly low. In this paper we study two main lines of research that aim to explain alliance performance; i.e. research that stresses the role of trust and personal interaction in inter-organizational relationships and research that points at the role of alliance competence as a main driver of alliance success. More in particular, we focus on the interplay between a firm's alliance capability and its relational capital. It is argued that relational capital and alliance capability are important constructs of alliance success. By studying the interrelations between these constructs and their effect on alliance performance we are able to provide some important insights in how firms can manage their inter-organizational relationships more effectively.

**Keywords:** Strategic Alliances, Alliance Capabilities, Alliance Management, Social Capital

## 1. Introduction

During the past two decades alliances have become one of the most important organizational forms, as shown by the fact that more than 20.000 alliances have been reported within a time frame of two years (Anand and Khanna, 2000). Alliances are often considered an important vehicle for value creation. (Chan et al., 1997; Anand and Khanna, 2000). The rapid proliferation of alliances has become a cornerstone of competitive advantages for many organizations. Competition through cooperation has become a key element of a firm's strategy to gain advantages and create value. As a result it has paved the way for the introduction of a new form of competition: group versus group rather than firm versus firm (Gomes-Casseres, 1994; 2000). Gomes-Casseres (2000) and Doz and Hamel (1998) have been among the first authors to point at the increasing frequency of collaboration as a reflection of a fundamental shift from the traditional form of competition (firm vs. firm) to a new form (group vs. group). Garcia-Pont (1992) postulates that an individual need for access to strategic resources, which are required for industry survival but not held by a single firm, will lead to new forms of alliances (strategic blocks). Such a collective strategic block of alliances represents an accumulation of those scarce and highly valued resources and capabilities which are accessible at both an individual and group level and which serve to tie individual firms in an industry into a much larger system of exchange (Garcia-Pont, 1992). Vanhaverbeke and Noorderhaven (2001) suggest that such competitive arrangements represent a new form of rivalry, in which firm-to-firm competition is superseded by group to group rivalry.

As firms increasingly attempt to access or absorb the capabilities of other firms, inter-firm alliances have become commonplace. An alliance can be defined as any independently initiated inter-firm link that involves exchange, sharing or co-development (see Gulati, 1995). Alliances can take many forms such as production agreements, marketing or distribution agreements, and technology exchange agreements. Furthermore, in a range of studies over the past twenty-five years the existence of tangible relationships between firms that are connected together to form a “quasi-organisation” has been observed (see i.e. Iacobucci, 1996; Laage Hellman, 1997; Ford et al., 1998; Sheth and Parvtiyar, 2000). These relationships are likely to be complex and have a long term orientation. Moreover, their current form is the outcome of previous interactions. These alliances enable firms to cope with their increasing technological dependence on others and the need to develop and tailor offerings to more specific requirements. Technologies are both developed and exploited within them (Lundgren, 1995; Ford and Saren, 1996). Although alliances have become a popular organizational form for accessing resources, they frequently fail to live up to expectations. Studies by Bleeke and Ernst (1993), Harrigan (1985), Kogut (1989) and Anderson Consulting (Alliance Analyst, 1998) report failure rates of 50%, 54% and 53% respectively. Previous research suggests that alliance failure can be attributed to a diversity of factors. Among the most frequently addressed factors are; a lack of strategic fit in terms of complementary resources (Harrigan, 1985), lack of organizational fit in terms of compatible cultures, decision-making processes and systems (Kale, Singh and Perlmutter, 2000), lack of trust (Arino and De la Torre, 1998), inappropriate choice of governance structure (Williamson, 1998; Hennart, 1988), inability to manage conflict (Doz and Hamel, 1998), lack of adaptable inter-organizational exchange processes (Zajac and Olsen, 1993), impact of sudden major environmental shocks (Mitchell and Singh, 1996). Taken together, these studies indicate that alliance success is difficult to achieve. Thus while alliance can create economic value and are a mean for competition, they are also fraught with risk. Therefore, understanding what firms can do to enhance the probability of success is an intriguing and important question for both managers and alliance researchers alike.

An important body of literature in alliance research (e.g. Morgan and Hunt, 1994; Dwyer et al., 1987) argues that trust plays a central role in relationship building and maintenance, thereby contributing to the probability of alliance success. Trust leads to co-operative behaviour that is conducive to alliance success. The alliance between Wal-Mart and Procter&Gamble in the United States is a typical example of the power of trust in

transforming channel relationships and in unleashing the benefits of partnerships (Kumar, 1996). Similarly, in Europe, Albert Heijn and Heineken, as well as Marks & Spencer and its suppliers have developed relationships based on mutual trust (Geyskens et al. 1998). Trust is considered as an essential ingredient for such relationships to realize their full potential. Morgan and Hunt (1994) presented a 'key mediating variable' model in which trust is positioned as a key variable, mediating the relations between important antecedents (e.g. communication) and consequences (e.g. conflict). The mediating role of trust is also implicit in other studies, examining the relation between various antecedents and consequences (e.g. Ganesan, 1994; Anderson and Narus, 1990). These studies do not suggest that trust accounts for the total effect of antecedents on relationship consequences, but that trust acts as an important mediator. (Geyskens et al, 1998). Critical to establishing the key role of trust in affecting important relationship outcomes (such as satisfaction and commitment) is to rule out other explanations. According to Geyskens et al. (1998) behavioural processes involving trust are crucial to understand co-operative relationship building and are certainly not redundant once its antecedents, and more in particular economic outcomes are taken into account. The importance of issues such as trust, but also friendship and respect, is often referred to as relational capital (Coleman, 1990).

The insights generated by these types of studies refer mainly to critical aspects in the dyadic relationship, but have been unable to assess the factors that determine performance across a portfolio of alliances (Kale and Singh, 1999; Duysters et al., 1999). As a consequence, in spite of their important contributions these studies are unable to explain the reported fixed-firm effects in individual firm's alliance performance (Duysters and Heimeriks, 2002). In more recent work other theoretical perspectives, e.g. evolutionary economics (Nelson and Winter, 1982; Lewin and Volberda, 1999), organizational learning and knowledge based theory (Conner and Prahalad, 1996; Grant, 1996), resource based theory (Wernerfelt, 1984; Barney, 1991; Das and Teng, 2000), have been used to deal with this omission in the traditional literature. These theories point to organizational capabilities rather than to dyadic and relational characteristics in order to explain alliance success. From these perspectives previous research suggests that one of the most important determinants of alliance success (and on a firm's ability to form new alliances) is prior and/or ongoing alliance experience (Fiol and Lyles, 1985; Child and Yan, 1999). Simonin (1997) found that greater alliance experience is linked with firms 'abilities to effectively select alliance partners and to manage conflict. More recently, Anand and Khanna (2000) found that firms with greater prior alliance

experience generate significantly higher stock market returns from alliance announcements than firms without alliance experience. They claim that firms learn to create more value as they accumulate experience in joint venturing. Even in the context of the same set of partners, some studies suggest that repeated tie arrangements by allying with the same partner helps the partnering companies in future alliances. Presumably, prior experience of this kind increases the success of future alliances with the same partners for several reasons. First of all, the firm in question may have greater commitment to make the alliance work given the trust among partners. Furthermore prior experience helps firms to effectively build partner-specific routines of coordinating resources and tasks (Kale et al. 2002). The implicit assumption behind the relationship between the presence of an alliance capability and success is that there are learning effects that enable firms to develop relational capital (Dyer and Singh, 1998). In the area of alliances, Hewlett-Packard, Corning and Coca-Cola have been described as firms that have been particularly successful at developing and managing alliances (Alliance Analyst, 1996; Harbinson and Pekar 1998; Kale and Singh, 1999). Anecdotal data and case-based studies have also provided support for the argument that some firms learn how to develop and manage alliances more effectively than others (Alliance Analyst, 1996, Dyer, 1996).

Although there have been ample studies on the central role of relational capital in alliances at the dyadic level (e.g. Geyskens et al, 1998; Morgan and Hunt, 1994; Anderson and Narus, 1990; Dwyer et al., 1987) and more recently on the role of alliance capability (e.g. Kale et al, 2002, Lambe et al., 2002; Anand and Khanna, 2000) at the firm level, an integrative approach providing insight to the critical aspects in the dyadic relationship, the fixed firm's effect and their interrelationship in alliance success is needed. An individual firm's ability to work effectively with other firms may be classified as a firm specific capability (which may generate relational rents), however there is value in distinguishing a relational capital view, which offers a distinct, but complementary, view on how firms generate rents. A relational capital view considers the dyad/network as unit of analysis and the rents that are generated to be associated with the dyad/network. A firm's specific capability focuses on how individual firms generate supernormal returns based upon resources, assets and capabilities that are housed within the firm. However, according to a relational capital perspective, rents are jointly generated and owned by partnering firms. Thus, relational rents are the property of the dyad or network. A firm in isolation, irrespective of its capabilities or resources can not enjoy these rents. (Dyer and Singh, 1998). Besides, these relational rents offer allying firms to gain

competitive advantage. Thus, on one hand an alliance capability is not a sufficient condition for realizing relational rents, on the other hand it is a prerequisite for realizing relational capital. This implies also that an analysis either on the level of the individual firms, dyad or network will fail to produce an understanding of the nature of competition shaping the industry. Instead competitive advantage must be understood as 'not only the result of firm based characteristics but also as the features of the alliances or network to which the firm belongs' (Vanhaverbeke and Noorderhaven, 2001). As Zajac and Olsen (1993) have argued, all parties use inter-organizational strategy to establish an ongoing relationship that can create value that could otherwise not be created by either firm independently. As a consequence alliance success itself can be considered as a three level construct, that includes a firm level success (the extent to which a firm has access to an other firm's resources), an alliance level success (the extent to which allying firms have effectuated their joint objectives) and industry level alliance success (the extent to which the alliance has succeeded to increase its competitiveness or attractiveness). The interplay of both alliance capital and relational capital and their impact on alliance success has not widely been discussed previously in the literature. Therefore the primary purpose of this study is to examine the impact of a firm-level alliance capability and a dyadic/ level relational capital on alliance success. In the following sections the main conceptual arguments of alliance capability and relational capital are discussed on the basis of a review of the relevant academic literature. Finally implications are discussed in the perspective of the firm, alliance and network level as well as directions for future research.

## **2. Alliance capability and alliance success**

Effective alliance management is of eminent importance. However, the ex-ante structuring of alliances is important as well. This is reflected in the extensive literature on topics such as partner selection and characteristics (e.g. Parkhe 1993, Geringer, 1991), performance effects of ownership and control (e.g. Geringer and Herbert, 1989; Beamish 1985). The underlying premise of these studies is that choosing the appropriate partner, aligning strategic and economic incentives of the partner firms and using ownership control have proven to be critical determinants of alliance success, and have been shown to mitigate the risk of opportunistic behaviour (Aulakh et al. 1996). Researchers argue that both relational factors (e.g. trust, commitment and satisfaction) and non-relational resources (e.g. complementary and idiosyncratic) contribute to partnership success. However this does not reveal how alliances successfully acquire and create the complementary and idiosyncratic resources that facilitate competitive advantage and superior (financial) performance. Moreover, it lacks a

sufficient understanding of the ability for finding developing and managing alliances: an alliance capability (Lambe et al., 2002).

Evidence suggests that there may be systematic differences in the co-operative capabilities that firms build up as they have more experience with alliances and that the extent of this learning may be an important indicator of the relative success of those firms with alliances (Lyles, 1988). This poses questions about the specific nature of these capabilities and the systematic tactics firms use to internalise such capabilities. Some of these capabilities have already been reported in the literature; i.e. identifying valuable alliance opportunities and good partners, using appropriate governance mechanisms, developing inter-firm knowledge-sharing routines, making requisite relationship-specific asset investments and initiating necessary changes to the partnership as it evolves while also managing partner expectations (Dyer and Singh, 1997; Doz, 1996)

From a theoretical perspective the organisational learning, dynamic capabilities and evolutionary economics literature offer some of the most useful insights with regard to capability development, since capabilities often rest upon unique sources of knowledge (Kale et al. 2002). Organisational capabilities develop as a result of recombining and/or integrating knowledge within the firm. This knowledge is typically built through learning that involves making associations between a firm's past actions, the effectiveness of those actions and future actions (Fiol and Lyles, 1985). According to Lambe et al. (2002) alliance capability has three main facets 1) alliance experience, 2) alliance manager development capability and 3) partner identification propensity. Experience with alliances is a resource that can be leveraged across an organisation, because it contributes to knowledge about how to manage and use alliances (Simonin, 1997). Day (1995) noted that such experience contributes to the quality of a firm's 'alliance management' by, among others, improving their abilities with respect to "selecting and negotiating with potential partners" and "planning the mechanics of the alliance so that roles and responsibilities are clear cut". Much of the knowledge about finding, developing and managing alliances is "tacit" (Polanyi, 1996), and firms must learn by doing (Anand and Khanna, 2000; Day 1995; Spekman et al. 1999). As a consequence firms should expect some of their initial attempts to create alliances to fail. Thus, firms' initial attempts should be focussed on relatively noncomplex alliances. More ambitious alliances can then be undertaken when experience builds over time (Spekman et al. 1999; Lambe and Spekman, 1997). In this line of reasoning, one could argue that firms might hire external support to fill



the experience gap. However, recent findings of Duysters and Heimeriks (2002) show that external parties did not play a significant role in determining alliance success. They argue that distinctive competitive advantage cannot be distilled from the mere possession of certain mechanism. It requires the development of managerial capabilities as well as difficult-to-imitate combinations of organisational, functional and technological skills.

Day (1995) and Spekman et al (1996) suggest that firms with an alliance competence have the ability to develop capable alliance managers. These managers then enable firms to plan and navigate the mechanics of an alliance so that roles and responsibilities are clearly articulated and agreed upon. Simonin (1997) stated that the lower-than-average failure rate of joint ventures in the oil industry can be linked to the fact that managers have learned the essentials of collaboration. Lambe et al (2002) draw the conclusion that competent alliance managers will negotiate structure and operate alliances in ways that allow such firms to secure attractive alliance partners and to minimise the chances of alliance mismanagement such as poor conflict resolution. Furthermore, they will work with their partner firms on successfully combining and synthesising their complementary resources into idiosyncratic resources that may well lead to competitive advantage.

Firms that have an alliance competence systematically and proactively scan and identify partners that have the complementary resources that are needed to “develop” a relationship portfolio or mix that complements existing competencies and enables them to occupy positions of competitive advantage (Hunt, 1997). Firms that can identify such partners not only enhance their ability to compete but also improve their chances of alliance success (Dyer and Singh 1998; Lambe et al, 2000; Simonin 1997; Sivadas and Dwyer 2002). In addition, Varadarajan and Cunningham (1995) and Day (1995) suggested that firms that scan for promising partners may also often achieve an alliance ‘first-mover’ advantage that allows them to gain access to and pre-empt competition from scarce resources offered by potential alliance partners. Day (1995) argues that a firm that is adept at identifying, consummating, and managing strategic alliances is likely to have first mover advantage in bringing the best candidates into the relationship.

A study of Kale et al. (2002) indicates that when a firm makes an investment in a dedicated alliance function designed to capture and apply the know-how from its alliance experience, its alliance success rate increases. They found that a firm’s investment in a dedicated alliance

function is a more significant predictor of the firm's overall alliance success experience than a firm's alliance experience. If accounted for self-selection, the effect of alliance experience on alliance success diminishes. This result has important implications for prior research that has focused on alliance experience as an important explanatory of alliance capability and success. Kale et al. (2002) come to the conclusion that although alliance experience is important it seems to facilitate through the creation of a dedicated structure to co-ordinate and leverage that experience more effectively. Having such a function can improve firms' alliance abilities so as to be able to identify appropriate alliance partners, screen alliance partners more effectively, attract alliance partners that are stronger and more compatible, and eventually present and position the alliance more appropriately to the external world of customers, competitors and investors. Most alliance functions seem to capture and codify knowledge to more effectively manage each phase of the alliance life cycle, being 1) the initiating stage (e.g. making the business case), 2) the development stage (e.g. designing alliance governance structure) and 3) the maturity stage (e.g. relationship evaluation) (see also figure 1).

Organisational experience with alliances contributes to a firm's knowledge of how to successfully form and implement alliances (Simonin 1997; Spekman et al 1999). Firms having such experience will improve their ability to select, negotiate and structure alliances so that they can secure alliance partners that have complementary resources (Spekman et al. 1999; Day 1995). An alliance competence implies that a firm produces capable alliance managers, it facilitates the ability of such firms to select and secure alliance partners that have complementary resources because alliance managers are often involved in initial negotiating and structuring of alliances (Spekman et al. 1999). An alliance competence will have a positive effect on complementary resources because it enhances the competency to identify potential alliance partners with complementary resources (Sivadas and Dwyer 2000; Spekman et al 1999; Dyer and Singh 1998, Simonin 1997). Lambe et al. (2002) conclude that an alliance competence is a key antecedent to complementary resources, idiosyncratic resources and alliance success. An alliance competence allows firms to acquire and combine their most basic resource advantage in a fashion that contributes to alliance success. This is considered to be an important finding that is likely to assist firms that wish to better understand the drivers of alliance success. In addition, identifying an alliance competence as a key antecedent of alliance success, is critical to study alliances because it contributes to a more complete explanation of its success

To summarize, a firm's alliance capability is conceptualised as an organisational ability for finding suitable partners and developing and managing alliances. Furthermore, if all partners in an alliance have an alliance capability (joint alliance capability) then they will work together more effectively than in an alliance where an asymmetric or unbalanced alliance competence exists. In other words an unskilled alliance partner can diminish the ability of the alliance partners to work together and make necessary resource investments in the alliance to create alliance value. For example, a firm, even one with a high degree of alliance competence, will have problems working with an alliance partner that cannot manage inter-firm cultural differences. Hence, it is likely to have difficulties co-ordinating activities with another firm, sharing control, and face problems in information sharing and the ability to attract the necessary investments in the alliance (Lambe et al. 2002; Sivadas and Dwyer 2000; Spekman et al. 1999). Hence, although it might be argued that one competent alliance partner can have a positive effect on the other, research indicates that the know-how required to be a competent alliance partner is complex and requires years of alliance experience (Anand and Khanna, 2000; Spekman et al, 1999; Lambe and Spekman, 1997; Simonin 1997; Day 1995). When all of the firms in an alliance have an alliance competence, there is a synergistic benefit that enhances the ability of the alliance to work together and to create value (Lambe et al. 2002). This might eventually lead to a more competitive position as a group of allying firms (see also figure 1).

### **3. Relational capital and alliance success**

The alliance literature has focused extensively on partner opportunism and most researchers have adopted a transaction cost economics perspective in an attempt to deal with this particular aspect (Hennart, 1988; Kogut, 1988; Pisano, 1989; Williamson, 1991). Firms' concerns about opportunistic behavior by their partners are likely to lead to high transaction costs and it has been suggested that firms can adopt appropriate contractual agreements or governance structures to address these concerns. Using transaction cost economics, scholars have identified two sets of governance properties through which equity alliances can effectively alleviate the transaction costs involved. One is the property of a 'mutual hostage' situation, in which shared equity aligns the interests of the partners involved. Since partners are required to make ex ante commitments to equity alliances, their concern for their investments reduces the possibility of opportunistic behavior over the course of the alliance (Pisano, 1989). Second, in equity alliances, the investing partners create a hierarchical supervision not only to oversee the day-to-day functioning of the alliance, but also to address

contingencies as they arise (Kogut, 1988). Numerous researchers have criticized the transaction cost economics perspective on alliances for its singular focus on partner opportunism and its advocacy of the use of contractual agreements or equity to resolve it. This approach fails to capture an important element in alliance partnerships, namely the role of interfirm trust and the evolution of interpartner relationships (Gulati, 1995)

'Trust' has been referred to in the literature in many different ways. First, it is considered 'a type of expectation that alleviates the fear that one's exchange partner will act opportunistically' (Bradach and Eccles, 1989). Offering a slightly different emphasis, Madhok (1995), suggests that trust between exchange partners has two components: a structural component which is fostered by a mutual hostage situation, and a behavioral component, which refers to the degree of confidence that individual partners have in the reliability and integrity of each other. Similarly, Gulati (1995) differentiates among knowledge-based trust and deterrence-based trust. Knowledge-based trust emerges between two firms as they interact with each other and learn about each other. Deterrence based trust is based on utilitarian considerations which lead a firm to believe that a partner will not engage in opportunistic behavior, owing to the costly sanctions that are likely to arise. Cullen (2000) differentiates credibility trust from benevolence trust, one rational and the other emotional (Kramer, 1999; Moorman et al. 1993). Credibility trust, the rational component of trust, is the confidence that the partner has the intent and ability to meet their obligations and make their promised contributions to the alliance (Johnson et al. 1996). It concerns beliefs about whether or not a partner can really deliver what they promise. Benevolent trust is the belief that an alliance partner will behave with goodwill toward the alliance and the partners (Johnson et al, 1996). Benevolence is the subjective or emotional side of trust. It refers to one's beliefs regarding a partner's caring about the relationship. Overall, there is an emerging consensus among alliance scholars that mutual trust creates the basis for an enduring and effective relationship between contracting firms. For example, Gulati (1995) shows how trust enables firms to reduce dependence on equity structures to govern the relationships. Zaheer et al., (1998) demonstrate how trust reduces negotiating costs in alliances and also enhances alliance performance. Trust between organizations has often been conceived as the agglomeration of trust between individuals in the organizations.

Numerous examples highlight the existence of stable obligatory relationships based on trust between individual members of the partnering firms. Accounts of the industrial districts in

Italy (Piore and Sabel, 1984), of subcontracting relationships in the Japanese textile industry (Dore, 1983), and those in the Japanese automobile industry (Dyer, 1996) highlight this aspect. The premise is that, as firms work with each other trust is built among individual members of the contracting firms because of the close personal ties that develop between them (Macaulay, 1963). Such trust is based upon close interaction and relationships that develop at the personal level. It is akin to the knowledge-based trust referred to by Gulati (1995) or the behavioral-based trust referred to by Madhok (1995). A history of close relationships helps individual members develop such trust in their counterparts in the partnering firm. Relational exchange theory (Dore, 1983) in economic sociology also discusses how personal relationships based on trust arise and exist between firms. Palay (1985) and Ring and Van de Ven (1992) have also pointed out the important role of personal connections and relationships between contracting firms. The combination of mutual trust, friendship and respect is often referred to as relational capital. Relational capital in the alliance is considered as the quality of the relationship that exists between social actors (Coleman, 1990). Relational capital consists of the socio-psychological aspects of the alliance, more specifically those socio-psychological aspects that are positive and beneficial to the alliance. It involves the pattern of interaction between partner firms that facilitates and allows for the effective functioning of the alliance on a day to day basis. It is through relational capital that the alliance is actually enacted and implemented. Relational capital involves having alliance partners attend to and invest time and effort toward building positive feelings and interaction patterns in the alliance relationship. Although often ignored completely or subordinated as secondary to financial considerations, an alliance cannot optimise performance without adequate relational capital (Cullen et al, 2000).

#### **4. The role of relational capital in alliances**

An additional reason for relational capital being important in alliances is associated with the aspect of learning, often cited as one of the major benefits and motivations for alliances. Firms that wish to absorb critical information or know-how from their alliance partner must first understand where the relevant information or expertise resides in its partner and who possesses it (Dyer and Singh, 1998). Close personal interaction between the partnering entities enables individual members to develop this understanding. Learning or transfer of such know-how is then contingent upon the exchange environment and mechanisms that exist between the alliance partners. Know-how is generally more sticky, tacit, and more difficult to codify than information and thus more resistant to easy transfer, both within and across firms

(Szulanski, 1996). However, Von Hippel (1988) and Marsden (1990) have argued that close and intense interaction between individual members of the organizations involved acts as an effective mechanism to transfer or learn sticky and tacit know-how across the organizational interface. Learning success also rests upon an iterative process of exchange between the member firms and the extent to which personnel from the two firms has direct and intimate contact to facilitate an exchange (Arrow, 1974; Badaracco, 1991). A social exchange approach provides the basis for such interaction and exchange. Strong relational capital usually engenders close interaction between alliance partners. It can thus facilitate exchange and transfer of information and know-how across the alliance interface.

The concept of relational capital becomes even more complex and dynamic when viewed in terms of interactions and responses of partners to each other in the relationship, that is from the dyadic perspective rather than the individual firm's perspective. In this case, the issues involve mutual trust and mutual commitment. As in all business interactions, the building of trust and commitment depends on the partners' signaling to each other and the interpretation and response to this signaling in the relationship (Butler, 1991; 1995). Most experts who study business negotiations believe that trust in relationships, such as those between alliance partners, builds in through a feedback pattern called a "trust cycle" (Butler, 1995; Zand, 1972). Just as individual people in personal relationships, partners in (strategic) alliances often feel vulnerable in the initial stages of the relationship (Neale & Bazerman, 1992). Firms often begin a relationship suspicious of each other's motives. This early vulnerability and suspicion makes partners tentative in their involvement in the relationship and reluctant to reveal true motives, business "know-how," or technology. For example, typical fears and questions include the following: Do they want to steal our technology? Are they trying to take us over? Are we creating a new competitor? Are we giving away too much proprietary knowledge? Will they or can they provide what we agreed on? If this reluctance is apparent in the firm's behavior and interactions with the partner firm, it can be interpreted as distrust. In turn the partner firm will reciprocate with distrust in their feelings and behaviors. Obviously, such a pattern in the signaling between partners makes trust building difficult. In fact, such early signaling may set a cycle of distrust into motion in the relationship. Conversely, by their behaviors and interactions in the relationship, partners in the alliance can signal trust of each other, thereby setting in motion a positive cycle. Examples include delivering more than expected in the exchange, concessions in negotiations, forbearance in the wielding of power even if justified, accommodation and flexibility when the partner faces organizational crises.

In addition, strong information sharing can signal trust and trustworthiness in alliance relationships. In related research, interviews with managers showed that trust signaling symbols can involve behaviors suggestive of openness and receptivity in communication patterns, fairness and discretion in interactions (Butler 1991). Gradually, as each side deals repeatedly with their partner, suspicion declines and trust grows reciprocally (Johnson et al., 1996; Ring & Van de Ven, 1992). This starts a process in which relational norms evolve. Relational norms are defined as expectations about behaviour that are shared by a group of decision-makers (Heide and John, 1992) and provide guidelines for the initial probes that potential exchange partners may make towards each other. Relational norms prescribe acceptable behaviour at the onset of inter-organisational partnerships, which, if considered equitable by partner firms, eventually lead to future expectations of trust (Ring and Van de Ven, 1992).

Nevertheless, certain scholars have suggested that pronouncements such as 'build relationships to create harmony and learning' are fraught with complications owing to the inherent contradiction among the different strategic objectives that firms seek in alliances (Yoshino and Rangan, 1995). A potential danger in alliance situations is the risk of unilaterally losing core proprietary know-how or capabilities to the partner (Hladik, 1988). A firm derives its competitive strength from its proprietary assets and will be well aware of the danger of about losing them to the alliance partner. Partnerships are fraught with hidden agendas driven by the opportunistic desire to access and internalize the partner's core proprietary skills much faster than the partner. These 'learning races' often leave a firm in a Catch-22 situation: if it contributes too little to building the relationship, the alliance may be doomed to fail (Khanna et al., 1998); on the other hand, if it contributes too much and too openly, its partner will gain the upper hand (Doz, 1988). Although the transaction cost perspective recommends a variety of contractual mechanisms to guard against partner opportunism, scholars from other perspectives have suggested alternate means for minimizing this specific risk. Dyer and Singh (1998) propose alternatives of self-enforcing agreements, which are sometimes referred to as 'private ordering' in the economics literature or 'trust' in the sociological literature. Sociologists, anthropologists, and legal scholars have long argued that informal social controls supplement and often supplant formal controls (Macaulay, 1963; Granovetter, 1985). These self-enforcing agreements rely on relational capital as governance mechanism and are often a more effective and less costly means of protecting specialized investments and proprietary assets (Sako, 1991; Hill, 1995). Relational capital creates a

mutual confidence that no party to an exchange will exploit others' vulnerabilities even if there is an opportunity to do so (Sabel, 1993). This confidence arises out of the social controls that such capital creates.

Within this context it is proposed that relational norms as well as social control are important determinants of relational capital and success of the alliance. Although a number of different overlapping relational norms have been identified in various disciplines, the three norms of continuity expectations, flexibility and information exchange are particularly important in alliances (Heide and John, 1992; Kumar et al. 1995; Aulakh et al, 1996).

The norm of continuity expectations is the mutual recognition that the relationship will continue in the future. As a relational norm of continuity expectations is developed, exchange partners achieve a level of satisfaction with the relationship and thus do not look for alternative partners (Anderson and 1989, Dwyer et al., 1987). The norm of continuity expectations has the effect of encouraging partner firms to perceive co-operation not as a means but as an end in itself (Buckley and Casson, 1988). The norm of flexibility in a partnership is defined as the willingness to make adjustments as circumstances change (Heide and John, 1992). Flexibility is particularly important in relationships because partner firms often operate in diverse political, cultural and economic environments, thus making relationship adjustments imperative to deal with different and changing environmental conditions. Furthermore, partner firms are often called to react to unforeseen changes. Bleeke and Ernst (1991) found that partnerships characterised by a high degree of flexibility evolved better in the face of unexpected contingencies arising from changes in strategies, skills and resources of partner firms. The norm of information exchange in inter-organisational partnerships is defined as the formal and informal sharing of meaningful and timely information between firms (Anderson and Narus, 1990). Timely information exchange between partner firms fosters trust (Morgan and Hunt, 1994; Moorman et al 1993), because communication helps to resolve disputes and facilitates the alignment of perceptions and expectations (Aulakh et al 1996). Furthermore, the expectations of getting all information on an ongoing basis enable firms to cope better with internal processes and external market conditions (Heide and John, 1992). Social control refers to an informal control that creates organisational context or culture whereby the need for formal measurement of either outcomes or behaviours is greatly reduced (Ouchi, 1979). Dalton (1971) suggests that informal controls can provide both the implicit rules and supportive structures to facilitate role



understanding in organisational exchanges. The social identity theory further posits that social control in inter-organisational exchanges is conducive to shared beliefs and mutual identification by the partner firms (Ashforth and Miles, 1989). Accordingly, in socially controlled partnerships monitoring occurs through interpersonal interactions and these repeated interactions over time lead to systematise and shared organisational values, which help in building trust between partners. The long term economic performance is also enhanced through social control. Through the process of socialisation and indoctrination, a partnering firm allows wide latitude to the partner firms thus enabling the latter to respond to conditions quickly and in a manner consistent with the goals and objectives of the alliance (Aulakh, 1996).

Thus, relational capital in the alliance is considered as the quality of the relationship that exists between alliance partners. It is through relational capital that the alliance is actually enacted and implemented. It facilitates exchange and transfer of information and know-how across the alliance interface (Kale et al. 2002). As in all business interactions, the building of relational capital depends on the partnering signalling to each other and the interpretation and response to this signalling, which requires an alliance capability. It is enhanced by a feedback pattern; a trust cycle (Butler, 1995; Zand, 1972). Relational norms and social control are important determinants of relational capital and success of the alliance. They enable partner firms to respond to conditions quickly and in a manner consistent with the goals and objectives of the alliance.

## **5. Towards an integrated model**

This study builds on the work of scholars who have stressed the role of trust and personal interaction in inter-organizational relationships (Gulati, 1995; Zaheer et al, 1998, Cullen et al. 2000, Kale et al. 2000) as well as on works of scholars who have stressed the role of alliance competence in the success of alliances (Kale et al., 2002 and Lambe et al. 2002). However, it is argued that relational capital is linked not only to alliance success in general, but also to specific and important objectives such as relational norms and social control. Hence, although most literature emphasises structural factors to explain alliance success, this study argues the need to pay attention to the interplay between a firm's alliance capability and relational capital. It considers the firm's alliance capability as a prerequisite for finding, developing and managing successful alliances. Where alliance capability contributes to more effectively managing each phase of the alliance life cycle, nursing relational capital, relational capital

based on mutual trust and respect increases the willingness and ability of alliance partners to engage in mutual exchange of information, willingness to adapt to changing environmental conditions and to perceive co-operation as an end in itself. Moreover, linking both alliance capability and relational capital to alliance success is advocated, because studies on alliance experience have shown that both do matter (Kale et al, 2002)

Mutual interaction and trust that engender relational capital not only enable partners to work more untidily, but also facilitates easier flow of information and skills between them. If all firms in the alliance have an alliance capability (joint alliance capability) then they will work together more effectively than in an alliance where an asymmetric and unbalanced alliance competence exists. In other words an unskilled alliance partner can diminish the ability of the alliance partners to work together and make the required resource investments in the alliance to create alliance value. As mentioned before, a firm, even one with an alliance capability, will have difficulty working on an alliance partner that cannot manage inter-firm cultural differences. Hence, it has difficulties co-ordinating activities with another firm that does not share control, does not easily share information and fails to necessary investments in the alliance (Lambe et al. 2002; Sivadas and Dwyer 2000; Spekman et al. 1999). As a consequence it will lack relational capital. Hence, although it might be argued that one competent alliance partner can have a positive effect on the other, research indicates that the know how required to be a competent alliance partner is complex and requires years of alliance experience (Anan and Khanna, 2000; Spekman et al, 1999; Lambe and Spekman, 1997; Simonin 1997; Day 1995).

Besides having an impact at the firm and dyadic level of alliance partners, relational capital and alliance capability can also play a significant role at the industry or network level. Certain scholars have argued that strong interpersonal ties among existing partners create a basis for larger alliance networks to evolve (Gulati and Gargiulo, 1999). Relational capital that rests upon such ties engenders greater trust between partners, thereby inducing them to form more alliances with each other in the future. It also allows each partner to form alliances with other companies, based on the referrals of trustworthiness that each partner is ready to give for its current partners owing the strong relational capital between them. Thus relational capital opens up greater opportunities for the firms concerned to form new linkages and collaborations with each other and with other companies and thereby increase the network of alliances in which they are embedded (Ahuja, 2000; Gulati and Gargiulo, 1999). In addition if

firms possess an alliance capability they probably have a first mover advantage in bringing the best candidates into the alliance (Day, 1995). When all of the firms in an alliance have an alliance capability, there is a synergistic benefit that enhances the ability of the alliance to work together and to create value (Lambe et al. 2002). These different perspectives are conceptualised in figure 1.

**[FIGURE 1 ABOUT HERE]**

It is argued that relational capital and alliance capability are important constructs of alliance success. To reveal the interrelation of these constructs and performance provides important insight in how to manage inter-organisational relationships more effectively and how to strengthen both the strategic position of individual partners and alliance arrangements (Geyskens et al., 1999, Lambe et al 2002; Aulakh et al 1996).

While strong relational capital and alliance capability can enhance the leverage and coordination within the alliance partners, actual leverage and coordination may differ because of different abilities of the concerned partners. Furthermore, relations are connected to other relations resulting in systems of interdependent relations. Just like firm's behaviour and performance depends on the behaviour of other firms. Also one should bear in mind that from a co-evolutionary perspective (Windler and Sydow, 2002), firms do not act in markets or networks conceived as externally given. Rather, firms interact with other firms and thereby actualise practices and structures of the respective business network. The development of industry and network processes becomes one which should not only be understood as a co-evolutionary process, but as a co-evolutionary multi-level constitution process (Windler and Sydow, 2002).

## **6. Directions for research**

From a normative point of view, managers are more interested in assessing whether their alliances are performing rather than focusing on whether alliance partners have an alliance capability and/or the level of relational capital. Therefore it is challenging to assess the performance implications of both alliance capability and relational capital. More precisely, examining how the presence of a firm-level alliance capability is affecting relational capital and performance of alliances. This can be illustrated by the following example. Some

suppliers felt that General Motors had betrayed their trust by allegedly sharing proprietary supplier designs with competing suppliers. This has resulted in a competitive advantage for Chrysler as automobile suppliers now present their newest designs to Chrysler first rather than General Motors. Furthermore, in 1990 Chrysler was ranked lower on trust than Ford Motors and General Motors by suppliers. Today, Chrysler ranks higher in supplier trust than its two main competitors (Dyer, 1996). This example makes clear the importance of examining the position of firms in networks of exchange relationships. Further research could enrich the present work on relational capital and alliance capability by considering antecedents and consequences located in the alliance's embedded network context. Some potentially useful constructs that might be related to both are 'anticipated constructive effects on network identity', 'anticipated deleterious effects on network identity' (Anderson et al., 1994), 'improved market position' and 'improved market relations' (Haughland and Reve, 1990). This provides a guide for predicting and explaining actual outcomes. Hence, conceptualisation of the processes that are involved in inter-organisational co-operation and providing more detailed analyses of these processes, their triggers and consequences will contribute to our knowledge about the outcomes of inter-organisational co-operation and their relevant contingencies and explanations of why particular antecedents associate with specific outcomes (Oliver and Ebers, 1998). In a more general perspective several lines of research can be indicated for studies of relationships. There are five groups of factors to consider, evolving from a firm's perspective towards a network perspective: a) characteristics of the relationships and interactions in which a firm is involved; b) characteristics of a firm's relationship partners; c) characteristics of connected relations and their interactions; d) characteristics of a firm's network position and e) characteristics of the network as a whole. In order to investigate the impact of these factors on firm, relationship and network behaviour and performance, different types of research designs and approaches are needed to compliment existing perspectives in relationship and network studies. Studies of relationships are usually based on samples of independent relations and firms, but to study the impact of connected relations and firms samples of connected relations and firms are required. For example, to study the impact of relationships and other network members one need to identify and measure the characteristics of a firm most important relationships and relationship partners, as Blankenburg-Holm et al. (1996, 1999) have demonstrated the significant impact of connected relations on relationship performance. However, existing models of buyer-seller relations tend to study dyads separated from any network context, including only a comparison with an alternative and other types of connections not included (Wilkinson and

Young, 2002). Network analysis methods exist to derive measures of various network characteristics and an individual firm's position in the network. These can be used to develop hypotheses and to predict the behaviour and performance of firms and relations in the networks. Only a few such studies have been carried out of the structure, evolution and behaviour of networks as a whole, however they are time consuming and difficult to carry out. An alternative approach is to simulate models of networks as complex adaptive systems and examine their behaviour and development under different conditions. Agent-based modelling and simulations techniques have been developed. These models are different from simulation models used in the past to study markets and networks. There is no controlling program, the rules governing behaviour can change in response to behaviour taking place and structure emerges in a bottom-up way. Such models can be used to explore how large-scale (macro) order is shaped by the characteristics of local interaction (micro) interactions, how different patterns of local interaction and firm adaptive behaviour impact on overall network behaviour and performance; the extent to which similar network behaviour and performance can emerge from different patterns of local interaction strategies and adaptive behaviour; and the impact and limits of types of intervention strategies on network behaviour and evolution (including attempts to shape local interaction patterns (Wilkinson and Young, 2002).

Hence, more integrative approaches are encouraged to understand and explain alliance success better, because many studies are limited by their unilateral approach and reliance on firm level measures of alliance success. From prior research is known that important dyadic or transaction-level attributes such as governance structures (Kogut, 1989), information asymmetries (Reuer and Koza, 2000), level of inter-partner trust (Kale et al., 2000), etc. also have an impact on alliance success (Kale et al., 2002). Also there is a need for longitudinal studies involving the same set of alliances over an extended period. Such research would make a great contribution to the process of dynamics and the cumulative effects of individual exchange episodes in establishing long-term relationships. This would make possible better inferences about the development on alliance constructs over time, their causal sequence and feedback effects.

## **7. Conclusion**

This paper aims to show how a firm's alliance capability and relational capital might contribute to alliance success. Both the role of alliance capability and relational capital are discussed. A firm's alliance capability might be considered as a prerequisite for finding,

developing and managing alliances, thereby, facilitating the development of relational capital. The latter can be seen as the ability to engage in mutual exchange of information, willingness to adapt to changing environmental conditions and to perceive co-operation as an end in itself. Both firms and alliances can benefit substantially by possessing and managing alliance capability and relational capital as aspects of alliance management. However, firms are quite heterogeneous with respect to their alliance capabilities and as a consequence heterogeneous in their ability to develop relational capital. This heterogeneity is linked both to the amount of prior alliance experience they have had (Anand and Khanna, 2000) and how they learn and leverage from that experience (Kale and Singh, 1999). In assessing the success of alliances this is of great importance, especially when competition is shifting towards group versus group competition. Hence, to study this requires samples of connected relations and firms and dyadic data-gathering, as well as a network perspective. Future research is challenged to explore these important research issues in greater detail.

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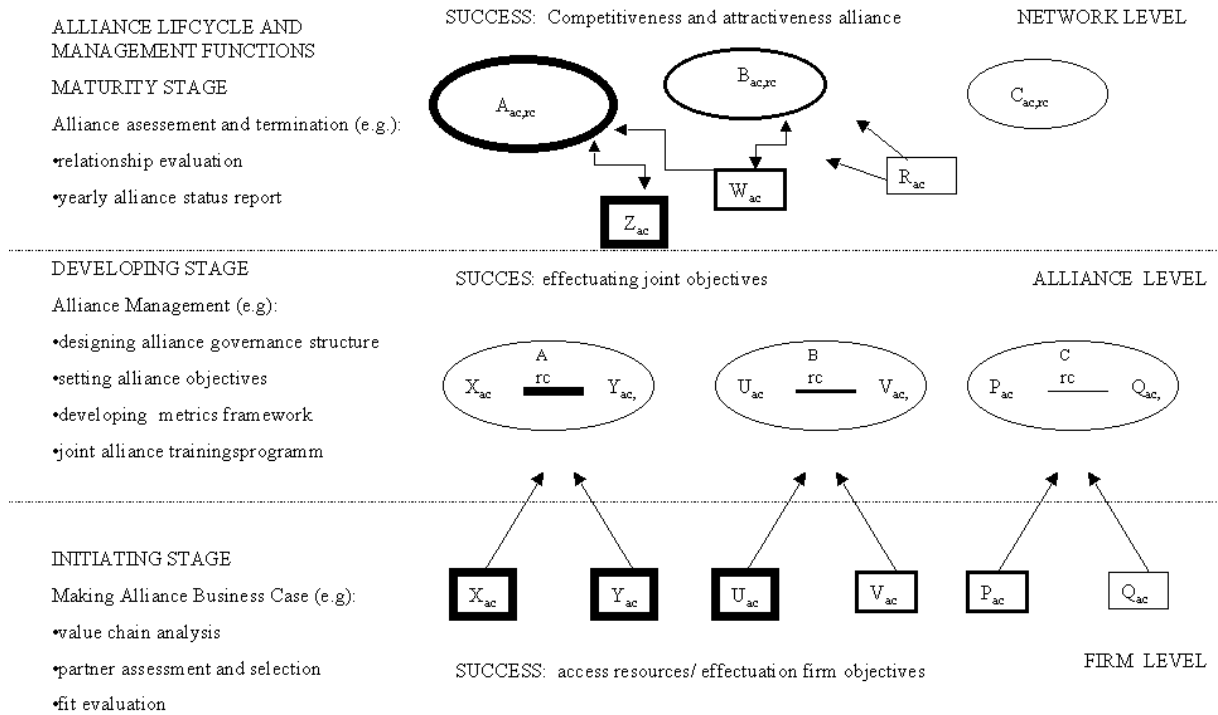
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**Figure 1: The presumed effects of alliance capability (ac) and relational capital (rc) on success at the firm-, alliance and network level.**

**ac firm  $X=Y=Z=U>V>W>P>Q>R$ ; ac firm  $V=W=P>Q>R$ ; ac firm  $Q=R$ . Rc alliance  $A>B>C$   
 competitiveness and attractiveness allianc  $A>B>C$ . Double arrow: mutual attractive; single arrow: one sided attractiveness.**