

# **Interorganisational Relationship Management: Managing Across Hierarchies, Markets and Networks**

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of Master of Commercii.



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Formation

Governance

Performance

Collaboration

Co-operation

Co-ordination

Assessment

Integrative framework



## **Abstract**

### **Interorganisational Relationship Management: Managing Across Hierarchies, Markets and Networks**

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This study focuses on understanding inter-organisational relationships (IOR) of a dynamic nature. A dynamic process that has repetitive sequences of negotiation, commitment, and execution stages is central to IOR. Parties assess each stage in terms of efficiency and equity, as IORs emerge, evolve, and dissolve. The dynamic process is a tool that is used by management through collaboration, co-operation, and co-ordination to engender formation, governance, and performance of IORs. IORs are there to achieve stated strategic objectives of parties involved. Parties avail themselves of the resources to enable the execution of the transactions that will deliver the stated objectives. An IOR facilitates the exchange of resources that enable the successful implementation of a transaction, making an IOR a value-creating vehicle, or a resource. As the IOR is a resource, and resources are exchanged by parties to deliver IOR benefits through a transaction, both the resource-dependence theory and the transaction-cost theory are relevant to the analysis of the emergence, evolution, and dissolution of IORs. In focusing managerial effort, resource-dependency theory is relevant to IOR formation and transaction-cost theory is relevant to IOR governance. Both theories are also important in understanding the performance of IORs.

## **Declaration**

I declare that **“Interorganisational Relationship Management: Managing Across Hierarchies, Markets and Networks”** (2006) is my own work, that it has not been submitted before for any degree or examination in any other university, and that all the sources I have used or quoted have been indicated and acknowledged as complete references.

Cedrick Muleya

August 2006

Signed:.....



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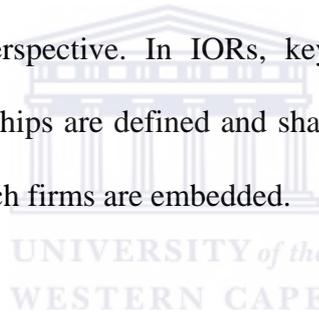
## **Background**

My experience in curriculum development in the Department of Information Systems at the University of the Western Cape inspired this research report. I joined the department while in its infancy, when it was involved in the design, development, and implementation of both undergraduate and postgraduate curricula. It was in the postgraduate curriculum design, development, and implementation that I made my claim. First, from first principles, and almost single-handedly, I designed, developed, and implemented an honours curriculum. Second, working with several universities in Africa and America, with assistance from resource partners, as UWC NetTel@Africa Coordinator, I was involved in the development and implementation of the master's curricula in ICT Policy and Regulation. While performing the coordination role the interorganisational relationship (IOR) phenomenon came into focus. I felt a need to share the acquired knowledge, skills, and insights into managing IOR relations, gained as coordinator. I attended to almost all the activities and/or meetings on behalf of UWC, the intense competition experienced, resulted in my categorisation of these activities as strategic, tactical and operations. As the language seemed inappropriate, I renamed strategic "collaboration", tactical "cooperation", and operations "coordination". In the end, for the need to share, I wrote what I term an "intellectual story" or generally known as "meta-research" or "meta-analysis" inspired in a way by curriculum development. In a limited way, I achieved this by using theory from the literature to formulate IOR theory through use of propositions and test this tentative theory using secondary data from a case study.

## **Introduction**

The aim of this report is three-fold. First, in identifying the essential constructs of IORs, the main problem is to establish the nature of these constructs and the interaction between them. Second, it is important to show that there is clarity and parsimony of the constructs. Third, constructs cannot be observed directly; propositions will be used to communicate relationships between constructs as a way to indicate their existence and the relationships between them.

Markets and hierarchies are an efficient alternative mechanism for allocating resources in transactions with uncertainty and prone to opportunism, as viewed from an organisation's perspective. In IORs, key precursors, processes, and outcomes of these relationships are defined and shaped in important ways by the social networks within which firms are embedded.



Social networks are key community actors and their interaction networks are key social structures in the modern community. The interaction networks function as delivery systems to meet the demand for goods and services in the community and function to protect certain special interests. Money networks, information networks and moral-support networks are some of these social networks. They allow economic action to take place through exchange processes and collective action. This happens when social networks create an environment where roles and personal relationships are established.

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These relationships, which are formalised in an IOR, become a resource that enables execution of the transaction that brings the parties together. Other resources sourced through social networks and the IOR become resources that implement the transaction.

This report will look into how the resource-dependency theory gives insight into the formation of an IOR and how the transaction-cost theory contributes to the understanding of IOR governance. It also enlightens on how both the resource-dependency theory and the transaction-cost theory account for IOR performance.

Chapter 1 introduces the integrative framework that gives strategic context to using propositions to give clarity and parsimony to IOR constructs. To achieve this, propositions must satisfy four conditions that fit the conceptions of objective research: they must exhibit internal logical consistency, they must be empirically testable, they must survive attempts at empirical testing, and they must at least be explanatory or predictive. It also introduces the IOR model.

Chapter 2 argues that social networks exploit opportunities for identifying prospective partners and resources. For the successful formation of an IOR, there should be strategic interdependence. Senior management use social networks to enter into collaborative activities. Through the dynamic process, senior management set strategic context that informs the strategic content, setting the tone for lower-level management focus and involvement. The dynamic process carries this to lower management through co-operation and co-ordination.

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Chapter 3 focuses on control mechanisms in hierarchies and markets that enable transactions to be implemented. Contracts can be configured to simulate controls in hierarchies and markets. In deciding which controls to incorporate into an IOR, the risk involved in the transaction and trust within relationships play important roles.

Chapter 4 argues that the type of resources involved in an IOR transaction influences the type of co-ordination, which can be formal, informal or both. Hierarchies and markets have built-in co-ordinating mechanisms, as articulated in transaction-cost theory. Performance depends on rent-seeking behaviours of parties in the IOR. Behaviour can be co-operative or competitive, or both.

Chapter 5 introduces a case study published in IOR literature that is an exemplar of the integrated framework and gives an opportunity to use its findings to test the propositions.

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# Chapter 1: Introduction

## 1.1. Introduction

Markets and hierarchies are viewed as efficient alternative mechanisms for allocating resources in transactions with uncertainty and with assets that are transaction specific and have a certain level of frequency (Bradach et al., 1991). Such a view has since been extended to give an interorganisational relationship view that adds more relationships to “dyadic exchanges, paying attention to the fact that the key precursors, processes, and outcomes of these relationships are defined and shaped in important ways by the social networks within which most firms are embedded” (Gulati, 1998:295). Such co-operative interorganisational relationships are negotiated, committed to, and executed, “in ways that achieve efficient and equitable outcomes, and internal solutions to conflict when they arise” (Ring & van de Ven, 1994:90).

Interorganisational relationships (IORs) have strongly emerged as delivery systems to meet the demand for goods and services in the community and function to protect certain special interests. In order to be able to achieve this, organisations enter into informal or formal agreements and then pool their resources (Smith, Carroll & Ashford, 1995).

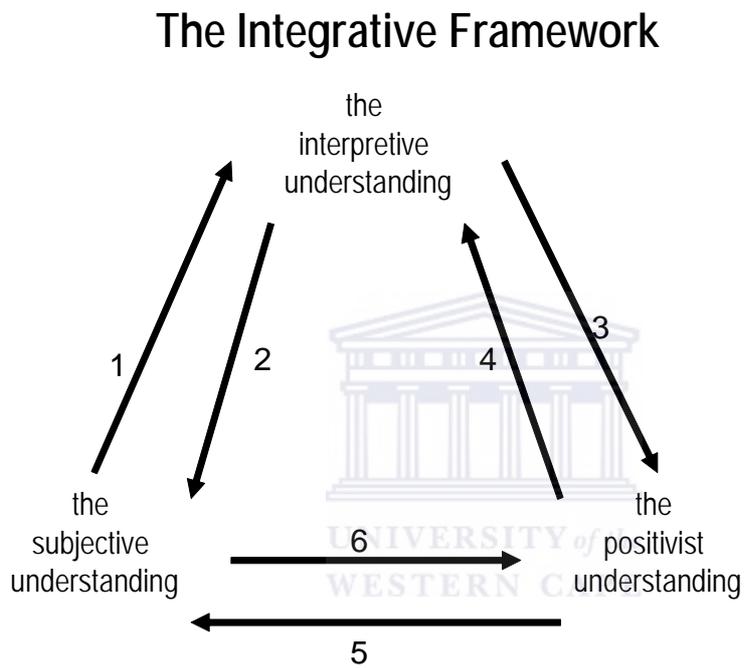
This research will focus on the management of the formation, governance, and performance of IORs. The intended contribution of this research is to theoretical explore and hopefully provide insights into management functions across

hierarchies, markets, and networks in economic exchange relations called IOR. This exploration may highlight gaps, which may give rise to opportunities that may guide managerial intervention. The insight may consist of a framework that integrates management across hierarchies, markets, and networks, based on the understanding that these entities are part of the social structure, embedded in the social system, and involved in economic action, which is collective in nature. The proposed framework is formulated to achieve a particular goal, subject to certain constraints. The goal is to convince management of the dynamic evolutionary nature of any IOR, present opportunities to them on how they may act individually and collectively, and advise them when to do so. Constraints on the framework are that fundamental social network concepts, IOR process concepts, and hierarchy and market governance concepts must be accepted. In satisfying these constraints, literature will be used to demonstrate how hierarchies and markets benefit from networks in the formation, governance, and performance of IORs

## **1.2. The Research Method**

The method used here is inspired by the work of Lee (1989a; 1989b; 1991). In organisational research, the subjectivist and objectivist schools of thought are different from each other “in offering different philosophies for different stages of research, not in offering contrary philosophies for the same stage of research” (Lee, 1989b:131). Subjectivists offer superior procedures pertaining to the development of an understanding from the perspective of the observed people, but objectivists offer superior procedures pertaining to the formulation and testing of

theoretical propositions (Lee, 1989b). The subjectivist stage is different from the objectivist stage, but the two are mutually supportive (Lee, 1989b). To demonstrate and explain this, Lee (1991) offers an integrated framework (Fig 1.1), based on cyclical relationships existing among the three levels of understanding, namely, subjective, interpretive and objective (positivist).



**Fig 1.1** Source: Lee, 1991.

In constructing the integrative framework, Lee (2004:8) argues, “a social science theory and a natural science theory are no different in their logical form”. The major difference is that social scientists’ empirical work interpret the meaning that the observed human individuals create and share, attach to one another, their organisational setting and their history, yet natural scientist do not do this prior to formulating a theory (Lee, 2004). This is because “the social reality examined by social science is fundamentally different from the physical reality examined by

natural science, natural sciences have to deal with material objects and processes, the social sciences, however, with psychological and intellectual ones and that, therefore, the method of the former consists in explaining, that of the latter in understanding” (Lee, 1989b:118). Another important methodological observation that Lee notes is that the natural science methodology represents a limiting case of the social science method, organisational methodologists call the “ natural science model of social science research” (Lee, 1989b:118) where, “subject matter has of itself, its setting and history go to zero” (Lee, 2004:9). In other words, social scientists use subjective meaning to create interpretive understanding, and then further perform the positivist procedures that inform positivist understanding, which the natural scientists do as well in constructing theory for explanation purposes.



### **1.2.1. The subjective understanding**

As discussed earlier, the first level of understanding refers to understanding the observed human subjects have of themselves, their setting and their history. This “consists of the everyday common sense and everyday meanings with which the human subjects see themselves, and which give rise to the behaviour that they manifest in socially constructed settings” (Lee, 1991:351).

Lee (1991:347) argues, “People create and attach their own meanings to the world around them and to the behaviour that they manifest”. Different subjects can attach different meanings to the same physical artefact, the same institution, or the same human action, to that of the observing researcher (Lee, 1991). Lee then

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argues that, this implies that the interpretation of the empirical reality by the researcher must be in terms of what it means to the observed people (subjects). The implication of this therefore is that the meanings held by the observed are an integral part of the subject matter (as noted above this is a distinct characteristic of social science research). This integral part must then inform the researcher when collecting facts and data, in that these should not only describe “the purely objective, publicly observable aspects of human behaviour, but also the subjective meaning the behaviour has for the human subjects themselves” (Lee, 1991:347).

The primary task of the researcher then is to understand the meaning an act has for the actor who is being observed, not for the researcher who is observing (Lee, 1991). This gives rise to two specific processes a researcher must perform. First, the researcher must pursue a process of understanding how “people in everyday life come to interpret and, therefore to understand and guide themselves in their world” (Lee, 1991:348). The methodological implication of this is that, qualitative methods (arrow 1) are used to gather data that is used to develop interpretive understanding from subjective understanding. “To test the validity of the resulting interpretive understanding is a, the researcher may refer back to the subjective understanding (arrow 2)” (Lee, 1991:352). For the researcher to achieve validity, based on interpretive understanding, is to reach a stage in which they are able “to read the behaviour of the observed human subjects as rational, rather than as absurd, peculiar, pointless, irrational, surprising, or confusing” (Lee, 1991:352). Second is a process of understanding “by which the observing researcher

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interprets the subjective meanings that give rise to the behaviour of people the researcher is studying” (Lee, 1991:348).

According to Lee (1991), the same method of reading text can be used in reading human behaviour. He gives an example of a writer who implants certain meanings in a text, and that readers of the text, especially those who belong to a different time and culture from the writer of the text, interpret the text for the meanings originally implanted in it. In the text, there will be primary parts that belong to the writer and others which are cross-referenced. The reader should note that in works of writing, parts of text are interwoven to give meaning to each other and to the whole. “The meaning in a particular passage in a text (or a particular human behaviour in a social setting), as interpreted by the reader (or the researcher/observer), is related inextricably to the meanings of all the other passages in the same text (or the meanings of all the other human behaviours in the same social setting). Clarification or change in the interpretation of a passage (or behaviour) has the effect of rippling through the circle and changing the framework, supporting the previous interpretation of the other passages in the text (or the other behaviours in the social setting)” (Lee, 1991:349). Lee (1989b:127) gives a similar example on how Kanter did an extensive review of the sociology, social psychology, and organisational behaviour literatures, then worked back and forth between literature and the field. This procedure will be utilised in informing both the interpretive and positivist understanding of the IOR model by moving back and forth between literature and a case study in the literature.

### **1.2.2. Interpretive understanding**

The second level “belongs to the observing organisational researcher, and is the researcher's reading or interpretation of the first-level, common-sense understanding” (Lee, 1991:351). Lee argues that when the interpretive understanding is judged valid, it provides the basis on which to develop the positivist understanding (arrow 3). The important thing to note is that the interpretive understanding is based on subjective meanings or subjective understanding of the human subjects (as discussed earlier, this is what distinguishes interpretive understanding from positivist understanding). In noting this distinction, Lee (1991:352) cautions, “a different reading or interpretation of what the organisation means to the human subjects will lead to different theoretical explanations for how the human subjects behave”. This implies that same human subjects' behaviour may be explained by more than one theory. For the purposes of this research, the IOR model is presented as tentative interpretive understanding, recognising that more than one theory may be needed to explain managerial behaviours.

### **1.2.3. Positivist understanding**

The third level refers to the theory that researchers develop in order to explain what they are observing and to satisfy their criteria of rigor (Lee, 2004). The scientific theory is made of constructs, consisting of formal propositions that posit the existence of unobservable entities (Lee, 1991; Bacharach, 1989). Theoretical explanation at this level must obey the same rules of formal logic and controlled empirical testing that apply to scientific explanations in general (Lee, 1991). The

resulting positivist understanding should be subjected to three tests that both adapt and check positivist understanding of social reality.

The first test would indicate whether the researcher has remembered to undertake the task of building the subjective meanings (earlier recorded in the interpretive understanding) into the positivist understanding. This is done by referring back (arrow 4) to the subjective meanings held by the subjects in the interpretive understanding (Lee, 1991). In other words, are the subjective meanings built into the theory (positivist understanding) similar or identical to those held by the subjects who provided them in the first place?

“The second test would indicate whether the researcher has performed the first test (or task) successfully” (Lee, 1991:353). It requires the use of hypothetico-deductive logic by specifically using the logic of the syllogism, which involves a major premise, a minor premise, and a conclusion (Fig 1.2) (Lee, 1991). This means that the theory must specify the actions so that those actions, if performed within the organisation, would be understandable to the participants (human subjects) in terms of the everyday meanings and common sense with which they see themselves and the organisation around them (arrow 5) (Lee, 1991). This is to say that an individual actor, as indicated by the typical construct in a scientific model of human action, must perform an act in such a way that it is similar to a human act performed within the real world (Lee, 1991). This is achieved through the utilisation of propositions.

## Proposition Verifying Model

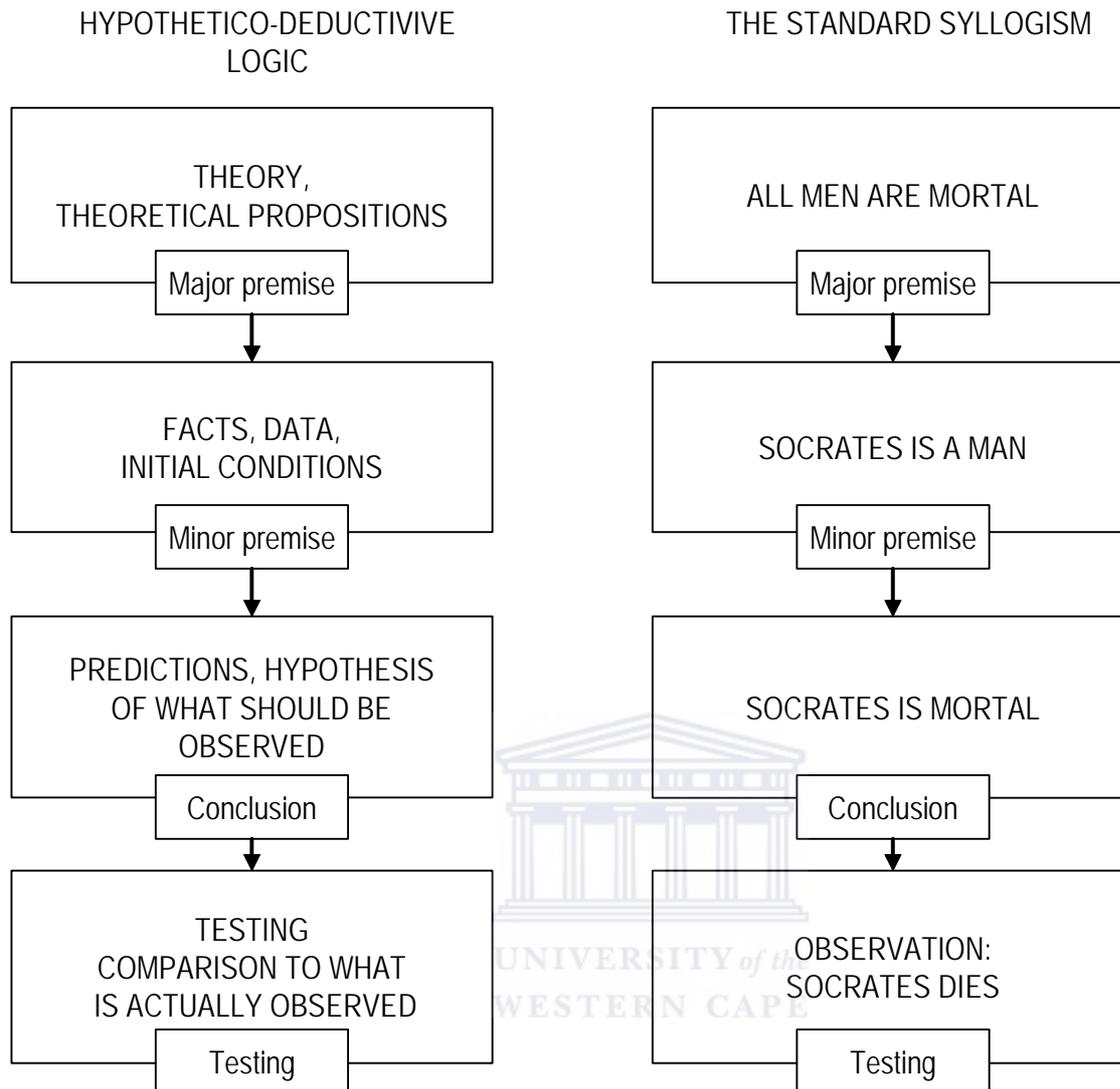


Fig. 1.2 Source: Lee, 1989.

The third test would indicate whether the positivist understanding is confirmed, based on controlled empirical testing (Lee, 1991). The challenge here is that the theory refers to unobservable entities. Lee (1991) argues that this is similar to the challenge faced by natural scientists when they posit the existence of unobservable entities, such as pressure, electric field and others. In dealing with the challenge, the organisational researcher borrows and uses the logical premise from natural scientists that unobservable entities have consequences that are

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observable, even though the entities themselves are not. The focus of the organisational researcher here is on collecting or observing the purely physical or behaviourist component of the predicted actions by employing theory. According to Lee (1989b:128) the focus will be on “private mental states of individuals, to the privately held meanings that the surrounding organisation has for them, and to features of the underlying social structure, none of which can be observed directly”. He further argues, “Theoretical propositions in the natural science studies also refer to things that cannot be seen directly, atoms, molecules, double bonds, photons, superstrings, black holes, evolution, and so forth. And just as natural science studies can verify, indirectly, that these entities exist by using hypothetico-deductive logic”, social science methods can do the same.

The positivist understanding is confirmed if the actions predicted by the theory match the actions of the actual people (arrow 6) (Lee, 1991). According to Lee (1991:353) the important thing is that the “subjective understanding, through publicly observable behaviours arising from it, may serve to confirm or disconfirm the predictions of the positivist understanding”. He further states “When undergoing the third test, the theoretical propositions must satisfy the rules of formal logic, the rules of hypothetico-deductive logic, and the four requirements of positivism: falsifiability, logical consistency, relative explanatory power, and survival”. Lee also highlights two points about the third test. The first is that “the proposed framework calls upon the researcher, not human subjects being studied, to render the final judgement that the positivist understanding is confirmed or disconfirmed”. The second is that “even though the test pertains to

the validity of the positivist understanding, it also provides a provocative, if indirect, method by which to judge the validity of the interpretive understanding”. In presenting the integrative framework, Lee (1991:354) makes a point that “the positivist understanding and interpretive understanding-far from being mutually exclusive and irreconcilable-may be utilised as mutually supportive and reinforcing steps in organisational research”.

In the concluding remarks about the cyclical relationships existing among the three levels of understanding, Lee (1991:354) states:

The subjective understanding provides the basis to the interpretive understanding (arrow 1), which provides the basis to the positivist understanding (arrow 3), from which follow predictions (arrow 5) about human actions. The actions that the human subjects display are outward signs or artefacts of their own subjective understanding. Through these publicly observable artefacts, the subjective understanding has the effect of either confirming or disconfirming the predictions of the positivist understanding (arrow 6). A disconfirming would call for an improvement in the positivist understanding, which would call for a fresh reading of the subjective understanding (arrow 2). The new reading would provide the basis to an improvement in the interpretive understanding (arrow 1), which would then provide the basis to an improvement in the positivist understanding (arrow 3), and so on.

#### **1.2.4. Traditional research methods**

The general principle is that the research strategy or strategies, and the methods or techniques employed, must be appropriate for the questions one wants answered (Robson, 1993). Traditional strategies are experiment, survey, and case studies. These methods share one common feature in that they define techniques of dealing with empirical data. Experiments are used when measuring the effects of manipulating one variable on another. Surveys are useful during the collection of

information in standardised form from groups of people. Case studies are suitable for detailed, intensive knowledge about a single 'case', or a small number of related 'cases' (Robson, 1993). A follow-up study to this research, dealing with empirical data, could use any of these methods. A researcher with a follow-up study could test the theory, whether through a rigorous statistical model or by some other means of "controlled empirical testing" (Lee, 1991:355) such as field experiment or a laboratory simulation.

This will be a deductive research study that will synthesise a "theoretical system, develop operational definitions of the propositions and constructs of the theory, and match them theoretically to some body of" knowledge from previous studies (Schriver, 1989:280). The approach will strive to fit "the conceptions of objective research" (Lee, 1989b:127) by involving limited aspects of "the manipulation of theoretical propositions, using the rules of formal logic and the rules of hypothetico-deductive logic, so that the theoretical propositions satisfy the four requirements of falsifiability, logical consistency, relative explanatory power, and survival" (Lee, 1991:343). As this is a theory-development process, logic replaces data as the basis for evaluation (Whetten, 1989). Although the orientation here is towards theory evaluation (testing), there is a close methodological relationship between theory-building research and its mirror, theory-testing research (Eisenhardt, 1991).

The function of theory is to prevent an observer "from being dazzled by the full-blown complexity of natural or concrete events" (Bacharach, 1989:496). In this regard, Bacharach argues that the purpose of theoretical statements is to organise

parsimoniously and communicate clearly. This is achieved by using rules of logic that “provide a powerful means by which to relate propositions to one another and to deduce new ones” (Lee, 1991:344). Lee further argues, “The rules of formal logic have two important consequences for the development of scientific explanation. First, the process of logical deduction is able to extract consequences that are contained only implicitly in the explanation’s opening premises, thereby leading to unanticipated discoveries. Second, any proposition that cannot be shown to be logically connected to, or logically deducible from, the remaining propositions would be “exposed” as groundless”.

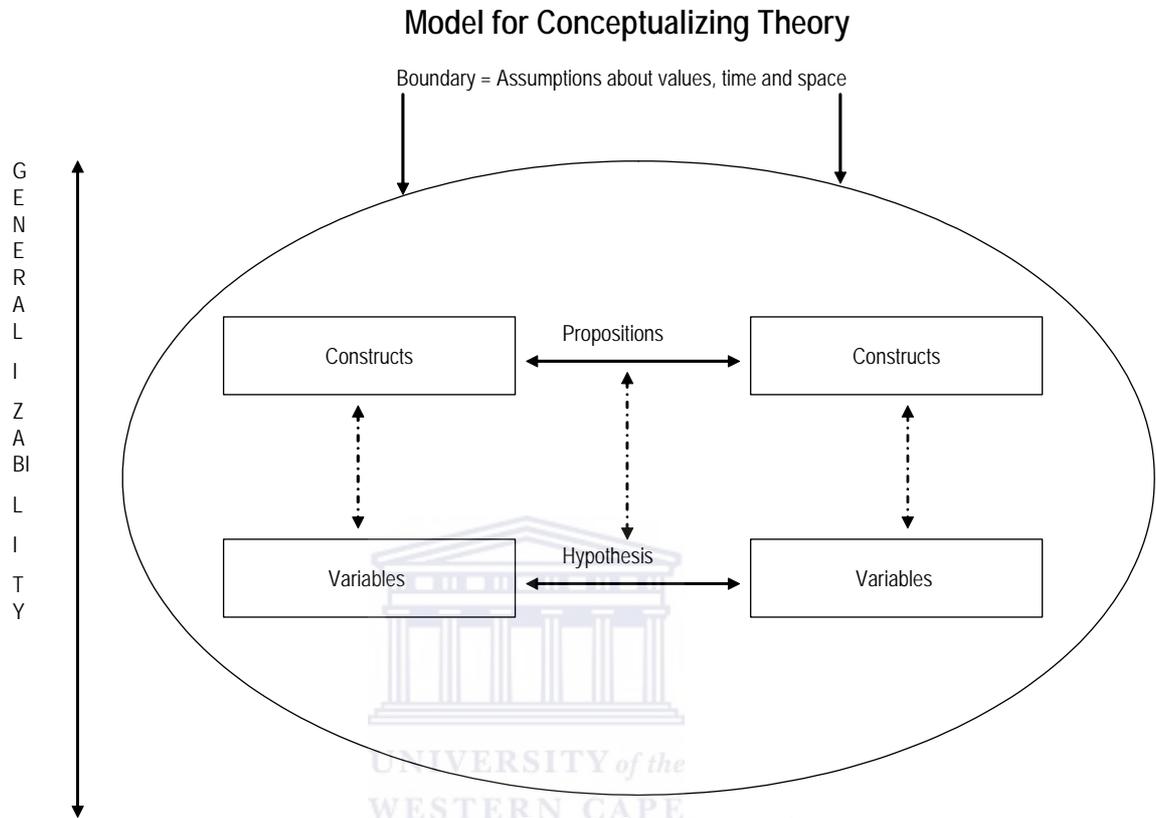
This pertains to how to relate propositions to one another by restricting one’s attention to the world of ideal relations, by artificially specifying formal propositions and the relationship between them, as indicated in Fig 1.3. A theory here is “a system of constructs and variables in which the constructs are related to each other by propositions and the variables are related to each other by hypothesis” (Bacharach, 1989:498). As discussed earlier, one cannot observe constructs directly, but constructs are made up of variables that can be observed directly. Although most tasks and procedures of theory development and testing will be performed, the fact that there will be no observation of variables points to the limitation of this study in terms of how far it is in theory formulation and testing (falsification).

Propositions propose the existence of entities, phenomena, or relationships that are not directly observable, leaving theorising about their existence as the only option

(Lee, 1991; Bacharach, 1989). According to (Bacharach, 1989:500) “On a more abstract level, propositions state the relations among constructs, and on the more concrete level, hypotheses (derived from propositions) specify the relations among variables”. A point to note that follows from the characteristic of propositions, namely being abstract in this research in this research is that, if they are successfully applied to by clearly communicating relationships between constructs using the hypothetico-deductive logic one may conclude that there is successful theory building or evaluation. Bacharach (1989:501” call this “the paradox of conceptualisation” as he notes that “The proper concepts are needed to formulate a good theory, but we need a good theory to arrive at the proper concepts”. Another related issue is construct validity. Take for instance convergent validity where “evidence from different sources gathered in different ways all indicated the same or similar meaning of the construct” (Bacharach, 1989:503), a procedure used with literature sources in this research. The point is that the use of propositions as discussed in this research is a tool in the toolbox of a researcher who is embarking in theory development and testing.

Bacharach (1989:498) state, “all theories are constrained by their specific critical bounding assumptions. These assumptions include the implicit values of the theorist and the often explicit restrictions regarding space and time”. Bacharach notes “theories cannot be compared on the basis of their underlying values as they are a product of the theorist’s creative imagination and ideological orientation or life experience”. Bacharach argues that taken together with space and time, values are theory boundary conditions that restrict the use of theory to specific units of

analysis and affect their generalisability. It is argued here that boundary conditions taken together with the fact that there was no measurement of variables are indicative of what testing was done in this research.



**Fig 1.3** Source: Bacharach, 1989.

According to Lee (1991:346) “When rules of formal logic and rules of hypothetico-deductive logic are used to manage theoretical propositions, there are four checks or requirements that the propositions must satisfy”, discussed above. In giving guidance as to how such evaluation is conducted to produce, acceptable and superior theory (Table 1.1) (Bacharach, 1989:501) adds utility.

## Checks or requirements that propositions must satisfy

	Falsifiability	Utility
Variables	Measurement Issues	Variable scope
Constructs	Construct validity	Construct scope
Relationships	Logical adequacy Empirical adequacy	Explanatory potential Predictive adequacy

**Table 1.1** Source: Bacharach, 1989.

As described earlier positivist understanding is confirmed or disconfirmed (falsification), based on controlled empirical testing which is the conclusion part of the hypothetico-deductive logic, specifically using the logic of the syllogism, with the first two parts being major premise and minor premise respectively (Lee, 1989b). Utility refers to the usefulness of a theoretical system as a bridge that connects theory and research, and “at the core of this connection are explanation and prediction” (Bacharach, 1989:501). According to Bacharach (1989:501) the first thing in understanding how to apply falsifiability and utility to theory “is to understand components of theory at different levels of abstraction and the two main types of criteria”. As discussed earlier this is based on the understanding of the researcher and the responsibility of the researcher is to perform procedures that test falsifiability and utility.

### **1.2.5. Falsifiability**

Construct falsifiability involves convergent validity, discriminant validity and chain of evidence. According to Bacharach (1989), to test for convergent validity

is when “responses from alternative measurements of the same construct share the same variance”. For discriminant validity, he argues, “identified objects of analysis must not share attributes and must be empirically distinguishable from one another”. As for chain of evidence, Bacharach states “evidence from different sources gathered in different ways all indicate the same or similar meaning of the construct”. The use of the literature and case study were designed in this study to meet these three aspects of construct validity.

Bacharach (1989:505) argues “evaluating the falsifiability of the relational properties of theoretical systems, must examine both logical adequacy of propositions and hypotheses (and their interrelationships) as well as their empirical adequacy (the capacity of the relationships implied in the propositions and hypotheses to be operationalised)”. The hypothetico-deductive logic, specifically using the logic of the syllogism in constructing the propositions of the IOR model ensures that issues of logical adequacy are addressed in that propositions are nontautological and the nature of the relationship is specified (Bacharach, 1989). For empirical adequacy Bacharach (1989:506) state “Specifically, propositions and hypotheses should satisfy the following criterion: *There either must be more than one object of analysis or that object of analysis must exist at more than one point in time*” (emphasis in the original). He also advises “the theory must be proposed in such a way as to permit longitudinal analysis”.

### **1.2.6. Utility**

A construct's utility is established when it "sufficiently, although parsimoniously, tap the domain of the phenomenon in question" (Bacharach, 1989:507). The design of study using literature and case study, and propositions achieve utility. The content of constructs gives them parsimony and the case study help in giving evidence of broader scope and overall explanatory power (Bacharach, 1989)

According to (Bacharach, 1989:507) utility of relationships is established when the following three aspects are addressed:

- When there is specificity of assumptions about the objects of analysis. In this study, the resource dependence and transaction cost theories are the specific assumptions in analysis IOR phenomena.
- When there is specificity of the substantive nature of the relationship between the antecedent and consequent. These are addressed in discussing formation, governance, and performance of IOR.
- Scope and parsimony. This is established where the application of IOR concept is identified, e.g. BEE and National, regional and local government in South Africa, joint ventures, strategic alliances.

The scope of this report will limit application of these requirements to a limited focus on falsifiability and utility of propositions. According to Bacharach (1989:503) "if the purpose of a proposition is to communicate the relationship between two or more constructs, then (unlike variables) the only operational

criteria which these constructs must meet is that they have good clarity and parsimony”.

### **1.3. Interorganisational Relationships**

An interorganisational relationship (IOR) is a relationship between organisations, but the same phenomenon can be observed between individuals and between groups or departments. This then makes it “a topic of interest in disciplines such as economics, sociology, anthropology, psychology, political science, and organisational theory, as well as strategic management” (Smith et al, 1995:9). This literature is varied, large, and fragmented, but Smith et al. categorises it into five theories, namely, exchange theories, attraction theories, power and conflict theories, modelling theories and structural theories. Literature in this report will be organised in streams: social networks, collaboration, co-operation, and co-ordination to reflect a strategic management perspective of IOR. This is based on Fig 1.4, which is a derived theoretical and conceptual framework from the literature to guide research and interpret findings (Cronk & Fitzgerald, 2002).

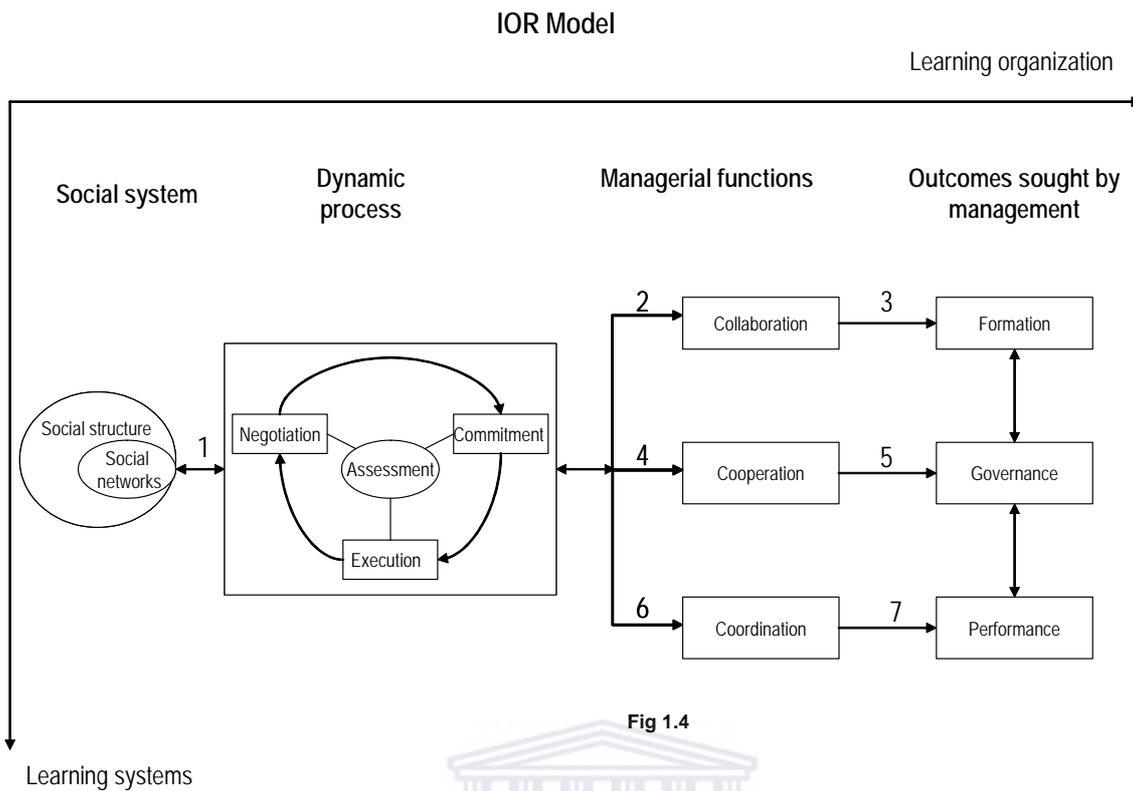


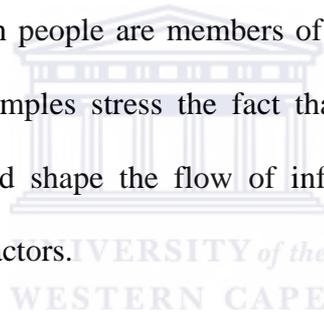
Fig 1.4

Social networks, as part of social structure within a social system, guide, in that through social networks, organisations learn about each other's existence, needs, capabilities, and interorganisational relationship requirements at a given time.

They learn about organisations that have resources or capabilities beneficial to but not possessed by the others. This information then guides the organisation's interorganisational relationship decisions. The implementation mechanisms of these decisions could be strategic alliances, partnerships, coalitions, joint ventures, franchises, research consortiums or network organisations. Collaboration, co-operation, and co-ordination are seen as management functions.

### **1.3.1. Social networks and the emergence of IORs**

Social networks are part of the social structure and guide an organisation's action by providing opportunities to learn about "the reliability and specific capabilities of current and potential partners" (Gulati, 1995:623). "Social networks are conduits of valuable information in a variety of contexts ranging from interpersonal ties, which are conduits for employment information, to interlocking directorates, which are channels of information on organisational practices" (Gulati, 1995:625). Personal ties can develop through shared interests by individuals when they are involved in the same sporting activities or belong to the same professional organisation. Interlocking directorates create formal ties of information exchange when people are members of the board of directors in the same company. These examples stress the fact that social networks of ties in which actors are embedded shape the flow of information between them and moderate the behaviour of actors.



Behaviour that results in the formation of interorganisational relationships has a dynamic and interactive relationship with social networks, making networks of interorganisational relations to be "both maps of and for strategic action" (Gulati, 1995:624). What makes social networks maps of and for strategic action is their relational component, made up of the direct relationships within which an organisation is embedded, and their structural component, which encompasses the overall social network within which organisations exist.

### **1.3.2. Social structure context**

Social networks are part of the social structure. This social structure provides a context that gives rise to factors that may lead to the availability of interorganisational relationship opportunities based on organisational interest and external opportunities. This social structure context has the following dimensions: relational, structural, cognitive, and positional (Tsai and Ghoshal, 1998).

#### **1.3.2.1. Relational dimensions (direct ties)**

In prior or current interactions, firsthand information about experiences provides an opportunity for the identification of the needs and capacity of the potential partners. Such interactions facilitate the development of organisational routines for certain tasks and for managing relations with each other. Direct experience-based knowledge about current and prior ties provides firsthand information and is effective because, according to Gulati (1995:625):

- it is cheap as there is no information search,
- “individual organisational members have cognitive bias toward trusting firsthand information”,
- “partnering organisations have an economic incentive to be honest, to prevent jeopardizing future ties”, and,
- “ties become suffused with social elements that enhance the likelihood of trustworthy behaviour”.

The relational dimension refers to assets that are rooted in these relationships, such as trust and trustworthiness. Trust is important and recognized in IOR

because it “can act as a governance mechanism” (Tsai & Ghoshal, 1998:465). Prior or current ties therefore create a strong social connection between organisations that may lead to future interaction. Ties provide greater “understanding of each other's needs and capabilities” (Gulati, 1995:625), making it easier to become aware of new opportunities for co-operation that would be difficult to identify outside of a closed relationship. Trust built by such ties “reduces the hazards associated with future transactions and increases the parties' interest in future ties” (Gulati, 1995:625). Direct ties are not the only ones that account for trusting relations.

#### **1.3.2.2. Structural dimensions (indirect ties)**

Indirect channels of communication that give information about the suitability and trustworthiness of prospective partners serve as referrals by making others aware of the availability of potential partners. Referrals are an effect mechanism for enforcing trust as they have associated effects on reputation, in that each party is aware that the other has a lot to lose from behaving opportunistically (Gulati & Gargiulo, 1999).

There is a distinction between structurally equivalent organisations and common third parties (Gulati, 1995). Structurally equivalent organisations have a number of common connections and “a similar pattern of relations in a system” (Gulati, 1995:628). According to (Gulati, 1995:628) “they are of similar status and develop similar perceptions of the utility of pursuing a given behaviour”. Common third party relations focus on cohesion by taking advantage of

information benefits and encouraging behaviour that is trust enhancing, while organisations that are status seeking tends to seek potential like-minded partners, and those organisations that are cohesion seeking will tend to seek trustworthy partners (Gulati, 1995).

#### **1.3.2.3. Cognitive dimensions**

Cognitive dimensions are embodied in attributes like domain consensus, a shared code, or a shared paradigm that facilitates a common understanding of collective goals and proper ways of acting in a social system. There is clear agreement among participants about the role and scope of ties (Gulati, 1995; Tsai & Ghoshal, 1998).



#### **1.3.2.4. Positional dimensions**

As a mechanism that influences the emergence of an IOR, positional dimensions go beyond direct and indirect ties. An organisation that occupies a central position in a social network is more visible compared to others and accesses information faster than rivals about the reliability of potential partners. In such a case “occupying a central location in a social interaction network is likely to be perceived as trustworthy by other actors in the network” (Tsai & Ghoshal, 1998:466). It also has easier access to specific resources.

### **1.3.3. The dynamic process**

Relational, structural, cognitive, and positional dimensions are the static aspects of the emergence of an IOR that the collaboration function must deal with. Once parties are satisfied with these aspects, engagement commences, where parties meet to negotiate and to get commitment, and prepare implementation plans. These events are connected in a temporal order and are themselves dynamic processes that develop in stages and are recurrent cycles that are critical to the evolution of an IOR (Arino & de laTorre, 1998; Doz, 1996; Ring & Van de Ven, 1994).

Central to emergence and evolution of IORs and their managing is process (Ring & Van de Ven, 1994:91) and they note that:

- “process issues have important temporal implications for performance” (Ring & Van de Ven, 1994:91) as partners in a relationship use them as a basis to judge whether the relationship is equitable and efficient,
- process issues influence “motivation to continue in, or terminate, the relationship over time” (Ring & Van de Ven, 1994:91),
- managers, as agents of their organisations, need to know (1) input conditions, investments, and types of governance structures required for such a relationship, and (2) ways to negotiate, execute and modify the terms of the IOR.

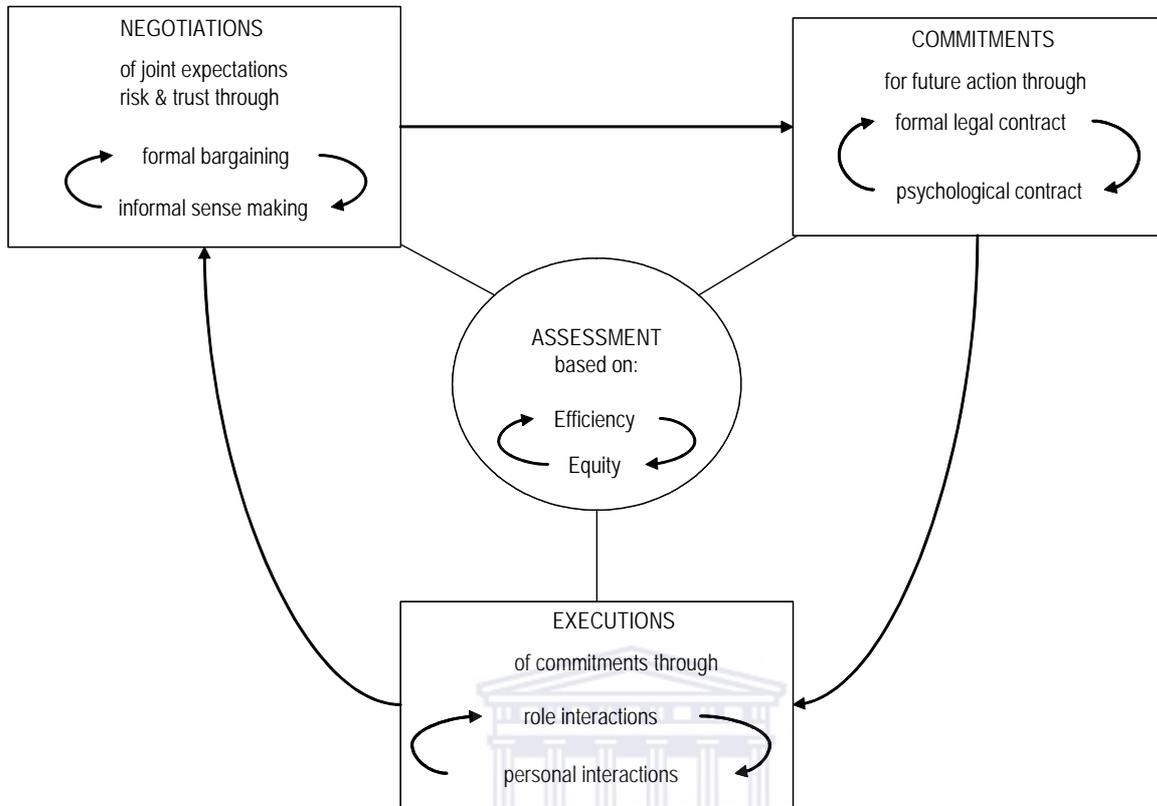
Ring and Van de Ven (1994) identified process as central to the management of inter-organisational relationships, and argued that the theory of process consists of statements about temporal sequence of events. An event is a theoretical construct; in developmental process (referred to as dynamic process in this paper), these

constructs are negotiation, commitment, and execution, each of which are assessed according to Ring and Van de Ven (1994) in terms of efficiency and equity (Fig 1.5). Each construct is taken as an event, where any number of incidents can act as indicators that the event has happened. These events are the processes that are mechanisms for creating and delivering value. A variety of processes that could be cycles spirals or sequences are the building blocks of IORs (Lofland & Lofland, 1995). The development of an IOR has teleological, evolutionary, dialectic, and cyclic processes (Van de Ven, 1992), which need management: (1) to allow the formation of an IOR to occur, (2) to put governance mechanisms in place that will allow the evolution and dissolution of an IOR to occur, and (3) to enable performance and harvesting of benefits within an IOR.

#### **1.3.4. Managerial functions in IORs**

Management of an IOR is about managing relationships. First, this is at social network level, and leads to formation by ensuring that an organisation has the resources that it needs to achieve its stated objectives. This continues through the evolution of an IOR. These resources can be categorised as money, which can be transformed from one form to another, information that is needed for decision making and successful completion of tasks, and moral support that ensures the legitimacy of the organisation. This management of resources will be referred to as collaboration. Second, is the choosing of governance mechanisms and implementing them, which will be called co-operation. Finally, the management of tasks, activities, and events, which will be called co-ordination.

**The dynamic process model**



**Fig 1.5:** Source: Ring & Van de Ven, 1994.

**1.3.5. Outcomes sought by management**

The dynamic process provides opportunities for the managerial effort to be directed at formation, governance, and performance of the IOR. Although all levels of management should be involved in these desired outcomes, senior management should be responsible for formation, middle management for governance and lower-level management for performance.

### **1.3.5.1. Formation**

Managerial effort is directed at the strategic context and content. The strategic context refers to how involvement in an IOR will help realise the strategic objective of the organisation. The strategic content refers to identifying what will be done within the IOR that will help the organisation to achieve its business objective. Once parties have negotiated and are committed to what will be done, this is executed by agreeing tentatively to enter into a formal agreement.

### **1.3.5.2. Governance**

The formal agreement is entered into by identifying the transaction and what would be done to implement it. The risk involved in the transaction and the level of trust among parties will determine the type of governance structure that the IOR will take. The dynamic process drives the choice of the type of governance structure that will also enable the harvesting of identified benefits.

### **1.3.5.3. Performance**

Performance depends on how parties conduct the tasks assigned to each party and those that will be jointly performed. Identifying these tasks and assigning resources to them is critical to harvesting the identified benefits. The strategic objectives of the IOR and those of the involved parties and the governance structures will determine whether the IOR will have co-operative or competitive aspects or both.

## **1.4. Conclusion**

The integrative approach incorporates both the qualitative and quantitative approaches to research. It offers a method to social scientists to use qualitative methods to develop models and then test those using quantitative methods. This is what is referred to as triangulation, and as such, the integrative framework incorporates triangulation, which if fully utilised can be a source of validity to the research method. The use of propositions improves the development and testing of theories. The research approach in this report is appropriate in that it is part of theory development of IOR.



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## **Chapter 2: Collaboration**

### **2.1. Introduction**

Organisations are key community actors and their interaction networks are key social structures that act as “delivery systems that meet the demand for goods and services and also function to protect certain special interests” (Galaskiewicz, 1979:1346). According to Galaskiewicz (1979), these interaction networks enable organisations to occupy positions of influence within networks. This enables the “organisational elites to protect their organisations’ interests by establishing exchange relationships that secure boundaries and ensure survival of their organisations in a competitive environment” (Galaskiewicz, 1979:1347). This interaction affords opportunities for ties to develop that play a role in yielding information about resources, capacity, and trustworthiness of potential partners. This information about potential partners is acquired directly by experience in past and/or current ties or through third parties who have had ties with potential partners (Gulati, 1995). According to Gulati, information acquired directly is referred to as relational and that through third parties as structural. This information plays an important role in establishing the basis of resource interdependence (Gulati, 1995).

When information is freely available and equally accessible to all actors, in such a context, if there is any case of interdependencies, actors will face and systematically identify partners through whom they could resolve those interdependencies (Gulati, 1995). Another way of looking at this is that strategic

actions of organisations are outcomes of matches between their competencies and external opportunities (Gulati, 1995). Collaboration is the managerial function that identifies, facilitates, and monitors the implementation of the strategic intent.

## **2.2. Collaboration**

According to Spekman, Isabella, and MacAvoy (2000:2), senior managers see being involved in IORs “as a means of survival and value creation”. IORs provide opportunities to leverage market presence and prowess, technological capability, and financial resources of other organisations. Parties in IORs also seek complementary resources and synergistic effects by seeking potential partners “with skills, expertise, and competencies that do not overlap” (Spekman, Isabella, and MacAvoy 2000:3). IORs are not only about business, they are also about people and relationships; therefore, ultimate goals in managing an IOR are to achieve the desired strategic returns and maintain a win/win relationship (Lynch, 1993). To maintain a win/win relationship, there are expectations surrounding the rules of engagement and how partners are expected to behave with each other.

To achieve strategic returns, the following are identified as reasons or motivations for collaboration (Bamford et al, 2003):

- setting standards: industrialised economies have been shifting from heavy industry to high technology, making setting standards an important activity,
- sharing risk: this is associated with developing new technologies,

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- entering emerging markets: access to new consumers or to secure low-cost production centres,
- expanding product lines: parties can use resources in an IOR to expand their product lines,
- reducing costs: by combining similar assets and reducing common costs,
- gaining market share: by leveraging IOR resources and capacity, parties can increase market share,
- creating new businesses: combining complementary capabilities and creating wholly new sets of skills.

To be able to implement strategic intent to meet these objectives, those responsible for the collaboration function need information. Information is not freely available and accessible to all organisations. Social networks play an enabling role by acting as conduits of information to the collaboration function.

### **2.2.1. Social networks**

Information that senior managers obtain in social networks are a result of different types of transactions, which may be episodic or long-term, that determine the nature of the exchange relationship. The type of information exchanged in social networks identifies the type of that social network. Galaskiewicz (1979) identified money networks, information networks and moral support networks as social networks that organisations use to mobilise resources to cope with different aspects of their environment. Money plays a major role in the exchange of goods

and services, information helps in management of risk brought by uncertainty, and moral support helps insure a participant's legitimacy. The liquidity of these resources enables individual actors to negotiate with one another, increase their own power relative to others, and ensure a position in the hierarchy of organisations that inevitably will evolve.

Some organisations easily gain moral support and access information that they need to enable them to secure money that they can use to procure other resources to enjoy competitive advantages over others. Such organisations access money due to the positions they occupy in social networks because these positions generally give them better access to all others in the system, making them structurally resourceful organisations. For an organisation to be able to secure boundaries and access resources, it must occupy key co-coordinative positions in these three resource networks. Networks of money, information, and support are important macro-social structures in a community (Galaskiewicz, 1979).

Information obtained from social networks helps managers to identify how best to use the organisational capacities and competencies by becoming involved in IORs. Involvement inevitably creates strategic interdependency that managers should strive to mitigate.

### **2.2.2. Strategic Interdependency**

Interdependency arises when one organisation has resources or capabilities beneficial to but not possessed by the other. Such interdependency could be intra-

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industry or inter-industry. Organisations deliberately seek prospective partners with complementary resources or beneficial capabilities (Gulati, 1995). Access to market information to identify viable partners and evaluate the reliability of potential partners becomes a strategic managerial function.

The dependency on others for resources needed to conduct business brings uncertainty in organisations as successful delivery of services or products to customers depends on others. Organisations would like to reduce this uncertainty. An IOR is a “means by which organisations manage their dependence on other organisations in their environment and attempt to mitigate the uncertainty generated by that dependence” (Gulati & Gargiulo, 1999:9).

Organisations use social networks as resources to identify strategic interdependency. This is consistent with resource-based theory in that having resources or access to resources can provide enduring competitive advantage to an organisation, especially if those resources are inimitable and not readily substitutable (Gulati, Nohria & Zaheer, 2000). Collaborative activities play an important role in the accessing of inimitable resources and capabilities through social networks. Further collaboration is instrumental in identifying, creating, and managing relationships. If this activity results in the emergence of an IOR, consistent with the resource-based perspective, then the relationships and the IOR have inimitable and non-substitutable value. The relationships become the basis for the dynamic process through which managerial effort become developmental and a value-creating process.

*Proposition 1*

1. Social networks facilitate negotiation and commitment by providing information about potential partners.

1.1. A money network is a social network.

1.1.1. A money network provides financial information about potential partners

1.2. An information network is a social network.

1.2.1. An information network provides information about whether potential partners have the appropriate tacit knowledge.

1.3. A moral-support network is a social network.

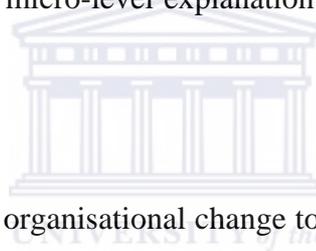
1.3.1. Moral-support networks provide information about whether potential partners have or will bring the appropriate legitimacy.

**2.2.3. Dynamic process and process theory**

In their seminal paper, Ring and Van de Ven (1994) identified process as central to the management of IORs. The theory of process consists of statements about a temporal sequence of events that explain how an observed stream of incidents or occurrences unfolds (Van de Ven & Poole, 1990). A process is as an invention and/or re-use and “implementation of ideas by people through transactions over a period of time in an institutional context that allows the people involved judging the outcomes of their efforts and acting accordingly” (Van de Ven & Poole, 1990:314). Each stage of an IOR has its own processes that connect in a temporal sequence of events. The whole IOR can be viewed as a complete single process that is a result of nested processes.

An understanding of different types of processes is important in understanding the complexity of events and the need to account for temporal connections among events, different time scales in the same process, and the dynamic nature of processes (Van de Ven & Poole, 2005). Van de Ven and Poole (2005:1384) argue that process explanations may include:

1. “an account of how one event leads to and influences subsequent events (e.g. events of type A have a 0.7 probability of being succeeded by events of type B and a 0.3 probability of being succeeded by events of type C),
2. an explanation of the overall pattern that generates the series (e.g. the process develops in three stages or recurrent cycles of A, B, and C), or
3. both (in which case the micro-level explanation and overall pattern should be linked)”.



Processes enable change or organisational change to occur. “To understand how a change occurs requires a story that narrates the sequence of events that unfolds as the changes occur over time” (Van de Ven, 1992), and this understanding happens when we move from description to explanation. “Explanation requires a story, and stories can be understood as process theories” (Van de Ven & Poole, 2005:1386). The meaning of process is defined as a developmental event sequence where “a sequence of events or activities describes how things change over time” (Van de Ven, 1992:170) that are observable or underlying patterns of unspoken cognitive choices, emotions or motivations, which are not directly observable (Van de Ven, 1992).

### **2.3. Dynamic process of IORs**

Ring and Van de Ven (1994:96) state, “From a developmental perspective, IORs are socially contrived mechanisms for collective action, which are continually shaped and restructured by the actions and symbolic interpretations of the parties involved”. Zajac and Olsen (1993) proposed a model of an IOR composed of an initialising stage, a processing stage, and a reconfiguration stage, with feedback loops to the earlier stages. Zajac and Olsen’s model is similar but seen as less robust to that of Ring and Van de Ven (1994) because it can be argued that it does not allow for a dynamic process. In the model, the temporal occurrence of stages of negotiation, commitment, execution, and assessment may be almost simultaneous in simple transactions. As shown earlier based on the work of Ring and Van de Ven (1994), the duration of each stage varies according to the following (a) the uncertainty issues involved, (b) disputes and the reliance on trust among the parties in an IOR, (c) assessment based on efficiency and equity, and (d) the role relationships of the parties.

Gulati (1998) identified formation, governance structures, dynamic evolution (dynamic process), performance and performance consequences for organisations as five key issues in IORs. In identifying these issues, Gulati also cited studies that have sought to uncover formal and informal processes that influence key stages that unfold in IORs. Zajac and Olsen (1993:142) agree with the process approach and when they argue that interorganisational exchange processes can be described in distinct temporal and logical stages. As argued earlier, the development and evolution of IORs consist of “repetitive sequences of negotiation, commitment,

execution”, and assessment stages (Ring & Van de Ven, 1994). These are repetitive evolutionary process cycles (Doz, 1996). These cycles enable the formation and governance of an IOR to occur and, importantly, its performance. As noted earlier (Van de Ven & Poole, 2005), events in the cycles lead to and influence subsequent events (e.g. formation, governance structures and performance), leading to an overall pattern that generates the series emergence, evolution, and continuation or dissolution of the IOR. The cycles are at a micro-level and the series at an overall level.

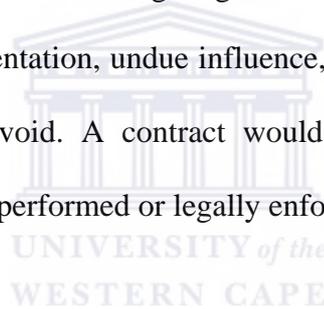
### **2.3.1. Negotiation stage**

In the negotiation phase, “parties develop joint (not individual) expectations about their motivations, possible investments, and the perceived uncertainties of a business deal that they are exploring to undertake jointly” (Ring & Van de Ven, 1994:97). The focus is on formal bargaining over possible terms and procedures of a potential relationship. Bargaining is about initial conditions, “comprising a definition of the task to be performed, a set of action routines borrowed from the organisational context of each partner, a design for the interface between the partners, and a series of expectations about the performance of the IOR towards and within it” (Doz, 1996:64). Underlying these formal bargaining proceedings are social-psychological processes of sense making, or enactment, that lead otherwise independent parties to enter into negotiations with one another. Both formal bargaining and informal sense-making processes are necessary in order to provide participants with opportunities to assess uncertainty associated with the

deal, the nature of each other's role, the other's trustworthiness, their rights and duties in the transaction, and also their commitment.

### **2.3.2. Commitment stage**

Commitment among parties is recognised when a formal or an informal agreement is reached on the obligation and rules for future action in the relationship. An important activity here is defining the terms and governance structure of the relationship. A formal relationship contract, or an informally understood psychological contract among the parties, is the basis for defining the terms and governance structure of the relationship. The degree of business risk and trust are critical factors in drafting the formal legal agreement to avoid legal impediments, such as mistake, misrepresentation, undue influence, or duress, which may render the relationship null and void. A contract would contribute to ensuring that commitments are willingly performed or legally enforceable.



### **2.3.3. Execution stage**

The commitments and rules of action are effected at this stage; the parties give orders to their subordinates, buy materials, pay the amounts agreed upon, and administer whatever is needed to execute the agreement. Formally designated role behaviour by parties reduces uncertainty when they execute commitments and makes interactions among parties predictable. Through a series of role interactions, parties may become more familiar with one another as persons, and they may increasingly begin to rely on interpersonal, as opposed to inter-role, relationships. Roles and personal relationships are important aspects of the

dynamic process as task execution mechanisms and the basis of managerial functions in their management of IORs. As management at different levels execute task, reflection on their performance avails the opportunity for assessment.

#### **2.3.4. Assessment**

Efficiency is a major criterion used for assessment in most standard models of economic exchange. Transaction-cost theory is one of the economic models that deal with efficiency. It focuses on a transaction and identifies those characteristics that may be implemented in a cost-efficient way. According to Williamson (1979; 1991), the characteristics of a transaction could be:

- Attributes: (1) uncertainty, (2) frequency - one time, occasional or recurrent, (3) asset specificity, (4) ease of measurement,
- Contractual relations: (1) frequency, (2) uncertainty, (3) investment characteristics - non-specific, mixed, idiosyncratic;
- Individuals involved: (1) bounded rationality, behaviour intended may be rational but only limitedly so, (2) opportunism: (a) blatant - breach contracts whenever binding reasons do not exist, (b) subtle - strategic, i.e. self-interest seeking with guile, (c) natural form - tilting the system at the margin;
- Governance structures: (1) performance attributes: (a) autonomous adaptability, (b) co-ordinated adaptability, (2) instruments (attributes): (a) incentive intensity, (b) administrative controls;
- Institution: (1) intuitional arrangements - these are arrangements that govern the ways in which units can co-operate and/or compete, (2) institutional

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environment - set of fundamental political, social, and legal ground rules that establish the basis for production, exchange, and distribution.

These characteristics of a transaction affect the determination or assessment of the efficiency of the transactions that will be carried out in an IOR. For example, frequency of a transaction could be assessed in terms of the most expeditious and least costly governance structure for undertaking a transaction, given production-cost constraints. Efficiency focuses on the assessment of the transaction, since people are also involved another criterion is equity, which assesses the relationship.

Equity is an important criterion for assessing co-operative IORs. It is fair dealing, which does not require that inputs or outcomes be always equal between the parties. It has its roots in exchange theory, in which individuals seek to reconcile their self-interests with the need to maintain social relationships. In fair dealing, reciprocity is sufficient, but equivalence in the *quid pro quo* is not necessary. Fair dealing as a standard for assessing co-operative IORs can be influenced by the personalities and individual differences of transacting parties, particularly in ambiguous situations.

Parties in IORs are motivated to seek both efficiency and equity outcomes so that they can preserve a reputation for fair dealing. A reputation of this nature is important in securing repeat transactions and for good referrals. It is in parties'

self-interest to resolve disputes and maintain the relationship in transaction-specific investments, which are under conditions of high uncertainty.

The dynamic process avails an opportunity for assessment as the IOR emerges, evolve, and dissolve and as such become an important delivery mechanism of IOR sought benefits. Assessment based on efficiency and equity provides parties with an evaluation mechanism that deals with issues of uncertainty, what will be assessed and how, disputes, and how the relationships will be managed, and this lead us to our second proposition:

*Proposition 2*

2. Developing joint expectations among parties increases the effectiveness of collaboration
  - 2.1. Establishing possible efficiency and equity measurements of a transaction as it relates to all parties is developing joint expectations.
    - 2.1.1. Efficiency and equity are outcomes sought for in collaboration.

## **2.4. Issues in dynamic process**

An IOR emerges when managers bargain over either the production or the transfer of property rights. Property rights entail specific, long-term investment in a business deal or a venture that cannot be fully specified or controlled by parties in advance of their execution.

### **2.4.1. Uncertainties**

There are two types of uncertainties: (1) uncertainty regarding future states of nature, and (2) uncertainty whether the parties will be able to rely on trust to counter the problems of adverse selection and moral hazard. Given this uncertainty, parties within a relationship need to trust each other.

“Trust reflects the extent to which negotiations are (or are expected to be) fair and commitments are sustained and a party’s belief that its requirements will be fulfilled through future actions undertaken by the other party”, and this gives trust an interpersonal and organisational dimension (Claro, Hagelar & Omta, 2003:706). The following two views of trust encompass these dimensions:

- a business-risk view based on confidence in the predictability of one's expectations, where parties hedge through contractual means such as guarantees, insurance mechanisms, laws, and organisational hierarchy (Ring and (Ring & Van de Ven, 1994) ,
- a view based on the confidence in another's integrity and the goodwill of others produced through interpersonal interactions that lead to social-psychological bonds of mutual norms, sentiments, and friendships (Ring & Van de Ven, 1994).

In developmental processes, where parties co-operate over the use of tacit know-how or invisible assets, as compared to the use of tangibles or codified know-how assets, trust will play an important role in building confidence in another's integrity and the predictability of one's expectations. Apart from relying on trust in

reducing uncertainty due to risk, explaining processes in each stage and explaining transitions from one stage to another can go a long way. Another way of looking at this is to make a distinction between transactional and relational exchanges. In transactional exchange, current events are viewed separately from events preceding and following it and from other events accompanying it temporally. Relational exchanges are an on-going dynamic state, no segment of which - past, present, or future - can sensibly be viewed independently from other segments. Such separation allows the possibility of assessing the activities.

#### **2.4.2. Assessment based on efficiency and equity**

As the IOR emerges, evolves, and dissolves, parties should always deal with this important recurrent issue. The managerial function role in each stage of an IOR should adequately deal with or put mechanisms in place that will assess the IOR in terms of efficiency and equity. Managers involved should focus efficiency measures on the transactions parties are involved in, and the focus on equity should be directed to the relationship matters within the IOR.

#### **2.4.3. Internal resolution of disputes**

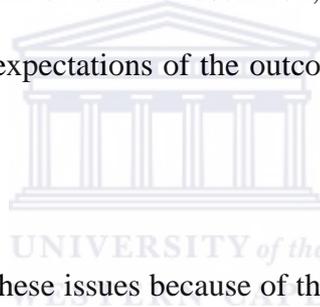
Benefits accrue to parties from preserving their relationships where there is a greater transaction-specific investment made under conditions of uncertainty, as economically redeploying assets committed to the IOR will be inefficient. In addition, in the temporal development of an IOR, social-psychological processes will create a separate set of pressures to preserve the relationship. These endogenous safeguards may end up in contracts that are more formal. As time

progresses, informal and psychological contracts are replaced by formal legal contracts that rely on trust stemming from prior fair dealing. The ability of parties to interchange personal relationships and role relationships also plays an important role in the resolution of disputes.

#### **2.4.4. Relationships**

In IORs, relationships emerge, evolve, grow, and dissolve over time because of individual activities. Actions of individuals affect IORs in three ways:

- in defining the degree of uncertainty associated with an exchange,
- in specifying the extent to which the parties can rely on interpersonal-based trust as an alternative form of conflict resolution,
- in defining the parties' expectations of the outcome to include both efficiency and equity.



Individuals have views on these issues because of their roles within organisations.

It is important to note that, although it is their organisational roles that are important, individuals often use interpersonal relationships to get things done.

Their interpersonal relationships are not identical to their role relationships.

There is an important relationship between these roles in an IOR. Ring and Van de Ven (1994:96) argue, “The ways in which individuals make attributions about others’ intentions and behaviours will vary significantly if the other is viewed as acting within a *role* as opposed to *qua persona*. When a person is willing to attribute sincerity or trustworthiness to *qua persona*, behaviour, this does not mean that the person will do the same if the individual were behaving in a role

context. Consequently, if individuals rely on trust in their *qua persona* relationships, they may be unable to do so when acting as agents for their organisations”. The advice to individual from Ring and Van de Ven (1994:96) is that, “in dealing with uncertainties brought upon their roles”, individuals must employ formalized contracts and exogenous safeguards that their organisations can recognize instead of relying exclusively on trust.

## **2.5. Formation of IORs**

In understanding how IORs emerge, understanding how people make present commitments to engage in uncertain future courses of action and the sources of security that lead them to believe that the terms of their representations and commitments are congruent and will be enforceable it is imperative that something that symbolises such a commitment be created. Parties normally gather to affirm a present sense of congruence of purpose, values, or expectations among those involved Ring and Van de Ven (1994). Senior members make speeches directed at the human need for identity and inclusion that create an environment conducive for bonding processes. These activities raise an expectation of both tangible and non-tangible outcomes and focuses on the implicit co-alignment between partners to learn and acquire skills, products, technology, and knowledge that are unique to that IOR (Spekman, Isabella & MacAvoy, 2000).

Although IORs emerge through a variety of “starting conditions, such as pre-existing friendship ties, institutional mandates, resource dependence”, or

brokerage activities “by venture capitalists, corporate sponsors, or investment bankers” (Ring & Van de Ven, 1994:100). These starting conditions have an impact on how one comes to know oneself in relation to others, and therefore affect negotiation, commitment and how rapid execution occurs. In IORs, parties who had “prior economic relationships or social ties tend to develop” relationships more quickly and efficiently than “parties who, initially, were strangers” (Ring & Van de Ven, 1994:101). Presentations and documents to formalise the relationship will reflect on the journey that parties travelled to reach the stage of celebrating the formalising of the agreed relationship. Therefore, our third proposition is:

*Proposition 3*

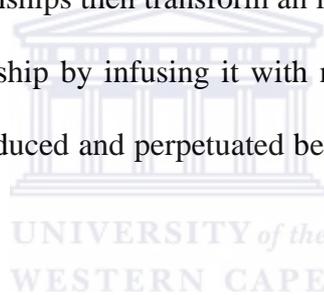
3. Formal negotiations to collaborate are successfully concluded by establishing formal commitments that symbolise the formation of an IOR
  - 3.1. Individuals or groups interacting and negotiating to collaborate with mandates from their organisations are involved in formal negotiations to collaborate
    - 3.1.1. Successful formal negotiations are concluded by establishing formal commitments like a memorandum of understanding (MOU) or a launch party.

## **2.6. Conclusion**

Social networks provide resources and information, endow parties who intend to be involved in IORs with reputation, and therefore contribute to efficiently and

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successfully negotiating, committing, and executing the stages in the emergence or formation of an IOR. Formation of an IOR is facilitated by senior management collaborative efforts and through their roles relationships. Social networks are conduits for information that identifies resources and potential partners, and therefore kick-starting formal bargaining and informal sense-making processes. The dynamic processes play an important role in realising the managerial objective of the formation of an IOR. Collaboration as a management function should therefore focus on understanding how social networks and dynamic processes contribute to the formation of an IOR. Collaboration institutionalises IORs by infusing them with value through establishing role and personal relationships. These relationships then transform an instrumental transaction into a socially embedded relationship by infusing it with norms and values that permit the relationship to be reproduced and perpetuated beyond the immediate tenure of its founders.



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## **Chapter 3: Co-operation**

### **3.1. Introduction**

Institutionalisation of IORs “objectifies and internalises the identity, mission, and procedures of a relationship into congruent expectations of participants and gives it a social integration that goes beyond its formal, legal structure of governance and economic exchange” (Ring & Van de Ven, 1994:103). Formal and informal processes influence the dynamic processes of negotiation, commitment, and execution that institutionalise relationships. Co-operation as a management function plays a critical role in the institutionalisation process. Ring & Van de Ven (1994:103) identify the following as the driving forces behind interactions that enable institutionalisation: (a) personal relationships that supplement formal role relationships, (b) psychological contracts that are substituted by formal legal contracts, and (c) the temporal duration of relationships that should extend beyond the tenure of initial contracting individuals, that is, formal agreements mirror informal understandings and commitments. Co-operation in management facilitates the social integration of IORs by implementing them through hierarchy, market, and contract mechanisms.

### **3.2. Co-operation**

Co-operation involves creating IOR structures with the basics being making “financial and legal arrangements - for example, valuation of partners’ contributions, value-sharing mechanisms, transfer pricing, exclusivity, product,

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and market scope, length of contract, and exit provisions” (Bamford et al, 2003:68). Although these are essential elements of an IOR structure, “incentive alignment, decision processes, and evolution are critical in creating a structure that produces success” (Bamford et al, 2003:68). In making, these arrangements or creating IOR structure, Doz and Hamel (1998:142) counsel that co-operation should involve the organizational context of IOR, the content of focus and the process on which processes must focus.

- Context: the strategic context of an IOR combines three elements: (1) “the strategic scope the partners see in the” IOR, (2) “the way the partners frame the” IOR by putting it in one or another category of relationships, and (3) “the ambitions the partners hope to fulfil within that scope”, that is, the benefits sought.
- Content: this refers to the task that will be performed jointly or the transaction as defined in the transaction-cost theory (Williamson, 1979; 1991).
- Process and norms of interaction: this is where intentions are converted “into reality through interactions”.

Bamford et al. (2003:70) argue that co-operation “is a way of managing an open-ended agreement between two or more organisations”. According to Bamford et al. (2003:70), “an open-ended agreement is one in which not all terms, conditions, and contingencies are defined at the outset; instead, it is accepted that the agreement will change and evolve over time and fill in some of the apparent gaps”. Managing an open-ended agreement involves “a way of sharing the task of making decisions in the future and provides a way to govern future negotiations

between organisations - it is a recognition that the initial agreement is in some sense incomplete” Bamford et al. (2003:70). They point out that the key to making an IOR work is effective governance of the "open end", and that there are three governance structural levels: (1) strategic decision-making and overall performance monitoring, (2) tactical resource management, and (3) executing work within the various components of the IOR.

*Proposition 4*

4. Agreement on the obligations and roles for future action in the relationship increase the likelihood of successful co-operation.

4.1. Committing resources and establishing how the combination will be accomplished complies with the requirement for agreement on obligations and rules for future action in the relationship.

4.1.1. Committing resources and establishing how they will be combined increases the likelihood of successful co-operation.

Hierarchies, markets, and contracts define the role of IOR governance as they determine information flows, establish decision-making rules and processes, delineate executive responsibilities, and integrate partner operations.

**3.2.1. Hierarchies and hierarchical control**

The logic behind hierarchical controls is that they “assert control by *fiat*, provide monitoring, and align incentives” (Gulati & Singh, 1998:782), making

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hierarchical control an effective mechanism in the management of uncertainty. This is in line with transaction-cost economists' arguments in that anticipated appropriation concerns are the primary basis of the choice of a governance structure (Williamson, 1979: 1991). In situations where participants anticipate such concerns, hierarchical controls have the ability to manage potential moral hazards. Resource-dependence theorists also favour hierarchical controls in dealing with moral hazards as exchange relations between superiors and subordinates within an organisation is seen in terms of power relations that give superiors authority to deal with the uncertainty raised by moral hazards (Gulati & Singh, 1998).

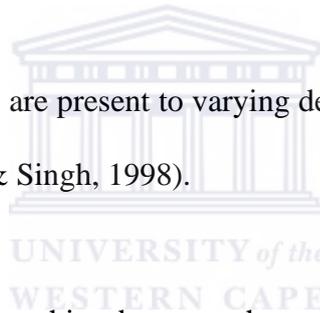
Parties involved identify and decompose tasks, and then assign tasks specifying a precise division of labour across partners in the IOR, according to those tasks that will be completed jointly or individually, with related communication and decision-making complexities that have cost-related co-ordination implications for the parties involved (Gulati & Singh, 1998). Task interdependence raises uncertainty, which requires superior information processing to co-ordinate. Hierarchical controls are an effective solution to such type of uncertainty. Hierarchical controls provide superior task co-ordination in situations involving high resource interdependence and high co-ordination costs, which is a similar argument to that raised by both resource-based and transaction-cost theorists.

Within hierarchies, there are contractual relationships that have hierarchical control elements embedded in them, such as (Gulati & Singh, 1998):

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- A command structure and authority system, and a system for certifying authoritative communications,
- Incentive systems that facilitate performance measurement and link rewards to performance,
- Standard operating procedures that allow quick decisions to be made by anticipating those decisions in advance,
- Dispute-resolution procedures that bypass courts and markets by specifying a hierarchy of entities or individuals to which appeals can be made,
- Non-market pricing systems, for example, cost-plus systems that enable greater precision in remuneration when changes in specification arise.

These hierarchical elements are present to varying degrees in different governance structures of IORs (Gulati & Singh, 1998).



IOR can benefit from hierarchies because they are effective in dealing with “transactions that have highly uncertain outcomes, recur frequently, and require unique or transaction-specific investments” (Ring & Van de Ven, 1992:485). IORs can simulate structures that typically include planning, rules, programmes or procedures that are important mechanisms for task co-ordination (Gulati & Singh, 1998). “Planning will involve presetting schedules, outcomes, and targets. Together with planning, rules, programmes and procedures emphasise formal control designed to minimize communication, simplify decision making, reduce uncertainty about future tasks and prevent conflicts” (Gulati & Singh, 1998:786). These elements allow the specification of regular meetings, roles assigned to

partners and, importantly, the type of IOR. This also serves to clarify boundaries on decisions and activities (Gulati & Singh, 1998). For example, procedures for dealing with disputes that may arise as partners deal with the task of co-ordination and the division of labour may be defined (Gulati & Singh, 1998). Such hierarchical controls serve to institutionalise or formalise interaction between partners. Each governance structure will be associated with distinct types and levels of hierarchical elements of control depending on the extent of anticipated co-ordination costs and interdependence at the time of the inception of the IOR (Gulati & Singh, 1998).

### **3.2.2. Markets and market control**

Markets are efficient facilitators of economic exchanges where there are many highly competitive and autonomous buyers and sellers bargaining over the transfer of property rights. Market transactions, or exchanges, are characterised by discrete contracts governing relationships for relatively short terms. Contractual relations governing markets can be specified, based on “sharp-in”, where they are accompanied by a clear-cut, complete, and monetized agreement, and on “sharp-out”, where the seller’s debt of performance and the buyer’s debt of payment are unambiguous (Ouchi, 1980; Ring & Van de Ven, 1992).

The first example is the ‘spot’ or sales contract where all obligations are fulfilled on the spot, an example being buying a can of coke: one asks for it and pays what the salesperson asks. Such contracts cannot deal with future transactions as individual buyers and sellers bear no dependency relation to one another. The

second one is the contingent-claims contract, where a document specifies all the obligations of each party to the exchange, contingent upon all possible future states of nature. Parties to a transaction maintain autonomy but are bilaterally dependent to a nontrivial degree. Identity is necessary if issues of premature termination arise or persistent maladaptation would place burdens on one or both parties. Ouchi (1980:133) argues, “given uncertainty, bounded rationality, and opportunism, contingent-claims contracting will fail”. Ring and Van de Ven (1992) agree with him but point out that it is a governance mechanism for competitive markets in which classical contract law is suitable in guiding the governance of relations, as any disputes can be referred to and can be resolved within any functioning justice system.

Sharp-in by agreement and sharp-out by performance emphasises and counsels partners to seek the efficiency-enhancing effects of competition and co-operation. In this regard, Lado, et al (1997:132) state, “managers should consider strategic phenomena as a firm’s quest for both competitive advantage and collaborative advantage by simultaneously competing and co-operating with stakeholders”. By selecting potential partners through current and prior ties, to negotiating roles, governance and performance measures can be achieved competitively in a co-operative way.

### **3.2.3. Contracts and contractual control**

Recurrent and relational contracting can also be effective in governing economic exchange relations (Ring & Van de Ven, 1992). Recurrent contracts involve exchanges of assets that have moderate degrees of transaction specificity, i.e.,

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limited asset mobility. Terms of exchange are certain, with contingencies left to future resolution. Contracts are short-term and parties are autonomous, legally equal, and “explore outcomes other than efficiency; they experiment with safeguards and alternative methods of resolving conflict” (Ring & Van de Ven, 1992:487). They are essentially; market-based transactions governed by neoclassical law (Ring & Van de Ven, 1992).

Relational contracts involve long-term investments based on relations established during recurrent bargaining. “The property, products, or services jointly developed and exchanged in these transactions entail highly specific investments; ventures involved cannot be fully specified or controlled by parties in advance of their execution. Disputes are resolved through internal mechanisms designed to preserve the relationship and insure that both the efficiency and equity outcomes sought in the long-term relationship are realised” (Ring & Van de Ven, 1992:487).

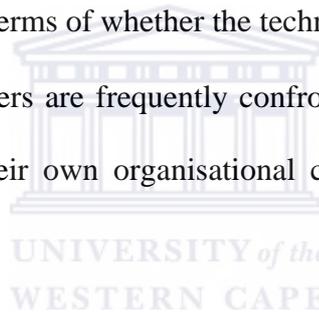
Agreeing on controls in hierarchies, markets and contracts, and how they will deal with interdependence and co-ordination cost, are issues central to governance of IORs. Deciding on the type of governance structure generally depends on the risk associated with the transaction and trust within relationships.

### **3.2.4. Risk and governance structure**

The responsibility of having to make decisions in ventures that are complex has risks for both the individuals and organisations involved. The risks are even more when the “accomplishing of the tasks involved requires the sustained co-operation with others” (Ring & Van de Ven, 1992:487). According to Ring and Van de Ven

(1992), uncertainty in transactions gives rise to different types of risks. Generally, these risks will arise in direct proportion to decreases in time, information and control. Ring and Van de Ven (1992) identify three categories:

- **commercial risk:** this type of risk involves the “probability of finding price-performance niches in the market”, that is, will the product or service meet the required demand at the price that will be charged.
- **technological risk:** technological risk involves the “probability of bringing technology to the market”. Another way of looking at this risk is to evaluate the probability of having or lacking the fundamental scientific knowledge required to produce a product. In addition, another useful way is to evaluate the engineering risk in terms of whether the technology will work.
- **corporate risk:** managers are frequently confronted with the need to choose between developing their own organisational capacities or to acquire them through mergers.



“Circumstances in which these forms of risk occur alone, or through co-operative arrangements, leads to corporate strategic risk” (Ring & Van de Ven, 1992:488). The type of risks that parties anticipate they will be confronting in the IOR will influence the choice of the governance structure of the IOR.

### **3.2.5. Trust and governance structure**

The need to work co-operatively over sustained periods of time means those parties must have “confidence in or be able to predict the expectations of others, and have confidence in the other’s goodwill” (Ring & Van de Ven, 1992:488). When others have confidence in parties that they are involved with, in that they

will do the right thing, it means that they trust them. In such circumstances, “idiosyncratic exchange relations that feature personal trust will survive greater stress and will display greater adaptability” (Ring & Van de Ven, 1992:488).

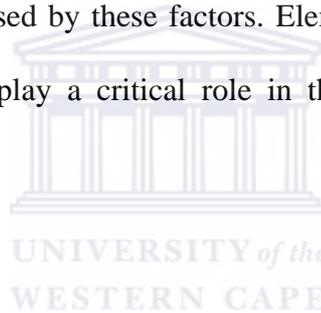
As argued earlier (Tsai & Ghoshal, 1998) identified trust as important and recognized in IORs as it can act as a governance mechanism. Ring and Van de Ven (1992) argue that trust emerges in two ways, in that it may be based on norms of equity or on prior ties. First, when norms of equity are the basis of trust, “one party judge that another party will fulfil its commitments and that the relationship is equitable” (Ring & Van de Ven, 1992:488). The elements of equity (Ring & Van de Ven, 1992) are (1) reciprocity, by which one is morally obligated to give something in return for something received. This is a social agreement that is “universal among societies across time and cultures” (Ouchi, 1980:137), (2) fair rates of exchange between utilitarian costs and benefits, and (3) distributive justice, through which all parties receive benefits that are proportional to their investments. According to Ouchi (1980:138), “a norm of reciprocity underlies all exchange mechanisms”. Second, utilitarian roots of being trustworthy. Ring & Van de Ven (1992:489) argue, “there are many non-legal sanctions which make it expedient for individuals and organisations to fulfil commitments”. In addition, reliance on trust by organisations can be expected to emerge between business partners only when they have successfully completed transactions in the past and they perceive one another as complying with norms of equity (Ring & Van de Ven, 1992).

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It follows therefore that, if trust is high among partners during the emergence of an IOR, both co-ordination costs and appropriation concerns are addressed, and therefore reducing the need for hierarchical controls in the IOR. According to Gulati & Singh (1998:790), the primary control mechanisms that “govern economic transactions between organisations are price, authority, and trust”, and Ouchi (1980) adds rules and tradition. Prices provide information for decision making as it is not easy to set correct prices in situations where there is a high degree of interdependence or uncertainty amongst partners as it is not easy to quantify skills contribution and other resources (Ouchi, 1980). Transactions between parties are “mediated by a price mechanism in which the existence of a competitive market reassures both parties that the terms of exchange are equitable” (Ouchi, 1980:130). Rules are “crude informational devices, specific to a problem, and a decision maker must know the structure of rules in order to apply the correct one in any given situation” (Ouchi, 1980:139). No organisation can specify in advance all rules that could deal with all situations. As situations arise that cannot be resolved by applying existing rules, they are referred to policy makers, who then create relevant rules (Ouchi, 1980). Traditions are not specified and are learnt or understood through experience (Ouchi, 1980:139). Trust plays an important role as a control mechanism in governance of economic transactions in that its presence during formation of an IOR influences participants in not considering hierarchical control mechanisms (Gulati & Singh, 1998).

“A key consequence of the embeddedness of economic transactions such as IOR in a social structure of trusting relationships is that the partners are likely to have

greater confidence in the predictability of each other's actions and thus anticipate lower appropriation concerns when they form an IOR" (Gulati & Singh, 1998:790). This trust obliges partners to behave loyally, gives them an opportunity to assess each other's behaviour in terms of appropriation concerns and affords them the ability to enforce property rights (Gulati & Singh, 1998). In situations where there is heavy interdependence and task co-ordination, trust can help in making the rules, routines, and procedures to be followed by partners (Gulati & Singh, 1998), this allows governance of transactions to be transparent. This can alleviate concerns about co-ordination cost. Trust has the ability to address both appropriation- and co-ordination-cost concerns and therefore allays the fears of uncertainty raised by these factors. Elements of risk in a transaction and trust in relationships play a critical role in the choice of the governance structure.



### **3.2.6. Relationship between risk and trust**

Organisations with successful prior transactions will not suffer the adverse affects of information asymmetry, as they will share information that reduces technological or commercial risk freely with each other (Gulati, 1995). Given a history of observing norms of equity, parties will trust others not to behave opportunistically when given access to proprietary information. This result in "management and contractual relations loosening constraints on operating autonomy employed to guard against opportunistic behaviour. These controls are normally manifest as *ex post* cost of contracting, such as bonding costs or agency costs such as monitoring expenditure of parties as principals" (Ring & Van de

Ven, 1992:489). The point is that the more an organisation transacts with different organisations, “the more its stock of information regarding the predictability or reliability of parties is likely to increase” (Ring & Van de Ven, 1992:489). With information about prior transactions, being easily and freely available to parties involved and as the ability to rely on trust increases, there is less risk inherent in a transaction.

### **3.3. Governance structures of IORs**

There are two types of IOR, namely, shareholding and contractual entities defined in terms of control (Gulati & Singh, 1998). In shareholding IORs, exchange agreements are such that participants share or exchange company-issued shares. Participants can create a new entity in which the shareholding is divided or buy shares in the other. “Shareholding is an effective mechanism for managing rent appropriation. Shareholding provides a mechanism for distributing residuals when *ex ante* contractual agreements are written but difficult to specify or enforce in a division of returns” (Gulati & Singh, 1998:791). Two types of shareholding entities are the joint venture and board representation through buying shares in another organisation (Gulati & Singh, 1998).

A joint venture is a separate entity in which parties own a portion of the shares. This allows the creation of “a separate administrative hierarchy of managers that sees to the day-to-day running of the business and deals with all matters that arise” (Gulati & Singh, 1998:792). A command structure, an authority and incentive system, and rules and procedures that are independent are set up. Standard

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operating procedures and dispute-resolution procedures are set during the formation of a joint venture (Gulati & Singh, 1998). All these elements allow a joint venture to have hierarchical controls in them. In board representation, partners buy minority shares in other organisations. This allows the investor to have command and authority by sitting on the board. Board representation affords the platform to exchange information, initiate, and ratify decisions.

In defining an IOR's governance, in terms of shareholding and contracts, it excludes markets as a governance mechanism. One reason is that the application of risk and trust has a limited scope as defined here. It does not include the contexts within which organisations pursue their strategies, strategic predisposition, stage of industry or product life cycle, and bargaining involved when transacting between parties from different nation states, cultures and languages. These contexts alter how trust and risk emerge and are perceived. This, however, does not take away the critical role that trust and risk generally play in conceptualising and implementing governance structures (Table 3.1). Contracts can simulate critical elements of the hierarchy in the markets, and contracts can simulate critical elements of a market in hierarchies (Ring & Van de Ven, 1992).

## A typology of governance structures

		Risk of transaction		
Reliance on trust Among the partners	1	2		Low
	Markets	Hierarchy		
	3	4		High
	Recurrent contract	Relational contract		
		Low	High	

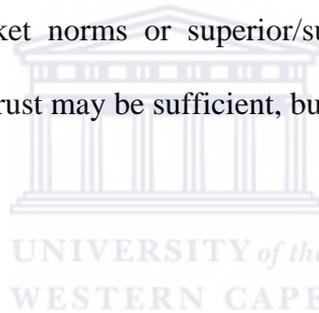
**Table 3.1** Source: Ring and Van de Ven, 1992.

### 3.3.1. Markets

The governance of transactions in markets are characterised by parties having easy and free access to information needed to evaluate commercial and technological risk (Ring & Van de Ven, 1992). Transactions are implemented in short periods to allow parties involved exercising appropriate levels of control, and parties do not depend on a single partner or their trustworthiness to accomplish a transaction (Ring & Van de Ven, 1992). In markets, “discrete contracts, classical contract law, and spot transactions provide an ideal combination for governing transactions” (Ring & Van de Ven, 1992:490). The courts can easily deal with “conflict, mistrust, or malfeasance” (Ring & Van de Ven, 1992:490), and reliance on trust is not necessary as transactions can be executed in instances where trust is nonexistent among parties.

### **3.3.2. Hierarchy**

In transactions having a high level of risk, with parties' sole objective as economic efficiency, and where time is of the essence in accomplishing the transaction, hierarchies offer an appropriate governance structure (Ring & Van de Ven, 1992). This unified governance structure mitigates opportunism and constrains it by role and authority relations (Ring & Van de Ven, 1992). In role relationships, disputes and conflicts are settled by "appealing to authority and *fiat*" (Ring & Van de Ven, 1992:491). Role relationships between legally unequal superiors and subordinates are institutionalised, reducing social relations to frictional matters (Ring & Van de Ven, 1992). In hierarchies, transactions are by discrete contracts and there is reliance on atomistic market norms or superior/subordinate role relationships. Reliance on high levels of trust may be sufficient, but need not be necessary.

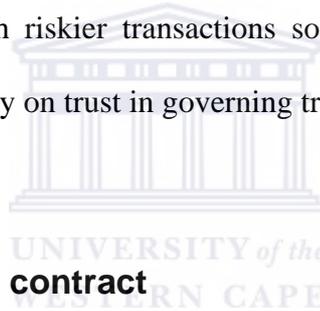


### **3.3.3. Contract**

The governance of transactions in contractual entities involves economic exchange relations of autonomous organisations without sharing or exchange of shares, and there are no formations of new organisations (as discussed above). Participants in these entities operate from the confines of their own organisations. Ongoing activities are jointly co-ordinated, and partners negotiate new decisions. "In contrast to the unified governance typically attributed to hierarchy, there is bilateral governance in relational contracts" (Ring and Van de Ven, 1992:487) but limited in recurrent contracts.

### **3.3.3.1. Recurrent contract**

Parties know that they have future needs within the transaction that they are undertaking, which they may not fully specify (Ring & Van de Ven, 1992). “Recurrent contracting enables the parties to build trust by demonstrating norms of equity and reciprocity”, and experiment by incorporating hierarchical controls in the contract (Ring & Van de Ven, 1992:491). Such experimentation with safeguards calibrated to higher degrees of risk and greater reliance on trust may offset the need to rely on the costly unified governance (Ring & Van de Ven, 1992). Neoclassical contract law gives the parties flexibility in governing transactions (Ring & Van de Ven, 1992). This flexibility both affords the opportunity to engage with riskier transactions sooner and offsets the parties’ inability to rely more heavily on trust in governing transactions.



### **3.3.3.2. Relational contract**

The nature of relational transactions is that of reciprocal dependency, which is “characterised by high asset specificity, uncertainty, and recurrence in a small-numbers’ bargaining condition” (Ring & Van de Ven, 1992:492). The uncertainty in these transactions is mediated by the embeddedness of IORs in social networks (Ring & Van de Ven, 1992). An important characteristic of relational contracting is the strong incentive to be involved with parties who are trustworthy. As transactions have a high level of risk, “high levels of trust are not only sufficient; they are also necessary” (Ring & Van de Ven, 1992:492). Relational contracting has in-built mechanisms, which are “a set of safeguards that are mutually agreed to by, and for, the immediate parties because they see their interests as

convergent” (Ring & Van de Ven, 1992:493) that achieve internal harmony and preserve relationships. Ring & Van de Ven (1992:493) argue, “Greater harmony flows from the increased production and transaction flexibility available to the parties through relational contracts”.

Transactions in an IOR that will require a high level of interdependence and have high co-ordination costs bring a high level of risk in the IOR (Gulati & Singh, 1998). If the management of the transaction is to be efficient, a high level of trust among parties will be required. This leads to the fifth proposition.

*Proposition 5*

5. Choosing a governance structure that optimises on risk and trust for a transaction increases the likelihood of an IOR

5.1. Markets are a governance structure

5.1.1. Markets are associated with low risk and low trust in a transaction

5.2. Hierarchies are a governance structure

5.2.1. Hierarchies are associated with high risk and low trust in a transaction

5.3. Recurrent contract is a governance structure

5.3.1. Recurrent contract is associated with low risk and high trust in a transaction

5.4. Relational contract is a governance structure

5.4.1. Relational contract is associated with high risk and high trust

### **3.4. Conclusion**

To achieve increased productivity and transaction flexibility at the same time requires managerial attention. Personal relationships and role relationships are critical in achieving co-operation between participating parties and realising these benefits. Co-operation refers to that managerial role that negotiates, gets commitment, and executes governance structures that recognize personal and role relationships that achieve increase productivity and transaction flexibility. Risk and trust play important roles in the dynamic processes that agree on and codify the governance structure.

Ring & Van de Ven (1994:105) argue that IOR implementation mechanisms involve formal codification of informal commitments, for the following reasons. First, relationships between firms imply that organisations, not individuals, are the principal parties to the IOR and that individuals act as agents for their respective organisations. Second, IORs will require formal documentation and standardisation, which will permit the IOR to be legally recognized beyond the time span of the individuals who negotiated the IOR. Third, the processes of institutionalisation transform informal commitments into organisational routines. Organisational routines are important because they are the ones that deliver products or services. Management must focus on synchronising activities between organisations into IOR routines that deliver IOR products and/or services. To be able to do this, the IOR initiates another cycle of negotiation, commitment, and execution for the purposes of co-ordinating resources and routines to meet the requirements as defined in formal contracts.

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## **Chapter 4: Co-ordination**

### **4.1. Introduction**

The importance of having formal governance structures in place between organisations is that this will enable role relationships to develop into personal relationships that are associated with the delivery of superior benefits to parties involved in an IOR. Individuals representing their organisations use personal and role relationships to avail themselves of material resources, know-how, and information to help deliver the stated benefits and to provide legitimacy to the IOR. The formalisation of role relationships is important in governing and anticipating the behaviour of parties that will affect the performance of the IOR. Parties can choose to be competitive, co-operative, or both. For the IOR to realise its objective, the co-ordination of resources and behaviour becomes an imperative managerial responsibility.

### **4.2. Co-ordination**

According to Spekman et al. (2000:89), “co-ordination describes the stage when the IOR goes to work”. Parties involved “organise their activities to achieve the espoused advantage, to realise scale and/scope, and to facilitate the seamless flow of materials and information between and among parts of the business in support of the work of the” IOR Spekman et al. (2000:151). Partners will be “scurrying around trying to do things; they have projects, and projects plans” are being developed and implemented Spekman et al. (2000:89). This stage is characterised

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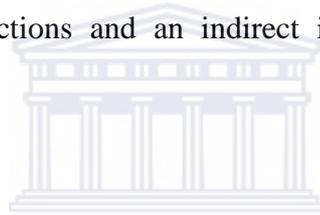
by focus on operations, tasks, division of labour and parallel activity. Co-ordination is the hardest management function in the IOR as partners must plan and execute the reality of their vision. In describing co-ordination as a control mechanism, Lynch (1993) noted the following:

- Co-ordination is accomplished by using excellent project management techniques that break down the tasks of IOR into discrete process steps by using people with good integration skills.
- For co-ordination to be effective, a strong communications system should be established, and “there must be delineation of the key issues that must be communicated, their frequency, and their criticality” Lynch (1993:157).
- Individuals “whose skills enable them to co-ordinate activities through effective communications are the best IOR managers. Co-ordination works when co-ordinating activities and communicating is everyone's job or is part of a team work function” Lynch (1993:198).
- Co-ordinators at the upper echelons use a variety of leadership styles to get the job done, picking a style that matches the current situation.
- “When problems emerge, the co-ordinator's role is to manage the decision making, not necessarily to make the decision, but in times of crisis or urgency, the co-ordinator may become the decision maker” Lynch (1993:198).

Central to the co-ordination function is the effective and efficient management of IOR resources.

#### **4.2.1. Sources of co-ordination**

Van de Ven and Walker (1984) identified the need for resources to achieve organisational goals as the most important factor that stimulates inter-organisational co-ordination. They note that during the initial phase of the emergence of IOR's, resource dependence influenced the development of inter-organisational communications and consensus, monitoring, monetary transactions and non-monetary transactions. As the IOR emerges, they noted that resource dependencies' greatest and most immediate effect was stimulating inter-organisational communications, which, in turn, had its most immediate and direct effect on formalisation of the IOR. Communication had an indirect formalising effect on monetary transactions and an indirect informalising effect on non-monetary transactions.



Another important issue Van de Ven and Walker (1984) identified was that the pattern of inter-organisational co-ordination depended on the kind of resources being co-ordinated. IORs “based on monetary transactions tended to have an impersonal and formalised mode of co-ordination, while non-monetary transactions reflect a more personal and informal co-ordination pattern” (Van de Ven and Walker 1984:617). They argue that non-monetary transactions are based on a more personal goal-congruence mode of co-ordination than monetary transactions, because of:

1. domain similarity, which is directly associated with consensus, i.e. ‘birds of a feather flock together’;

2. communication, which plays an important role in initiating and formalising procedures for non-monetary transactions; and
3. incremental engagements, which allow consensus to develop and emerge.

A distinguishing characteristic of monetary transactions is that they are “clearly measurable and analysable and therefore can easily be co-ordinated through formalised contractual arrangements” (Van de Ven and Walker 1984:617). Yet, non-monetary transactions are difficult to measure and analyse, thus making their co-ordination less formalized and more personal, relying on shared or complementary understanding on how such transactions should be implemented (Van de Ven & Walker, 1984). Van de Ven and Walker could not establish any relationship between consensus and conflict in terms of dependence on resources. What they noted was that as “parties begin to negotiate specific means or methods for conducting transactions, inconsistencies in the assumptions brought to the relationship begin to emerge”, and this leads to conflict with tendencies for a drive for greater autonomy (Van de Ven and Walker 1984:617). Resources involved and transaction costs of exchange between parties become central to the drive for autonomy, bringing complex dynamics in the relationship.

#### **4.2.2. Dynamics of co-ordination**

Madhok & Tallman (1998:327) argue that “transaction-cost perspective is primarily concerned with the management of transactions in an efficient manner, through the least costly (i.e. TC minimising) form of governance, under the assumption that there may be opportunism. On the other hand, the resource-based

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view is concerned with the management of resources in a manner that increases the competitive advantage and consequent rents from an organisation's resources". Transaction costs incurred in the exchange of resources are dependent on the nature of resources transacted, and, similarly, the returns realised from resources are dependent on the transaction-specific expenditures incurred in effectively combining them and maintaining the combination (Madhok & Tallman, 1998).

For value creation and realisation to happen, it is important to differentiate rent-yielding organisation-specific assets from the transaction-specific assets. There is interdependence between these two categories of assets. Lado, Boyd and Hanlon (1997) argue that this interdependence is mediated by the quality of the relationship in the IOR, and has important implications for earning rent through the IOR by leveraging knowledge-based assets.

In understanding this interdependence, Madhok & Tallman (1998:237) identify three important issues underlying IOR co-ordination. First, IORs are embedded in a system of resource relationships within social networks, between organisations in IOR and inside an organisation. This implies that relationships in an IOR can be recognised as value-bearing assets in and of themselves. Second, the output of an IOR is a collective good in that it is generated collectively, with benefits available only to those inside the IOR. The production of this "collective good is inextricably intertwined with the underlying dynamics of exchange among parties involved, putting a premium on the quality of the relationship as well as on the

returns from investing in it” (Madhok & Tallman, 1998). The implication here is that the focus is shifted from the “form of governance that emphasises governance structures and formal safeguards against opportunism” (Madhok & Tallman, 1998:328), to focus on and emphasise the process of governance that has direct implications for value creation and realisation. Third, there is an important relationship between different kinds of “quasi-rents and the implications of the interrelationships among them” (Madhok & Tallman, 1998:327) for the calculations associated with opportunistic behaviour. This explains why organisations might “forego opportunities to take advantage of their partners” (Madhok & Tallman, 1998:328). This explanation can be utilised without using trust as a factor, and therefore allows transaction-specific expenditure to be seen not as a cost but as investment for the future (Madhok & Tallman, 1998).

### **4.3. Identifying Value in IORs**

Madhok and Tallman (1998) argue, “there is a key distinction between the potential value attainable through an IOR and the realisation of such value”. Potential value is a theoretical construction based on synergies arising from the ideal combination of complementary resources and capabilities. This ideal combination has a direct relationship to the chosen form of governance. Realised value reflects realities on the ground and is “more to do with the effectiveness of the actual management of the IOR” (Madhok & Tallman, 1998:328). The relationship between these two types of value is in that the realisation of value will not be beyond its underlying potential (Madhok & Tallman, 1998). It therefore

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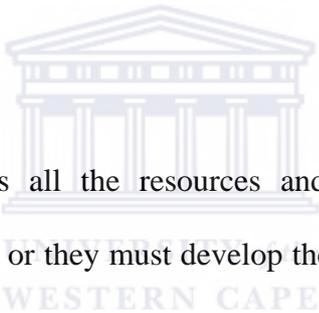
follows that the pursuit and realisation of value through IOR requires the understanding and management of formation, governance and performance (outcome) of IORs. Doz and Hamel (1998:127) recognise different levels of co-ordination that identify whether the IOR is “defined through a set of contracts or as a separate institution, such as a joint venture”. Doz and Hamel (1998:128) argue, “Contractual forms of organisation imply legal agreements on contributions and benefits such as technology transfers, the use of brands, and distribution channels. Institutional forms typically involve the creation of a legally separate corporate entity, but do not exclude contractual arrangements, such as shareholders' agreements between joint venture partners”. The question that arises is which factors lead to choice of governance structure that will give effective and efficient co-ordination. It is hard to specify all contingencies in a contract, and therefore, “when contingencies are many and complex, an institutional form of governance is preferable” (Doz & Hamel, 1998:128). They identify the following contingencies “that make the crafting of IOR contracts difficult and ineffective, lending weight to the choice of institutional forms of co-ordination”:

- task integration: “implies process integration, output co-ordination”, and working together on common tasks in the same or separate institutions.
- joint optimization against uncertainty: “the more uncertain the nature and value of future trade between partners, the more difficult it is to govern through *ex-ante* contracts. An institutional form will not guarantee that an IOR can handle long-term uncertainty. However, when change occurs, an institutional arrangement may be easier to revise than one based on contracts”.

- urgency of decision making: the fact that “joint-venture managers enjoy autonomy in decision making and may also hold key positions in their parent companies makes quick decision making possible. Contractual arrangements between partners would not be supportive of such unplanned decisions” (Doz & Hamel, 1998:129).

Transaction-cost theory recognises hierarchies and markets as governance structures that give effective and efficient co-ordination.

#### **4.4. Hierarchies and markets as co-ordinating mechanisms**



Organisations must possess all the resources and capacities needed for the sustainable earning of rents, or they must develop the capability competitively in-house (Madhok & Tallman, 1998). In doing so, they must use “tacit and complex resources that are largely path-dependent, idiosyncratic, and specialised to the history of the organisation, and yet are not subject to economies of scale, scope, and time, when compared to another organisation that already possesses them” (Madhok & Tallman, 1998). They argue that, if an organisation cannot develop these capabilities from its own key strategic resources timeously and cost-effectively, then it must look outside its boundaries for help. In doing so, it will be consistent with transaction-cost perspective in that transactions must be organized in a transaction cost-effective way.

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Markets, on the other hand, are unable to cost-effectively “bundle together the relevant tacit resources and capabilities” (Madhok & Tallman, 1998:329). This is because tacit resources (skills) have an associated value; it is not easy to separate them from the organisations possessing them without the risk of losing their value. Markets are effective (i.e., efficient) at exchanging general and substitutable resources and know-how, “which are easy to identify and articulate and can be separated from the possessing organisation without loss in value” (Madhok & Tallman, 1998:329). They cannot transmit “deeper knowledge even if the value of the resource/asset can be established” (Madhok & Tallman, 1998:329). This is when an IOR is important as a value creation and realisation vehicle. Madhok and Tallman (1998) argue that rents generated and realised through an IOR and the associated costs in the process of producing the rents are closely bound to each other. Actual rents depend on both what resources are combined and how the combination is accomplished.

An important activity for parties involved in an IOR is to avail both physical and tacit resources timeously and combine them to earn superior rents. Undoubtedly, managerial time, energy and effort are required to ensure the timely availability and combination of the resources as expected by partners. This therefore leads to our sixth proposition.

*Proposition 6*

6. Establishing behaviour that appears trustworthy to partners increases the likelihood of successful co-ordination.

6.1. Providing promised resources or assets timeously by partners is exhibiting trustworthy behaviour

6.1.1. Making promised resources available timeously by partners increases the likelihood of successful co-ordination.

Availing resources in managing IOR relations and those needed to execute the transaction facilitate effective and efficient performance of IOR.

## **4.5. IOR performance**

In introducing the syncretic model that recognizes strategic action in rent-seeking behaviours, Lado, Boyd and Hanlon (1997) recognize the value-enhancing dynamic interplay between competitive and co-operative phenomena that could be harnessed in IORs (Table 4.1). By recognising this phenomenon as the context under which the IOR can extract superior economic rents, management can deliberately seek behaviours that give an IOR superior economic performance.

**Model of rent-seeking strategic behaviour**

		Competitive Orientation		
Cooperative Orientation		Collaborative rent-seeking behaviour	rent-seeking Syncretic behaviour	High
		Monopolistic rent-seeking behaviour	Competitive rent-seeking behaviour	Low
		Low	High	

Table 4.1 Source: Lado, Boyd and Hanlon, 1997.

**4.5.1. Competitive rent-seeking behaviour**

There is high competition and low co-operation where partners’ behaviour seeks “to achieve a position of superior performance and to generate competitive advantage over other organisations by either manipulating the structural parameter of an industry to their advantage or developing and nurturing hard-to-copy distinctive competencies” (Lado, Boyd & Hanlon, 1997:118). According to Lado, Boyd & Hanlon (1997), such behaviour is normally characterised by:

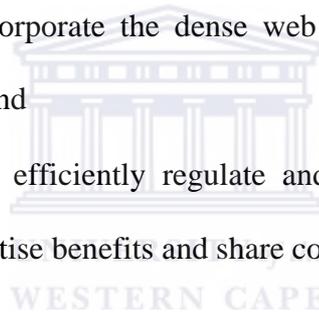
- striving for something that all as individual parties cannot achieve,
- economic rent accruing to organisations that can acquire and are able to utilise scarce resources more efficiently than others,
- behaviour that enables organisations to reduce organisational slack and achieve greater efficiency in production,

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- entrepreneurial rents through stimulating a process of creative destruction by carrying out new combinations of resources, methods, systems, and processes that produce new goods and services, and
- promoting efficiency in economic exchange by reducing transaction costs.

Lado, Boyd & Hanlon (1997) argue that such behaviour is limiting in that:

- rivalry tends to structure relationships with stakeholders, such that when one organisation gains other losses. This arrangement encourages organisations either to erect barriers around their distinctive competencies or to behave opportunistically toward others; it does not create a “win-win” situation,
- it may fail to take incorporate the dense web of social relations in which organisations operate, and
- it becomes difficult to efficiently regulate and enforce property rights, as organisations may privatise benefits and share costs.



This behaviour limits the potential of an IOR to achieve superior performance.

### **4.5.2. Monopolistic rent-seeking behaviour**

This behaviour is characterised by low competition and low co-operation. Organisations that seek monopoly rents usually lobby governments to introduce policies and regulations that preclude potential organisations from entering an industry or collude with other organisation to horde outputs and hike prices (Lado, Boyd & Hanlon, 1997). They argue that such behaviour has short term benefits, but reduces societal welfare and undermines the long-term viability of the

organisation. It is not “a necessary or sufficient condition for sustained IOR performance” (Lado, Boyd & Hanlon, 1997:120).

### **4.5.3. Collaborative rent-seeking behaviour**

Collaborative rent-seeking behaviour tends to seek to co-produce and share value by fostering and maintaining reciprocal interdependencies (Lado, Boyd & Hanlon, 1997). Interdependencies “generate “composite quasi rents”, which are economic rents generated by a resource that depends on continued association with resources of others” (Lado, Boyd & Hanlon, 1997:120). Interdependencies foster and maintain collective interests that contribute to building trust. Lado, Boyd & Hanlon (1997) argue that trust plays a role in contributing to the generation of rent in that:

- it reduces uncertainty as it provides cognitive and moral maps of expectations that guide how parties interact,
- it is a mechanism that fosters social control,
- it reduces costs in governance in that parties do not have put mechanisms in place to safeguard against the hazards of partner opportunism,
- it induces reciprocity in that there will be an open commitment to mutual expectation, such reciprocity may serve to further embed and deepen trust and co-operation.

Lado, Boyd & Hanlon (1997) note that co-operation may be economically disadvantageous when:

- “economic exchanges are characterised by high uncertainty, small-numbers’ trading or trading in small numbers, asset specificity, and information

asymmetry that provide an opportunity for parties to behave guilefully toward others,

- transactions are completely discrete and their expected future benefits can be determined with complete certainty in the present,
- future exchange relationships are less important to some participants, and
- reputation effects on participants acting opportunistically are inconsequential”

(Lado, Boyd & Hanlon 1997:121).

Greater co-operation that heightens reciprocal commitments of idiosyncratic and specialised resources to the IOR may exacerbate strategic inflexibility. This makes collaborative rent-seeking behaviour not sufficient for achieving sustained IOR performance (Lado, Boyd & Hanlon 1997:122).

#### **4.5.4. Syncretism rent-seeking behaviour:**

Simultaneous co-operation and competition stimulate greater knowledge seeking, technological progress, and market expansion than is achieved when each strategy is pursued separately (Lado, Boyd & Hanlon 1997:122). They argue that if property rights are well-protected, syncretic rent-seeking behaviour may emphasise the positive-sum, efficiency enhancing effects of competition and co-operation. This gives parties strategic flexibility in that (Lado, Boyd & Hanlon 1997:123):

- “they can achieve competitive advantage through leveraging their rare, valuable, and inimitable resources in competitive contexts,

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- they can achieve collaborative advantage by: (a) effectively locating genuinely co-operative and trustworthy partners, (b) identifying strategic opportunities for realising positive-sum gains, and (c) making the resource commitments necessary to realise the strategic goals of the IOR”.

Syncretic rent-seeking behaviour requires working within an IOR on a long-term basis. A good example of this behaviour is that of Toyota forming supplier IORs as a means of further enhancing the inputs to the Toyota manufacturing system (Lado, Boyd & Hanlon 1997:123). They argue that the ultimate co-operative behaviour between Toyota and its suppliers is Toyota’s practice of sharing with a given supplier any profits determined to result from innovations made by the supplier to reduce costs.

There are limitations in pursuing competitive and co-operative strategies simultaneously (Lado, Boyd & Hanlon 1997:124). Syncretic rent-seeking behaviour may fail to improve an organisation’s competitive position if:

- cost of maintaining and implementing such a strategy outweigh feasible alternatives. These “costs result from the need to maintain a greater and more diverse repertoire of cognitive maps, behavioural routines, and organisational resources for engaging in both co-operative and competitive behaviour and for choosing when to pursue each option with specific transaction partners,
- it entails contributions of organisation-specific human and technological competencies that are difficult to evaluate or monitor; in this instance, the opportunity exists for some partners to behave guilefully,
- partners have incongruent goals and expectations,

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- one partner accumulates knowledge-based assets from the IOR at a slower rate than the rate at which other partners absorb competencies,
- a partner becomes increasingly closed by disclosing less and less information” (Lado, Boyd & Hanlon 1997:124).

Each IOR will have its own “individuals, projects, and organisational and strategic contexts raising a need to blend content, context and process” (Doz, 1996:80). Through behaviours that reduce risk in task interdependence and co-ordination costs, parties in IORs provide resources and perform activities that are rent-seeking. This leads us to our final proposition.

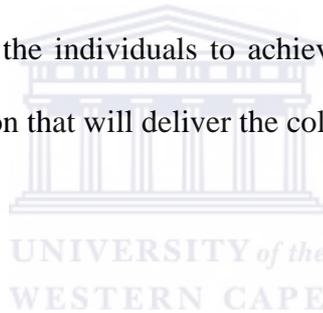
### *Proposition 7*



7. A balance between competitive and co-operative behaviour that is rent-seeking increases the likelihood of delivering performance that fosters greater knowledge development, economic and market growth, and technological progress than either competition or co-operation alone within an IOR would do.
  - 7.1. collaborative rent-seeking behaviour has a high co-operative orientation and a low competitive orientation
  - 7.2. syncretic rent-seeking behaviour has a high co-operative orientation and a high competitive orientation
  - 7.3. monopolistic rent-seeking behaviour has a low co-operative orientation and a low competitive orientation

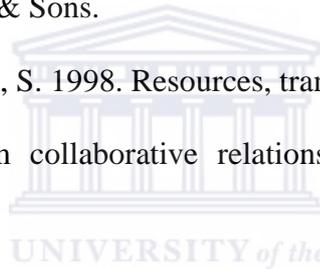
## **4.6. Conclusion**

Identifying resources, categorising them into those that are monetary transactions and those that are non-monetary transactions, is the first step in co-ordination. This initiates communication that eventually leads to the formalisation of IOR routines that will deliver products and/or services. This first step is the initiation of another cycle of negotiation, commitment, and execution through the dynamic process. The focus of the managerial effort, in this case, referred to as co-ordination, is to make resources available that are needed for IOR activities and have participants (employees) who will have the appropriate personal and role relationships to successfully execute the activities. The second step is to co-ordinate the behaviours of the individuals to achieve the appropriate balance of co-operation and competition that will deliver the collective goals of the IOR.



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## **Chapter 5: Exemplar, discussion and conclusion**

### **5.1. Introduction**

Using propositions, the previous chapters described the IOR model. The following chapter uses an exemplar to test the propositions. It also serves as an exemplar of the integrated framework (Fig 1.1). The exemplar is a study published in IOR literature.

### **5.2. Exemplar**

The rationale of choosing the paper by Doz (1996) as an exemplar is its focus content (IOR evolution) and the research strategy that the study utilised. Doz (1996:56) specifically set out to consider “how learning processes mediate between initial conditions and outcomes” of IORs, and generally to assess the relative contributions of initial conditions and of evolutionary learning processes to the outcomes of IOR. His research strategy, based on the case study method, demonstrates how to use qualitative methods in establishing qualitative understanding and, based on this understanding, how to construct interpretative understanding, then use it to construct positive understanding, which he immediately tested (Lee, 1991). It is argued that the exemplar demonstrates the implementation of the integrative framework research strategy presented in this report. In addition, the exemplar offers an opportunity to test the propositions developed in this paper. Although Doz (1996) does not cover the emergence of IOR, his review of the IOR literature is exemplary. The review identified major

contributions in IOR research, demonstrated that the emergence of an IOR was well covered, and identified the gap in the literature on IOR evolution, where he made his contribution.

### **5.2.1. Exemplar research design**

In the three cases selected, the IORs were involved in new business and new product development, this controlled for initial conditions, process variables and learning. The choice of new business and new product development made it possible to track initial conditions and process variables from their start. Projects were chosen to allow a combination of skills between the partners in pursuing a new opportunity, subject to significant market and technological uncertainties, which could only be resolved over time rather than at the inception of the relationship. A nested approach to individual cases was used, where two projects within each of the IORs were selected. In the two projects, both products were in the same product area, but were different product lines. The choice of projects allowed gathering of data, and analysis to be conducted at project-level, IOR level, and corporate level. The research design was such that data analysis, theory development and theory testing followed each other sequentially.

#### **5.2.1.1. Subjective understanding in exemplar**

To ensure that empirical reality was captured in terms of what it meant to the participants in the six projects, archival data and interviews were used. Archival data was used in three ways: (1) for retrospective analysis, that is, capturing the

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whole history of the IORs, (2) identifying participants who played key roles (a) at day-to-day level, (b) at senior executive level, (c) at senior line-manager level, and (3) to prepare for interviews, to challenge interviewees' memories, and check *ex post* data and perceptions with the documented trail of the relationship. In addition, this use of archival data contributed to the validation process as it controlled for participants' selective retrospective bias. In the interviews, the focus of each interview was the person's own factual experience with the IOR, the evolution of their involvement, understanding, commitments and feelings toward the partnership, their own interaction with members of the partner organisation and of their own organisation on partnership matters, and their recollection of events that they saw as important in the evolution of the IOR.

To help the researcher comprehend fully the events within and around the partnership and the perceptions of key participants, the focus was on two things. First, on general understanding of decisions, perceptions and events. Second, identification of how these were perceived, at various points in time, by key individuals. In doing this, Doz (1996) fulfilled the requirements for activities of research as represented by arrow 1 in Fig 1.1., which is a process of understanding how people involved in IORs come to interpret and, therefore, to understand and guide themselves in these relationships (Lee, 1991)

The initial case study, Ciba Geigy-Alza, was used to generate the initial framework. Data were aggregated in a series of charts, summarising the evolution of IOR, and to make sense of the streams of data, the focus was on the question of

‘what changed over time, and why’. This allowed conceptualization of IORs as interactive and iterative cycles of learning, re-evaluation, and readjustment. Case histories and chronologies were constructed and within-case analysis conducted, which is consistent with case study method.

Validity of the resulting interpretive understanding is achieved by referring back to the subjective understanding (arrow 2, Fig 1.1). In the exemplar, validity was achieved by using research associates in data collection on AT&T/Olivetti and GE/SNECMA, who were not involved in the initial framework development, and were not familiar with the framework.

Parallels can be drawn on this report with the procedures followed by Doz (1996) to arrive at subjective understanding. Interpretive reading in this paper involved reading of text, not reading of human behaviour as done by Doz (1996). In reading the text, the paper by Ring and Van de Ven (1994) had significant impact as it described IOR emergence, evolution, and dissolution. The interpretive model was brought to life by the paper by Gulati (1998), in which he argued that IORs are socially embedded and key issues in researching them are their formation, dynamic evolution, governance and performance. These two papers played an important role in constructing the IOR model, as presented in Fig 1.4. This similar role is played by the Ciba Geigy-Alza case study and describes some of procedures that may be performed referred to by arrow 1 in Fig 1.1. Other papers, including the exemplar, have since contributed to the improvement and better understanding of the model. This is similar to the role played by the

AT&T/Olivetti and GE/SNECMA cases and these are some of the procedures that may be performed as indicated by arrow 2 in Fig 1.1.

#### **5.2.1.2. Interpretive understanding exemplar**

The procedure in established interpretive understanding in the exemplar was through using case histories, chronologies and within-case analysis, and using the Ciba Geigy-Alza case, to establish an initial framework. The other cases, AT&T–Olivetti and GE-SNECMA, were then used as theoretical replications and extensions, to challenge and refine the framework. The refined framework is the interpretive understanding that provided the basis for developing the positivist understanding.



#### **5.2.1.3. Positivist understanding exemplar**

Theory testing relied on qualitative pattern matching between the framework and data. The comparative cross-case analysis and the consolidation of the data were tested by a researcher not directly involved in the field research at any of the six companies who used all of the detailed transcripts of interviews to test the framework. This allowed someone new to both the data and framework to run an independent test of the pattern matches between the various cases. The positivist understanding was confirmed, based on controlled empirical testing (Lee, 1991), giving the summary model of IOR evolution. A comparison can be drawn with what was done in this report, where, the positivist understanding to a limited extent is achieved through (1) the formulation of propositions, and (2) testing them using the findings of the exemplar.

## **5.2.2. Testing propositions**

### **5.2.2.1. Proposition 1**

1. Social networks facilitate negotiation and commitment by providing information about potential partners

1.1. A money network is a social network

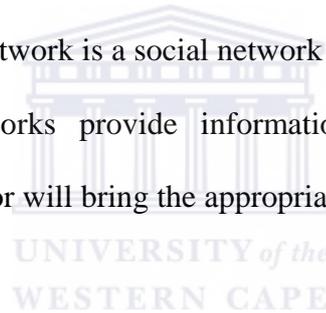
1.1.1. A money network provides financial information about potential partners

1.2. An information network is a social network

1.2.1. An information network provides information about whether potential partners have the appropriate tacit knowledge

1.3. A moral support network is a social network

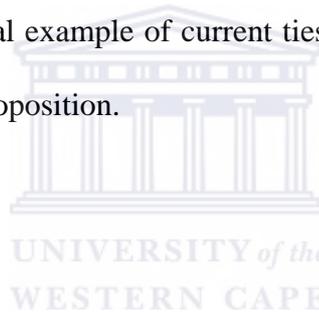
1.3.1. Moral networks provide information about whether potential partners have or will bring the appropriate legitimacy



In testing this proposition using the exemplar, we note that it is stated in the exemplar that the observation excluded the emergence of IORs. The retrospective analysis revealed some of the factors that we find in the exemplar supporting proposition 1, in that the IOR was the initiative of Dr Alejandro Zaffaroni, Alza's founder and CEO, and Dr Gaudenz Staehlin, the head of Ciba Geigy's pharmaceutical division. Dr Zaffaroni sought to secure sustained funding and market access for the advanced drug delivery systems (ADDS). As senior managers in their respective organisations and as professionals within the pharmaceutical industry, they leveraged the information benefits of social networks in identifying the legitimacy of each other and resources needed to

implement the transactions. Ciba Geigy had financial resources and experience of pharmaceutical development, production, and marketing, while Alza had expertise in the development of advanced drug delivery system (ADDS). Alza was a small distinguished research company with unknown reputation in the pharmaceutical industry, yet Ciba Geigy was major chemicals and pharmaceutical multinational. Ciba Geigy brought to the relationship legitimacy, resources, and expertise of taking the product to the market.

In addition, the GE-SNECMA IOR supports the proposition in that starting with the CF6 engine in 1960, its recurrent contract moved from recurrent to relational contracting. This is a typical example of current ties leading to an IOR, therefore indirectly supporting the proposition.



**5.2.2.2. Proposition 2**

2. Developing joint expectations among parties increases the effectiveness of collaboration

2.1. Establishing possible efficiency and equity measurements of a transaction as it relates to all parties is developing joint expectations

2.1.1. Efficiency and equity are the outcomes sought for in collaboration

This proposition is well supported by the case of the GE-SNECMA IOR, in that partners had worked together to develop civilian jet engines. This partnership enabled them to develop joint expectations when they initiated a project to develop and manufacture a midrange engine, the CFM56. Partners were aware of each other's experience and skill base, and easily established task interdependence

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of the new project. Managers at both GE and SNECMA jointly sought the best ways to serve the market. There was clarity of expectations about the environment of the relationship, the task, the process of co-operation, skills of partners, goals, and motives. Partners were convinced about their ability to implement the transaction successfully, hence believed that efficiency outcomes will be achieved. Prior ties enabled interpersonal trust to develop and parties believed that there were fairness within the relationship and, hence believed that equity outcomes would be achieved.

### **5.2.2.3. Proposition 3**

3. Formal negotiations to collaborate are successfully concluded by establishing formal commitments that symbolise the formation of an IOR

3.1. Individuals or groups interacting and negotiating to collaborate with mandates from their organisations are involved in formal negotiations to collaborate

3.1.1. Successful formal negotiations are concluded by establishing formal commitments like a memorandum of understanding (MOU) or a launch party

Ciba Geigy-Alza had a joint research conference to set R&D priorities, to get to know each other and they signed a research agreement. In addition, Ciba Geigy bought shares in Alza, giving it a majority representation on Alza's board.

**5.2.2.4. Proposition 4**

4. Agreement on the obligations and roles for future action in the relationship increases the likelihood of successful co-operation

4.1. Committing resources and establishing how the combination will be accomplished complies with the agreement on obligations and rules for future action in the relationship

4.1.1. Committing resources and establishing how they will be combined increases the likelihood of successful co-operation

In the case of Ciba Geigy-Alza, this proposition was partly supported. Obligations and roles were clear from the start; Alza would do the advanced development of their oral slow-release technologies (OROS), full development of transdermal technologies (TTS), and "hand over" the results to Ciba-Geigy for clinical tests for production and marketing of both products. The proposition was partly supported as parties agreed to co-operate, but the project was not a success. In the case of the GE-SNECMA IOR, they sought to develop an engine jointly. There was no explicit mention of obligations and roles, "liaison desks" coordinated roles. The two cases point to the fact that there is no direct relationship between agreeing on the obligation and roles for future action and successful co-operation.

**5.2.2.5. Proposition 5**

5. Choosing a governance structure that optimises on risk and trust for a transaction increases the likelihood of an IOR

5.1. Markets are a governance structure

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5.1.1. Markets are associated with low risk and low trust in a transaction

5.2. Hierarchies are a governance structure

5.2.1. Hierarchies are associated with high risk and low trust in a transaction

5.3. Recurrent contract is a governance structure

5.3.1. Recurrent contract is associated with low risk and high trust in a transaction

5.4. Relational contract is a governance structure

5.4.1. Relational contract is associated with high risk and high trust

Both the Ciba Geigy-Alza and the GE-SNECMA findings support the proposition. The risk in both cases was reasonably high; this is assumed from the choice of the cases. In the Ciba Geigy-Alza case, trust was low and the two types of governance structures were implemented. Ciba Geigy bought shareholding in Alza and research contracts were signed. In the case of GE-SNECMA, trust was very high; there was no shareholding, but a programme management joint venture was set-up, acting as a buffer structure that operated as “liaison desks” on each other’s premises. Trust did not only play a role in choosing governance structures, but in the case of GE-SNECMA, it was the basis of a governance structure.

### **5.2.2.6. Proposition 6**

6. Establishing behaviour that appears trustworthy to partners increases the likelihood of successful co-ordination

6.1. Providing promised resources or assets timeously by partners is exhibiting trustworthy behaviour

6.1.1. Providing promised resources timeously by partners increases the likelihood of successful co-ordination

The Ciba Geigy-Alza case supports the proposition in that co-ordination failed in this IOR because:

- Alza was surprised by Ciba-Geigy's "reinventing the wheel" in manufacturing ADDS, a signal that Ciba-Geigy did not wish to remain permanently dependent on Alza's know-how and its manufacturing capability for ADDS.
- Alza became suspicious about Ciba Geigy's ultimate motives because they were not sharing information about TTS. In addition, Ciba-Geigy's pharmaceuticals division framed the relationship as a potential acquisition opportunity. Suspecting a likely takeover, Alza's scientists, and managers, whose involvement was essential to the success of the IOR, were guarded in their interactions with counterparts at Ciba-Geigy. Alza was reluctant to work closely with Ciba-Geigy lest its technological knowledge be transferred to a partner whose motives it did not trust.
- Alza managers perceived Ciba Geigy to be slow to the market,
- Ciba Geigy suspected Alza did not have a long-term commitment; they needed Ciba Geigy for the funds and doubted Alza's top management's commitment, especially Dr. Zaffaroni's growing involvement with new ventures.

**5.2.2.7. Proposition 7**

7. A balance between competitive and co-operative behaviour that is rent-seeking increases the likelihood of delivering performance that fosters greater

knowledge development, economic and market growth, and technological progress than either competition or co-operation alone within an IOR can provide.

7.1. Collaborative rent-seeking behaviour has a high co-operative orientation and a low competitive orientation

7.2. Syncretic rent-seeking behaviour has a high co-operative orientation and a high competitive orientation

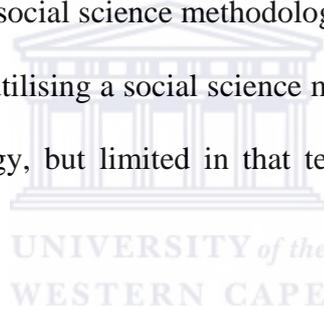
7.3. Monopolistic rent-seeking behaviour has a low co-operative orientation and a low competitive orientation

The exemplar supports the proposition. The findings from the GE-SNECMA case were that they co-operated on the civilian products and competed indirectly on the military side and succeeded in acquiring the knowledge to build the engine. On the Ciba Geigy-Alza case, Alza lost trust in Ciba Geigy. Alza management saw Ciba Geigy running down Alza, and that Ciba Geigy built its own in-house ADDS development capabilities. Such behaviour is not rent-seeking and does not deliver performance that fosters knowledge development or economic and market growth; it was a simple duplication and a waste.

### **5.3. Discussion**

This research does not present the meanings constructed by human subjects as observed in their social settings that social scientists seek to explain, but human subjects were substituted with text. It sought to develop a model to guide the

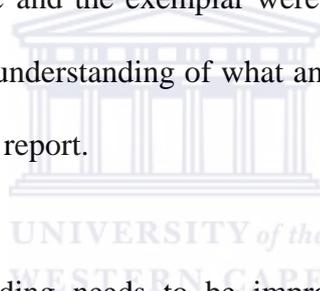
observations, because “it is not easy to start with observing the facts, for to determine what the facts are is the very object of scientific inquiry” (Boddy, 1951:121). Theory helps in determining what the facts are, “in order to find something we must first look for it” (Boddy, 1951:121). The integrative framework presented in Fig 1.1 provides a guide on how to collect both subjective and objective meaning in building frameworks that will determine what the facts are. Natural science methods are seen to deal competently with objective facts; the integrative framework is robust in that both subjective and objective meanings are accommodated. Lee (2004) argues that social science methodology deals with both the subjective and objective meanings, and therefore natural science methodology is a subset of social science methodology. Another way of looking at this research is to say it is utilising a social science methodology that excludes the natural science methodology, but limited in that text is used instead of human subjects.



According to Lee (2004:9), “the organisation is that which stays the same even when all the people change”. In focusing on IOR as a unit of analysis, this research focuses on things that stay the same, or at least change at a slower pace than the turnover of people. Lee (2004) identifies these as social objects, namely social structure, social networks, business processes, standard operating procedures, and management processes. The IOR is then a social object, which is the unit of analysis “that enables, constrains, and shapes behaviours and thinking of all the different generations of individuals who enter, pass through and leave the organisation” (Lee, 2004:9).

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The IOR ideal framework elaborated in a set of propositions to describe how IORs emerge and evolve over time has very limited application. The first limitation is that it is a theoretical construction of limited scope, based on a review of the literature. The second limitation is concerned with the objective of the study, which was to, “identify essential constructs to ensure that they have good clarity and parsimony, and use propositions to communicate relationships between them”. Since the constructs are not observable, propositions were formulated based on hypothetico-deductive logic (Fig 1.2) to allow for indirect verification. In addition, an exemplar was used further test the propositions. In both instances, there was support for the propositions. Assuming the application of both hypothetico-deductive logic and the exemplar were correct, then the IOR model (Fig 1.4) is an interpretive understanding of what an ideal IOR is as derived from texts cited elsewhere in this report.



The interpretive understanding needs to be improved, as pointed out by the inconclusive support of proposition 4. There are two immediate issues that proposition 4 raises.

- First, collaboration, co-operation and co-ordination are defined in the model as managerial functions. The assumption is that collaboration is a senior management function; co-operation is a middle management function and co-ordination is a lower level management function. This was supported by Doz and Hamel (1998:137) when they discussed three interfaces (management levels) between organisations that build bridges. The first level is the

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operational level, “where the detailed knowledge of the IOR tasks resides and where specialists can communicate with specialists”. The second level is the strategic level, where senior “executives of partner organisations understand and share the value-creation logic of the IOR, put valuation conflicts and operational problems into a broader strategic context, and set IOR tone for lower levels”. The third level is “the middle-manager level that brings operating personnel together on operational and strategic issues” identified by senior level management.

- Second, these managerial functions interface with the dynamic process (negotiation, commitment, and execution) during formation, governance, and performance. To understand this interface calls for the understanding of the nature of process. The dynamic process is one process, and so are formation, governance, and performance. As there seems to be a convergence of different types of processes, further studies of how these processes interact and the significance of intervention of management need to be undertaken to strengthen the model.

As demonstrated by the exemplar, there is a symbiotic relationship between the dynamic process and the learning process. They seem to drive the formation, governance, and performance of an IOR. The model does acknowledge learning systems and learning organisation constructs, but these were not dealt with due to the limited scope of the study. Another assumption that needed more attention than was given is that of the managerial functions. Management has three levels, namely top, middle and lower levels. The assumption in the IOR model presented

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is that top level should be involved in collaboration, the middle in co-operation and the lower level in co-ordination. The findings in the Ciba Geigy-Alza case was that Ciba Geigy's middle-level management felt left out of the IOR and were particularly annoyed by Alza's style of by-passing them. This demonstrated the weakness of the study in identifying propositions that were needed to relate the constructs. This suggests that the propositions may have been inadequate or inappropriate and need further investigation.

No claim is made here that this is a complete IOR model or the only IOR model. The contribution is that, using the identified literature, we have demonstrated the existence of an IOR model. Based on this research:

- Management may find this model useful in guiding their activities in understanding how IOR emerges, evolves, and dissolve, and who may be involved in these stages.
- Researchers may use this model and method in studying transactions that involve two or more organisations, particularly in South African, it may be useful in studying, Black Economic Empowerment transactions, and service delivery to local communities by national, regional, and local government.
- Post-graduate students may benefit in designing their research projects. The integrative method and the exemplar give insight into research design and implementation. In addition, it is pointed out what constitutes a theory, and from this, one can gain insight into the development and testing of theories.
- Social movements like civic organisations, trade unions, and political parties may benefit from the use of the IOR model, as it is a social action model.

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- Agencies such as the United Nations, African Union and consulting firms that need more than one group or organisation to work together in delivering products and services may also benefit from the model.
- The model can also benefit organisations that are involved in inventions and/or innovations, in particular in information communication technologies (ICT) sectors.
- Those that are working in curriculum development, or intend to, can benefit from this model not because it was this area that inspired the development of this model, but that organising knowledge in the form of curriculum need more that one person, one group or one organization.

### **5.4. Relevance and rigor**

This IOR model has potential for use by individuals, groups, and organisations intending to work with two or more parties. It is, however, not appropriate for use, at this stage. It does not capture aspects of behaviour or variables that can be observed. The IOR model is in an incomplete state. It is a group of constructs joined by propositions, which need operationalisation of variables and hypotheses in further studies in the development of tentative theory. This limitation is due to the scope of the report. The research strategy of using an integrative framework, defining theory as having two levels of constructs and variables, should be a minimum that social scientists in theory development and testing need to do. Boddy (1951) argues, “Previous knowledge and reflection are necessary (though insufficient) conditions. Great scientific achievements are never made by those

who start with an open mind without any knowledge or anticipation of nature. In order to find something, we must first look for it". We must therefore have a profile of what we are looking for. The model can be seen as a tentative profile of what we should be looking for in trying to identify an IOR. It is only when this model has been fully developed that relevance can be established among different types of IORs. As it is, the IOR model is part or a step in the learning process on how to conduct rigorous research in the social sciences.

## **5.5. Conclusion**

The emergence, evolution and dissolution of IORs are a process that had inside nested processes. These processes enable transactions to either succeed or fail. The dynamic process composed of negotiation, commitment, execution, and assessment is central to the process nature of IOR. It puts the space and time dimensions into the IOR model in that, aspects of the dynamic process is an "instance" or "event" that happen at a give place and time, and therefore, each IOR will have a history. Time becomes an important variable for observation purposes. Constructs can then be confirmed when certain events happen at identified times.

Social structure (within social systems) provides social networks that enable a social object we call IOR to exist as a mechanism for the creation and delivery of value. Its formation, governance, and performance mark its emergence and evolution. Formation describes a formal acknowledgement by involved parties to

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enter into such a relationship. Governance describes how the relationship will be governed. Performance is about harvesting the sought-after benefits that brought the parties together. Management with different competencies is critical in managing IOR as a value-creation and delivery mechanism. Collaboration is crucial to the formation, co-operation is important in governance, and without coordination, performance of an IOR cannot be guaranteed.

This report identifies “the transaction” which is sometimes referred to as “the project” as the focus of IOR. Resources and skills are needed to implement the transaction. This bestows risk to a transaction at the same time requiring parties to have trusting relationships. Role relationships require parties to have the skills set to implement the transaction and personal relationships create a trusting environment. Process plays a central role as part of the environment that enables the successful implementation of a transaction, particularly in relationships issues at the strategic, tactical, and operational levels.

## **5.6. References**

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