REFRAMING OPPORTUNISM IN STRATEGIC ALLIANCES

ABSTRACT

Literature suggests that opportunism in strategic alliances reduces performance by limiting collaborative opportunities, inciting retaliation, and causing reputational damage. While acknowledging that this is likely when opportunistic behavior is egregious, we suggest that modest instances of opportunism may not follow the same pattern. Building from in-depth interviews with alliance managers, we underscore how opportunism can occur at varying levels of intensity that may generate different performance outcomes. We argue that mildly opportunistic behavior can enhance performance through superior private benefits in addition to common benefits; while preserving or increasing future performance. By illustrating how opportunism can be beneficial, we demonstrate that it is a more complex behavior than extant strategic alliance research may imply.

AUTHORS

Tadhg Ryan Charleton
PhD Candidate [1] and Visiting Fulbright Scholar [2]
Tadhg.RyanCharleton@nuim.ie

&

Robert J. Galavan
Chair of Strategic Management [1]
Robert.Galavan@nuim.ie

[1] *School of Business, Maynooth University, Maynooth, Co. Kildare, Ireland.*

[2] *Department of Management, R. B. Pamplin College of Business, Virginia Tech, Blacksburg, VA 24061.*

ACKNOWLEDGEMENT

The first author gratefully acknowledges financial support from the Irish Research Council, Fulbright Commission of Ireland, Enterprise Ireland, and the John F. Kennedy Fund.

As a core tenet of transaction cost theory, risks of opportunism in inter-firm exchanges have been studied extensively (Coase, 1937; Williamson, 1975). Within strategic alliances, opportunistic behavior is considered to be a suboptimal practice that leads to additional long-term costs including reduced opportunities for repeated cooperation and reputational damage across social networks (Axelrod, 1984; Hill, 1990). However, some firms behave opportunistically in alliances and escape unscathed. Our paper is motivated by the opportunity to better understand such instances where firms achieve self-interested gains at the partner's expense *without* jeopardizing future prospects. For instance, in Samsung's joint venture to develop LCD-TV panels with Sony, their capabilities to harvest private benefits meant that they achieved disproportionately large individual gains (Gnyawali & Park, 2011). In subsequent years, these resulted in a steadily rising share of the rapidly growing LCD-TV segment and annual revenues of $200bn for the first time. Over the same period, Sony's LCD-TV market share more than halved. Yet Samsung's pursuit of private benefits does not appear to have harmed their reputation with others in the network – they continue to enjoy alliances with key players such as Intel, Panasonic, and IBM. Industry examples like this suggest there is potential for a more sophisticated understanding of opportunism in strategic alliances. Just as cooperation may not follow a more-is-better approach (Bercovitz, Jap, & Nickerson, 2006), we question whether less opportunistic behavior is always desirable.

To enhance our comprehension of a "rich, complex and nuanced" construct (Rindfleisch et al., 2010: 2), we present an analysis of relevant literature and in-depth qualitative interviews with alliance managers. We find that opportunism can occur at varying levels of intensity — ranging from mild pursuit of self-interest (absorbing knowledge in areas beyond the alliance) to more egregious opportunistic acts (poaching key employees). While acknowledging that egregious acts can lead to inferior outcomes, we suggest that milder acts will not follow the same pattern. Opportunism can generate short-term gains by combining joint creations with internal resources and capabilities (Gnyawali & Park, 2011), by applying knowledge and skills appropriated in other areas (Hamel, 1991), and by motivating rapid internal innovation (Lado, Boyd, & Hanlon, 1997). At modest intensities, these can be achieved while simultaneously *enhancing* future opportunities through increases in partner dependence, more rapid value creation, and the development of superior technological capabilities.

Our paper makes two contributions. First, by illuminating varying levels of opportunism, we highlight that the 'one size fits all' approach often employed may not be appropriate. This is in line with Williamson's (1979) seminal conceptualization and suggests a need to revisit theories that treat opportunism as dichotomous ('present' or 'absent'). Second, we highlight instances where opportunism can be beneficial. This suggests that it is a more complex concept than alliance research has recognized. Our paper therefore extends insights concerning how firms can create value through alliances (Khanna, Gulati, & Nohria, 1998; Rai, 2016).

SAMPLE AND METHODS

There is a dearth of research explicating the dimensions and idiosyncrasies of opportunism as they relate to strategic alliances. Therefore, while our paper builds from extant literature, we also incorporate insights from in-depth interviews with eight managers in high technology industries. Interviewees held senior positions where most their time was spent managing inter-firm alliances. They were selected because of their extensive alliance experience and hailed from industries including medical devices, software, IT, and data hosting, where the intangible nature of advantage-generating resources means that the risks associated with opportunism are significant. Each interview was semi-structured, lasted 75-100 minutes, and was digitally recorded.

CONCEPTUAL DEVELOPMENT

Williamson defines opportunism as "self-interest seeking with guile" (1979: 234). Yet, this definition has led to two critical misconceptions. First, Williamson intended that the concept would reflect varying intensities of opportunism – "it is not necessary that all agents be regarded as opportunistic in identical degree" (1979: 234) – but this is often lost in subsequent theory development. Subsequent considerations of opportunism, often adopting a game theory lens, implicitly treat opportunism as a dichotomous construct – one which is either present or absent (e.g. Hill, 1990; Quintana-Garcia & Benavides-Velasco, 2004; Ritala & Hurmelinna-Laukkanen, 2009). Therefore, analysis rarely extends beyond the positive or negative performance implications generated by the black box of 'opportunism'. Second, it is largely overlooked that the outcomes of opportunism are critically determined by context (Rindfleisch et al., 2010). Different levels of opportunism may be acceptable depending on firm and alliance level conditions and the same level of self-interest that is acceptable – or even expected – in a learning alliance (Hamel, 1991) may lead to termination in an alliance for joint development and sales (e.g., Fernandez, Le Roy, & Gnyawali, 2014). The term 'opportunism' is best reserved for actions that disadvantage other alliance members – not those occurring through the normal process of appropriating benefits (e.g., Rai, 2016). Therefore, opportunism is more appropriately defined as the pursuit of self-interest at the expense of other alliance partners (Das & Rahman, 2010). This definition returns to Williamson's initial intention by explicitly acknowledging varying levels of intensity, while evaluating behavior within the firm and alliance context in which it is rooted.

Varying levels of intensity

Opportunism is a complex construct. Our interviews illustrate two extreme variations — milder pursuits of self-interest and more egregious acts. More benign forms include skills absorption and shielding knowledge that a partner might reasonably expect to access. This behavior is quite routine between alliance partners. As one manager outlined:

> "*When our partner's engineers come to our site, the priority is knowledge protection. They ask us to help because they don't have the required technical ability. That's an advantage that we need to preserve so we share information on an as-needed basis only. If a competitor or supplier does not absolutely need to know something, we don't share it. It's like being audited — answer what you're asked and nothing else.*"

Such approaches are recognized in extant literature (Hamel, 1991) and are highly common among the managers we interviewed. More severe forms may involve poaching employees, misappropriating core assets, and violating secrecy agreements (Khanna et al., 1998). Another manager explained:

> "*Before formalizing an alliance agreement, we generally share a detailed breakdown of our ideas for whatever problem we're trying to solve. It contains internally developed technical data and there are extensive NDAs [non-disclosure agreements] built into the pre-alliance contract. But we had one client who was recycling this data to build components with other partners. We had shared under*

assurances of non-disclosure but ultimately it was being sent back to us via a mutual partner. Eventually, we took action but we were burnt badly the first time."

This is a more severe form of opportunism and highlights the concept's inherent complexities. While both behaviors illustrated are opportunistic, each will have notably different consequences. In the following subsections, we consider how consequences may vary depending on intensity of opportunism.

Opportunism and short-term performance

It is acknowledged that a firm acting opportunistically can achieve performance improvements in the short-term. As well as common benefits from joint value creation (Dyer & Singh, 1998), opportunistic firms can achieve additional private benefits through the combination of non-shared knowledge and capabilities with internal resources and capabilities (Hamel, 1991; Khanna et al., 1998; Rai, 2016). This can motivate internal innovation, generate process efficiencies, and trigger incremental improvements (Lado et al., 1997). Firms that do not pursue private benefits can find themselves redundant within the alliance and vulnerable in the market (Hamel, Prahalad, & Doz, 1989). A manager describes:

> "*Working alongside our competitor, there have been many learning opportunities… better ways to develop processes, manufacture parts, trouble shoot problems, root cause analysis, increase output; and especially how be more efficient at achieving quality. We don't set out to strip our partners bare of their knowledge, but we do learn many things that are very good for us... we even won some of their contracts when they were up for renewal.*"

We assume that the firm will only act opportunistically where additional private benefits are anticipated (Buckley & Casson, 1988; Hennart, 1991). External resources are a critical source of rent generation (Dyer & Singh, 1998; Garrette, Castañer, & Dussauge, 2009; Gnyawali & Park, 2011) and a firm that pursues private benefits as well as common benefits, will achieve superior short-term performance relative to a firm that pursues only common benefits. Mild opportunistic acts like this can drive performance improvements for the firm by contributing to private value creation (Rai, 2016).

Sometimes, the partner may be unaware of opportunistic behavior (e.g. Williamson, 1985) and therefore cannot react (Chen, Smith, & Grimm, 1992). Where the partner is aware, they will make a rational decision to respond by weighing their own value creation against the cost of the partner's actions. Many partners will recognize that some tolerance of the other's mildly opportunistic acts is necessary to achieve their own private aims (Zajac & Olsen, 1993). As was Sony's rationale for sharing their TV expertise in the S-LCD venture; "if we put up barriers, they'll close up too" (Gnyawali, He, & Madhavan, 2008: 389). Therefore, rather than opportunism as a sole determinant of alliance outcomes, its varying degrees are "simply a subset of total costs to be aggregated and then compared with the total benefits/gains in an overall calculation of the value of an interorganisational strategy" (Zajaz & Olsen, 1993: 133). These sentiments were echoed by the managers we interviewed:

> "*There is a degree of 'out for themselves' that we tolerate with our partners. Every company is out for themselves at the end of the day… I suppose we are willing to tolerate certain levels of noncooperation depending on the partner's importance.*

> *If the venture involves something small and relatively generic, we will be less tolerant than a partner who is working on a large part of the supply chain that would take months to re-establish elsewhere. Yes, cooperativeness is important but, above a certain threshold, it is secondary to innovation, costs, service level — the overall value that the partner creates.*"

If we take the partner's involvement in the alliance as a signal that the alliance is a source of value, and the opportunism is relatively mild, then tolerance may be more likely than retaliation. Up until a point, opportunism can open new channels for private value creation while preserving common benefits. However, where the firm's opportunistic behavior exceeds a certain level, costs for the partner surpass the value creation benefits of the alliance. The partner may opt to terminate, severing the firm's access to common benefits. More egregious forms of opportunism may also incite retaliation in other areas, such as overlapping input or output markets. Thus, we anticipate that egregious opportunism may reverse initial performance improvements available (e.g., Baum & Korn, 1999; Gimeno & Woo, 1996).

Proposition 1: In an inverted-U shape, firm opportunism will increase firm performance up to a point, after which this effect will be reversed.

Opportunism and future performance

Known as the 'shadow of the future' (Axelrod, 1984), a firm can have multiple cooperative relationships with a range of partners over their lifetime. Firms are embedded in a dense web of social relations (Granovetter, 1985) and their reputation has an economic value (Fama, 1980) that affects their ability to engage future partners. Hill (1990) asserts that, although opportunism may lead to short-term gains, it will ultimately be damaging for future performance. He argues that opportunistic behavior erodes the potential for future interactions with the current partner (Axelrod, 1984), and destructs the firm's reputation as a collaborative partner across the social network. While accepting this thesis when opportunistic behavior is egregious, we outline how milder opportunistic acts may not have the same effect.

Having illustrated how a partner may be willing to tolerate mild acts of opportunism in the short-term where value creation opportunities exceed costs, this tolerance can be reasonably assumed to persist in the future. In addition, there are two reasons why mild opportunistic acts, as previously described, may actually enhance future opportunities with the current partner. First, opportunism frequently involves learning and skill absorption – to the point where the firm can fulfill the alliance activities without the partner's help (Hamel, 1991). This alters bargaining power. A partner who is not learning to the same extent becomes progressively more dependent on the firm and must continue to share more and more to maintain the firm's interest. Therefore, paradoxically, the partner's evolving dependence – a result of the firm's opportunism – can motivate increased commitments to the cooperative relationship. Second, a proactive partner may also harvest private benefits themselves (Hamel, 1991; Khanna et al., 1998; Rai, 2016). This rivalrous dimension of the alliance can spark greater internal innovation (Lado et al., 1997) and make it an important and sustained source of value creation for both parties. Thus, while egregious opportunism will damage the firm's future opportunities with the partner, we expect that mild opportunism can increase these opportunities.

Proposition 2a: In an inverted-U shape, firm opportunism will increase future opportunities with the partner up to a point, after which this effect will be reversed.

We propose that milder opportunistic acts can also increase future collaborative opportunities across the network. Again, this marks a departure from extant literature suggesting that opportunism destructs the firm's collaborative reputation leading to *reduced* collaborative opportunities with other partners (Hill, 1990). Information about the firm's opportunistic behavior is most often transmitted to the network by the partner who has been on the receiving end (Hill, 1990). It can be communicated either directly (information flows through network ties) or indirectly (litigation, termination or other visible signals). Where opportunism is mild, and tolerated by the partner, there can be few signals transmitted and the firm's reputation is preserved. In addition, mild opportunistic acts achieve private benefits such as learning, skill absorption, and additional revenues to stimulate the accumulation of internal capabilities and resources. Thus, the firm's attractiveness as a partner may increase where it is determined by knowledge, capabilities and performance (Dyer, Singh, & Kale, 2008; Hamel, 1991). This occurs because the firm has more to offer potential future partners – greater learning opportunities and more chances to combine complementary resources.

<u>Proposition 2b</u>: In an inverted-U shape, firm opportunism will increase future cooperative opportunities with other partners in the network up to a point, after which this effect will be reversed.

DISCUSSION

Extant theory often assumes that opportunism, when present, is undesirable. This is excessively simplistic and overlooks complex realities of collaborative arrangements. Alliances involve congruent and conflicting goals (Cox, 2004; Padula & Dagnino, 2007), and partners make contextually bound trade-offs by weighing value creation potential against costs of opportunism (Zajac & Olsen, 1993). Building from a literature analysis and qualitative interviews, we highlight how opportunistic behavior can vary in intensity (Williamson, 1979). We illustrate how variations in intensity can generate different performance outcomes for the firm. While acknowledging that high levels of opportunism may be damaging, we find that modest intensities may not follow the same pattern. Mildly opportunistic acts can generate gains from private and common benefits while increasing future opportunities by creating partner dependence, stimulating innovation in the alliance, and enhancing technological capabilities. Therefore, we anticipate that opportunism will influence short-term and future performance in the shape of an inverted-U. Mild opportunism is often accepted, and perhaps even expected, but dichotomous labels of present or absent cannot account for this.

Our insights offer two theoretical contributions. First, by illuminating varying levels of opportunism, we highlight how a 'one size fits all' approach is not appropriate. In line with Williamson's (1979) seminal conceptualization, we illustrate that there are varying levels of opportunism which produce different performance outcomes. This has important implications for extant research, mainly from a game theoretic tradition, relying on models that treat opportunism as dichotomous. Our demonstration of the continuous nature of the construct challenges Hill's (1990) assertion that opportunistic behavior is damaging for firms across a longer time horizon. When variation in the intensity of opportunism is considered, it appears that mild opportunism will not destruct future value creation in the same way as more severe acts. This may be true even where reputational effects are important (c.f. Williamson, 1985) or potential for future exchanges is high. By demonstrating how milder competitive acts may be tolerated in alliances, our research also exposes an important limitation of the Prisoner's Dilemma model when employed to approximate payoffs for interfirm alliances (Quintana-Garcia & Benavides-Velasco, 2004; Ritala & Hurmelinna-Laukkanen, 2009). Prisoner's Dilemma suggests that one partner acting opportunistically can capture the largest individual reward (total value minus what is eroded in common benefits), while mutual cooperation offers slightly smaller individual rewards but the largest aggregate amount. Yet our analysis suggests that behavior within the alliance is not a dichotomous 'defect or cooperate' choice as Prisoner's Dilemma suggests. Rather, there are varying degrees of opportunistic acts; not all of which erode common benefits. Our proposal implies that more sophisticated models may be required to map the payoff structure in alliances where 'defect' and 'cooperate' are not the only options.

Our second contribution stems from an illumination of how firms can simultaneously and sustainably pursue both common and private value creation in alliances (Rai, 2016). Traditionally, a relational view focuses on joint value creation (Dyer & Singh, 1998) while a learning perspective emphasizes private benefits (Hamel, 1991). Thus, it is unsurprising that 'compete' and 'cooperate' are often treated as two sides of the same coin (Chen, 2008). Yet, we demonstrate that both actions can coexist within a strategic alliance and potentially complement one another. For instance, fear of a competitive response is an excellent antidote for the inertia that accompanies unchecked cooperation (Molina-Morales & Martinez-Fernandez, 2009; Yli-Renko, Autio, & Sapienza, 2001). Managers seeking superior value creation may recognize that some opportunism is the price paid for enhanced performance and that success cannot not be measured in terms of a 'happiness index' (Hamel, 1991). By illustrating how opportunism can be beneficial, our proposal illuminates the complexities of how firms create value in alliances.

In summary, we hope that our research begins to capture the dynamic nature of interfirm relations and the managerial challenges where value creation requires an intricate balance of competitive and cooperative behavior. We illuminate varying intensities of opportunistic behavior and demonstrate how, up to a point, opportunism may generate short-term and future performance benefits. This has important implications for how the concept is conceptualized and examined. We urge researchers to be innovative in their falsification efforts and we hope that these efforts can spark timely and important debate.

REFERENCES

Axelrod R. 1984. *The Evolution of Cooperation*. Basic Books: New York.

Bercovitz J, Jap SD, Nickerson JA. 2006. The antecedents and performance implications of cooperative exchange norms. *Organization Science* **17**(6): 724–740.

Buckley PJ, Casson M. 1988. A Theory of Co-operation in International Business. In *Cooperative Strategies in International Business,* Contractor FJ, Lorange P (eds). Lexington Books; Lexington, M.A.: 31–54.

Chen MJ, Smith KG, Grimm CM. 1992. Action characteristics as predictors of competitive responses. *Management Science* **38**(3): 439–455.

Chen, MJ. 2008. Reconceptualizing the competition–cooperation relationship: a transparadox perspective. *Journal of Management Inquiry* **17**(4): 288–304.

Coase, R. 1937. The nature of the firm. *Economica* **4**(16): 386–405.

Cox, A. 2004. Business relationship alignment: on the commensurability of value capture and mutuality in buyer and supplier exchange. *Supply Chain Management: An International Journal* **9**(5): 410–420.

Das TK, Rahman N. 2010. Determinants of partner opportunism in strategic alliances: a conceptual framework. *Journal of Business and Psychology* **25**(1): 55–74.

Dyer JH, Singh H, Kale P. 2008. Splitting the pie: rent distribution in alliances and networks. *Managerial and Decision Economics* **29**(2-3): 137–148.

Dyer JH, Singh H. 1998. The relational view: cooperative strategy and sources of interorganizational competitive advantage. *Academy of Management Review* **23**(4): 660–679.

Fama, EF. 1980. Agency problems and the theory of the firm. *Journal of Political Economy* **88**(2): 288–307.

Fernandez AS, Le Roy F, Gnyawali DR. 2014. Sources and management of tension in co-opetition case evidence from telecommunications satellites manufacturing in Europe. *Industrial Marketing Management* **43**(2): 222–235.

Garrette B, Castañer X, Dussauge P. 2009. Horizontal alliances as an alternative to autonomous production: product expansion mode choice in the worldwide aircraft industry 1945–2000. *Strategic Management Journal* **30**(8): 885–894.

Gnyawali DR, He J, Madhavan R. 2008. Co-opetition: promises and challenges. In *21st Century Management: A Reference Handbook*, Wankel C (ed). Sage Publications: London, U.K.: 386–398.

Gnyawali DR, Park BJ. 2011. Co-opetition between giants: collaboration with competitors for technological innovation. *Research Policy* **40**(5): 650–663.

Granovetter, M. 1985. Economic action and social structure: the problem of embeddedness. *American Journal of Sociology* **91**(3): 481–510.

Hamel G, Doz YL, Prahalad CK. 1989. Collaborate with your competitors and win. *Harvard Business Review* **67**(1): 133–139.

Hamel, G. 1991. Competition for competence and interpartner learning within international strategic alliances. *Strategic Management Journal* **12**(4): 83–103.

Hennart, JF. 1991. The transaction costs theory of joint ventures: an empirical study of Japanese subsidiaries in the United States. *Management Science* **37**(4): 483–497.

Hill, CW. 1990. Cooperation, opportunism, and the invisible hand: implications for transaction cost theory. *Academy of Management Review* **15**(3): 500–513.

Khanna T, Gulati R, Nohria N. 1998. The dynamics of learning alliances: competition, cooperation, and relative scope. *Strategic Management Journal* **19**(3): 193–210.

Lado AA, Boyd NG, Hanlon SC. 1997. Competition, cooperation, and the search for economic rents: a syncretic model. *Academy of Management Review* **22**(1): 110–141.

Molina-Morales FX, Martínez-Fernández MT. 2009. Too much love in the neighborhood can hurt: how an excess of intensity and trust in relationships may produce negative effects on firms. *Strategic Management Journal* **30**(9): 1013–1023.

Padula G, Dagnino GB. 2007. Untangling the rise of coopetition: the intrusion of competition in a cooperative game structure. *International Studies of Management & Organization* **37**(2): 32–52.

Quintana-Garcia C, Benavides-Velasco CA. 2004. Cooperation, competition, and innovative capability: a panel data of European dedicated biotechnology firms. *Technovation* **24**(12): 927–938.

Rai, RK. 2016. A co-opetition-based approach to value creation in interfirm alliances: construction of a measure and examination of its psychometric properties. *Journal of Management* **42**(6): 1663–1699.

Rindfleisch A, Antia K, Bercovitz J, Brown JR, Cannon J, Carson SJ, Ghosh M, Helper S, Robertson DC, Wathne KH. 2010. Transaction costs, opportunism, and governance: contextual considerations and future research opportunities. *Marketing Letters* **21**(3): 211–222.

Ritala P, Hurmelinna-Laukkanen P. 2009. Whats in it for me? Creating and appropriating value in innovation-related coopetition. *Technovation* **29**(12): 819–828.

Williamson OE. 1975. *Markets and Hierarchies: Analysis and Antitrust Implications*. The Free Press: New York.

Williamson OE. 1985. *The Economic Institutions of Capitalism*. The Free Press: New York.

Williamson, OE. 1979. Transaction-cost economics: the governance of contractual relations. *Journal of Law and Economics* **22**(2): 233–261.

Yli-Renko H, Autio E, Sapienza HJ. 2001. Social capital, knowledge acquisition, and knowledge exploitation in young technology-based firms. *Strategic Management Journal* **22**(6-7): 587–613.

Zajac EJ, Olsen CP. 1993. From transaction cost to transactional value analysis: implications for the study of interorganizational strategies. *Journal of Management Studies* **30**(1): 131–145.