Relationship Marketing in the Era of Network Competition

In this era of network competition, successful partnerships require commitment, trust, and choosing partners carefully.

The economies of the world's nations have become interconnected and interdependent to an extent unparalleled in history. Industry after industry is discovering that competition is no longer just regional or national, but truly global. The global economy anticipated for years finally is being realized in the '90s because of several factors:

- The collapse of the world's command economies and socialism.
- The triumph of market economies and capitalism.
- The explosive growth of technology and its worldwide dissemination.
- The development of instantaneous worldwide communications.
- The rise of knowledge and skills as principal sources of competitive advantage—for individuals, for organizations, and for nations.

Marketing managers must prepare themselves to deal with the consequences of a global economy and the realities of global competition. First of all, the traditional multinational corporation is giving way to the global corporation. Although

EXECUTIVE BRIEFING

The globalization of modern economics is forcing countries and corporations to take a new approach to competition. Firms are forming alliances—or strategic networks—with suppliers, buyers, governments, and even competitors to produce levels of quality, efficiency, and effectiveness never possible under firm-to-firm competition. However, some networks achieve extraordinary success while others fail abysmally. That's because corporate alliances, like marriages, are cooperative efforts built on commitment and trust. Beware of opportunists when prospective partners come courting.
multinational corporations, by definition, always have operated across national boundaries, most of their high value-added activities—such as product design, manufacturing, and R&D—took place in the headquarter’s nation.

In contrast, all the activities of the emerging global corporations, including high value-added activities, are dispersed worldwide. The Mazda MX-5 Miata, for example, was designed in California, financed in Tokyo and New York, and prototyped in Woking, England. It currently is assembled in Michigan and Mexico from components produced in both the United States and Japan. The Miata is a truly global car and Mazda is on its way to being a truly global corporation.

Now, as never before, companies that “think globally” will enjoy significant competitive advantages over those that treat their foreign operations and divisions as subsidiary to divisions in the headquarter’s nation.

As another consequence of the global economy, nations find it increasingly necessary to seek alliances with other nations in order to compete. The United States—the most successful “alliance” the world has ever known—is aligning itself with Canada and Mexico to compete better with Japan and the European Common Market (which is trying to become a “United States of Europe”). The emergence of trading blocs proves that no nation, even the United States, can stand alone; to compete in the global economy, each nation-state must secure allies and cooperate with them.

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**New Era of Competition**

It takes an appreciation for the dynamics of these new relationships to achieve marketing success in this era of strategic network competition. And managers must understand the processes involved in establishing, nurturing, developing, and maintaining successful relationships with all the firm’s exchange partners—be they suppliers, competitors, nonprofit organizations, government agencies, or even the firm’s own divisions and employees.

**Traditional Competition**

Exhibit 1 illustrates the traditional view of competition, using the auto industry as an example. Competition is horizontal and firm-to-firm at each level; that is, auto manufacturers compete with other auto manufacturers, materials’ suppliers compete with other materials’ suppliers, ad agencies compete with other ad agencies, and so on.

The advantages of traditional competition in such an industry structure are numerous, both for individual firms and for society as a whole:

- All firms specialize in those activities they do best, i.e., their core competencies.
- All firms are optimally positioned to take advantage of economies of scale because marketplace forces punish firms that are either too large or too small.
- The discipline of marketplace price ensures efficiency because all firms negotiate at “arms length.”
- The capital investment of each firm is kept to the absolute minimum.
- All firms can (and must) adapt quickly to changes in the environment, such as technological advances. For example, if a new firm develops a radically new battery that would obsolete...
all the capital equipment of current battery producers, automakers could adopt the new battery without thinking about the investment losses of its current battery suppliers.

Traditional, firm-to-firm competition is efficient, productive, and dynamic because it unleashes what economist Joseph Schumpeter called the forces of "creative destruction."

Hierarchical Competition

Even though traditional, firm-to-firm competition has many advantages, it also has some inherent disadvantages, so some companies engage in the kind of integration that results in competition between what economist Oliver Williamson calls "hierarchies." In its early days, Ford was, for all intents and purposes, "just" an assembler of automobiles made from parts that were manufactured by other companies. Over the years, however, Ford adopted the structure illustrated in Exhibit 2, integrating backward to such an extent that at one time it even made its own steel!

In contrast with firm-to-firm competition, highly integrated firms have:

- Lower transaction costs, realized by not having to buy and sell goods/services from independent suppliers.
- Less likelihood of being the victim of opportunistic behavior, such as suppliers not fulfilling their contractual responsibilities.
- More autonomy through increased control over the resources necessary for survival and growth.
- Better coordination of activities.
- Greater opportunity to plan for the future.

By 1980, Ford was one of the most highly integrated corporations in the world (as were Chrysler and General Motors). The benefits of integration, thought many, exceeded the disadvantages: decreased competency fit, potential diseconomies of scale, lack of price discipline on components produced "in-house," high investment expense, and lack of the kind of flexibility and adaptability associated with creative destruction.

Strategic Network Competition

During the '80s, business academics began theorizing about a form of competition that could potentially combine the best parts of both traditional and hierarchical competition without incurring the disadvantages of either. This resulted in strategic network competition, illustrated in

**Exhibit 1**

**Traditional view of competition**

- Raw materials supplier
- Auto parts supplier
- Advertising agency
- Ford
- Automobile dealer
- Automobile buyers

**Exhibit 2**

**Hierarchical view of competition**

- Raw materials supplier
- Auto parts supplier
- Advertising agency
- Ford
- Automobile dealer
- Automobile buyers

- Ford raw materials division
- Nissan raw materials division
- Volkswagen raw materials division
- Ford parts division
- Nissan parts division
- Volkswagen parts division
- Ford advertising department
- Nissan advertising department
- Volkswagen advertising department
- Ford assembly division
- Nissan assembly division
- Volkswagen assembly division
- Ford company dealerships
- Nissan company dealerships
- Volkswagen company dealerships
Exhibit 3 and exemplified by the Japanese car companies and their keiretsu.

Formally speaking, a network is a group of independently owned and managed firms that agree to be partners rather than adversaries. Because each partner's individual success is tied to the success of the overall network, the firms pursue common goals. They engage in cooperative behaviors and coordinated activities in such areas as marketing, production, finance, purchasing, and R&D. Although each firm is independently owned, the extent of cooperation and coordination among the firms is so great that company boundaries become "fuzzy," as illustrated by the broken lines surrounding each firm in Exhibit 3.

Network competition best describes the current situation in the auto industry. Ford no longer just competes with Nissan and Volkswagen; rather, Ford and all its partners compete with Nissan and its partners and Volkswagen and its partners. Although (arguably) not as far along as the auto industry, competition in such industries as computers, communications, and consumer electronics increasingly is leaning toward a network orientation. Firm after firm is turning from discrete, arms-length exchanges with large numbers of suppliers toward long-term, "relational" exchanges with a smaller number of partners.
Relationship Marketing in the Era of Network Competition

As shown in Exhibit 4, relational exchanges in network competition take place between firms and their (1) goods suppliers, as in just-in-time procurement; (2) services providers, as in integrated marketing efforts involving sales promotion, advertising, and marketing research agencies; (3) competitors, as in strategic alliances; (4) nonprofit organizations, as in ties with universities, the Olympics, and “green” marketing groups; (5) government entities, as in joint R&D; (6) ultimate customers, as in database marketing; (7) intermediate customers, as in franchising and other distribution channels; (8) functional departments, as in cross-functional project teams; (9) employees, as in internal marketing and total quality management; and (10) business units, as in cooperation across corporate divisions, subsidiaries, or other strategic groupings.

IBM alone is thought to have more than 500 strategic alliances, and other examples of relationship marketing abound.

- Procter & Gamble has assigned permanent employees to live and work at Wal-Mart’s headquarters to coordinate sales of P&G products.

- Sega Enterprise, a powerhouse in video games, was dubbed a “master collaborator” because of its alliances with AT&T in communications, Hitachi in chips, and Yamaha in sound.

- Corning now defines itself as a “network of organizations.”

- Glaxo has an alliance with the city-state of Singapore to develop drugs that treat diseases of the brain.

- Rochester, N.Y., has joined with three major universities, Kodak, Xerox, and several smaller firms in a collaborative effort to make the city the leading center for optics technology.

- Levi Strauss, using electronic data interchange (EDI), monitors daily product sales at major retailers to better coordinate purchasing, manufacturing, and inventory.

- Saturn considers its employees and customers to be partners and uses both groups in its advertising. (Note that in Exhibit 3 ultimate customers are part of the network.)

- The Pacific Wood Products Cooperative in the Northwest has a network of more than 185 wood-products firms to coordinate purchasing and marketing.

- Leaf Inc. and Ben & Jerry’s team up to make Ben & Jerry’s Heath Bar Crunch ice cream.

- Motorola allies itself with 11 partners in Iridium, a consortium for developing a global wireless communication system.

- Revlon works with the National Breast Cancer coalition to develop relationships with women by supporting cancer research and early breast-cancer detection.

- AT&T develops relationships with small businesses through its Customer Access Program.

- Nestle courts families by operating Le Relais Bebe rest stops—sparking clean facilities, complete with hostesses, where parents can feed their babies and change their diapers—along main travel routes in France.

The success of each partner depends on the success of the network.

All of these firms are cooperating with other entities to compete successfully. The starting point for all partnerships is the exchange of complementary resources. For example, most strategic alliances involve partners exchanging technology for technology, technology for market access, or market access for market access. But the mere fact that two entities have complementary resources will not ensure success.

Relationship Marketing

No matter how many partnerships constitute the overall network—from just two in a “simple” strategic alliance to thousands in a large franchise chain—the success of each partner depends on the success of the network. It is crucial, therefore, for each firm to manage relationships with its partners. “Relationship marketing” refers to all marketing activities directed at establishing, developing, and maintaining successful relational exchanges in the supplier, lateral, buyer, and internal partnerships shown in Exhibit 4. (Historically, relationship marketing referred only to partnerships with ultimate customers.)

Some partnerships are much more successful than others. Indeed, though estimates vary, about one third of all strategic alliances appear to be outright failures, and many others are only moderately successful, as judged by the participants. A study of 895 strategic alliances across 23 industries found that participants rated them to be successful only 45.3% of the time.

As a case in point, consider the auto industry. Although the Ford-Mazda strategic alliance is widely regarded to be an extraordinary success, industry observers generally view the General
The Commitment-Trust Theory

The traditional concepts of power and conflict characterized in research on buyer-seller interactions fail to explain the success of marketing relationships intended to extend over long, if not indefinite, periods of time.

Our early investigations led us to believe that successful marketing relationships involve cooperative partners, not power-conscious adversaries, and that commitment and trust are the key drivers of cooperative relationships.

To test our theory, represented by the model in Exhibit 5, we conducted a national survey of more than 200 independent automobile tire retailers. Competition in the tire industry is increasingly global; Europe is home to Dunlop (Britain), Michelin (France), Pirelli (Italy), and Continental (Germany); the United States has Goodyear and Cooper; and Japan is represented by Bridgestone/Firestone, Sumitomo, and Toyo.

The manufacturers view OEM sales to automakers as so critical to success that many take losses to become OEMs for automakers in hopes of building brand loyalty among consumers in the replacement market. Furthermore, European and U.S. tire manufacturers find that establishing relationships with Japanese automakers is an arduous task because the local tire companies enjoy membership in automobile keiretsu.

These conditions create some interesting dynamics for the relationships between tire manufacturers and retailers. In 1992, Goodyear announced that Sears stores would carry Goodyear tires, marking the first time in the company's history that it strayed from its own dealer network. Also, Bridgestone/Firestone began converting its Firestone stores to "Tire Zone by Firestone" in an attempt to refocus retail efforts on tire sales instead of automobile services.

All of these moves reflect the turbulence of an industry dealing with global competition and make relationships in the tire industry ideal for testing our theory.

Using LISREL, our results strongly supported both the overall model shown in Exhibit 5 and eight of its nine arrows, or "effects." The single exception was the effect of relationship benefits on relationship commitment. Apparently, the specific benefits of the relationships we explored, i.e., product performance, customer satisfaction, and gross margin, either had no substantial effect on relationship commitment or they were statistically accounted for by other factors.

From our analysis of tire dealers, we drew these conclusions:

* A firm will trust its relationship partner when both partners share similar values, when communication in their relationship is healthy, and when their relationship history is not characterized by one partner maliciously taking advantage of the other.

* Relationship commitment arises not only from trust and its antecedents, but also from the direct effects of shared values and the beliefs that partners would be difficult to replace.

* More than half the differences in levels of cooperation from one relationship to the next can be explained by relationship commitment, trust, and their antecedents.

Therefore, if managers hope to build cooperative relationships with their business partners, they must first work to establish commitment and trust.

**Exhibit 5**

Key mediating variables in relationship marketing
Motors-Daewoo, Chrysler-Mitsubishi, and Fiat-Nissan alliances as either outright failures or significantly less successful than Ford-Mazda.

Because all the alliances were cross-cultural and all the partners brought complementary resources to the table, neither of these factors can explain the disparity between the marketing success of Ford-Mazda and the disappointing results of the other auto partnerships.

Rather, Ford-Mazda's success results from the partners managing the relationship to maximize the likelihood of effective cooperation. The paradox of relationship marketing is that being an effective competitor in the era of network competition also means being an effective cooperator. The success of the Ford-Mazda alliance can be attributed to two characteristics of their relationship that bring about effective cooperation: commitment and trust.

In our research on partnerships involving distribution channels, we found that effective cooperation entails both mutual trust and mutual commitment—not just one or the other. Successful alliances, like successful marriages, don't just happen; both require commitment to make them work, and both can be destroyed by mistrust.

Examining the details of the Ford-Mazda alliance reveals that it has been managed—purposefully or accidentally—to promote commitment and trust. First, both parties must perceive every cooperative project to be mutually beneficial; senior managers ensure that there is an overall balance of benefits for both companies. Second, top management sets the “tone” for the relationship by letting it be known in no uncertain terms that middle managers are expected to cooperate with their counterparts to achieve these benefits. Third, the partners maintain open lines of communication and hold frequent face-to-face meetings.

For example, the senior management strategy group, comprised of top executives from both Ford and Mazda, meets for three days every eight months to discuss present and future projects. One of these days is always reserved for informal “getting to know each other” activities, which adds the critical human dimension to the relationship.

Perfect Unions

Our research investigating the commitment—trust theory of relationship marketing, outlined in more detail on the facing page, prompts us to offer the following maxims for relationship marketing success.

Choose partners carefully. Partnerships of all kinds involve significant investments of time, money, personnel, and possibly equipment. Although such investments signal relationship commitment to the other party, they also can become “sunk costs” that have little salvage value outside the specific relationship. Because terminating an unsuccessful relationship can be very costly, it makes one partner vulnerable to opportunistic behavior by the other.

For example, a partner can exploit the alliance for short-term advantage by not abiding by the (formal and informal) terms of the agreement. Even written contracts will not necessarily protect companies from opportunistic behavior, such as withholding or distorting information, appropriating proprietary technology or key personnel, making late payments, and delivering sub-standard products.

For example, General Motors tore up hundreds of contracts with its suppliers and demanded immediate, double-digit price cuts from them. Moreover, GM distributed suppliers’ own proprietary blueprints to rivals to satisfy its quest for lower prices. Some GM suppliers now (privately) claim that they will never again invest in technical research for GM.

In the era of network competition, firms should maintain traditional arms-length relationships with firms that have opportunistic tendencies and develop partnerships with trustworthy firms. For example, Inverness Castings Group Inc. in Grand Rapids, Mich., is a major partner of Chrysler Corporation. Chrysler recently purchased a new part from Inverness that cost 30% more than the part it replaced. Why? Because Inverness’ research showed that the new part would save on assembly time and result in a higher quality final product. As another major Chrysler supplier put it: “At Chrysler, the price does not fall until the team gets the cost out, as opposed to putting a gun to your head and saying ‘lower your prices.’”

In all relationships, disagreements are inevitable. The real issue is, do the partners perceive these disagreements as an effective way of bringing problems out into the open or do they bristle with anger and begin looking for other partners?

Our research suggests that parties who trust each other handle disagreements or conflicts in a positive manner, working to identify ways to solve the underlying problems that led to the disagreement. Because communication is an important part of this process, a key concern in choosing a partner should be its willingness to share timely, meaningful information.
When searching for trustworthy partners, past personal experience with a potential partner is the most valuable guide. However, in the case of totally new partners, evaluations must be based on the company’s reputation in the industry gleaned from a thorough investigation.

“Investigate before you invest” is the credo of the International Franchise Association, and it’s wise counsel for any firm that is considering entering a network with a new partner.

Shared values signal a potentially trustworthy partner. Firms should seek out partners that hold similar beliefs about what business behaviors are appropriate or inappropriate, right or wrong, proper or improper, and acceptable or unacceptable.

In cross-cultural partnerships, for example, one factor that can make an alliance doubly difficult is a potential lack of shared values, even though global corporations are becoming increasingly cosmopolitan. Alas, cross-cultural alliances are like multicultural societies such as the former Yugoslavia and the Soviet Union; both self-destruct in the absence of a common “core” culture. Like porcupines making love, one should approach cross-cultural partnerships very, very carefully.

Structure partnerships carefully. The key structural issue in relationship marketing stems from its raison d’etre: exchanging resources to provide mutual benefits and, thus, achieve mutual goals.

To build a successful partnership, managers must have not only a clear understanding of each partner’s contributions and goals, but also a structure that ensures an equitable balance of benefits. Baldrige award winner Motorola, for example, uses quarterly confidential surveys of major suppliers to track its own performance in providing benefits to its partners.

Consider Ford’s relationship with Excel Industries Inc., a maker of car windows. Ford discovered that windows produced by Excel reduced inventory requirements and assembly costs. Ford was so impressed that it not only “de-integrated” by selling its own Fulton, Ky., window company to Excel, but also guaranteed Excel 70% of its window business. Thus emboldened, Excel plowed $4 million more into better manufacturing systems.

As a result, Excel’s sales and profits have flourished, and the company now equips new Ford models a year faster than before. “There’s a spirit of trust,” said the general manager of Ford’s glass division. “We’re both trying to find the most efficient solutions.” Structuring partnerships for mutual benefits, therefore, leads to better products, lower costs, and relationship marketing success.

Long-term partnerships, again like marriages, either grow in complexity over time or wither on the vine. Therefore, devising formal, written contracts that cover all future contingencies is impossible. Although negotiating a formal contract may assist parties in communicating their expectations, if the partners refer frequently to the contract after it is signed, the relationship is already on its way toward failure status.

If you must have a formal contract, we highly recommend including mediation or arbitration clauses. In the franchising arena, franchisors have long known that arbitration is a far superior method of dealing with franchisee conflicts than is litigation.

Allow time for relationship growth. Because commitment and trust develop slowly, start with small projects with a new partner and expand the scope of the relationship gradually. As the relationship grows, a complex set of norms will evolve for making the relationship work. These norms cover such aspects of the relationship as how each party will exchange information of value to the other and how each party must react to safeguard the relationship in the face of unexpected circumstances. Norms, then, substitute a kind of psychological agreement for formal contract clauses.¹⁵

When Harley-Davidson cut 200 members from its supplier roster and entered long-term relationships with its remaining 120 suppliers, Harley’s legal department suggested a 40-page book that codified every detail of the relationship.¹⁶ Harley’s president, in his words, “threw the lawyers out” and signed brief documents with each supplier outlining goals and a way to resolve disputes. Harley-Davidson now relies on informal norms to guide the relationship, not clauses in formal contracts.

Maintain open lines of communication. Network organizations should have multiple points of contact because communications—both formal and informal—enable partners to align their expectations of what the partnership can produce. Informal socializing builds the personal relationships that contribute significantly toward the development of trust. As International Computers Ltd. puts it in its guidelines for successful collaborations, “friends take longer to fall out.”¹⁷

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Opportunism brings short-term gains at the expense of long-term success.

Consider the case of the Blimpie sandwich chain. As rival Subway began to corner the submarine sandwich market, Blimpie ignored its own franchisees to concentrate on developing new Mexican food concepts.

When Blimpie franchisees complained that they were not receiving appropriate marketing support, the chain's co-founder Anthony Conza set out to rebuild trust by opening communications. He traveled to more than 75 cities to meet the franchisees personally and discuss their problems, formed a franchisee advisory council to get continuing input on key issues, launched a newsletter to communicate with franchisees on a regular basis, established an 800-number franchising tips hotline, and gave franchisees more control over their own advertising through regional advertising cooperatives.

Moreover, recognizing that all the partners in the network must share in the benefits, Conza allowed some franchisees in distress to divert their 6% royalty fees to advertising. "We don't want to open a bunch of stores...and have them fail," he said. "That's just not the way we like to do things."

Maintain a corporate culture that is trustworthy. In the global village, there is no place for opportunists to hide. Therefore, having a reputation for corporate integrity is critical in the era of network competition. Character counts, and opportunism brings short-term gains at the expense of long-term success.

Consider the press reports of alleged billing fraud at Sears, Roebuck and Co.'s auto service centers in 1992. The California Department of Consumer Affairs accused Sears of systematically overcharging auto repair customers 90% of the time at 33 Sears centers, with overcharges averaging $223 each.

"Sears has used trust as a marketing tool, and we don't believe they've lived up to that trust," said the Consumer Affairs Department director. Indeed, the retailer's ads maintain that "You can count on Sears." Sears's response has been to scrap commissions and product-specific sales goals for auto center employees nationwide. Maybe Sears can regain consumers' trust and maybe not. But wouldn't it have been better for Sears to monitor the behavior of its own employees to ensure that such policies as commissions and sales goals were not encouraging unethical, if not illegal, behavior?"  

Time and time again, research shows that successful relationships of all types are built on trust. As the Sears example illustrates, to be recognized as a trustworthy partner at the organizational level, firms must be recognized as trustworthy at the personal (employee) level. After all, customers don't interact with "Sears" the organization, they interact with the employees.

Research on corporate culture and relationship-building implies that when a firm's culture emphasizes the values of honesty, fairness, responsibility, and competence in its relationships with its own employees, this in turn helps ensure that employees perform their jobs in a way that portrays the firm as a trustworthy partner for others.

Cooperate to Compete

The very nature of competition in the global economy is changing. Firms increasingly realize that they need allies to compete effectively in the era of network competition.

The message here is not that national economies should turn toward cooperative structures similar to state monopolies or cartels; the central lesson of the 20th century is that such structures become not only massively inefficient and stagnant, but economically and spiritually impoverished as well. Rather, the message is that the unit of competition has shifted from the firm to the network. And companies that engage in network competition must cooperate within their own networks.

There are no guarantees for relationship marketing success in the global economy. But this much is certain: In the era of network competition, going it alone and/or opting for the short-term gains of opportunism are sure-fire formulas for failure.

Endnotes


Business Week (1992), "Learning From Japan" (Jan. 27).


Business Week (1992), "Learning From Japan" (Jan. 27).


Business Week (1993), "Blimpie Is Trying Hard to Be a Hero to Franchisee Again" (March 22).

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