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Networks alliances as strategy: A case study of an SME in an emerging economy.

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TITLE: Networks alliances as strategy: A case study of an SME in an emerging economy.

ABSTRACT: This study adopts a qualitative approach to examine key factors to build successful network alliances in emerging economies. A market leader firm in the retail optical industry in China was used in this study. Data from interviews was collected from senior management of the firm, suppliers and customers in relation to effective strategies and factors for successful network alliances. The result in this study showed that relationship management and knowledge sharing management had the highest impact on effective network alliances. That is, trust, relationship and knowledge sharing play a dominant role.

KEY WORDS: Strategic network alliance; relationship management; knowledge sharing management; SMEs.

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1. Introduction

The global financial crisis (GFC) and the rise of the BRIC (Brazil, Russia, India, China) economies have shaped a new business environment requiring new strategies and a reconfiguration of resources, skills, and processes to sustain competitiveness. In particular, the BRIC economies have delivered significant challenges to the developed economies through their low cost, production and service advantages which challenge the traditional business models used by western MNCs and drive continued global hyper-competition. Sirkin et al (2008) argue that ‘globality’ is with us; that is, companies are competing with everyone, from everywhere for everything. In addition the impact of the GFC highlighted liquidity, credit and risk management as major concerns with financial institutions and firms in various industries (Pisano & Verganti 2008).

Firms now need to develop new business models and new value chain networks that can further deliver stakeholder value. Each firm or network of firms leverages different resources and activities to create unique strategy and value chains. Although the network alliance is not a new business model (Kleindorfer & Wind 2009), and there are both examples of successes and failures, there is a lack of research as to what the critical success factors are in the development of effective network alliances in the post GFC environment in emerging economies such as China.

With the strength of the Chinese economy in recent years, foreign firms are eager to enter the China market. These foreign firms can choose from a number of entry options (such as joint-ventures, solely owned firms, licensing, and alliances) to compete with local firms. This choice is particularly important for foreign firms entering an emerging economy like China where intense structural challenges and barriers are the norm (Khanna & Palepu 2010).

This study aims to identify some of the key factors, and their relative impact, required by firms to build successful network alliances (in this case successful means sustaining competitiveness) within small enterprises in China in a post GFC environment.

Using a single case study of a market leader firm in the retail optical industry in China, this study contributes to the development of an actionable network alliance framework. The empirical evidence and associated discussions that follow corroborate the calls for placing a greater emphasis on relationship and knowledge management in the network alliance process in order to sustain competitiveness in an ever changing business environment like China.

The paper begins with a literature review of the key notions of this study, namely, the structural challenges in emerging economies, the concepts of value creation in a network approach, and the value drivers for effective network alliances; this is followed by a brief description of the case used in this study (the Baodao Optical Group). After a discussion of the methodology, the research findings are discussed and the paper concludes with the limitations of the study, the contributions made, and suggestions for further research directions.

2. Literature review

2.1 Structural challenges in emerging economies

The integration of suppliers and buyers to create a value chain is a continuing challenge for all economies. However, the challenges for value creation in emerging economies are different to developed economies. Khanna & Palepu (2010) noted that emerging economies have structural voids (barriers) which require firms to adopt different strategies to navigate around these challenges in their value creation strategies.

As emerging economies are unlikely to offer efficient market intelligence foreign firms cannot adopt similar strategies to those in their home (developed) markets. They may need to form joint
ventures with local firms to gain local market intelligence. For example, local needs and willingness to pay are market intelligence that firms need to have. Furthermore, local government regulations are likely to pose significant challenges to firms to navigate around without a local partner; as well as the process of contract enforcement because of the non-transparency in the legal system.

The lack of an efficient financial transaction system for procurement and payment will add additional costs to both buyers and sellers. Furthermore, the issue of trust with payments could be another challenge. Without an efficient banking system, firms may not be able to raise capital easily to expand. Another challenge is distribution channels as emerging economies often have inadequate logistical infrastructure and deliveries, particularly in the rural areas, are problematic. The sharing of knowledge between suppliers and buyers, to create a better value chain, is a continuing challenge for most firms.

Firms entering emerging economies need to consider the many challenges discussed above and decide whether they should compete independently or collaborate with local partners. New market entrants can choose either to accept existing market constraints or attempt to change the market context (Khanna & Palepu 2010). The strategic network alliance framework as discussed in this paper identifies key drivers required by firms for building an effective network alliance that shapes the market context, and overcomes structural barriers, in order to expand their markets in China.

2.2 Value creation in the network approach

The dynamic capabilities approach (Teece et al 1997, Helfat et al 2007) highlights the importance of integrating, building, and reconfiguring internal and external competencies (i.e. how to adjust the firm’s resource mix) to address rapidly changing environments and to create competitive advantage and extra value for the firm (i.e. emphasize the process of resource development and renewal). Furthermore, the concept of co-creation of value with consumers (Prahalad & Krishna 2009) whereby customer inputs could add to the total value chain is becoming a significant factor. Based on the concepts of dynamic capabilities and co-creation of value, the strategic network alliance is an approach that leads to a new value chain. The strategic network alliance approach focuses on the right connectivity of opportunities, processes, and partners to create the value chain (Kleindorfer & Wind 2009). As a business model the strategic network approach is not new. For example, airline alliances like One World and Star Alliances, Li & Fung global sourcing (Fung et al. 2008), have operated successfully in the past. However, not all strategic network alliance models are successful. For example, Boeing has confronted many challenges in adopting the network approach in the construction of its latest aircraft Boeing 787 – the Dreamliner (http://www.exostar.com). The right connectivity, relationships (guanxi) and business partnership is not new although the transparency of this practice may be different in various cultures and countries (Chen 2004, Khanna & Palepu 2010).

Partners bring in various resources and skills, and share knowledge and learning, all of which can result in: advantages in scale, scope and speed; innovative product development and market penetration; the connecting of various activities to satisfy new opportunities or structural holes/gaps (Zaheer & Bell 2005); cost reduction; value creation, and benefits to all network members (Koza & Lewin 2000, Douma, Bilderbeek, Idenburg & Loosie 2000).

With the challenges facing emerging economies and in this post GFC environment, the strategic network alliance framework may be the model that provides sustained competitiveness in this uncertain environment. This is a model that could provide flexibility, lower risk, increase global reach, and provide opportunities for smaller firms to grow. However, key factors contributing to the effectiveness of network alliances for smaller enterprises to sustain competitiveness may be different in China. Although outsourcing is another practice which can be seen as a network activity, this does not fit with the concept of a strategic network alliance. Outsourcing tends to have more of a functional focus (e.g. outsource production) and there is little sharing of strategic issues between the host firm and the outsourcer.
Why is now the right time to exploit the strategic network alliance approach in China to sustain competitiveness and create value for stakeholders? What are the key drivers that are critical for the success of this strategic network alliance approach now which may be different to the past? Are you ready for this network collaboration approach? These are critical questions for individual firms to answer. In particular, value creation in emerging economies has unique challenges. Emerging economies have structural challenges (Khanna & Palepu 2010) which firms have to navigate around differently as compared to developed economies. Despite this what is clear is that the network challenge is a growing trend in business model innovation (Kleinforfer & Wind 2009, Markides 2008).

One of the reasons that the network model is becoming more important as a business model is because firms are now competing with everyone, from everywhere for everything (Sirkin et al. 2008) and firms when operating in emerging economies may need to adopt different strategies to achieve value creation. For example, firms may need to seek opportunities from local sources and network with partners from everywhere. Previously, only multi-national firms would expand from domestic to global. Nowadays, small firms can form strategic alliances and challenge existing multi-national firms. What is new is the networking ability of smaller firms (not exclusive to multinationals) that could adopt this strategic network alliances approach (with lesser financial risk) to create a new value chain to challenge established players.

### 2.3 Value drivers for effective strategic network alliancing

The discussion on networks in types, innovation and coordination, leadership, value creation and competition is not new (Kleinindorfer & Wind 2009). Literature has well covered the challenges of network-based innovation and value creation (Prahalad 2004); knowledge management (Tapscott & Williams 2006); social capital (Jackson 2008), process efficiency (Fung, Fung & Wind 2008); and risk management and global supply chains (Kleinindorfer & Wassenhove 2004). A review of the network alliance literature (Kleinindorfer & Wind 2009) and an examination of successful firms participating in network alliances (for example Li & Fung, Dell etc) suggested that successful factors in forming an effective business network alliance can be grouped into four key value drivers as follows: (1) advances in information and communication technologies (ICTs) (Obmae 2005, Irani & Love 2001). The speed, cost and reach of ICTs has enabled firms from everywhere to network with each other. ICT provides the backbone for technology development, process improvement, knowledge and relationship management; (2) processes and design improvement (efficiency and differentiation) is ever changing (Zott & Amit 2008, Taylor 2005, Gupta 2004). Firms can rapidly change their processes and connect the right activities to suit multiple customer needs more readily; (3) flexible and rapid responses are demanded by customers to co-create value (Prahalad & Ramaswamy 2005) and unique relationships enable knowledge sharing (Blumentritt & Johnston 1999) with network partners (Kleinindorfer & Wind 2009, Fung et al. 2008, Prahalad & Krishnan 2008); Customers in the ‘noughties’ demanded their input into the supply chain, for example, the customised delivery of Dell PCs through the internet. Knowledge regarding customer needs, production capability, delivery channels and the network of suppliers or stakeholders are readily shared among strategic partners. However, firms are now expected to go beyond this through the increasing involvement of their customers in the R&D process; (4) relationship, risk management and trust (Buehler, Freeman & Hulme 2008, Jarillo 1993).

The leverage of each of these four value drivers depends on the individual firm or network of firms’ abilities (Figure 1). The alignment and integration of the drivers is important for the network alliance particularly in the post GFC environment, and in an emerging economy, because it can create greater flexibility, lower financial risk, and reach bigger markets for smaller firms. Consequently this strategy can enable firms to create increased value customised to its own environment.
3. Research methodology

3.1 The case study approach

This study adopted a case study approach to determine key themes and success factors in a strategic alliance network model in a post global economic crisis in China. This single case method was useful because it provided the in-depth contextual information on network alliance strategy, knowledge sharing capabilities, trust and the complex cross-functional processes between partners embedded in inter-organisational fabric (Dyer and Wilkins 1991, Eisenhardt and Graebner 2007, Flyvbjerg 2007, Halinen & Tornroos 2005). This corroborates suggestions of past studies (Ogbonna and Wilkinson 2003, Yin 1989) that recommended the use of single-case design for the study of contextual information such as organizational culture and processes.

3.2 The case study firm - (Baodao Optical Group- BOG)

Baodao Optical Group (BOG) is the largest optical retail chain in China (covering all major cities in China). In 2006, BOG had 618 retail outlets and 1700 employees. In 2011, it now has 1002 retail stores, 12 strategic partners, and exclusive rights to 10 foreign brand licenses (e.g. international brands such as Louis Vitton, Prada) and 5000 other outlet shops in China. BOG has an effective performance culture, innovative leadership, talented teams, and a leading IT (Enterprise Resource Planning-ERP) system to share knowledge with its stakeholders and employees.

Baodao Optical was the first private firm in China to introduce ERP in 2000. The ERP system has provided a leading edge in information communication technology (ICT) within the optical industry in China and has contributed significantly to its current commanding position. Process management activities based on its ERP system provide Baodao with state of the art procurement, inventory/warehouse management, CRM, and financial reporting capability. Knowledge management is captured by working with its stakeholders and the ability to co-create value with its suppliers, strategic partners and customers. For example, customers can change and modify their frames and lens anywhere in China and after service can be done anytime and anywhere with its existing network. All data are captured to assess the needs, trends and activities to continue to improve on customer satisfaction. Upstream and downstream innovation is constant. With an annual value of purchases of close to 70M RMB relationship management is a critical part of the firm. Apart from the focus of customer satisfaction, Baodao has leveraged on social responsibility as part of its relationship management policy. Finally, Baodao Optical has excellent capability in generating social capital and a strong network of strategic partners through collaboration, knowledge sharing and trust. As commented by Jim Wang Zhimin (CEO Baodao), ‘knowledge sharing with suppliers is a continuing challenge and a continuation of network collaboration to expand is our growth strategy for the future. There are still a lot of opportunities in and outside China in this industry’.

Although Baodao Optical has a successful track record with network alliancing and is the market leader in the optical industry in China, with the new post GFC environment, would the alignment and integration of drivers for effective network alliance remain the same?

3.3 Sampling, data collection and data analysis

This case was selected because Baodao optical is the leading optical group in the market in China and has adopted the strategic alliance network model to grow and sustain its business. Access to the field to study strategic network is very limited because most firms would regard such activities as highly confidential.

In-depth semi-structured interviews were conducted with the CEO of Baodao Optical Group, the chief procurement officer, the deputy CEO of its main supplier, and the purchasing manager of its main retail customers. A combination of methods: observations, archival data and in-depth interviews were used in the data collection. This arena offered detailed data that illuminated key
factors for effective network alliance formation; the challenges and barriers for these factors; the interface and processes between partners; the management style of key executives; the history and culture of the firms; the social and government linkage; the existing processes and their future development; the competencies and capabilities of partners; the alignment of strategic goals between partners; the internal IT capabilities of firms; and the willingness of partners to share knowledge. The analysis of these data enabled the understanding of the interaction between partners, as to how they developed a network based on the links between the key drivers for effective network alliance. That is, the main themes were developed and grouped into key drivers in the development of a network alliance framework.

In order to reduce interview effects, the authors were involved in the interview process so as to protect from researcher bias in data collection (Denzin 1989). Subsequently, they analysed multiple interviews independently and discussed research notes and coding systems with each other. Each interview lasted between 90 to 120 minutes. All interviews were tape-recorded and transcribed. Interview respondents were invited to elaborate on each question.

The interviews were largely unstructured and open. Preliminary questions were used to explore the history and culture of the firm, the challenges in doing business in China, and the effect of the GFC in the business environment. Later on, specific questions were asked based on key words or themes. For example, ‘Can you describe how you select your strategic partners?’; ‘What are the important factors in the market to sustain growth in the optical industry in China?’ (e.g. ICT, process improvement, knowledge sharing and trust etc).

The data collection activities resulted in 4 audiotapes, 13 pages of field notes, 37 pages of archival document (including organizational chart, strategic plan, minutes of executive meetings, operational and financial data etc) and 41 pages of transcripts. The transcripts were analysed using Nvivo software. Deductive and inductive approaches were adopted to provide the final framework for effective network alliance.

In order to increase the validity and reliability of this case study, between-method triangulation to capture investigated phenomena from different perspectives (Yin 1989) was adopted. Data triangulation is based on the collection and comparison of data from multiple respondents (the CEO of Baodao Optical Group, the chief procurement officer, the deputy CEO of its main supplier, and the purchasing manager of its main retail customers) (Denzin 1989). Furthermore, between-method triangulation relied on the use of multiple methods such as interviews, observation and archival data in order to explore the key drivers for effective network alliances.

3.4 Result of analysis

The analysis of interview data (using Nvivo) provided a total 154 nodes. Key words from nodes such as trust, collaboration, sharing knowledge, long term relationship, openness, top management team (TMT) support, leadership, alliances, market knowledge and efficient information system, were often repeated in interviews. Key words and frequency from interviews are provided in Table 1.

<table>
<thead>
<tr>
<th>Keywords</th>
<th>frequency</th>
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<tbody>
<tr>
<td>Knowledge sharing</td>
<td>40</td>
</tr>
<tr>
<td>Relationships</td>
<td>38</td>
</tr>
<tr>
<td>Information systems and technology</td>
<td>36</td>
</tr>
<tr>
<td>Trust</td>
<td>35</td>
</tr>
<tr>
<td>Collaboration</td>
<td>12</td>
</tr>
<tr>
<td>Openness</td>
<td>10</td>
</tr>
<tr>
<td>TMT support</td>
<td>5</td>
</tr>
<tr>
<td>Leadership</td>
<td>7</td>
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Interview data also provided a summary of key challenges for foreign firms in strategic partnership in China (Table 2). These challenges are not new and they are common for foreign firms in emerging markets (Khanna & Palepu 2010).

*Table 2: Challenges for foreign firms in strategic partnership in China*

<table>
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<th>Challenges</th>
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<tr>
<td>1. Lack of local marketing knowledge</td>
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<td>2. Challenges of identifying the right strategic partner</td>
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<tr>
<td>3. Lack of local insights and regionalized market information</td>
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<tr>
<td>4. Difficulties in knowing principles of relationship, trust, and law</td>
</tr>
<tr>
<td>5. The biggest problem of foreign firms is their rigid codes of operation</td>
</tr>
<tr>
<td>6. Inflexibility at times of strategic decision making in foreign firms due to their distant and rigid codes of conduct</td>
</tr>
<tr>
<td>7. Lack of relationship and know-how of relationship with different levels of local government</td>
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</tbody>
</table>

Although literature review (the deductive approach) suggested there may be four main drivers for effective strategic network alliancing: (1) advances in information and communication technologies (ICTs) (Obmae 2005, Irani & Love 2001); (2) processes and design improvement (efficiency and differentiation) (Zott & Amit 2007, 2008, Taylor 2005, Gupta 2004); (3) knowledge sharing (Blumentritt & Johnston 1999) and (4) relationship management (Kleindorfer & Wind 2009, Fung 2008, Prahalad & Krishnan 2008); the analysis of nodes in this study resulted in seven major themes (factors) for effective strategic network alliancing (Table 3).

*Table 3: Seven major themes/factors for this study*

<table>
<thead>
<tr>
<th>Major themes</th>
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<tr>
<td>1. Finding the right strategic network partner</td>
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<tr>
<td>2. Building strong relationships with local market</td>
</tr>
<tr>
<td>3. Acquiring and sharing market intelligence</td>
</tr>
<tr>
<td>4. Developing localized products/services</td>
</tr>
<tr>
<td>5. Knowledge sharing and ICT</td>
</tr>
<tr>
<td>6. Process improvement and ICT</td>
</tr>
<tr>
<td>7. Trust and relationship management</td>
</tr>
</tbody>
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The analysis of the knowledge sharing interview data revealed that there are three types of knowledge. These are:

- Localized market knowledge as China is a multi-market country
- Product development knowledge
- Political legal knowledge to deal with local government issues

Furthermore, content analysis of knowledge sharing data suggested that both parties must be willing and able to share knowledge for strong strategic network alliance and openness, trust and relationship building were key behaviors between partners. For example, the following are samples of responses supporting the above proposition: “Strategic partners must be willing to share information and have tight contracts in their transactions” and “Trust, collaboration and sharing must be in alignment to achieve the mutual benefit of the partnership”.

The analysis of the process improvement interview data revealed that it is conceptually coupled with ICT and entails the integration of Enterprise Resource Planning (ERP) and logistics; The integration of ICT between partners would further enhance the effectiveness of processes and network alliance.

Finally, key sample interview statements supporting relationships between key themes and effectiveness of strategic network alliances is presented in Table 4.
Table 4: Sample of interview statements for key drivers

<table>
<thead>
<tr>
<th>Explored link</th>
<th>Sample interview statements</th>
</tr>
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| Trust and relation with a strategic network partner and sharing | – Procurement director: Partnership must have the fit, trust, risk and profit sharing……..Baodao and us have many things in common, we trust and shared our key market information with them. We shared our distribution costs and we have clear simple contract transactions.  

– CEO Badoo (Jim Wan): the main challenges are still finding the right partner who has the right fit in market knowledge and willingness to share and trust. |
| ERP, ICT and process improvement                       | – CEO Badoo: We are upgrading our ERP system. We had SAP for over 8 years now and it is due for an upgrade. We used SAP before but we are thinking changing it into a lego system…..still have SAP as the platform but input with different plug-in module to integrate our functions.              |
| Knowledge sharing and ICT                              | – CEO Badoo: Although we have an IT system based on SAP integration, it is not sharing to its full potential. We have got something like financials, inventories, suppliers etc…..some of these information are not totally integrated with partners…..we can share more to fully utilize our knowledge data base…. |
| Local knowledge sharing                                | – CEO Badoo: we cover all major & secondary cities, we covered north to south, we are also good in product testing. Pricing to different tiers – 6 tiers of cities and 6 tiers of consumers; we have good local knowledge….we are also looking at long term ….and we shared with our suppliers and key customers. |
| Product knowledge and sharing                          | – Major Supplier: With communication, I can send messages out every day to sales team once I know which product is lagging and ask them to push certain products with incentive. |
| Localized knowledge                                    | – Major Supplier: alliance is more difficult for foreign firms in china. They lack the local insight for different markets.                                                                                                  |
| Political legal knowledge                              | – Retail customer: Furthermore, good relationship with all stakeholders are important. We have good relationship with them, including local governments. We contribute to community projects and local government are happy with us.  

– CEO of Badoo: you need local knowledge, you need good trustworthy partners, you need connections and relationship with local warlords (government officials), |

The content analysis coupled with the Nvivo analysis show that the eight themes derived from Nvivo analysis can be grouped into the four drivers suggested in the literature review. Finally, based on the result of the above discussion, a conceptual framework for effectiveness of strategic network alliance in China is provided (Figure 2).
Discussion

This study explored key value drivers, and their relative impact on the effectiveness of network alliances. While literature review suggested four major drivers, this research highlights the relative importance of relationship management and knowledge sharing management as the dominant forces in effective network alliances. The results from Table 1 & 3, suggest that the themes of trust/relationship and knowledge sharing play a dominant role. The relative importance of these two drivers has been discussed in previous studies (Tiessen & Linton, 2000, Young-Ybarra & Wierseman, 1999, and Gerhard & Odenthal, 2001).

Figure 2, highlights that sharing capability in a network alliance is dependent on partner willingness and ability. The findings relating to the theme of ‘sharing of knowledge’ include product-market knowledge, political-legal knowledge and local customer knowledge, which suggests that the challenges in emerging economies (Table 2) remain a significant part of building network alliances in China. Although there is a link between information communication technology (ICT) and process improvement themes (Table 1, 3 & Figure 2), these two themes command a lesser effect on effectiveness of strategic network alliances. Hence, the finding in this study, based on the inductive qualitative approach, has partially supported the original premise that four key drivers are necessary for strategic network alliance success.

Based on the above discussion and the new business environment in the post GFC climate in China, the key drivers suggested in previous studies for effective network alliances are still relevant. However, the empirical evidence from this study revealed that relationship management and knowledge sharing management could exert a bigger role in China. Furthermore, it can be seen that small entrepreneurial firms (small to medium enterprises –
SMEs can form effective network alliances to become the market leader and compete with strong MNCs. The traditional strategic alliances, joint ventures, and long-term buyer-supplier partnerships used by big global firms (Gulati, Nohria & Zaheer 2000) may not be appropriate in this new business environment. Key challenges such as efficient ICT infrastructure, support from local/regional government policies and good social capital are also important in an emerging economy such as China. This study suggests that if the key drivers for effective network alliances are used appropriately, SMEs can reconfigure activities and key drivers to develop new sources of value through a strategic network alliance framework.

Conclusion

In the post financial crisis of firms are more focused on risk management and banks remain cautious and reluctant to lend to small businesses. Furthermore, with the challenges and constraints of an emerging economy, small firms need to be more innovative to align and integrate their limited resources. As firms navigate through the constraints imposed by the post GFC period, the dependence on financial resources to grow is still a major challenge. The findings in this study showed that other resources such as relationship management and knowledge management could be better deployed to form an effective strategic network alliance framework that could sustain growth and competitiveness. That is, resources could be more focused on relationship and knowledge sharing management to form an effective network alliance in China. However, there are key questions that each partner needs to address: What capabilities can your firm bring into the partnership? Are these capabilities in alignment with the four key drivers discussed in this case? Is collaboration right for you and are you ‘alliance ready’?

Limitation and future studies

Given the limited generalizability of a single case study design, further studies may benefit from large scale longitudinal studies in order to identify cause-effect relationship between key drivers and effectiveness of network alliances for sustained competitiveness.

Future studies can examine similar research themes in non-Asian countries to determine whether the relative impact of drivers/themes for effective strategic network alliancing could be influenced by cultural factors. Since China is heavily influenced by ‘confucianism’, there are differences in values, business practices, political and social norms with other Western cultures (Chen 2004, Haley et al 2004).

Another interesting area could be comparisons between industry groups. The empirical evidence presented in this study was with networks between SMEs. Similarly, the linkage between SMEs and MNCs and network between MNCs in the area of strategic network alliances could be explored
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