

Competition and international business networks- Aggregated actors and development of macro networks and hubs

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Abstract

The paper discusses the development of macro networks. It examines the fight over market share, position and development opportunities which influence this trend. It attempts to analyse the reasoning behind this shift of operational models and business concepts, why companies join macro networks and choose to be part of aggregate actors. The paper presents three case studies on telecom, paper and automotive industry. The preliminary findings suggest that these actors improve their competitiveness and position by getting connected into strategic networks although they lose parts of their autonomy the advantages in knowledge transfer, capability utilisation and market positions are far beyond the disadvantages. The objective of the paper is to contribute to the understanding of dynamics in macro network and hub building and mechanisms.

Keywords: International business networks, market share, position, business opportunities

Introduction: International business networks and the competition using consolidation

This paper discusses the development pattern of increasing market power of business networks. The consolidation of actors into organised business networks, strategic alliances and organisations is rapidly developing underneath the ordinary marketing, sales and distribution network. Also supply is intensifying the competition by joining forces. However, these central actors are rather invisible and unknown to end-customers, consumers and even to smaller competitors. They act on a level, which is out of reach for most of those less organised business actors. This megatrend of organising business into consolidated structures using accumulated power is an interesting actual phenomenon that influences the work of almost all small and medium-sized (SME) distributors in the developed world.

The purpose of the paper is to present a multiple case study on business networks that are internationally active and illuminate their role in the contemporary competition and expansion. The dynamic development and its impact are analysed and described. The study attempts to increase our understanding on the functions and positions of these actors who influence business often on a global scale. The aim is to improve the theoretical and managerial understanding on aspects like strategy, particularly for SMEs and highlight the grey area on the perception of competition.

The research frame and perspective

Strategic marketing and management literature forms the backbone of research frame. The study follows the Industrial marketing and purchasing group related approaches (see Ford ed. 2002), especially the work of Hertz and Mattsson (1998, 2001, 2003) on markets as networks is used as a basic frame building on their work on collective competitive dynamics. Also Hertz (1998, 2002) on domino effects and overlap on supply chains is applied.

A multiple case study on business networks

This is an explorative and descriptive study. The paper examines three business networks and their positions in comparison to a certain market area. The cases include paper and paperboard industry and distribution, automotive aftermarket industry and telecommunication industry. A multiple case study is selected as method (Yin 1984). A combination of qualitative and quantitative methods is used (Alasuutari 1999, p.212).

The research questions are: How and why this consolidation process takes place? What are the core dynamics? How do these large networks expand further and where does it lead the other actors, the SMEs? The paper concentrates on the network dynamics and the way they manage and form development.

Gummesson's (2001) interactive research model is applied and a process view in a selected time period is used. A processual view is chosen (Alasuutari 1995), which has a progressive logic (Pettigrew 1997). Pettigrew (1997, p.338) defines process as: "a sequence of individual and collective events, actions, and activities unfolding over time in context". Van de Ven (1992, p.169) sees process as a logic to explain a causal relationship in variance theory, as a category of concepts referring to activities of individuals and organisations and as a sequence of events that describe how things change over time. Case study methods are used for descriptions and explorations (cf. Yin 1984; Bonoma 1985; Eisenhardt 1991; Alasuutari 1995; Van de Ven and Poole 1995). Case study is suggested as a suitable research method for real, complex situations where the case is analysed as part of its environment using several research methods for data collection and multiple material sources (Yin 1984; Christiansen and Hansen 1987; Hirsjärvi, Remes and Sajavaara 1997). Easton (1995) pinpoints the appropriateness of case study for research in industrial networks due to the embedded character of network relationships. Data is collected from several sources with selected methods. Triangulation is applied as a combination of research methods, various forms of triangulation are used (cf. Denzin 1978; Alasuutari 1995; Stake 1995; Silverman 2001). The research material consists of three existing studies. Events and changes inserted in the time frame are analysed (Halinen, Salmi and Havila 1999; Hedaa and Törnroos 1997; Halinen and Törnroos 1995; Anderson and Mattsson 2006). A focal network approach is chosen for the analysis (Halinen and Törnroos 2005).

The theoretical and managerial discussion

Key issues faced for managing in international business networks can be viewed from four interrelated levels: (1) industry-level macro networks, (2) international strategic business networks, (3) actor portfolios within an industry cluster, and (4) position management.

Industry-level macro networks: Industries are constituted of entangled networks of actors making them often dynamic. Management has to be able to understand and to recognize the existing and emerging value systems and their actors through which the industry-level macro network produces value to the existing and future customers. The more multifaceted the existing or emerging value system is, the more challenging the management task is. Identifying technological development paths and the opportunities and challenges involved is part of the key capabilities related to this management task. The amount of existing or available resources do not always guarantee the existence of this capability as illustrated by the Swiss clock industry failure in the 1980s when they did not anticipate the breakthrough of digitalization of clock industry and thus lost their position in markets. Another example is the American automobile industry and its failure to identify the power of Japanese automobile industry and the attractiveness of small economical family cars in 1990s.

International strategic business networks: Industry clusters are made up of multiple overlapping strategic networks. Jarillo (1988, 32) defined strategic networks as a "mode of organization that can be used by managers and entrepreneurs to position their firms in a stronger competitive stance", and he suggested a strategic network to be "a purposeful and conscious arrangement among distinct, but related profit-seeking organizations often led or set up by a hub firm" (cf. Miles and Snow, 1986; Park 1996, 797). Mobilizing and coordinating the relevant actors is essential in managing in strategic business networks. Important questions are: (i) How a hub organization to create and develop a value-producing strategic network in an international context? It requires a constant monitoring of changes in the competitive environment of each actor of a strategic network within actors' own industries as well as tuning the network's strategy, and the actors' roles and positions according to industry's and competitive environment's changes. Besides the common network strategy, each member has their corporate and business strategies to obey (cf. Mintzberg, Ahlstrand and Lampel 1998, 255). According to Mintzberg, Ahlstrand and Lampel (1998, 255), the participants in a business net negotiate through a web of relationships to come up with a collective strategy. Sometimes the collective strategy of a net is not enough. If, for example, there are powerful industries in which technological development can generate major changes in industry structure and in actors' positions in the markets, then the hub should have a cluster strategy for the network actors of a particular industry in order to ensure its own position, the network's competitive advantage, and predict possible future additional changes within the field. When the operational management concentrates in the coordination and maintenance of a single relationship, the strategic management of relationships involves the assessment of any single relationship within the company's strategy in markets. Any single firm has only limited control over its relationship portfolio and network position (Håkansson and Ford, 2002). Further, strategic management covers a portfolio of relationships and it is concerned with the interplay between them and their particular importance and the resulting resource allocation. (Ford, 2002, 75) However, the managerial challenges of strategic management

of a portfolio of relationships in a creation of a business net seem to be less studied than operational management of relationships.

(ii) What positions or roles the hub should try to attain in different business networks and what would be its strategic actions? The position describes how the hub is connected to the other actors, to what external resources it has access and with which actors it competes, and the attributes of its internal resources. Strategic actions are aimed at influencing one's own and other actors' positions in a network and therefore how actors are connected to each other. Strategic actions are both controlled and facilitated by the network's structure and by strategic actions by other actors in a network.

At the international strategic business network level the network strategies can be divided into (i) performance and operational efficiency, (ii) capability development and acquisition (iii) actor portfolio management within a cluster in a strategic network (cf. Loeser 1999, Juntunen, 2005, 243-246). Increasing network's performance and operational efficiency is a key issue in existing value systems (cf. Juntunen 2005, 161-197). The incremental improvements of existing and acquired capabilities require abilities for creating trust and fostering existing relationships in joint projects. When firms try to develop and implement new technologies in a business context, managers have to be able to orchestrate actors from several different fields. This demands, besides the envisioning capability discussed previously, such networking capabilities as assessment of actors' value to the network now and in the future, developing network strategy and direction through agenda setting and engaging, and coordination and control of actors' resources. A key aspect is the capability of identifying the positions, capabilities and business strategies of other network actors and modifying one's own business strategy to match the network situation. (Juntunen, 2005, 241-249) The effects of external relationships are expected to be particularly important in e-business and in technology-dependent business as exemplified by the case in this study (see e.g. Jarillo 1988, 1993; Parolini, 1999).

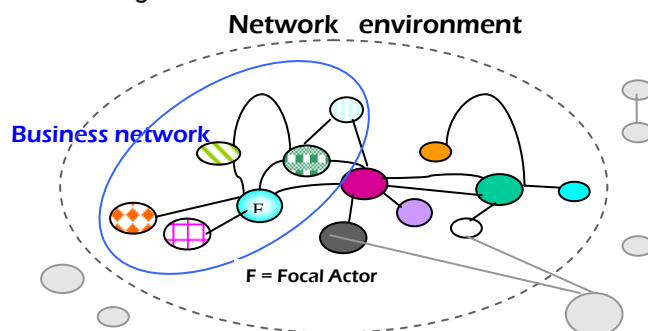
Actor portfolio-level: Business networks are constituted by relationships between actors. At the portfolio-level managers have to decide what kind of organizational forms and contracts their organization will need and use to handle its network's actors and the resources and capabilities it acquires through them. New business creation is not an independent, isolated process but a collective process that requires interaction and cooperation with other actors. It involves the establishment and maintenance of a network of relationships with other organizations including suppliers, competitors and customers (cf. Håkansson and Snehota, 1995). Actor portfolio management is tightly related to the questions of previous level concerning position and actors value in the network. Managers have to decide which activities are carried out internally and externally. This means optimising the processes and the usage of resources. The managers try to handle different horizontal relationships as effectively as possible. The challenge in the actor portfolio management is to evaluate the future value of each of the network actors and to adapt the investments and usage of actors' resources to their value and potential. In addition managers should foresee the potential risk and benefits of actors bonds with other actors in the network – especially with competitors or market leaders. Some actors will deter some new relationships with other industry actors while encouraging others (Juntunen, 2005, cf. also Ford-McDowell 1999).

Position management-level: We contend that the managerial challenges of international business networks are influenced by the position of the specific network in the value system continuum (cf. Juntunen, 2005; cf. also Möller et al, 2005). There are three types of networks (cf. also Möller et al, 2005): Horizontal, vertical and multidimensional networks (MDNs). *Horizontal networks* are created when competing organizations within an industry cluster recognize that they have products, channel relationships or customer service systems that can be combined to achieve a stronger position in global level competition (Möller et al, 2005). *Vertical networks* seem to increase the operational efficiency of the value system within a cluster. Well-specified supplier systems directed and developed by a hub represent the basic form of vertical networks. Examples of these are large national retail chains like K-mart and Wal-Mart. Vertical networks can also lead to incremental and local improvements in the products of the existing value system (Möller et al, 2005). An example of these local product development efforts are Taco Bell's crispy wraps, a combination of a traditional supreme crisp taco and a soft wheat-shell burrito. *Multidimensional networks* (MDNs) range from well-defined value systems to emerging systems presenting radical change, for example, the Mega concept of Home Commerce Business in Elisa Communications (Juntunen, 2005). A MDN contains a hub that directs the network, plans and develops its target customers and products, and integrates the products and services of different types of suppliers and manufacturers. The Mega concept's networks own core capabilities are formed by network envisioning, business and technology knowledge, network creation capabilities, building and developing processes and services, network coordinating capabilities and relationships management skills. According to Eisenhardt and Martin (2000) and Wernerfelt (1984), an actor that commands resources through which it can carry out activities that are valuable, rare, inimitable, and nonsubstitutable holds a very

strong power position in a strategic network. This actor can often appropriate the largest share of the revenue that the net creates (cf. also Möller and Svahn, 2003). The physical manifestation of this power is a formal, written contract stating the boundaries and responsibilities of the cooperation in a specific context between focal actor and another actor in a business network. The contract limits the activities that each actor is responsible of and performs. The exogenous and endogenous factors that can affect the network position are the changes in the corporate and business strategy, the result-based management in a company which in turn can foster the single units results instead of the benefit of the whole organization or the whole network, the organizational structure and its changes over time, the position in the industry (leader, follower, small/large market share), the changes in legislation at the national and in the industry level like deregulation in the telecommunication sector in Europe in 1995 which lead to the emergence of new competitors in the field, and the radical or fast technological developments and innovations like the Internet and the mobile technology which lead to the emergence of new actors and new business possibilities (see Juntunen, 2005, 75-79, 154-160 and 197-200).

Markets and positions

The position describes how the firm is connected to the other actor that is to what external resources it has access, with which actors it competes and includes the actor's internal resources (Mattsson, 2003). Any single firm has only limited control over its relationship portfolio and network position (Håkansson and Ford, 2002). The position in a business network in the scope of this study is defined by the characteristics of the company's relationships and the benefits and commitments that arise from them (see Ford et al., 2002, 7; Johansson and Mattsson, 1988). To get a business network established and a new business started, a firm has to build relationships, which are new to both parties involved (Forsgren et al., 1995, 22). Moreover, the organization's current position is often determined and shaped by its evolution-path (see Teece et al., 1997, 522-523). Also, companies can use the networks to strengthen their position in the markets (cf. Jarillo, 1988, 2; Miles and Snow, 1986; Park 1996, 797), for example focal actors like Nokia and Elisa and their multidimensional networks in the ICT-sector: without a strong intention and well-defined network strategy the focal actor could not have been able to develop its position in the emerging new internet and mobility related services during 1990s.



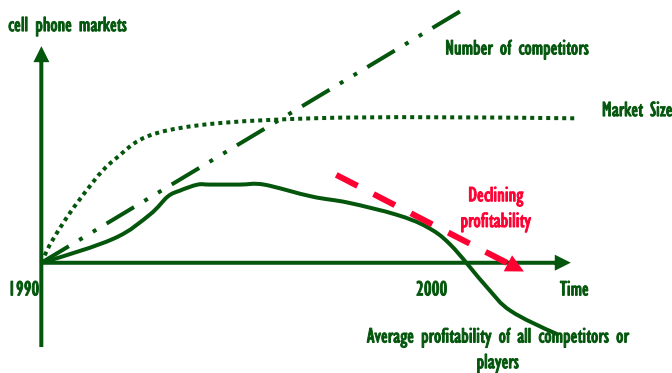
a business network refers to the overall configuration of interconnected actors around a focal actor. **A network environment, a macro network**, refers to the overall configuration of interconnected organizations around a focal actor. The surrounding macro network includes such entities as a market area, economy and society that the focal actor cannot openly influence. The network environment in this study incorporates many other companies which are not visible to the focal actor and to a particular net, and which cannot be directly influenced by the focal actor.

Consequently, according to Eisenhardt and Martin (2000) and Wernerfelt (1984), an actor that commands resources through which it can carry out activities that are valuable, rare, inimitable, and no substitutable holds a very strong power position in a strategic network. The network position itself is not dependent only on the focal actor and its decision-making but also on the changes elsewhere in the network that have an effect upon the position. Therefore it is also important to network with opinion leaders or regulators that have authority to make decisions in certain business area to ensure the firms' future positioning in the markets (cf. Larson, 1991; Liao & Welsch 2002).

At each point in time the firm occupies certain positions in the business network. The position is a result of earlier activities and constitutes the base, which gives both the development possibilities and constraints of the firm within a network context (Forsgren et al., 1995, 22; Johansson and Mattson, 1988). The network position itself is not dependent only on the focal actor and its decision-making but also on the changes elsewhere in the network that have an effect upon the position.

For example, the telecommunications sector and the cell phone markets can be considered as mature markets today. They are dominated by a few major players. However, due to new technologies and market segmentation, many new entrants have found a niche markets in that sector. The fierce competition has caused a hyperfragmentation of the cell phone markets and declining profits in markets. However, the early entrants that gained the leading position in the markets, and are considered as architecture designers, still

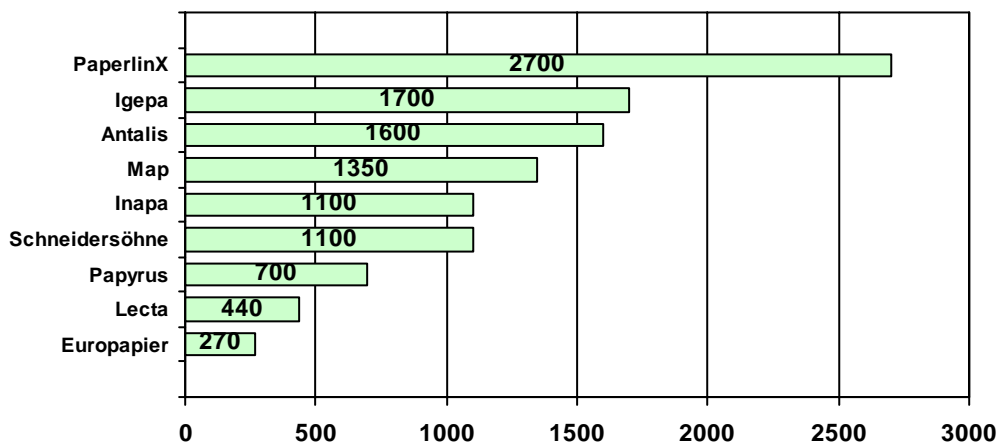
hold a good position in the markets, like Nokia and Motorola. It is not easy for a new entrant to shake their established position in markets.



In many markets, The result of repeating vertical marketing process (segmenting the market, selecting a target segment, and crafting the appealing marketing mix) leads hyperfragmentation of markets as the growing number of competitors in mature markets leads companies to target niches of low profitability. (Kotler & Trias de Bes, 2003)
The different models, sizes and colors of cell phones are examples of hyper fragmentation of mature cell phone markets.

Concentration of activities on vertical level has changed its character during the last years in forest industry, also a very mature industry in Europe and USA (see Siitoinen 2004). The paper and paperboard manufacturers used to have a rather large vertical integration starting from ownership of forests and energy plants to the sales network of own end-products. Nowadays, the vertical networks have been redesigned and the importance of forest and energy investments have been reduced or changed and the significance of sales and distribution channels has been increased. In paper business the distribution channels are rapidly changing and the traditional wholesaler as an independent actor is a decreasing element. Direct sales offices, paper distribution chains, merchants and their e-businesses have become the key actors in many European markets. The change in sales, marketing and distribution strategy represents a fundamental change towards development of large business networks and strategic alliances. StoraEnso, for example, has invested heavily in its distribution strategy and has acquired competitor chains and merchants. The power aggregation is visible when brand presence is analysed. The market presence is visible to purchasers, they can now buy the products from StoraEnso from several suppliers. StoraEnso has created a strong network of distributors all over Europe, it participates in Papyrus and it recently bought Schneidersöhne and a Dutch merchant. The group is a macronetwork in paper supply. Strongly branded products have a good coverage and an excellent availability also at other merchants on a local level.

Major fine paper merchant organisations in Europe, their sales volume and market share in tons in 2004.



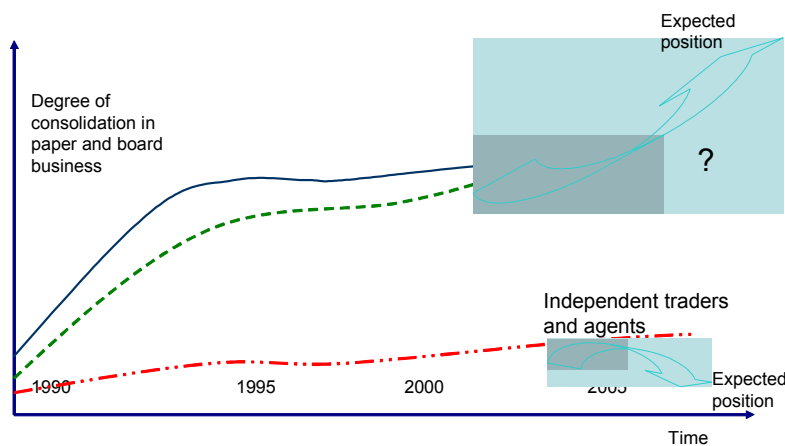
In 2004 the top 7 business network actors had a market coverage, which reached more than 79% share of the total market, where the European market was estimated to be 13 million tons (source: Capi statistics). The concentration of power into aggregated actors leads to change in dynamics. These merchant organisations are active across borders and markets, they may negotiate as one unit and utilise their market share in a more efficient manner than local companies. They transfer knowledge and benefit from marketing and logistics systems. The organisations benefit from the ownership advantage provided by paper and paperboard manufacturers. The organisational nature and strategy of paper sales shows the change in marketing paradigm applied and indicates the significant role of information systems, logistics and marketing

as well as market presence in paper business target markets. The competitive advantages stem from capacities and capabilities, not only from prices and brand names. The role of independent merchants and traders has changed fundamentally, those who have not connected their activities to supplier groups or international business networks have often suffered from declining sales and encountered increasing problems in competition. Organisation into international groups has advanced the position on many local

actors in comparison to those who have preferred to stay fully independent. Branding of products has become one significant issue in sales strategy, pull strategy shows its power putting the no-name merchants in an inferior position. The consolidation process in various trade levels is expected to continue together with the structural changes in paper and paperboard industry (cf. Siitoinen 2004, Elo 2005). The development concerning horizontal integration is unclear, there is high diffusion in customers' and other business actors' perceptions, see Figure . The value chain from

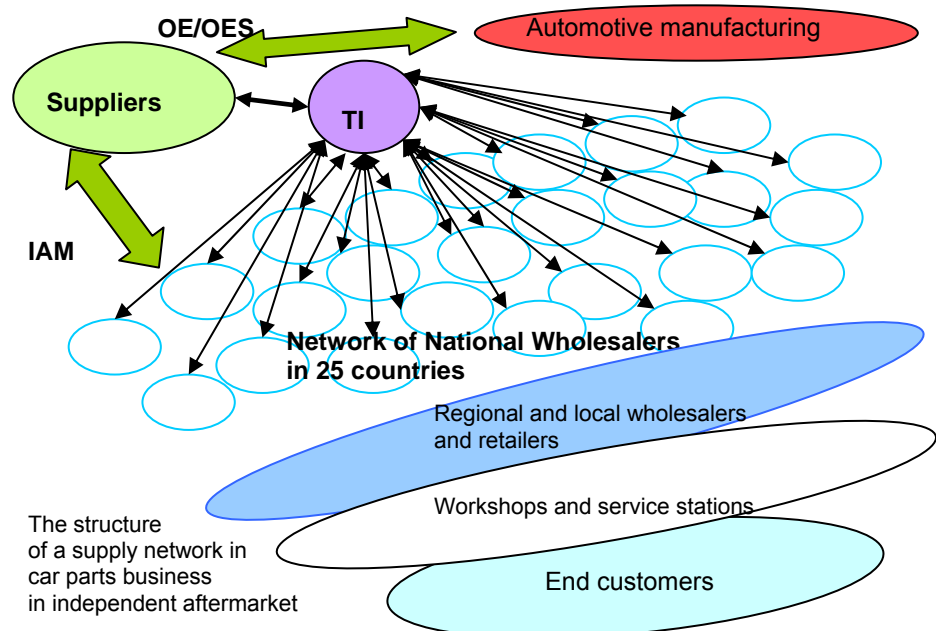
The customer's perspective on consolidation

Development trend in positions: capacities and capabilities



production to market has got shorter when the number of middlemen has decreased, but also the market structures have changed and become more complicated. Access to production and to market is a strategic aspect. Products such as printing paper are no longer seen as commodity type of raw material, but branded products with specific characteristics and an organised marketing, sales and distribution channels.

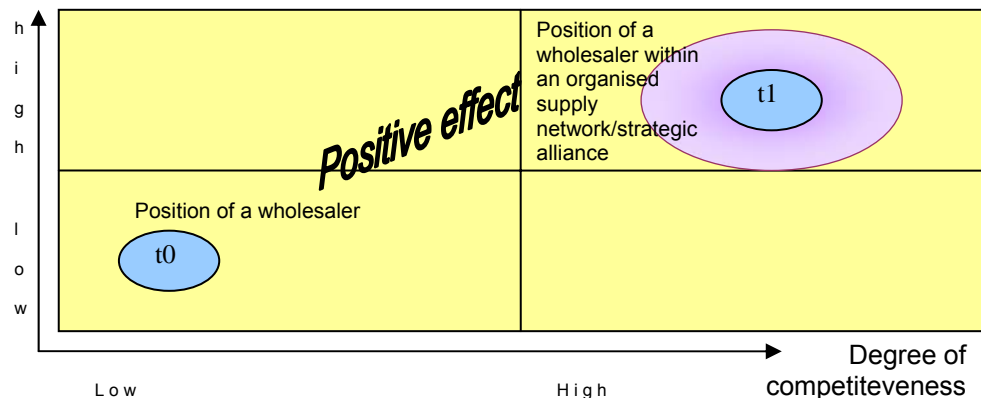
In automotive aftermarket sector (IAM) the business has undergone great structural changes, where business networks and strategic alliances are built and international distribution systems are organised. The traditional independent service outlet system has transformed itself into organised chain partnerships using marketing concepts and common logistics and IT systems, in most European countries there are already many international actors present. These chains support their wholesalers, sales outlets and service



stations with multiple methods and have gained a remarkable market share in comparison to unorganised independent traders and service shops. One example of the business networks in automotive aftermarket is Temot International Autoparts GmbH, (TI). The company represents the trading interests of 20 shareholders in 25 countries and its strategic alliance partners in the USA. This business network illustrates a system of horizontal network which coordinates also parts of the vertical activities in value chain of the members. The

members are wholesalers and groups in car parts and service business, which have united their forces into a central unit that functions as an interface for suppliers, but also coordinates and guides marketing activities, IT systems and logistics systems for its members. The advantages are numerous, the

The positive effect of an organised business network on an individual wholesaler
Degree of market power



members may transfer knowledge and know-how across markets without interest conflicts, they get access to the latest product and supplier-related information and training, they participate in logistics and IT systems that are developed on their practical needs, not distributors. The aggregate actor formation is part of the competitive edge of the member companies due to the increased market power, the economic and commercial benefit and the improved position in the market. See above, at time t0 a wholesaler who was not organised had a considerably lower market power and competitiveness against competitors, suppliers and customers than at time t1 after being a member of a strategic alliance which is an international supply chain. The hub system is developing strongly in IAM and the development is expected to continue.

The theoretical and managerial discussion and conclusions

The trend towards larger units and strategic business network creation indicates the mechanisms of aggregation and consolidation. These interlinked groups that can consist of small and medium sized family companies apply modern methods of organising their businesses and economic interests in such a manner that allows them to grow and compete successfully. The fight for market share and market position is no longer a local one, it is a global one. The degree of interconnectedness in management and operations has increased visibly, there is a kind of shift in business concept paradigm. Particularly in those smaller companies who can “log in” larger business networks without losing fully their independence, this change is of importance. It is an approach in which hubs organise and engineer resources and capabilities globally by orchestrating local actors. The impact of this megatrend is larger than expected, it changes the way companies are connected to each other and how they organise their functions and activities. They are more powerful, but less autonomous. The management is getting increasingly diffuse when the organisational form evolves.

The previous research and the literature indicate the importance of local dimension also in large international business networks, the companies search for “coverage”. The usage of market power and critical masses is not something new, but the efficient way it may be carried out today creates true challenges to any manager, both for those orchestrating the powerful networks and for those trying to hold on to their family companies and regional businesses on local level.

There are trade political tools and regulations, but for many aspects it is the fierce competition that shares and divides the markets according to the interests of the well organised actors. How this development functions and how visible it is to the others outside these organisations is a vital question. Those who were not able to get connected in suitable groups are losing market share and declining. Who has the position to use negotiation power, utilise and transfer efficiently its knowledge and tacit information and use the image of a future key actor has a definite advantage, and these aspects are increasingly congested into groups of actors. These organisations and networks often have the economic power of a large multinational company, which provides them another capacity to lead the development through acquisitions and investments. The findings suggest that the idea of being part of strategic business networks has become a very attractive alternative and the smaller actors are competing heavily between them for the positions in these networks, not only for customers. Twenty years ago the idea of cooperation was for many smaller companies a taboo, it was not considered possible to be that much interconnected with other actors.

The on-going study is expected to contribute to the understanding of the macronetwork dynamics and mechanisms and their form providing descriptions of cases from large networks in international arena. As an outcome of the paper we expect to provide managerial implications on strategic management.

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