

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6315

Memorandum

To: Members, Committee on Small Business
From: Committee staff
Date: March 26, 2012
Re: Hearing: "Large and Small Businesses: How Partnerships Can Promote Job Growth"

On Wednesday, March 28, 2012, the Committee on Small Business will meet at 1:00 pm in Room 2360 of the Rayburn House Office Building for the purpose of receiving testimony on large and small businesses partnering to create added value, jobs and economic growth. This hearing will be an opportunity for Members to learn more about these strategic affiliations, and how they can help us to create more jobs and grow the economy.

I. Introduction

For many years, businesses have entered into agreements with other companies to supply a part for a larger product or to provide a good or service. Today, large companies are creating alliances with small firms to access the innovative ideas, research and services they need to expand their current market or product offerings, expand into new markets, or simply gain a competitive advantage in a challenging economy.¹ Increasingly, large companies are joining with small firms to benefit from the leanness, nimbleness and creativity that are their hallmarks.

II. Strategic Alliances and Partnerships

Large businesses have long partnered with other large concerns for goods and services. Globalization has expanded these opportunities and even made them essential,² and such alliances are even more prevalent today.

¹ Matthew J. Slaughter, *Mutual Benefits, Shared Growth: Small and Large Companies Working Together* (2010) (hereinafter *Mutual Benefits*), available at <http://businessroundtable.org/studies-and-reports/mutual-benefits-shared-growth-small-and-large-companies-working-together/>.

² YVES L. DOZ & GARY HAMEL, *ALLIANCE ADVANTAGE: THE ART OF CREATING VALUE THROUGH PARTNERING* ix (1998) (hereinafter *ALLIANCE ADVANTAGE*).

In the past, technology entrepreneurs and small technology companies partnered with large companies to market their services.³ During the 1980s, alliances between software and hardware companies flourished. Later, the partnerships moved beyond the tech industry to other sectors, such as energy. In the 1990s, innovative entrepreneurs with high-growth companies valued the “small to large” ventures called entrepreneurial partnerships.⁴ This concept captured the Fortune 500 and the Inc. 500,⁵ because neither can function well without the other. Whatever the company or the reason for the alliance, the choice of partner is critical.

These alliances can be numerous; in fact, one study found that the top 500 global businesses have an average of 60 alliances each.⁶ The jump in alliances has only been accelerated by the quickened pace of advances in technology and communications.⁷

III. Large Business/Small Business Partnerships

Partly because of anemic growth in the U.S. economy, and partly because the global economy demands it, small and large companies are connected. Increasingly, they are working together to create more jobs and economic value.⁸ In fact, U.S. small businesses are vitally important to larger businesses.

The typical U.S. multi-national corporation purchases goods and services from more than 6,000 small businesses; purchases a total of more than \$3 billion in inputs from these small businesses; and relies on these small business suppliers for more than 24% of its total input purchases.⁹ Collectively, U.S. parents of multinational corporations purchased about \$1.52 trillion in intermediate inputs from U.S. small businesses, or about 12.3% of their total sales.¹⁰

Small firms account for about 99.7% of businesses in the U.S.¹¹ Collectively, their output accounts for more than half of private non-farm GDP,¹² and, importantly, they generated 64% of net new jobs created in the economy between 1993 and 2008.¹³ As the economy attempts to recover from the recession, small firms are forming partnerships to create jobs and grow. It is

³ Mickey Meece, *Partnerships Based on Service, Not Size*, N.Y. Times, Apr. 30, 2009, available at <http://www.nytimes.com/2009/04/30/business/smallbusiness/30sbiz.html>.

⁴ JAMES W. BOTKIN AND JANA B. MATTHEWS, WINNING COMBINATIONS (1992) (hereinafter WINNING COMBINATIONS).

⁵ Inc. magazine was founded in the late 1970s as a resource for growing companies. It publishes an annual list of the 500 fastest growing non-public companies.

⁶ Jeffrey H. Dyer, Prashant Kale & Harbir Singh, *How to Make Strategic Alliances Work*, MIT SLOAN MANAGEMENT REVIEW 37 (July 1, 2001) (hereinafter *Strategic Alliances*), available at <http://sloanreview.mit.edu/the-magazine/2001-summer/4243/how-to-make-!strategic-alliances-work/>.

⁷ ALLIANCE ADVANTAGE at 2.

⁸ *Mutual Benefits* at 3.

⁹ *Id.* at 3.

¹⁰ *Mutual Benefits* at 3.

¹¹ U.S. Census Bureau, *Statistics of U.S. Businesses* (2009), available at <http://www.census.gov/econ/susb/>; UNITED STATES SMALL BUSINESS ADMINISTRATION, *Frequently Asked Questions*, available at <http://web.sba.gov/faqs/faqindex.cfm?areaID=24>.

¹² *Id.*

¹³ *Mutual Benefits* at 5.

imperative that the climate for growth, expansion and job creation be as conducive to growth as possible. The small businesses of today may well expand to become the big businesses tomorrow.¹⁴

Today, large companies have voracious appetites for new ideas, products and processes. Many large firms can't supply all of the creative ideas they need to grow in today's marketplace, and if they can, they likely choose not to. Large firms are becoming more efficient through vertical integration,¹⁵ an old concept in which a company controls every process from materials to manufacturing to distribution.¹⁶ As companies become more vertically integrated, they increase efficiency, lower costs and benefit consumers.¹⁷ Today, vertical integration means that companies are controlling not every part of their supply chain, but instead the critical parts of it.

Small companies have proven to be particularly adept at reacting to changing economic conditions. Small firms can provide the cutting edge research and technology the larger ones need.¹⁸ Large companies are adept at marketing, while small ones often are not. And both large and small companies often realize that they are stronger together than they can be alone.¹⁹ Even large companies have found that to compete globally, they need the innovative edge that small firms can provide.

Contrary to the view that big companies don't care about small businesses, some large companies now believe that they *need* them.²⁰ Moreover, large companies are aware of the great economic potential that small firms can provide.²¹ Small firms with strengths in various specialties can essentially function as a complementary part of the large firm.²²

Whether firms are large or small, and no matter what they excel in doing, they are more likely to succeed if they partner with a company that does well what they do not. Some studies have found strategic alliances to be critical to the ability of large businesses to develop and sustain a competitive advantage.²³ Conversely, relationships with large companies may help to free small firms from the constant search for additional financing and allow them to focus on their core capabilities.²⁴ Some small companies can get caught in the dilemma of whether to raise capital or sell their product or service.

¹⁴ *Mutual Benefits* at 5.

¹⁵ Rita McGrath, *Why Vertical Integration is Making a Comeback*, HARVARD BUSINESS REVIEW (2009), available at <http://blogs.hbr.org/hbr/mcgrath/2009/12/vertical-integration-can-work.html>; see also *Companies More Prone to Go 'Vertical,'* WALL ST. J., Nov. 30, 2009, available at <http://online.wsj.com/article/SB125954262100968855.html>.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ WINNING COMBINATIONS at 38.

¹⁹ Mickey Meece, *Partnerships Based on Service, Not Size*, N.Y. TIMES, Apr. 30, 2009, available at <http://www.nytimes.com/2009/04/30/business/smallbusiness/30sbiz.html>

²⁰ *Id.*

²¹ *Id.*

²² *Small Business/Large Business Relationships*, INC. MAGAZINE, available at <http://www.inc.com/encyclopedia/small-business-large-business-relationships.html>.

²³ Olumide Ijose, Slippery Rock University of Pennsylvania, *Strategic Human Resource Management, Small and Medium Sized Enterprises and Strategic Partnership Capability 1*, JOURNAL OF MANAGEMENT AND MARKETING RESEARCH, available at <http://www.aabri.com/manuscripts/10430.pdf>.

²⁴ *Small Business/Large Business Relationships*, INC., available at

Typically, Fortune 500 companies have large research and development functions, vast distribution networks, and the cash flow to establish the systems they need.²⁵ Inc. 500 companies, on the other hand, are lean in management and financing, and specialize in quickly bringing innovative ideas to the market.²⁶ Working together, both can excel.²⁷

A. The Supply Chain

One important component of a business is its supply chain. The supply chain offers many opportunities for small businesses to work with larger ones, supplying intermediate inputs²⁸ such as product parts, ingredients or packaging. Small businesses may need assistance from a large firm's distribution network.

Small businesses face many challenges in their supply chain relationships, but research has shown that their size makes them good candidates for supplier partnerships.²⁹ In fact, strategic relationships can increase the likelihood that a small company will survive, and the failure to enter into these partnerships can be a contributing factor to their failure.³⁰ Small suppliers are nimble and flexible, and because they place a high value on strong relationships with suppliers and customers, they can prove to be particularly reliable partners.³¹

B. Managing the Alliance

Alliances appear to be becoming both more important and more difficult to manage.³² Some studies have found that technology companies believe strategic alliances are essential to their ability to stay competitive.³³ Advisors recommend closely evaluating partnership offers. The company leadership must honestly determine whether the relationship will deliver the results they seek.

<http://www.inc.com/encyclopedia/small-business-large-business-relationships.html>

²⁵ WINNING COMBINATIONS at 7.

²⁶ *Id.*

²⁷ *Id.*

²⁸ Intermediate inputs of an industry are the goods and services that are used in the production process to produce other goods or services rather than for final consumption. Intermediate input equals the industry's gross output minus value added. BUREAU OF ECONOMIC ANALYSIS, UNITED STATES DEP'T OF COMMERCE, FREQUENTLY ASKED QUESTIONS, available at http://www.bea.gov/faq/index.cfm?cat_id=0&searchQuery=&start=360.

²⁹ William C. McDowell, Michael L. Harris & Shanan G. Gibson, *The Impact of Trust and Dependency on Business Performance: A Study of SME Suppliers*, 6 THE SMALL BUSINESS INSTITUTE JOURNAL 42 (Oct. 2010), available at <http://www.sbij.org/index.php/SBIJ/article/viewFile/81/46>.

³⁰ *Id.*

³¹ WINNING COMBINATIONS at 7.

³² *Id.* at 6.

³³ Micheál J. Kelly, Jean-Louis Schaan & H el ene Joncas, *Managing Alliance Relationships: Key Challenges in the Early Stages of Collaboration*, 32 R&D MANAGEMENT 11 (2002), available at http://seangallaghersite.com/yahoo_site_admin/assets/docs/Business_Alliances_early_stage_problems.6013056.pdf.

Many companies that excel at managing alliances have a dedicated strategic alliance function.³⁴ A dedicated function acts as a central point for planning, information sharing, decision making and due diligence. Many companies have established routine processes to better manage the relationships.³⁵ Some have found value in viewing the relationships as long-term, and evolving over time. To establish a successful partnership for both companies, it should be structured to provide value, promote cooperation, provide continuity, adjust over time and create value.³⁶

As with any relationship, communication is vitally important to success. Both parties must be responsible for communicating, and for doing so frequently.³⁷ Expectations should be discussed and progress measured. Partnerships are said to be most difficult to implement at the mid-management level, since these are the people carrying out the day-to-day work.³⁸ Although the partnership should be viewed as a long-term one, short-term benchmarks should be identified and marked so that progress and interest stay constant.³⁹

C. Examples of Partnerships

Many large companies are partnering with small companies. For its bottled products, a global beverage company has partnered with a small supplier of new plastic resins made from sustainable resources. A multinational consumer products company has partnered with a small supplier of packaging material for its paper products. The large companies view the small companies as vital suppliers of technology. The small companies depend on the larger companies for marketing and distribution of their products. Both relationships are important for growth.

Particularly at a time of changing economic conditions, these large and small companies view partnerships of their researchers as essential to their economic growth.

IV. Conclusion

This hearing will give Members the opportunity to learn more about the partnerships between small and large businesses. Members will hear from a large business, a small business and a researcher on the important elements of these relationships.

³⁴ *Strategic Alliances* at 38.

³⁵ *Id.* at 39.

³⁶ *See generally* ALLIANCE ADVANTAGE.

³⁷ WINNING COMBINATIONS at 138.

³⁸ *Id.* at 137.

³⁹ *Id.*