SMALL FIRM- LARGE FIRM RELATIONSHIPS: WHEN DO THEY CREATE VALUE?

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Abstract

This dissertation investigates the dynamics of alliances between very small firms and very large firms. Small firms largely rely on alliances with large firms as a source of legitimacy and as an endorsement of their goods and products. Large firms, due to their greater size, typically have extensive bureaucracies and more elaborate processes. These factors may inhibit the exploration of new knowledge. To overcome these limitations, large firms may rely on alliances with smaller firms, as a source of new knowledge.

The first research study investigates the conditions under which alliances with large firms create value for the small firm. Using a resource dependency perspective, it is hypothesized that high power differences between the alliance partners may create instabilities in the alliance. These instabilities may negatively affect the value which the small firm ultimately gains from the alliance operations. It is further argued that the degree of mutual interdependence between the alliance partners will foster an atmosphere of cohesion and information exchange which will serve to positively affect the value gained by the small firm from their alliance operations. Data is tested on 142 small firm-large firm alliances in the biotechnology industry. The results suggest that high power differences between the alliance partners will negatively affect the value which the small firm gains from their alliance operations. The results further suggest that small firms were able to overcome the disadvantages associated with their power handicap when they established repeat alliances and when these small firms established coalitions or multi-partner alliances with their large firm partners. Finally, the study suggests that small

firms must be extremely cautious and prudent when establishing alliances with larger firms.

The second research study takes the large firm perspective and investigates the conditions under which Corporate Venture Capital (CVC) investments create growth options for the large firm. Using a real options perspective, the study hypothesizes that number of CVC investments is positively correlated to the number of growth options generated for the large firm. It is also hypothesized that the growth option value generated from the CVC investments will be higher under several conditions. These conditions include situations where the CVC is executed through a dedicated subsidiary, the CVC sponsoring firm has a high R&D intensity, and also when firms pursue CVC investments internationally. Results on a 6 year panel study comprised of 237 CVC investments undertaken between 1996 and 2002 suggest that the number of CVC investments is positively correlated to the growth options which the large firm generates. The growth option value generated from the CVC investments was also seen to be higher when the firms had a high R&D intensity. However, contrary to what was hypothesized, the results suggested that CVC investments undertaken through dedicated subsidiaries create lower value when compared to CVC investments undertaken by groups which are an integral part of the larger corporation. No support was found for the hypothesis which suggested that the number of international CVC investments is positively correlated to the growth option value.

The overall conclusion that can be derived from the two research studies undertaken in this thesis is that, alliances might be more beneficial or have the potential to generate higher value for the large firm rather than the small firm. This also implies that, to extract maximum direct and indirect benefits from their alliance operations, small firm managers must be cognizant of the challenges and difficulties they may encounter in their alliances with larger firms.