

Increasing MBE Competitiveness through Strategic Alliances

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INCREASING MBE COMPETITIVENESS THROUGH STRATEGIC ALLIANCES

Tuck School of Business
at Dartmouth

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in collaboration with the

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EXECUTIVE SUMMARY

Strategic business relationships are a means by which minority business enterprises can enhance their competitive advantage, which is the ability to secure business that otherwise, might go to another supplier. The relationship decision will be shaped by what the targeted customers need, what contribution to value creation the minority business enterprise (MBE) can provide, and what the strategic ally has to offer that will help the MBE secure customers' business and deliver the promised value.

The alliance decision process begins with an understanding of where an MBE fits into its value chain. This analysis pinpoints which customers the MBE wants to serve, and establishes what value needs to be created to get those customers' business. Upon identifying the "deliverable," the MBE has to assess its own core competencies (what it can do well), its capacity (how much business it can take on, whether its operating strategy is compatible with customer demands, and how much global reach it has) and what competitors are offering.

At this point in the analysis, it often becomes obvious that a particular MBE can't achieve success by working alone. In such cases, the MBE will need to consider various forms of collaborative business relationships, commonly referred to as strategic alliances. Business relationships take many forms, from simple contractual relationships to acquisitions. Strategic alliances are enduring business arrangements falling on a spectrum anchored by these two extremes.

Preliminary data from a survey of MBEs indicated that although MBEs are participating in strategic relationships, the number, complexity and diversity of these relationships is correlated with how long the MBE has been in business, and its current size. MBEs seem most likely to enter into the simplest business relationship that will serve their immediate needs. But MBEs really need to consider the relationship that will best serve their long-term strategic goals.

This paper establishes a common vocabulary for talking about business relationships, takes the reader through the analysis of competitive advantage, inventories the various forms the strategic alliance can take, presents some data about the relative popularity of the alternative arrangements among MBEs, and then discusses some illustrative case studies.

INTRODUCTION

Let's start by saying what a strategic alliance is, and what it isn't. We need some clarity because different people use the same relationship terminology in different ways, leading to confusion and communication difficulties. A precise understanding of the concepts allows people to identify what is the best business arrangement in a particular set of circumstances. This will lay the groundwork for exploring the various options, and look at some examples of how strategic business relationships have enhanced minority business enterprises' (MBEs') competitive advantage.

A strategic alliance is an enduring relationship between two companies designed to achieve mutual gain. Let's examine the terms we just used to describe it:

- An **alliance** is different from a transaction in that allied companies have made a commitment to do—or seek—business together beyond the immediate deal: that's what makes the relationship **enduring**.
- An alliance is **strategic** if it has a significant impact on competitive advantage: that is, if it allows an MBE to get business that might otherwise go to a competitor. For example, getting another company to do groundskeeping instead of doing it yourself is not a strategic arrangement for a Fortune 50 company; but it could be strategic for a landscape design company that wanted to offer clients a turn-key design/create/maintain service.
- **Mutual gain** is achieved when each company achieves results by working together that are better than each could achieve working alone.

MBEs should explore the opportunities that could arise from strategic alliances when reviewing their business strategy (which they should do regularly, given how dynamic markets are today). In addition to making the MBE more attractive to customers—perhaps even being a prerequisite for securing some contracts—strategic alliances can create the effect of larger size without investing the time and expense of growing a business to scale; they can extend the MBE from the domestic into the global business arena; they can provide an opportunity for learning and innovation; and they can foster lean enterprise advantages by eliminating duplicated functions and the associated costs.

There are two major motives for MBEs to form strategic alliances: the MBEs are too small to satisfy contract requirements working alone, or their core competencies and capacity only allow them to do part of a job. As an example of the motivation to achieve functional scale think of an MBE-owned trucking company that has a good record of providing statewide

transportation services, but has the opportunity to make a lot more money if it can offer nationwide service. The MBE may not have the resources to achieve the required geographic scale in time to take advantage of the current contract opportunity, but can achieve the effects of national scale by partnering with a large trucking company that can handle the out-of-state transportation. An example of motivation to ally due to insufficient core competency or capacity would be if the same small MBE-owned trucking company encountered an attractive multi-year within-state contract opportunity where the client needed logistic support and extensive warehouse storage as well as transportation. In the latter case, the MBE can satisfy its client's needs by partnering with a logistics company to supplement core competencies and with a warehousing company to create capacity. Mutual gain is achieved in both these scenarios because the MBE and the partnered businesses gain a revenue stream they would not obtain if working alone.

The next section of this paper explores the economic context in which the decision is taken to seek strategic alliances. We'll explore value chain positioning and choice of customers in some depth because these are prerequisites for building the business case for strategic alliances. Then we will look at the various strategic relationship options MBEs might want to consider, illustrated by some case study examples that will take us out of the abstract and help us to visualize what arrangements can help MBEs be successful.

THE MBE'S ROLE IN THE VALUE CHAIN

When *Homo sapiens* progressed from being simple hunter-gatherers or subsistence farmers to more complex forms of economic activity, we began creating value chains. Exhibit 1.1 shows a simplified, generic manufacturing chain. Let's suppose the manufactured product is an automobile. Raw materials such as steel, rubber, and plastic resin aren't very valuable in their unrefined state, but value is added when these are stamped or molded into components—such as gas tanks, tires, and steering wheels. When the components are assembled to become a drivable car, additional value has been created. When the car is on-site at a local dealership, even more value has been added because the car has been transported nearby and made available for a test drive. Further value is added by businesses that perform services such as financing, insurance, maintenance, and refueling.

Exhibit 1.1: A Simple Manufacturing Value Chain—Automobiles



In the automotive example, a considerable amount of value has been added by the time iron ore has been transformed into something that provides income for an insurance agent. *Members of the value chain are rewarded for increasing the product's value, but the rewards are not equally distributed: some value-contributors are rewarded handsomely, and others are rewarded meagerly.* This is a very important point for MBEs to keep in mind. The ability to generate wealth depends on where the MBE is located in the value chain.

Service value chains tend to be more complex, but are analyzed the same way. Exhibit 1.2 shows a simplified service value chain involving U.S. tax-return preparation. Many taxpayers find the IRS tax codes difficult to apply optimally to their own situation. As a result, value is added when experts interpret the latest tax regulations and create decision trees. But all this knowledge resides inside the head of the tax expert. So value is added when the decision trees are written into lines of code that become software. For taxpayers who have complex tax situations or are uncomfortable using the software, specialists add value by preparing

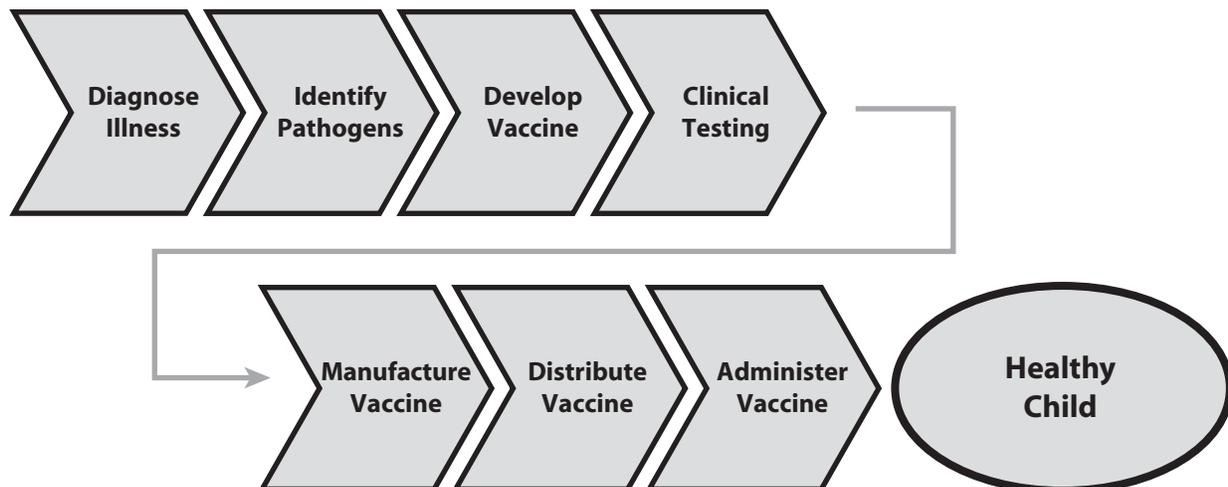
their returns. Further value is added when the specialist submits the return to the IRS. Value has been added at each link in the value chain, but the profitability of each value-added contribution is different.

Exhibit 1.2: A Simple Service Value Chain—Tax Preparation



Many value chains involve both products and services, and these are analyzed the same way (although it is common to have multiple value chains linked together to create composite value). Exhibit 1.3 shows a simplified service/manufacturing value chain that results in a child being vaccinated in a program of preventative health care. Value is added when symptoms of sickness are transformed into a diagnosis. Further value is created when the germs that cause the sickness have been identified, then when a vaccine is developed to create antibodies in children’s immune systems, and next when the vaccine is tested in clinical trials to ensure it is effective and not harmful. From here we move to the manufacturing domain, with further value being created when the manufactured vaccine is distributed to clinics, hospitals, and doctors’ offices. The final opportunity for value creation is in the administration of the dose. As is typical, contributors to this value chain are not equally rewarded.

Exhibit 1.3: A Simple Service/Manufacturing Value Chain—Vaccination



The three different examples of value chains were presented because it is vital for MBEs—and the organizations that foster their economic success—to understand the value chains in which MBEs are embedded. Simply put, *MBEs can't make wise decisions about strategic relationships unless they understand their value chain, how they fit into it, and where the opportunities for growth and profitability are.*

THE LOGIC FOR OUTSOURCING IN THE VALUE CHAIN

Mainstream companies outsource value chain activities when they lack the ability to effectively and efficiently perform these roles in-house, or when there is little profit-potential in that activity. In the case of not being able to do the job effectively, outsourcing makes good business sense because the company lacks the core competency or manufacturing capacity to meet its own demand; or perhaps suppliers have special expertise, specialized capital equipment, lower cost of labor, lower cost of capital, local access to raw materials, or some other economic advantage. In the case of low profit potential, outsourcing is rational because capital is best deployed where the return on assets is greater than the return expected from alternative investments (that is, even when incremental revenues of “in-sourcing” exceed incremental costs, the opportunity costs may not justify doing the work in house). Major corporations, in short, may be better off outsourcing because scarce resources—such as capital, facilities, and managerial attention—would be better off assigned to uses that will generate greater shareholder wealth.

The economic wisdom of outsourcing can be compelling for the majority corporation, but that same logic may not bode well for the MBE. It would be irrational for major corporations to outsource value-chain functions from which they derived strong profit returns: shareholders would object because doing so would curtail their return on investment. The result is that MBEs tend to be offered contracts with low profit potential. Often, what they are offered is not even a value-chain role, but rather is a peripheral support activity such as waste removal, temporary staffing, or grounds-keeping. Let's be clear that there is nothing wrong with MBEs fulfilling peripheral roles in the value-chain, but we must recognize that these rarely result in high wealth-creation for the minority owners or their communities. *Usually, the highest profit potential for the MBE occurs when the outsourcing involves an indispensable value—chain role that the corporation cannot perform efficiently or effectively.*

A clear understanding of the value chain should lead the MBE to be proactive in choosing a value-chain role that has strong potential for profitability and growth. With a strategic direction established, the minority business enterprise needs to be organized to enter and compete in that domain. Doing so entails targeting customers; developing a value proposition that appeals to those customers; creating an operating strategy that will allow the MBE to deliver on its value proposition; ensuring appropriate core competencies and capacity—either by working alone or in a strategic relationship with another firm; and then refining business arrangements so that it can effectively implement its strategy.

This last step, though vital, is beyond the scope of this paper. Briefly, the MBE and its strategically must have a clear strategy; processes that create value for customers while maximizing profitability; organizational and value-chain architecture that supports process optimization; appropriate financial, technological and human resources; systems that ensure control and communication; and employees empowered to ensure value creation and process optimization at the operating level.¹

THE MBE'S CHOSEN CUSTOMERS

It is important for MBEs to *be proactive* in selecting a value chain role and choosing customers. The alternative is to be reactive and respond to RFPs and RFQs. It is unusual for major corporations to use a reverse auction to select suppliers that are strategically important to them. For example, my laptop computer has stickers on it that advertise “Intel Inside” and “Designed for Windows XP.” IBM didn’t put those contracts out to bid: rather, the company negotiated a strategic supply relationship with Intel and Microsoft at the design stage. MBEs need to target specific companies that they can serve well, figure out what it takes to be selected as a supplier, then decide whether they need partners of some sort to create the value their customer is seeking.

MBEs tend to occupy peripheral or upstream² roles in the value chain, and to target mainstream companies as their customers—because these tend to be the ones that dominate their value chains, generate large outsourcing volume, and therefore seem to offer the most opportunities to MBEs. But smaller companies may represent niche customers that are easier for MBEs to serve, often because there tend to be fewer suppliers competing for the business. Alternatively, MBEs can choose to be business-to-consumer rather than business-to-business suppliers, serving the downstream end of the value chain by providing services and goods directly to retail customers. The general point is that *MBEs need to make a thoughtful, strategic choice as to where they best fit into their value chains, rather than settling for whatever business is offered through supplier diversity programs.*

Whether the decision is strategic or opportunistic, an MBE takes a position in a value chain by targeting particular customers. They can be retail customers, tier one suppliers to the ultimate customer, tier two suppliers to tier one, and so on. That choice determines their value chain position. The next step is to formulate a value proposition—the basis of a “sales pitch.” The value proposition declares what value is added by the MBE and implies what the customer

¹ For further details, see Chapter 1 of Leonard Greenhalgh, 2001. *Managing Strategic Relationships: The Key to Business Success*. New York: Free Press.

² The language used by consultants and strategy scholars to describe value chains is somewhat confusing because it mixes metaphors. A value chain conjures up the image of chain links, each attached very strongly to the adjoining links and each being indispensable to the chain’s integrity. The second metaphor is running water, flowing from raw materials to finished product. Upstream refers to the supply end, while downstream takes us closer to the end-user. Despite the possibility of confusion, the terminology is used in the manuscript because readers will encounter this vocabulary when reading or hearing about value chains.

can expect when selecting that MBE as its supplier. A strong value proposition not only assures the customer that their needs will be met, but also highlights the MBE's competitive advantage.

The value proposition is therefore very important. Buyers are pondering why they should do business with this MBE rather than with a competitor—often an established majority-owned supplier. If the MBE's value proposition doesn't promote its competitive positioning, then purchasing agents are likely to assume there is no net benefit to giving business to the MBE, and will be tempted to take the safer route of sticking with the established majority-owned supplier. When the MBE does compare its offerings to the competitors', the value proposition needs to emphasize what marketing scholars call "points of parity" and "points of difference." Points of parity are comparisons of equivalence: the message is that the MBE is giving the customer everything other suppliers can provide. Points of difference explain the greater value the MBE can provide. In the absence of points of difference, business goes to the lowest price bidder, which is seldom a pathway to MBE prosperity.

Once a clear value proposition has been articulated, the next step is to assess whether the MBE has the capability—the core competencies, the capacity, the reach, and an appropriate operating strategy—to serve the customer well (or, stated more formally, to deliver on the value proposition, "the promise" it makes to customers).

Exhibit 2: The Customer-Capabilities Matrix

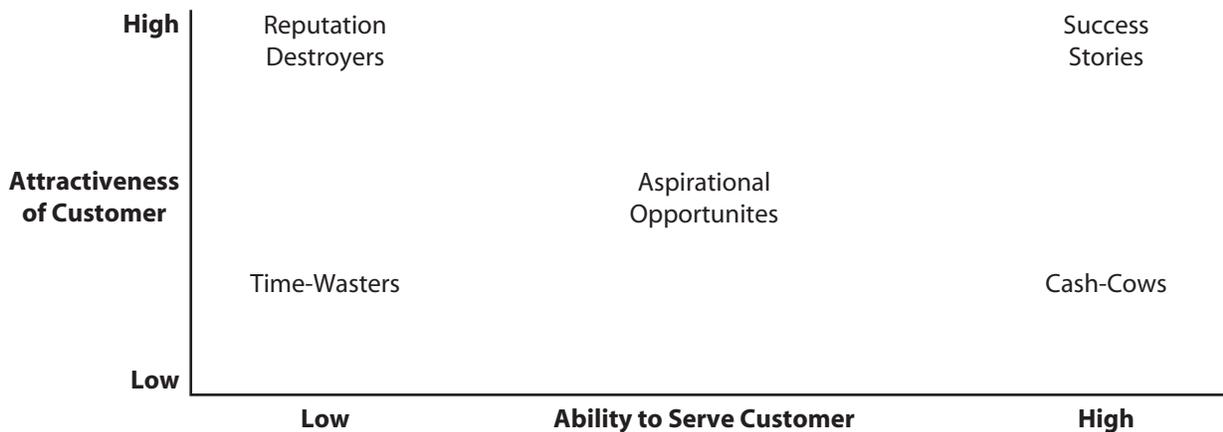


Exhibit 2 shows how the MBE should be thinking about marketplace opportunities.³ MBEs tend to over-emphasize the vertical axis— attractiveness of the customer. Here are the top six characteristics that make particular customers attractive to MBEs:

³ I am deeply indebted to Punam Anand Keller in guiding my thinking about how the conceptual frameworks of marketing strategy illuminate the options for and challenges facing MBEs.

- **Cash flow:** The customer pays its suppliers within a reasonable amount of time, so that the MBE has cash on hand when its own payment obligations come due.
- **Profitability:** Some industries have razor-thin margins, as a result of competitive pressure on prices—due to market saturation (e.g., automotive), commodity status (e.g., janitorial or other industrial supplies), or competition from low-cost countries (e.g., toys). More attractive are the high-profit industries, such as pharmaceuticals, financial services, and health care.
- **Growth potential:** In general, the larger the customer, the more business it can offer to the MBE. But smaller, high-potential customers that are on a promising growth trajectory can offer the MBE ever-expanding volume. Remember that Microsoft, Wal-Mart and Starbucks all started out as small enterprises with high potential.
- **Prestige:** A potential customer is going to be interested in learning who the MBE is currently doing business with. Some current clients will impress and reassure purchasing agents: he or she will think, “If this MBE can successfully serve that customer, it can probably do a good job for us.”
- **Global reach:** Only a few industries—such as nursing home care, landscaping, and automobile retailing and servicing—are primarily local these days. Profitability and growth are more likely to be associated with global value chains. Customers are more attractive if they can bring the MBE opportunities to participate in the global marketplace.
- **Development assistance:** Customers can do a better or worse job of helping to develop suppliers. It is in their interests to invest in their suppliers, not just financially, but in the form of mentoring, sharing consultants, and making training programs available to suppliers. The rationale for doing this is that the stronger their value chain, the greater their competitive advantage against other value chains. Yet some customers are unconcerned with supplier development: they put the business out to bid, sign the contract, then act as if the procurement job is done. The problem with this logic is that if a supplier underperforms or fails, the customer is worse off; so, in essence, the purchasing agent has underperformed or failed, too. Customers that develop their suppliers are more attractive than those that simply give MBEs an opportunity to succeed or disappoint.

Most MBEs spend more time focusing on customer attractiveness than on their capacity to serve their clientele. Here are the top five factors that determine capacity:

- **Core competency:** MBEs are good at doing some things, but they are not good at doing everything. (Nobody is!) If customers require suppliers to provide services or goods that are beyond the MBE’s core competencies, strategic allies may complement their offerings in a way that creates value for their chosen customers. Let’s think about innovation in this context. Innovation is an extension of core competency into a new realm: the MBE working alone may not be capable of offering new goods or services, but may be able to create novel value for customers by partnering with a strategic ally.

Expansion of core competency is a process of learning, therefore a strong motive for strategic alliances is to acquire knowledge or skills from other businesses.⁴

- **Volume potential:** Scale is important—more often than not—in the global economy. An MBE working alone may be simply incapable of supplying the volume a customer requires in a large-scale value chain (as an extreme example, Wal-Mart sells a million dollars worth of merchandise in less than two minutes, 24 hours a day, seven days a week). An MBE partnered with another company may be able to jointly meet customers' volume demands, and get business that would otherwise go to a larger competitor.
- **Operating strategy:** Different customers have different criteria for what creates value from suppliers. Suppliers that can meet customers' particular needs have a competitive advantage over those who are less able to do so. Customer requirements usually involve a tradeoff between cost, quality, delivery, and flexibility. An MBE that has an operating strategy that is aligned with customer demands has a competitive advantage; an MBE that doesn't ought to consider a strategic alliance with a company that can help give the customer what is needed. For example, an MBE might want to do business with an auto company that is most concerned with just-in-time delivery, but has no transportation equipment of its own. That MBE might be a more appealing supplier if partnered with, say, Rush Trucking, a Native American-owned business that has considerable experience meeting the exacting delivery demands of the auto industry.
- **Ability to finance operations:** One of the most common causes of MBEs' failure to prosper and grow to scale is running out of cash. MBEs have to issue paychecks and pay bills early on, but tend to get paid by their customers some time later. Inability to fund the shortfall of cash creates illiquidity, a problem that increases in magnitude when the company is growing. An MBE that has a high-potential business model and an early record of success may nevertheless experience difficulty getting bank loans, perhaps due to lack of collateral. Partnering with a cash-rich company will be the answer for some MBEs. For example, some Alaska Native Corporations with considerable financial resources have partnered with MBEs as a way of diversifying their business portfolios and reducing long-term risk of over-reliance on a primary industry. These strategic alliances have benefited the ANC and the MBE.
- **Market reach:** Sometimes, the MBE will have trouble connecting effectively with the global value chain. In such cases, the value the MBE creates cannot be realized by working alone. Many global corporations need to source from low-cost countries, but lack the cultural knowledge, language, and networks to vet suppliers. Others want to sell in foreign markets, but don't know how to tailor offerings to the market, establish distribution-channel relationships, or navigate the foreign country's unique importing processes. In such cases, MBEs with cultural affinities to target markets can be

⁴ For more information on the process of innovation see Chris Trimble, *The Sophisticated Innovator. Practical Insights from Provocative Stories of Innovation in Minority Business Enterprises*. Prepared in collaboration with the Minority Business Development Agency (2007).

important allies to the global corporation, resulting in mutual benefit.⁵ Many MBEs have an affinity for doing business outside the United States. For example, the 2002 Census data show that MBEs were twice as likely as majority-owned companies to generate ten percent of their sales through exports.⁶ These natural advantages of MBEs also pertain to domestic emerging markets, and the advantages grow in magnitude as demographic changes transform what used to be thought of as “ethnic” markets into mainstream market segments.⁷ Latinos are an increasingly prominent example of a domestic emerging market.⁸

It should be evident from the foregoing analysis that strategic choices about where the MBE should be positioned in the value chain involve two considerations—how attractive is the customer and how well can the MBE serve the customer’s needs. Exhibit 2 shows different categories of customers arrayed on these two axes.

- **Cash Cows:** Customers that are easy to serve but not particularly attractive have a place in most MBE portfolios. The term “cash cow” suggests that these customers can be “milked” to provide a reliable cash-flow stream. It is strategically sound for MBEs to have enough repeat business from cash cows to cover all their fixed costs.
- **Time-Wasters:** These are unattractive customers that the MBE cannot serve effectively. So why even bother mentioning them? Because MBEs that are desperate for revenue sometimes respond to RFPs and other opportunities just because these represent a revenue stream. The problem is that time is a scarce resource for minority entrepreneurs. The probability of the bid being successful is low, because the MBE’s capabilities are insufficient and are likely to be recognized as such by the customer. And if the bid is successful, management will expend an enormous effort trying to deliver on a contract that should never have been pursued. Either way, the time spent on such dead-end proposals is time that can’t be spent building the business in positive ways. In economic terms, the opportunity cost of responding to these potential contracts is too high.
- **Reputation Destroyers:** Suppose a minority entrepreneur is a persuasive enough salesperson to be able to convince an attractive customer to issue a contract. If the MBE is incapable of delivering on the contract, the customer will remember the performance deficit and be wary of dealing with this MBE in the future. Supplier diversity professionals discuss good and bad contract experiences with their peers,

⁵ John Owens and Robert Pazornik, *Minority Business Enterprises in the Global Economy: The Business Case*. Prepared in collaboration with the Minority Business Development Agency (2003).

⁶ U.S. Department of Commerce, Minority Business Development Agency, *Characteristics of Minority Businesses and Entrepreneurs: An Analysis of the 2002 Survey of Business Owners* (2008).

⁷ The minority population represented more than a third of the U.S. population in 2007 based on annual population estimates released by the U.S. Census Bureau in May 2008. Minorities will continue to increase as a proportion of the U.S. population and will become the majority by mid-century.

⁸ Hispanics represented 15 percent of the U.S. population in 2007 based on annual estimates released by the U.S. Census Bureau in May 2008. Hispanic purchasing power was estimated at \$862 billion in 2007 and it is expected to increase to \$1.2 trillion by 2012 according to the Selig Center for Economic Growth, Terry College of Business, The University of Georgia, May 2007.

spreading the MBE's reputation damage to other potential customers. Worse still, people in the customer's organization may draw the broader conclusion that supplier diversity initiatives create problems, and are to be avoided. When this happens, the reputation damage is much wider in impact, creating or reinforcing a stereotype that can negatively affect all minority businesses.

- **Success Stories:** These are highly attractive customers that the MBE can effectively serve. The obvious question is, why not just concentrate on these customers? Why pay any attention to cash cows at all? The answer is that customers that are highly attractive to an MBE are usually highly attractive to every other potential supplier. This results in severe competition with subsequent downward price pressure and erosion of profit margins. So Success Stories tend to be transitory opportunities for the MBE: it is therefore wise to create a broad customer portfolio and a dynamic business development strategy. *As a rule of thumb, an MBE is accepting too much risk when any one customer accounts for more than 30 percent of revenue, no matter how attractive the customer may seem.*
- **Aspirational Opportunities:** Some moderately attractive customers can be served well if the MBE pays very close attention to performance on the contract. The managerial time demands would be high, and employees would have to be on a steep learning curve. This situation requires both management and workers to put in extra effort to avoid contract failure. Again, this consideration has implications for the customer portfolio: too many aspirational opportunities will exhaust the entrepreneur and his or her work force: a continual stream of them can burn everyone out, leaving the MBE longing for easy-to-handle cash cows.

Appropriate strategic alliances can increase the MBE's capabilities—by broadening core competencies, increasing capacity, and providing increased value to customers—and thereby make the MBE more appealing to targeted customers. In effect, well-chosen and well-managed strategic alliances can move the MBE upwards and to the right on the Customer-Capabilities Matrix shown in Exhibit 2. And because of the expanded capabilities, opportunities that were Time-Wasters and Reputation-Destroyers for the MBE doing business alone can become viable contract opportunities for the strategic alliance. Likewise, Aspirational Opportunities can be taken on with less of a challenge. And the appropriately-partnered MBE can compete more effectively to capture Success Story business.

THE MBE’S GROWTH STRATEGY

High growth *potential* does not always result in high growth—certainly, not sustainable high-profit growth. Any lucrative opportunity is likely to attract stiff competition. MBEs tend to see other MBEs as their main competition, but in reality, if there’s money to be made, any business that can provide similar services or products is a potential competitor. Furthermore, the more growth and profit potential, the more the MBE has to worry about its own suppliers and customers trying to take over the MBE’s space in the value chain.

This raises the question of how can the MBE use the power of strategic relationships to grow to scale and make money while countering competitive threats. Exhibit 3 shows that the high-growth potential MBE can consider various options for growth.

Exhibit 3: Options for Growing MBE Business Volume

		Customer/Market Segments	
		Current	New
Services/Products	Current	1. Customer Penetration	2. Market Penetration
	New	3. New “Product” Development	4. Diversification

Customer Penetration: The easiest pathway is to simply sell more of the same services or products to existing customers. For example, the MBE with a strong success record might go from being one of five suppliers to becoming sole-source provider. In some cases, a strategic alliance is not needed to accomplish this. In other cases, a strategic partner will be an asset in increasing the MBE’s “share of customer;” for example:

- The customer may prefer the MBE to have backup capacity (what if there were a fire, a strike, or a sudden bankruptcy at the MBE’s facilities?).
- A partner may have cash to finance the expansion of payroll, work-in-process inventory, or physical facilities.

- When time-to-market is a critical issue, a partner may allow the MBE to meet short-term delivery deadlines while scaling up operations.
- A partner might have innovations that would keep the MBE at the cutting edge.

The form of this strategic alliance will depend on the longevity of the business arrangement and the degree of interdependence the partnering organizations will need to have (the various forms of alliance are discussed in detail in the next section of the paper).

Market penetration is the next-best option: the MBE sells the same services or products to new customers, or sells them in new market segments. In such cases, strategic alliances may be very helpful. If the partner already has an established supply relationship with customers that are new to the MBE, it will be easier for the MBE to obtain contracts and adapt to the customer's way of doing business (the learning process is accelerated when working alongside an experienced partner). The partner may also be able to gain access to new market segments it could not penetrate without the MBE's contribution. For example:

- An established African-American business may find it easier to sell to Latino customers if partnered with a Latino-owned company that understands how to tailor offerings to that consumer group.
- An Asian-American company may find it easier to sell to the Department of Defense if partnered with an Alaska Native Corporation that already has 8(a) certification.
- A Native American business may find it easier to sell its products in Mexico if partnered with a Mexican-American owned company that understands the export processes and subtleties.

The appropriate strategic alliance form in this scenario may involve anything from a simple contract (for example, "sub-contracting") to a formal joint venture.

New "Product" Development: Developing new products and services is more challenging (people often refer to services as "products"—such as "an insurance product"—so we will use that encompassing vocabulary here). Due to the MBE's inexperience in this line of business managers and employees are starting at the bottom of the learning curve, hence the term "development." On the other hand, by selling to existing customers, the MBE can benefit from having established business relationships. Examples of when it's advantageous to partner with a business that has experience in manufacturing the product or delivering the service could be that the partner:

- is high up on the learning curve.
- owns the intellectual property that would create a product-line extension.
- has the capacity to supply the new service or product at the required scale.

Again, the strategic alliance may be a transitional arrangement, such as a mentor-protégé agreement, that fosters the progress of the MBE during development of the new line of business.

Diversification: The greatest challenge is to offer new products or services to new customers or market segments. It's a journey into the unknown. The strategic ally might provide any of the benefits previously discussed, but may simply be a risk-sharing partner. This is an important consideration because while the fourth quadrant may offer the greatest rewards, it tends to embody the greatest risk. It's wise for the MBE not to "bet the farm" if there's a safer alternative.

STRATEGIC BUSINESS RELATIONSHIPS

MBEs can choose from the array of alternative business relationships shown in Exhibit 4. The appropriate choice would take into account the strategic objective, the risks, and the degree of control sought. The options are listed from the simplest arrangement to the most complex. Each is explained briefly, and then illustrated with an MBE example.

Exhibit 4: Options for MBE Business Relationships

BUSINESS ARRANGEMENT	DEGREE OF COMPLEXITY
Simple contract	Simplest
Open-ended contract	
Joint contract	
Mentor-protégé relationship	
Supplier development relationship	
Strategic partnership	
Joint venture	
Acquisition	Most complex

Simple Contract: This basic transaction occurs when a business offer is accepted, and something of value is exchanged. A contract is specific about what is expected of each party. It does not obligate the businesses to any future deals. Simple contracts can be used to replace trust in a vendor-buyer relationship, to impose penalties for disappointing performance, or sometimes to communicate unambiguously what has been agreed to. When companies issue an RFP, for example, it is usually for a specific supply arrangement. By responding, the MBE makes a commitment to comply with the terms of the RFP, and can subsequently be sued for non-compliance.

For example, Wells Technology of Bemidji, Minnesota is a Native American-owned manufacturer of over 12,000 precision metal products for the aerospace and medical industries, as well as a distributor of over 250,000 industrial supplies through vendor-

managed inventory and integrated supply arrangements. The nature of this business favors simple contracts, and Wells Technology processes about 600 simple contracts a year in its manufacturing business. Nevertheless, owner Andy Wells had learned that securing these contracts was not simply a matter of presenting the most attractive bid in response to an RFP; customers valued long-term relationships based on integrity in business and delivering more than the customer expected.

In long-term relationships, the simple contract may simply formalize the current transaction. But it also can serve to document a strategic business relationship, such as when outsourcing to a partnered organization involves sub-contracting.

Open-Ended Contract: This arrangement is specific about the terms on which the companies will do business, but perhaps not specific about how much business will be done or when. It can represent more or less of a commitment to do business; the range of possibilities includes licensing or franchise agreements, or contracts to produce goods under private label. A sole-source open-ended contract commits the buyer to deal only with the supplier. An exclusive open-ended contract guarantees that other customers will not receive goods and services from this supplier. Whatever the specifics, there may be little to the relationship beyond what is required in the contract.

Annette Taddeo is founder and CEO of LanguageSpeak, a South Florida-based comprehensive language services company. She primarily uses three-year open-ended contracts to provide translations, conference interpretation and private tutoring in over 100 languages. Most of LanguageSpeak's customers are global businesses that represent repeat business, but the need for particular services varies over time. The open-ended contract establishes a long-term working relationship between Taddeo and her clients, specifying little more than the rates at which services will be provided. The volume of business may be zero in a particular month, or it may represent a challenging workload for the business. Taddeo uses the same open-ended contract form to establish the relationship with her professional translators, who translate into their native tongues. She screens the translators for quality, trains them to work to LanguageSpeak's standards, then uses the open-ended contract to establish the terms on which they will provide their services when needed. It would be hard to run this type of a service business on any other basis.

Joint Contract: A company can contract with two or more other entities to supply services or goods. The suppliers' relationship is usually one we would characterize as a strategic alliance. It could be that the two suppliers are working together very closely and the contract has the primary purpose of communicating what the client expects of them. But it could also be essentially a separate contract with each of them, with the client managing the vendor-supplier relationship and thereby insulating its business from possible relationship problems between the two suppliers.

A novel and creative example of the use of a joint contract involves the construction activity of the Barnes-Jewish St. Peter's Hospital in St. Louis (BJC Health Care). Like many U.S. cities, St. Louis has a shortage of minority contractors of sufficient scale to take on major construction projects, despite the large volume of construction activity in the private as well as the public sector. The St. Louis Minority Business Council (SLMBC), affiliated with MBDA, has worked hard to build minority capacity, and found a strong ally in Steve Cockerham, Vice President of BJC. Not only did BJC insist on minority involvement in its ongoing construction projects, the hospital contracts *jointly* with a team of construction service providers that includes minority firms. The novel incentive structure of the joint contract encourages team members to collaborate to drive out costs, exceed deadlines, and build team members' capacity; as a result, the MBE's success benefits all the other participating construction firms and BJC. The concept was introduced at the recent St. Louis Minority Business Council Construction Opportunity Summit. It is an effective approach because the contracting mechanism shapes the business relationship between the parties, fostering both customer value and supplier development. With the support of the SLMBC this concept will be leveraged throughout the St Louis Business Community.

Mentor-protégé relationship: People acquire wisdom with age, usually as a result of trial and error. A personal mentor can accelerate the learning process, be a sounding board for ideas, and give the protégé access to the mentor's network. Minority business enterprises likewise typically have limited know-how in their early years, a phenomenon known to organizational scholars as "the liability of newness." Established companies can be more or less helpful in getting fledgling enterprises through the challenges of their early years. At the less-helpful extreme, large corporations assign a middle manager to "talk to the MBE" so that the company can check off a box required for contract compliance. At the most-helpful extreme, the MBE is coached to succeed by experienced people who want to "give back," and who can provide meaningful guidance because they understand the MBE's business.

IBM, for example, with its 109-year commitment to diversity, has been a pioneer in ensuring the impact of mentor-protégé relationships—by assigning a manager to oversee the program, recruiting high-level managers as mentors, organizing strategic retreats where mentors and protégés can learn and refine strategy together, and devoting a significant budget to ensure the success of this endeavor. Furthermore, because IBM is a truly global company, its mentor-protégé program is specifically geared toward helping protégé companies be successful global suppliers.

IBM made a significant investment in fostering the success and growth of Artech Information Systems, LLC, founded and run by Ranjini Poddar. Based in Cedar Knolls, New Jersey, Artech provides IT staff augmentation and consulting, project management, and business process outsourcing services for an extensive commercial and government client base. Even though corporate self-interest was not the primary motive for investing resources in its mentor-protégé program, IBM benefited directly from this strategic relationship: IBM gained a world-class MBE/WBE supplier as Ranjini Poddar and her top management team honed their

business acumen. But Artech benefited even more: with major operations in the USA, India, and China, Artech is a tier-1 vendor and preferred supplier to over 30 Fortune 500 companies.

Supplier development relationship: The nature of competition has changed. Only a few decades ago, the primary competition was between large, vertically-integrated companies vying for share of stable domestic markets; today, competition is between rival value chains struggling for share of rapidly-evolving global markets. With the trend away from vertical integration and toward outsourcing, competitive advantage (and disadvantage) can arise from various points in the value chain, so the strength of the value chain really matters. It's therefore important to global businesses that minority suppliers develop into strong value chain partners.

A good example of a supplier development relationship is the capacity-building of minority construction firms that Clark Construction has undertaken in collaboration with MBDA and the Tuck School. Clark opens up its own training programs to minority suppliers, organizes a tailored program to teach minority contractors how to run their businesses, and gives them opportunities where they can succeed. Clark gains competitive advantage by strengthening its supply chain.

More specifically, in response to the lack of development programs for small businesses in the construction industry, Clark developed the Local, Small, and Disadvantaged Business Enterprise (LSDBE) Strategic Partnership Program. Led by Vice President Wesley Stith, the initiative is an intensive 10-month capacity-development program designed to supplement the capabilities of LSDBE businesses in the Washington, DC metropolitan area—where minority-owned construction businesses of scale are almost nonexistent. The program is structured in an interactive format, with a focus on providing core construction management and business skills to its participants. Courses are taught by local industry experts and include classroom learning, team projects, as well as presentations by the students. The program has made a difference in the minority business community. For example, before Titus LLC—an African-American owned 8(a) electrical subcontractor—completed the LSDBE Strategic Partnership Program, they had annual revenue of \$300,000. Upon their successful completion of the program, Titus is projecting revenues approaching \$3 million. Titus' success story is typical of the companies that have completed Clark's LSDBE program.

Strategic Partnership: Here the two or more suppliers have coordinated their strategies so that they have become either dependent on each other or else have made a binding commitment to seek business together.

Ideal Contracting is an example of the latter. This LLC is 51 percent owned by Frank Venegas, Jr., a Mexican-American entrepreneur, and 49 percent by Barton Malow, a larger privately-owned majority company with more than \$1 billion in annual sales revenue. Frank Venegas had been a successful steel contractor, but the large auto manufacturers with strong supplier diversity programs were seeking to do business with a capable minority general contractor.

The scale required for major construction projects could eventually have been achieved through organic growth, but not on a timetable that would have enabled Frank Venegas to take advantage of the opportunities in front of him. The strategic partnership with the larger firm created the scale required to take advantage of the immediate opportunities, but the partnership has endured long after these projects were completed, and led to a stream of joint business. A key ingredient of success of this partnership has been an open, candid relationship between the two owners: putting long-term partnership interest ahead of short-term self-interest has allowed the joint business to flourish.

Joint venture: A joint venture, as the term is used here, is a legally-independent business entity that is owned by the strategic allies. It operates entrepreneurially, drawing on resources as needed from the parent organizations. It is distinct from a strategic partnership in that a new organization is created for the purpose of achieving competitive advantage that neither parent organization could accomplish alone. Minority entrepreneurs can create joint ventures, but for many contract domains, they need to know how the ownership arrangement affects their minority status.

For example, Johnson Controls and a Hispanic-owned firm, SAT Auto Technologies Ltd., have created a new joint-venture operation—called Avanzar Interior Technologies—to manufacturer vehicle interiors for the Toyota Tundra truck. Avanzar is an independent business entity that has been certified by the Central & South Texas Minority Business Council as a Minority Business Enterprise. Berto Guerra, a former executive of SBC/AT&T, serves as chief executive officer of the joint-venture operation, and production began in the fall of 2006 at the Toyota campus in San Antonio, Texas. In this venture, Johnson Controls provides engineering and program management. SAT Auto Technologies provides on-site manufacturing, quality and sales support.

Acquisition: The most encompassing relationship between two companies is when one legally acquires the other. The term “merger” is sometimes used to describe this relationship in order to portray the two former companies as being equals. In practice, dual control is usually unstable, and the instability becomes resolved when one organization dominates the other. The merger between Daimler and Chrysler was a well-publicized example of this phenomenon, with the merged companies having dual CEOs for an interim period. Daimler subsequently asserted formal control and sold Chrysler. MBEs can acquire companies to quickly build their capabilities, but they need to be aware that there are management challenges to running an acquired business in addition to running one’s own on-going business.

A good example of successful acquisition is to be found in the packaging industry. Specialized Packaging group was created in 1983 by Carlton Highsmith, an African-American entrepreneur in Hamden, Connecticut. His strategic challenge was to create large enough scale and scope to serve major packaged goods manufacturers in an era of supply-base consolidation. His chosen pathway for providing greater value for customers was to acquire

existing businesses that would increase Specialized Packaging's value to customers. Acquisition, rather than partnering, provided the degree of predictability, control, and synergy that allowed him to effectively compete head to head against majority suppliers. Highsmith's strategy of acquiring the requisite scale and scope enabled him to grow sales volume from \$457,000 in 1983 to \$150,000,000—with 500 employees deployed at eight sites—in 2007.

To recap, the point of explaining the various options for business relationship is to clear up misunderstandings of what the terminology means, and to identify the implications for how the business will be run as some sort of a collaborative—and perhaps even joint—entity. Strategic alliances are business relationships formed for a purpose, and that purpose, ultimately, is to gain competitive advantage.

In the next section, we present data that shows the extent to which MBEs are engaged in various business relationships.

MBE PARTICIPATION IN STRATEGIC ALLIANCE FORMATION

To better understand the patterns of MBE strategic relationships, we conducted a small-sample survey of MBEs that are graduates of the Tuck-MBDA Partnership executive programs. All of the surveyed MBEs qualified for MBDA's Strategic Growth⁹ Initiative category: firms that had grown—or had the potential to grow—large enough to create wealth for their owners and jobs in their communities. The survey was long (13 pages) and the high respondent burden this imposed accounted for the low response rate (6.2%). The tradeoff was that the survey yielded rich data from those who did respond. The survey was supplemented by selected follow-up interviews to explore specific responses that called for further investigation. Preliminary findings of the survey are as follows.

The Sample. Our sample included 35 respondents to our survey:

- Thirteen (38%) were African-American, nine (26%) Hispanic, eight (24%) Native Americans, and four (12%) Asian-American. One respondent did not provide racial/ethnicity information.
- Twelve (36%) of the companies reported annual sales revenue of less than \$1.5 million and another 13 (40%) companies reported sales revenues between \$1.5 million and \$5 million. The remaining eight (24%) firms reported sales revenues of greater than \$5 million. Two firms did not respond to this question.
- Most of the companies (n=15; 44%) were small in terms of payroll, with ten or fewer employees. Twelve (35%) of the firms employed between 11 and 49 employees and seven (21%) had 50 or more employees. One company did not respond.
- The sample consisted of established companies, rather than recent startups. Eleven (32%) of the respondents had been operating their business five years or less. Seventeen (50%) had been in business between 5 and 15 years and six (18%) had been in business for more than 15 years. One company did not respond.

Strategic Alliance Involvement. Respondents reported a wide range of involvement in strategic alliances, categorized according to the typology shown in Exhibit 5:

- MBEs reported utilizing the simple contract most frequently, averaging 15 simple contracts per firm but ranging from 0 to more than 150 contracts. Nine firms (26%) in

⁹ The Strategic Growth Initiative resulted from analyses conducted by Heywood Davenport and his staff in the MBDA New York National Enterprise Center. See, e.g., U.S. Department of Commerce, Minority Business Development Agency. *Accelerating Job Creation and Economic Productivity: Expanding Financing Opportunities for Minority Businesses*. (2004).

the sample reported no simple contracts and 25 (71%) reported having more than one contract.

- Open-ended contracts were utilized to a lesser degree. MBEs reported an average of 2.77 open-ended contracts. The sample was split with 16 (45%) indicating they had more than one open-ended contract and 19 firms (54%) reporting no open-ended contracts.
- Joint contracts were used even less with 11 respondents (31%) reporting one or more.
- Mentoring and supplier-development relationships were also rare, with 10 (29%) and nine (26%) of the responding firms reporting such arrangements.
- Some MBEs were engaged in strategic partnerships, with nine firms (26%) reporting one partnership and five (14%) reporting more than one.
- Eleven (31%) of the responding firms were engaged in joint ventures.
- And only one of the MBEs (3%) had acquired—or been acquired by—another company.

Exhibit 5: Overall Findings of MBE Business Relationships

Business Relationship Type	Overall Statistics				Number (Percentage)		
	Average	Standard Deviation	Minimum	Maximum	Reporting none	Reporting one	Reporting more than one
Simple Contract	15.34	31.52	0	150	9 (26%)	1 (3%)	25 (71%)
Open-ended Contract	2.77	3.94	0	15	19 (54%)	0 (0%)	16 (43%)
Joint Contract	0.49	0.82	0	3	24 (69%)	6 (17%)	5 (14%)
Mentor-Protégé Relationship	0.43	0.88	0	4	25 (71%)	8 (23%)	2 (6%)
Supplier-Development Relationship	0.34	0.64	0	2	26 (74%)	6 (17%)	3 (9%)
Strategic Partnership	1.71	5.97	0	35	21 (60%)	9 (26%)	5 (14%)
Joint Venture	0.49	0.85	0	3	24 (69%)	7 (20%)	4 (11%)
Acquisition	0.03	0.17	0	1	34 (97%)	1 (3%)	(0) 0%
N=35							

The data show that MBEs tend to favor simple business relationships: the more complex the relationship, the fewer MBEs chose that form of strategic alliance. But a further analysis of the data revealed that choice of alliance form was likely to be affected by the size of the business.

Specifically, correlation data show that the number of employees that a firm has is related to their choices of strategic alliance. Having a mentor and being in a supplier-development relationship was associated with having more employees ($r = 0.52, p < .001$ and $r = 0.42, p < .01$, respectively). Firms with more employees reported greater numbers of simple contracts ($r=0.35, p < .05$), strategic partnerships ($r=0.64, p < .0001$) and joint ventures ($r=0.40, p < .05$).

The exhibits presented below make the patterns in the data easier to visualize.

Annual Sales Revenue and Contract Portfolio

We found that the size of the company, defined in terms of annual sales revenue, affected the use of different types of business relationships. Exhibit 6 shows the average numbers of contracts reported by MBEs as a function of company size—defined by annual sales volume.

Exhibit 6: Size of Company and Contract Portfolio

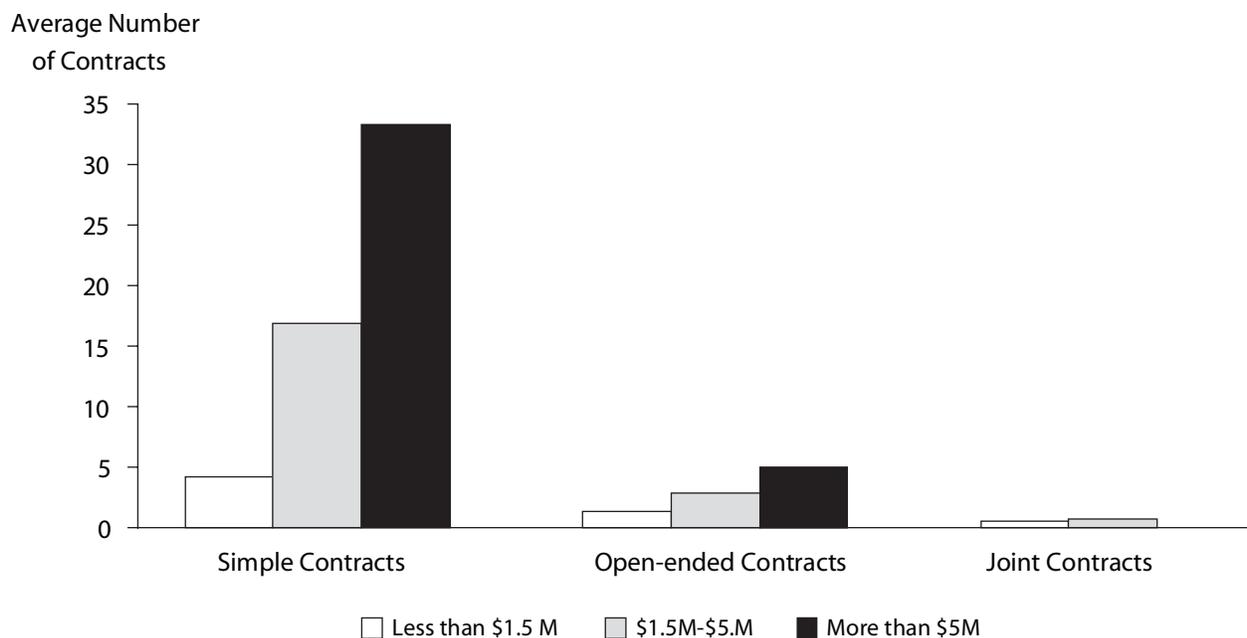


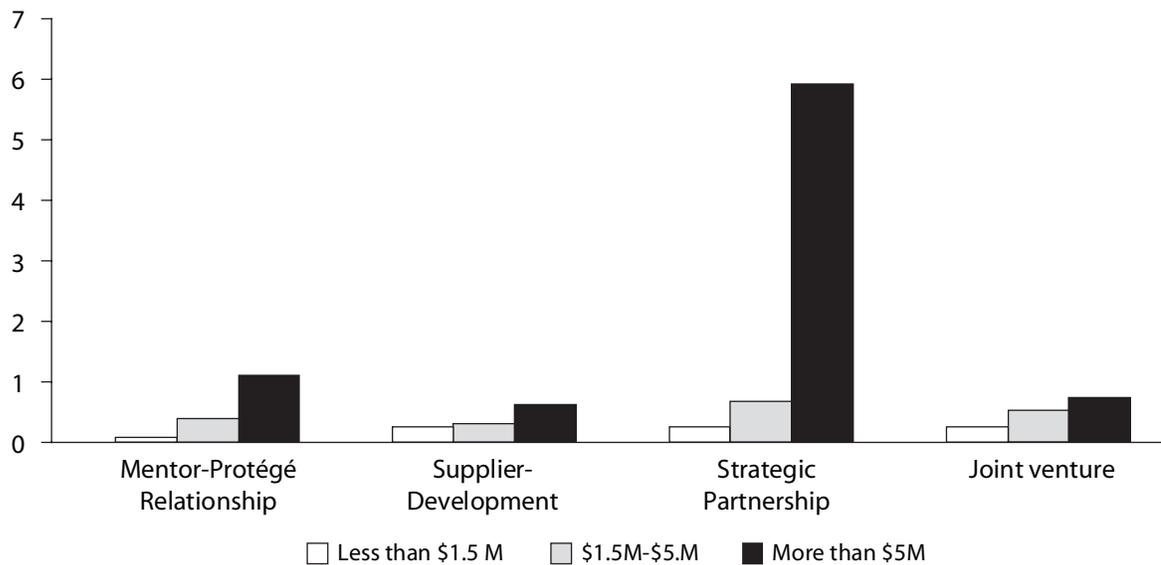
Exhibit 6 shows that MBEs with annual sales of more than \$5 million have greater numbers of simple and open-ended contracts than companies reporting lower sales. In addition, larger companies have a more sophisticated mix of contracts—which is desirable in terms of having a diversified portfolio of business arrangements.

Annual Sales Revenue and Complexity of Business Relationships

We also find that annual sales revenue is related to the types of relationships that MBEs make with other businesses. Exhibit 7 shows the average number of relationships that companies report by MBE revenue category.

Exhibit 7: Annual Sales Revenue and Complexity of Business Relationships

Average Number
of Relationships



MBE size does make a difference. In general, we see that companies reporting more than \$5 million in annual sales revenue tended to have more mentoring relationships, supplier-developer relationships, strategic partnerships, and joint ventures than did smaller companies.

In analyzing the data, we suspected that businesses with larger annual sales revenue would tend to have been in business longer, and would have a larger payroll. This raised the possibility of alternative explanations of the relationship we are seeing in Exhibit 7 between total sales volume and engagement in strategic alliances. So we did further analysis to find out whether annual revenue had an effect on strategic alliance formation independent of company age and number of employees.

We found that the relationship between strategic alliance use and annual revenue was evident even when we statistically controlled for company age and number of employees. For simple and open-ended contracts, firms with more than \$5 million in sales revenue reported the greatest number of contracts, followed by firms with sales revenues between \$1.5 million and \$5 million. A different pattern emerged for joint contracts: firms reporting revenues greater than \$5 million had fewer joint contracts than the other revenue categories.

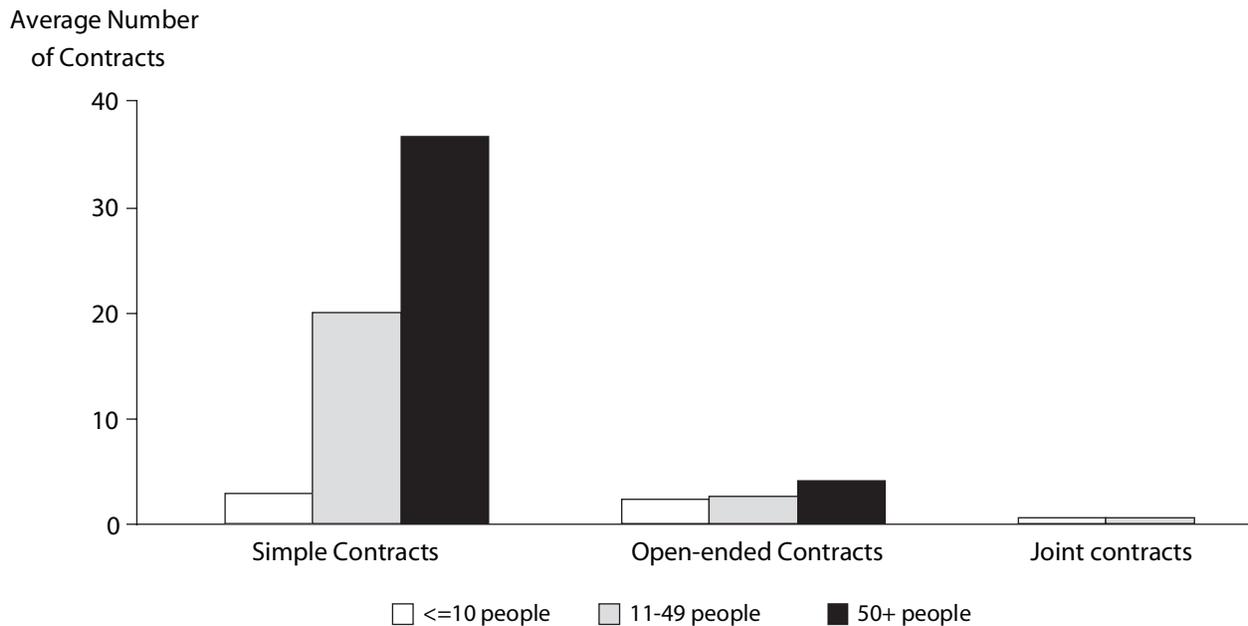
We found similar patterns when we examined firm revenue and strategic relationships while statistically controlling for number of employees and firm age. Firms reporting greater revenues also had more mentor-protégé relationships. But surprisingly, firms with more than \$5 million in sales revenue reported fewer supplier-developer relationships and joint ventures than their counterparts with lower sales revenue.

Number of Employees and Contract Portfolio

An alternative index of size is number of employees. Alternative measures are called for because the appropriate measure of MBE size depends on the industry. In a labor-intensive business, for example, number of employees on the payroll is less an indicator of business size than it would be in a capital-intensive business. Similarly, a realtor or brokerage with \$10 million in sales would be considered small, whereas the same sales volume in an arts and crafts operation would probably be considered large-scale. For this reason, we repeated the statistical analysis using number of employees to measure size of the business

We found that companies with greater numbers of employees report using more simple and open-ended contracts, whereas the number of employees and use of joint contracts do not appear to be related.

Exhibit 8: Number of Employees and Contract Portfolio

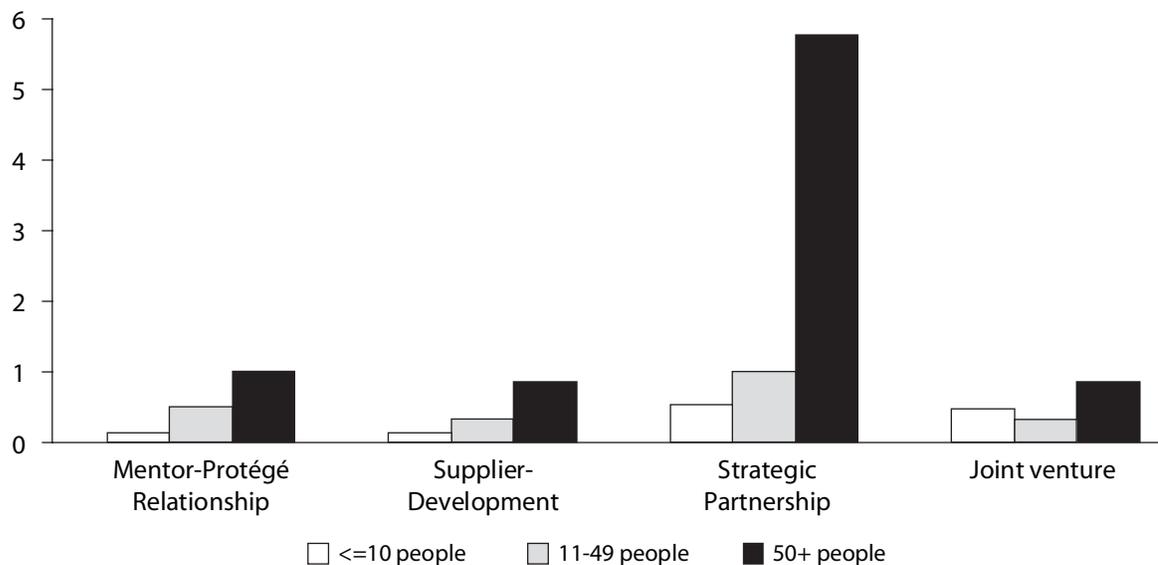


Number of Employees and Complexity of Business Relationships

We also find that MBEs with a larger number employees report having a broader range of business relationships. With the exception of joint ventures (the exception to the pattern being attributable to small sample size; anecdotal evidence suggests that the pattern holds for joint ventures, too), we find that as the number of employees in the firm increases, the number of relationships increase.

Exhibit 9: Number of Employees and Complexity of Business Relationships

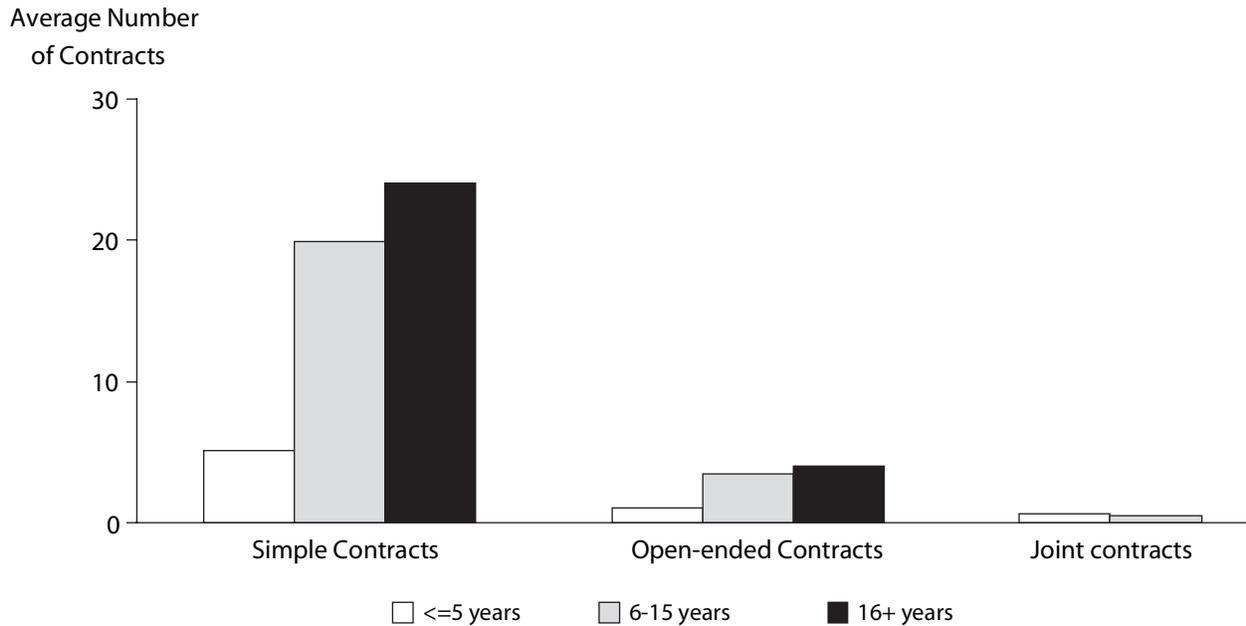
Average Number of Relationships



Age of Company and Contract Portfolio

We examined the relationship between the number of years that the company had been in business and the types of contracts they utilized. As expected, the firms that were in business longer tended to report using more simple and open-ended contracts. Very few companies in the sample reported using joint contracts.

Exhibit 10: Age of Company and Contract Portfolio



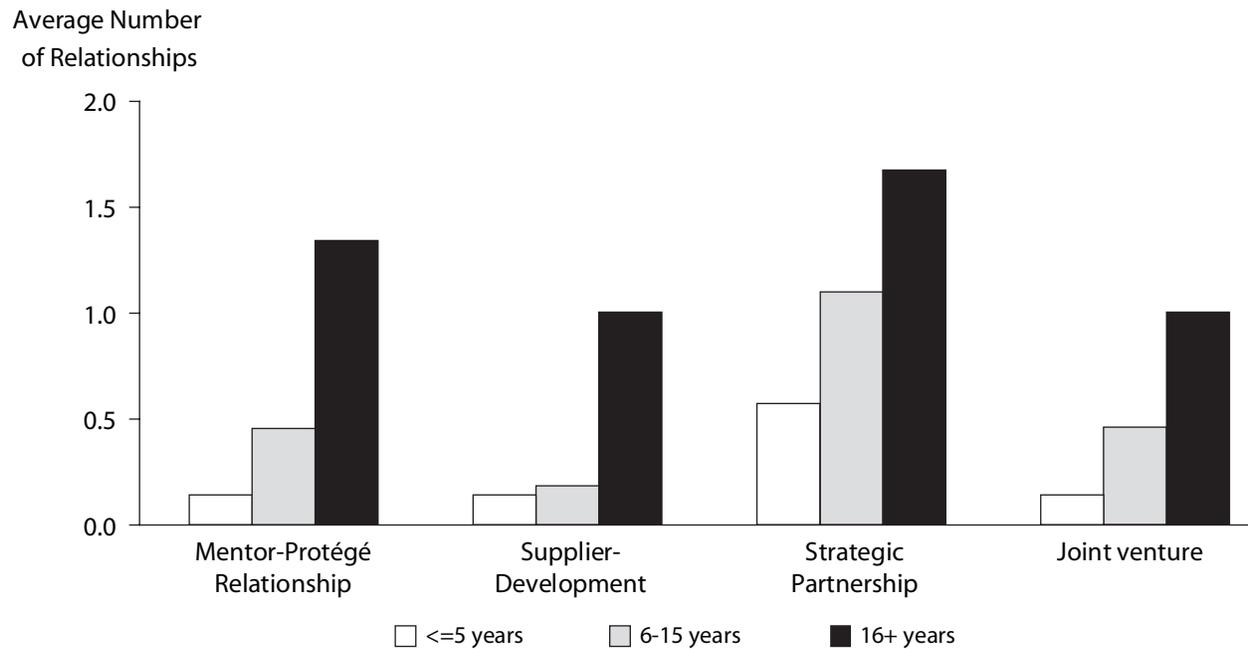
Age of Company and Complexity of Business Relationships

An insightful analysis by Andrew Bernard and Matthew Slaughter¹⁰ focused attention on the life cycles of minority business enterprises. That study led us to understand that the choices minority owners and key executives make is influenced by stage in the life cycle. The data presented in this paper support their point of view. While we were not able to categorize life cycle stage from respondent data, firm age is a reasonable proxy for life cycle stage, from youth to maturity.

Exhibit 11 confirms that involvement in the more-complex business relationships is a function of MBE age. This may be caused by potential strategic partners being hesitant to tie their economic fortunes to a young, as-yet unproven MBE, or it may be caused by minority business owners having their hands full keeping the business economically viable in its early years. Whatever the reason, the more-sophisticated forms of business relationships seem to come with business maturity.

¹⁰ Andrew B. Bernard & Matthew J. Slaughter. *The Life Cycle of a Minority-Owned Business: Implications for the American Economy*. Prepared in collaboration with the Minority Business Development Agency (2004).

Exhibit 11: Age of Company and Complexity of Business Relationships

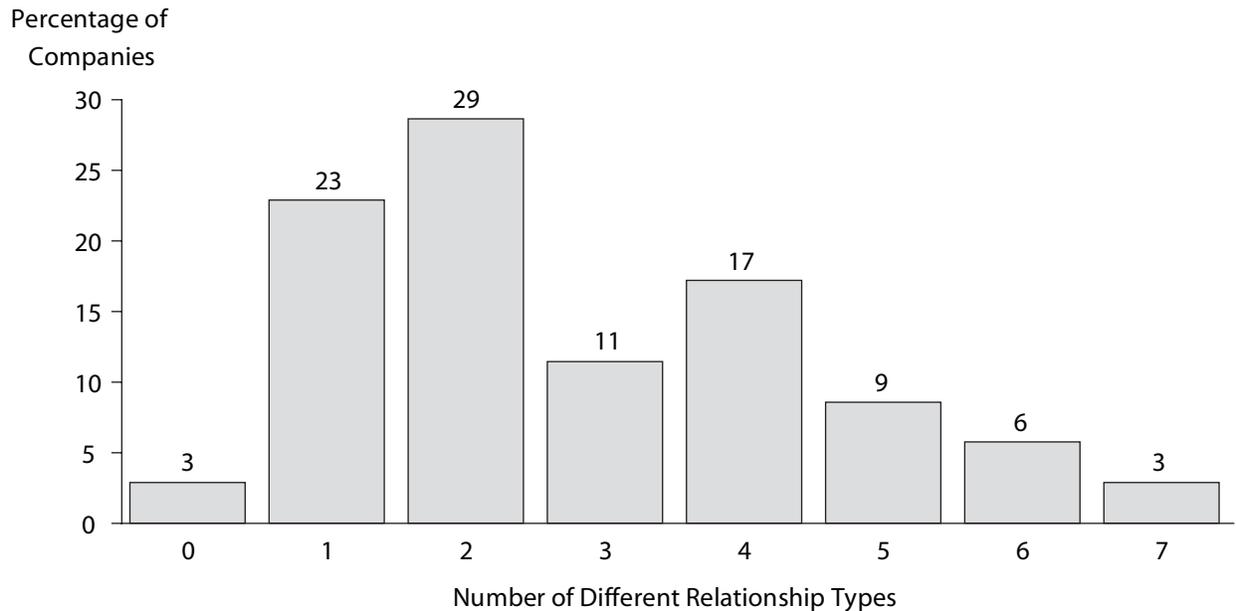


Diversification of Business Relationship Portfolio

A minority business enterprise is more robust—able to survive the ups and downs of dynamic markets, evolving industries, and a shifting competitive landscape—when it does not have “all its eggs in one basket.” This is true in terms of customer mix, product portfolio, service line, and sectors served. It is also true in terms of the breadth of its set of business relationships. Over time, we would expect MBEs with a broad range of business relationships to fare better than MBEs that became over-reliant on a narrower set.

To shed light on the breadth of business relationships our MBEs were involved in, we summed the number of different forms of business relationships reported by the companies in our sample and created an aggregate measure that represents the diversification of the business relationship portfolios.

Exhibit 12 shows the results, indicating less overall diversification than would be preferable for sustainable prosperity and growth in a dynamic business context. About 19 (55%) respondents surveyed indicated that they had two or less different types of relationships.

Exhibit 12: Diversification of Business Relationship Portfolios

The number of different contracts and relationships was moderately associated with firm size. Companies with more employees tended to report having greater numbers of relationship types ($r=0.30$, $p < .10$).

In summary, a broader set of business relationships, provided they are appropriate to the industry, is generally better than a narrower set, simply because a broad portfolio dilutes risk.

CONCLUSIONS

This study generates several conclusions about how the use of strategic relationships can impact the long-term business success of MBEs.

- MBEs must understand their value chain, how they fit into it, and where are the opportunities for growth and profitability before they consider the kind of strategic relationship that best addresses their needs.
- Usually, the highest profit potential for the MBE occurs when the outsourcing involves an indispensable value-chain role that the corporation cannot perform efficiently or effectively. If the MBE chooses a peripheral role, or a role that any other supplier can easily take, profit potential may be low and continuity of business risky.
- MBEs need to be proactive, not reactive. They must make a thoughtful, strategic choice as to where they best fit into their value chains, rather than settling for whatever business is offered through supplier diversity programs.
- Once a clear, credible, and customer-relevant value proposition has been articulated, the next step is to assess whether the MBE has the capability—the core competencies, the capacity, the reach, and an appropriate operating strategy—to serve the customer well.
- Appropriate strategic alliances can increase the MBE's capabilities—by broadening core competencies, increasing capacity, and providing increased value to customers—and thereby make the MBE more appealing to targeted customers.

The appropriate strategic relationship will take into account the strategic objective, risks, and degree of control desired. Strategic relationships range in complexity from simple contract and open-ended contracts to joint ventures and acquisitions. Although no relationship is intrinsically better than any other one, there is a most-appropriate relationship which would best achieve the MBE's business goals in the long-term. Determining, creating, and managing that chosen business relationship has great strategic importance for the MBE.

Preliminary data from a survey of MBEs indicated that MBEs are participating in the full spectrum of strategic relationships, however they are most likely to enter into simple contracts. In addition, the number, complexity and diversity of these relationships is

correlated with the firm's size and age. It appears that with experience, MBEs gravitate toward a portfolio of business relationships aligned with their strategy.

The community that supports MBEs—educators, advocates, and service-providers—can accelerate minority executives' learning. We must continue to educate MBEs about the benefits of strategic alliances in gaining competitive advantage, particularly in an increasingly competitive and dynamic global economy.

IMPLICATIONS FOR PRACTICE

Today, the United States operates in a global economy. In the face of formidable competition from rival economies—particularly China and India—U.S. national competitive advantage has become more important than at any time in the nation’s history. In this context, the United States cannot afford to have sectors of the economy making less of a contribution than they should be capable of making. Thus, it is vitally important that minority businesses survive, prosper and grow to scale. Their historical under-participation in the U.S. economic system has resulted in lost opportunity—to boost gross domestic product, energize the entrepreneurial growth engine, and develop human capital. As minorities grow in proportion to the U.S. population, soon to become the majority of the entrepreneurial economy as well as the workforce, ensuring their economic success is a national priority.¹¹

A number of initiatives have been undertaken to foster MBEs’ economic progress. In recent decades, corporate supplier diversity programs and public sector agencies focused on causal explanations in terms of easily-administered solutions—access to contracts and access to capital. But research conducted by the Tuck School of Business at Dartmouth on hundreds of MBEs revealed that the causes of underperformance were much more likely to be attributable to internal factors—the adequacy of the MBEs’ strategies, their customer responsiveness, their strategy implementation efforts, and their operations—rather than external factors.

Our experience at the Tuck School in helping minority businesses succeed—supported by the data reported here—suggests that MBEs do not give enough attention to the strategic advantage that can come from optimizing business relationships. If this is a valid observation, it is understandable, for two reasons. First, until they get to be large-scale enterprises, MBEs are run by entrepreneurs, and the entrepreneurial personality is likely to be more attuned to self-reliance than to the possibilities that arise from a network of business relationships. Second, our conceptual frameworks in economics and management were developed shortly after the industrial revolution, at a time when businesses were largely self-contained. But the businesses that dominate the global economy today are seldom vertically-integrated, largely self-sufficient enterprises: they are more likely to be integrators of value-creation by network partners—the suppliers and customers within their value chains, strategic allies, and various global associates. The success of these global corporations largely depends on the competitive advantage that arises from the business relationships they form and manage.¹²

¹¹ Greenhalgh, Leonard, with Michael Bolger. *A Different Future for Minorities in the U.S. Economy*. (Hanover, NH: Tuck School of Business at Dartmouth, 2006).

¹² Leonard Greenhalgh. *Managing Strategic Relationships: The Key to Business Success*. (New York: Free Press, 2001).

To appreciate the importance of decentralized value chains in the modern economy, consider that two thirds of the value of a modern automobile is not created by the manufacturer, it is outsourced; and in pharmaceutical development, the value created by outsourcing can exceed 90 percent.

The MBE Support System

MBEs need to be major players in today's and tomorrow's economy. Their full participation will require them to become effective in marshalling and managing strategic business relationships, many of them global in scope. The support system we currently have in place does not seem up to the challenge. Here are some things that will need to change:

Education needs to be up-to-date, and available to all the MBEs that can benefit from intensive learning experiences. The pace of transformation of the business environment is accelerating, but many schools teach what was relevant to yesterday's business system. As a result, many educators tend to teach entrepreneurs to run their businesses as self-contained economic enterprises, emphasizing inputs, throughputs and outputs—whether these stocks and flows involve cash, inventory, personnel, capital, or intellectual property. But in reality, businesses are not self-contained units: they are situated in a context, of which they are an integral component—a value chain, a dynamic competitive environment, a global economy, and a local culture. Thus it is important that educators stress the network of relationships that the MBE will need to cultivate, manage, and, at times, terminate.

The extent of coverage is going to be more of a challenge. Despite the increasing number of minority businesses, only a tiny fraction of U.S. business schools have offerings tailored to this audience. There are currently more than 4 million MBEs in this country, and the Tuck School—the nation's largest provider of intensive learning experiences—is able to touch the lives of less than a thousand minority owners and executives each year. Nationally, less than one per cent of MBEs are getting the educational input they need to operate in the modern globalized economy.

Service providers likewise serve only a small fraction of the MBE population, and need to broaden their focus beyond certification, access to contracts, and access to capital to include fostering relationship-building. In the past, minorities have been excluded from some relationships, and catching-up can be accelerated by networking events.¹³ Furthermore, many entrepreneurs are highly competitive, and while competition has its place in a capitalistic system, it sometimes is a detriment to strategic business relationships. Service providers can foster collaboration by hosting lateral as well as vertical matchmaking events.

Supplier diversity programs, and the professionals that operate them, can achieve better results if they focus on impact rather than expenditure. For example, even a billion dollars in

¹³ MBDA deserves credit for giving as much emphasis to networking in its events as the agency gives to access to capital, access to contracts, and access to education.

minority spend will have a low net impact if it involves low-margin business at the edges of value chains, allowing “minority-owned front-companies” to subcontract to majority-owned businesses, and such indirect activity as sponsorship of the proverbial golf outings or power breakfasts. *Minority spend does not equal minority impact.* For example, greater impact could be achieved with a fraction of those billion dollars if it involved fully developing a high-potential minority supplier, giving the MBE a strategic role in the value chain, and then connecting the MBE to the major corporation’s own relationship networks.

Based on the fast growth of minorities, which now account for a third of the U.S. population, as well as the increase in number of minority businesses, it is justified to augment the investment in federal, state and local programs that support the growth and expansion of minority-owned businesses. The orientation of government programs also must change. When the federal programs were introduced, decades ago, minority businesses were considered a social issue. Today, we are realizing that MBE success is an economic imperative. MBEs *must* fully participate in the U.S. economy.

Recommendations

We need to update the way we have approached the inclusion of minority business in generating gross domestic product. The themes of Minority Enterprise Development Week in the past few years have highlighted some of the areas needing attention—globalization, innovation, growth and development throughout the life cycle, positioning in dynamic value chains, and now gaining competitive advantage through participating in strategic business relationships. But the overarching issue is that *we are approaching the MBE challenge by means of a paradigm that is seriously outdated.*

The minority development movement—from supplier diversity programs to certification to education—was developed more than a quarter of a century ago. Meanwhile, the marketplace has changed, technology has evolved, the number of MBEs has mushroomed, global competition has become intense, and we have transitioned from a manufacturing/service economy to a knowledge economy. The world has changed; our approach has not. We need a new paradigm of intervention and support.

The need for a paradigm shift becomes more urgent with each passing day. Today, minorities are not participating in the entrepreneurial economy in proportion to their numbers. That underperformance will have greater economic consequences as their presence grows steadily into becoming the majority. Thus it is in our self-interest—as well as the national interest—to ensure minority inclusion in value chains, relationship networks, and to provide minorities with the comprehensive support that will help them reach their full economic potential. *We need to help MBEs become what they are capable of becoming.*

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