

# STRATEGY, STRUCTURE AND PERFORMANCE – EMERGING ORGANIZATION STRUCTURE

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**Abstract:** Role of strategy, structure, culture, technology and environment in organizational performance, growth and success can never be disputed. Organizations have been found to change its strategies at much faster rate than changes it brings about in its organization structure. For this reason there is profound literature available for implementing strategy but very less on organization structure. Strategy-Structure-Performance (SSP) theory is reviewed from national and international research stream. SSP principles are linked to management concepts and synthesized in to explanatory framework. The paper attempts to foster better understanding to strategic decisions, organization structure and aspects related to superior performance. An iterative relation between organization strategy, structure and performance is shown; highlighting that firm’s strategy should be consistent / complementary with organization structure.

**Keywords:** Decision Making, Network Alliance, Strategic Management, Strategic-Structure Alignment, and Strategy Structure and Performance.

## INTRODUCTION

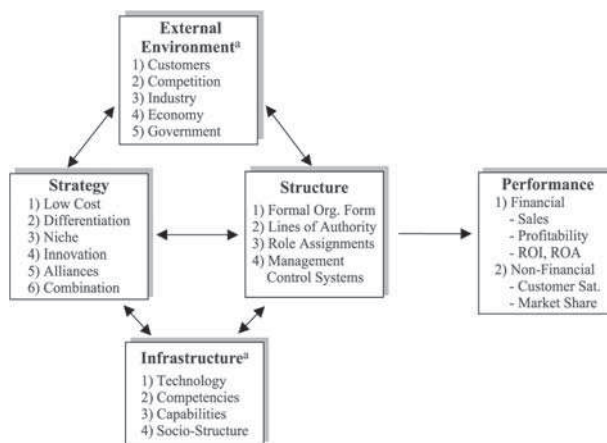
Goal of business strategy is to define how a firm can remain competitive in its chosen domain. Finally goal of functional strategy is to identify how it will utilize its functional knowledge and expertise to execute the chosen corporate and business strategy.

Apart from above, companies continues search for ways to sustain competitive advantage by investing heavily in enhanced business processes through approaches like Total Quality Management, Re-engineering etc. But these approaches do not offer competitive advantage for long as they can be duplicated quickly by competitors reducing performance advantages (Teece, 1981; Schonberger, 1982; Atkinson 1986; Bechtel and Jayaram, 1997). Significant performance enhancement can come from firms that can exhibit greater congruency and alignment amongst its strategy and execution structure consistently.

Research on strategy and structure is divided in two broad areas- One national strategy – structure relationship between general strategy elements like size, product diversity etc. & organisation structure as a whole and second strategy-structure relationship focuses from international opérations perspective. Although this démarcations now seem unnecessary as most of nations are following global integration policy. Elements of strategy include Size, Product, Competitive Strategy, Degree of Internationalization and type of international strategy. Types of organization structure include functional structure, product structure, regional structure, matrix structure, mixed structure and tensor structure.

Strategy-Structure-Performance (SSP) paradigm posits that a firm’s strategy created in its operating / external environment drives the development of organization structure and its processes (Miles and Snow, 1978; Galbraith and Nathanson, 1978). Firms with strategy – structure fit facilitates performance at desired level and those with better alignment then its competitors are expected to perform better (Miles and Snow, 1984; Galbraith and Kazanjian, 1986).

With the advent of information technology the organizations have to find new ways to organize themselves that are built around information technology and advanced information processing capabilities. In network organization, structure will dominate strategy and human resource will provide sustainable competitive advantage due to their ability to acquire, store, disseminate, analyze and initiate actions based on information’s.



Note: <sup>a</sup>Contingent factors

### Figure 1: Elements of Strategy – Structure – Performance

Source: Applying the strategy-structure-performance-paradigm to supply chain environment by C. Clifford Defee and Theodore P. Stank, *IJLM* 16, 1, pg 28 – 50. **Place Figure 1 here**

Figure 1 summarizes key concepts that have been extensively investigated in SSP literature. It shows different relationships between strategy, structure and performance and identifies factors governing strategy and structure relationship and interplay amongst them.

#### Evolving organizational structures

After industrial revolution three forms of business organization structure were prominent, each with its unique alignment with environment in which it operated.

1. Vertically integrated functional organizations were prominent during times when environment was relatively stable with minimum variations in consumer preferences. Successful firms were high volume, production oriented that provided standardized goods at low cost. Ford Model T introduced assembly based mass production system that made car affordable to common middle class earner.
2. After World War I, multi divisional form replaced functional form of organizations. Alfred Sloan of GM introduced the concept of decentralisation that helped organizations cope up with greater variety of tastes and preferences.
3. However market preferences and product technologies started changing more frequently and became more complex. Multidivisional form could not provide effective cross functional coordination needed to address these changes at market place. Matrix form of organization started gaining popularity from 1960's through 1970's that laid emphasis on lateral relationship and dual line of authority and responsibility.

Changes in business strategy and need for coordination & information processing reflects corresponding change in organization structure. This Strategy and structure relationship was first described by business historian Alfred Chandler in his review of growth and development of four large firms DuPont, General Motors, Standard Oil of New Jersey and Sears, Roebuck and company. He found that as each of these companies grew through a strategy of product diversification, they implemented a divisional form of organizational structure.

Several studies of western European and multi-national firms supported Chandler's discovery (Stopford and Wells,

1972; Channon, 1973; Dyas and Thanheiser, 1976; Franko, 1976 and Egelhoff, 1988). Rumelt (1974) research study of the financial performance of more than 200 Fortune 500 companies from 1949-1969 showed Firms diversifying into a related product line or business, showed consistently better performance than either firms diversifying into unrelated businesses or vertically integrated firms with limited diversification options. Rumelt's findings were subsequently confirmed while looking at combinations of different structural types, and using stock market return as a performance measure (Williamson, 1975; Teece, 1981; Hoskisson, 1987).

Due to change in pace of technology, opening of political and economic boundaries, improvement in technical and managerial skills and knowledge, organization needed flexible organization structure. They needed to migrate from hierarchy based structure to market driven structure which led to emergence of Network organization (Achrol, 1997). Formal network organization gave rise to strategic alliances. Alliances provide access to external knowledge but on their own they do not guarantee effective detection, assimilation and its transfer. Their successful recombination depends upon partners incentives to cooperate and share knowledge (Hamel, 1991).

Strategy must be consistent and complimentary to each other supporting shared broad network strategy. Network based strategy differs from traditional single firm strategy in the sense that it demands coordination and commitment from different firms in a network towards common strategy. Traditional single firm strategy required internal coordination to produce low cost, distinctive products and / or innovation but competitiveness in network alliance comes from external degree of coordination amongst firms. This inter-organizational relationship introduced the concept of strategic network alliance (Achrol, 1997; Varadarajan and Jayachandran, 1999).

Continuum of strategic alliances range depicted below highlights degree of removal of boundaries and extent of interactions between individuals and firms. Organizations in network are leaner, flatter and focus on their contribution in value chain. These networks are held together by mutual expectation and trust.

#### CONTINUUM

Preferred vendor—> licensing arrangement—>  
Original equipment manufacturer—> Contractual alliances—> Partnerships and Joint Ventures—>  
Boundary less working organizations.

Achrol (1997) has classified networks in to four types:

**1. Internal market network:** where units primarily of single firm are organized independently and operate as independent profit centre. Example Asea Brown Boveri organized in to independent enterprise units.

**2. Vertical market network:** where parts of activities in value chain are subcontracted example Sun Microsystems that has subcontracted chip manufacturing, distribution and service functions.

**3. Inter-market network:** where alliances cut across multi firm, multi product and multi industries in which a firm operates. Japanese keiretsu and Korean Chaebols are examples of such inter market networks.

**4. Opportunity market network:** where business firms form alliances for particular projects or business opportunity.

All of these network types are families of independent units or units of one single firm that are free to compete with each other and united in their ability to help each other.

Dess, Rasheed, McLaughin and Priem (1995) gives following continuum of network evolution:

Modular—> Virtual—> Barrier free

Modular organization subcontracts only non vital functions retaining with itself strategic control, which allows firm to focus on the areas that provide them competitive advantage. Ex. Nike, Dell.

Virtual organizations are network of companies linking suppliers, customers and competitors to share cost, market access and skill sets. Examples Paramount pictures have network of companies forming virtual network facilitated by convergence of publications, communication, computing and home electronics.

Barrier free organizational network of firms organized functionally tied with cooperative exchange relationship.

Another network type beyond the above is cited by Miles, Snow, Mathews, Miles and Coleman, 1997 as “Cellular organization”. Like cells (self managed teams, autonomous business units) that can perform alone and in concert with others more complex tasks, these organizations are living and adaptive.

Vertically integrated functional structure—> Multi Divisional form—> Matrix—> Network—> Cellular organization

Hamel (2000) describes Technological advancements, rise in capital investment and emergence of new managerial class as new forces driving new organizational structures viz.: virtual organizations, federated organizations, multi company coalitions and network structures.

A Deloitte research technology, media and telecommunication study, titled ‘The elements of value network alliance – Strategies for building alliance partnerships’ (2008), has established surge in number of corporate alliances. Bartlett and Ghoshal (1991) in their study have found that firms adopt multiple strategies to remain competitive.

Strategic alliances offer advantage of ability to learn from other partners (Ciborra, 1991). Learning opportunities are not the same for all member firms in a network and one firm may learn more than the other. In that sense the strategic alliance may provide larger competitive edge creating a learning battlefield (Hamel, 1991; Lei & Slocum, 1992). Member firms of strategic alliance compete and cooperate simultaneously leading to coining of term “Coopetition” (Dowling, Roering, Carlin & Wisneiski, 1996). Thus all the firms working together must trust and accept the norms of relationship.

#### Strategy - Structure - Performance Challenges of Network Alliances

But why would the firm not focus on one product or one geographical area? Often firm finds that it can create more value by leveraging its resources to multiple business activities. This is why many organizations expand its business via vertical integration and diversification. Leveraging resources would result in large dedicated investments and enhanced organizational complexity leading to coordination problem and bureaucratic inefficiency. If these inefficiencies aren’t managed well, bureaucratic cost would exceed its advantage (Ramanujam and Vardarajan, 1989).

Motives behind forming network alliance could range from seeking control to their environment, acquiring resources, reducing uncertainty, securing market advantage to gaining required business knowledge. Varadarajan and Cunningham (1995) categorized motives of forming network alliance into eight key areas and briefly list the main motives in each area:

**Table 1: Motives underlying strategic alliance formation**

**1. Market entry and market position-related motives**

- Gain access to new international markets
- Circumvent barriers to entering international markets posed by legal, regulatory, and/or political factors
- Defend market positions in present markets
- Enhance market position in present markets

**2. Product-related motives**

- Fill gaps in present product line
- Broaden present product line
- Differentiate or add value to the product

**3. Product/market-related motives**

- Enter new product/market domains
- Enter or maintain the option to enter into evolving industries whose product offerings may emerge as either substitutes for, or complements to, the firm's product offerings

**4. Market structure modification-related motives**

- Reduce potential threat of future competition
- Raise/erect entry barriers
- Alter the technological base of competition

**5. Market entry timing-related motives**

- Accelerate pace of entry into new product-market domains by accelerating pace of R&D, product development, and/or market entry

**6. Resource use efficiency-related motives**

- Lower manufacturing costs
- Lower marketing costs

**7. Resource extension- and risk reduction-related motives**

- Pool resources in the light of large outlays required
- Lower risk in the face of large outlays required, technological uncertainties, market uncertainties, and/or other uncertainties

**8. Skill enhancement-related motives**

- Learning new skills from alliance partners
- Enhancement of present skills by working with alliance partners

Source: Varadarajan & Cunningham (1995: 285).

Structure defines the lines of responsibility, authority and communication through which the organization administered, including flow of information and data between the different administrative elements. In addition structure includes techniques of coordination, relationships among organizational subunits, methods of reward and punishment, policies and activities occurring within an organization, and social & political networks (Chandler, 1962; Dalton et al., 1980; Galbraith and Nathanson, 1978; Miles and Snow, 1978; Rumelt, 1974).

The alignment, or fit, of strategy and structure is bare minimum requirement for organization performance which includes two broad areas viz.: financial (e.g. revenue, profit, and ROI) and non-financial (e.g. customer satisfaction and market share) assessments (Galbraith and Kazanjian, 1986; Miles and Snow, 1978).. Organizational performance is influenced by contingent factors beyond the domain of strategy and structure. These contingent factors can be either external environmental factors or infrastructure. Environmental factors are customers, competitors, industry structure and general economic and regulatory controls (Christensen and Montgomery, 1981; Porter, 1985, 1980). Infrastructure are the firm's technology and systems, core competencies, capabilities, and socio-structure or firm culture that are interdependent and help organization maintain its competitive position (Day, 1994; Fombrun, 1986; Prahalad and Hamel, 1990; Thompson, 1967).

SSP paradigm posits congruency between the firm's strategy and structure and strategic fit an underlying requirement for superior organization performance (Miles and Snow, 1984). Firms that pursue different strategies must seek to develop structures that support such a strategy. Integration, both within the firm and across other firms is required for effective communication and coordination of activities across multiple firms. Integration aims at the coordinated use of common resources and systems for timely producing high quality product and services and ensures information flows in a manner that drive superior performance.

Thus organization structure needs to integrate organizations governing the network of member firms and the links between firms through which the enterprise is administered. A lack of integration may lead to the failure of multiple partners attempting to work together. SSP denotes that structure may be adapted to support the desire of tighter integration across members. Critical components of structure include Information technology, communications, standards, decision-making authority and reward / revenue sharing systems that can be applied to create SSP framework.

Information Technology facilitates and requires flexible organization structure. Knowledge is widely and heterogeneously distributed in organizations (Hayek, 1945). Knowledge exchange between firms is necessary for its use and recombination (Nahapiet & Ghoshal, 1998). Technology facilitates connecting people, teams, stakeholders, organization from different parts of the world. Technology integration helps in coordinating data and systems with intra & inter group network members (Choy et al., 2003). Systems coordination is necessary for exchanging information with internal (design, manufacturing, marketing) and external (customer, suppliers) firm members in a timely, responsive, and usable format. Internal coordination of information allows a firm to coordinate internal resource deployment; facilitates inter-organizational synchronization and improved resource use.

Technology integration needs system flexibility at the points of integration between members. Organizational design must be transformed to include “loose coupling” and “open systems” modular perspective (Lei, Hitt and Goldhar, 1996). Coordination and flexibility ensures dissemination and availability of real time information to support decision-making. Network firms become clusters of autonomous divisions that behave like separate firms, where tasks and roles are not rigidly defined (Halal, 1994).

Incomplete Data & information, inconsistency & redundancy delays organizations decisions. Network member firms are geographically dispersed and decentralised adding to the difficulty of coordination. Communication among network firm’s personnel creates a shared interpretation of goals, trust and closer ties among the firms. Well established formal and informal communication channels facilitates quick learning in change of customer preferences and quick formulation and implementation of actions for gaining competitive advantage.

Alliance performance consists of two processes: Acquisition - by which information is received and distribution – by which acquired information is, shared synergistically leading to new information and knowledge. Information sharing is particularly more important in network firms as apart from other knowledge base, tacit knowledge requires effective communication and coordination with member firms.

Language standardisation of information is crucial element of structural integration. Standards facilitate data coding and order notation terminology. Effective communications do away with frequency of need to decode communications up and down the value chain. The proliferation of internet has not only reduced the cost of integration but enhanced

the flexibility of the firms in creating an integrated set of standards.

Decision-making authority at proper level has a positive impact on its success of the firm (Chow et al., 1995). Centralized planning and decision-making in a hierarchical firm have proven to provide better coordination, control, and consistency. However network alliance responsiveness may be improved by allowing problem-solving decisions to be handled locally. Implementations of decisions are beneficial when managers, possessing intimate knowledge of local information, are given decentralized decision-making authority.

Rewards and compensation as elements of structural integration, relate to the critical issue of motivating both employees and organizations for overall organizations growth. Individual rewards and compensation should be created to induce boundary-spanning personnel to focus on improving process coordination and service. Boundary spanners should be motivated to extend greater cooperation and coordination amongst other network member firms. Determining an effective rewards and compensation strategy require a comprehensive understanding of all the variables that affect a strategies ability to deliver value to the customer.

Rewards and compensation must apply to not just internal performance of the firm but also to interconnected firms. Sharing or mutually reinvesting gains motivates member firm to seek more ways to improve. Conversely, strategy involves risks that should be shared when appropriate. A policy of sharing mutual gain and risk reflects commitment to the belief that a firm’s performance is closely linked to overall network alliance goal attainment.

### **Measuring Performance of Network Alliance**

Firm’s performance considerations SSP portrays performance as resulting from the fit of structure to the chosen strategy of the firm. Strategic determination is equated with establishing goals while performance is the evaluation of how well the goals are met (Chandler, 1962; Hofer and Schendel, 1978).

Atkinson et al. (1997) define three roles for performance measurement:

- (1) Coordination that focuses decision-making on the most important objectives;
- (2) Monitoring, or the actual measurement and reporting of performance; and
- (3) Diagnostic, which is used to evaluate performance, identify improvements needed, and tie the non-financial metrics to financial measurement criteria and goals.

The shared goals identified in Network strategy formulation are used to derive performance measures for the firm. Failure to link performance to strategy may lead to the inability of the firm to achieve goals and meet customer expectations, and will not provide the vision necessary to influence individual goal-directed behaviours (Atkinson et al., 1997; Kaplan and Norton, 1992).

According Mentzer and Konrad (1991) two elements of performance - efficiency and effectiveness, both are necessary to accurately measure performance. Efficient performance measures how well the resources expended were utilized while effectiveness assesses the degree to which goals are accomplished. Assessment of overall corporate performance has been limited in network alliance arena, as the metrics employed have often been measures of internal corporate operations. Moreover they also exhibit following weaknesses with respect to capturing the efficiency and effectiveness of corporate strategy:

- (1) Important issues like customer satisfaction are ignored;
- (2) The basis in historical cost limits predictive ability; and
- (3) Little or no ability exists to objectively judge effectiveness.

Possible solution to this limitation is the balanced scorecard method of performance reporting, which measures relationships developed with customers, the continuous improvement of processes, and innovative learning capabilities of firms (Kaplan and Norton, 1992). The balanced scorecard approach has four components:

(1) Financial measures that provide the efficiency perspective are retained from the traditional performance reporting approach.

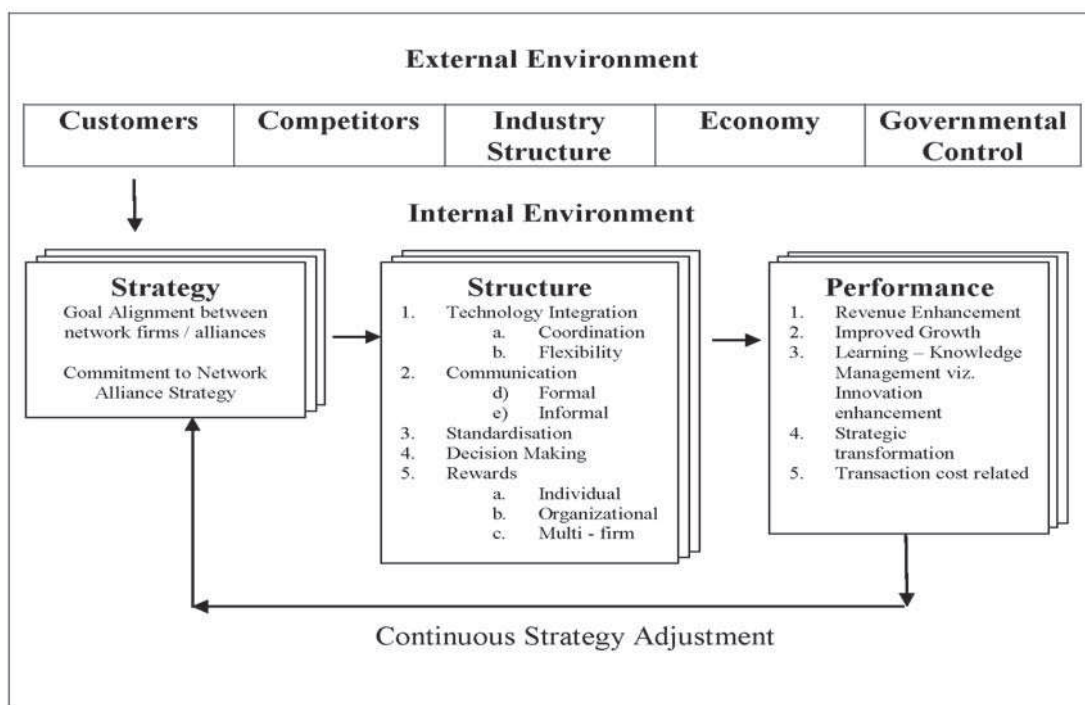
(2) Customer perspective measures are developed to answer the question “how do customers see us?” Customer concerns may be classified along the four dimensions of time, quality, performance, and service.

(3) Internal business perspective measures address the activities in which the firm must excel.

(4) Innovation and learning perspective measures are more future-oriented and focus on the ability to create new sources of value for customers.

Failure to link performance to strategy may lead to the inability of the firm to achieve goals and meet customer expectations, and will not provide the vision necessary to influence individual goal-directed behaviours (Kaplan and Norton, 1992). In the current environment, the leader firm is generally responsible for negotiating and enforcing such performance standards. Rather than reducing compensation, non-performing firms may be replaced, and thus lose the revenue stream entirely.

The major elements of strategy, structure and performance presented in the above narrative are presented in the form of layered boxes in Figure 2. Layered Box represents multiple firms working together in a Network. The concepts relate across all members of the Network firms, although the elements should be viewed from the perspective of a single, focal firm in a Network.



**Figure 2: Strategy, Structure and Performance Alliance Integration Framework**

Source: Adapted from SSP Supply chain integration framework, the strategy-structure-performance-paradigm to supply chain environment by C. Clifford Defee and Theodore P. Stank, *IJLM* 16, 1, pg 28 – 50.

The framework shown in Figure 2 describes an iterative relationship between internal firm strategy, structure, and performance measurement systems. It implies that a company's strategy should be complementary with that of alliance firms. Disjointed strategies prevent firms from developing shared goals and utilizing capabilities. Figure also identifies the elements comprising firm structure required to support strategy implementation, the nature of the relationship between strategy and structural characteristics including technology integration, communication, standardization, decision-making location, and reward and compensation programs.

SSP integration framework in network firms requires investment in computer systems technology that supports coordination and flexibility among its entities, creation of formal and informal modes of communication to facilitate the rapid sharing of information and business plans, standardization of information and processes, integrated individual and organizational reward structures aimed at achieving overall goals.

Strategy research has consistently predicted structural outcomes in light of prior strategic decisions at the firm level of analysis (Chandler, 1962; Egelhoff, 1988; Rumelt, 1974). Strategic research in a multiple firm's perspective is a much younger field, and the research to date has been primarily descriptive rather than predictive – with strategy often equated with the degree of integration achieved across multiple firm entities.

## CONCLUSION

There is a compelling case for a new multi firm SSP theory. Even though the tools may not be in place entirely, multi firm structural and performance outcomes may be predictable. Conflicting strategies existing across member firms will limit overall corporate performance of network alliance.

Continuous performance monitoring and identification of bottlenecks is necessary, especially during early stages, as they are more easily correctable. Further, member performance must be followed regularly over time to identify situations of member misalignment, member incompatibility or recently changed strategy.

The primary implication of the framework for professionals is to “know your partners”. Are other members actually in line with your firm's goals? Do their strategies mesh –

either as consistent or complementary – to your own firm's strategy?

Addressing the performance problem may require from a minor structural modification to replacement of member firms with incompatible strategies in the extreme case. Network Strategies used to deliver to each customer or customer segment must align with the strategic value sought by those customers.

Structural elements, such as formal communications processes may facilitate the understanding that change is needed and is coming across member firms. Therefore it is essential for the firm to do competitive benchmarking and maintain knowledge of other firms that could fit in the future. If proactively identification of new candidate firm or correction in existing member firm is not done in schedule, it may translate in poor performance leading to crisis.

## Implications for future research

How these structural elements are manifested in an environment and how they are associated with structural integration. What form these elements take when member firms have complementary strategies? How these one or more of the structural elements impact performance of members that have differing or inconsistent strategies? Does central leadership or leadership of dominant member firm impose their will on less powerful members, or at least establish rules and standards of members that are expected to support.

In a smoothly functioning firm the trust formed through repeated experience may lead to replacement of formal communications structural elements with informal or may even lead to elimination of formal communication, except those associated with “management by exception”.

An area that has received significant focus in the strategic literature is the environment of rapidly changing industries like those found in high technology (Eisenhardt and Martin, 2000; Teece et al., 1997). Future multi firm research may follow this trend by investigating the incidence of member firm's strategic alignment supporting high-tech industries or products, compared to member firm's experiencing relatively less change.

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