Exploring decision behavior of small-business owners/managers in the alliance partner selection: A qualitative case study

Zelimir M. Petrovic \textsuperscript{a,b}

Presented at the Economics and Management of Networks Conference (EMNet 2013) (http://emnet.univie.ac.at/)

Robinson Hotel and University Ibn Zohr Agadir, Morocco

November 21-23, 2013

\textsuperscript{a)} University Union – “Nikola Tesla”, Faculty of Entrepreneurial Business, Cara Dusana 62-64, 11000 Belgrade, Serbia. E-mail: petrovic.z@fpb.edu.rs

\textsuperscript{b)} Vienna University of Economics and Business, Institute for Small Business Management and Entrepreneurship, Welthandelsplatz 1020 Vienna, Austria
Abstract

This paper aims to examine rules that small-business owners/managers use to estimate partner attractiveness in the process of alliance partner selection. Empirical analysis is based on qualitative case study of alliance in hospitality industry. The research findings show that small-business owners/managers are risk-averse and rely on trustworthiness when estimating partner attractiveness. At the end a model of decision behavior of small-business owners in alliance partner selection is presented.

Keywords: Alliance, partner selection, decision behavior, small-business owners/managers, intuition, heuristics.
1. Introduction

Interorganizational partnerships, such as alliances, have become a useful cooperative strategy that can improve business success of small firms. An alliance relates two or more partners who share business goals. Firms are entering alliances to overcome its limitations by gaining access to complementary resources (Das and Teng 2000; Eisenhardt and Schoonhoven 1996). Because small firms are characterized by tight resources, they are forming alliances more frequent than large firms do (Suarez-Villa 1998). However, these partnerships are not always successful and often experience high failure rates (Spekman et al. 1996). The problem of alliance failure has its roots in the partner selection and in the basis on which partner selection decisions are made (Bierly and Gallagher 2007).

Previous studies have examined decision behavior from normative view and associate partner selection with a formal analysis (e.g. Nielsen 2003). In this way, literature postulates that decision makers rely only on instrumental rationality when evaluate alternatives. This leads to the choice of the most efficient way for achieving a particular goal (see’s Einhorn and Hogarth 1981; Slovic et al. 1977), and considers decision maker as an analytical in partner selection. On the contrary, strategic choices in small firms are personification of an owners/managers behavior and individuality (Hambrick and Mason 1984). While they are less prone to formal analysis and have strong personal influence in the firm, they reduce the rationality of strategic decisions (Brouthers et al. 1995; Kraus et al. 2006; Schade 2010). As a result, instead relying on formal analysis to solve a problem, small-business owners/managers use mental shortcuts, called intuitive heuristics (Busenitz and Barney 1997). Although small-business owners/managers are more intuitive when deciding, it remains unclear what heuristics rules they use to estimate partner attractiveness?

This study aims to clarify decision behavior of small-business owners/managers in the alliance partner selection. To better understand on which rules owners/managers rely when
estimate partner attractiveness, this study analyzes cases of small firms involved in alliances in hospitality industry. The rest of the paper is organized as follows. The next section presents theoretical background of the problem. The third section presents and describes the research methods. The fourth section presents the results of study, which starts with brief description of case, and later report important findings. In addition, a conceptual model of decision behavior of small-business owners in alliance partner selection is presented. The last section offers conclusions, limitations and implication for further research motivated by this study.

2. Theoretical background

2.1. Decision behavior

Each small-business partnership begins with selection decision as a necessary condition for alliance formation (Das and Teng 2002; Huang et al. 2011; Williams and Lilley 1993). Despite of the way in which decisions are made, the decision result has important implications for the partner selection (Bierly and Gallagher 2007). In general, decision making is a mental process of building preferences toward some alternative in given situation (Einhorn and Hogarth 1981). In such situation, it is reasonable to assume that some preferences are better than others. The way in which decision maker evaluates and build a preference over alternatives is called judgment and result of this mental process is called choice (Hogarth 1987). Thus, each decision has two following parts: judgment and choice. While judgment refers to the way in which decisions are made, choice refers to the result of judgments.

From psychological view, the way in which judgments are made, depends on the one’s mental style (Allinson and Hayes 1996; Armstrong et al. 2012; Sadler-Smith 2004). Mental style is either inborn quality or it is developed at an early age. According to the dual process theory, each person has two distinct mental styles: intuitive and analytical (Evans 2003;
In contrast to the analytical style, intuitive style comes from the right-brain hemisphere and it is seen as a feature of successful manager. Managers, who use intuitive style, rely on instinct, emotions or their “gut feeling” to solve problems (Sadler-Smith and Shefy 2004). Because intuitive style is explicit and fast, small-business-owners/managers are using it more frequent to avoid formalities (Sadler-Smith 2004). Thus, they use mental shortcuts to solve problems, called heuristics (Busenitz and Barney 1997).

Decision process depends on decision maker view of reality and his subjective interpretation of environment. However, the way in which decision maker behaves and evaluates alternatives is not necessarily based on the reality by itself, but on one’s view of reality. Similarly, quality of a decision and its goodness is subjective at each parts of decision (Einhorn and Hogarth 1981). While the quality of choice rest on moral norms and subjective opinion of goodness someone who decides, the quality of judgment rest on efficiency of evaluation. In sum we can say that decision behavior is determined in the way in which decision are made.

2.2. Partner selection decision

In general, each decision regarding partner selection is driven by several reasons that can be separated on decision motives and expectations from a decision result (Koza and Lewin 1998). Decision motive can have either exploration and/or exploitation nature (Lavie and Rosenkopf 2006). When partner has an exploration needs, his decision is motivated by need for an intangible resources such as, new knowledge (March 1991). On the contrary, when partner has exploitation needs, his decision is motivated by need for tangible resources. Several theoretical perspectives offer explanation why firm decided to form an alliance. However, the resource-based view is dominant in explaining small firm alliances formation, because small firms are characterized by the thigh resources (Eisenhardt and Schoonhoven
According to a resource-based view, partnership decisions are driven by the shortage of tangible and/or intangible resources (Das and Teng 2000). In this way, small firms are expecting to overcome their limitation and improve its competitive position by gaining access to complementary resources (Hoffmann and Schlosser 2001).

Small-business owners/managers, guided by the motives and expectations, search and analyze a prospect partner. Because, they cannot estimate future events with certainty and predict future state, their decision is not deterministic. As a result, events occur under probability laws and results are subjected to prediction errors. Thus, small-business owners/managers face risk when analyze prospect partner.

3. Research method

When there is less knowledge about topic of interest, exploratory qualitative research design is useful (Creswell 2009). Qualitative research can provide new insights into this topic of interest through deeper interaction with respondents, which is not possible in quantitative study. Thus, this study use qualitative approach to the study of small-business owners/managers who were directly involved in alliance formation.

While it was difficult to identify such cases, because there is no existing public databases of small firms engaging in partnerships, snowball approach was used to find and select participants suitable for this study (see’s Goodman 1961). This approach has its advantages over others, particular when respondents are not easily accessible. This technique is simple and it means that researches expand its sample by asking a respondent to recommend others for interviewing.

The unit of analysis where selected based on three following criteria. First criterion refers to the firm size, and infers that firm was included in the study, if it corresponds to the EU definition of small firm. Second criterion refers to involvement of managers/owner in
alliance formation, and infers that they were included in the study, if they were involved in
decision process while forming alliance. Third criterion refers to the industry type, and infers
that included firm operates in hospitality industry. Hospitality industry is interesting because
in this type of industry alliances are formed often (see’s Strate and Rappole 1997).

After the respondents were identified and selected, we have scheduled in person
interviews by telephone with owners/managers. The interviews took place at the respondents’
ofices, where each participant has responded to semi structured questions. All interviews are
digitally recorded and later transcribed into a digital form, after interviewees give us
permission to do so (Arksey and Knight 1999). Because of difficulties involving in
investigation of these events in the real time, respondents were asked to provide answers
about retrospective events. Interview contained question about four topics: 1) Motives to
form an alliance 2) Expectation from alliance 3) Partner search 4) Partner evaluation.
Summary of categories is provided in figure 1, while the interview guide is provided in the
Appendix.

Fig. 1: Decision behavior in partner selection
Data that were collected from the interviews are analyzed using Mayring’s (2000/2010) techniques of qualitative content analysis. Although Mayring presents two ways to develop categories, in this situation inductive approach is preferable in comparison with deductive, because it enables researcher to rationalize categories after 50 percent of coded material.

To assess the validity of this study, two following issues are addressed. First, to assess the stability and reproducibility of content analysis, data were recoded after two weeks and the same data were recoded by additional coder. Second, to assess the interrater reliability of coded data, Cohen’s kappa (1960) was calculated. This measure enables us to know how much coders consistent among themselves were in their coding task. By following Cohen’s (1960) recommendation, coded data is reliable when the values of alpha coefficient are greater than .7.

4. Results

4.1. Case description

Alliance between hotels and restaurants has become popular in recent years (see’s Strate and Rappole 1997). Hostels, in general, offer a budget accommodation in a sociable surrounding for their guests. Because of high costs related to in house restaurant, hostels make contractual agreements with externally developed restaurant. In this way, hostels can improve competitive position. Next to financial benefits, alliance can improve overall business image and provide greater value to its customers (see’s Strate and Rappole 1997). Contractual alliances are formed more frequently than equity and provide greater autonomy in decision-making among partners (Rothaermel and Deeds 2006; Stafford 1994).

Unit of analysis is alliance based on contractual agreement between hostel and restaurant. Hostel is located in the city center of Serbian capital. Hostel is privately owned and two of tree owners are actively involved in managing hostel that operates in the form of a small firm.
It offers modern accommodation for 30 people, and has visitors from all parts of the world during the year. In recent years, guests are expressing increased interest for arrangements with affordable meal, in particular breakfast and lunch. Hostel cannot offer meals to its guests because it has no restaurant of its own, management of hostel have decided to find partner restaurant in the neighborhood. In this way, hostel could improve satisfaction of guests with their service, and gain competitive advantage over other hostels. After a while, hostel manager has found suitable restaurant in the neighborhood. Restaurant was newly opened at the time and could meet all demands and provide meal for their guests. Because, most of its regular customer comes in evening time on dinner, restaurant was also interested to arrange some affordable meals for hostel guests. Hostel was providing guests two times a day, as a part of their regular offer, while restaurant was providing the meals two times a day for hostel guests. Yet each had common goal and managers were involved in coordination of the activities related to this particular task.

4.2. Analysis and discussion

Three distinct themes emerged from the data about heuristic rules that small-business/owners use in partner selection. Each theme was discussed with interviewees, to support the validity of these findings. A summary of heuristic rules that small-business owners use in partner selection, is presented in Table 1.

A first theme emerged around the way in which the partners are found. Small-business owners/manager gave priority to the partner with whom they had some prior ties. As one respondent explained:

“...Well we have found partner, circumstantial ... mutual friend of mine and mine co-owner has opened restaurant in the meantime. Literally, in about five minutes from our hostel, so, we came up with the idea, because of the
proximity of restaurant and hostel, to make the deal ...

Perhaps, in the situations that includes risk, such as partner selection, small-business owners/managers tend to reduce level of risk. One way to reduce risk is to adopt social orientation and search for partner with who they worked before and have some prior ties. Social network theory offers insight into importance of social capital and embeddedness of alliance formation (see’s Gulati 1998).

Second theme emerged around the way in which the partners are selected. Small-business owners/manager gave priority to the partner they perceive as trustworthy. As one respondent explained:

“...So, above all, we have relied on confidence and mutual friendship, and we did not want to make business with some other restaurant ... so we rely concretely on confidence in our mutual friend, and at the end it turns out to be a real hit....”

Perhaps, contrary to the rational partner selection approach, the decision maker with an intuitive decision behavior relies more on abstract information, and less on formality, details and rationality (Sadler-Smith 2004; Sadler-Smith and Shefy 2004). Because trustworthiness is an orientation toward others that has social meaning beyond instrumental rationality (Kramer and Tyler 1996), decision maker relies less on contracts to guarantee predictability (Gulati 1995). As a result, decisions are based on heuristic rules common for an intuitive decision behavior. Trustworthiness can be caused by the altruistic behavior of a partner and improve the cooperative behavior (Barclay 2004). Partners are trustworthy if they possess abilities, skills, and competencies to perform some particular task, to show the bona fide (benevolence), and hold personal integrity as an acceptable moral principle (Mayer et al. 1995).

Third theme emerged around circumstance under which partners is evaluated. Small-
business owners/manager try to avoid risk when select partner. As one respondent explained:

“... I am not sure that I would take my chances with someone else ... we did not want to make business with some other restaurant and to take chances, because we did not know what the food there was... and what was the meals ...

Perhaps, the decision maker with an intuitive decision behavior have propensity to avoid risk (see’s Kahneman and Tversky 1979). This includes both relational and performance risk (Das and Teng 2001). In general, propensity to avoid risk distinguishes small business owners/manager from other managers (Covin and Slevin 1998), and they consistently behave in the same manner in the process of partner selection.

Table 1. Heuristic rules that small-business owners/managers use in partner selection (k = .9)

<table>
<thead>
<tr>
<th>Heuristic rules</th>
<th>Quotations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Theme 1: Prior ties</td>
<td>“... we know each other for decades, we grow up together and lived in the same neighborhood ...”</td>
</tr>
<tr>
<td>Theme 2: Trustworthiness</td>
<td>“...we have rely on confidence ... he never let me down so far, and he is a pretty good chef”</td>
</tr>
<tr>
<td>Theme 3: Risk Aversion</td>
<td>“... I am not sure that I would take my chances with some else ...”</td>
</tr>
</tbody>
</table>

Based on these findings, the conceptual model concerning small-business owners/managers decision behavior in the alliance partner selection is proposed and presented in figure 2. As the analysis shows, small-business owners/managers are not relying on formal analysis while selecting an alliance partner. Instead they search for partner with whom they had some prior ties. As a result shown, they perceive such partner more
trustworthy and more attractive than others. While economic exchange is traditionally related
to normative perspective and maximization of expected utility, social exchange entail partner
willingness to be uncertain about future benefits and materialization of relationship (Das and
Teng 2002). As a result, social exchange between partners is built upon trustworthiness and
commitment in contrast to economic exchange. Contractual agreements will bring less
formalized governance structure in which partners are more willing to be exposed to relation
risk and thus have more confidence in prospect partner. Small business owners/manager are
more likely to entail social exchange into these partnerships, and when they evaluate partner,
they prefer some certain outcome with lesser risk. However, perception of risk is subjective
and outcome can be considered risky if decision maker believes so. Therefore, if we consider
partner selection from this perspective, a small business owner/manager who is a decision
maker with an intuitive decision behavior and who relies less on formality and rationality
(Allinson and Hayes 1996), will rely to a higher degree on trustworthiness when estimating
partner attractiveness. Thus, following proposition is developed:

**Proposition 1:** Prior ties and trustworthiness will affect attractiveness of partner in alliance
partner selection between small firms.

![Figure 2. Heuristic rules in partner selection](image)
5. Conclusion

This paper has explored decision behavior of small-business owners/managers in the process of alliance partner selection. In this study, the aim was to determine what heuristics rules small-business owners/managers use to estimate partner attractiveness. The results of this study show that small-business owners/managers are risk-averse and rely on trustworthiness and prior ties when estimating partner attractiveness. This study contributes to the overall knowledge on the decision behavior of the small-business owners/managers in the alliance partner selection, and serves as a basis for future studies. A problem not addressed in this study was whether the intuitive decision behavior was efficient and how it could be improved. Further research might study how trustworthiness and prior ties affect partner attractiveness in partner selection among small firms.
Bibliography


Appendix

**Interview guide**

1. Reasons to form an alliance
   - Reasons for forming an alliance
   - Expectations from partnership
   - Feature of an alliance

2. Partner analysis
   - Search process
   - Evaluation of partners
   - Desirable partner characters/ attractiveness of partner
   - Final decision

---

1 A small enterprise is defined as an enterprise which employs fewer than 50 persons (number of persons expressed in annual work units) and that has a turnover or balance sheet totaling less than 10 million € (Retrieved oct. 12., from: http://ec.europa.eu/enterprise/policies/sme/facts-figures-analysis/sme-definition/index_en.htm)