Introduction bhp and rio tinto are the second and third largest iro...

Contractual partnership can bring a lot of advantages, but also brought along increase in complexity and loss flexibility. Thereby, need to use the selection criteria to choose a partner.

Rio and BHP form joint venture aims to sharing each other benefits. For these two companies, the management style and structure and nature of products were similarly. They are listed on the London stock exchange. Also, BHP proposed acquisition of Rio in 2008 (www. accc. gov. au) that means before JV they have collaborate experience so they can know more about each other such as background of company, ways of communication, capacity, financial situation etc… it can easy to formation of JV and minimize risk of failure.

China is the world's largest importer of iron ore and BHP-Rio together would account for 80 percent of Australia's exports of the ore (www. miningmx. com). Even is a major manufacturing base for iron and steel product but they did not produce high-grade iron ore, so they depend on two mining giants to supply raw material (www. news. bbc. co. uk). Thus, if BHP and Rio JV successful it can maintain the iron ore supply to China stable and enjoy economic of scale.

Why a joint venture was chosen as the vehicle of co-operation?

FDI is the most advanced and complex for foreign market entry (FME) strategy, and involves establishing manufacturing plants, marketing subsidiaries, or other facilities aboard (Cavusgil, 2008).

Rio and BHP is a project based, non-equity venture, which means project with a narrow scope and defined timetable, no new company formed (Cavusgil, 2008).

This Domestic joint venture would have led to Rio and BHP to sharing each other's mines and transportation facilities. For example, can reducing costs through shorter rail hauls and more efficient allocations of port capacity (press release, 2009). Also, the chairman of Rio Tinto believed that: “ this joint venture will establish an unrivalled iron ore business with world class assets and infrastructure”(press release, 2009).

Rio and BHP can combine the management, procurement and general overhead activities into a single entity (press release, 2009). It can simply management structure and can be adjusted easily. The companies had estimated cost savings of around $10bn (£6. 3bn) a year through the sharing of infrastructure and personnel. (www. news. bbc. co. uk).

However, JV has some disadvantages to Rio and BHP. It is because JV did not have equity commitment. Also, two companies need to puts greater emphasis on trust, communication and developing relationship (Cavusgil, 2008).

On the other hand, some of literature identifies many motivations to formation JV such as minimize the risks and costs with market entry, access to assets and skills, enjoy the economies of scale and share the acquisition of knowledge (style & Hersch, 2005).

c. What external events gave rise to the opportunity or pressure to work together?

Use PESTEL and Porter's Five Force framework to analysis the external events give rise BHP and Rio Tinto to the opportunity or pressure to work together.

PESETL:

Political- highlights the role of governments

Regulator resistance may have played an important role in the companies' decision. In BHP proposed to acquisition Rio , the Australian Government have negative attitude , the government ask this two companies meet the concession which are the government provided.

Economics- macroeconomic factors such as exchange rates, business cycle and differential economic growth rates around the world. (Gerry, 2008)

In 2008 the global financial crisis has impact the steel and mining industry (www. steelorbis. com). The economy and weak demand, iron-ore prices should be half their 2008 levels (Robert Guy Matthews, 2009). Even financial crisis effect economic around the world but some of the developed countries such as: Brazil, Russia, India and China they are financial situation can maintain in the growing. Thereby, the demand of iron ore will again be leading the growth with an expected increase of 11. 1% for 2008 and 10. 3% for 2009 (www. worldsteel. org). Also, iron ore prices were climbing quickly, mainly because China was consuming more steel and miners had supply chain problem-not enough ports, railroads and ships-both of which kept supplies scarce (www. online. wsj. com).

Porter's Five Force devised by Michael Porter to describe forces that shape competition within an industry and help to identify strategic opportunities and threats.

Vale of Brazil is the only other main competitor with Rio and BHP (SJ Berwin, 2010).

Bargaining power of supplier: Australian government is a major supplier to the iron ore industry, so the bargaining power is higher.

Bargaining power of competitor: In the global market those three suppliers dominated the iron ore market which is Vale, Rio and BHP. Vale is the largest supplier in the world. In 2008, Vale to hold 32. 8% shares in the Seaborne iron ore market and Rio and BHP respectively 18. 6% and 17. 1 % (www. worldsteel. org). Before JV Vale is the only one competitor for Rio and BHP. If JV successful, Rio and BHP will control nearly 36 % shares of the seaborne iron ore market. Thurs, the bargaining power will higher than before.

Bargaining power of buyer: Iron ore industry the buyer major buyer which is China, Japan and Korea, they are bargaining power is lower. It is because this industry dominates by 3 major miners. Those buyer difficult to find others supplier in the market.

Question 2

In a global market iron ore dominated by an oligopoly with just three suppliers, Vale, Rio Tinto and BHP Billiton (Moffat, 2009). The commodity's price is set in annual negotiations dominated on the supplier side by Rio, BHP and Vale of Brazil, the world's largest producer (www. ft. com). If the joint venture successful may restrict competition in relation to the fundamental competitive parameters in the seaborne iron ore markets such as: price, volume and quality (Moffat, 2009).

The follow picture can show big three miners dominate the seaborne iron ore market:

Shares of Seaborne Iron Ore Market, %

2006

2007

2008

Vale

36. 1

36. 1

32. 8

Rio Tinto

19. 0

19. 3

18. 6

BHP Billiton

14. 2

13. 8

17. 1

Total

69. 3

69. 2

68. 5

Source for market shares: Raw Materials Group quoted in UNCTAD Trust Fund on Iron Ore Information “ Iron Ore Market 2008-2010”, Geneva, June 2009

However, Iron ore is a globally traded commoidty it can linkage with different industry in the economic market such as automotive industry, steel industry etc.. so it plays an improtant role in the world. Rio and BHP form JV , many commissions come from different country and play different role to against the JV. They aim to ensure the business can operate fairly and to tackle unfair competition. In this case, three countries such as China, Japan and Korea have largest respond.

China is the largest steelmaker in the world, on this joint venture proposal it would concerned about the price of iron ore control in hands of the top three iron ore miners (David Fickling, 2010). Also, the Japan Iron and Steel Federation estimates a combined BHP-Rio would control 60% of the country’s iron ore imports (www. lowyinterpreter. org). Thus, steelmakers in China, Japan and Europe have all opposed the tie-up between the mining giants, saying the joint venture will tilt the global iron ore market further in favour of three producers who already dominate the seaborne iron ore trade (www. ft. com). Otherwise, The South Korea's FTC said a joint venture would have reduced competition in the iron ore market, it is because Rio and BHP would share the same cost structure, output volume and quality (www. bestshippingnews. com). Furthermore, Rio and BHP form JV this two companies will combine iron ore production facilities in the Pilbara, means that many workers will face job losses so Australian Government to against this JV (www. wabusinessnews. com. au).

Question 3

Definitions of corporate culture:

Meschi and Roger (1994) when an organization develops into a MNC, the corporate culture can have it basic on the ' original' organizational culture, or the national culture, or a combination of two.

Two of Australian which is Rio and BHP form JV in Australian, in this section use determinants of organizational to analysis their corporate culture.

National culture

The follow picture showed the characteristic of Australian had higher level in individualism and lower level in power distance country (www. geert-hosfstede. com). That means Australians tend to work independently and the management team would like to invite they are employee to participate in decision making.

Source from: www. geert-hofstede. com

History of organization

Rio and BHP they develop their business in different country, so they did not have pure nation culture.

Industry culture

Rio and BHP those two iron ore companies they have similar business area. Hence, they can share same value and culture.

Management style

Jacques Nasser the director of BHP has 33 year career experience in different country such as America. Jan du Plessis the Chairman of Rio also have career experience in America and British company (www. riotino. com& www. bhpbilliton. com). Those two decision makers have international management style so they can use the experience to management their company.

Size of organization

Rio and BHP are the MNE, they are business activities cover different country such as UK, Australian, Brazil etc…

Nature of employees

Whether educated or skills worker, Rio and BHP is mining industry so the structure did not have more different, so they required their employee's background is similar.

What is negotiation

Brian J. Hurn (2007) getting people of different cultures to see agreement by considered dialogue on an agreed agenda.

Usunier (2003) suggested threes facets of culture different affecting international negotiation:

Negotiation process

Australian prefers to negotiate in a fairly straightforward and honest style (Katz, 2009). Australian did like being pressured so do not make the final offer early in the negotiating process and avoid making more than once (Katz, 2009).

In the communication process, some of Australians will some they are emotions and positive and negative directly. Also, they can respect people who give any idea whether they agree or disagree with them (Katz, 2009). When Australians make decision they may apply universal principles rather than considering the specific situation (Katz, 2009). In outcome orientations, Australians tend to written a detail contracts. They can list out detailed terms and conditions for the core agreement.

Behavioral predisposition of parties

Australians appreciate who has a sense of humor, they prefer the meeting atmosphere is usually very informal (Katz, 2009).

Australians believe in the negotiation process can get the win-win situation even in the negotiation process two party have conflicts, they hope both parties should keep a positive attitude and show willingness to work with other in an effort to reach agreement (Katz, 2009).

Underlying concepts of negotiation

In the strategic time-frame, Australian expect they business partner to be one time. They can’t not accept they partner late more than 10 to 15 minutes without having a reasonable excuse (Katz, 2009).

Australian believe in negotiation sharing information is a way to build up trust with each other. Also, in pace of negotiation information and bargaining move smoothly but the decision making can be rather slow. That means they prefer use more time to negotiation with their business partner (Katz, 2009).

Base on above analysis, Australian is refers to Universalism and they are emotionalism is low context. Two Australian companies which are Rio and BHP when work together, they are aspects individualists and the attitude can be overtly competitive. Also, in the business negotiation and decision making process they can keep it smoothly and harmony.

Rio and BHP these two Australian companies did not access to foreign market to form JV so it can define they are a domestic JV. They have same country culture so their corporate culture may simplify than other international corporation.

In the cooperation stage, when two companies come together to form JV, the major objective is to learning knowledge from their partner and get benefit from the JV. However, in determinates of organizational culture this two companies the national culture and industry culture are similar therefore in the implementation stage did not play a significant role.

Rio and BHP form JV, ‘ senior management of the entity will be determined jointly on the basis of the ‘ best person for the job’ with broadly equal participation from Rio Tinto and BHP Billiton. The initial Chairman of the non-executive owners’ council will be Sam Walsh, currently Rio Tinto Chief Executive Iron Ore, and the initial CEO of the production joint venture will be BHP Billiton Iron Ore President, Ian Ashby’ (press release, 2009).

In conclusion, When Rio and BHP JV successful the key personnels of the JV will be change, the management style it may affect the corporation. Thus, to grantee the good JV implementation or operation, these two companies need the best management skill between two partners within JV.

Question 4

Finance strategic

Financial manager play an important role in the company, is involved in the acquisition and allocation of financial resources for the company’s current and future activities and projects, with the primary objective of maximizing the company value (Cavusgil, 2008, p. 581). Also, in the company the financial manager need to concern three major principles financial management skills such as cost of capital and capital structure, methods of financing, currency risk and taxation management.

Cost of capital can define ” The rates of return that a company has to offer finance providers to induce them to buy and hold a financial security”

From the company's perspective cost of capital equal to cost of investment, it is the rate (%) that the company needs to pay to the investors and financiers in order to obtain funds. It is an indicator for the minimum rate of return; the company needs to obtain from making a decision on a new project (Elteman , 2004).

From the finance manager's perspective need to concern how to minimize the cost of capital, what is the optimal financing structure and which kinds of financing instruments are most effective and efficient.

Before the company makes an investment decision they need to compare the rates of return of investment with the cost of capital of company. If the expected return on the investments is low as compared with the WACC, the investment is compelling.

According to the study by Arnold and Hatzopoulos (2000), WACC is most commonly used by different types of companies, ranging from small to large sized, as well as those listed companies within the stock index.

The concept of " Weighted Average Cost of Capital (WACC)" is used for calculating the Cost of Investment (Elteman , 2004, p. 301-303).

WACC

=

D

X

(r debt)

X

(1- tax)

+

E

x

(r equity)

E+D

E+D

Base on the risk of JV different with parent’s company so they need to use cost of capital to judge the investment.

WACC of Rio and BHP did not represent of cost of capital of the JV, it is because different project will carry different cost of capital it will depend on the level of risk.

As compare JV with Rio and BHP, the risk of JV higher than Rio and BHP. It is because JV focuses on single product but Rio and BHP they focus on diversity products, so if the price of one product decrease, the others product price it may increase that can minimize the level of risk.

Normally, have two methods to source of financing which are internal and external.

The internal source of financing includes inter-company loan and transfer pricing. The external source of financing includes equity financing and debt financing. ‘ Equity financing is the issuance of share of stock to raise capital from investors and the use of retained earnings’. Debt financing is the borrowing if money from banks or other financial intermediaries, or selling corporate bonds to individuals or institutions bonds to raise capital’ (Cavusgil, 2008).

Inter-company loan that means Rio Tinto borrow funds from outside for JV purpose.

External funds means JV borrow funds from outside by them self. Use the equity or debt to source of financing can have more advantages and disadvantages.

The main advantage of equity financing “ is that the firm obtains needed capital without incurring debt; that is, without having to repay funds to the providers at any particular time” (Cavusgil, 2008). The main disadvantage of equity financing “ is that the firm’s ownership is diluted whenever new equity is sold” (Cavusgil, 2008).

In the JV, Rio and BHP can use different ways to raise equity financing such as direct public share issue, private placement and private equity fund. Rio and BHP they listed stock in Australia and New York market. When they use issue share in the local market to rise of capital for the JV, they need to consider market liquidity refers to the degree which a company issue new securities without lowering the existing market price. If Rio and BHP listing in foreign stock exchange, they can improve liquidity of its shares and thus allow bigger market for new share issues but they need to concern the trading volume in the foreign market. On the other hand, they need to consider the asymmetric information. It is because imbalance information available to different investors in the world. In the segmented domestic market, normally foreign investor may have limited information about the domestic companies that discourage the investors to invest in those shares (Elteman, 2004).

In conclusion, the above decision is just based on financial implications. However, for a company to involve in long term investment, not only decide from the financial aspects, but also to consider the strategic aspect such as growth potential and competition.