Selecting right partner in forming international joint ventures management essay

Over the past twenty years, there has been a surge of interest of companies coming together, many of which were reflected in the popular management press and the academic journals of corporate links being formed. Many organisation now uses strategic relationship rather than competition among themselves to grow their business. These are formed for a variety of reasons, which include new technology development, expansion to new domestic market, reducing manufacturing cost, new product development, ability to increase profit margin, financial support and sharing of economics risk, overcome legal and trade barriers and many more. These are some of the reasons why collaboration sometimes called partnering, alliances or joint venture among many terms are formed. Joint venture is one of the most popular forms of strategic relationship and it utilises separate business entities like cooperation, limited liability company or partnership, this entity makes the involved parties to limit the liabilities involved. In recent years global challenges has fostered many companies from many countries to go into international joint venture more stronger than in the past, manufacturing companies, oil and gas companies, construction companies, banking sectors, automobile companies and many more are forming the international joint ventures.

Objectives

As partner selection is considered to be very important to have a successful collaboration, this module will be focusing on selecting the right partner in forming an international joint ventures. The answers will be focusing on the literature on how to select a good and successful partner when forming a joint venture. Also the following factors will be considered in forming a successful collaboration:

The main characteristics to look for in a good collaborative partner, selection criteria and the strategic, political and tactical implications.

The factors that's determines the good partners match in collaboration.

And what the two companies going into collaboration can do to create good partnership condition.

Literature review

introduction

As it was started in the objectives in the previous chapter, this report will be discussing various factors that are needed to be highly considered in selecting a partner when forming international joint venture, but before going further below are the definitions of some common terms of collaboration.

Some Basic Definitions

Collaboration

Different companies go into collaboration with different reasons, and the reason why many companies go into collaboration is to try and gain competitive advantage, entering new market and many more. Collaboration accomplish shared vision, achieve positive outcomes for the audience involved and it also build interdependent system to address issues and opportunities. It is a world in which almost anything, in principle, is possible since you are not limited by your own resources and expertise only but by tapping into resources and expertise of others. (Huxham and Vangen, 2005). Members of the collaborations needs to be ready and willing to share their vision, mission, power, goals and resources to achieve success.

Also Collaboration is the act of working together to create or produce something for mutual benefit. (Oxford Advanced Learner Dictionary, 2001).

http://ayanthianandagoda. files. wordpress. com/2009/07/collaboration. jpg

Fig 1 collaboration

Source : http://ayanthianandagoda. files. wordpress. com/2009/07/collaboration. jpg

Joint ventures

There are many different definition for joint ventures, as experts opinions differ significantly.

A joint venture is a strategic alliance formed by two or more parties usually in businesses, partner together to share markets, assets, intellectual property, knowledge and profit. (Valerie, 2006).

Stephen et al.(1993) consider joint venture as a form of collaboration. He later defined it as a distinct business entirely created and jointly owned by two or more parent organisations.

Robert L . Wallace (2004,) defined joint venture as the coming together of two or more independent businesses in which both of them have sole purpose of achieving a specific outcome that might be difficult for each of them to achieve individually.

http://www. internationaltradelaw. org/images/partnership. jpg

Fig 2 joint venture

. Source : http://www. internationaltradelaw. org/images/partnership. jpg

International joint ventures

When joint ventures crosses across the border, it becomes international joint ventures. International joint venture is defined as the joint ventures that involve firms coming together from different countries cooperating across national and cultural boundaries. (Aimin and Yadong, 2001). At times, international joint ventures are formed by two companies in the same country but located in a country other than their parent countries. (Geringer and Hebert 1989).

Though majority involve two parent firms, one from foreign and the second one a local company. Also it may involve partners with complex nationality and cultural background. For example, Xerox Shenzhen company formed from Xerox (china) and fuji Xerox (US-Japanese joint venture in Japan.).

International Joint Venture

Fig 3. International joint venture

Source : http://t3. gstatic. com/images? q= tbn: shC_GkI4UDgeCM:

http://farm4. static. flickr. com/3504/3841640658_367ae3ab0d. jpg

Merger and Acquisition

There is a big difference between merger and acquisition, they should not be mistaken to be the same. Merger is when two companies come together to form a new company while acquisition is when one company purchase another company.

Fig 4 merger and acquisition

source : class module

Motives of collaboration

According to Ian Hewitt (2005), A company should not just go into collaboration just because other companies does, in fact different companies go into collaboration for different reasons. Below are few of the reasons why many companies does

Increasing competitive pressure : competitors or rivalries in the market is one of the major reasons that force some companies into joint venture.

Sharing cost and risk : one of the main reasons for joint venture is cost saving and risk sharing. It helps to achieve synergy through rationalizing of employment and other fixed cost, and it also research and development project like pharmaceutical, electronics, aero-engine, telecommunication and so on. Joint ventures are frequently used in capital intensive project like power stations or infrastructural projects

Entering new markets : partnering with another company already established in a particular market also helps in entering new and emergence market effectively and it also helps in marketing an existing products and service to new customers.

Total-quality-management. Do more with less : it brings about a quality management into business and help in achieving the companies objectives in less time.

Access to new technology, technology know how and customers : joint venture helps to gain access to and to learn from partner's technology , experience and skills as there is a rapid change in technology advancement day by day.

Improve access to financial resources : coming together of the two companies improves the financial resources.

Expand customer base : international joint venture also help to expand customer base in by making use of partner's strength in different geographical area and both develop a wide network.

Developing new products : a company can go into joint venture to provide new products or service to their current customers or new customer. Since it is joint venture, the companies can develop a new products to sell to their customers.

In this new wave of technology, you cannot do it all yourself, you have to form alliances. Carlos Slim Helu.

The Benefits and Risks

Having considered few of the reasons why companies go into collaboration, it may sound interesting that collaboration is everything but an extreme care need to be taken when choosing the collaboration partner. Collaboration is good (when the right partner is selected) and it is bad (wrong partner). Before going into details of selection criteria in choosing a partner, below are the types, benefit and Risks associated with collaboration.

Benefits

Increased financial resources and stability : it allows the partners to contribute financially to the project in an appropriate ways to the joint operation and it increases the financial stability of the business.

Improve buying power and economies of scale : it gives cost advantages and better purchasing power to increase the volume of business.

Expansion to new market : forming joint ventures can help in capturing a new market.

Share R & D, engineering, production costs : joint venture helps when a company is trying to enter a new field of business, by forming joint venture with a company already established in the business, it makes it easier to enter into the market. Examples include research institute and national government level.

Shorten lead time : collaboration shorten lead times and it makes it possible to achieve more in less time.

Risks

Loose overall control or desire for control : if it is not well managed, the stronger partner becomes a dominant and this can undermine the interest of the other partner and it may eventually leads to termination.

Cultural issue : the partners must understand each other's culture very well by doing an intensive research. Competent team that can negotiate in with people of different culture should be assigned to manage.

Foreign exchange risk : in joint venture, high volatility in the foreign exchange market, the movements of Dollars, Yen, Pounds, Rupee, Franc and many more cannot be predicted, and even due to this in the oil transaction, it is generally accepted in the western world to trade in US dollars.

Communication and translation problems : multinational project can become more complex if there is communication problem, and it is even better to have a translator or even two translators.

Loose identity : individual company can lose their identity and they may end up in forming a new name and old customers loyalty may be lost, though if the partnership is well managed it will create new customer loyalty.

Partner's failure : if the partner failed to deliver, this mat cause a serious consequence or termination to the contract while the objectives have not been meant.

Types of collaboration

There are many ways in which collaboration can be formed, depending on the common objectives of the companies involved. Collaboration can be grouped into two namely : those defining the structure of the relationship and those defining the technical or commercial purpose of the relationship. Below are few types of collaboration that can be formed.

Purpose

Research Collaboration : which is most effective in scientific research and high technology new products.

Joint Design and Development : involves two or more companies coming together to share the risk of developing a new product and this often leads to joint or parallel production.

Joint Production : when two companies agree to produce separate sub-assemblies of the final product and this can leads to joint venture company.

Parallel Production : when same and similar product is manufacture in two or more countries and one partner leads the development of manufacturing facilities.

Licensing : formal agreement between two companies where primary company allow to use it design or know-how, or to manufacture a product and it involves payment of royalty fees. It may be of two types namely ; licensing in and licensing out, or both .

Franchising : this involves third party to market proprietary products or services under the original supplier's brand name e. g. stores and supermarkets, fast food outlets, petrol stations, etc.

Structure

Informal and Gentleman's Agreements : this can be word of mouth agreement usually between partners of common interest and trust is essential. It can be a starting point for formal arrangement.

Strategic Alliances : Michael and Srinivasa 1995) said it can be defined by simultaneously possessing the following three necessary characteristics;

Two or more firm that unite to pursue a set of goals already agreed upon

Partner firms share the benefits of the alliance and control over the performance of the assigned task

Both contributes on a continuous basis in one or more strategic areas, e. g technology and product.

It has no legal form, it is a relationship formed between two or more companies that share (proprietary), participate in joint investments, and develop link and processes to improve their performance of their companies. (http://www. apics. org/.). It can lead to creation of joint venture company.

Strategic partnership : is a form of strategic alliance in which the partners are linked by a non-controlling level of shareholding, either bilateral or unilateral. (W. J. Bacchus 2005)

Joint venture companies : this is an independent business entity, it involves ownership, operational responsibility and financial risk and reward.

As it was started in the objectives in the previous chapter, this report will be focusing on joint venture companies.

How to select a compatible Partner

Companies that are more thorough and comparative in selecting international joint venture partners are more likely to be successful. When there is a need for joint venture, choosing the right partner is another important factor. Only few companies today believe they can achieve their goals and objectives on their own but by seeking partnership with another company to stay ahead in today's global economy, So due to this, there has been an high increase in the numbers of companies coming together around the globe .

When a company is going into a joint venture, collaboration strategy need to be established. Furthermore in this report, it should be noted that a company in question will be represented by Company A and other companies that are available to choose from will be represented by Potential partner A, B, C……

The company A planning and operational stages can be established as :

1st stage 2nd stage 3rd stage

Fig 5. Planning stages

Company strategic planning

For any company going into collaboration, internal check is the first thing to consider. Internal check allows company A to analyse its performance so far in the competitive market, the knowledge and skills, financial stability and status, government policy, benefit and risks associated with joint venture, and most importantly their objectives of going into collaboration.

To properly analyse these factors, S. W. O. T analysis can be used as follows :

SWOT

Analysis

S- Strength

What makes company A to remain strong in the market, backbone of its performance so far and this is part of what will attract a partner to go into joint venture with company A.

W- Weaknesses

Where they have been lagging behind, and affecting the company performance, it may be new technology innovation, lacks of skills or experience staff, inadequate training, breaking into new market and many more.

O- Opportunities

Opportunities can be to how strong company A is where it operates, reliability, wide network of customers, government connection, fast developing market, regional growth, license, market expansion and many more.

T- Threats

The treats can be government policy, competitors, Intellectual property right, fakes or fraud copies etc

Table 1. S. W. O. T analyses of Company A

After the S. W. O. T analysis of company A, having clearly analysed the needs and the objectives of the company, then a decision can then be made on types of strategy that will be best suited for them, either growing internally to combat the threats and weaknesses analysed while making best out of their opportunities and strength , or by sourcing for a potential partner that they both have common objectives, and make sure the SWOT analyses of the two companies complement each other. The company A’s decision can be to grow internally or to seek a potential partner of product or project relatedness.

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Fig 6. (Source : Class Module) Growth of Company A

At this stage, company A should be clear of the strategy best suited for them, and to assume that collaboration is the best. Then what type of collaboration and with what type of partner. How to maximise the benefit of collaborations and how to mitigate the risks should also be noted.

Initial Assessments of the Potential Partners

Having decided to go for collaboration (international joint venture), Initial assessment of the potential partners is very essential at this stage before going into details or make any commitment to avoid some of the risks attached to forming a joint venture, which is money and time wasting. In doing this, the following factors need to be considered :

Objectives : the objectives of the two companies should be common and complement each other.

Backgrounds : knowing about the companies background is important, knowing about their past, present and future intention records.

Reputation : integrity of the company going into business with is important as people tend to judge you by the company you keep. Check what people say about them in terms of trust and reputation and also the success of collaboration they have had in the past if there is any. There should be a clear indication that trust can be build inside the relationship.

Reliability : the company must be reliable to trade with.

Experience : also it should be checked if they have had any collaboration experience in the past, then what was the outcome of it, if it was a success or failure, What type of management team do they work?

Capital : they must be financially secured and they do not have credit problems and free from debt .

Culture : the culture of the potential partners must be well read and understood. In international joint venture, cultural issues need to be taking care of as different cultural background sees contracts different ways.

Structure ; also the structure in which they operate must be understood, also their mission, vision and values must be clearly considered and check if the joint venture can work.

Performance : the way they perform in the market is also important, their level of performance in satisfying their customers and suppliers also need to be considered. Their production performance is also important.

Product : the brand value should complement each other .

These are the characteristics to look for in a potential partner and these factors can be known by checking the websites of the potential partners, company magazines, company reports (quarterly, mid-year, or annual), journals, trade publications, consultants, investment banks, collaboration track records, their suppliers and customers, ex- employee, newspapers and/or from the proposal sent from the potential partner.

Tactical planning

The next stage is the tactical planning and analysis, it is one of the most important aspect to consider when selecting a partner, having gotten SWOT analyses of your company and all the companies involved.

Analyses

Company A

Potential partner A

Potential partner B

S- strengths

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W- weaknesses

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O- opportunities

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T- threats

Table 2. S. W. O. T Analyses Comparison

These allows to compare the general features of each of the potential partners with company A's S. W. O. T analysis to check which ones complement each other , and to make initial consideration of the company that can be collaborated with.

Key issues and objectives at this stage need to be analysed from these S. W. O. T analysis, and the type of options each company can offer in terms of working together. If collaboration is the best, then what type can be the best for each of the potential partners. Which partner share the common strategy with company A. Also what can be the benefits and risk of forming joint venture with each company need to be carefully accessed.

Also at this stage, evaluation and initial assessment of most suitable partner attributes is next. Then the objectives must be clearly defined . it must be S. M. A. R. T.

S- Specific

M- measurable

A- achievable

R- realistic and

T- time bound

The following factors are must be carefully considered when selecting a partner :

Cultural issues

In international joint venture, cooperation between different partners of different cultures can be a major challenge. In America tends to be individualist and not group oriented but unlike the Japanese that practices collectivist and are group oriented. Aimin and Yadong,(2001), Said one partner may impose its cultural values and norms on the other partner without even consider what the latter attribute might be. And later said that Americans are not very good in learning from their partners as Japanese does, so many foreign companies uses joint venture as an easy way of gaining access to America market and technology. And apart from the national culture, company operational culture need to be well access and make sure that there is compatibility in organisational and management practices with potential partner.

Other factors that need to be taking into consideration about cultural issues when forming an international joint ventures are :

Language : the language of the contract must be well understood. Since it is international joint venture, it is most likely that the companies comes from a very different nationality, so there must be a common language agreed upon to be used in meetings. Moreover if it is difficult to communicate better in that language, then a competent interpreter that can easily understand the two languages can be used and to be more clear and perfect, two interpreters can be used. The language must be well understood with no hidden agenda.

Negotiation : negotiation in international joint venture require a very good management team in order to be successful. The strength and success of o joint venture depends on the interactions of its people. The team must have the experience, skills and attribute it takes to manage joint venture or people with moderate experience but motivated and committed to gain more knowledge. The management team consider the following factors ;

Possible outcome : it is essential to outline what the possible outcome of company A and even the potential partners can be. Either it will be a win-lose or win-win approach or mixed.

Alternative to agreement : also Company A need to have in mind what can be the best alternative to what they have already agreed on, and also what can be the best alternative for the potential partners as well. Then Company A should find a creative ways to strengthen their own and weakens their partners alternatives.

Contract termination : there must be a clear agreement on how to terminate the deal and the price at which any of the companies can breach the deal must be set and estimated for each company.

Records keeping : proper record is essential in international joint venture and at the end of every meeting, they need to check what they have already agreed on and what is still open to be discussed.

Build trust : the team must be very open, ask many questions for clarity, show respect and highlight complementary need and interest.

Resources : a company going into collaboration might not have the full resources require available to meet the demand and may need to tap resources from the joint venture partner. Resources can be human (people), skills and training, technology, raw materials, manufacturing facilities and so on. It must be ensured that the there will be availability of full resources.

Political issues

The partnership should be checked if it is politically accepted in each country and political risks should be considered.

It is possible for the international joint venture to be affected by the political events or political instability in a host country. Also when there is a change in political relationship between the two countries, it may also have an implication on the joint venture. The system of government of the host country, political stability, laws and regulations, existence of other governing bodies must be taken into account.

In order to plan ahead of any unforeseen political risk, an insurance policy need to be done and there must be an agreement on financial and operating policies.

Financial issues

This is another critical aspect of joint venture, it is very important in choosing a joint venture partner. There must be negotiation and the involved parties should agreed on the financial requirements.

Financial status or position of all parties involved, debt etc. should be checked

Partners market credibility : the market credibility of all the potential partners should be considered

Partnership records : their financial performance in the previous partnership they had in the past.

Capital contribution : the percentage of capital contribution of each partner should be clearly stated

Raising capital : in case there will be a need to raise capital, this can be overdraft, short or long loan, government sources etc. likely source must be outlined

Working capital : the capital needed while working must be agreed upon

Shareholding : the ownership right of each company should be stated and clear

Financial management structure

Transaction risk : to avoid transaction risk due to unstable foreign exchange market, trade in home currency or open foreign bank account in the country where the partner comes from. E. g if companies from US and Uk form a partnership, there can be a an account in US Dollars and another in Pounds Sterling to run the project.

Taxation (import and export) : different countries with different tax policy, it is very important to discuss the percentage of taxation in the country, the import and export rate

Board of directors : the board of directors should be decided.

Chairman : the chairman of the joint venture must be decided

Governance : the rule of the countries to govern the joint venture

Role definition : each party role must be stated clearly

Profit share : the percentage of sharing profit between the parties must also be agreed upon.

Inflation : possible solution in case of inflation in any of the countries must be taken into account.

Resources availability : resource availability in terms of assets, equipment, rent, intellectual property right must be well planned.

Legal issue

In joint venture company, legal agreement is essential and this can be by word of mouth, gentlemen's agreement, memorandum of understanding (MOU), detailed specification, evergreen, full contracts and many more (class module).

In international joint venture, the following issues must be considered

Governing law : the law of the country to govern the contract must be agreed upon.

Payment method : there must be an agreement on the type of payment method accepted.

IPR : the right of each partner in terms of Intellectual Property Right must be stated. Patent right, copyright, trademarks etc must also be considered.

Termination : it should be stated under which condition can any partner terminate the contract. Common events that terminates contracts are

When the contract expires

Change of goal of one of the partners

Breach of contract by any of the parties

Financial or legal issue.

Responsibilities : what is expected from each party need to be understood

Financial right : they must know their financial right.

Veto power : there must not be a partner enforcing power on the other

Communication : the way in which communication will be transferred from place to place must be addressed.

Managerial right : the level in which each company will operate in terms of management must be stated.

Capital : what each partner will contribute and what they will get out of it in terms of profit, product etc

Transfer of share : there must be a mutual agreement on the share transfer, normally the parties entering into a joint venture is not expected to transfer its share to third party without the consent of its joint venture partner.

Agreement : the management team must ensure that there is a proof of agreement between the partners.

Language : the language of the contract must be plain and well understood by the joint venture companies.

Criteria for selecting a partner

Clear definitions and Common Objectives : select a partner that brings no hidden agenda when negotiating with them, the objectives must complements each other and there must be an evidence that the parties need each other, the language of the contract must be well understood.

Strategy clarity and compatibility : the strategy of company A and the potential partner must be very clear, well understood and compatible with each other.

Financial strength : it is advisable to partner with a company that has a very strong financial base as it was explain in this module.

Mutual benefit : win-win attitude and approach is the ideal for the joint venture partner there must be a low risk of either of the partners becoming a competitor.

Previous track records : it is not advisable to go into joint venture with a company that has a poor track record in terms of partnership, financial or customer’s satisfaction.

Management :

Culture compatibility : as different companies from different countries operates on different culture, there must be a clear understanding of the potential partner culture in compatible the your

Compatibility of CEO’s and Senior managers

Market power : how strong the potential partner are in the market, customers satisfaction, suppliers relationship

Overseas experience : the experience they have in doing business outside their parent country, how it was managed and the success stories they have had in the past.

Product relatedness : the products of the joint venture companies must supplement each other, there must be product relatedness.

Proper match : there must be proper match in terms of objectives, strength, weakness, opportunities, weakness, culture, financial capability, product relatedness, strategy and so on. There must not be gaps left behind or overlook.

Common Objectives

Strength

Strength

More opportunities

Less threats