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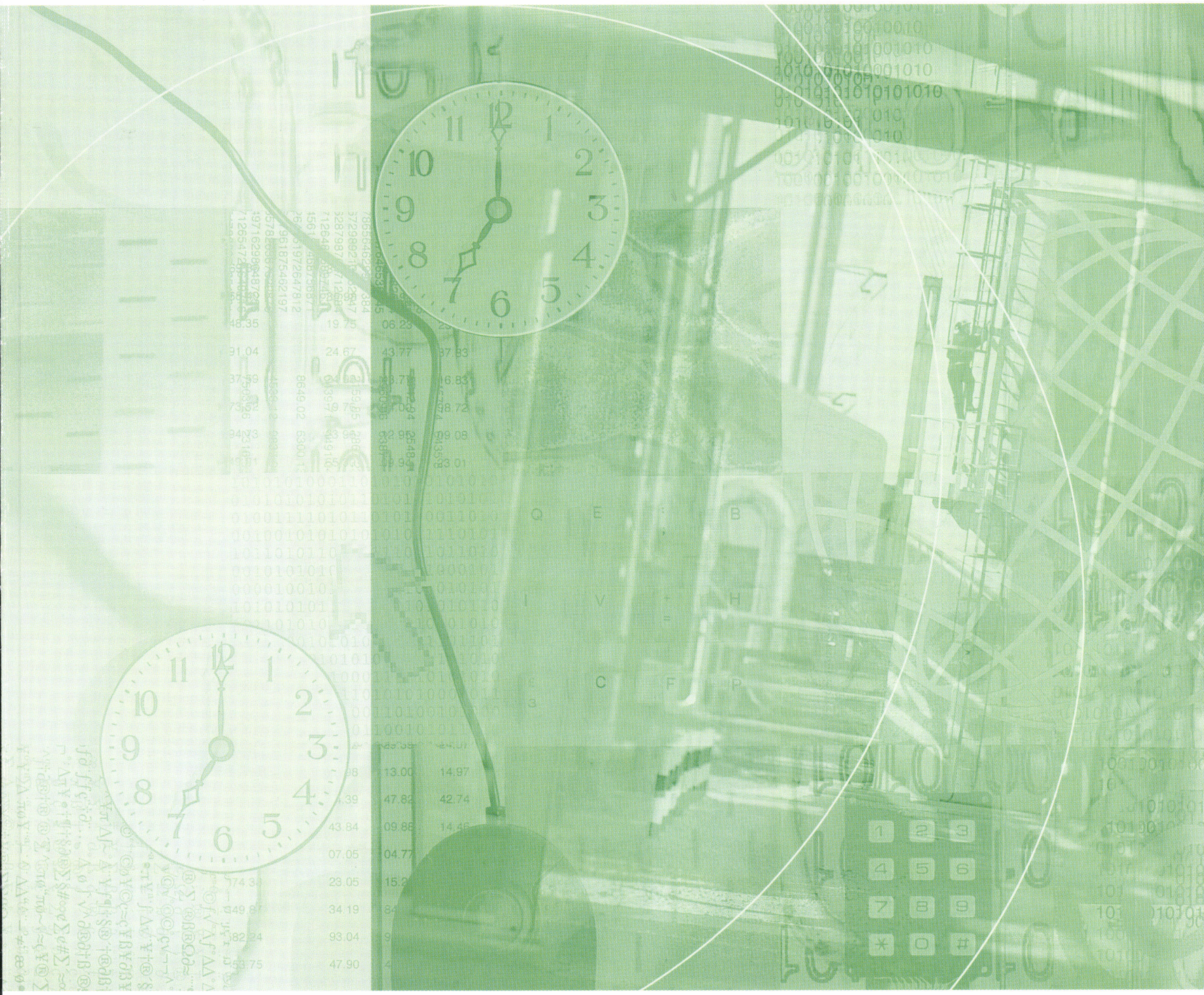
TRAINING PACKAGE ON INVESTMENT AND TECHNOLOGY PROMOTION

Joint ventures and strategic partnerships



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TRAINING PACKAGE ON INVESTMENT AND TECHNOLOGY PROMOTION

Joint Ventures and Strategic Partnerships

UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION
Vienna, 2004

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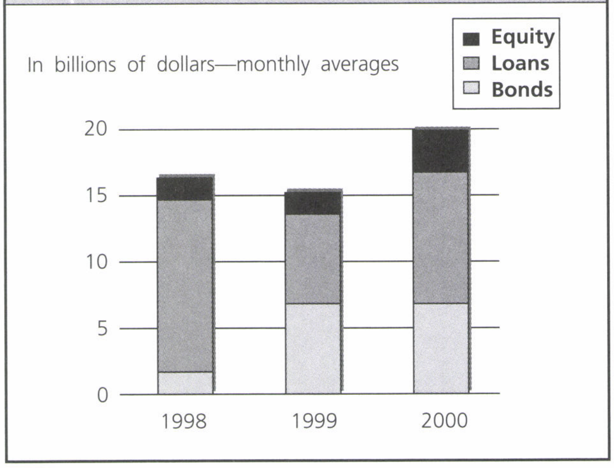
INTRODUCTION

There are three major factors currently changing the world economic system. They are the globalization of markets, the rapid diffusion of information technology and foreign direct investment (FDI). FDI continues to expand rapidly, enlarging the role of international production in the world economy. Global investment flows have been one of the major forces driving change during the last 10 years. The average monthly flow of FDI to developing countries has reached US$20 billion as shown in figure 1.

Figure I. Gross capital market flows to developing countries

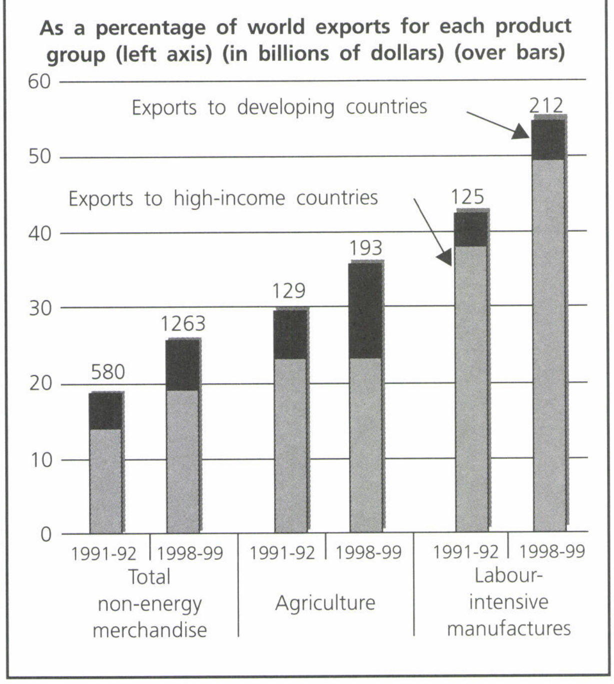


Source: World Bank, *Global Economic Prospects 2002* (Washington D.C., World Bank, 2002).

FDI has been a major determinant of economic growth in developing countries as well. With the conclusion of the Uruguay Round there has been a wave of unilateral reforms. Barriers to trade have fallen substantially around the globe, driving world trade. At the same time, developing countries as a whole gained significant market share in world trade as shown in figure II.

At the same time, the gap in income between developed countries and developing countries increased over the years. FDI has turned out to be one of the major routes for inducing growth and enhancing market access. The combined effect of globalization and the increase in FDI has been the intensification of competition. Such an increase in competition,

Figure II. Increased share of developing countries in the global market



Source: World Bank, *Global Economic Prospects 2002* (Washington, D.C., World Bank, 2002).

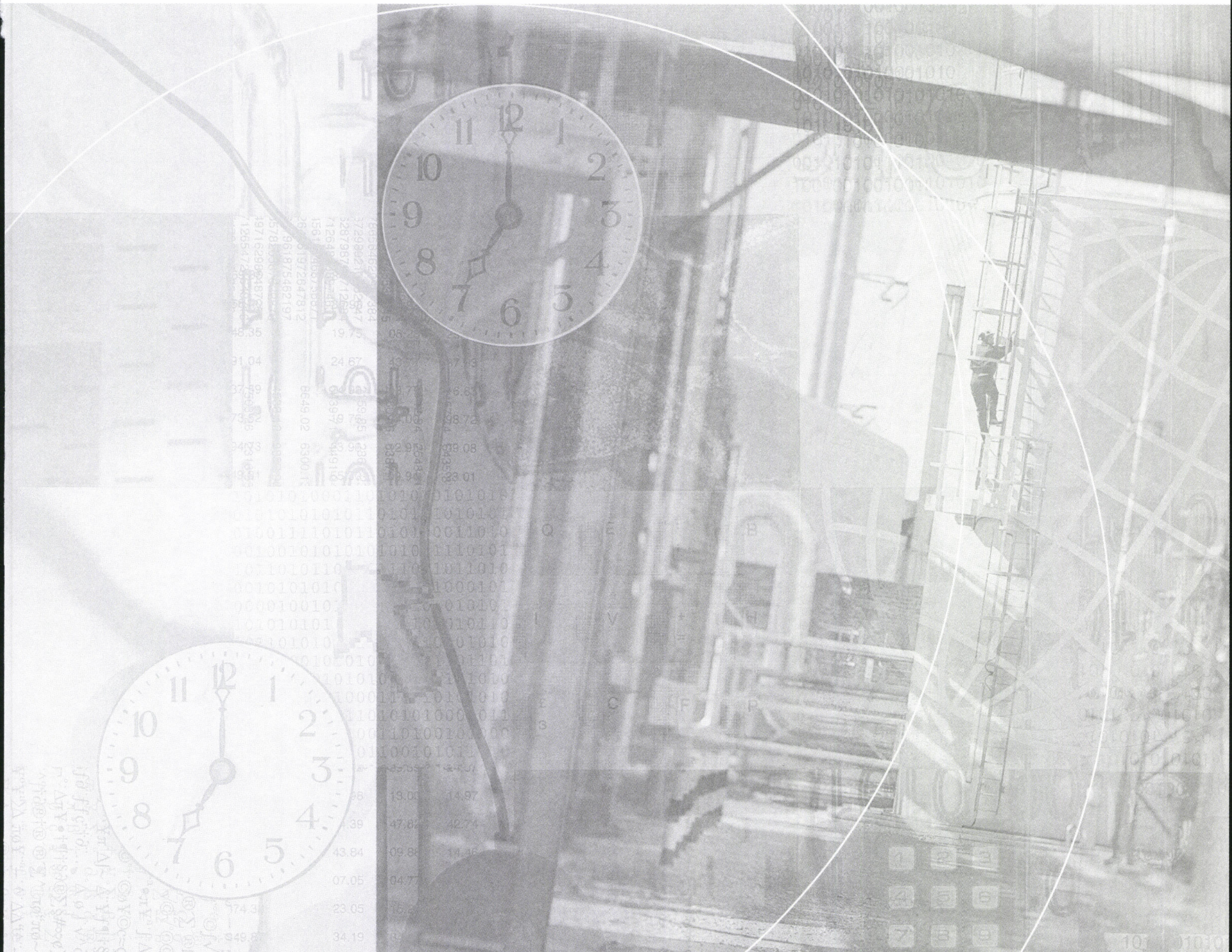
paradoxically, has given rise to increased cooperation among firms as a means of coping with intense competition. Such forms of cooperation have been broadly termed "strategic alliances". Recent years have witnessed a surge in formation alliances among firms throughout the world. The formation of large firm-large firm alliances, large firm-small firm alliances and small firm-small firm alliances are being observed increasingly. Hardly a day goes by without announcements in the business press of new linkages, partnerships or alliances. Whatever they are called, such inter-firm relationships involve partners from various parts of the world and cover a range of functions and activities. Partnering is likely to be crucial for growth in every economic activity.

The present module provides a manual on forming and managing joint ventures and strategic partnerships. Joint ventures and strategic partnerships are two distinct classes of cooperative forms. Joint ventures are forms that involve equity relationships among partner firms; strategic partnerships are non-equity alliance relationships. The term "strategic alliance" is used broadly to cover all inter-firm cooperation arrangements. The term "strategic" is used to indicate relationships formed between or among firms in direct response to major strategic challenges facing the partner firms. Joint ventures are forms in which two or more firms form an equity shared structure. On the other hand, strategic partnership agreements are cooperative forms in which firms work together to further the common interests and goals without equity. The present module deals with both forms of cooperative relationships. In the present module, when the term "alliance" is used, it covers both types: joint ventures and strategic partnerships. Only the negotiating and implementing aspects will be different for the two forms.

The structure of the manual is given below:

- Concepts (section 1)
- Types of inter-firm cooperation (sections 2-5)
- Selection of partners (section 6)
- Negotiating joint venture and partnership agreements (section 7)
- Implementing and managing cooperative arrangements (sections 8-10)

SECTION 1. CONCEPT OF COOPERATION



SECTION 1. CONCEPT OF COOPERATION

One of the major consequences of the increase in competition has been an increase in the formation of partnerships to counter competition. Although inter-firm linkages are clearly not unusual, the "new" strategic joint ventures and strategic partnerships are different, perhaps most strikingly in the seeming readiness of firms that have long shunned joint ventures or close collaboration with other firms in their core business areas to enter into such arrangements.

1.1. Logic of cooperation

When competition increases, the only way to improve competitive strength is to network and cooperate with others. Large firms are not flexible enough to respond rapidly, whereas small firms are not robust enough to meet the competitive pressures. Networks are structures that are responsive and resilient. Joint ventures and strategic partnerships are essentially networked structures with one or more partners. In business, there are two forms of governance, namely, market governance, involving market mediating transactions, and hierarchical governance, involving firms mediating the transactions. Strategic alliance attempts to combine the advantages of both forms of governance. Two or more partners will be stronger than a single firm. In a firm, strategic competencies are created and leveraged internally, whereas access to non-strategic assets is gained through joint ventures and strategic partnerships. Competencies and assets that are strategic but not critical can be leveraged through joint ventures and strategic partnerships. For example, a small- or medium-sized enterprise (SME) focusing on manufacturing could form a partnership with a marketing firm to increase its market reach. The alliance form of business allows a firm to focus on the core business and to access non-core competencies and competencies from partners. Alliances are, thus, forms of collaboration in which strategic assets are pooled and business risks are shared through partnering. The partnering concept is an extension of the make or buy concept. Strategic activities are carried out internally and non-strategic activities are sourced from external sources. Alliances are emerging as a viable option for firms from developing countries for enhancing competitive capabilities. The following are some of the ways in which firms from developing countries could benefit from the formation of joint ventures or strategic partnerships:

- Upgrading technologies for manufacturing by partnering
- Using the market networks of partners rather than creating their own distribution channel
- Acquiring a product technology that is proved
- Using technology licensing for a product or service
- Leveraging economies of scale by swapping products

A few years ago, alliances were perceived as an option reserved only for corporate giants. In a globalizing economy, a "go it alone" strategy no longer seems to be a viable alternative even for firms from developed countries. The focus of inter-firm cooperation is the creation of a competitive advantage through sharing of resources, pooling assets, and reducing the business risk. In a way, it is designing a win-win business strategy through cooperative action.

Box 1. Partnership between a global firm and a small- or medium-sized enterprise

Coca-Cola has entered into a partnership agreement with an SME that makes herbal products to market its drinks in the rural market. The idea is to place the product in every grocery and general store. Coca-Cola has entered into the powdered drink market with the drink "Sunfill". Sunfill will mainly piggy-back on the manufacturing and distribution strength of its partners. The strategy is to use the distribution and logistics networks of the partners to market the product where the company does not have the required strength of its own. The focus is to ensure low distribution costs through partnership. As competition increases, shared distribution networks will become increasingly common.

1.2. Concept of cooperation

Joint ventures and strategic partnerships are inter-organizational forms of cooperation through which partners could achieve their respective goals. For example, an SME in a developing country could form a joint venture with a firm from a developing country for manufacturing a new product. The SME gets the technology, whereas the developed country firm could sell the product through the SME. Joint ventures and strategic partnerships could be defined as organizational forms in which two or more firms unite to pursue a set of agreed goals while remaining organizationally independent of each other. Strategic alliances constitute a useful set of business forms but they are conflict prone as there could be problems of managerial control among the partnering firms. In a world in which globalization is increasing, both competition and cooperation seems to be increasing. It has been stated that the twenty-first century will be the century of alliances. It has been found that firms from developing countries can use joint ventures and strategic partnership options to grow faster, in terms of both large firms and SMEs.

1.3. Importance of cooperation

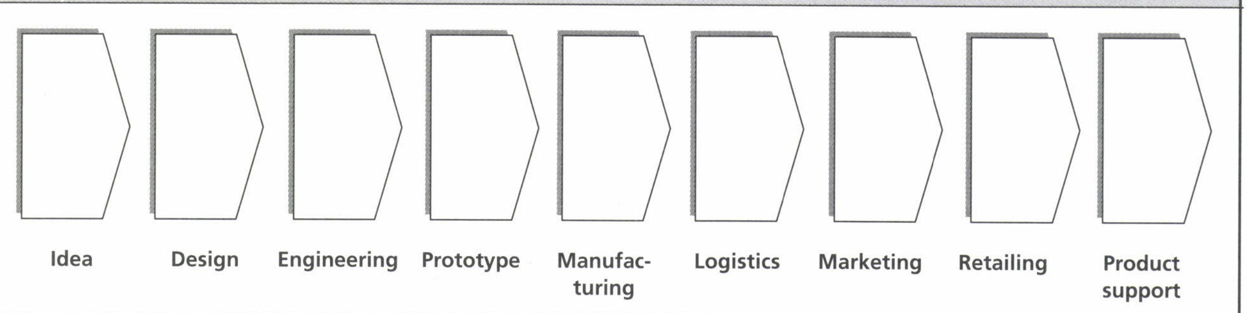
Any business could be conceptualized as a value chain. A value chain represents how value is created in a business as one moves from concept to design to manufacture to service delivery, as shown in figure III.

Cooperative action helps in enhancing both the speed and depth of response. A firm with strong manufacturing skills can form a joint venture and strategic partnership with a firm that has strong marketing skills, thereby creating synergy and sharing risks. The Pillsbury Company of the United States of America has joined to form a joint venture with Godrej Foods, which is a marketing firm with a strong distribution chain in India. Processed foods are manufactured by the joint venture and distributed through the distribution channels of Godrej Foods. Both firms benefit from such a multifaceted cooperation. Technology is obtained from Pillsbury. The manufacturing is done by the joint venture under the license from Pillsbury. Godrej markets the products with the Pillsbury brand name.

In joint ventures, both partners have an equity relationship. The equity issue with respect to financial return as well as managerial control comes up in joint ventures. Thus, in joint ventures, managing relationships and structure become an important additionality. Managing joint ventures and strategic partnerships has become a major concern in industrial development. It is reported that there are 60,000 transnational corporations working through joint ventures for expanding businesses and creating new markets across the globe. Joint ventures and strategic partnerships are becoming one of the most viable options for firms to exploit global business opportunities.

Non-equity alliances are essentially strategic partnerships. An example is the operational alliance be-

Figure III. Business value chain



Box 2. Shifting to value adding partnerships

Arvind Mills Ltd. is one of the high technology textile producers from India. It decided to move away from a buyer-seller relationship with its customers to building strategic partnerships with major brands worldwide. The firm has decided to change its business strategy. It will provide a range of cutting-edge fabrics that are expected to lead international fashion trends. Fabrics manufactured by Arvind Mills Ltd. are sourced by internationally acclaimed brands such as Tommy Hilfiger, Gap, JCPenny, Polo Ralph Lauren, Banana Republic, Allen Solly, Benetton and Lee. The change in relationship is in tune with the "fibre to fashion" focus. The mill has produced a variety of new fabrics, such as:

- Performance finish fabrics with micro coatings that are water and oil repellent
- Teflon finish that is fragrant and anti-microbial
- Natural look fabrics
- Stretch fabrics

Strategic partnerships help in smoothing out the requirements, as production has a lead time of a year. The focus of Arvind Mills Ltd. is new product development in keeping with the latest fashion trends. Arvind Mills Ltd. has invested heavily in high technology. It started a dedicated design and development centre with an investment of US$400 million and its product range covers more than 150 different products. Strategic partnerships are non-equity long-term relationships that involve joint work, mutuality in relationships, close cooperation and information exchange. As competition is becoming global in nature, partnering is also becoming a global phenomenon.

tween international airlines such as Malaysia Airlines, KLM Royal Dutch Airlines, Northwest Airlines and Kenya Airways. There is a code-sharing operational agreement that allows them to work as a single global airline system. That again is a win-win-win-win arrangement, in which they share the infrastructure and use an integrated baggage handling system to provide customers with a single airline system.

Most developing countries are primary commodity exporting countries. High technology exports originating from developing countries continue to be a small fraction of the total global high technology trade. Developing countries have to deepen their mastery over emerging technologies. To do that, the firms from developing countries need to attract FDI, enhance technological capability, upgrade manufacturing facilities and increase market reach. Joint ventures and strategic partnerships seem to be the most effective options for that; they facilitate the learning process. Both joint ventures and strategic partnerships help firms operating in developing countries to move up the value chain by acquiring the technologies and also by acquiring managerial competence needed to meet the competitive challenges in the globalized context.

1.4. Uses of inter-firm cooperation

Both joint ventures and strategic partnerships can be used for a series of business purposes. The activities in which cooperative arrangements could be used cover a wide spectrum including:

- joint marketing: one firm forms a joint venture or a strategic partnership with another in order to market a product in one or more countries
- Private label: one firm produces a product for sale under another firm's label
- Licensing: one firm provides know-how to another company for payment
- Original equipment manufacturing: one firm manufactures a product to be sold as original equipment by someone else
- Cross manufacturing: one firm manufactures a product and swaps it with a product that another firm manufacturers
- Technology transfer: one company transfers knowledge of its technology and the right to exploit it to another company for cash payment or other value
- Research and development (R&D) partnership: two or more companies join for the development of a new technology and/or products for mutual exploitation

- Equity investment: the purchase of part of one company's equity by another company for cash, stock or other consideration

- Joint venture: two companies cooperate in creating a new business entity in order to reach mutually compatible goals

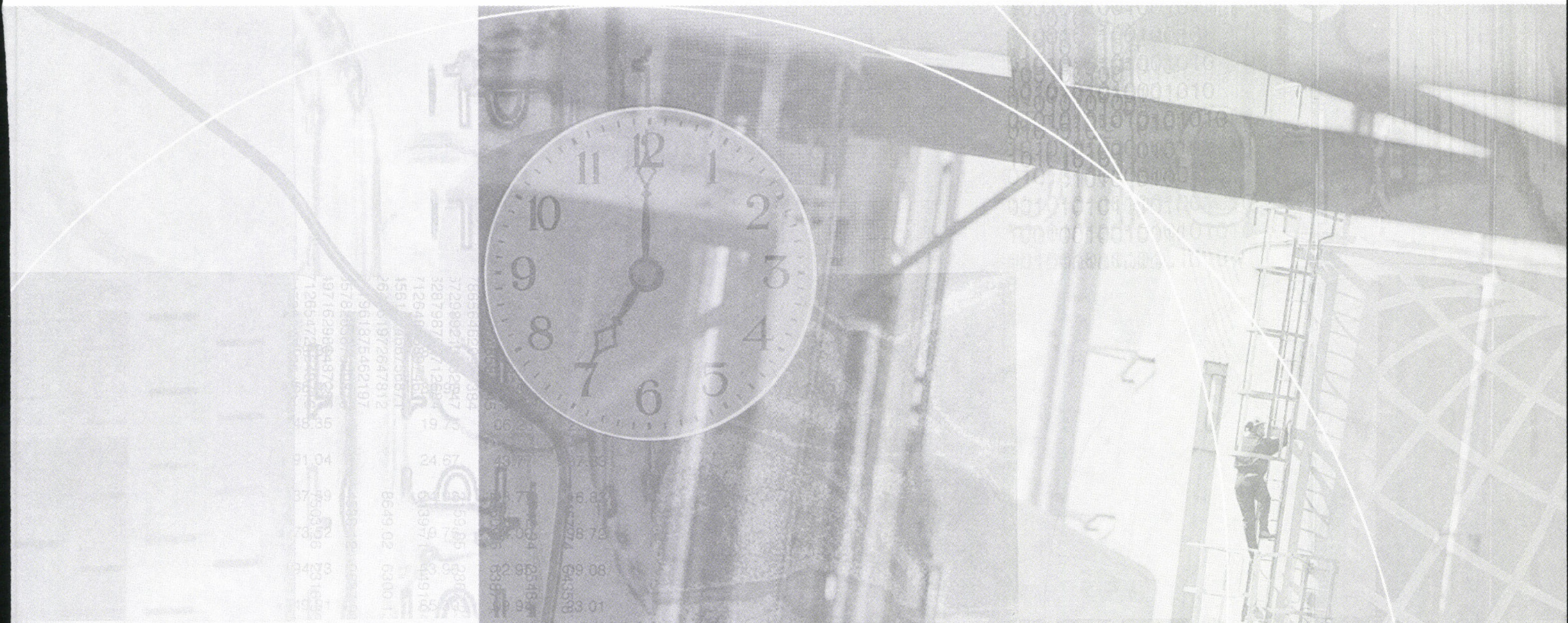
Of the activities listed, only the last two may involve an investment. Others could be achieved through strategic partnership agreements. Strategic partnerships are essentially operational protocols and are less difficult to manage. A joint venture is more difficult to manage as it involves investment and managerial control issues.

Both joint ventures and strategic partnerships are used for achieving a variety of purposes:

- To obtain product knowledge
- To obtain know-how for a licensed product
- To gain access to the market network of another firm
- To transfer process technology
- To swap products in different markets
- To develop a new product jointly
- To market a product
- To share production or testing facilities
- To create new competencies.

The term "alliance" covers a variety of forms of institutional cooperation. One of the definitions states that an alliance is a strategic or tactical relationship entered into for the mutual benefit of two or more parties who have compatible or complementary business interests and goals. The emergence of competition has given rise to a sea change in thinking about joint ventures and strategic partnerships. Conventional thinking and the new perspective on joint ventures and strategic partnerships are very different. Both joint ventures and strategic partnerships are considered a major instrumentality that could facilitate efforts of a corporation to achieve its strategic intent. The focus of cooperation today is on achieving competitiveness and cooperative knowledge creation. Growth of joint ventures and strategic partnerships are being facilitated by the diminishing cost of communication and the emergence of networking technologies.

SECTION 2. TYPES OF COOPERATIVE RELATIONSHIPS



SECTION 2. TYPES OF COOPERATIVE RELATIONSHIPS

As indicated, joint ventures and strategic partnerships encompass a variety of institutional forms or formats. The format of cooperation will depend on the business needs. If technology is closely held, then joint venture is likely to be the only acceptable form. All the possible inter-firm links are given in figure II.

There are essentially five categories of inter-firm cooperative arrangements, namely:

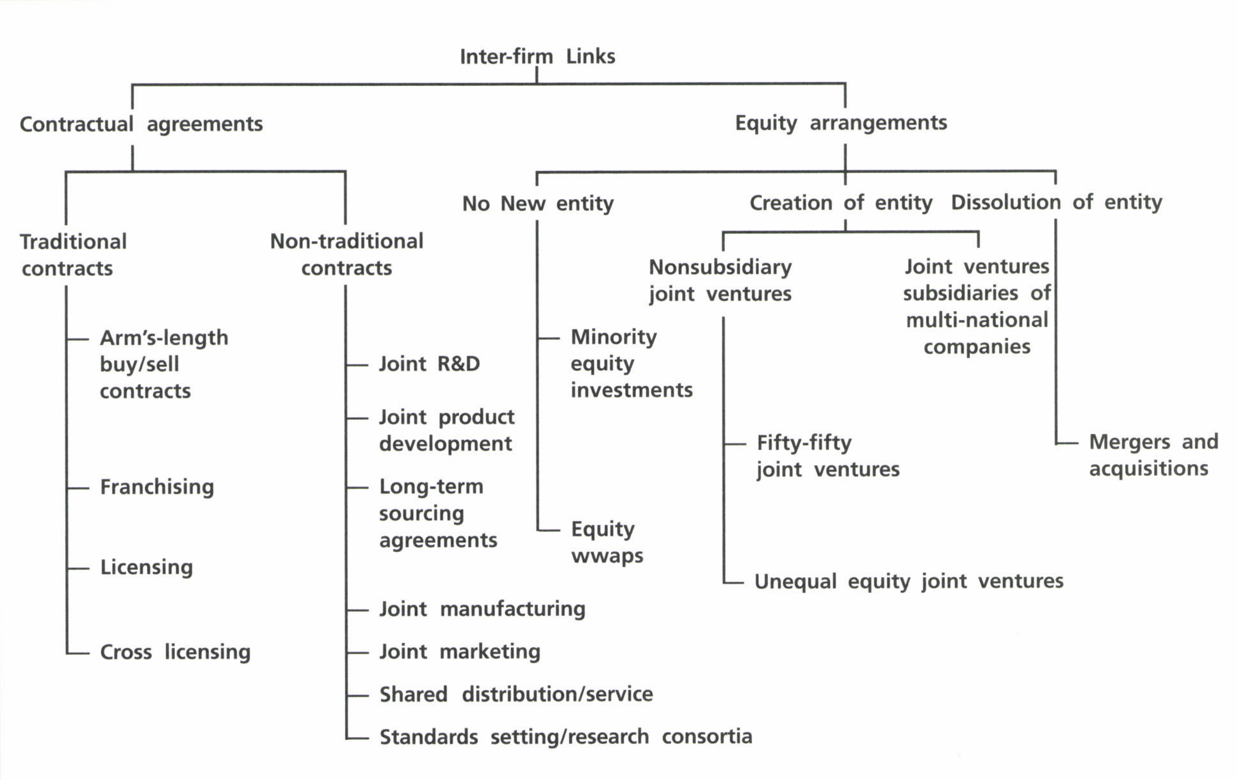
- traditional contracts
- non-traditional contracts
- equity arrangements in existing entities
- creating new entities
- dissolution of entities

The first and the last categories are not considered strategic partnerships or joint ventures. The following section explains the three possible varieties of cooperative relationships.

2.1. Non-traditional contracts

There are seven purposes for which strategic partnership agreements are used. No equity arrangements are envisaged under such a class. They could be considered as extending conventional contracts by adding certain aspects such as mutuality, trust, profit sharing, joint working, training, etc.

Figure IV. Inter-firm links and alliances



Source: M. Y. Yoshino and U. S. Rangan, *Strategic Alliances, Harvard Business* School Press, Boston.

Joint R&D

Two or more firms undertake R&D jointly, essentially to share risk and to pool resources. It could also be done to reduce the development time. In such a case, the partners need to maintain confidentiality. The output could be used by all, or one partner may have the exclusive right as decided upon in the original agreement. For example, Toyota has entered into a strategic partnership agreement with the Indian Institute of Chemical Technology for enhancing the protective power of coatings. They have entered into a time-bound agreement that has a non-disclosure clause so that only Toyota has the right to R&D results. Previously, most of the R&D was done within the firm. Now that competition has increased, firms focus on core themes and other aspects are procured from specialized firms.

Joint product development

In such an arrangement, two or three firms join together for product development. One of the most striking examples is the strategic partnering of Toyota and Peugeot, although they are competitors. The car will be jointly developed as a common platform. Joint product development reduces the cost of product development, shortens the cycle time and facilitates pooling of resources. In recent years, there has been an increase in the number of new product agreements. In the context of developing countries, it could be for customizing a product for a specific market. It is a flexible arrangement, if future options are assessed correctly before entering into the agreement.

Box 3. Technology development partnership

QualCore Logic Inc is an SME specialized in the design of embedded systems. Sequence Design Inc. is a company based in Silicon Valley that works on "system on chip" design. These firms have formed a partnership. The partnership will help Sequence Design to expand and develop leading edge technologies in the areas of power management, signal integrity and timing closure. Chip design for electronics, networking equipment and personal computers is becoming global in scope and there is a need to work with specialized firms. QualCore Logic is specialized in electronic design automation and will help in generating and validating the chip library. QualCore will be able to increase the functionality of Sequence Design's products by applying the tools to actual design.

SMEs can benefit enormously through the use of the partnership concept. Partnerships help to expand markets and both partners benefit from the partnership. Cost of innovation is lower in the case of Sequence Design, because of the use of strategic partnerships, and they have been able to reduce the product development cycle time.

Long-term sourcing agreements

The third non-traditional contracting arrangement is for long-term sourcing. Many multinational firms are sourcing components from firms based in China, India, the Republic of Korea, South Africa and Thailand. For example, General Motors sources all radiator caps and high tensile strength fasteners from a firm in India: Sundaram Fasteners Ltd., the first company from India to be given the ISO-9000 certification. The company was able to supply components with zero defects. For the last four years, Sundaram Fasteners Ltd. has been given the best supplier award by General Motors. The scope of outsourcing has increased over the years and sourcing agreements are becoming widely prevalent.

Joint manufacturing

Joint manufacturing involves two or three firms sharing manufacturing operations. Grupo Diamante, manufactures for select private garment labels from the United States in state of the art installations located in Mexico. Manufacturing covers both apparel and non-apparel products. They have been able to link up through supply chain management systems so that monitoring can be done through the Internet. Joint manufacturing helps firms in achieving economies of scale. For example, Anheuser-Busch Companies Inc. has an agreement with Compania Cervecerias Unidas S.A, Argentina for manufacturing its beer. Anheuser-Busch has two international breweries (in China and in the United Kingdom of

Box 4. Long-term sourcing agreement

The Toshiba Corporation of Japan has entered into an outsourcing agreement with Semiconductor Manufacturing International Corporation (SMIC) of China. Low power static random access memory (SRAM) chips will be produced by SMIC. The production technology was licensed by Toshiba to SMIC. The low power SRAM chips are used in mobile telephones and their demand will go up in China. This strategic partnership will provide a strong outsourcing base that can manufacture a range of products. The agreement is expected to pave the way for potential technology and outsourcing strategic partnerships in other product areas. Through such a relationship, Toshiba expects to reinforce its semiconductor business in China. Subsequently, Toshiba may enter into an equity relationship with SMIC if this relationship works. SMIC has a large manufacturing facility in Shanghai that can produce SRAM, Logic LSI, analog integrated circuit (IC) and flash memories, as well as liquid crystal display (LCD) driver ICs. Outsourcing agreement covers both technology agreement and procurement. Outsourcing is one of the high growth areas in global business, in which the partners have a win-win opportunity.

Box 5. Joint marketing in China

China has a huge tobacco market. Historically, the cigarette market in China has been highly protected. Foreign nationals were not permitted to market tobacco products. Since the liberalization of the Economy in China, the cigarette market has opened up. The China National Tobacco Corporation (CNTC) uses a variety of organizational forms for marketing tobacco products in China, using both joint ventures and non-equity partnerships. The foreign partner does not have to set up a distribution network. China accounts for about 37 per cent of the world's tobacco leaf production, and generates 31 per cent of the world's cigarettes. Philip Morris International entered into a number of joint ventures with CNTC to grow tobacco as part of an agreement to produce and sell Marlboro cigarettes in both domestic and foreign markets. R. J. Reynolds Tobacco Company has built a cigarette factory as a part of a joint venture with CNTC to produce 2.5 billion cigarettes including Camels, Winstons and Golden Bridges. Other foreign companies have been involved in many marketing agreements, importation of high-speed cigarette making equipment and construction of tobacco processing facilities.

Great Britain and Northern Ireland). In 10 countries, it manufactures through strategic partnerships. The quality is maintained as the production is under the direct supervision of Anheuser-Busch brew masters.

Joint marketing

Joint marketing is the marketing of a product by another partner or partners. It has become a widely prevalent institutional form.

Shared distribution and/or services

Sharing a common facility or sharing a distribution channel helps in reducing the cost by dividing it over a larger number of transactions. It is like two organizations sharing a common executive aircraft. Such an arrangement has become very common, especially in areas where investment requirements are substantial. A car manufacturer and a petroleum company can use a common dealer service. Two non-competing drug manufacturers can share a common logistics and distribution channel, which is useful when volumes are low or there is a fluctuation in demand.

Research consortia

A consortium is a multi-organizational arrangement for carrying out a specific task in which each partner contributes one element. Electronics firms from Japan operate through consortia in priority areas. Such a form of pre-competitive partnerships essentially helps in enhancing the skill or resource base. The main prerequisite for the success of a consortium is an excellent operational protocol for harmonizing operational aspects. Establishment of research consortia is becoming a preferred arrangement in high technology markets.

2.2. Equity arrangements in existing entities

Taking a part equity in an existing entity so as to create a business partnership can be done in two ways: minority equity investments and equity swaps.

In minority equity investments, one firm takes a minority equity in another venture so as to create a networking relationship. For example, a fruit processing firm may take an equity alliance in a packaging firm so that there is a minimum degree of control on the inputs.

Equity swap is an arrangement in which A takes a certain equity in B and B takes a certain percentage of equity in A. Many airlines and automobile firms use such a relationship. For example, Singapore Airlines has an equity relationship with Virgin Atlantic and Virgin Atlantic has a small equity stake in Singapore Airlines. Creating a cross holding is a way of creating a partnership among the firms. Small equity share arrangements are one way of creating reciprocity in relationships among firms.

Box 6. BPL and Sanyo equity relationships

BPL Ltd. is a consumer electronics firm in India in which Sanyo Electric Company Ltd. of Japan has a minority stake. Sanyo provides audio products to BPL to be marketed in India. Sanyo also supplies certain ICs. In addition, Sanyo and BPL have another joint venture for plastic infection moulding and styling for television cabinets. To create mutuality in their transactions, BPL makes alkaline batteries under licence from Sanyo for the market in Japan. Sanyo markets part of the production in Japan and the remaining is exported to Europe. By creating mutuality in the relationship, they are able to evolve a long-term relationship. BPL has the highest market share for colour televisions in India. The BPL-Sanyo equity relationship is one of the oldest partnering relationships and there is no conflict between the partners. It started initially as a technology transfer agreement and then it moved into a minority equity alliance.

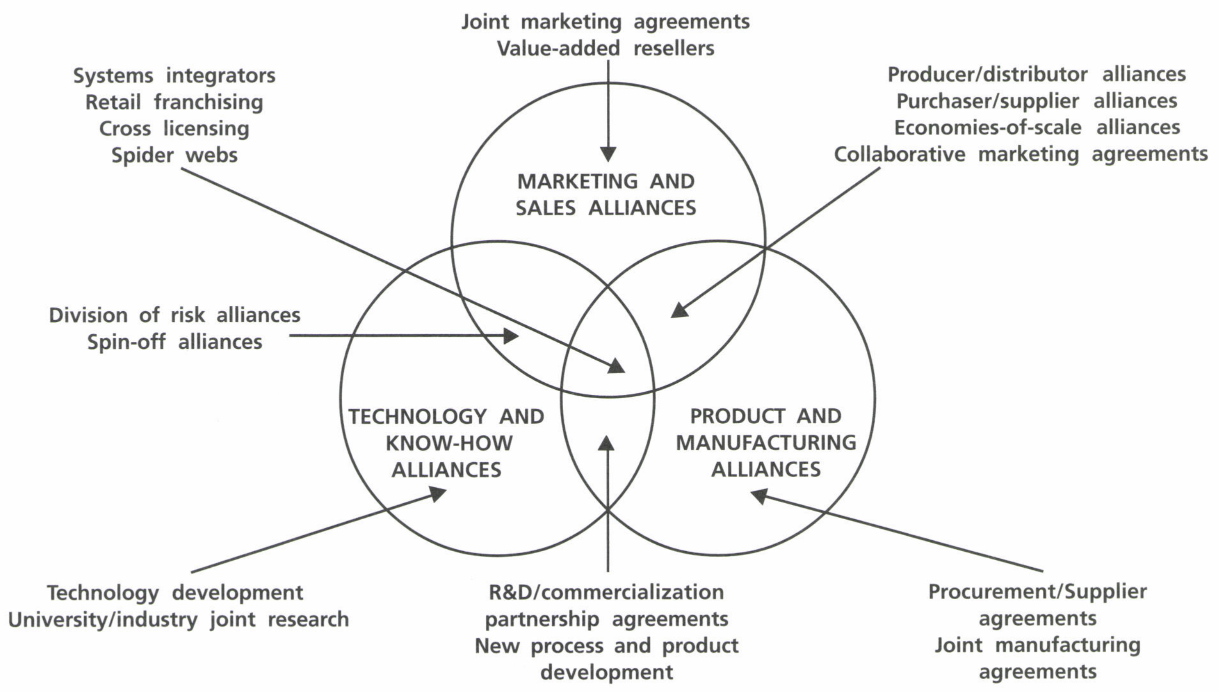
2.3. Non-subsidiary joint ventures

The third type of strategic alliance is the non-subsidiary joint venture. In such a venture, both equal (fifty-fifty) equity joint ventures and unequal equity joint ventures are included. In equity joint ventures, both financial and managerial control issues need to be addressed. The importance of joint ventures will increase in the global economy as 60,000 transnational corporations are planning and operating joint ventures all over the world. Because of these, it has become essential to switch over to network structures: either equity joint ventures or non-equity partnerships. Networks are both robust and flexible. They are used when organizational costs and switching costs are high. The alliance relationship has the benefits of both. Fast response and mutuality are the two major advantages of a network relationship. Market uncertainty and technological uncertainty have been increasing, and the only way of enhancing flexibility has been to go for a network architecture. Membership in networks can easily be expanded and terminated. In network relationships, the scope can be reduced easily, unlike the scope in joint ventures and strategic partnerships. Strategic partnerships and joint ventures have become the preferred form of business today. If a network has to have strength, it needs a higher level of trust among the partners.

Advances in information technology (IT) and the emergence of Internet-based transactions have induced virtual forms of organizations to evolve. As indicated in section 1, many aspects of the value chain could be carried out virtually. Networks are virtual forms that support collaborative organizational forms. As new broadband communication technologies emerge, more and more collaborative work, distributed over many locations, is possible. The transaction costs have come down and many new interactive applications such as Internet collaborative commerce, collaborative design, collaborative logistics and collaborative product development involving many organizations, are becoming economically viable.

A variety of cooperative relationships are possible, depicted as possible alliance (joint venture or strategic partnership) candidates in figure V.

Figure V. Types of alliances



Source: R. P. Lynch, *Business Alliances Guide* (New York, John Wiley & Sons, Ltd.).

Networks have five distinct advantages over other organizational forms:

- Reduce uncertainty: networks imply developing relationships in comparison with impersonal relationships in markets
- Provide flexibility: networks are flexible as members provide for slack
- Provide speed: fast response is possible as they are less hierarchical
- provide information: networks eliminate information asymmetries as there could be multiple channels
- share the resources

To illustrate, both Intel and Microsoft are strategically powerful because of the network architecture. Microsoft has as many as 400 developers in Asia and they are able to create a large network of software developers through distributed work centres located in many areas.

2.4. Foreign direct investment and joint ventures

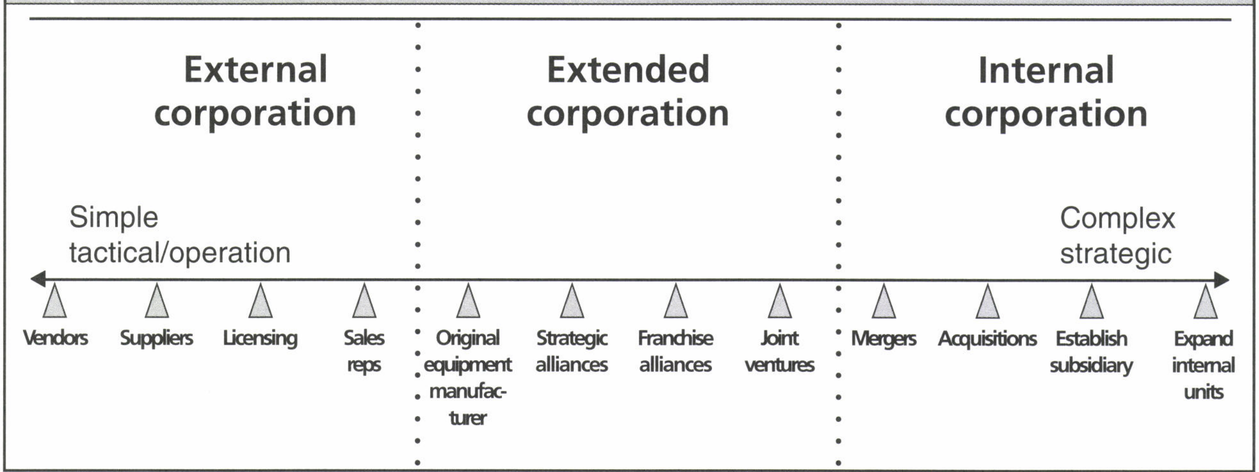
In a dynamically changing global market, firms need access to technology, capital, finance, products, markets and skills. Firms in developing countries need strong and competent partners who can provide such inputs. Deepening technological capability could be achieved faster through FDI, as shown by the experience of many countries. The differences in the efficiency with which mastery over new technologies is achieved are themselves a major source of difference in competitiveness between countries. Deepening industrial activities could take any one of several forms, namely:

- Technological upgrading of products and processes within industries
- Entry into progressively more complex activities
- Increasing local inputs and links
- Mastering complex technological capabilities within the technologies in use locally

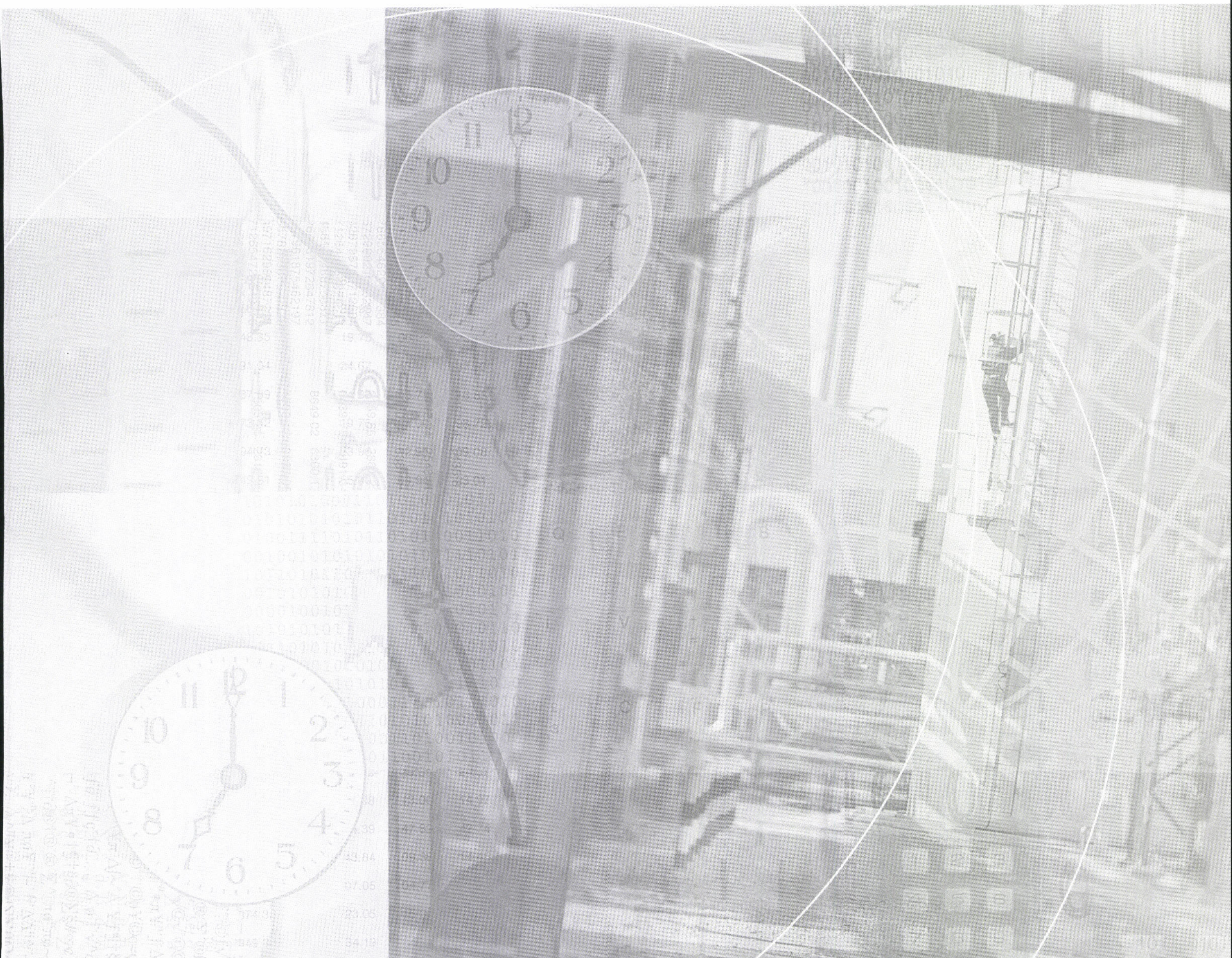
These activities are more effectively carried out through joint ventures. The experiences of Hong Kong, Japan, Province of China and Hong Kong, Special Administrative Region of China, the Republic of Korea and Taiwan show that they developed innovative capabilities by combining effectively foreign investment and indigenous technological activities to achieve higher levels of growth. China has been able to move over to a knowledge economy mostly through the judicious use of FDI. Most of the transnational corporations have started joint ventures in China.

More and more businesses in future are likely to be through joint ventures. The various modes of organizing businesses are shown in figure VI. Firms are increasingly using the middle path of investing and managing joint ventures rather than operating independent units. Globalization will increase the flow of FDI and the emergence of joint ventures.

Figure VI. Organization of businesses



SECTION 3. OBJECTIVES OF JOINT VENTURES AND PARTNERSHIPS



SECTION 3. OBJECTIVES OF JOINT VENTURES AND PARTNERSHIPS

There is now a much greater appreciation of the critical role that innovation and technological improvements play in the relative economic performance of countries. Joint ventures and strategic partnerships help in accessing innovation and facilitating technological improvements through technological partnerships. Nevertheless, it is ultimately how individual firms perform in the marketplace that determines a country's overall economic strength. Joint ventures and strategic partnerships facilitate the induction of better capabilities in individual firms. Competitiveness of firms normally comes from the four factors, namely:

- Effective use of human capital
- Technical skills of the labour force
- Managerial practices
- Government policies

Joint ventures and strategic partnerships help in strengthening the first three factors. Competing in the world market requires exploiting existing strengths, while searching for new areas of competence. That requires a deliberate strategy to keep abreast, if not ahead, of technological development elsewhere. The interactions of trade, technology and competitiveness have undergone a major change in recent years. As global competition increases, the linkages among them will increase. The world market has come to resemble a battleground where economic survival depends on the ability of producers to adapt to changing market conditions and anticipate future technological and economic trends, as well as on short-term marketing tactics and long-term production strategies. Joint ventures and strategic partnerships are both strategic routes for adapting to changing market conditions and meeting technological needs for supporting market needs. The following are five broad objectives that could be achieved through joint ventures and strategic partnerships:

- Sharing resources
- Creating networks
- Leveraging competence
- Reducing risk
- Expanding markets

Each of those objectives is examined in detail with illustrative examples.

Box 7. Market entry facilitation through joint venture

HarperCollins Publishers formed a joint venture with the India Today Group. The joint venture plans to publish a wide range of books and titles published by the company around the world to the market in India. The initiative is a part of the vision of HarperCollins to become a global publisher. The joint venture will take advantage of the printing facilities of the partner from India. The objective is as follows: it is seen as a very powerful partnership combining the strengths of a diversified and well-established media group in India with HarperCollins, unparalleled editorial and publishing capabilities. Such an example illustrates the use of a joint venture for entry into a new market. It is a win-win relationship for both the partners, as it uses the complementary strengths of them both. The joint venture helps in reducing transaction costs.

3.1. Sharing resources

Sharing resources and infrastructure is one of the objectives of joint ventures and strategic partnerships. Airbus is one of the oldest and most successful examples of a cross-border joint venture. Airbus consists of four joint venture partners that use a shared infrastructure: the European Aeronautic Defence and Space Company (EADS) is the result of the merger of Aerospatiale Matra SA of France, Daimler Chrysler Aerospace AG of Germany and Construcciones Aeronauticas SA of Spain. EADS and BAE Systems of the United Kingdom now share the Airbus equity. Each uses its infrastructure and they have been able to compete jointly and capture the market share. Sharing resources not only creates networks but leads to optimal resource use. Airbus has been able to achieve a market share of 45 per cent in 2001 and, as such, is one of the most successful cross-border joint ventures.

"A relentless assault of trust and respect is the major factor in making alliances work"
G. Slowinski

3.2. Creating networks

Another possibility is different national firms joining together to form a global network. Lufthansa, Scandinavian Airlines System, Thai Airways International, Air Canada and United Airlines Inc. (United) formed a strategic partnership with no equity relationship. For the passengers, it becomes a single airline system, whereas operationally they are independent airlines. Partners share the costs. They use an integrated baggage handling system connecting all the strategic partners. Networks have enormous potential to make savings. Strategic partnerships are creating a network of relationships in many industries and services. Air transport, telephone networks, banking networks, travel networks and tourism networks are the ones in which partnerships are becoming the order of the day.

"Cooperate to the extent necessary to create a seamless air transport system while retaining their corporate and national identities."
Delta Airlines

In manufacturing industries, strategic partnerships among supply chain partners and manufacturers have become common industry practice. Toyota was one of the first organizations to adopt the concept of the supply chain partnership. All the components are supplied by the partners with whom Toyota has a long-term relationship. Partnerships involving supply chain members are characterized by trust, long-term relationships and mutuality of transactions. These are essentially win-win business relationships. Most business transactions were previously considered zero sum games. Strategic partnerships designed for win-win outcomes are likely to be sustainable and beneficial for fostering business stability.

Box 8. A three-partner joint venture of rubber growers

Major rubber producers, Indonesia, Malaysia and Thailand, established a joint venture to regulate rubber sales and stocks from the three countries. The joint venture will be called International Tripartite Rubber Corporation. The objective is to create fair and remunerative prices for smaller rubber farmers. If prices fall below a certain level, the corporation will start buying rubber from farmers. The joint venture will be located in Thailand and will have an authorized capital of US$225 million. It is a multi-country consortium among three competing countries that will stabilize supply and help to ensure good supply coordination. It is an example of a partnering arrangement in the form of a joint venture among competitors to protect their long-term interests.

3.3. Leveraging competence

Strategic partnerships involving a manufacturing firm and a marketing firm come under the leveraging competence class. Partners tend to have complementary competencies. Depending on the proprietary character of the technology, it may be a joint venture or a strategic partnership. If technology is highly proprietary, the relationship will be a joint venture and if the technology is generic, it may be a strategic partnership. Swapping of competence creates a mutual relationship among the partners. Such relationships are possible between SMEs and large global firms, or between large and large or between small and small firms. For example, General Motors entered into a long-term strategic partnership agreement with Sundaram Fasteners Ltd. for the supply of high tensile strength fasteners and radiator caps. There is an agreement for technological know-how. The firm supplied the components with zero defects to General Motors. Slowly, the firm started increasing the supply and received the best supplier award consecutively for four years from General Motors. It is the only firm that has such an achievement. Such partnerships involve a sharp learning curve. Sundaram Fasteners Ltd. moved up the value chain by learning and it has captured a larger share of the domestic market for automobile components in India. The learning involved improving the business process and technological updating.

3.4. Reducing risks

Franchising or licensing partnerships come under the reducing risks class. Risks are always present in business since one cannot accurately determine the contingencies of the future. The risks that a firm has to manage can be divided into the following 10 categories:

- Market
- Competitive
- Technical
- Environmental
- Managerial
- Political
- Resources
- Capital
- Prospective partner
- Compounded

For example, franchising is an institutional arrangement that could reduce many risks. A franchising company may not have a marketing network in a host country where the franchisee has to manage the marketing risk. For the franchiser, the risk is low as the investments are made by the franchisee. On the other hand, for the franchisee, the risks are low as the brand name ensures greater market success. Risk sharing reduces the risks for both the franchiser and the franchisee. Franchising or producing under licence is emerging as one of the high opportunity areas in developing countries.

Box 9. Franchise partnership

Coca-Cola entered into a strategic partnership with Mittals Himjal Beverages to bottle and co-pack its Kinley pure drinking water. Himjal Beverages has set up a state of the art greenfield project for bottling pure drinking water that will include small as well as large bottles. Coca-Cola will be able to increase market share through such a franchising partnership. Through this strategy, Coca-Cola has been able to increase the market share of drinking water to 40.8 per cent, thereby overtaking its competitors. Partnerships allow Coca-Cola to focus on brand building and logistics planning. Franchising is essentially a multiple partnership for enhancing the market reach. Coca-Cola has been able to enhance its reach in India in a short time frame through partnerships.

3.5. Expanding markets

Both joint ventures and strategic partnerships are used for rapidly expanding markets. For example, the best option for entering Viet Nam is to have either a joint venture or a strategic partnership with a firm that has a market network in Viet Nam. A firm from Thailand producing processed fruits and planning to market them in Viet Nam can apply leverage to the market through joint ventures or partnerships. Gaining access to markets could be done through either joint ventures or partnerships. Both help in gaining access to markets quickly. In addition, a firm could use a different set of joint ventures and partnerships for gaining access to different markets. Partnerships are flexible arrangements for exploiting markets. The Xerox Corporation started a joint venture in the republic of Korea to service the market in that country. It started its operations in India through another joint venture. Similarly, Xerox started another joint venture in Egypt to gain access to that market. Both joint ventures and strategic partnerships can be used for expanding the ever growing global opportunities.

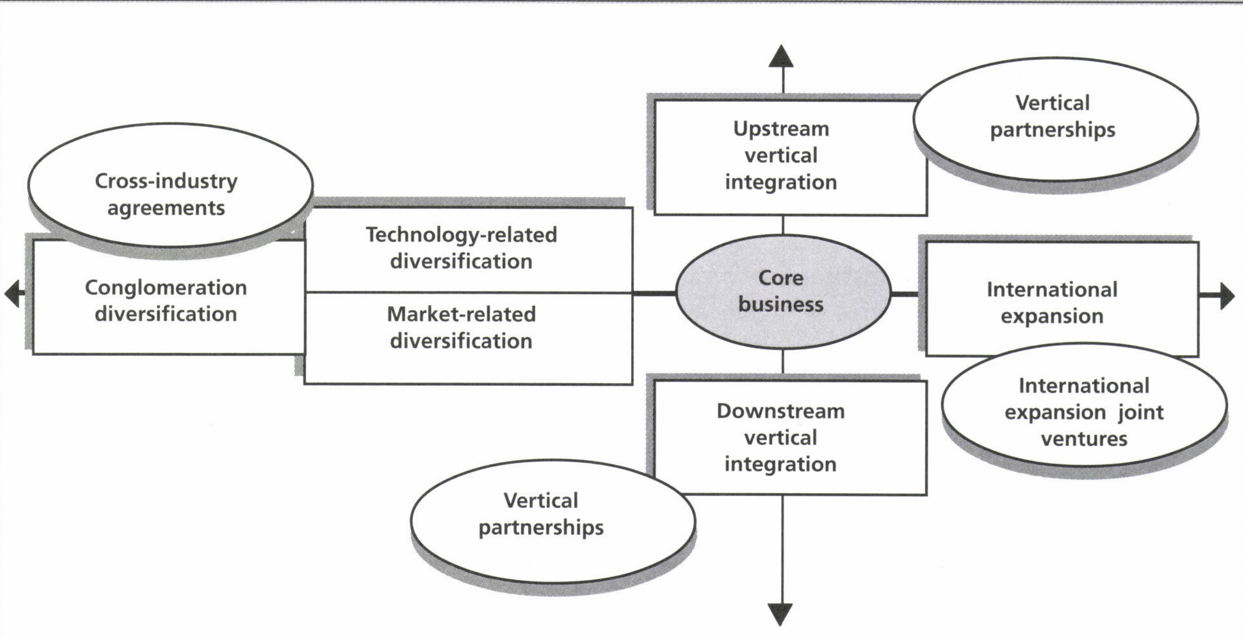
Box 10. Strategic partnership for marketing

Shantha Biotech has entered into a strategic partnership with Baxter International for selling Baxter's Meningococcal-C vaccine in India. Shantha Biotech will be using its distribution network for this. It is a win-win strategy. Baxter reduces its entry costs and Shantha Biotech enhances its revenue using its existing network. Shantha Biotech has a network to sell its hepatitis B vaccine. Baxter International sells intravenous fluids and vaccines internationally. Such a partnership helps both the partners: it enhances the reach of Baxter and it increases the products in the marketing basket of Shantha Biotech, thereby helping it to derive economies of scope. Shantha Biotech has a co-marketing arrangement with Pfizer for its hepatitis B vaccine. Marketing partnerships increase the reach without increasing the transaction costs.

Both joint ventures and strategic partnerships have to be designed in a systematic manner to really gain leverage with opportunities. Carefully planned joint ventures and partnerships could help both partners to evolve a win-win relationship. Such links provide knowledge, assets, inputs, feedback, processes, product design, etc. Joint ventures or strategic partnerships help a firm to expand its business in the following four dimensions (shown in figure VII):

- International expansion
- Upstream integration
- Downstream integration
- Corporate diversification

Figure VII. Expansion options and types of partnerships



Source: P. Dussauge and B. Garrette, *Cooperative Strategy* (New York, John Wiley & Sons, Ltd., 1999).

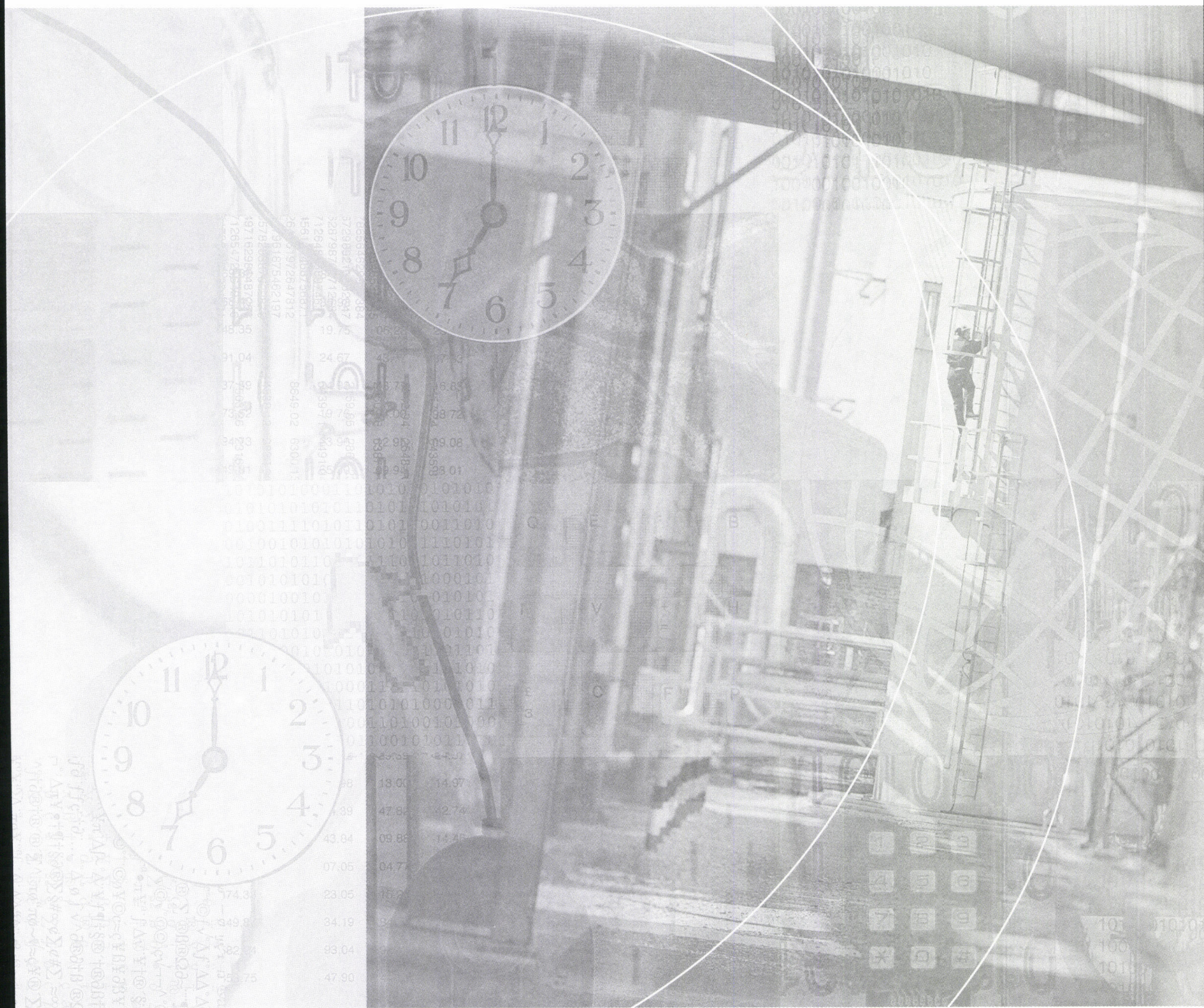
Box 11. Satyam Infoway Ltd.—Citibank partnership

Satyam Infoway Ltd. is an Internet service provider (ISP). It formed a strategic partnership with Citibank to start an Internet payment gateway (IPG). The payment gateway enables many organizations to clear their cheque payments instantaneously at various locations, cutting across many cities. Large firms as well as SMEs benefit from it. The partnership reduces the transaction costs. It is an example in which value chains of the two firms are linked, resulting in a new service. It could be termed a value chain partnership in which there is a win-win relationship. Two partners create a new opportunity that no firm can independently satisfy.

Box 12. Global reach through strategic partnerships

Frontier Life Sciences is a bioinformatics company in India. It is an SME with specialized skills that has entered into a strategic partnership agreement with DataCore Software Corporation, a firm in the United States. Through this partnership, Frontier Life Sciences will gain entry into the drug discovery platform and outsourcing market in the United States. Frontier Life Sciences will act as an offshore development centre of the DataCore Software Corporation. In return, DataCore will help Frontier Life Sciences in marketing value-added services and products in the pharmaceutical sector. Frontier Life Sciences has started incubators in two biotechnology laboratories in India, the Centre for Cellular and Molecular Biology (at Hyderabad), and the Bioinformatics Centre at the University of Pune. Each of the centres has a core team of six people specialized in data mining, data warehousing, three-dimensional modelling and functional analysis. The focus of Frontier Life Sciences is to exploit opportunities for the analysis of large genomic and proteomic databases so as to reduce drug discovery to market cycle time. Such a partnership is a learning partnership and also a globalization partnership. The growth of the biotechnology industry has been mostly through partnerships. The critical success factor in the evolution of partnerships in biotechnology industry is learning.

SECTION 4. IDENTIFICATION OF OPPORTUNITIES



SECTION 4. IDENTIFICATION OF OPPORTUNITIES

One of the major steps to be undertaken before starting a joint venture or a strategic partnership is to examine the need and opportunities for such a form of cooperation. Formation of either a joint venture or a strategic partnership has to be considered if the strategy of the firm is to increase the level of competitiveness through some joint initiatives. A firm need not go for a joint venture or strategic partnership if it has control over the technology, the channels for obtaining the necessary capital resources, managerial capability to steer the firm, sufficient business knowledge and capability to bring together those resources to launch a product or a set of products or services. The need for forging a partnership or joint venture should come from the overall business needs. If there are favourable factors and weak points, then a joint venture or strategic partnership should be considered.

4.1. Deciding on the need for a joint venture or strategic partnership

Before planning for a joint venture or strategic partnership, a firm has to carry out an in-depth analysis to examine the strong and the weak aspects of the business of the firm, as well as the threats and opportunities. Such an analysis could give an indication of the aspects a firm should consider in joint ventures or strategic partnerships. If some opportunities are unexploited and the firm does not have sufficient strength and competence to manage on its own, a joint venture or strategic partnership may be needed. Opportunities may be in the form of expansion into new segments, entering new markets (geographic) and diversification. Joint ventures or strategic partnerships may be required to overcome weakness and to reduce competitive threats. This step ensures that partnership formation or joint venture formation has a strategic purpose behind it.

4.2. Opportunity—Competence matrix

The decision to go for a joint venture or strategic partnership is similar to a decision to make or buy. Here, an organization examines whether it should carry out the activity internally or externally. The opportunity essentially examines whether there is scope for a product or a service in a national or international market. Care must be taken to ensure that the assessment is realistic. One of the tools used for this is the opportunity-competence matrix. A win-win situation from which both partners can benefit is an ideal proposition. Some of the questions that need to be examined are:

- What are the risks associated with realizing the opportunities in a reasonable time frame?
- What are the sources of business risk?
- Is the partner really interested in the partnering or is a hidden takeover being planned?
- How stable is the business environment and the industry?
- Can fast changes be expected that might lead to an immediate exit of the partner?
- Will the partnership help in exploiting the new opportunity?
- What can the influence of the parent company be?

The opportunity-competence matrix is a tool for identifying asset and capability complementarities. The matrix is given in figure VIII.

The matrix attempts to answer the question whether the firm should do the business independently, whether it should outsource or whether it

Figure VIII. Opportunity–competence matrix

Strategic importance of activity or market opportunity	Low (Competence compared with the best in market)		High
High	Alliance	Invest and make	Do it yourself
	Alliance	Alliance	Do it yourself
Low	Buy	Buy	Buy

Source: J. Child and D. Faulkner, *Strategies of Coooperation* (Oxford, Oxford University Press, 1998).

should seek an alliance. It assists a firm to determine how best it should carry out specific activities. The vertical axis shows market opportunity and the horizontal axis depicts competence compared with the best in the market. In consonance with the core competence concept, the firm should do certain strategic activities very well. Other activities should be done by suppliers or partners. The logic behind this is that a firm should deploy its internal resources only for strategic activities. Thus, if the activity is of little strategic significance to the company, it should be outsourced, even if the company would be very proficient at carrying it out by itself.

The logic for partnerships and joint ventures flows from the matrix. If the activity is strategically important but the firm cannot carry out that in the best manner, an alliance may be needed to enable the company to learn the necessary skills to improve its performance and remain competitive. The operational value of the matrix depends on how accurately it is possible to measure strategic significance and the efficiency of performance needed to achieve the company's mission. A firm has to outsource all low opportunity arenas, as shown in figure VIII and has to look at either a partnership or joint venture if the opportunity is good but the internal competence base is weak. The success of using such a tool will depend on the reliability of the assessment of the opportunity, as it is a dynamically changing one.

4.3. Criteria for prioritization

The most difficult aspect to determine is which activity is critical for the success of the business. The business that each party brings into the partnership or joint venture should be assessed in terms of its strength in relation to competitive requirements. In each business, there are certain critical success factors: partnering should address these critical success factors, as should strategic partnership or equity arrangements. The need for a partnership or a joint venture investment has to be assessed and then prioritized. In negotiations, such factors should be given priority. Owing to the emerging tight intellectual property (IP) regime, priority may be given to ownership of IP in industries where patents, designs, brands or trademarks are crucial for market dominance. Normally, there are eight aspects of IP rights that are likely to be crucial for a business, namely:

- Patents
- Copyrights
- Designs
- Trademarks
- IC layouts
- Geographic indicators
- Trade secrets
- Gene sequences

The value of a strategic partnership or joint venture will be higher if one or two elements of IP can be brought in. Any search for joint venture and strategic partnerships should clearly examine elements of IP that could be of use in enhancing the value of the product or increasing competitiveness. IP rights such as designs, patents, IC layouts, etc. provide for tangible benefits and things such as brands and trade secrets provide for intangible benefits. In a world of intense competition, only a combination of tangibles and intangibles could provide a sustainable competitive advantage. Prioritizing the competencies, the tangible assets and the intangible assets that a partner could bring into the joint venture or strategic partnership is essential, as such priorities could make a difference in a competitive business. Because of globalization, intangibles such as reputation, brand image and goodwill are becoming crucial assets that will tilt the strategic advantage in favour of one product in relation to another.

4.4. Value chain analysis

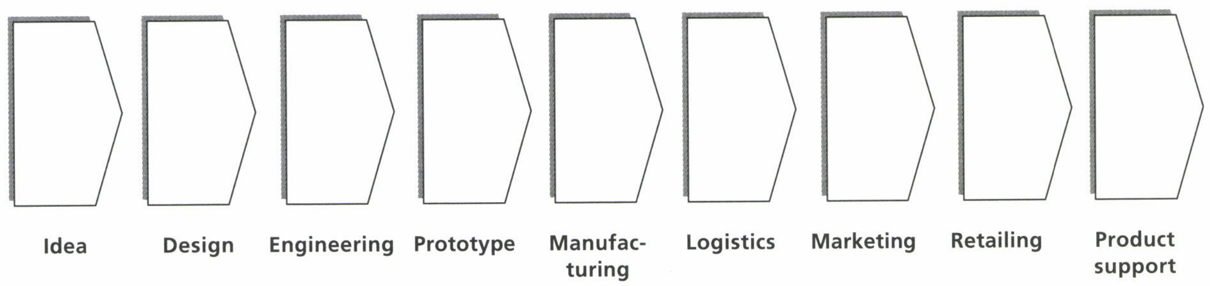
One of the tools that could be used for identifying competence, tangible assets and intangible assets needed from a partner is value chain analysis. The value chain depicts how the value of an idea moves up and finally reaches the customer. A typical value chain represents the steps through which an idea is developed and the ultimate customer is reached, and the product delivered. A typical value chain is shown in figure IX.

The value chain indicates how the value of an idea progresses as it reaches the customer. The value chain concept can be used for identifying the activities in which inputs from partners may be needed so that the firm can become competitive. Partners can provide complementarity competencies thereby making the value chain globally competitive. When businesses restructure, value chains can be disaggregated and the analysis can be delivered through a conglomerate of partners, facilitated by the use of IT. Digital delivery of the value chain, such as design, is possible. This has been one of the reasons for the increase in the number of strategic partnerships and joint ventures.

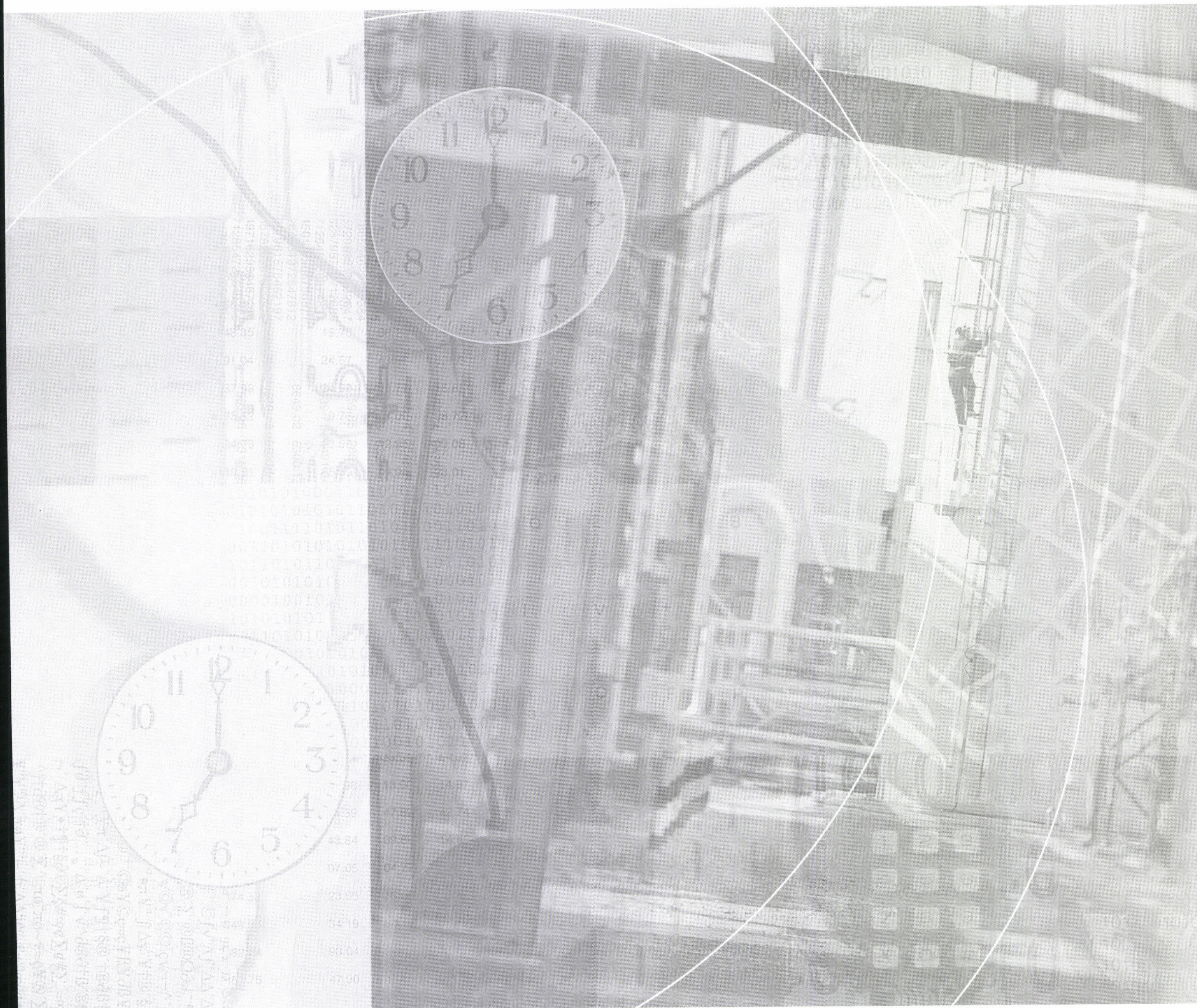
The present section has provided answers to two questions:

- Is a partnership or joint venture needed from a business perspective? (Answer: This can be determined by mapping competence related to opportunity.)
- In which activity does the focus need to rest for partnering? (Answer: The value chain analysis will help in disaggregating the business needs and pinpoint activities that need a partner for strengthening business competence.)

Figure IX. Business value chain



SECTION 5. SELECTING THE FORMAT



SECTION 5. SELECTING THE FORMAT

Once the competence, asset or intangible element needed to enhance business strength or market share is identified, the next step is deciding the format, whether a partnership or joint venture. There could be a variety of arrangements and each could have a high opportunity for project success and potential benefits. The format will depend on the need for partnering.

Strategic partnerships or joint ventures involving firms from developing and developed countries will have very different sets of capabilities. Firms from developed countries will most often possess knowledge about manufacturing and technology. The partner from the developing country will contribute mostly in the area of marketing, distribution, approval and local support. The competence bases of partners will be distinctly different and complementary.

5.1. Partnerships for sales and services

The simplest form of inter-firm relationship involves a partner having manufacturing competence working with a partner who will provide the sales and service part of the value chain. This occurs in developing countries. The technological capability needed will be mostly product application and sales support. In general, this will involve only the transfer of product maintenance technology and will need operational cooperation between the two firms. Such a format is the preferred form when the conditions are as follows:

- When the market uncertainty is high and a considerable degree of risk exists with respect to the acceptance of the product. Though the agreement could be long term, the arrangements can be flexible. The costs and risks involved are relatively low. Such a partnership will not involve considerable investment

- When the partners have not worked together previously, as this will help in knowing each other well

- When the product life cycle is short and investment requirements are low (the partnership form of relationship helps in obtaining a rapid stream of revenues)

- Strategic partnerships are preferred when a firm is planning to enter a new geographical territory. Without a major commitment of resources, the market can be tested. Such a partnership will provide an opportunity for both partners to share the risk and slowly develop a deeper relationship

- When investment requirements are high and a product may be imported and marketed without involving manufacturing investment

- When the demand is high but there is no manufacturing facility prevalent in the country in which market demand exists

- When the firm has the technology but the licensing option is not available

Strategic partnerships are, thus, a good option when a firm that has manufacturing technology and facilities is willing to form a partnership with a firm from a developing country. For the foreign partner, it provides a way of increasing market access without substantial investment. The firm from the developing country gets an opportunity to learn product maintenance without considerable manufacturing investment. In essence, it is a win-win type of strategic partnership.

Box 13. Product development partnerships

Nippon Steel Corp. of Japan, Arcelor International of Europe and Tata Steel of India entered into a partnership agreement for joint product development and its subsequent manufacturing. The objective of the partnership agreement is to provide the automotive industry in India with effective total steel solutions, and in the process improve the market share. The first effort will be to develop high quality steel sheets for the automotive industry in India. It started with a project between Nippon Steel Corp. and Tata Steel. Nippon Steel Corp. and Tata Steel worked towards developing cold rolled sheets for the automobile sector in India. Another focus area is the development of galvanized sheets. The partnership will include joint activities required for the wider acceptance of high tensile strength steel sheets and galvanized steel sheets so that the safety, weight and environmental needs of the auto sector are met. It is essentially a win-win-win relationship for sharing knowledge and creating new products.

5.2. Partnership or joint venture option

The second level of the partnership option involves manufacturing, apart from sales and services. The format may be partnership or joint venture depending on the marketing condition. In such a case, investments are higher. Apart from marketing, the firm also needs manufacturing experience. The technology absorption requirements are higher. A significant amount of capability has to exist in the firm from the developing country. Many firms move to this phase once they are successful in the marketing partnership arrangement. Under some conditions, flexible forms bordering partnership and joint venture are used, namely:

- When product acceptance is high and investment commitment and risks are high, either partnership or joint venture is possible. When growth opportunities are high and long-term growth requires investment a joint venture is used

- When the product life cycle is long and adequate returns are available, the joint venture option is ideal. On the other hand, when market uncertainty is high and the investments needed are not substantial, partnership is better from the point of view of flexibility

- When product development infrastructure needs are low and the required R&D capability is not substantial, it may be ideal to go for a partnership arrangement

- The manufacturing option is useful only if the country has a sufficient level of IP protection. Any firm would resist the transfer of manufacturing technology if sufficient legal protection is not available for protecting the IP

- The manufacturing option requires the availability of an adequate manufacturing infrastructure. High technology manufacturing operations in developing countries tend to be in the form of joint ventures. Technologies involving low levels of manufacturing expertise such as beverages, engineering components, generic food processing and non-branded goods may use partnerships.

Joint ventures are used when prospects for future growth are reasonable and a firm would like to maintain its managerial control. Partnerships, in contrast, are used when the parent from the developed country is not keen to control the future options. Joint ventures generally involve a higher level of learning.

5.3. Joint venture option

The third level of partnering involves marketing, manufacturing and R&D and is a sophisticated form. Negotiating such agreements requires considerable experience. They are used only when projects are long and high-investment intensive. The joint venture option involves investment as well as considerable strategic planning and is an arrangement that helps both firms; however, sharing R&D requires long-term commitment. In most cases, when marketing, manufacturing and R&D are involved, joint venture is the most likely format as joint control reduces the possibility of a technology leak or acquisition of the company by a foreign partner. The following is a summary of the advantages and limitations of the joint venture option:

- The joint venture format is the preferred form when market acceptance is higher and when R&D and manufacturing are involved

- A joint venture is preferred only when the firm partner can be trusted, as there is R&D that requires joint work as well as non-disclosure agreements

- A joint venture that includes manufacturing and R&D activities is the only option if a competitive business context dictates an innovative operational arrangement. General licensing can be in the partnership format, but R&D is not normally preferred in the partnership format, as technological ownership will be an open-ended issue. Large corporations usually use either the joint venture format or their own subsidiary format when a considerable flow of technology or joint performance of R&D is involved

- Joint ventures are used when both firms have a favourable inclination towards a long-term relationship

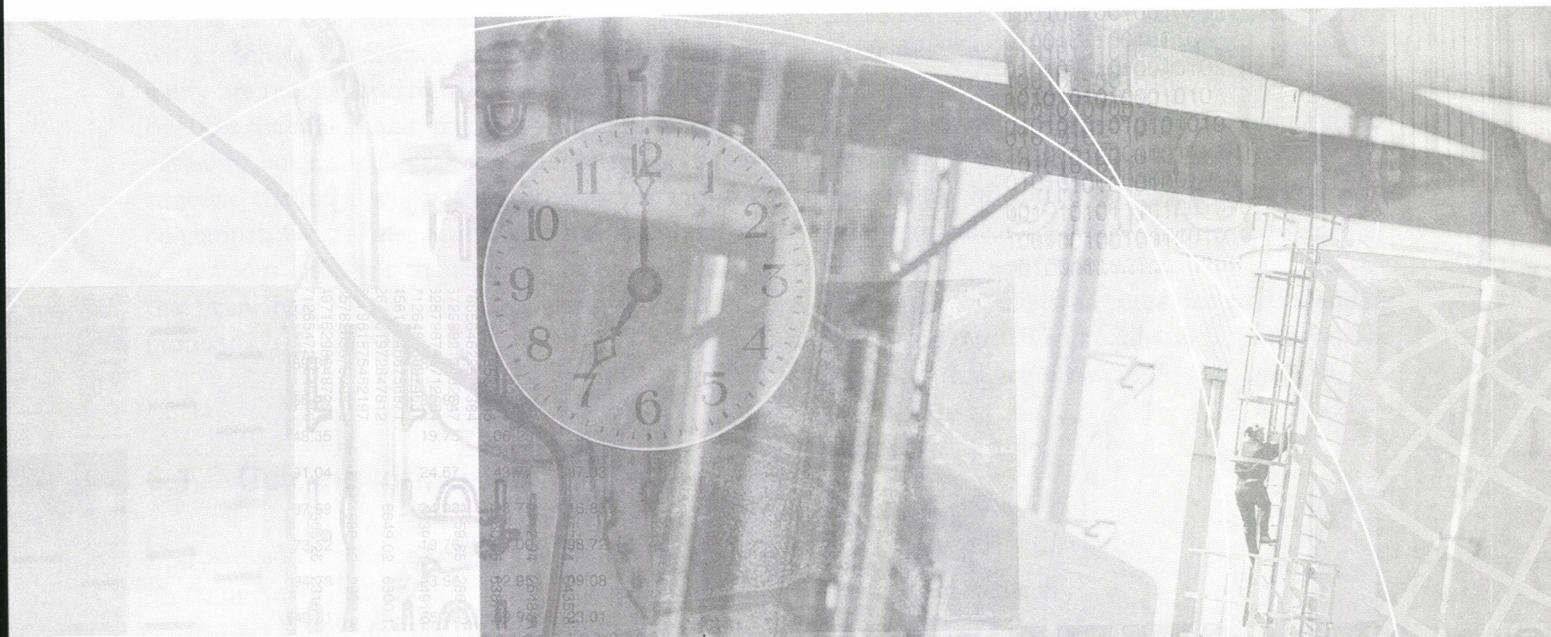
If the focus of inter-firm cooperation is marketing or sales, the optimal option is a strategic partnership. If the focus is marketing and manufacturing, it could be a joint venture or a partnership, depending on the capital investment requirement and competitive rivalry in the industry. If marketing, manufacturing and R&D are involved, it usually takes the form of a joint venture.

Cooperative relationships involving only marketing or sales are low-level intensity alliances. Such relationships involve relatively low-level risks. Returns are quick and they can be terminated easily. Cooperative relationships involving manufacturing, apart from sales and service, are projects with longer payback periods. They will work only when IP protection is adequate. High-intensity relationships are those involving marketing, manufacturing and R&D cooperation. Since the investments involved are high, time horizons involved are also high. Success of such a form will require commitment on the part of both the partners. Such cooperation will need both technical and personal relationships. There has to be a favourable attitude towards a long-term relationship for such relationships to evolve and flourish.

For food products and other low-technology products, marketing alliances are most common, which are also ideal for low-volume markets, as no commitment for investment is needed. For engineering products with less R&D intensity, manufacturing and marketing activities are the focus of partnerships. The manufacture of drugs also will have such forms of cooperative relationship. Products such as automobiles, earth moving equipment, precision equipment and speciality chemicals involve mostly joint venture forms as they need high-intensity relationships with extensive R&D interactions.

The identification of the format for cooperation needs to be carried out based on an assessment of the market. High-intensity relationships involving R&D have to work for the long-term. The partners have to be compatible and they have to be committed. If the cooperative relationship is to work, partner assessment, market assessment and investment analysis have to be done jointly involving partners. Many partnerships and joint ventures have failed because of unfulfilled expectations arising from poorly carried out market assessments and improper scanning of market opportunities. The critical success factor in any joint venture or strategic partnership is the precise assessment of market opportunities.

SECTION 6.   SELECTION OF PARTNERS



SECTION 6. SELECTION OF PARTNERS

The selection of partners in strategic partnerships and joint ventures is the most crucial determinant of success and is a multidimensional issue. Partners with technical capabilities but no cultural compatibility are problematic from the operational perspective. On the other hand, partners with cultural compatibility but no technical competence to meet the strategic challenge will not help the partnership to be competitive. Partner assessment has long been a contentious issue but there are six broad guidelines that can help in guiding the partner selection process.

6.1. Guiding principles

- Possession by the partner of the desired source of competitive advantage: Both partners should possess certain distinctive advantages if partnerships or joint ventures are to succeed. For example, the Fuji-Xerox partnership has succeeded since Fuji has strong competence in designing and developing small photocopiers, and Xerox has an excellent marketing and service network

- The need for a complementary or balanced contribution from both partners. Sundaram Fasteners Ltd. and General Motors have a strategic partnership. General Motors provides the manufacturing technology and Sundaram Fasteners Ltd. provided components with zero defects to General Motors. One provided the technology and the other developed high-level manufacturing competence to become the best supplier

- A compatible view of international strategy. The partners should have a congruent view of the future and how growth is likely to emerge

- There must be a low risk of the partner becoming the competitor. Though competitors do cooperate, the possibility that cooperating firms face the risk of acquisition has to be low for both

- The partner has pre-emptive value in relation to rivals. Setting up an alliance should be perceived as something useful by both partners. Such a perception increases the level of commitment

- There has to be organizational compatibility among the partners. Such a step reduces the probability of future problems that can arise owing to cultural conflict

A number of methods are used for understanding and assessing mutual compatibility of partners. The four aspects that require examination are:

- Partner fit
- Partner risk
- Partner antecedents
- Trustworthiness

6.2. Fit among partners

Two qualities sought in a partner are contained in two simple terms: strategic fit and cultural fit.

Strategic fit essentially means strategic compatibility among the partners. Strategic fit means agreeing on *what to do* and essentially examines whether the joint value chain of the partners seems likely to achieve sustainable competitive advantage for the partners. If the joint value chains of the partners are not complementary and both partners will not be able to make a difference in the market, the success of a strategic partnership or joint venture would be doubtful regardless of its nature and form. If the value chains are complementary in terms of both assets and competence, the problem of how to set up the alliance should not prove too intractable. Complementarity does not ensure success in the marketplace unless both partners are able to create a competitive advantage through joint work. Without complementary assets, any partnership or joint venture is likely to have problems settling the issue of who does what and how the joint organization is to function. Joint ventures and partnerships among partners of a similar size are generally less problematic. One of the reasons for strategic incompatibility is one-sided dependency. If the partners are of significantly different sizes, power imbalances may arise.

Cultural fit essentially deals with *how to do things*. Smooth operation of a partnership and joint venture requires cultural compatibility. Cultural similarity is a difficult thing to expect. An attitude of understanding towards cultural differences and willingness to compromise in the face of cultural problems may well be vital to partnership and joint venture. In short-term cooperative relationships, cultural fit is not a prerequisite but in long-term cooperative relationships, cultural fit is as important as strategy fit. Cultural fit is one of the determinants of longevity of cooperative relationships.

> "You may be deceived if you trust too much, but you will live in torment if you do not trust enough."
>
> *F. Crane*

A partnership or joint venture could encounter four distinct conditions, namely:

- Low cultural fit and low strategic fit. Neither partner may derive substantial benefit. Such partnerships or joint ventures are short-lived
- High cultural fit and low strategic fit. Relationships are normal but there may not be any substantial strategic advantage
- High strategic fit and low cultural fit. This may lead to conflict-creating conditions. If it is to work, cultural compatibility would need to be improved.
- High strategic fit and high cultural fit. Such a relationship gives rise to a synergistic relationship as it is an optimal situation for both partners.

Both partners need to do a detailed analysis of the fit and systems that will work when there is a partnership. There needs to be a frank assessment and both partners should do such an assessment first independently and then collectively. Strategic fit looks into strategic aspects such as strategic intent, vision, business road map, business plan, business model, revenue models, pricing philosophy, etc. Cultural fit deals with issues such as mindset, ethical orientation, welfare, openness, equity, concern for employees, etc., and ensures smooth operation. Strategic fit ensures competitive advantage.

6.3. Risk mapping

The second exercise that needs to be carried out is to map the risks that could come up. Risks in strategic partnerships and joint venture depend on the relationship, nature of technology, nature of the market, power of the firm to influence, etc. Some of the risks are listed below. A firm has to consider such risks and the ways in which they can be minimized. The types of risk encountered come broadly under the following categories:

- Market risk is the likely risk arising out of changes in the market. New products face the market acceptance risk
- Competitive technology risk relates to the performance risk that can arise in comparison with that of the competitors
- Technical risk relates to the technical performance. The variance between the planned and actual technological performance, if high, can pose a risk
- Contextual risk relates to the likely changes in the economic or business context that could pose a risk for the operation of the partnership or joint venture
- Management risk relates to the availability of adequate managerial resources and the necessary competence for fulfilling business goals

- Political risk represents risk that could arise from changes in political situations, government regulations and public pressures
- Resources risk denotes the likely risk owing to changes in the availability of resources
- Capital risk refers to changes in inflation, exchange rates and government policy that can change the investment value. The objective is to ensure that value is not lost
- Prospective partner risk examines whether there will be any risk from the partners, both positive and negative. Expected strategic contribution may not come through, the financial situation may not be as expected or the firm may be acquired, etc.
- Compounded risk refers to multiple risks involving many organizations and many interfaces

6.4. Monitoring antecedents

Before negotiating a partnership or joint venture, the strategic intent, antecedents of the partners and credit worthiness of the partners have to be assessed. This is usually a difficult task if the proposed partner is an unlisted firm. There are international firms that could do it for a fee and there are corporate databases that provide such information. Banking institutions do it as a new consulting service. Not carrying out an assessment could lead to problems at a later date. The possible attitude towards partners could be deduced from the antecedents of the firm.

6.5. Developing partner selection criteria

Partner selection starts with a mission statement for the potential partnering goals stated both qualitatively and quantitatively. The preparation of the criteria starts with the following questions:

- What are the ideal characteristics of the potential partners in terms of size, market share, corporate personality and position in the relevant industry?
- What kinds of inputs and competence are expected from the partner?
- What kind of working relationship is desirable with the partner?
- What is the strategic framework of the potential partner, and where does the firm seeking a partner fit in?
- Could an existing partner be a candidate for an expanded relationship, perhaps one higher on the value pyramid? Partnership pyramids represent partnerships that face a higher level of risk
- What is the strategic vision and will the partner help in achieving the vision?

The analysis starts with strategic options and strategic goals of the company vis-à-vis the role of the partners.

Box 14. Partner selection criteria for a food processing firm:

- Width of product line
- Cost leadership
- Strong brand presence
- Customization capability for meeting the local market needs
- Previous experience in similar markets
- Proven technology
- Expertise in food certification
- Willingness to transfer technology
- Ability to solve product technology problems
- Ability to deal with variability in raw materials
- R&D expertise to handle quality snags
- Opportunity for exports
- Ability to provide total technology package
- Cultural compatibility

6.6. Strategic fit analysis format

It may be worthwhile to carry out a strategic fit analysis before identifying and selecting the partner. A format for fit analysis is given below:

- Does the potential partner fit the quantitative and qualitative criteria that have been developed?
- Will the relationship meet the mission statement goals that have been created?
- Can the investment be managed?
- What are the details of the partner's business, such as their management capabilities and the intention of key managers or project champions to remain in the partner company?
- What is known about the key champion in the partner company—the individual who will carry the flag of the relationship within their own company?
- Has information been diligently collected on the company, its business history, financial background and general position in industry?
- What is the strategic potential for the company seeking a partnership with respect to the candidate?
- Is there another partner in the same industry that would be a better candidate?
- In such a relationship, what would the risk exposure for the company be in terms of both embedded and migratory knowledge transfer?
- What is the partnering activity of the candidate company at present?
- What if there is a poor strategic fit between the firm seeking a partner and the potential partner?

A detailed fit analysis will help a company to examine the possible issues before negotiations begin.

6.7. Role of trust

Both strategic partnerships and joint ventures require trust among the partners. Though control and trust are cited as the central themes needed for ensuring success, the role of trust as the factor that can facilitate the sustainability of a relationship between the partners is increasing. Trust has been defined in many ways, including predictability of behaviour and the willingness of one party to relate to the other in the belief that the other's actions will be beneficial rather than detrimental to the partner. Trust is the basis of any long-term relationship and is generally slow to evolve. Organizational trust evolves from personal trust. It is essentially a "soft" aspect and can be considered the glue that binds the partners. Joint ventures between partners in developed and developing countries usually involve a greater investment of specific assets by the partner from the developed country than by the host partner from the developing country and in this way, the former bears the greater risk because the process of building trust has to be a part of the management of partnerships as well as joint ventures.

Strategic partnerships and joint ventures with low levels of trust are generally unsuccessful. On the other hand, strategic partnerships and joint ventures in which trust levels are high are successful. Trust creates a "virtuous circle" leading to better performance. Cooperative relationships could develop over time, supported by a corresponding evolution of trust.

Trust develops gradually as the parties move from one stage to another. It has been observed that when both partners have knowledge about the operation of the other, the development of trust is faster, mutual confidence is higher and the working atmosphere is cordial. Without trust, strategic partnerships and joint ventures cannot be sustained.

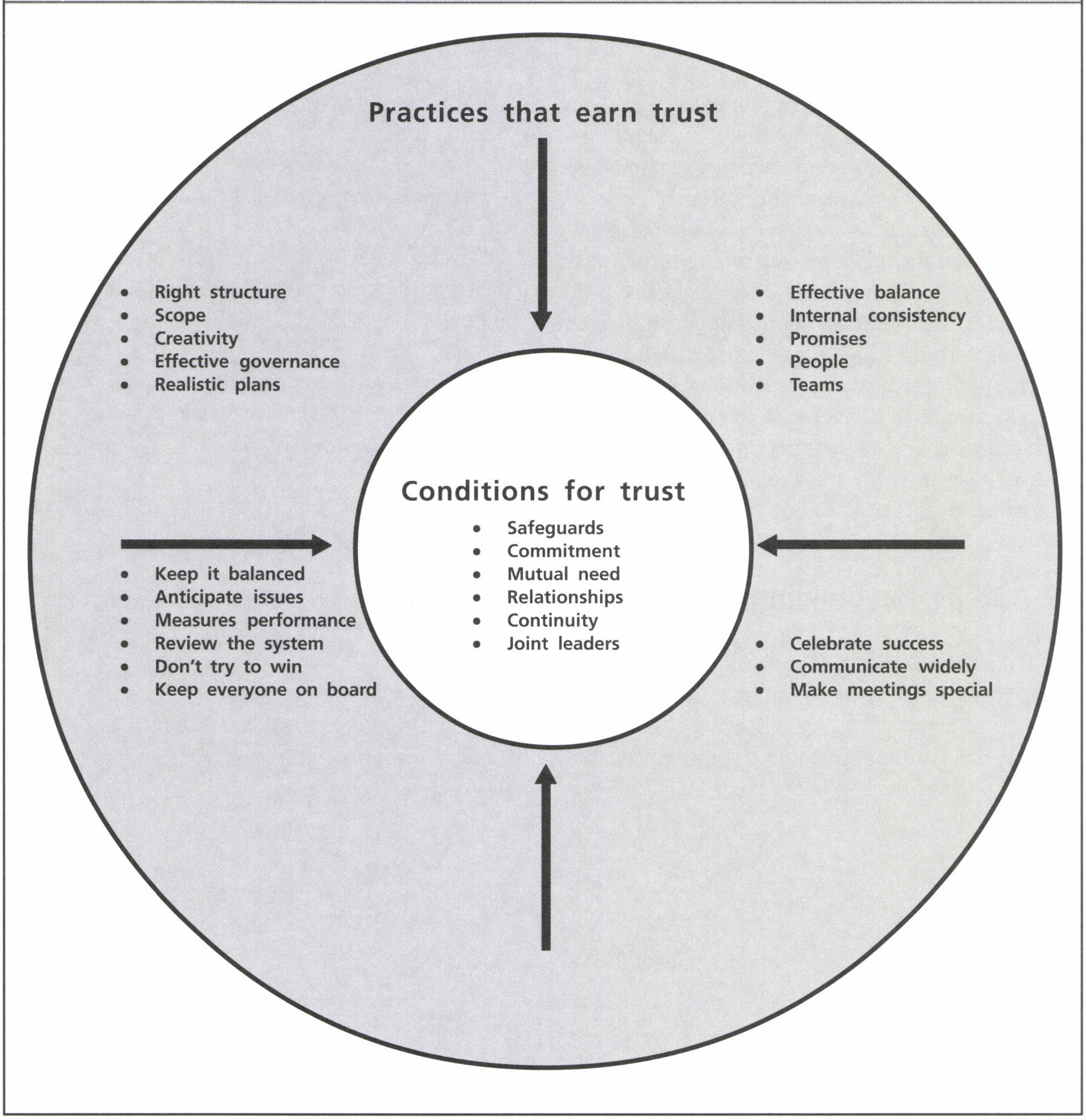
There are certain minimum conditions that are essential for the evolution of trust. They are shared objectives, close relationship and regular communications.

They should be supported by practices that include:

- Clear scope
- Realistic plans
- Consistency of goals and action
- The right structure
- Effective governance

Trust has both procedural and behavioural components. Both aspects need attention if trust is to evolve. Those components are schematically shown in figure X.

Figure X. Practices that earn trust



Source: J. D. Lewis, *Trusted Partners* (New York, Free Press, 2000).

6.8. Evolution of trust

Strategic partnerships and joint ventures are among people, not just companies. Unlike transactions, documenting intangibles such as shared understanding of each other's situations, and how to manage change in partnerships and joint ventures is not possible. Both are essential if trust is to evolve. A joint working team has a better chance of trust evolving among partners through joint work. When a firm is made up of closely related businesses, allying them with another firm's similarly related units can produce far more value than connecting just one part from each. Requirements of trust are higher in networks. The consequences of failing to meet them could be severe. Within networks, trust allows reduced transaction costs. Both external relationships between network partners and internal arrangements in network firms are dependent on high levels of trust. When managers attempt to operate in network settings with low levels of trust, failure is almost certain. Trust has a more important role in sustaining networks than was discussed earlier with respect to partnerships. Firms working in different cultural settings (in developing and developed countries) sometimes have a different basis for trust. Trust, in essence, is the building element that keeps the partners together.

6.9. Steps for building trust

The major imperatives needed for building trust among partners are the following:

1. Start by defining the priority objectives that could help in facilitating joint work.

2. Identify special cultural features of both organizations that need to be understood in order for trust to develop among the partners.

3. Define the shared vision collectively: the vision has to be realistic, futuristic and feasible.

4. Convert the vision into business and financial objectives that need to be met.

5. Verify whether the partnership or joint venture can meet the objectives of the partners individually and the collectively defined vision.

6. Rank the objectives in order of strategic importance.

7. Prepare the objective realization sequence.

8. Develop a set of subordinate mutual objectives for each of the functions and activities that are being planned.

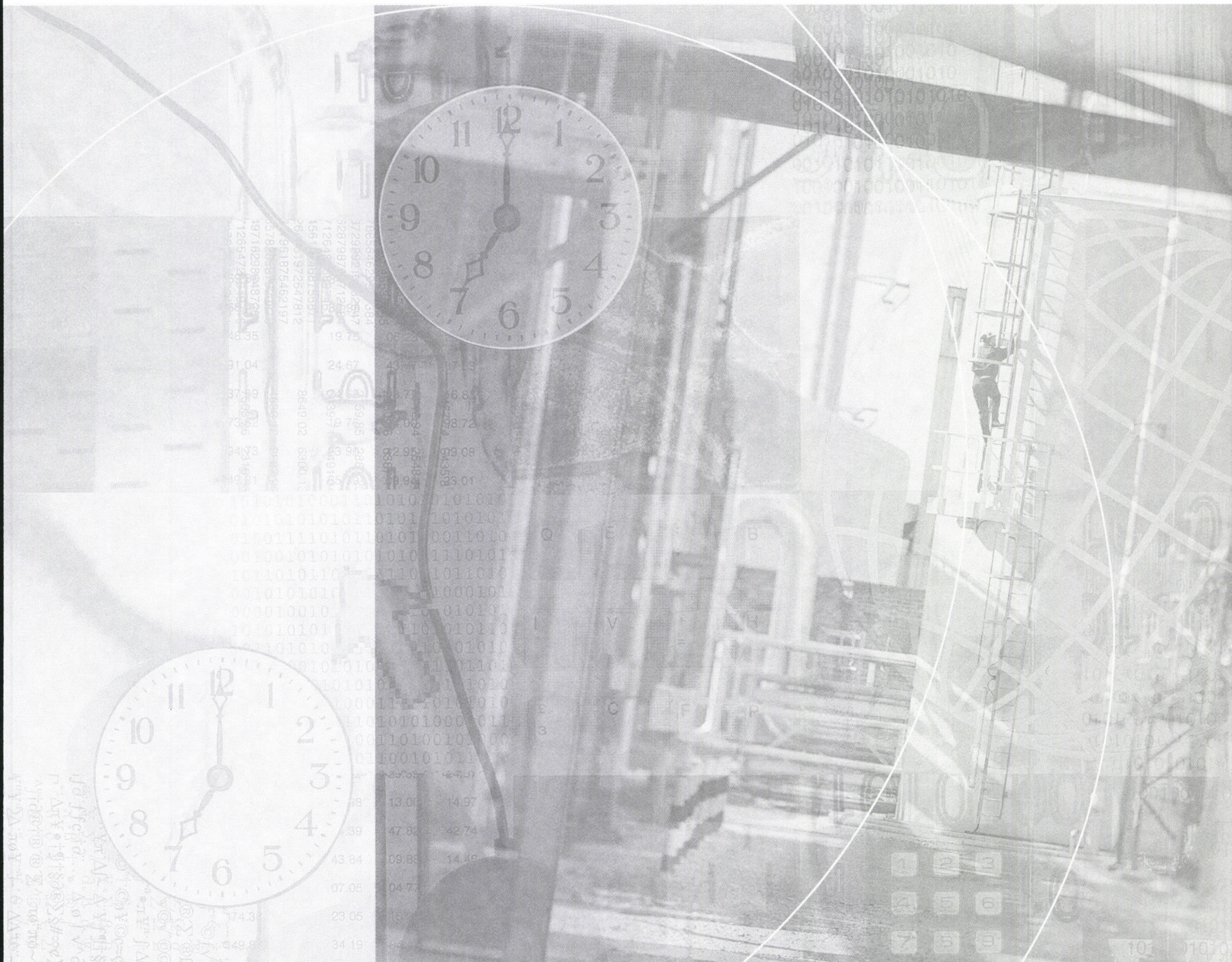
9. Ensure that the partnership or joint ventures meet all the desired objectives through operational guidelines for day-to-day actions.

10. Evolve future objectives, especially the ones that need immediate attention.

11. Identify the objectives each partner has to meet separately from the mutual objectives of the partners.

12. State the organizational boundaries of each firm that separate objectives from conflicting internal objectives.

SECTION 7. NEGOTIATING AGREEMENTS



SECTION 7. NEGOTIATING AGREEMENTS

Negotiating is one of the most critical aspects in realizing a strategic partnership or joint venture, but negotiating agreements is a "soft" skill requiring considerable experience. Selecting the right negotiating team is one of the crucial elements in creating a workable alliance. Good negotiations achieve the following outcomes:

- Convey what their companies expect to achieve from the alliance
- Evolve a plan for structuring and managing the alliance
- Agree on the contributions each partner brings to the table
- Develop a framework that can be used for resolving potential problems

Integral to the negotiating process is the concept of developing a win-win situation for both partners. As a principle, the win-win mandates the negotiators and managers to continuously seek flexible solutions that maximize gain and value for both partners. Negotiations require considerable preparation and should be done only after thorough preparatory work. Maximum leverage in any negotiation occurs prior to signing the agreement. In some cases, broad agreement is reached firstly by accepting a set of mutually acceptable boundary conditions. The final details are worked out by the operating executives. As a process, the win-win business logic requires both the partners to expand the pie, to thrive for creative solutions and to provide new pathways of opportunity. Good negotiators evolve flexible agreements that are not ambiguous and that will not lead to future conflicts. Firms from Japan use broad agreements to arrive at a consensus.

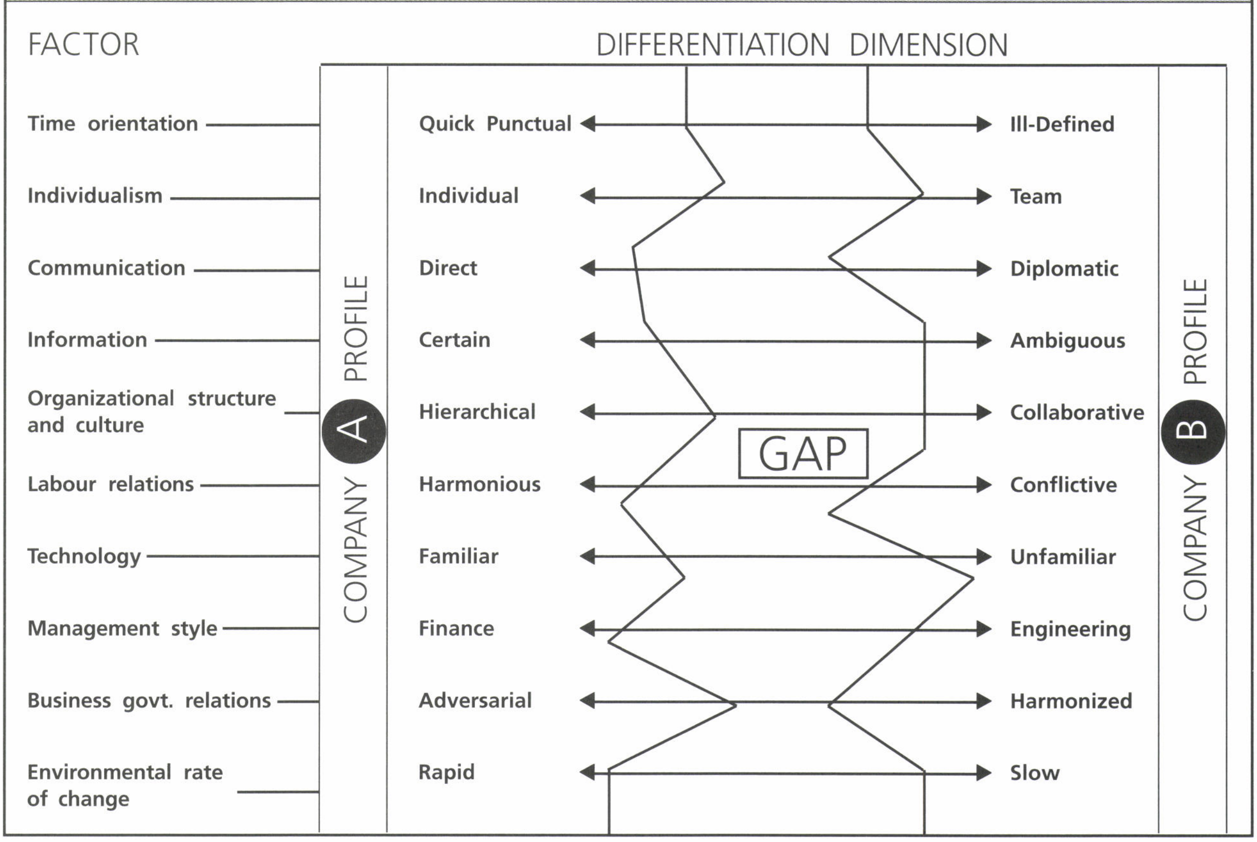
It may be worthwhile to start the negotiations with a statement of principle. The statement of principle crystallizes the broad boundaries of cooperation. It enables two or more firms that are planning to enter into a partnership to ensure that there is ample internal support and understanding for the cooperative venture. The statement of principle also summarizes the structure and operational framework that will become the vehicle for the evolution of the strategic partnership or joint venture. The statement of principle converts into a memorandum of understanding subsequent to negotiations. It also signifies the intent of the partners to join forces and to work cooperatively in an environment of trust and mutuality of benefits. The starting point of negotiations is understanding both sides and their requirements. In order for that to take place, this operational differential profiling is used as a tool. The requirements from partners in partnerships and joint ventures are different. They will be discussed separately.

7.1. Operational differential profile

The characteristics of both partners are profiled to identify the gaps in the characteristics of the partners. The partners are profiled on the following 10 dimensions such as:

- Time orientation: response time
- Individualism: decision mode
- Communication: transparency of communication
- Information: information base for decision-making
- Organizational culture: hierarchical or collaborative
- Labour relations: nature of relationship
- Technology: new or old
- Management style: technical or relational
- Business/government relations: adversarial or harmonious
- Environmental mindset: rapid change or slow change

Figure XI. Differentiation profiling



Source: R. P. Lynch, *Business Alliances Guide*, (New York, Wiley & Sons, Ltd., 1993).

The result of a typical profile exercise of two partners is given in figure XI. While negotiating, care has to be taken to ensure that the operational profile gaps do not become a conflict initiating variable. Special attention may be given to minimizing that gap through proper communication and deriving operational protocols. The profile analysis indicates the areas in which there are significant gaps. Some amount of joint working may be essential if the gap is to be minimized. Cultural gaps can be slow to eliminate and both partners have to work together if gaps are to be reduced.

7.2. Selecting a negotiating team

Selecting the team is a critical aspect in negotiations. Some of the issues to be kept in mind while selecting the negotiating team are:

- Who will serve as the chief negotiator?
- Will the executives who eventually manage the partnership or joint venture participate in the negotiations?
- What is the best role for top management in negotiations?
- How sensitive are the negotiations to the national and corporate cultures of the partners?
- Are line managers included in the negotiations?
- If line managers are excluded from the negotiating team, what early steps could be taken to avoid later antagonism from lack of understanding?

The starting point of negotiations is preparing a pre-negotiation checklist that maps out the "musts" and "wants". A pre-negotiation checklist could benefit both parties as all the issues are considered up front. By rigorously determining what the firm wants and must absolutely have in the partnership or joint venture, managers are better able to critically determine whether cooperation is feasible.

7.3. Structuring the venture

One of the crucial decisions in a joint venture or strategic partnership is deciding the structure. The structuring could be grouped into two segments: strategic partnerships and equity ventures.

Strategic partnerships are mostly functional, non-equity alliances. Strategic partnerships are easy to form, since most involve operational issues and do not have to deal with equity or managerial control. Though there can be conflicts in such alliances, they can be operationalized quickly. Typically, they start as projects involving two or more companies that decide to cooperate on one specific function or more. Some of these functions are given below:

- Joint manufacturing: two or more partners manufacturing a product by sharing the production (one doing one part, another doing another)
- Joint marketing: two or more partners marketing the same products in a number of outlets
- Cross licensing: swapping the product licences such that A manufactures a product licensed from B, and B manufactures a product licensed from A
- Original equipment manufacturing: using the technology from A, firm B manufactures a product labelled as product of A
- outsourcing partnership: a partnership for outsourcing a component by a firm on a continuous basis.
- marketing partnership: a product of firm A is being marketed by firm B through a partnering agreement
- research partnership: a firm entering into a partnership for research

There could many such partnerships for design, testing, certification, etc.

Many firms prefer to form strategic partnerships as the scope is not very broad and such partnerships do not involve equity. They are easy to manage. Strategic partnerships are more flexible compared with joint ventures and can be transformed into joint ventures. Strategic partnerships are ideal for learning processes. The weakness of a strategic partnership relationship is that since there is no equity, there could be less commitment to ensure success. Strategic partnerships generally do not involve holding assets or investments and asset transfer could be problematic in such cases. Strategic partnerships need a higher degree of trust if they are to succeed. If technology requirements are not substantial, strategic partnerships are preferable.

Joint ventures are useful when investments are planned or agreed upon by both partners. Joint ventures are separate legal entities formed by the partners. The new entity possesses its own identity and management structure, with the inherent operating and strategic problems inevitably presented by a new company.

Some major aspects to be considered in joint ventures include the following:

- Reaching an amicable equity breakdown
- Agreeing on the scope of joint venture activities
- Deciding on how the functions will be combined
- Identifying the strategic focus
- Delineating the business segments for operation
- Location of managerial control
- Conflict resolution mechanism
- Future growth options
- Ownership of technology
- Payments to the parent entity

The third option is a combination option between partnership and joint venture. Instead of starting a joint venture, a partner takes a small equity in one of the existing firms of the other partner. The equity may be purchased from the capital market so that it is not a joint venture. Buying a share of the investments of the prospective partner is the essence of such a format or structure. In that form, partners usually draw up a number of functional specific agreements to exploit complementary strengths. This is done when two partners would like to strengthen the relationship. It provides an extra defence against hostile corporate raiders. The motive is to keep competitors out. The main disadvantage is that it could affect the independence of the company operations. On the whole, the joint venture format is preferred when the option is a long-term one. When the strategic investment needed is low, partnerships are used as they are operationally flexible. When investment is large and considerable technology transfer is needed, joint ventures are the preferred option.

7.4. Managerial control

Managerial control has been a major issue that needs to be addressed if a partnership or a joint venture is to succeed. In joint ventures, the issue is also problematic because of the managerial control aspect arising out of equity investments. In strategic partnerships, collaboration between partners is balanced against the potentially competitive aspects of their relationship, and each partner seeks to reconcile the alliance activities with its own strategy and pattern of operations. Control and equity holdings may not have any direct relationship. Partnerships and joint ventures involve a mix of control and commitment options. In joint ventures, duration of commitment is long and degree of control is high. In strategic partnerships, degree of control is medium to low. The issues of control and commitment are both crucial and very sensitive. There are no hard and fast rules that can help in managing the issues, except to state that joint work and proper working protocols can minimize the recurrence of conflicts.

Control refers to the process by which the partners influence, to varying degrees, the behaviour and output of other partners and managers. Control represents the "soft" or, rather, difficult aspects of corporate relationships. The attributes include:

- Power to command strategic resources
- Authority and rights based on the size of holding
- Expertise needed to manage the specialized assets
- Rewards to offer compensation

Control is an issue mostly in joint ventures. There could be three control options, namely:

- Dominant partner joint ventures, where only one of the parent companies plays a dominant role in decision making
- Shared management joint ventures, where each parent plays an active role
- Independent joint ventures, where neither parent plays a dominant role and the joint venture general manager enjoys extensive decision-making autonomy.

The best way to minimize potential problems is to demarcate decision-making and participatory role.

7.5. Intellectual property

Some of the most important aspects to be included in the negotiations include ownership of IP, assigning rights, payment for IP, exit conditions, export obligations and IP restrictions. In both partnerships and joint ventures, there will also be questions related to the ownership of inventions and developments generated by joint work. The issues that have the potential to create conflict should be considered in the beginning, at the time of negotiations. Major forms of IP rights recognized around the world and available to protect valuable information, techniques and symbols developed and used by various business enterprises are the following:

- Patents
- Trade secrets
- Copyrights
- Designs

- Trademarks
- IC layouts
- Gene sequences
- Geographic indicators

Each form of IP right is designed to cover a different element of the creative process, namely:

- patents: patents are intended to protect new inventions
- trade secrets: they cover proprietary business information
- copyrights: copyrights are intended to protect books and other tangible forms of creative work from unauthorized copying and misappropriation
- Designs: they cover architectural forms, aesthetics and configurational aspects of products
- Trademarks: they are intended to protect books, records and other tangible forms of creative work from unauthorized copying and misappropriation
- IC: they are meant to protect layouts or architecture of microcircuits in electronics
- Gene sequences: they are to claim ownership of property relating to gene sequences or protein sequences in genes
- Geographic indicators: they are for protecting products that have a geographic connotation

The partners need to identify the technology transaction that will suit their business goals. This is done through due diligence and discussions. Any IP rights discussion starts with signing a confidentiality and non-disclosure agreement. The main issues with respect to confidentiality and non-disclosure to be looked into are:

- Mutuality of obligation
- Content and scope of confidential information
- Obligations of recipients
- Extent of disclosure to outsiders
- Status of information exchanged during discussions
- Protective conditions.

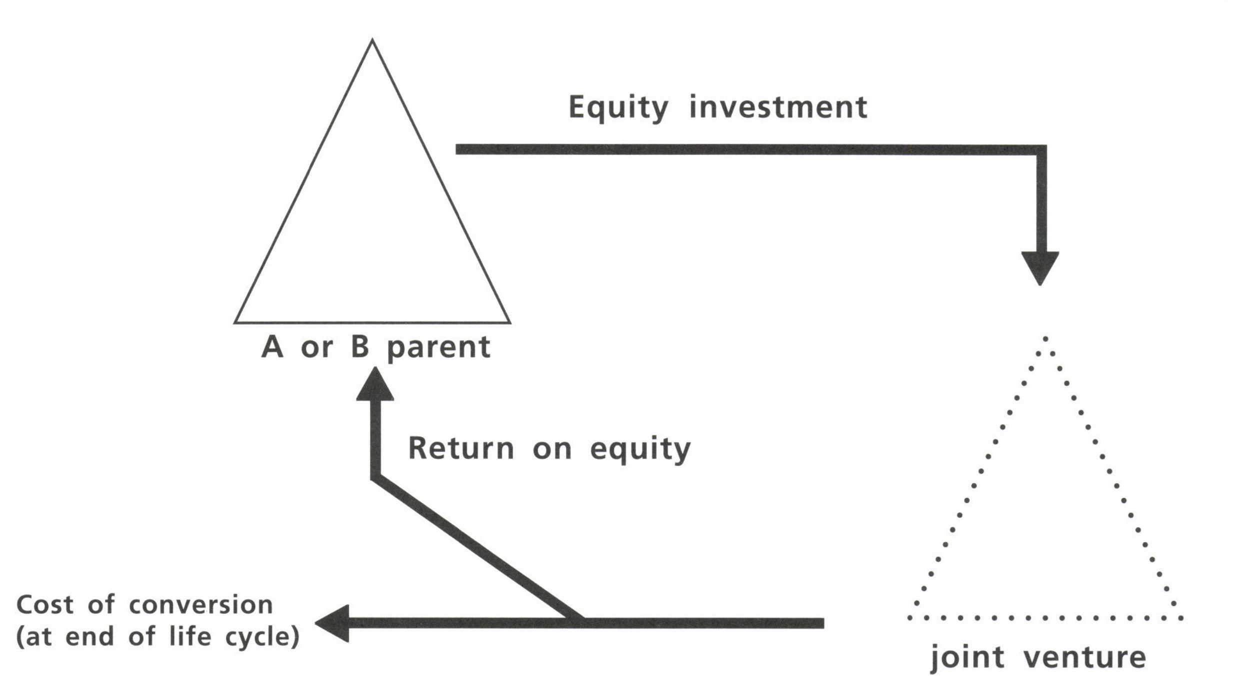
7.6. Financial aspects

Another crucial issue in negotiations involves financial aspects. The financial aspect is one of risk, tinged with the expectation of reward. Short product life cycle, intense competition in the capital market for funds and high discount factors have resulted in the contraction of financial activity cycles. Financial issues in partnerships are not two-way oriented, unlike those of joint ventures. Financial aspects are sometimes difficult to deal with, as they may involve operations in many different countries. Generally, three issues are important, namely, funds, capital structure and exit.

The funds for alliances require special consideration, both in terms of sources of funds and the cost of them. In some cases, since there may be more than one country involved in the transaction, fund management needs both special attention and skills. There are generally three sources for funding: a firm interested in investing funds, debt finance from a bank and funds from the countries.

Some developing countries do not have a well developed capital market, nor is the credit rating good for raising funds from the capital market. The cost of funds will be a function of the market rating of the company. Under normal conditions, it is the status and the past history of the firm that govern the cost of funds rather than the firm's future status. International financial institutions seek a premium when joint ventures are involved as it is considered a high-risk category. The critical parameter that is operationally important is the true cost of equity capital to the joint venture, which will be different from the nominal cost. The true cost of equity will be return on investment plus cost of conversion as shown in figure XII. Cost of conversion is the provision to be made for the cost of the capital value of the investment. Risk also plays a role in increasing the true cost of equity. A risk premium is added to the true cost of equity capital because the investing partner wants a higher return from its investment.

Figure XII. True cost of equity to the joint ventures



Source: C. Matthews, *Managing International Joint Ventures* (London, Kogan Page, 2001).

If the partnership involves debt finance, its cost has to be examined. Debt finance in developing countries has essentially three characteristics: debt has to be secured; short-term floating rate debt is easy to obtain; and the concept of debentures is not well developed.

Owing to such characteristics, the cost of debt is normally high in the case of developing countries. The most viable option is to obtain long-term debt at a fixed interest rate. Regarding the capital structure, most joint ventures use a model close to venture capital rather than a calculated portfolio risk.

An investing partner plans to obtain return for the investment through three modes: capital gain over the operational life of the joint venture investment; revenue stream; and profitable exit routes.

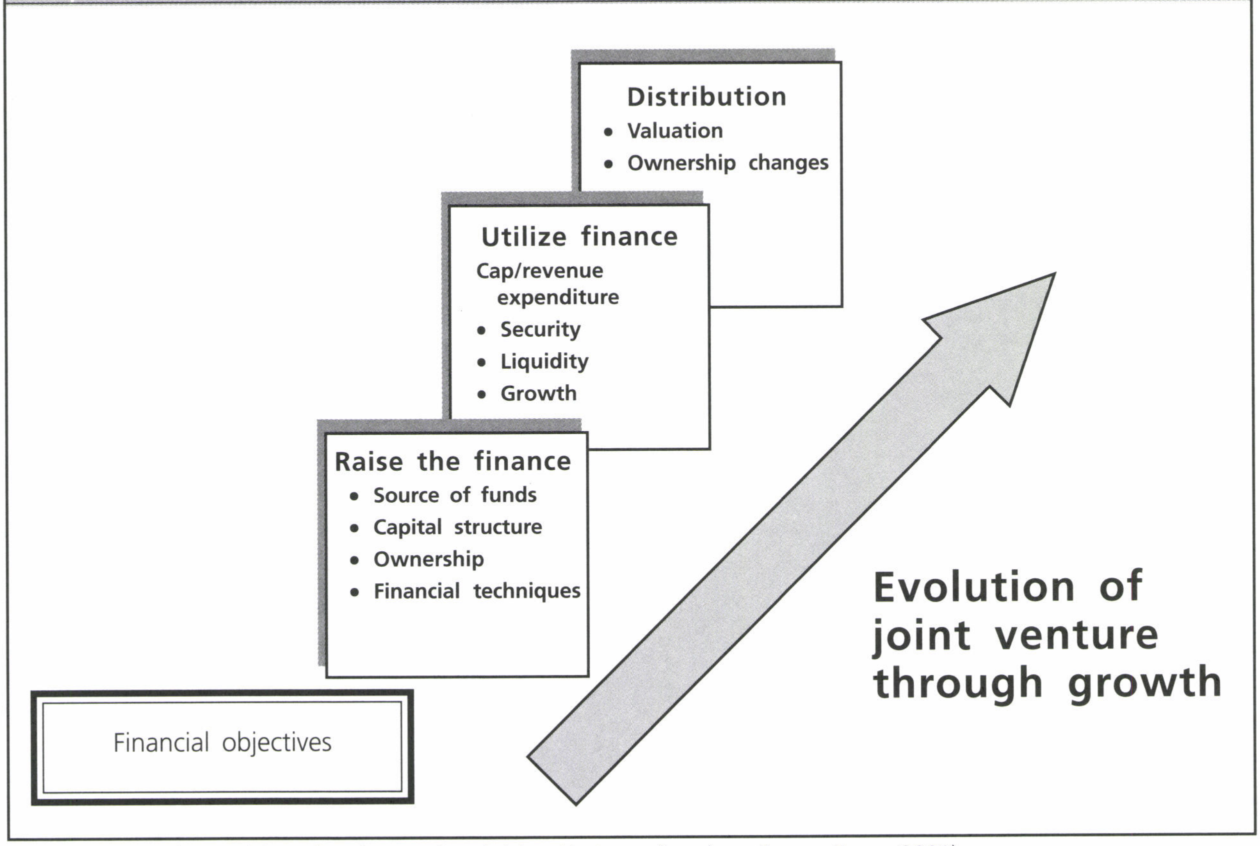
This is achieved by the apportionment of the various types of equity and debt elements of inputs in a typical joint venture.

The financial plan of any joint venture needs to include consideration of the exit route. There are four options for exit:

- Sale to a third party
- Buyout by the developed country partner
- Buyout by the developing country partner
- Restructuring and expansion

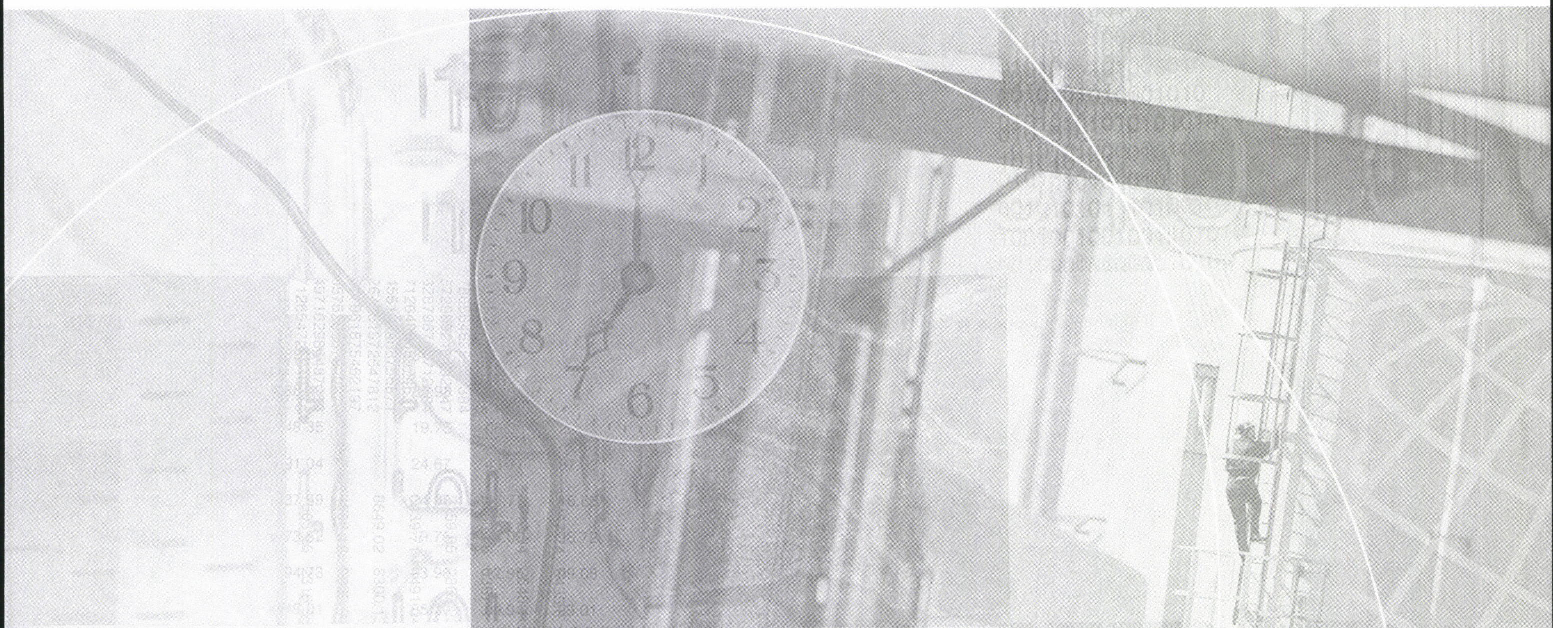
There are no universal solutions to the problem. It depends on market conditions and the strength of the partners. The financial issues in a joint venture will change as the project evolves, as shown in figure XIII. Negotiating and signing an agreement acceptable to both partners is a very involved proposition and requires consideration, homework and careful discussion.

Figure XIII. Possible financial issues in joint ventures



Source: C. Matthews, *Managing International Joint Ventures* (London, Kogan Page, 2001).

SECTION 8. DISPUTE REDUCTION



SECTION 8. DISPUTE REDUCTION

Disputes between partners are commonplace in international joint ventures. They are almost a part of their character. Nor are they unique to any particular form of joint venture—they are a product of the existence of a joint business operation that extends across geographic and cultural boundaries. There are three phases in a partnership and joint venture formation. Disputes could occur in any one of the following phases:

- Pre-partnership or joint venture formation (phase one)
- Partnership or joint venture formation (phase two)
- Post-partnership or joint venture formation (phase three)

In phase one much of the emphasis has to be on strategic and financial aspects. The decision to start a partnership or joint venture is thus framed in terms of the combined turnover or enhanced revenues based on projected cash flows and hoped for return on investment. In most successful partnerships, as well as in successful joint ventures, partners have a strategic mindset.

Problems generally encountered in partnerships and joint ventures are similar in each of the three phases, though the degree may differ. The generic problem encountered in phase one are:

- Unclear business strategy: the strategic objectives to be achieved may not be clear
- Weak core business: owing to the weak core of the partner may not be ready to take the responsibility
- Poorly planned managerial protocol: poorly planned protocols may make joint working difficult
- Pressure to do a deal: the partner or partners may be in a hurry to complete the deal
- Hurried due diligence: a proper due diligence helps partners to understand each other's capabilities
- Overvalued targets: in the initial enthusiasm, partners may set unrealistic targets that are difficult to achieve
- Overestimated synergies and returns: synergies from joint working may be overestimated owing to lack of mutual understanding

An open discussion and a clear strategy can minimize the occurrence of such problems. In the second phase, where the partnership or joint venture begins, organizational dynamics and power politics take the upper hand. Political game playing runs rampant in many organizations. In successful partnerships and joint ventures, the emphasis in phase two is on planning and relationship building. The problems encountered in phase two are the following:

- Integration seen as a distraction: in phase two, inadequate attention given to organizational integration can create tensions and conflicts
- Misunderstanding critical success factors: every business has some specific critical success elements and insufficient attention to them may lead to lack of strategic success
- Organizational aspects are ignored: in certain cases, organizational aspects are neglected as the emphasis may be on technical issues. That may lead to disharmony
- Cultural clash is ignored: when two partners work together, they may bring with them different cultures. Unless the issue is addressed, the operating climate will not be smooth

- Increased centralization: when two partners come together, there could be an increased tendency for centralization to ensure success. This can cause friction

- Decreased communication: in the starting phase, if adequate organizational communication is not present, smooth operations and the evolution of working relationships do not take place

Phase two requires close work and the evolution of operational systems.

Phase three is the adjustment phase. In successful partnerships and joint ventures, managers and staff from both sides accept the strategic logic, understand their roles, and responsibilities and strengthen the working relationships. Common problems encountered in phase three are the following:

- Rushed implementation: if adequate attention is not paid to growth problems while implementing the operational relationships, dysfunctional conflicts are created

- Insufficient resources deployed: if sufficient resources are not deployed for achieving the required objectives, there could be slippages in targets, which may trigger conflicts

- Unanticipated implementation obstacles: if contingent situations or uncertainties are not properly conceived, the responses envisaged may be inadequate and the situation may get out of hand

- Coordination snags: both partnerships and alliances need coordination to ensure that partners get what they want, which needs coordination and good communication

- Lack of attention to team building: most successful partnerships and joint ventures have given sufficient attention to team building, as personal compatibility is one of the major determinants of success

- Missed opportunities: partners have to jointly scan the market for creating new strategic opportunities. If that is not done, it could lead to stagnation.

Some of these snags may develop into disputes if not managed properly. The disputes encountered could be classified into four kinds, namely:

- Style

- Financial

- Services

- Quality

Disputes can occur at any of the phases of the life cycle of a partnership or joint venture. The potential for disputes exists in intra-international joint ventures. Research shows that in intra-international joint ventures, disputes can arise over just about anything.

Box 15. Conflicts in partnering

Prolease, a process solution provider located in the United States entered into a joint venture agreement with KGISL, a firm in India. The objective of the joint venture was to make software products for the global market. Though an agreement was signed in October 2001, the joint venture was called off owing to changed market conditions. The decision not to continue was primarily owing to the perceived conflicts in exclusivity and potential competitive engagements in a few verticals that the companies had individually chosen to expand into. The press release reported "as these issues could not be resolved in a mutually beneficial manner in spite of detailed deliberations, we agreed against taking the venture forward in the interest of shareholders of the respective companies". This is an illustration of change in partner strategy owing to internal revisions in business strategy and growth plans. Joint ventures can become unviable when there are drastic changes in the market conditions, as business plans are sensitive to market conditions.

8.1. Management style disputes

Management style disputes are those arising out of differences in managerial style with regard to certain decisions. Many disagreements could evolve into a dispute. Unclear targets and lack of proper planning at the negotiations stage could be major reasons for management style disputes:

- Management disputes occur at all levels of resolution. In the early stage, they occur in the form of disagreements while both partners are becoming familiar with each other. They may also occur later and may be deeper and more divisive. Only a give and take mindset can resolve such disputes, and this requires regular communication to minimize their occurrence

- Management style disputes in joint ventures may be one-sided. They generally affect technologically oriented ones than their developing country parent

- Disputes are generally founded in cultural differences rather than on any substantive issues

- Good managers resolve disputes through negotiation or by prevention through anticipatory action.

Open discussions and good negotiating skills can reduce the occurrence of such disputes.

8.2. Financial disputes

Financial disputes may be about investments, accounting, profits and financial cash flows. Financial disputes are normally about more esoteric areas of management finance rather than straight disagreement over who owns what—they could be reduced by clearly setting out the terms of procedures at the time of agreement, or resolved by negotiation between the partners. Since financial disputes relate to money and payment matters, they have to be resolved as early as possible, as they could affect both partners. The disputes of frequent occurrence are about funding, cost and pricing.

Disputes relating to investment and expansion occur in the later stages of the life cycle. At a later stage, the originally planned funding may no longer be relevant or sufficient. Both partners of a joint venture may use different investment models; using them at a later stage may be difficult. Use of different investment models and criteria can make it difficult to arrive at an acceptable payback, return on investment and financial exit route. Careful consideration and discussions could resolve the financial disputes. Again, it may be better to prevent them by considering possible dispute-creating conditions and preventing them.

8.3. Cost disputes

Cost disputes are those relating to cost of inputs, cost of manufacturing, cost of output, transfer pricing, cost margins, etc. Cost disputes are of frequent occurrence and they may also recur. They occur because of a variety of dynamic reasons that are outside the business. Normally, cost disputes occur under the jurisdiction of the developing country partner. They also could occur for competitive reasons. Sometimes they occur because of foreign exchange parity fluctuations.

8.4. Pricing disputes

Disputes relating to the pricing of products, services and intermediates come under the categories of pricing disputes. Transfer pricing is a part of the commercial reality both in strategic partnerships and in joint ventures. Such disputes occur in all parts of the life cycle of a partnership or joint venture. Transfer pricing follows a well-defined pattern progressing from at cost through to fully commercial transfers as the business matures. That in itself can be a source of disputes. The resolution can be done at the operational level so that any disputes are resolved as and when they occur.

8.5. Anti-competitive disputes

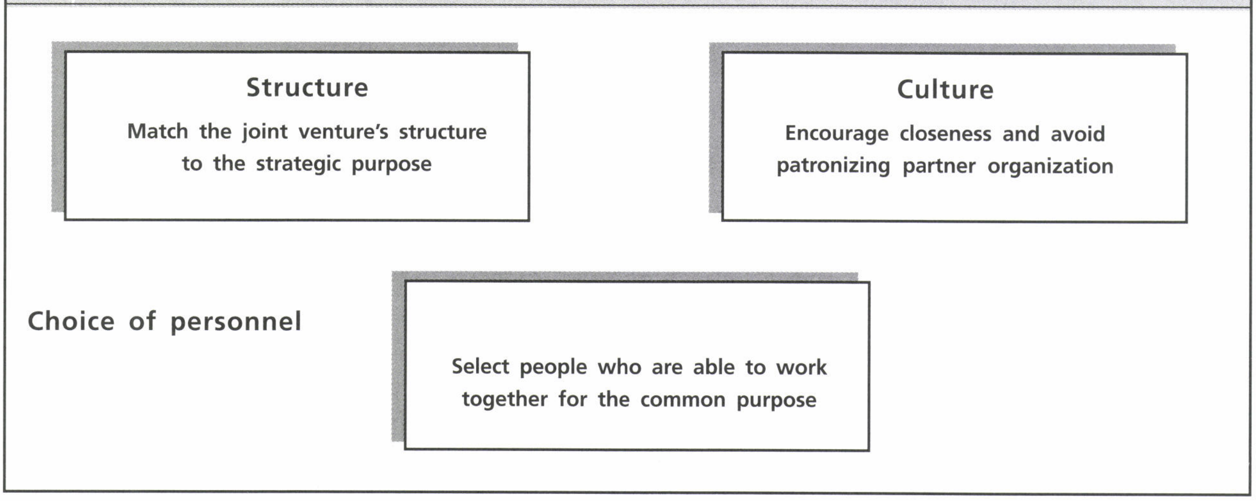
Anti-competitive disputes are about the activities of one partner acting as a competitor to the other. It is possible that a joint venture may become a competitor to the other. Many joint ventures could become competitors to the partners who started the joint venture. To prevent the recurrence of such situations, anti-competitive clauses are generally incorporated into the joint venture agreements. There could be four types of such disputes:

- Technical diversification: This occurs when one partner using the joint venture competence starts competing with the other partner. In that context, it can happen that the first firm is from a developing country
- Competitive bidding: If a joint venture exists between two or three partners, and one of the partners bids independently, a problem can emerge. Regional exclusions are included in the agreement to eliminate the problem. Many joint ventures, in their enthusiasm to perform, can create such disputes unless they are dealt with in the agreement
- Third party disputes: Such disputes involve selling a product or service to a third party who may in turn resell them to others. It is a problem and may become a high-level dispute if export markets are involved. For example, McGraw-Hill Companies has a joint venture in India for publishing books. These books are not to be exported to other markets except through McGraw-Hill. If the joint venture sells products to a seller, and that seller exports it to another market, a dispute can arise
- Quality or service disputes: Generally, quality and customer service could be the unique selling features of a joint venture. Quality and service disputes have the potential to recur unless they are resolved. Such disputes need to be resolved as they may affect the reputation of the joint venture.

8.6. Solving disputes

There are three approaches to resolving disputes relating to joint ventures. The first and foremost approach is anticipating and preventing the disputes. The essence of preventing internal disputes is to minimize their recurrence, which needs an excellent operational protocol. There are three essential ways of preventing internal disputes, as shown in figure XIV.

Figure XIV. Dispute reduction mechanisms



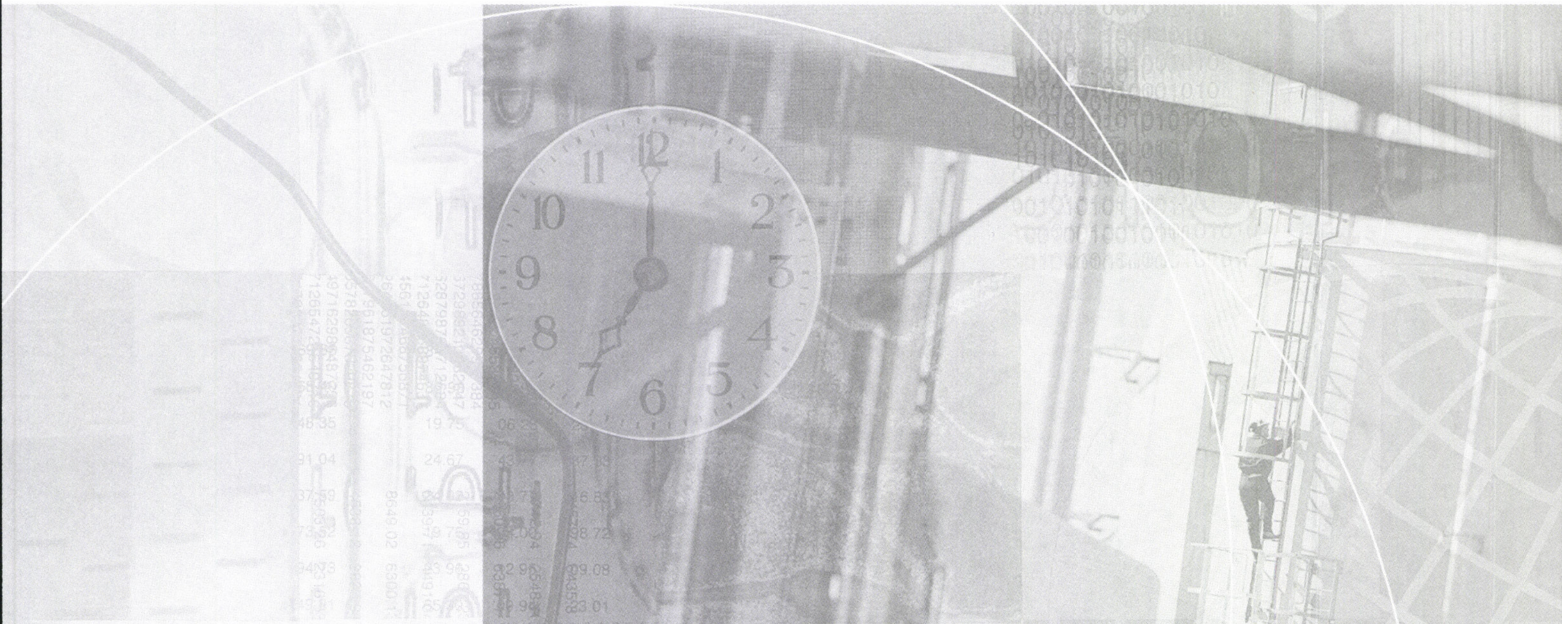
Source: C. Matthews, *Managing International Joint Ventures* (London, Kogan Page, 2001).

The approaches come broadly under three groups:

- Structure: This involves matching the partnership or joint venture structure to the joint venture life cycle. The structure has to be flexible in the beginning. As the relationships mature, the structure can evolve. The structural rigidity may become a barrier for performance, as partnerships or joint ventures have to be responsive
- Culture: The objective is to provide a culture that encourages closeness and builds trust. As organizational trust emerges from personal trust, trust building through joint work is essential. In joint ventures, it is important that the respective partner organization is not patronized
- Choice of personnel: In both strategic partnerships and joint ventures, one of the essential methods of dispute reduction is to ensure personal compatibility. Choice of personnel, thus, becomes a prerequisite for dispute reduction.

Disputes are common both in strategic partnerships and joint ventures. By devising a joint working protocol and a communication arrangement, and constituting a dispute resolution group, the occurrence of a dispute can be eliminated. Some critical incident early warning indicators forecast events, decisions, etc., that have the potential to create disputes. Resolution requires considerable patience, discussion and emphasis on win-win objectives.

SECTION 9. IMPLEMENTING STRATEGIC PARTNERSHIPS AND JOINT VENTURES



SECTION 9. IMPLEMENTING STRATEGIC PARTNERSHIPS AND JOINT VENTURES

Good strategy alone will not ensure the success of a strategic partnership or joint venture. If a strategic partnership or joint venture is to succeed, not only should the goal be excellent but the road leading to it must be smooth. Hence, only when strategy and implementation are both sound, will partnerships or joint ventures deliver competitive advantage. The main issues can be categorized into three subsets: operational issues, learning issues and ending alliances.

9.1. Operational issues

While the premises for good strategic partnerships or joint ventures are put in place through planning and negotiation, and subsequently through signing an adequate contract, only a smooth implementation of the alliance agreement can ensure the expected results. Managing strategic partnerships is easy, whereas managing joint ventures requires more attention as both partners have the power to control. There are five points to remember, namely:

- Managing a strategic partnership or joint venture is very different from managing an internal organization
- Managing a strategic partnership or joint venture requires a different mindset from traditional economic thinking
- Strategic partnerships or joint ventures that work are based on trust and mutual interest
- Relationships in both strategic partnerships and joint ventures evolve over time and many entail surprises
- In both strategic partnerships and joint ventures, the quick acquisition of technologies requires tremendous learning skills

Managing a strategic partnership or joint venture is a contingency process in which relationships emerge and change. There is no single recipe that is valid for all circumstances. The operational guidelines differ for strategic partnerships and joint ventures. Priority concerns will change depending on the nature of the relationship and degree of autonomy. There are four options:

- Strategic partnerships with autonomy
- Strategic partnerships with a high degree of control
- Joint venture with autonomy
- Joint venture with a high degree of control by partners

In strategic partnerships with high autonomy, the critical success factor is trust and cooperation. In strategic partnerships with a high degree of control, priority has to be for maintaining operational independence, autonomous access to markets and freedom for pursuing growth opportunities.

In joint ventures with high autonomy, focus has to be on trust, coordination and operational integration. In joint ventures with a high degree of control, the focus has to be on maintaining joint venture identity, independence and freedom to grow.

Three generic principles that guide a good relationship in strategic partnership and in joint ventures are:

- Manage partners as equals and continue that way
- Attract and retain senior management support
- Manage diversity but do not resist it

The Economist Intelligence Unit has identified some critical tasks that are essential for ensuring smooth functioning of both strategic partnerships and joint ventures.

Figure XV. Division of authority and responsibility between partners and alliance managers

	Partners		*Alliances managers*					
Activities and decisions	*A*	*B*	*CEO*	*FIN*	*OPE*	*MKT*	*HR*	*R&D*
Select technologies manufacturing route					D			P
Start Production					D	P		
Pricing						D		
Select distribution channel		D	P			P		
Approve new investments	D	D	P					
Design the joint strategy			A	P	P	P	P	P
Approve joint strategy	D		P					
Implement joint strategy			D					
Evaluate performance	A	A	P					
Design R&D plan				P	P	P	P	A
Approve R&D plan					P	P	P	P
Implement R&D plan					P	P		A

A = Performs the activity, D = Decision making, P = Participates

Source: R. R. Miller, J. D. Glen, F. Z. Jaspersen and Y. Karmokolias, *International Joint Ventures in Developing Countries, Discussion Paper No. 29*, International Finance Corporation, (Washington, D.C., 1996).

Operational problems are common in strategic partnerships: control issues are more common in joint ventures. Any joint venture involves three or more entities, namely, two partners who form the joint venture and the joint venture itself. Many of the operational problems would be resolved by having a protocol for decision-making. In both strategic partnerships and joint ventures, the authority and responsibility between partners and joint venture entities will differ. For example, in the case of starting production, the joint venture managers are responsible whereas for investment approval, the partners are responsible for making decisions and the joint venture manager only participates. The division of authority and responsibility between partners and alliance managers is given in figure XV.

9.2. Learning issues

Organizations often adopt cooperative strategies with the specific intention of acquiring new knowledge and know-how. Successful cooperation itself requires a learning process by the partners, especially if both partners have no prior experience in negotiating, implementing and managing strategic partnerships or joint ventures. Organizational learning consists of both cognitive and behavioural elements. An important requirement for converting knowledge into an organizational property is to make it sufficiently explicit to be able to pass around the knowledge network. At the same time it is important to ensure that competitors do not use it to their advantage. The sustenance of a strategic partnership depends on the ability to learn.

Strategic partnerships as well as joint ventures exhibit three levels of learning:

- Technical learning: routine improvements within the boundaries of existing organizational knowledge
- Systematic learning: changes in boundaries and structures of existing firms
- Strategic learning: learning how to learn through reflexive cognitive processes, which requires changes in the managerial mindset

Cooperation could enhance a partner's capabilities such that they could assume greater significance if the cooperation also opens a door to new strategic possibilities. Cooperation sometimes can involve co-operative action and joint learning. Even competitors whose goals and interest diverge may also collaborate to benefit from learning opportunities. For example, Ford Motor Company, DaimlerChrysler and Ballard Power Systems joined together for developing fuel-cell based automobiles. This is an example of a learning network. Opportunities to learn are greater when the cooperation is between competitors. There are two ways in which alliances between organizations can enhance their learning. Ballard is a pioneer in fuel cells. Ford could learn jointly with Ballard and Ford could also learn from DaimlerChrysler. Such an alliance, thus involves learning from a partner (Ballard) and learning with a partner (DaimlerChrysler) in the case of Ford Motor Company. Learning has been a key factor driving the evolution of both strategic partnerships and joint ventures. Apart from cooperative learning, there can be competitive learning. Competitive learning is where one partner intends to learn as much as possible from the other, rather than adopting mutual learning. Learning depends on a combination of factors, namely:

- Transferability of knowledge
- Receptivity of members to new knowledge
- Willingness to share knowledge
- Existence of competencies needed for learning
- How previous experiences and learning are synergized
- Ability to create a system for using collective knowledge

In essence, every strategic partnership or joint venture needs a strategy for learning that can encompass the following three steps:

- Identify key core capabilities. That is what the parties involved know how to do better than others
- Identify areas of improvement, protection and renewal for the core capabilities
- Manage cooperative learning so that the core capabilities can grow to their expected portfolio

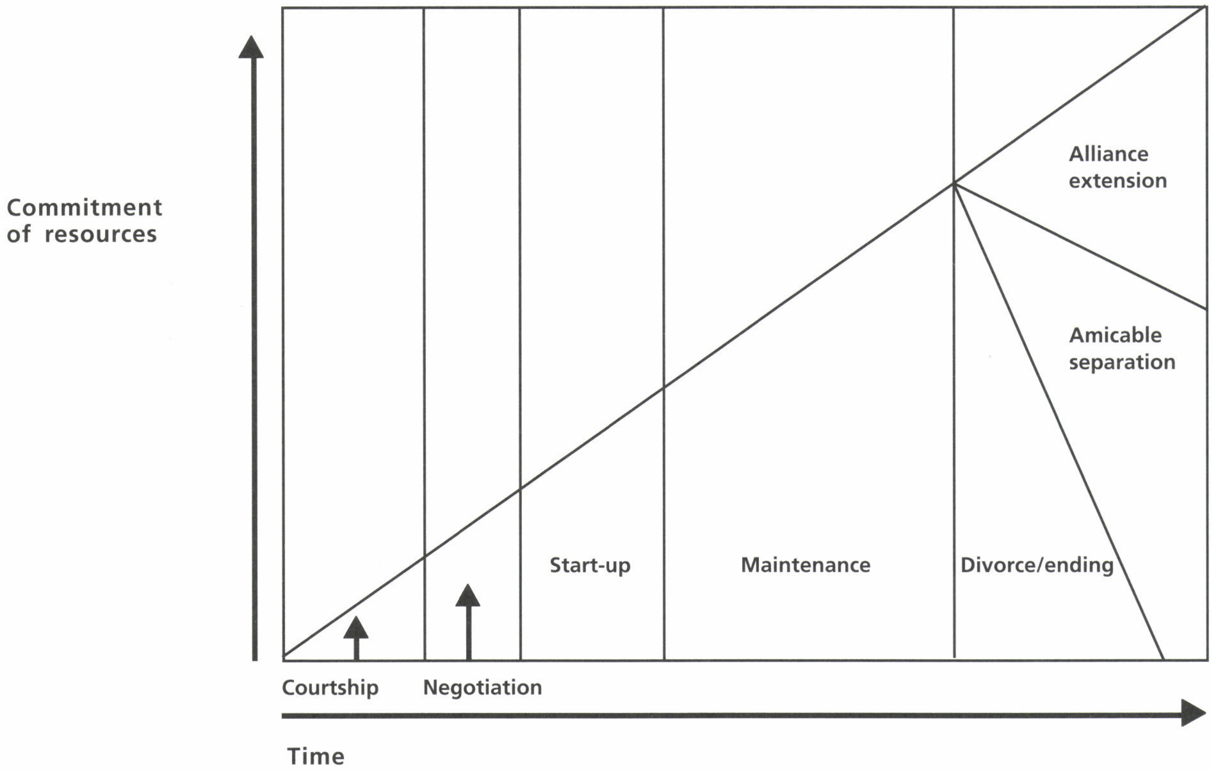
Box 16. Joint venture for facilitating learning

Although the textile industry in India has been in existence for the last 150 years, it has not been known for producing superfine goods that can be used for high-value garments. Morarjee Mills, two centuries old, entered into a joint venture with Manifattura di Valle Brembana Spa of Italy. Morarjee Brembana Ltd. is a joint venture that started in 1995. The fabric is created from double twisted yarn using 100 per cent extra long staple cotton from Egypt. The production of superior fabric using such cotton started in 1997. The products have found wide acceptance from leading brands such as Hugo Boss, Paul Smith, Jaeger, Takashimaya, Isetan, etc. The joint venture has helped Morarjee Mills to enter into different and value-added products. A joint venture of this nature will help the partner in creating a niche product/niche market. The price realization has been double for the newly designed products. The joint venture set up its own design studio in India. Morarjee Brembana Ltd. came up with its First Line Collection, consisting of 77 hand-picked designs with a classic European flavour. First Line, which sells at over US$5 per metre, has been a hit with most of the international dress makers. During the last year, the joint venture had a turnover of US$12 million. The joint venture has been able to sell the fabrics to firms in Japan, where buyers are known to be quality conscious. Morarjee Brembana Ltd. has been the first firm in India to get into the area of designed, double-spun, yarn-based shirting fabrics. This illustrates how a firm has been able to enter into a niche market by learning through a joint venture.

9.3. Ending strategic partnerships or joint ventures

Neither strategic partnerships nor joint ventures stand still—not at least, if they are to survive. For most strategic partnerships and joint ventures, however, the choice appears to be to evolve or to fail. There are a number of ways in which strategic partnerships or alliances can end if they are not extended, including as a sale of one partner to the other, in a separation or by extension of the agreement to work together.

Figure XVI. Alliance evolution pattern



Source: J. Child and D. Faulkner, *Strategies of Cooperation* (London, Oxford University Press, New York, 1998).

Such patterns are shown in figure XVI. Ending strategic partnerships or joint ventures could take any one of the following forms:

- The end of the specific relationship with extensions into other areas of mutual interest
- An amicable separation with no immediate joint activity
- A hostile parting, with no more joint initiatives
- Extension to an indefinite period

The evolution of strategic partnerships and joint ventures also depends on the development of personal relationships between those involved in the cooperation.

Box 17. Exiting a joint venture through a rights issue

Suzuki Motor Corporation and Maruti Udyog Ltd. (owned by the Government of India) have a joint venture in which Suzuki has a 50 per cent stake. Suzuki wanted to have a majority stake in the company before its expansion, so that expansion plans could be decided as per the strategic vision of Suzuki Motors. The control will go to Suzuki after the issue of a rights offering. After the proposed rights issue, Government holdings will be reduced to 44 per cent. Suzuki has agreed to subscribe to the entire portion of the Government's rights being renounced. After that, the Government will sell its residual equity in the market through an offer for sale. The proposed rights issue constitutes the first stage of the Government's plan to divest its holding in the fifty-fifty joint venture. Exiting arrangements from a joint venture require considerable deliberation. The exiting route has to be acceptable to both the partners.

The key condition for the success of a strategic partnership or joint venture is that one partner does not move sharply ahead of the other in strategic and other benefits. Successful strategic partnerships and alliances use strong bonding mechanisms, namely:

- Successfully going through an external challenge together
- Exchanging personnel at a number of levels on a regular basis
- Developing a culture that is a combination

Box 18. Exiting from a joint venture

Matsushita Air-Conditioning India Pvt. Ltd. was started in 1998 as a joint venture between Matsushita Electric Industrial Co. and Videocon with an investment of US$12 million. The company from Japan held 70 per cent and Videocon 30 per cent. The firm produces 75,000 air-conditioners per month. Matsushita then increased its share in equity to 90 per cent. Recently, the Foreign Investment Promotion Board approved its proposal to increase its stake to 100 per cent and convert it into a fully owned subsidiary. Matsushita purchased the entire stake of the partner at market price. The new company plans to increase the number of models in the market and to upgrade the product through leveraging of new technologies. Such a case illustrates one mode of exit from a joint venture relationship.

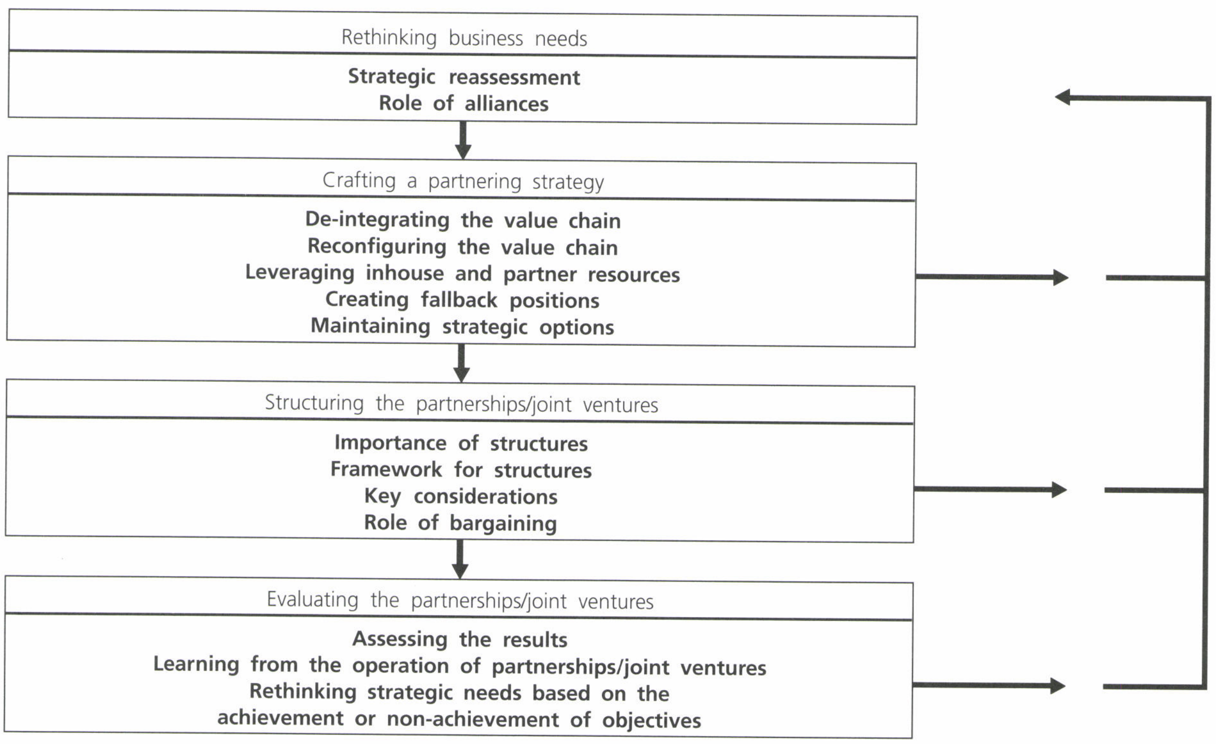
SECTION 10. LESSONS FROM PREVIOUS EXPERIENCES

SECTION 10. LESSONS FROM PREVIOUS EXPERIENCES

As strategic partnerships and joint ventures evolve as a major form of business architecture, firms need to develop a competence in identifying partners, forming partnerships or joint ventures, and managing partnerships or joint ventures. The starting point could be the preparation of a broad vision of the partnership or joint venture. The strategy should flow from the vision. Once a vision is made, the next step is to make a road map for alliances that consists of rethinking the business, crafting an alliance strategy and structuring an alliance, as shown in figure XVII.

The main lesson emerging from an analysis of how strategic partnerships and joint ventures work is that there has to be a mechanism for integrating a strategic partnership or joint venture strategy and the overall strategy of a firm through a series of feedback loops from an analysis of the operation of strategic partnerships or joint ventures. Opportunities for strategic partnerships or joint ventures are enormous and there has to be a proper fit between business strategy and strategy for partnerships or joint ventures. Any strategic partnership or joint venture has a life cycle. In every phase, the problems that are

Figure XVII. Road map for initiating partnerships



Source: R. R. Miller, J. D. Glen, F. Z. Jaspersen and Y. Karmokolias, *International Joint Ventures in Developing Countries, Discussion Paper No. 29*, (Washington, D.C., International Finance Corporation, 1996).

likely to be encountered are different. The focus of business activity changes as one moves from one phase to another. The dominant activities at each stage are:

- Partner search
- Partner identification
- Validation and negotiation
- Coordination
- Expansion
- Adjustment
- Re-evaluation

The role of executives dealing with a strategic partnership or joint venture in every stage has to be distinctly different. Such a switching of roles requires considerable preparation and introspection as well as experience. The present section contains some "dos and don'ts" as well as some of the best practices.

10.1. A list of "dos and don't's"

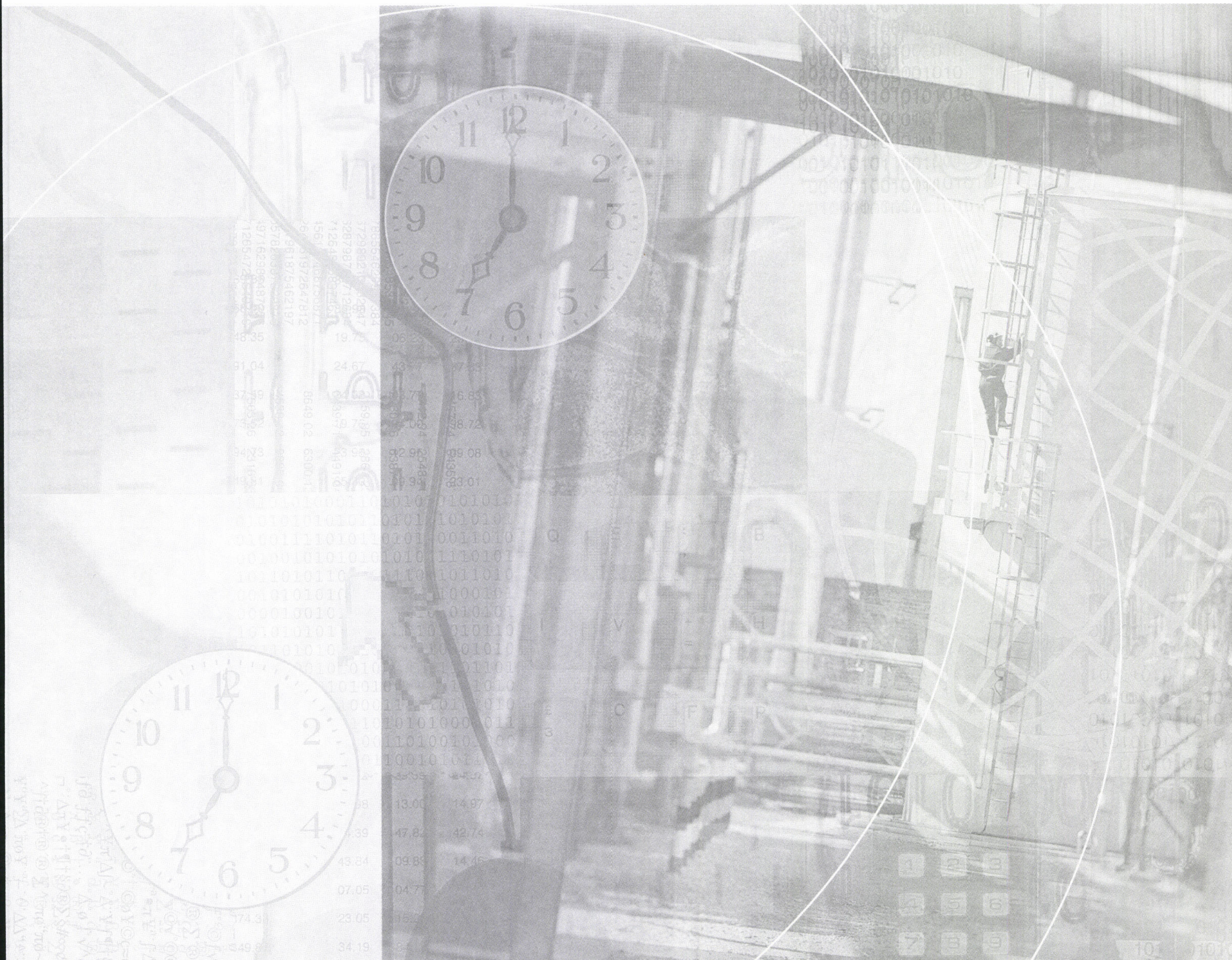
"Dos" List—good practices:

- Treat the partner's ideas and suggestions with respect
- Encourage partners to offer their opinion about the opportunity, even if they were not the ones that brought it to the table for consideration
- Be honest about what is thought of the opportunity and express reservations about the alliance's ability to capitalize on it as well as reasons for pursuing it
- Project where the opportunity may take the alliance
- Talk about the requirements of pursuing the opportunity and what each partner must contribute for it to be successful
- Look into the future so that concerns, fears and doubts about working with the partner on such problems can be identified

"Don'ts" list:

- Shy away from sensitive areas related to the opportunity
- Encourage conflict or confrontation for keeping things under control
- Use any opportunity to put the initiating partner in a better position simply because that partner brought it to the alliance's attention
- Lose the partner's trust by upsetting the delicate balance of power
- Use the partner only as a resource to capitalize on the opportunity
- Allow one partner to take all the brainstorming and strategic responsibilities and leave the dirty work to the other partner
- Act as if one partner is the brain of the partnership or joint venture

ANNEX 1. HOW TO DRAFT AGREEMENTS



ANNEX 1

The following are some sample joint venture agreements prepared for UNIDO.

How to draft agreements

Joint venture agreement

Introduction

One of the most important principles to remember when drafting a joint venture and technology transfer agreement is to use simple, clear, everyday language. The text should be as balanced as possible.

The principle of contract drafting has been dealt with at length in various UNIDO publications, including the *Manual on Technology Transfer Negotiations*, the UNIDO Guidelines for Infrastructure Development through Build-Operate-Transfer (BOT) Projects and separate draft contract agreements. IPS Centres, IPPN, Technology Centres and UNIDO Representative Offices can also be contacted for guidance in drafting such agreements.

In an international setting, contract drafting is a complicated task owing to the differences in legal systems and terminologies. There is, for instance, a striking difference in approach between business people and attorneys in the United States of America and most other countries towards negotiating and drafting contracts. In the United States, business people prefer a detailed agreement listing an almost infinite variety of possibilities of action that can be undertaken by the joint venture and its shareholders. Businesspeople from the United States also expect to be accompanied by an attorney during the entire negotiation period.

That should in no way reflect on the honesty or credibility of the other party; it is merely the normal way of negotiating in the United States.

In other countries, businesspeople often prefer to negotiate and draft the joint venture agreement without the assistance of attorneys. Such agreements are shorter as the parties prefer to leave the responsibility for future problems to managers, the board of directors or others in charge. These negotiators believe that such agreements imply a degree of trust in the other party that would not be shown if the agreement was more detailed.

Some examples of specimen clauses that appear in a normal joint venture agreement are provided below.

1. Formation of a joint venture company

Sample clause

1. Local and Foreigner (or else Local alone) shall take all necessary steps for the incorporation of a (type of corporation to be formed) corporation under the laws of (jurisdiction of incorporation), which said corporation shall be hereinafter referred to as the "Joint Company".
2. Local and Foreigner (or else Local alone) shall cause the Joint Company to be duly organized in accordance with the terms of this Agreement, with (name of the documents of incorporation under the law of the jurisdiction of incorporation, such as "Statutes", "Letters Patent of Incorporation", "Memorandum and Articles of Association", etc.) which in the English translation shall read in the form as in The Schedule attached hereto.
3. The costs of incorporating the Joint Company shall be borne equally (or according to some other formula) by Foreigner and Local.
4. If any of the provisions contained in the said Schedule should not be approved by the appropriate authority for inclusion in the documents of incorporation of the Joint Company, then the parties agree to make such amendments thereto as shall be acceptable to the said authority without altering their purpose or intention or, failing such amendment, to take all such other steps and do such other things, including the execution of any other agreements as may be necessary, to achieve the interest and purpose of such of the provisions as may not have been found acceptable by the said appropriate authority.

2. Ownership and capital structure

(a) **Type of equity joint venture.** Mention should be made as to whether it is a minority foreign ownership, a majority foreign ownership or equal or 100 per cent.

- (i) The number and kind of shares;
- (ii) Changes in the company's purpose and capital structure;
- (iii) Compliance with the host company's policies;
- (iv) Requirement for national ownership and any restrictions.

Sample clause

1. (name of nominee shareholder), do hereby declare that I am the holder of (number and type of shares) of (name of Joint Company) in trust for (name of partner), its successors and assigns, upon such trust as (name of partner) shall from time to time be declared or that I am not the beneficial owner thereof.

(b) **Capital structure.** This may be ordinary shares, preference shares, debentures or fixed rates of dividends. There may be financial benefits to one of the partners in the form of a licence fee.

(c) **Capital Structure.** This may be ordinary shares, preference shares, debentures or fixed rates of dividends. There may be financial benefits to one of the partners in the form of a licence fee, management fee, director's fee, salaries to key individuals, interest or prerequisites, etc.

There are other obligations, such as management, supply of computers or technical know-how, raw materials and machinery, etc., including veto powers. There may be alternative or nominee shares.

The payment for shares can be made by cash, machinery and equipment, land, industrial property, patents, trademarks, data and technical assistance and other services. This should be incorporated into the agreement.

Sample clauses

The Joint Company shall have an authorized capital of (amount) consisting of:

1A. (number) common (or ordinary) shares with par value of (amount each or with nominal, or par value).

Or

1B. (a) (number) Class A shares of a nominal value of (amount) each;

(b) (number) Class B shares of nominal value of (amount) each;

(c) The said Class A shareholders shall be entitled to appoint (number) directors of the Joint Company and the said Class B shareholders shall be entitled to appoint (number) directors of the Joint Company.

2. (number) (interest rate) non-voting (or voting), cumulative (or non-cumulative), redeemable (or non-redeemable) preference shares with a par value of (amount) each.

3. (number) (interest rate) non-voting (or voting) (cumulative or non-cumulative), convertible preference shares with a par value of (amount) each, which said shares shall be convertible into common shares on the basis of one preference share for one common share any time after the last business day of the calendar year 2.... .

Sample clause

In payment for the shares of the Joint Company to be required by Foreigner (Local) at the time of the incorporation of the Joint Company (or, within ... days after the incorporation of the Joint Company). Foreigner (Local) shall assign and transfer to the Joint Company:

1. **Cash:** (amount) in cash.
2. **Machinery and equipment:** all the machinery and equipment set forth in The Schedule annexed here to and said machinery shall become the sole property of The Joint Company, free and clear of all liens, charges and claims of any kind whatsoever.
3. **Land:** the absolute title, free and clear of all liens, charges and claims of any kind whatsoever, to the property and all buildings and other structures thereon, including all fixtures, equipment and machinery located therein, situated at (municipal address), which said real property, buildings, structures, fixtures, equipment and machinery are more specifically described in The Schedule annexed hereto.
4. **Industrial property:**

   i. **Assignments**

   (a) Patent: Foreigner's entire right, title and interest in and to all unexpired patents and patent applications Theretofore issued or assigned or to be filed by Foreigner anywhere in the world for the licensed products or production, manufacture or use thereof (a list of such patents and patent applications heretofore issued or assigned to or filed by Foreigner being set out in the attached Schedule), together with all rights which Foreigner then has to apply for patents in the territory on inventions relating to the licensed products or to their production, manufacture or use, and including all of Foreigner's rights with respect to patents which may thereafter be issued anywhere in the territory or any such patent applications, and with respect to divisions, patents of addition, continuations, renewals, reissues and extension of all such patents, patent applications and patents which may be issued on such patent applications:

   (b) Trademarks and trade names: Foreigner's entire right, title and interest in and to all rights in the territory which then has all of the following trademarks and trade names, namely: (to all the trademarks and trade names set out in the attached Schedule)

   ii. **Licence:** Foreigner shall enter into a Licence Agreement with the Joint Company in the forms as set out in Schedule ... hereto annexed, under which said Licence Agreement the Joint Company shall become the exclusive licensee for the world for all unexpired patents and patent application of Foreigner for the licensed products or to the production, manufacture or use thereof, together with all rights which Foreigner then has to apply for patents in the territory on inventions relating to the Licensed products or to their production, manufacture or use, and including all of Foreigner's rights with respect to patents which may thereafter be issued anywhere in the territory;

iii. **Sub-licenses:** Foreigner's entire right, title and interest in and to all rights in the territory which it then has under patents owned by others relating to the licensed products or to their production, manufacture or use a list of Foreigner's present rights under such patents being set out in the attached Schedule.

5. **Technical data:** Foreigner's entire right, title and interest in and to the use in the territory of all technical data which Foreigner is then entitled to use anywhere in the world; and thereafter during the term of this Agreement, Foreigner shall assign and transfer promptly to the Joint Company, those which Foreigner shall acquire during such period or relating to such products:

Foreigner shall take all such actions and shall execute all such documents as the Joint Company may deem necessary or desirable to effect, confirm, record or otherwise transfer and assign to the Joint Company referred to above, including without limitation the full and complete disclosure to the Joint Company of Foreigner's technical data and lists of Foreigner's distributors and customers for all the licensed products and other products produced or sold by Foreigner which may be similar to the products manufactured or sold from time to time by the Joint Company.

In the above sections, the term "technical data" shall mean formulae, inventions, whether or not patentable, secret processes and technical information relating to the product and to the production, manufacturing, engineering and test data, specification, application, instruction, information regarding uses, raw materials and methods or for controlling and analysing quality, and sample copies of advertising and publicity materials, except that information received in confidence from others or information forbidden to be disclosed by virtue of any law or governmental regulation restricting the dissemination of such information shall not be included.

Board of directors and management

The powers of the board, size of the board, control of each promoter, percentage of shares, special majority, export directors and business efficiency should be mentioned here.

Besides this, how many representatives of the promoters would be on the board? Resident or non-resident directors, etc., are to be mentioned.

The election of directors by majority or nominations, binding by the local laws, classes of shares owned by them, etc., are also to be mentioned.

Sample clause

A. Binding nomination:
(Number) directors shall be appointed by Foreigner and (number) by Local in their capacities as shareholders. Foreigner and Local agree that they shall nominate (number) directors respectively and that each shall vote for the nominees of the other.

B. Alternative clauses:
The affairs of the Joint Company shall be managed by a Board of (number) Directors, of whom (number) shall be nominated by Foreigner and (number) of whom shall be nominated by Local. The Foreigner and Local shall each vote for the persons so nominated.
Foreigner and Local agree that prior to the annual meeting of the shareholders of the company each will inform the other of the names of (number) persons qualified in all respects to be elected, such persons hereinafter being referred to as "nominees" and each will support or cause to be supported at each annual meeting the election as directors of the company for the ensuing year by nominating or seconding their names as candidates, by voting in favour of their election, and by supporting their election in any other fashion which may appear necessary. In the event that either Foreigner or Local fails to notify the other party, prior to any annual meeting, of the names of its (number) nominees, then it shall be deemed to have selected its nominees who were representing it on the Board of Directors of the Joint Company immediately prior to the annual meeting.

or

C. Different classes of shares
As registered owner of the Class A shares, Foreigner shall be entitled to make binding nominations for the appointment of (number) directors, and Local as registered owner of the Class B shares shall be entitled to make binding nominations for the appointment of (number) directors. Both Foreigner and Local agree to take all steps necessary to secure the appointment of the above said nominees in accordance with the laws of (jurisdiction of incorporation of Joint Company).

Replacement of directors should be provided for in an easy manner. Check that it is easy and without legal complications. The method of filling casual vacancies should be specified.

Sample clause

In the event that, between annual shareholders' meetings of the Joint Company, either Foreigner or Local wishes to replace any or all of its nominees on the Board of Directors of the Joint Company, the other shall join in all necessary acts, steps and proceedings, and shall cause the shares of the Joint Company to which it is beneficially entitled to be voted in favour of the removal of such nominee or nominees and the transfer of the qualifying share or shares of such nominee or nominees to the person or persons selected by Foreigner or Local, as the case may be, and the election in his or their place of the persons so selected by the party hereto whose nominee has been so removed.

Nothing contained in this Agreement is intended or shall be construed to bind the parties hereto or their nominees on the Board of Directors of the Joint Company as to the method or manner of the exercise of discretion vested in them as directors of the Joint Company concerning their management of the affairs thereof. All clauses of this Agreement will be read subject to the provision of this paragraph.

Executive committee

In case the board is of large size, an executive committee can be nominated to deal with the day-to-day matters that are normally required to be decided by the board. Thus, the board may delegate some or all powers to such a committee.

Sample clause

The directors may delegate all or any of their powers to committees, constituted for one or more purposes as they think fit.

All committees so formed shall, in the exercise of the powers delegated to them for the transaction of business conform to the mode of proceedings and regulations prescribed by the directors and regulate their proceedings in the manner as the directors do.

The decision of the board may be by majority but provision should be made to protect the interest of the minority shareholders. All questions of a basic nature thus should be decided by special majority, which means, in effect, that the minority promoters will have veto power. It is better to state the exact number of votes required to decide on issues of vital importance.

Such issues can relate to the appointment of the Chief Executive Officer and important officers, sales of assets of the company, loans to shareholders, choice of auditors, liquidation and increase or decrease in authorized capital, share transfer and the issue of new shares, and any change in the joint venture agreement.

Sample clause

Simple majority

All decisions of the Board of Directors shall require an affirmative vote of at least ... (the number should be half of the total number of directorship plus one) directors.

or

Special majority

All decisions of the Board of Directors shall require an affirmative vote of at least ... (the number should be at least the total number of nominees of the partner with the largest number of nominees on the Board, plus one for each of the other partners) directors.

And/or

No casting vote

The Chairperson shall not have a casting or second vote in the event of a deadlock.

Quorum and notice

The quorum and notice are safeguards for minority promoters to ensure their participation. This can be ensured by providing a large quorum and voting, and can be achieved by providing the presence of a fixed number of directors from each side.

Sample Clause

Notice

1. Written notice of all directors' meetings shall be sent to all directors at least fourteen days before the meeting, specifying the time and place of the meeting and indicating all matters to be considered thereat and including copies of reports, studies, etc. relating thereto.
2. Notice may be waived by the unanimous consent of all directors (in writing).

Quorum

3. The quorum of a meeting of the directors shall consist of ... (the number should be at least large enough that it cannot be constituted unless at least one nominee of each partner is present) directors.
4. Where a quorum is present, a simple majority vote of those present and voting shall suffice to pass a resolution, except where, as referred to herein, a special majority is required.
5. In lieu of a validly constituted meeting as described above, any directors' resolutions shall be considered to have validly passed if consented to in writing by all the directors.

There are other clauses on maximizing the employment of local people, appointment of chief executive officers and whether they should alternate, the need for a joint chief executive and functional chief executives. Such provisions are of great concern to foreign promoters; therefore, a suitable clause may be built into the joint venture agreement to allay any fear or doubt in the minds of the partners.

On the job training obligations

Sample clause

Whereas Foreigner and Local recognize that, as expeditiously as sound business practice will permit, officers and employees of the Joint Company should be recruited locally in (host country), they hereby agree that all officers and employees of the company who are appointees of Foreigner, recruited from outside (host country), in addition to their normal responsibilities and duties as officers and employees of the Joint Company, are responsible for assisting in training individuals recruited locally in (host country) in all aspects of their office or employment with a view to ensuring that as many of the offices of the Joint Company as possible shall be or become occupied by such locally recruited individuals.

Appointment of officers

The establishment of the posts of the officers of the Joint Company should be provided for in the documents of incorporation. In most countries, officers are appointed by the directors of the company. In many others directors are regarded as fiduciaries of the company and not of particular shareholders.

Financial policies—joint company

Profit policy

The Joint Company must decide on whether its profits are to be retained or distributed to the shareholders. The following are some of the reasons for retaining profits:

(a) Working capital;

(b) Expansion of production and sales facilities;

(c) Acquisitions;

(d) Replacement of capital assets;

(e) Redemption of capital stock;

(f) Compliance with local laws or the conditions of issuance of some of the capital stock of the Joint Company, requiring certain compulsory reserves, etc.;

(g) Compliance with foreign exchange controls preventing the expatriation of profits from the host country.

The partners, especially the foreign partner, can derive profits from the Joint Company through:

(a) Dividends;

(b) Interest;

(c) Royalties;

(d) Management fees;

(e) Fees for provision of technical data, information and know-how;

(f) Salaries paid to their personnel who are employed by the Joint Company;

(g) Increases in their own net worth from consolidated accounting principles.

In the absence of prohibitions against distribution, the approaches outlined in the sample clause below may be adopted to ensure the greatest possible retention of profits in the Joint Company.

Sample clause

A. *The parties hereto recognize that their own and the interests of the Joint Company will be best served by taking all reasonable steps to ensure the expansion of the production facilities of the Joint Company as rapidly as market conditions permit and, to this end, agree to retain sufficient earnings in the Joint Company before distributing profits to the shareholders, as shall be reasonably required in the circumstances to provide for such expansion and for the other requirements of conducting the affairs of the Joint Company according to sound business practices.*

or

B. *Before any profits of the Joint Company shall be distributed as dividends to the shareholders thereof ... per cent of each year's net after ... tax profit shall be set aside to meet the capital and other requirements of the Joint Company.*

Auditors and Books of Account

The Joint Venture Company must adopt accounting procedures that represent accurately its financial status and provide the directors with the requisite data for making sound business decisions. In a wholly owned operation, the books of account do not necessarily have to reflect the worth of the company. They may be designed, for example, to minimize taxation by taking maximum allowable depreciation. In joint ventures, however, the books must satisfy the needs of the partners as well, so that they can ascertain the true state of their investments.

Most joint venture agreements provide that the auditors must be acceptable to all partners and that they shall be from an internationally recognized firm of auditors.

Where competent local auditors can be found, two major advantages in using them will be, firstly, that their services often cost less than those of foreign auditors; and secondly, they may be more familiar with local administrative practices and have closer contacts with local officials, which can often obviate many difficulties.

Sample clause

1. Proper books of account and other records shall be maintained regarding all transactions entered into by the Joint Venture Company and they shall be freely accessible to the partners at all reasonable times.
2. A. The auditors of the Joint Venture Company shall be (name of selected accounting firm).

   or

   B. The auditors of the Joint Venture Company shall be appointed at the annual meeting of shareholders by unanimous vote (or by a special majority large enough to require the approval of all shareholders).

Marketing arrangements

In a free enterprise economy, the ultimate success of the Joint Company will depend on its ability to sell its products and obtain a reasonable profit on sales.

Sample clause

Foreigner shall supply to the Joint Company at cost without any charge for creative work all advertising and marketing aids which it now has or shall acquire during the term of this Agreement and which relate to the products manufactured or sold by the Joint Company. More specifically, but without limiting the generality of the foregoing, such advertising and marketing aids shall include brochures, pamphlets, catalogue sheets, labels, boxes, cartons, packaging, diagrams, manuals, designs, pictures, descriptions, instructions, films, scripts, recordings, colour schemes and other data designed to explain, assist or promote the sale, distribution, use and servicing of the said products.

Marketing area

Unless the objective of the joint venture is to limit its marketing activities to the host country or other specified area, it should not be prevented from gaining access to as large a market area as it is capable of supplying, consistent with the existing obligations and commitments of the foreign partner. Three market regions that the joint company may wish to supply are:

(a) The host country;

(b) The country of the foreign partner;

(c) Other designated countries.

Accordingly, as a prerequisite to entering negotiations, the host country partner may wish to obtain the following information from the foreign partner or the licensor:

(a) The industrial property rights affecting the products, including the patents, trademarks and trade names owned by or licensed to the foreign partner;

(b) Relevant licence and sub-licences granted by the foreign partner or licensor to other parties, indicating;

  (i) Date of expiry of each licence;

  (ii) Geographical area covered;

  (iii) Conditions under which each may be terminated by the foreign partner or licensor;

  (iv) Products and industrial property included in each such licence or sub-licence;

  (v) Royalties payable under each.

Marketing aids

Provision should be made for the joint company to obtain all data and information available to the foreign partner for the promotion, advertising and sale of its products. Provision should also be made for the right to use all new aids developed during the term of the Joint Venture Agreement.

Industrial property

Marketing organization

Provision should be made in the joint venture agreement for the Joint Company to enjoy the foreign company's worldwide marketing organization, including selling, advertising, merchandising and after sales servicing.

Licence agreement for trademarks and trade names

Trademarks and trade names

The joint venture company may wish to use trademarks and trade names on the best possible terms. Because the foreign partner will participate in the profit of the Joint Company, that partner should cooperate in making such trademarks and trade names available to the Joint Company without charge. Some of the provisions of a typical licence agreement for trademarks and trade names are discussed below.

Parties

The licensee will be the Joint Company and the licensor will be the foreign partner, or some other third party.

Recitals

Recitals usually mention that the licensor has the right to license certain industrial proprietary rights and the licensee wishes to use them in respect of certain specified products.

Definitions

It is common to define items such as (a) the territory for which the rights are granted; and (b) the products on which the names and marks are to be used, i.e., the authorized products.

Grant of Licence

The joint company will wish to ensure that the licence granted is an exclusive one for the territory. Generally, the Joint Company will wish to obtain as large a territory as practicable in the circumstances.

In some developing countries, it may be national policy to prohibit the use of foreign trade names and trademarks in competition with locally produced goods. Where that is the case, the partners will have to agree on new names and marks for the host country.

Sample clause

1. Foreigner hereby grants to the Joint Company the right during the continuance and subject to the provisions of this Agreement to use each and every of the trademarks and trade names upon or in connection with the authorized products manufactured and/or assembled by or on behalf of the Joint Company within the territory and which comply with the relative standards, and the Joint Company agrees that it will use the trademarks and trade names upon or in connection with all authorized products so manufactured and/or assembled.
2. The Right of the Joint Company to use the trademarks and trade names as aforesaid is an exclusive right for the whole of the territory.

Registration

To protect against unauthorized use of the trademarks and trade names by third parties, registration is usually required.

> **Sample clause**
>
> Prior to the use by the Joint Company of any of the trademarks or trade names, Foreigner and the Joint Company shall take all steps necessary to ensure that the said trademarks and trade names in this Agreement, where necessary, are registered in all of the appropriate jurisdictions within the territory and take all such other necessary steps as are required to prevent the unauthorized use by other parties of the said trademarks and trade names. Foreigner and the Joint Company shall from time to time execute and do all such documents, acts and things as may be required to ensure that the Joint Company's use of the trademarks and trade names is in all respects in accordance with the law and practice of the various jurisdictions within the territory and is not injurious to Foreigner's rights as proprietor of the trademarks and trade names.

Termination

The grant of license may be made (a) in perpetuity; (b) for a fixed term in years; (c) for the duration of the Joint Venture; or (d) the duration of the Patent License Agreement.

The Joint Venture Company may become owner of the trademark by:

(a) Assignment from the foreign partner. An arrangement may be made whereby trademarks and trade names are purchased by the Joint Company from the foreign partner or it may constitute the foreign partner's contribution to capital;

(b) Adoption of new marks and names. If the goodwill to be derived from use of the foreign partner's trademarks and trade names is not significant or may not be necessary to assist in either domestic or foreign sales, the Joint Company may seriously consider establishing its own marks and names so that all goodwill generated will accrue to it and will not be lost by expiry of time or withdrawal of the foreign partner.

> **Sample clause**
>
> 1. The term of the Agreement shall be ... years, provided that notice of its intention not to renew this Agreement be sent by Foreigner to the Joint Venture Company at least six months prior to the termination hereof. In the event that no such notice has been given, this Agreement shall continue for a further period of ... years and thereafter; until six months' notice has been received by the Joint Venture Company.
> 2. Notwithstanding the above provision, this Agreement shall terminate if the Joint Company is dissolved or enters into liquidation (whether voluntary or compulsory) or becomes subject to or submits to any law for the relief of insolvent debtors or if a receiver is appointed in respect of any of its assets or if any execution is issued against the Joint Company.

Licences

The foreign promoter shall enter into a License Agreement with the Joint Company in the form set out in The Schedule annexed hereto under which the Joint Company will become the exclusive licensee for the world for all unexpired patents and patent applications.

Sub-Licences

The Joint Company's operations will generally be more flexible if it has the right to assign its licence and sublicence for their use to another.

> **Sample clause**
>
> The Joint Company shall have the right to assign the benefits of this Agreement, and to sub-license the right to the trademarks and trade names, to such other parties upon such terms and conditions as it may in its absolute discretion determine, provided that it remains responsible to Foreigner for its obligations hereunder and further provided that such assignment or sub-licence applies only to the designated territory.

Terms for the protection of the foreign licensor:

(a) Use of trademarks and trade names. It is customary for the foreign licensor to insist on having clauses inserted in the Licence Agreement requiring the licensee to undertake:

(i) To comply with the legal requirements for affixing marks and names on the product;
(ii) To notify the licensor of the manner of using the names and marks;
(iii) To use only the authorized marks and names in association with the products;
(iv) Not to use the names and marks for unauthorized products;
(v) Not to violate the territorial restriction placed on the use of the marks and names.

(b) Inspection. To ensure that the goodwill associated with these marks and names is maintained, the licensor will generally require the right to:
(i) Inspect the products bearing the names and marks;
(ii) Test the products to ensure quality;
(iii) Investigate the marketing techniques relating to products bearing the marks and names;
(iv) Prohibit the sale of any non-complying products.

(c) Ownership. The licensor may require the licensee to affirm that:
(i) The use of the marks and names by the licensee will not derogate the ownership of the licensor;
(ii) The licensee will not deny or question the validity of the registration of the marks or names.

(d) Infringements. In case of unauthorized use of the marks or names, the licensor will often stipulate that:
(i) The licensor will have the exclusive right to take action against the infringer;
(ii) The licensee will assist in bringing any such action;
(iii) The licensee will notify the licensor of any suspected infringements.

(e) Rights after termination. The licensor will often insist that clauses in respect of some or all the following conditions come into effect upon termination of the licensee agreement:
(i) The licensee will assist in cancelling any registration there may be of the licence agreement;
(ii) The licensee will discontinue use of the marks and names;
(iii) The licensee will either resell to the licensor at cost, or else destroy, at the option of the licensor, all advertising, stationery, containers, etc. bearing the marks and names;
(iv) The licensee will permit the licensor to purchase all inventories bearing the marks and names; the cost thereof should be the fair market value.

Patent license agreement excluding royalties

A standard agreement shall have the following clauses:

Recitals

The recitals generally state that the licensor (here assumed to be the foreign partner) is engaged in the manufacturing of certain products pursuant to a patent of which that partner is the owner (or licensee) and that the licensee (in that case, the Joint Company, which also may be a sub-licensee) wishes to manufacture the same products using the same patents.

Definitions

It is common to define the following terms:

(a) Licensed products (meaning the products that the licensee is authorized to manufacture);

(b) Territory (meaning the geographical area in which the licensee is entitled to manufacture and sell the licensed products);

(c) Technical information, including an enumeration of all possible types of printed matter and data that may be necessary for the licensee to produce the licensed products.

Grant of licence

In the grant of licence clause, the licence is granted to the licensee for the duration of the agreement and the licensee is authorized to manufacture and sell the licensed products within the territory. *The Licensee should attempt to obtain an exclusive licence for the territory.*

Quality control

The licensee will generally have to guarantee to maintain certain standards of quality required by the licensor and the licensor will be given the right to inspect the licensed products to ensure such standards.

Infringement actions

The licensor will generally require a clause in the licence agreement stating that the licensor warrants that the patents do not infringe industrial property rights of third parties. In the event of infringement, the licensor will indemnify and save the licensee from any harm and the licensor will be responsible for defending any action brought against it.

Sale of licenses

If the production needs any special materials or supplies, the licensor will use its best efforts to have them supplied either by the licensor itself or by its affiliates or by other parties.

Assignment and sub-licences

The licensee should attempt to secure the right to assign the agreement to sub-license it to other producers throughout the territory.

Termination

The licensee may wish to terminate the obligation to pay royalties either after a definite period or the expiration of the patents being licensed. The licensee may also wish to obtain an option to continue with the licence even after the expiry of the agreement.

Related know-how

Other provisions obligating the licensor for the supply of technical data, information assistance and know-how related to the licensed patent may also be provided.

Sample clause

1. The licensor shall make available to the licensee without charge and as required by the licensee all such technical data and information as may be necessary for the licensee to manufacture, sell and service the licensed products and any other products related thereto.
2. If the licensee shall require technical assistance in connection with the manufacture, sale or servicing of the licensed products and any other products related thereto, the licensor shall make available to the licensee the same.
3. Representatives of the licensor and the licensee shall consult each other from time to time regarding research, production, sales, servicing, advertising, promotion, etc. and pertaining to the manufacture and sale of the licensed products, including all developments and improvements in respect thereof which the licensor may undertake and the licensor shall supply all the technical data and information, and technical assistance in respect thereof to the licensee on such a request in accordance with the terms of this Agreement.

Royalty agreement

Types of royalties

Royalties, or fees paid for the use of industrial property, may be in the form of lump sum payments or payments on a continuing basis as follows.

(a) Lump-sum royalties. Some possible considerations for determining or computing lump-sum royalties are:

- (i) The cost to the foreign partner of transferring the industrial property including the related know how, technical information and technical assistance to the Joint Company;
- (ii) The amount the foreign partner feels should be demanded as a token of good faith from the licensee;
- (iii) The goodwill which the foreign partner feels may be attached to the right to use the industrial property in the particular region.

(b) Continuing royalties

Some ways in which continuing royalties may be computed or expressed are the following:

- (i) As a fixed amount for each unit produced through use of industrial property;
- (ii) As a fixed amount for each unit sold;
- (iii) According to the gross selling price of each unit;
- (iv) According to the net selling price of each unit;
- (v) As differential royalties for units sold abroad and units sold in the host country;
- (vi) As minimum royalty requirements, often based on a rule of thumb;
- (vii) As differential royalties based on the number of units produced or sold, usually varying inversely with quantity;
- (viii) As net royalties, after deduction of all taxes payable by either or both the foreign and the Joint Venture Company to the host country in respect thereof.

It is impossible to specify which basis should be taken for computing a continuing royalty and will be best for industrial joint ventures in developing countries. Some points to be considered are discussed below.

A royalty based on the net selling price is probably better in most instances than one based on either production or the gross selling price because it encourages the foreign partner to do everything possible to maximize the selling profits of the joint company and does not burden the joint company with payments when goods are produced but not sold.

Minimum royalty requirements may provide a certain measure of security to the foreign partner and prevent the joint company from "sitting on the patent". As an equity participant in the joint venture, however, nothing should be done that would enable the foreign partner to profit unreasonably at the expense of the Joint Company.

Licensing agreements often provide for progressively decreasing royalties based on the number of units produced or sold: the greater the number, the smaller the royalty. Such a practice may not be ideal for joint ventures where the foreign partner is the licensor.

Provision for net royalty payment, "net" of all host country taxes, may sometimes be required by the foreign licensor for tax reasons.

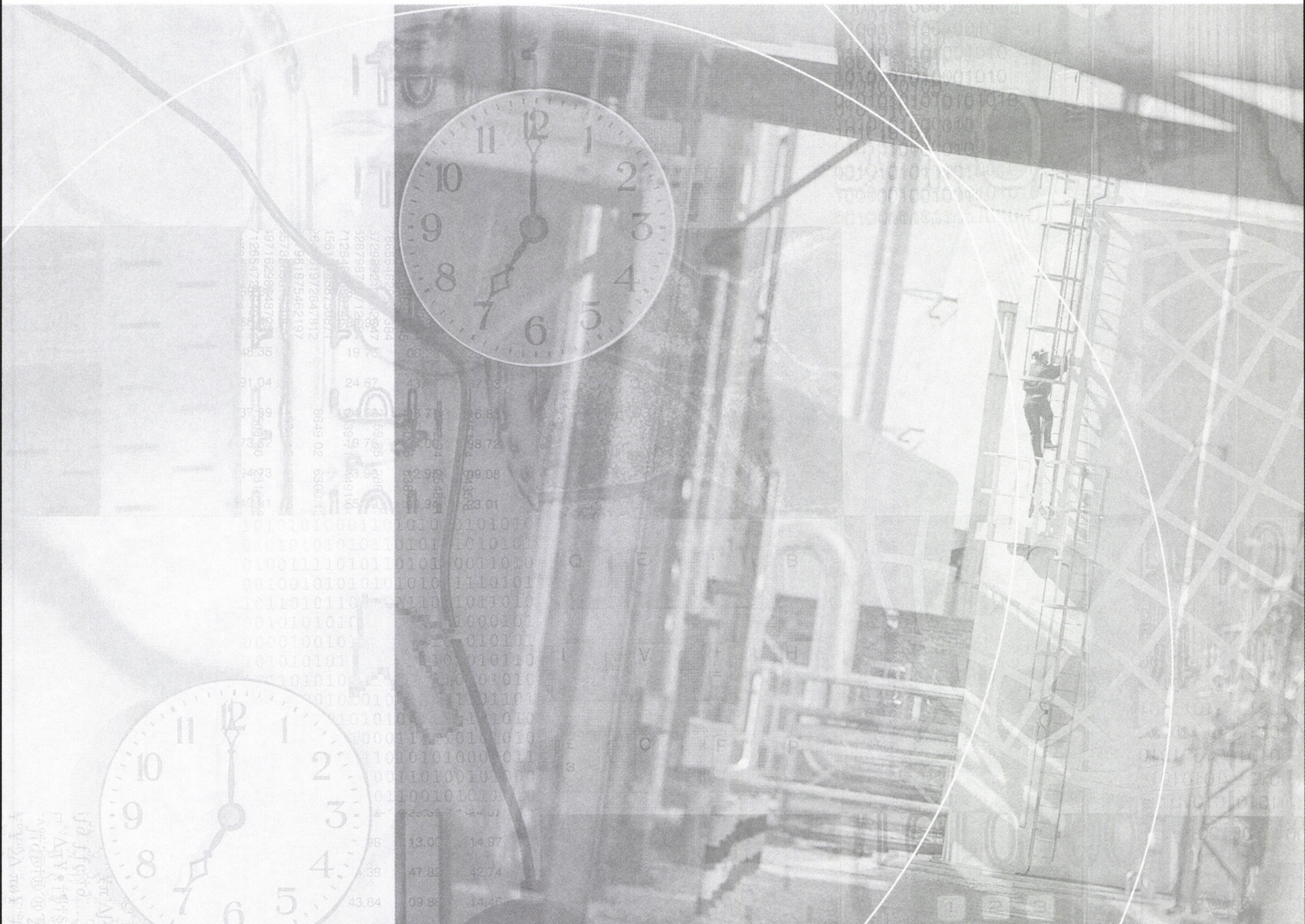
Payment of royalties

There are three issues that arise in respect of the payment of royalties: the currency in which the royalties are to be paid; the form of payment; and the place where it is to be paid.

Sample clause

1. In consideration of the granting of the Licence contained in this Agreement, the Joint Company hereby agrees to pay to the Foreigner within 60 days following the end of the calendar year royalties equal to ... per cent of the net sale prices of all licensed products manufactured and sold by the Joint Company during each year.
2. Licensed products sold by the Joint Company pursuant to the licence herein granted shall be deemed to have been sold when paid for.
3. If the licensed products are returned or deductions are made from the prices on which the royalty has been paid, the Joint Company shall be entitled to make adjustments for such over payment from the royalties to be paid thereafter.
4. Each payment to be made hereunder shall be made in ... (currency); or in the respective currencies in which sales of the licensed products are invoiced by the Joint Company at such place as Foreigner may designate.
5. In lieu of payments as provided for in clause 4 above, the Joint Company shall have the option of satisfying such obligations to pay either:
   (a) Issuing fully paid-up shares in the capital stock of the Joint Company to Foreigner, in which case the shares shall be valued at the higher of either their book value as determined by the auditors of the Joint Company or at their par value, and shall be issued in sufficient multiples so that their aggregate value satisfies but does not surpass the payments due hereunder, with any difference being paid in ... (currency).
   (b) By delivering to Foreigner free on board (nearest point to production facilities in host country), sufficient quantity of the licensed products as listed in the annexed Schedule, to satisfy but not surpass the aggregate payments due hereunder; however, for the purposes of this clause the unit cost of production will be as determined by the auditors of the Joint Company, plus ... percent.
6. Any taxes, duties or imposts other than income or profit taxes assessed or imposed upon the sums due hereunder to Foreigner pursuant to this Agreement, shall be born and discharged by Foreigner, and if so required by law, the Joint Company shall deduct them from any payment to be made to Foreigner under this Agreement.
7. The Joint Company agrees to use its best efforts to obtain necessary approvals from the authorities of (host country) or of any other country, countries or groups of countries falling within its territory for this agreement and for the remittance of payments falling due to the Foreigner under this Agreement.

ANNEX 2. SLIDES PRESENTING KEY ISSUES IN JOINT VENTURES AND STRATEGIC PARTNERSHIPS



JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Joint Ventures and Strategic Partnership Agreements

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

FDI is more powerful than world trade

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Global business context qualitatively different today

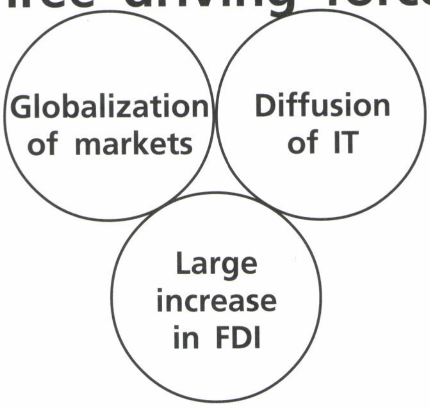
JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

FDI: what it does

- Creates assets
- Adds value
- Drives trade
- Develops skills

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Three driving forces



JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

FDI is enlarging role of international production

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Role of FDI

- Increasing over time
- Profound role on developing countries
- Increasing exports from developing countries

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Disparities remain

Gaps in income between developed and developing countries have increased

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Factors facilitating change

- Flow of global capital
- Removal of trade barriers
- Falling communication costs

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Broad structure of the module

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Market Share

Developing countries' share in world trade is increasing

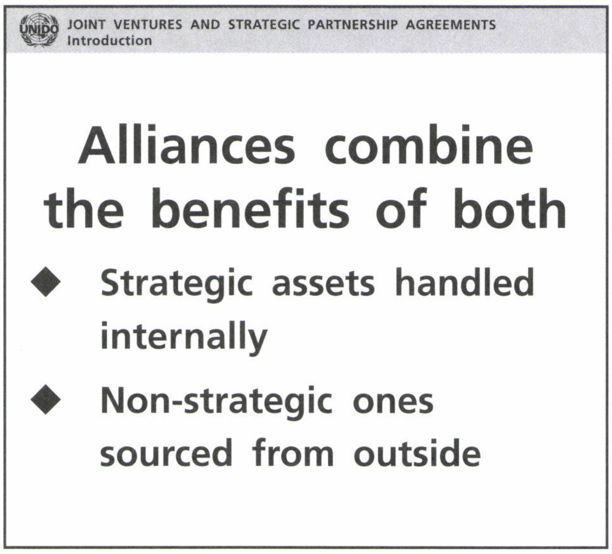
JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction

Structure

- Concept of alliances
- Types of alliances
- Selection of partners
- Negotiating agreements
- Implementing alliances


JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction
Logic of partnership
Competition increasing
Cooperation increasing
Large firms not flexible
Small firms not robust


JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction
Alliance advantages
Upgrade technologies
Use partner network
Acquire proven technology
Licensing
Product swap
Reach new markets


JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction
Alliances combine the benefits of both
Strategic assets handled internally
Non-strategic ones sourced from outside


JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Introduction
Alliances for whom?
Go-it-alone strategy not useful
Alliances not reserved for corporate giants
Alliances create competitive advantage for SMEs

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Section 1

Concept of cooperation

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Need of the day

- Forming alliances
- Managing alliances

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Definition

Two or more firms uniting to pursue a set of agreed goals through independent entities

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Growth

- Local presence
- Global presence
- Cooperative structures

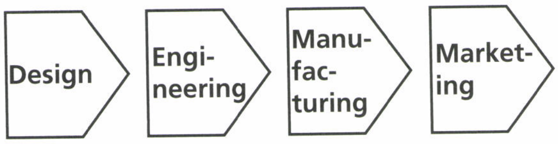
JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

21st Century

Century of corporate alliances

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Importance of alliances



VALUE CHAIN COMPLEMENTARITY

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Firm A: strong in

- Design
- Manufac-turing

Firm B: strong in

- Marketing

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Alliances

- Attract investment
- Enhance capability
- Modernize production

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Alliances of A+B = an invincible combination

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Use of alliances

- R&D partnerships
- Equity investment
- Joint ventures

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Developing countries

- Primary commodity exporters
- Alliances could deepen technological capability

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Concept of cooperation

Networking technologies: driving force of alliances

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Types of cooperative relationships

Section: 2

Types of cooperative relationships

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Types of cooperative relationships

Hierarchies

- Good for assets with high specificity
- Ideal for high-change cost conditions

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Types of cooperative relationships

Business forms

- Markets
- Hierarchies

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Types of cooperative relationships

Networks

- Robust
- Flexible
- Responsive

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Types of cooperative relationships

Markets

- Good for transactions with low-asset specificity
- Fast response
- Ideal for low-change cost or low-transaction cost situations

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Types of cooperative relationships

Advantage of networks

- Reduce uncertainty
- Provide flexibility
- Provide speed
- Provide information
- Share resources
- Reduce risks

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Types of cooperative relationships

FDI and JV

- Upgrading technology
- Move into complex activities
- Increase local inputs and links

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

Section 3

Objectives of joint ventures and partnerships

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

2. Creating networks

Star Alliance

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

1. Sharing resources

Airbus

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

2. Creating networks

SAS ↔ Star Alliance
Lufthansa ↔ Star Alliance
Thai Airways ↔ Star Alliance
Air Canada ↔ Star Alliance
United ↔ Star Alliance

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

Aerospatiale 37.9% → Airbus
Deutsche Airbus 37.9 % → Airbus
British Aerospace 20% → Airbus
CASA 4.2% → Airbus

% denotes share in equity

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

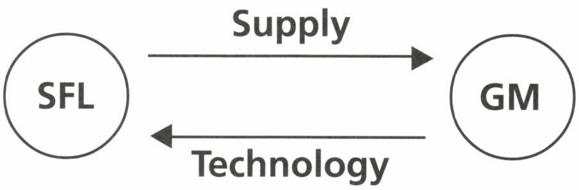
Alliance objective

"Cooperate to the extent necessary to create a seamless air transport system while retaining their corporate and national identities"

Delta Airlines

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

3. Leveraging competence



Supplier alliances

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

4. Reducing risks

Franchise alliances

- KFC
- Pizza Hut
- McDonalds

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

5. Expanding Markets

Fuji — Xerox (Japan)

Korea — Xerox (Korea)

Modi — Xerox (India)

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Objectives of joint ventures and partnerships

Alliances

- Leveraging competencies
- Creating win-win situations
- Minimizing investment risk

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Section 4

Identification of alliance opportunities

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Alliances: similar to make or buy decision

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Why alliances?

If a firm has all the resources, no alliances needed

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

The basic question

Could we join together and create a win-win situation?

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Tool for decision making

Opportunity – competence matrix

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Opportunity – competence matrix: a tool for identifying asset and capability complementarities

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Market opportunity			
High			
Low	Buy	Buy	Buy
	Low		High

Competence

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Market opportunity high and internal competence low:

need to go in for alliances

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Opportunity			
High		Invest and Make	Do it your- self
			Do it your- self
Low			
	Low		High

Competence

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Market opportunity high and internal competence high:

do it yourself

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Opportunity			
High	Alliance		
	Alliance	Alliance	
Low			
	Low		High

Competence

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

If opportunity low:

should be outsourced even if the firm is proficient

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Identification of opportunities

Creating a criteria for prioritization:

critical success factor in each industry different

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Section 5

Alliance format

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliance format options (1)

- Sales representation agreement
- Original equipment manufacturing
- Franchising
- Licensing
- Cross licensing
- Technical services

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliance format

- Competence identification
- Alliance format

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliance format options (2)

- Engineering agreements
- Joint R&D
- Joint manufacturing
- Equity swaps
- Joint ventures

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliance format options

- Contractual arrangements
- Equity arrangements

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliance intensity categories

- Sales and services
- Manufacturing, sales and services
- Research, manufacturing, sales and services

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliances: Sales & Services

Level I

- Risks involved are low
- Learning potential low
- Returns are quick
- Could be terminated easily

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliances for consumer products marketing

Level I Alliance

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliances: Manufacturing & Services

Level II

- This requires investment
- Time required for recouping investment
- Intellectual Property Rights support essential

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliances for high tech products

Level III Alliance

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

Alliances: Research & Manufacturing

Level III

- Succeeds only when there is strong product acceptance
- Investment high
- Time horizons available are long

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selecting the format

High intensity alliances

- Partner assessment, market assessment and investment analysis critical

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Section 6

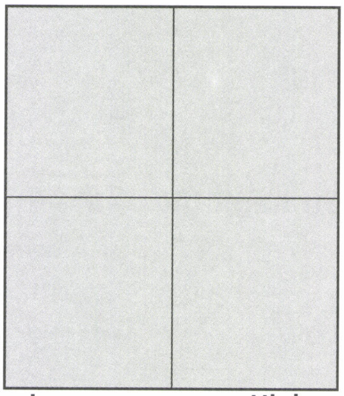
Selection of partners

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

High

Strategic fit

Low



Low High

Cultural fit

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

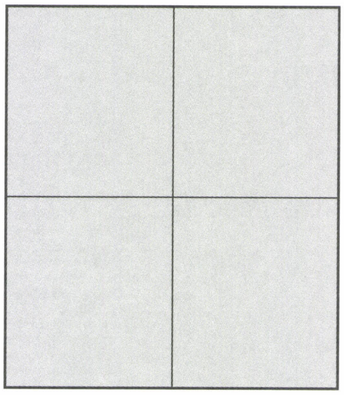
Partner assessment

- Fit
- Risk
- Antecedents
- Trust

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

What to do

Strategic fit



Cultural fit
How to do it

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

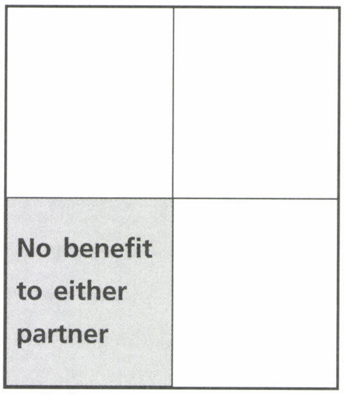
Strategic and cultural fit assessment

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

High

Strategic fit

Low



High Low

Cultural fit

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Strategic fit	Cultural fit: High	Cultural fit: Low
High		
Low	No benefit to either partner	No distinct competitive advantage

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Strategic fit	Cultural fit: High	Cultural fit: Low
High	Conflicts and problems	
Low	No benefit to either partner	No distinct competitive advantage

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Strategic fit	Cultural fit: High	Cultural fit: Low
High	Conflicts and problems	Synergy and harmony
Low	No benefit to either partner	No distinct competitive advantage

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Risk mapping

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Types of risk (1)

- Market
- Competitive technology
- Technology
- Environmental
- Management

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Types of risk (2)

- Political
- Resources
- Capital
- Prospective partner
- Compounded

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Monitoring antecedents

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Criteria

- Ideal characteristics of partner
- Whether existing partner could be a candidate

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Monitoring antecedents

- Strategic intent
- Credit worthiness
- Alliance antecedents
- Liabilities

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Alliances & trust

- Inter-organizational cooperation requires trust
- Trust is the most important variable in partnerships
- Trust is the basis of long-term relationship

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Developing partner selection criteria

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Trust is the glue that binds the partners

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Trust is the bandwidth of communication among the partners

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Practices that earn trust

- Clear scope
- Realistic plans
- Right structure
- Effective governance

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Essential conditions

- Shared objectives
- Close relationships
- Mutual need

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Selection of partners

Trust is crucial in networks and partnerships

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Section 7

Negotiating agreements

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Negotiations

Time for operationalizing win-win situations

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Good negotiations

- Clear expectations
- Plans for managing
- Contributions of partners
- Useful solutions to potential problems

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

1 Statement of purpose

- Concept of alliance
- Clarity on operations
- Structural clarity
- Benefits

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Negotiations

Require considerable preparation and, after negotiations, changes are not easy

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Important negotiating points

- Equity structure
- Technology transfer
- Marketing issues
- Staffing issues
- Dividend policy

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

2 Operational differential profiling of partners

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

3 Selecting a negotiating team

- The chief negotiator
- The role of top management
- Cultural sensitivity

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Ten critical parameters

- Time orientation
- Individualism
- Communication
- Organizational culture
- Labour relations

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

4 Structuring the venture

- Functional alliances

  or
- Equity alliances

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Ten critical parameters

- Information
- Technology
- Management style
- Business-government relations
- Environmental rate of change

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Functional alliances

- Joint manufacturing
- Technical assistance
- Joint marketing
- Cross distribution
- Cross licensing
- Research pooling
- Consortia

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Functional alliances

- More flexible
- Easily rewritable
- Could be converted to equity alliances
- Ideal for learning

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Equity alliances

- Technology needs high
- Equity needed
- Technology transfer needed

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Functional alliances

- No assets could be held
- Need higher degree of trust
- Short-term needs

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Aspects in equity alliances

- Equity breakdown
- Scope of alliances
- Combination of functions
- Delineating business segments

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Equity alliances

- Investments high
- Its own identity
- Needs clear strategy
- Similar to new firms

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

5 Control in alliances

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Control

- Power to command strategic resources
- Authority and rights
- Expertise needed to manage
- Rewards to offer compensation

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

7 Financial aspects

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

6 Intellectual property

- Patents
- Designs
- Copyrights
- Trademarks

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Financial aspects

- Funds
- Capital structure
- Exit

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

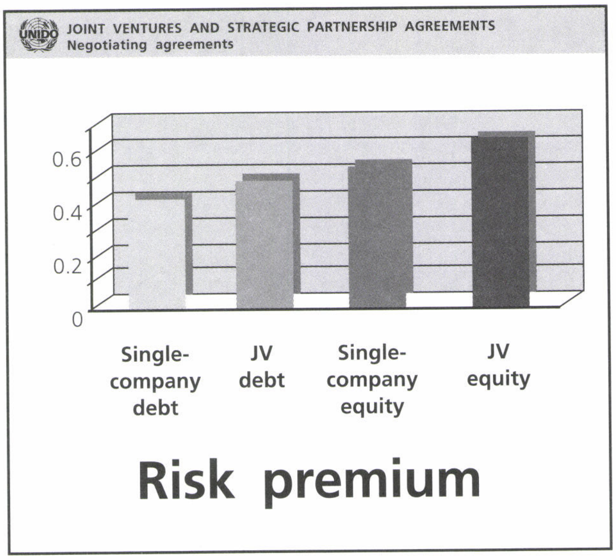
Issues in intellectual property rights

- Confidentiality
- Terms of transactions
- Warranties
- Legal considerations
- Assignments

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Risk premium

- Cost of funds a function of rating
- Joint ventures are considered a high-risk category

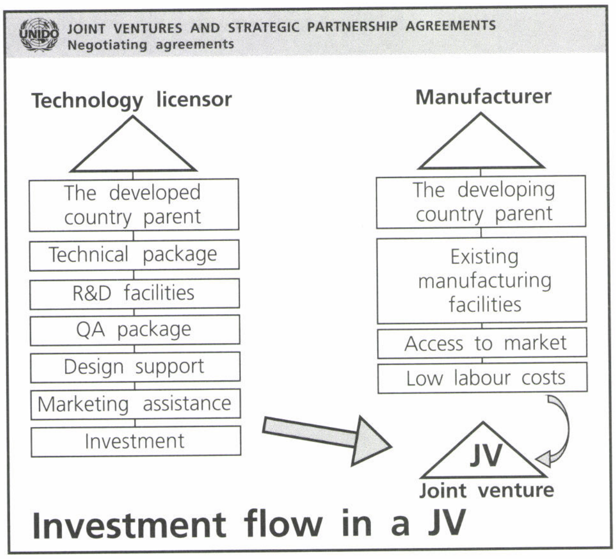


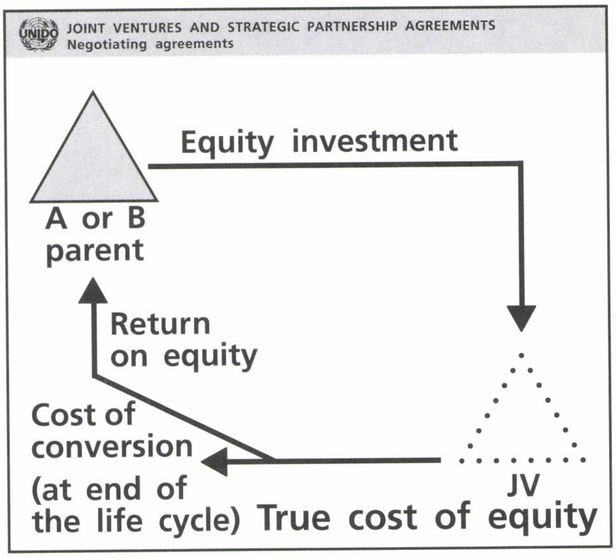
JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Typical investment flow in a joint venture

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

True cost of equity to joint venture is different





JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Alliance evolution

Financial issues change over time

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Negotiating agreements

Negotiations require considerable preparation

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Section 8
Dispute Reduction

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Problems in prealliance phase 1

- Unclear strategy
- Weak core
- Poor alliance strategy
- Pressure to do a deal

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Disputes in alliance

Inter-parent disputers are commonplace

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Problems in prealliance phase 2

- Hurried due diligence
- Overvalued targets
- Overestimated returns
- Overestimated synergies

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Dispute potential in the three phases

- Pre-alliance phase
- Alliance phase
- Post-alliance phase

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Problems in operational phase 1

- Integration seen as a distraction
- Misunderstood optical success factors
- Organizational aspects ignored

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Problems in operational phase 2

- Cultural differences
- Increased centralization
- Decreased communication

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Problems in post adjustment phase 2

- Coordination snags
- Poor attention to team building
- Missed opportunities

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Post-alliance is the adjustment phase

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Types of disputes

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Problems in post adjustment phase 1

- Rushed implementation
- Insufficient resources
- Unanticipated implementation obstacles

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

1 Management style disputes

- Unclear targets
- Lack of details
- Process disagreements

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

2 Financial disputes

- Funding
- Cost
- Pricing

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

3 Cost disputes

- Frequent changes in currency exchange rates
- Inter-parent disputes

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

4 Pricing disputes

- Transfer pricing
- Occurs at all phases
- Routinely occurring

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

5 Anti-competition disputes

- One party acting as a competitor
- Third party disputes
- Quality disputes
- Service disputes

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Dispute reduction mechanisms

- Matching structure
- Encouraging closeness
- Selecting suitable people

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

"Don't give up on alliances; work them harder, manage them better and build them with more intelligence"

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Critical incident early warning indicators 1

- Back-burner
- Missed deadlines
- Role conflict
- Winners and losers
- Cost overruns

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Dispute reduction

Critical incident early warning indicators 2

- Missed goals
- Missed milestones
- Missing communications

Source: ***Lynch***

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Implementing strategic partnerships and joint ventures

Section 9

Implementing strategic partnerships and joint ventures

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Implementing strategic partnerships and joint ventures

Main issues

- Operational
- Learning
- Ending alliances

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Implementing strategic partnerships and joint ventures

Operational issues 1

- Managing alliance is different
- Managing alliance needs a different mindset

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Implementing strategic partnerships and joint ventures

Operational issues 2

- Entail many surprises
- Both trust and mutual interest needed

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Implementing strategic partnerships and joint ventures

Guiding principles

- Manage partners as equals
- Attract top support
- Manage diversity, do not resist it

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Implementing strategic partnerships and joint ventures

Learning

- Technical
- Systematic
- Strategic

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Implementing strategic partnerships and joint ventures

Airbus-Tenzing

- Learning and creating new markets

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Implementing strategic partnerships and joint ventures

Ending alliances

- Function of time and resources

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

Section: 10

Lessons from previous experiences

- ◆ Strategy essential

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

8. Contribution
9. Participation
10. Sharing the profits
11. Sharing the assets
12. Sharing the losses
13. Working capital account
14. Surety ship

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

Alliance strategy

- ◆ Strategy essential
- ◆ Strategy should be integrated with business strategy
- ◆ Strategy should be supported by vision

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

15. Books
16. Fiscal year
17. Use of joint venture's name
18. Cost and expenses
19. Compliance with low
20. Permits
21. Taxes
22. Joint liability

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

Model agreement: clauses

1. Object
2. Duties
3. Members
4. Decisions
5. Minutes
6. Joint liability
7. Bank transactions

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

23. Transfer
24. Collaboration

- ◆ Services
- ◆ Billing
- ◆ Quality
- ◆ Common property
- ◆ Exit

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

1 Joint ventures are useful but require careful planning

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

2 Trust and mutual interest are essential for success

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

3 Alliances have to be designed for maximum learning

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

4 To be useful, alliances have to be driven by strategic vision

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

5 Personal, cultural and strategic compatibility are essential

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

6 There has to be built-in dispute reduction mechanisms

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

7 **Communication at all levels is crucial for success**

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

8 **When the objective is short-term, functional alliances are useful**

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

9 **When the objectives are long-term, equity alliances are useful**

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

10 **A win-win perspective will bring in a cordial relationship**

JOINT VENTURES AND STRATEGIC PARTNERSHIP AGREEMENTS
Lessons from previous experiences

"We cannot negotiate with those who say: what is mine is mine and what's yours is negotiable"

J.F. Kennedy

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