Week 7: Engaging in Cross-Boarder Collaboration: JV

What is a Strategic Alliance?

- A strategic alliance is a formal and mutually agreed commercial collaboration between companies.
- As a result, the partners pool, exchange or integrate specific business resources in which both partners will benefit.
- Yet they remain separate businesses, making these alliances (join ventures) different to mergers and acquisitions.
- By forming alliances and partnership, organisations are able to develop, produce their products more quickly and penetrate the market by introducing the new product.
- It should be noted that; sometimes, doing it alone will be slower.
- There is a strategy known as 'Asset light strategy' – Using less assets, your return on asset ratio will be greater.
- **Merger and acquistions are not a strategic alliance because once both these companies 'merge' then they are one company. – Important for quiz –**

Strategic Alliances

- Strategic alliance is one of the many forms of commercial interaction.
- It is just one of four forms of investment.

	Partially Owned	Wholly Owned
Existing	Capital Participation	Acquisition
New	Joint Venture	Greenfield

- Capital participation refers to buying their shares (partially own a company)
- Joint Ventures – a brand new company

Popular Views of Joint Ventures

- A transitional organisation form
- A strategic alliance is less profitable
- Often impossible to manage
- Its very risky in terms of the partner 'backstabbing' the other and stealing their technology or intellectual property.
- Only undertaken as a last resort.

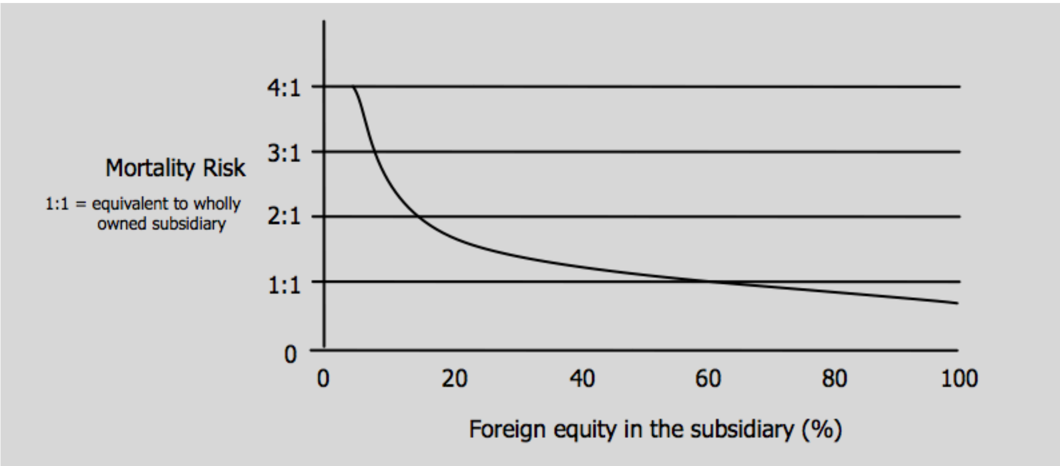
However, the reality is quite different;

- The average age of international JV is nearly 10 yrs

- Profitability identical with other organizational alternatives.
- Managing joint ventures have become easier, so the utilisation of such a structure have increased.
    - 40% of all investments in Asia Pacific are JVs.
- It is not the last resort. It is now the first resort because an alliance with competitors or rivals can yield better innovations.
- Some companies which possess strong technology often prefer to use JVs.
- Even the very largest MNCs have recognized the investment and growth benefits associated with partnering, rather than "going it alone" (i.e., Dow Chemical's "asset-light strategy").

<u>Effect of Foreign equity holding on subsidiary morality risk</u>

- The more shares or more equity that foreign companies own of another company (joint venture), the greater the chance of the surviving.
- This is because companies will be more committed in seeing their company succeed as they have invested a large amount. There will be more managerial resources and attention into the company to ensure its success.



<u>Join Venture checklist: How to choose a partner</u>

1. Test the strategic logic
    - Do you really need a partner? For how long? Does your partner need you?
    - How big is the payoff for both parties? How likely is success?
      - Both parties must receive equal benefits
    - Is a joint venture the best option?
    - Ensure congruent performance measures exist.

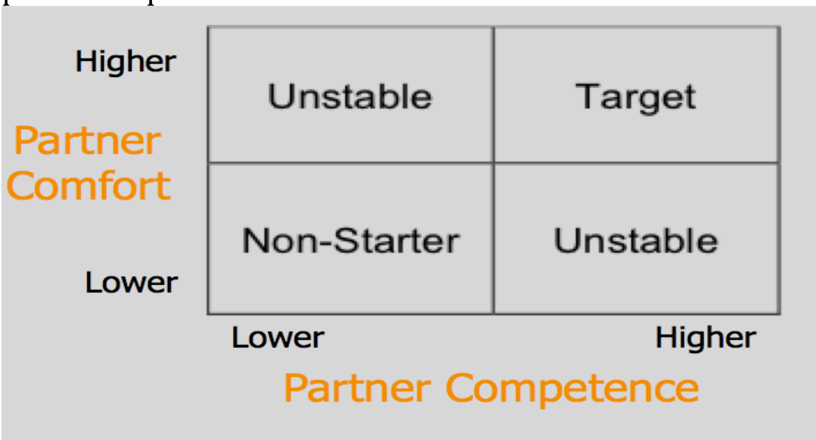
In relation to the 'both parties must receive equal benefits':
Due to the ratification in the WTO, Eli Lilly did not need Ranbaxy anymore. They could 100% establish themselves as a company in the Indian market. As such, Rambaxy realizes this and sells their company to Eli Lilly. There was a good relationship until one started benefiting more than the other.

2. Partnership and fit.
    - Does the partner share your objectives for the venture?
      - Organisational cultural fit is important.

- Does the partner have the necessary skills and resources? Will you get access to them?
- Will you be compatible?
- Can you arrange an “engagement period”?
- **Is there a comfort versus competence trade-off?**

<u>Comfort vs Competence</u>

- It should be noted that there will never be a perfect partner.
- Therefore, you must choose the best alternative and help to improve their ‘not so good’ aspects as long as they have to capability to improve.
- Below is a chart to determine whether or not to pursue a joint venture partnership with them:



<u>What do you want from your partner? Talks about motivation</u>

- When both companies want access to knowledge this is the ideal position (Top left)
- Other mixed motives will eventually cause an unstable relationship. (Bottom left and top right)
- If both companies want to acquire knowledge through deception, this will be a very unstable join venture partnership. (Bottom right)

		Parent A	
		WANTS ACCESS TO PARTNER'S KNOWLEDGE	WANTS ACQUISITION OF PARTNER'S KNOWLEDGE
Parent B	WANTS ACCESS TO PARTNER'S KNOWLEDGE	The Classic “Joint” Venture - A cooperative alliance (very stable)	Mixed Motive - A pseudo alliance (eventually unstable)
Parent B	WANTS ACQUISITION OF PARTNER'S KNOWLEDGE	Mixed Motive - A pseudo alliance (eventually unstable)	“Race to Learn” - A competitive alliance (very unstable)

How do we make Joint Ventures happen?

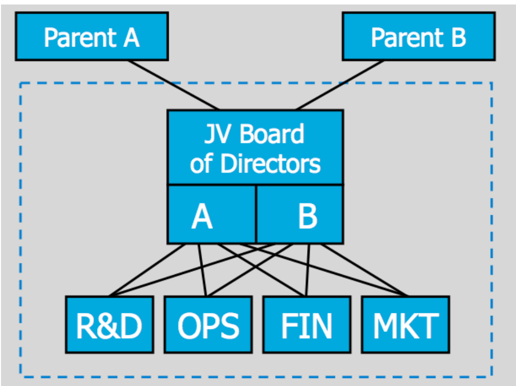
3. Shape and design.
    - Define the venture's scope of activity and its strategic freedom in relation to its parents.
    - Lay out each parent's duties and payoffs to create a win-win situation. Ensure that there are comparable contributions over time.
        - Make sure both parties benefit equally
    - Establish the managerial role of each partner.
        - Ensure that the new company alliance doesn't die. There must be participation by both companies to ensure stability and survival in the business environment.
    - Ultimately, an alliance's governance structure must include clear rules pertaining to decision-making among the entity's partners and its general manager.

Control of Joint Ventures

1. One parent dominates the venture's decision making (...but is this a "joint" venture?)
2. Parents are both involved in decision making
    - Shared
    - Split

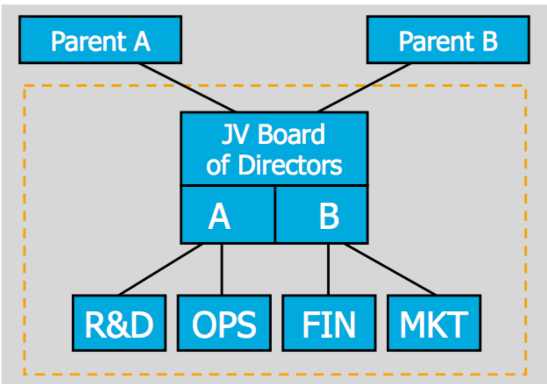
Shared Control:

- Company A & B will both appoint people from their companies to manage a division. A shared and co-operative approach.



Split Control:

- Whichever function the company is good or specialised at they will split their responsibility.



Joint Venture checklist Continued

4. Doing the deal.
    - How much paperwork is enough? Trust versus legal considerations?
        - This refers to a contract. It should be noted that companies should not find comfort in agreements. Not everyone will obey their obligations. However, you should look for comfort and confidence in partners. Eg: In Ranbaxy and Eli Lilly's situation, both were ethical businesses and leaders and they took comfort in knowing that both would not deceive the other.
    - Agree on an endgame: Agreements on what breaches or scenarios will end a partnership. Termination of partnership.
5. Making the venture work.
    - Give the venture continuing top management attention.
    - Manage cultural differences.
    - Watch out for inequities.
    - **Be flexible – When an agreement is not working, make compromises. Think strategically. What will be the effects of your actions? Sometimes things change and compromises will need to be made.**

In Summary:

	The True Alliance	The Pseudo Alliance
Planned level of parent input and involvement	Continuing	One-time
Distribution of risks/rewards	Roughly even	Uneven
Parent attitude toward the JV	A unique organization with unique needs	One more subsidiary
The formal agreement	Flexible guideline	Frequently referenced rulebook
Performance objectives	Clearly specified and congruent	Partially overlapping/ ambiguous