# Joint venture as strategy for international market entry: an introductory survey

*Eltayeb Mohamed Elgobbi*[*]

## Introduction

The rapid growth of international activities is one of the most significant developments in a business practice in recent years. Therefore, a large number of firms enter new international markets in order to source components more competitively and also to enter new growing product markets holding more promise than the domestic market. The market entry concept relates to ease or difficulty with which a firm can become a member of a group of competing firms by producing a close substitute for the products they are offering. Consequently, entering new markets may be achieved in a variety of ways, e.g. joint ventures and foreign direct investment and acquisition, exporting and its various derivatives, competitive alliances in their various forms including marketing co-operation agreements, licences, franchising. According to Terpstra and Sarathy (1997) the selection of the methods of entry to foreign markets depends on some factors peculiar to the firm and its industry, for example, company goals regarding the volume of international business desired, geographic coverage, and the firm span of foreign involvement; the size of the company in sales and assists; the

* Faculty of Economics, Altahadi University.

company's product line and the nature of its products (high or low price, industrial or consumer).

This paper investigates and looks at the joint venture as a strategy for international market entry. It is divided into three main sections excluding the introduction. The first section tries to define joint venture as a method of entering foreign markets. The second section covers the advantages and disadvantages of this method of entry, while the third and final section summaries and draws together some of the key issues raised by the study, and analyses material from earlier sections.

**Definition**

Joint ventures are described by Johnson and Scholes (1993) as arrangements whereby parent organisations remain independent but set up a new and separate organisation that is jointly owned by the two parents. Joint ventures is also defined by Bennett (1996) as collaborative arrangements between unrelated parties which exchange or combine various resources while remaining separate and independent legal entities. Moreover, Walsh (1994) defines an international joint venture as an operation in which two or more companies in different countries join forces, not merely for manufacturing purposes but also (usually) for marketing, financial and management advantage, and all participants have both a share in the equity and voice in management, Gilligan and Hird (1989) note that the two major attractions of joint venture management are firstly, that the returns are generally higher and, secondly, that the company can exert a degree of control over the production and marketing operation. According to Finnerty et al (1986) the participants are partners rather than an acquirer and a target, and thus the formation of a joint venture does not provide the opportunity for one party to be the aggressor as in the whole unit combination. Further to this Czinkota and Ronkainen (1993) note that the participating partners share assets, risks, and profits. Equality of partners is not necessary. In some joint ventures, each partner holds

an equal share; in others, one partner has the majority of shares. Again according to Gilligan and Hird (1989) the formation of joint ventures is frequently cited as a way of reducing risk to the partners. The essential feature of a joint venture is that no one participant holds a sufficient shareholding to exercise effective managerial control.

According to Bennett (1996) there are two types of Joint venture: equity and contractual. The first type involves each partner taking an equity stake in the venture, while the second type relies on contractual agreements between the partners.

**Advantages and disadvantages of joint ventures**

Joint ventures have advantages and disadvantages. The following points cover both of them.

**Firstly: Advantages and Benefits of Joint ventures**

Joint ventures are commonly used because they offer important advantages to the foreign firm. By bringing in a partner, the company can share the risk for a new venture. Moreover, the joint venture partner may have important skills or contacts of value to the international firm, sometimes; the partner may be an important customer who is willing to contract for a portion of new units output in return for an equity participation. In other cases, the partner may represent important local business interests with excellent contacts to the government. A firm with advanced product technology may also gain market access through the joint venture route by teaming up with companies that are prepared to distribute its products (Hennessey 1992). Furthermore, Terpestra and Sarathy (1997) lists the following advantages of Joint ventures:

- Greater control over production and marketing.
- Potentially greater returns from equity participation as apposed to royalties.
- Better market feedback.
- More experience in international marketing.

There are also several reasons why joint ventures enjoy certain benefits. Onkvisit and Shaw (1993) mention that some of these benefits substantially reduce the amount of resources (money and personnel) that each partner must contribute. Joint venture can also give benefits to organisations; these benefits can be categorised into two segments. Firstly the economic benefits of having two parties involved in the same business project, and secondly the non - economic benefits of working with another organisation with deferent skill areas or culture. Datta (1988) lists the economic benefits to include, reductions in factor cost; transportation costs through the use of the local organisation's transport facilities; general overheads such as wages, and taxes e.g. the avoidance of importation taxes through producing locally. The non-economic benefits include the loss of a drain on managerial resources that on organisation would incur; should it choose to set up a wholly owned subsidiary as with an international joint venture, the partner in the host country would be able to manage the venture. In addition, there are other benefits of joint ventures, which are:

**Access to resources.**

- Rapid product diversification strategies as means of corporate growth favours joint ventures.
- Provide funds and access to local capital markets.
- Each partner concentrates resources on an area of greatest advantage.
- Avoid necessity of developing international management skills.
- Access to knowledge of local environment and markets.
- May reach critical mass for internationalisation.
- More efficient competitive position.

**Political pressures.**

- Meets host country pressure for local participation.
- Provides local control of job creation and technology transfer.

- Preferential treatment (remittance of royalties).
- May avoid local tariff and non - tariff barriers.

**Facilitates technology transfer.**

- Codification/public knowledge.
- Converting head knowledge to production.
- Impact of technology on marketing relationships.
- Discovery of price of technology.

**Other reasons.**

- Good public relations.
- Curbs potential competition.
- Provides temporary relief for weak product portfolio.

**Secondly: Disadvantages of joint ventures**

On the other hand, joint ventures have some disadvantages to the involved partners. Bennett (1996) lists the following disadvantages:

- Partners may become locked into long - term investments from which it is difficult to withdraw.
- Problems of co - ordination.
- Profits have to be shared with partners.
- Completion of a joint venture project might overburden a company's staff.
- Need to share intellectual property.
- Difficulties associated with the integration of a joint venture into an overall corporate strategy.
- Partners are not free to act independently.
- Transfer pricing problems may arise as goods pass between partners.

- The importance of the venture to each partner might change over time.

Terpstra and Sarathy (1997) indicate that the major consideration favouring joint venture entry is oligolistic competition. In industries characterised by a small number of competitors, the foreign firm may find entry barriers to high for solo entry into a market. It may need to join with a competing firm or a firm in a complementary line to have a viable presence in the market. For example, Bols and Heineken formed a joint venture to survive in the merging European market. Molson and Elders joined together to maintain a share of the UK beer market. When Coca - cola joined with Cadbury - Schweppes in the UK, Pepsi responded by joining with three British brewers. In Brazil, Pepsi joined with Brahma, Brazil's largest brewer, to gain market share against the leader coke.

The stability of any business organisation is influenced by number of factors. Bradley (1995) notes that Joint ventures may be criticised because they are unstable for a variety of reasons, because they may be instrumental in creating a competitor, and because the costs of control becomes high. Taking the instability issue first, many studies have highlighted the high break - up rate of joint ventures (Killing 1983). The cost of controlling the joint venture becomes significant. The need for control strengthens the argument for unambiguous control within a single firm (Bradly 1995). Moreover, Kogut (1988) states that some current work suggests, that joint venture stability is influenced jointly by competitive incentives among partners and competitive changes in industry structure. However, Killing (1983) argues that ventures are a means to resolve competitive conflicts inherent in economic relationships or to affect the competitive positioning of a firm relative to rivals, including buyers and suppliers. But ventures motivated on the bases of competition are unlnerable to changes in bargaining power of the partners and in competitive structure of the market, whereas the design of the venture and overall partner relationship can mitigate competitive incentives.

Pearce and Robinson (1991) believe that joint ventures still entail huge costs when used at wrong time, the loss of control is real, as are the risks of creating new competitors, damaging the firm's reputation, and eroding its technological edge. As a result of such a costs, joint ventures are often not stable. According to Kogut (1988) a joint venture can be destabilised also by the degree of co - operation and competitive behaviour among the partners. To isolate the factors which are unique in influencing joint venture stability requires analysing the stability of co - operative and competitive incentives among the partners. Changes in the environment, of strategies, and bargaining power over the life of venture can affect dramatically the longevity of co-operation.

In any joint venture, disagreements are yet more likely to arise. In any joint venture there is an inherent conflict of interest. Walsh (1994) states that the disagreements in the case of an international joint venture, comes as a result of national differences in culture, business practices and management styles, and also of the inadequate communications arising from both distance and language problems. Killing (1982) argues that managers of international joint ventures may not only have communication problems because of language barriers; they may also have different attitudes towards time, the importance of job performance, material wealth, and the desirability of change. For example, an American - Iranian venture did have problems until a new general manager sent most of the American back home, they could not adapt to dealing with the workforce that they had. The American replaced with Iranians who were first sent for short training periods with the U.S parent. Performance improved considerably. Furthermore, according to Hennessey (1992) the international firm can no longer function independently, which sometimes leads to inefficiencies and disputes over responsibility for the venture, he believes that if international firm has strictly defined operating procedures such as for budgeting, planning, and marketing, it may become difficult to get the joint venture company to accept the same methods

of operation. The joint ventures may, for example, identify a particular market as a profitable target, yet the headquarters of one of the partners may already have plans for serving this market, plans that would require competing against its own joint venture «divorce» is disagreement about third - country markets where partners face each other as actual or potential competitors. Again according to Hennessey (1995) problems may also arise when the joint venture partner wants to maximise dividend payout instead of reinvestment, or when the capital of the joint venture has to be increased and one side is unable to raise the required funds. Killing (1982) believes that the problems in managing joint ventures stem from one cause; there is more than one parent. The owners, unlike the shareholders of a large publicly owned corporation, are visible and powerful. They can - and will disagree on just about any thing; How fast should the joint venture grow? Which products and markets should it encompass? How should it be organised? What constitutes good or bad management? Therefore, it is essential to minimise the possibility of these disagreements and conflicts. Walsh (1994) suggests some strategies to minimise the possibility of conflict by:

- Undertaking the most careful and detailed evaluation of joint venture partners.
- Negotiatiating a joint venture agreement of benefit to both sides.
- Covering in that agreement all eventualities that might reasonably be expected to give rise to different opinion.
- Arranging in advance some mechanism by which any unforessen disagreements can be resolved.

A major cause of failure in joint ventures is the inability on the part of one of the partners to understand the external environment factors: cultural differences; government rules and regulations; the market, sources of supply, competition, and currency movement (Bradly 1995). Therefore, international joint ventures are difficult to manage Datt (1988). Furthermore, not all joint ventures are successful and ful-

fil their partners' expectation. Killing (1982) believes that joint ventures do have a high overall failure rate, and many of the failures are very costly for the partner companies. According to a study done by the Boston Consulting Group, more than 90 ventures in Japan collapsed between 1972 and mid - 1976. Many of these were large ventures that involved Prominent U.S companies such as Avis, Sterling Drug, General Mills, and TRW. The most fundamental problem was the different benefits that each side expected to receive. Furthermore, according to Franko cited in Keegan and Green (1997) a study of 170 multinational firms, more than one - third of 1,100 joint ventures were unstable, ending in divorce or a significant increase in the U.S firm's power over its partners, In most cases, the ventures were either liquidated of taken over by one of the original partners. Financial Times (22 January 1990) reported the following items for a checklist for successful joint ventures.

- Do not enter joint ventures with partners that are initially over-concerned with control or how to split up if venture should fail.
- The venture must be able to get the resources to grow and should not be restricted technologically or geographically.
- The venture must develop its own culture.
- Venture managers need good access to top management at the parent companies.
- Stay a way from partners who are overly centralised and have no experience in sharing responsibility.

Joint ventures can be affected by choosing the wrong partner, who can, for a number of reasons spell disasters. Root (1994) states that the most critical decision in joint venture entry is the choice of the local partner. For that reason, joint ventures are often compared to marriages. And like marriages, joint ventures frequently end in divorce when one or both partners conclude they can benefit by breaking their association. Therefore, before any joint venture is formed the potential partners should recognise the differences in their objectives

and then take the necessary steps in reconciling them. Killing (1983) believes that one of the greatest problems with partner selection is that many of the characteristics which one might be willing to agree are generally desirable, such as honesty, dependability and trustworthiness. Lorange and Roos (1992) suggest that a firm must be clear of what itself needs from a joint venture partners. This involves examining its own core competence and calculating what needs to be added in order to gain a competitive advantage in the target market.

Joint ventures are useful in any country, which restricts market entry by exporting through tariff or non - tariff barriers (Bradley 1995). However, Hennessey (1992) believes that joint ventures are sometimes necessary to enter countries where the economy is largly under state control. In such countries, foreign investors are only allowed to take minority positions in conjunction with local firms. In this case of government controlled economies, this means a joint venture must be signed with government - owned firm. Warren and Green (1997) state that a joint venture may be the only way to enter a country its government bid award practices routinely and favor local companies or its laws prohibit foreign control but permit joint venture.

People have the potential to make or break a joint venture. Therefore, management must be highly qualified and capable of being able to ensure that the demanded goals are fulfilled. Lorange and Roos (1992) claim, it is the responsibility of each party to assign human resources, which will reflect the specialised skills and qualities of each partner agreed upon when forming the venture. Killing (1983) says that it is probably best for a joint venture to be successful if its managers develop into an effective, cohesive, operational team.

**Example: Successful joint venture**

**Gillette,** The U.S. razor company blade manufacturer, is a successful joint venture company. It has gone through extensive joint venture experience in Japan. In the early 1980s, the company formed a first, small joint venture called Shenmei Daily Use Products with Chinese authorities in a province Northeast of Beijing. That plant had produced older - technology blades under a local brand name for a several years. However, annual production was only sixty million units in the market of one billion units, and the Northern location was too far away from the booming provinces in the south. So a second joint venture was formed with the Shanghai Razor Factory. Gillette obtained 70 percent ownership and management control, The company employs about one thousand people and has allowed Gillette to boost its market share in China from 10 percent to 70 percent.

**Example: Unsuccessful joint venture**

Borden Inc., a U.S. -based dairy company with world-wide sales of some $7 billion, was one of the companies, which faced difficulties with its JV in Japan. Originally entering Japan in the early 1997s, Borden joined up with Meiji Milk Products of Japan to form several Joint ventures. Meiji had produced Borden branded ice cream since 1971 and margarine since 1983. Borden cheese was made part of a different venture in 1972. By 1990, sales for the three product categories in Japan had reached $192 million. However, Borden felt that, with the liberalisation of the dairy business in Japan, a major expansion to some $400 million was possible. A major disagreement developed over the ice cream business, where the Lady Borden brand had slipped from its 60 percent of imported premium to about 50 percent. Major competitors were now Haagen - Dazs and Dreyer, both U.S. entries. Faced with increasing competition but also more opportunities, Borden reportedly demanded a higher performance from Meiji as a precondition for extending its arrangements. Over the talks, the companies broke up. The three agreements expired in 1990.

**Summary**

There are several methods to enter the international markets. Joint venture is one of these methods, which means joining the forces and resources of two or more companies in different countries. Joint ventures are the only means of entering some markets, especially those where public policy encourages the transfer of technology and Know - how to local firms. Joint ventures tend to reduce the risk involved since the capital is shared between the partners. The benefits of joint ventures include ease of technology transfer, access to resources, ability to comply with political pressure and access to markets. However, ventures have some disadvantages, such as partners are not free to act independently and the profits have to be shared with partners. In addition, ventures may face some disagreements and difficulties due to national differences in culture, management styles, and also the inadequate communications due to language problems.

Despite the difficulties involved, it is apparent that the future will bring many more joint ventures. Successful international firms will have to develop the skills and experience to manage joint ventures effectively, often in different and difficult environmental circumstances.

# References


- Bennett, R (1996) **International Business.** Pitman publishing, the UK.
- Bradley, F (1995) **International marketing strategy,** Prentice hall. UK.
- Czinkota, M.R., Ronkainen, I. A (1993) **International Marketing,** the drydon press. USA.
- Datta, D.K (1988) **International joint ventures: a framework for analysis.** Journal of General Management.
- Finnerty, J.E., Ower, J.E., Rogers, R.C **The valuation impact of joint ventures.** Management International Review (MIR), Vol. 26, 1986/2 p.14 - 24.
- Gilligan, C., Hird, M. (1986) **International Marketing Strategy and Management,** Croom Helm. UK.
- Hennessey, J (1995) **Global Marketing Strategies.** Houghton Mifflin. USA.
- Jonson, G., Scholes, K (1993) **Exploring Corporate Strategy - Text and Cases,** Prentice Hall International. UK.
- Keegan, W.J., Green, M.C (1997) **Principles of Global Marketing.** Prentic - Hall. USA.
- Killing, P.J (1983) **Strategies for joint venture success,** Croom Helm London and Canberra.
- Killing. P.J. **«How to make a global joint venture work»,** Harvard Business Review, V.60, 1982 May - June, Page 120 - 127.

- Kogut, B. **A study of the life cycle of joint ventures.** MIR, Vol. 28, Special issue 1988, pp. 39 - 50.
- Lorange, P., Roos, J (1992) **Strategic Alliances: Formation, Implementation and Evolution,** Blackwell Publishers.
- Onkvist, S., Shaw, J.J (1993) **International Marketing: analysis and strategy,** Macmillan. USA.
- Pearce, A. J., Robinson, B.R (1991) **Strategic management practice: readings in strategic management,** IRWIN. USA.
- Root, F.R. (1994) **Entry Strategies for International Markets,** Jossey - Bass, Inc. USA.
- Terpstra, V., Sarathy, R. (1997) **International marketing.** The Dryden Press. USA.
- Walmsley, J. (1982) **Handbook of international joint ventures,** Graham & Trotman, London.
- **Hard word on joint ventures.** Financial times. January 22, 1990, P.30.