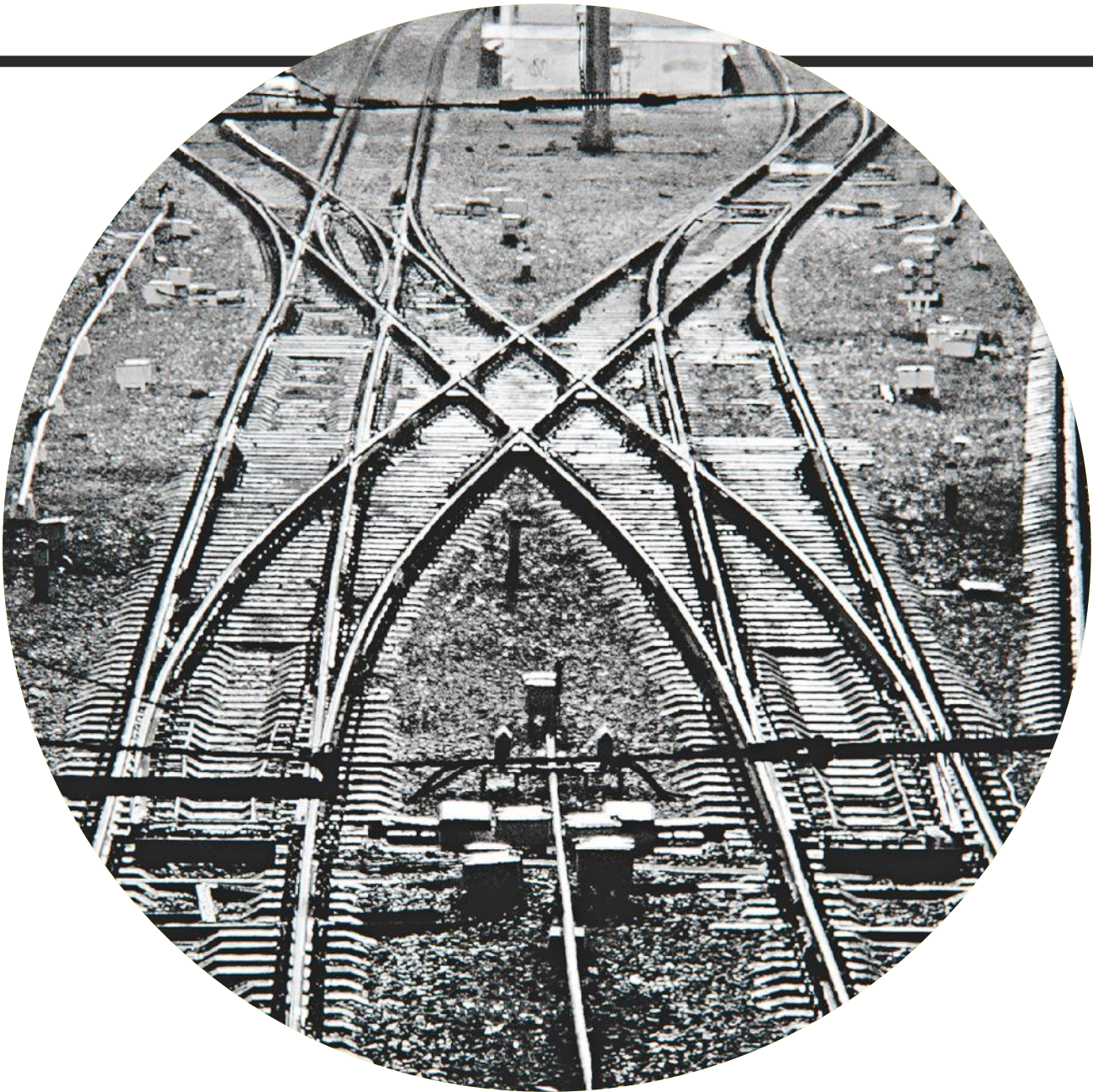




Managing international joint ventures

Philippe Dume and **Sergey Frank**
provide practical joint venture advice



Over the last 15 years, we have both participated in the creation and management of a number of international joint ventures. In theory, a joint venture can be the ideal form for a business organisation. This is particularly true on the international stage where a joint venture can help mitigate risk and maximise partner synergies.

This is a great theory, but reality has a nasty habit of biting back. What started out as a promising joint venture may turn out to become a lasting nightmare. To make an international joint venture work, we have three recommendations. Some of the points may appear obvious, but should never be underestimated. In fact, you might be surprised to learn how rarely they are actually considered and how dramatic the consequences of this can be.

1. Don't underestimate the cultural gap

Three main things should be taken into account. First, is what we label different place, different timing. One of many significant problems arises when the two parent companies of a joint venture (the shareholders) have different expectations about the overall timeline as well as the particular milestones while developing their strategy. Many Western companies tend to work on a three- to five-year plan, while enterprises from developing parts of the world usually plan only one year ahead, in view of local economic uncertainty. This different timeline has a significant impact on the decision-making process when it comes to investments and skill development that have a long payback.

The second cultural aspect that needs to be borne in mind is different management styles. There can be a great difference across geographies between an autocratic and a more participatory management style. Take Russia: if a Western leadership team is used to a more participative management style – giving greater freedom to employees and expecting a proactive attitude from them – it might become difficult to establish proper communication if the local Russian employees are accustomed to a more autocratic style of leadership, expecting repeated and detailed instructions. This difference in management styles requires alignment on both sides to have a good level of execution.

The third cultural element is the existence of different negotiation styles. Negotiation styles between different cultures can also be a source of frustration during the deal phase and the critical moments of the operating phase. For example, northern Europeans tend to be linear in their argumentation ('First things first', including the definition of milestones and a clear action plan), whereas the Chinese tend to negotiate in a more circular manner (going back and forth in their argumentation).

The best way to anticipate such gaps is to go through a learning process of each other's differences. This can take place in an informal setting, e.g. during after-work gatherings or lunch breaks. This allows both parties to better understand and anticipate the other side's way of thinking and points of view. It will also enable both parties to better grasp difficulties and restraints that can come up during the decision-making process.

2. Don't overestimate the local market

On too many occasions we have seen management teams entering a new geographical market through a partnership in order to save time (since the local partner already had the right and necessary understanding of the

market) and in order to share the risk with a local key player.

In the first attempt to seize opportunities, common issues we noticed were:

Too much reliance on the local partner. The role of a business development or strategic team is to check the results of a market analysis for real opportunities. When dealing with a partner who has local connections and market know-how, the trap could be to rely more on his or her data than establishing real customer contact.

Local partners can sometimes be over-enthusiastic. The lack of reliable information for the business development/strategic team can be exacerbated if the local partner provides distorted information in order to attract foreign investment. This information is often willingly used by the foreigners wishing to provide the head office with promising news. As a result, everyone involved gets caught in a trap we call 'the good news syndrome'.

Advisers are not the doers. The good news syndrome between local and foreign partners is also magnified by the clear separation of deal phase and operating phase. The initial strategic/business development teams are indeed responsible for making a deal happen and not of executing the business plan. At least

There can be a great difference across geographies between an autocratic and a more participatory management style

some individuals who were involved in the deal phase must be carried over to the operating phase so as to create bridges from one phase to the next. If the future general manager is absent from this entry phase, this can lead to a missing reality check from the person in charge of delivering results for the following years.

Mitigating this issue should take two forms. First, install a robust process to check market information directly, while the follow-up needs to take different assumptions into consideration that both parties made when establishing the business plan. Second, hire the future general manager as early as possible to ensure accountability in the business plan structuring.

3. Don't set off on different tracks

The advantages of a joint venture partnership are manifold, representing a fusion between partners of capital, assets and access to

technology and markets. Although these points can be clearly understood by everyone involved in the decision-making process, they are often poorly reflected in the actual obligations of both shareholders to achieve the target. Such problems usually only appear when partners fail to deliver what they initially promised.

A second important issue occurs when a joint venture is not up to the economic expectations and, as a consequence, your partner may hide margins in their home units through the transfer price.

The purpose and strategy of a joint venture determine the kind of people who should be assigned by each partner. The partners will generally appoint an international management team, where the CEO can be local or foreign (depending on the relationship with customers and local authorities), the COO most likely a foreigner (when performance and technology are at stake) and the CFO a local (for identifying legal and compliance issues).

Problems can arise when such a team has to learn how to work together, since the interests, attitudes and objectives of each partner in making the joint venture work can differ considerably.

Mitigating these issues must be based on a real risk analysis concerning the foundation of the partnership and its sustainability. This mainly requires a clear transfer-pricing scheme (if applicable) and a system to measure the other partner's performance. It is also crucial to choose the staff that will lead the joint venture very carefully. The importance of selecting a fully entitled management team tends to be overlooked all too often. Finally, a pragmatic escalation process to ensure timely decision-making supported by the right protocols will allow teams to focus on their business goals.

These three considerations – cultural differences, local market realities and the overlapping of vital interests – are crucial for a successful international joint venture. It is particularly important to have people on both sides, ideally in middle management, who constantly take care of these aspects. The chances of success of a joint venture are then highest, but only in combination with a dedicated and fully authorised staff, as well as a continuous follow-up and adjustment system. ■

Philippe Dume is Managing Director for Alstom Service in Romania. He worked for McKinsey and Company after graduating from London Business School.

Sergey Frank is the founder of the consulting firm Sergey Frank International (sergey-frank.com) which has offices in Leipzig, Moscow and Vienna.

Copyright of Business Strategy Review is the property of Wiley-Blackwell and its content may not be copied or emailed to multiple sites or posted to a listserv without the copyright holder's express written permission. However, users may print, download, or email articles for individual use.

Copyright of London Business School Review is the property of Wiley-Blackwell and its content may not be copied or emailed to multiple sites or posted to a listserv without the copyright holder's express written permission. However, users may print, download, or email articles for individual use.