The Management of International Joint Ventures

An organizational learning perspective

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Chapter 1

Introduction

The continued growth in the formation of alliances and joint ventures (JVs) has lead to speculation that today's notion of global firms will be superseded by networks of strategic alliances among firms spanning many different industries and countries. One of the driving forces behind the increased use of strategic alliances is the realization by many firms that self-sufficiency is becoming increasingly difficult in an international business environment that demands both strategic focus and flexibility. Alliances provide the opportunity for firms to leverage their strengths with the help of partners.

This book focuses on the management of equity JVs, one of the most common forms of international alliances. For this book, a JV is defined as a means of performing activities in combination with one or more firms instead of autonomously. A JV occurs when two or more legally distinct firms (the parents) pool a portion of their resources within a jointly owned legal organization. This definition excludes other forms of cooperative agreements such as licensing, distribution and supply agreements, research and development partnerships, or technical assistance and management contracts.

Using multiple sources of field-based data, the book examines various JV management issues, with a particular focus on collaboration and organizational learning. A primary objective in the book is to develop some clear linkages between organizational learning concepts and learning through JVs. To provide a realistic perspective of IJV management and to develop managerial implications, examples drawn from in-depth interviews are utilized throughout the book. The examples and comments from managers illustrate many of the concepts discussed and anchor the research in managerial practice.

THE EMPIRICAL BASE

Over the past decade there has been a wave of Japanese investment in the North American automotive industry, both at the assembler and supplier levels. Much of the Japanese investment has involved JVs between Japanese and North American firms. A multi-stage project examining North American–Japanese JVs provides the primary empirical base for this book. The research stages include:

1 an initial field survey of 40 North American–Japanese JVs;
2 a longitudinal case study involving a subset of the JVs examined in the initial study (see the Appendix for a detailed discussion of the research methodology).

The Japanese–North American JVs provided an interesting data source because for many of the US firms, JV involvement represented the first close US-based relationship with both a Japanese partner and a Japanese customer. For many of the Japanese firms, a JV was the first significant investment outside Japan. In collecting the data and interacting with JV managers, it was possible to observe firms struggling with many of the strategic and operational problems inherent in IJV management.

JVs AND ORGANIZATIONAL LEARNING

A variety of strategic objectives has been suggested to explain firms' motives for the formation of JVs (Beamish and Banks 1987; Contractor and Lorange 1988; Hennart 1988; Porter and Fuller 1986). The objectives include the reduction of risk, economies of scale, access to technology or markets, and the search for legitimacy. In much of the JV literature, the focus has been on firms' mutual desire to cooperate as the basis for JV formation. This focus emphasizes the performance of the JV task and the benefits of pooling resources and skills for cooperative results.

After discussing JV characteristics and several performance issues, the focus of the book shifts to a detailed examination of learning through collaboration. The focus is on how JV partners exploit and leverage alliance knowledge. Viewing JVs as learning opportunities provides an alternative to mutual JV value creation. JVs can provide firms with access to the embedded knowledge of other organizations. This access creates the potential for firms to internalize partner skills and capabilities. In an alliance, two or more organizations are brought together because of their complementarity and their differences. The differences in partner skill areas are the fuel for learning. Whether or not the differences are identified and internalized determines whether learning occurs. An important conclusion from this research is that while organizations often talk in glowing terms about their alliances' learning potential, learning is a difficult, frustrating, and often misunderstood process.

STRUCTURE OF THE BOOK

The initial chapters deal with some fundamental JV issues and provide a contextual overview of the organizations examined in the book. Chapter 2 draws on survey data to examine characteristics of the Japanese–North American JVs. After examining the JVs in terms of ownership, formation objectives, initiation, and management style, the issue of JV performance is considered. The concluding section raises some issues associated with JV termination and JVs as a viable organizational form.

Chapter 3 considers the implications for North American firms gaining temporary, and perhaps even permanent access to Japanese networks through the formation of JVs with Japanese firms. The chapter first provides an overview of Japanese corporate networks, emphasizing corporate relationships in the automotive industry. The transfer of Japanese networks to North America is then considered as the basis for examining problems US managers have encountered when confronted with the ambiguity and uncertainty of Japanese networks.

Chapter 4 examines an important theme in the literature on IJVs – the relationship between JV control and performance. The main argument in the chapter is that control over JV activities creates a dependency perspective and, therefore, a lack of bargaining power in a particular area is potentially a key factor in the evaluation of JV performance. Three different conceptualizations of the control–performance relationship are examined using both the survey data and an additional sample of Japanese JVs.

Chapter 5 shifts the focus to the organizational learning issue. Given the premise that IJVs create learning opportunities for the venture partners, this chapter explores the conceptual background associated with learning and collaboration.

Chapter 6 begins with a discussion of the learning experience of the American JV parents and their efforts to exploit JV learning opportunities. The chapter then empirically examines organizational dimensions that can shape the learning experience. The dimensions examined are:

1 learning capacity;
2 parent experience;
3 partner interactions.

Chapter 7 builds on the earlier conceptual discussion. Some of the more controversial areas in the organizational learning literature are examined as the basis for developing a multi-level learning framework. The framework provides the underpinnings for the argument that an existing set of managerial beliefs can constrain the learning process. Applying the framework to the JV context provides insights into why firms with explicit learning objectives struggled to capitalize on their JV learning opportunities.

Chapter 8 provides seven case vignettes dealing with JV management. The vignettes provide some 'thick' description of JV issues such as JV learning potential, JV failure, performance and learning, and collaborative knowledge management.

Chapter 9 examines the relationship between learning, collaborative knowledge, and IJV stability. If IJVs are inherently unstable organizational forms, as researchers and managers have suggested, why do some ventures survive and prosper for many years? This chapter argues that foreign partner knowledge of the local economic, political, and cultural environments is a critical factor in the stability of IJVs. When the foreign partner is no longer satisfied with access to local knowledge and seeks to acquire this knowledge, the probability of JV instability increases substantially. This chapter suggests that if managers are aware of the factors influencing JV stability, they may be able to prevent or control for premature changes in partner relationships.

Finally, the concluding chapter examines the organizational learning and IJV findings from two theoretical perspectives: resource-based theories of strategy and transaction costs.

Chapter 2

Japanese JVs

Characteristics and performance

This chapter draws on the survey data to examine the characteristics of the Japanese–North American JVs.[1] After examining the JVs in terms of ownership, formation objectives, initiation, and management style, the issue of JV performance is considered. The concluding section raises some issues associated with JV termination and JVs as a viable organizational form.

THE AUTOMOTIVE INDUSTRY

Five key trends characterized the automotive supply industry of the late 1980s. One, the assemblers were increasing their outsourcing of parts through the establishment of multi-tiered supplier arrangements. First-tier suppliers deal directly with the assemblers, the second-tier suppliers manage a third tier, and so on. Two, automakers were pushing their suppliers toward just-in-time delivery systems and increased investment in design and engineering capabilities. Three, mergers were becoming prevalent in the supplier sector, largely because of heavy demands for research and development, new equipment, and employee training. Four, suppliers were moving away from their traditional focus on home markets toward foreign investment. During the 1980s, more than 250 Japan-based supplier firms established operations in North America and most arrived in the 1987–88 period. Finally, the movement of the Japanese transplants into North America established an important new customer sector for North America-based suppliers.

By the early 1990s and mirroring the situation with automaking capacity, excess capacity at the supplier level was becoming a reality. With the US automakers under pressure from the Japanese companies, North American suppliers found their traditional customer base shrinking. The overcapacity and competition from foreign-based component suppliers created increasingly difficult conditions for North American automotive suppliers. These conditions were forcing North American suppliers to adapt to a very different competitive environment. A 1989 statement by a senior manager in a US component supplier reflects the new environment:

> The next five years are going to be horrible. With the new Japanese companies coming in, with peripheral capacity, and with component integration and the car companies all chasing the same market . . . a lot of suppliers are going to fall out.
>
> (Smith 1989: 37)

It was against the background of a changing automotive industry and the recent wave of Japanese–American supplier JVs that the JV survey was carried out.

JV CHARACTERISTICS

All the JVs studied were suppliers to the automotive industry and only one had less than 50 per cent of its sales to automotive customers. Most were direct suppliers to the automotive assemblers (i.e. tier one suppliers; see Table 2.1 for a summary of JV characteristics). Three-quarters of the ventures were manufacturers of parts and components while the remainder produced materials such as paint, steel, glass, and chemicals. In 27 cases, the JV products were functionally similar to existing American parent products. In the other 13 cases, the JV represented a product diversification for the American parent. The mean number of employees was 206 and 15 JVs had between 150 and 300 employees.

The American JV parents were almost evenly divided between single business firms and divisions of diversified firms. There were 22 single business parents and 18 diversified parents in the sample. In all but two cases, the JVs were startup or greenfield organizations. A JV was classified as a greenfield venture if an organization was created where none existed before. One of the non-greenfield ventures was formed when the American parent spun off a small downstream operation. In the other non-greenfield case, the American partner contributed an existing plant and domestic customer product line to the JV. The product line was subsequently expanded and a transplant customer base developed through the efforts of the Japanese partner.

Most JVs were comprised of single plants geographically separated from the American parents' facilities and, generally, new plants and

Table 2.1 JV characteristics

Characteristics	*Number of cases*	*Per cent*	*Characteristics*	*Number of cases*	*Per cent*
American partner equity (%)			**Number of years operational**		
20-30	4	10.0	1	2	5.0
31-40	5	12.5	2	5	12.5
41-48	3	7.5	3	14	35.0
49	3	7.5	4	12	30.0
50	17	42.5	5	5	12.5
51	4	10.0	6	2	5.0
60	4	10.0	—	—	—
JV customers		Tiers supplied (%)			
Tier 1	33	82.5	Single transplant	11	27.5
Tier 2	4	10.0	Multiple transplants	13	32.5
Tier 1 and Tier 2	3	7.5	US assemblers and transplants	11	27.5
			US assemblers	5	12.5

equipment were built or acquired specifically for the JVs. In four cases, the JVs acquired existing, unused plants from their American partners. In two cases, the JVs had separate production lines but leased space within existing American partner facilities, and in one case, the JV used American partner production lines exclusively (although a new plant was planned). In the fourth case, the JV bought land from the American partner and constructed a new plant on the site of an old plant. In several additional cases, the JVs began operations using American partner facilities and constructed new plants several years later.

Formation objectives

The cases were classified according to the American partner's motive in forming the JV. In making this classification, it was recognized that JV parents often are motivated by multiple factors in forming JVs. Thus, the motive represents the American partner's primary motivating factor.

The primary motive for 29 American partners was access to the transplant market. All but five JVs were transplant suppliers and 11 supplied a single transplant (Table 2.1). The prevalent opinion of managers involved with transplant customers was that American firm access to the transplant market would not have been possible without a Japanese connection. A Japanese JV partner was viewed as the most effective and timely means of acquiring the connection that would enable the American firms to become transplant suppliers. Within the American partner firms there was a strong belief that the Japanese transplants wanted to deal with Japanese suppliers and were willing to sacrifice the locational experience of American suppliers and even the potentially lower costs of American suppliers.[2]

Nine non-transplant access ventures were classified as technology oriented. Four American firms sought access to manufacturing technology and the capital necessary to implement the technology. In five cases, the primary motive was access to technology that would allow the American partner to broaden its product line and give the Japanese partner entry to the North American market. As an American parent executive commented, 'We had the market access through our own plants and the administration talent to run the business. We did not have the manufacturing expertise.'

The remaining two non-transplant access ventures involved risk-sharing and legitimacy. In the risk-sharing case, the two partners wished to enter the North American automotive market with a product both firms manufactured outside North America. The JV allowed the partners to combine forces and share the risk of entering a new market. In the legitimacy case, the formation of the JV was motivated by the desire of the American partner to collaborate with a Japanese firm because 'everyone else was doing it'. This motive is called legitimacy because the American partner was motivated to appear in agreement with the prevailing norms in the automotive industry. Several managers indicated that forming a JV with a Japanese partner was a very 'fashionable' thing to do during the period 1985–90.

Broadly speaking, all of the JVs were formed to strengthen an existing business. With the size of existing domestic markets stable or declining, a JV could compensate the American partners by providing relatively quick access to a new customer or product market. Consequently, many of the ventures were defensive and associated with an American parent attitude of 'we better form a JV before it is too late'.

While product and customer market motives provided a specific and often short-term objective for American firms, two less tangible objectives were also important. The first was a learning objective. Many of the American parent firms, struggling to compete in an industry in transition, saw their JVs as a point of leverage for the development of new skills and capabilities. The second was a desire to internationalize and move beyond domestic markets. As a JV manager explained:

> The JVs were formed because we felt we [the American partner] had to have a greater international presence in an industry that was rapidly becoming more international in scope. The American partner wanted to be a supplier with a 'window to the world'; the JV helps give us that window. Access to the transplant market may have provided an initial short-term objective for the formation of the JVs and it may have brought the firms together. However, our longer term objective is to become a world leader.

The manager went on to contend that alliances were critical to an international strategy and that the Japanese were much better at using alliances than North American firms. Another manager echoed those comments:

> We wanted to establish a global connection in the automotive supply industry. The JV is one step toward becoming a more international player in the automotive industry. We are now investigating alliances in Europe. The OEMs [assemblers] are getting closer to having common products across regions (i.e. North America and Europe). For a supplier it would be advantageous to be capable of supplying the same part in different parts of the world.

A common theme expressed by many managers was that gaining access to the transplant market provided the American firm with their first step toward becoming more international. The American firms usually recognized that the automotive industry was changing rapidly and wanted to participate in that change. Unfortunately, the objectives of transplant access and internationalization often took precedence over economic reasons for forming an alliance. Several managers indicated that 'faith' drove the JV formation process; both the American and Japanese firms entered the JV with little more than faith in each other. In these cases, neither partner communicated its objectives and little effort was made to establish financial objectives. Not surprisingly, many JVs subsequently experienced problems because of the lack of communication during the formation process.