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INTERNATIONAL EXPANSION THROUGH JOINT VENTURE – RISKS AND BENEFITS

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Abstract *There are many reasons as to why a company wants to enter an international joint venture. Among those things are lower manufacturing costs, advantageous monetary conversion rates and lower taxes and therefore, they can make international joint ventures favorable. Though, even though there are many advantages to entering an international joint venture, there are also many considerable risks. Though, an adequate structured agreement can help mitigate the risks to support a successful partnership.*

Keywords
Joint venture, partnership, risks, advantages

JEL Codes:
G3

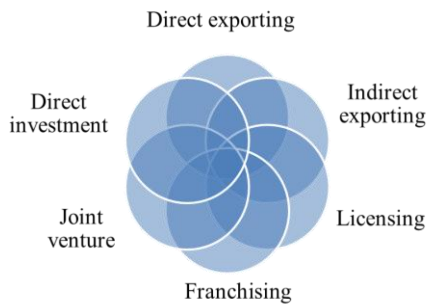
1. Introduction

When preparing for their international expansion, enterprises must confront the question of identifying the most suitable legal form to conquer new markets. A successful international expansion strategy depends on the choice of the legal structure. If firms do not want to cooperate with foreign local businesses, they can decide on a subsidiary or a branch.

More and more companies are challenged by the changes of international economic environment and in many cases are forced to expand globally — or they risk losing ground to foreign and domestic competition, so they realized that international expansion is key to succeeding in the economic environment. The hard work begins once the decision is made to expand internationally. So, the decision to internationalize a business in a certain country is of strategic importance and should be developed following a thorough study of all the factors that can influence the activity of the company and the risks to which it is subject. (Militaru and Zanfir, 2014).

There are many strategies a company can choose from to expand internationally. Among those are exporting, establishing a joint venture or strategic alliance in a foreign market, acquiring a firm through direct investment or licensing technology abroad. The benefits and risks associated with each technique depend on many aspects, including the type of product or service, the need for support, and the foreign economic, political, business and cultural environment companies are seeking to enter. The strategy that is best for any enterprises depends on the level of resources and commitment, and degree of risk they are willing to incur.

Thus, in order to remain competitive, companies are forced to cooperate among themselves in various forms, to share knowledge and resources in order to gain the necessary competitive advantage (Nicolau, 2010).



(*Source*: www.yourarticlelibrary.com)

Figure 1. Ways to enter a foreign market

2. Joint venture

The business dictionary defines joint ventures as a "new firm formed to achieve specific objectives of a partnership like temporary arrangement between two or more firms. Joint ventures are advantageous as a risk reducing mechanism in new-market penetration, and in pooling of resource for large projects". Therefore, a joint venture is a strategic alliance where two or more partners, form a partnership to share markets, intellectual property, assets, knowledge, and, mainly profits. A joint venture differs from a merger in the sense that there is no transfer of ownership in the deal.

The term “joint-venture” is understood rather differently from country to country around the world. The global regions and each country have different laws and understanding of what constitutes a “joint venture”. Even within the European Union there are numerous terms for forms of joint ventures *(Groupement d’Intérêt Economique, Konzern, Unión Temporal de Empresas, Gemeenschappelijke Onderneming etc.)* and each form has somewhat different set of legal and common law requirements, as well as business practices involving partnering solutions.

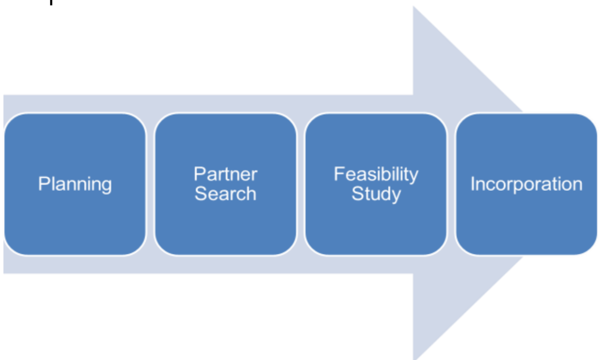
Commercially speaking, by setting up a joint venture, a firm depends on a partner that has grate knowledge of the local market and of the practices of the competitors, the administrative authorities and the political authorities. So, the company can adjust more quickly to the specific requirements and needs of the foreign market, through the pooling of expertise, and technical and human means.

The basic reason to entertain in this activity is simple to: to save money and sharing the risk in case the business fails. . Joint ventures are very helpful to many companies in achievement access to foreign markets. Such businesses generally represent a direct investment, which is sometimes restricted by laws in the country in which the action takes place. One of the aims of a partner in a joint venture is to have a majority interest in it; that way, it maintains control over a business. This is the reason why some states do not permit foreign corporations to hold majority interests in their local business ventures.

In a joint venture can exist almost any type of combination of partners, including:

- two companies from the same country joining together in a foreign market, such as NEC and Mitsubishi (Japan) in the United Kingdom
- a foreign company joining with a local company, such as Great Lakes Chemical (U.S.) and A. H. Al Zamil in Saudi Arabia
- companies from two or more countries establishing a joint venture in a third country, such as that of Diamond Shamrock (U.S.) and Sol Petroleo (Argentina) in Bolivia
- a private company and a local government forming a joint venture (sometimes called a mixed venture), such as that of Philips (Dutch) with the Indonesian government
- a private company joining a government-owned company in a third country, such as BP Amoco (private British-U.S.) and Eni (government-owned Italian) in Egypt (Kim S. H. and Kim S. H, 2009).

This type of partnership can happen between giants in an industry. A much known example is Cingular, a strategic alliance between SBS and Bellsouth. It can also occur between two small companies which consider that partnering will help them fight their bigger competitors.



(*Source*: jointventurestrategies.net)

Figure 2. Steps in formation of Joint venture

Companies with identical products and services can also join forces to enter markets they wouldn't or couldn't consider without investing great resources. Besides, due to native regulations, some markets can only be entered through joint venturing with a resident business.

In some cases, a large company can decide to form a joint venture with a smaller one in order to obtain rapidly critical intellectual property, technology, or resources otherwise hard to attain, even with plenty of money at their disposal.

3. Benefits of joint ventures

Among the most significant benefits resulting from joint ventures is that each partner save money and reduces their risks through capital and resource sharing. Joint ventures give smaller firms the opportunity to work with bigger ones to develop, manufacture, and market new products and services. Joint ventures also give enterprises of all dimensions the chance to raise sales, gain access to wider markets, and improve technological capabilities.

Businesses of any size can use joint ventures to develop and strengthen long-term relationships. In the right circumstances a joint venture can help businesses to grow faster, increase productivity and generate greater profits. The success of a joint venture depends on a carefully planned strategy, strong partners, equal contribution, effective execution of the agreement, and fast and efficient integration of work processes. This involves commitment and respect for the other company's work culture and a clear understanding of each one's responsibilities and accountabilities in the partnership.

A joint venture can help companies to grow faster, to increase their productivity and to generate bigger profits. A successful joint venture can offer:

- access to new markets and distribution networks;

- reduction of entry barriers;
- worldwide coverage – complementary geographies;
- growth without borrowing money or seeking outside investment;
- companies can develop quicker, reach a wider market and earn more money;
- grow capabilities–expand knowledge and expertise;
- protection by sharing risks with venture partners;
- access to more resources, including specialized staff, technology and finance;
- does not require a long-term commitment.

A joint venture can also be very flexible. Joint ventures are especially popular with businesses in the transport and travel industries that operate in different countries.

4. Risks of joint venture

While the benefits associated with joint ventures are often emphasized, the risks regularly are not completely reflected or understood by the involved partners prior to the arrangement. By their nature, joint ventures are usually risky because of the probability that the new product, new market or new technology for which the joint venture was formed is not feasible. Other than operating risks, joint ventures occasionally fail or are considered ineffective from the perspective of one or more participants. This primarily is due to problems that appear in the course of relations between the joint venture and the associates or between the associates themselves.

Problems are likely to occur if:

- the objectives of the venture are not entirely clear and communicated to everyone involved;
- governance – lack of agreed to decision-making processes;
- the partners have not the same objectives;
- planning time;
- there is an difference in levels of expertise, investment or assets got into the venture by the different partners;
- different cultures and management styles result in poor integration and co-operation;
- the partners do not deliver sufficient management and support in the early stages.

5. Conclusions

Building a successful joint venture strategy can be challenging and it can take time, commitment and effort from both partners. Many companies which are at the expansion stage typically face a dilemma: to make a distinction between themselves and their competitors, they must add a new product or service, a new market. But they need a massive investment for that kind of extension, and there is no guarantee the investment will pay off. So, joint ventures are a popular technique to share the costs of expanding into new territory. A joint venture is a combined entity, in which each participating company is responsible for the entity's actions and responsibilities. However, unlike a merger a joint venture is temporary and is often dissolved or sold on completion of the project that brought the partners together.

But, before entering into a joint venture, both partners must have a clear understanding of the objective of collaboration. This understanding must be translated into a simple written agreement that defines the responsibilities of partners. Assessing the strengths and weaknesses of both partner firms can help in building a strong alliance on each other's strengths that can result in fast growth of the business and profitability.

An essential step in the formation of any joint venture is the contingency planning. But the overall benefits, weighed against the mitigated risks and limited costs make joint ventures, as well as strategic alliances and other collaborative frameworks a very attractive, flexible business proposition.

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