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Proceedings of the

Conference on Strategic Alliances in Transitional Economies

Edited by Cynthia Koch

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The *Conference on Strategic Alliances in Transitional Economies* was held May 20, 1997, at the Davidson Institute in Ann Arbor, Michigan.

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On May 20, 1997, the Davidson Institute convened the ***Conference on Strategic Alliances in Transitional Economies*** *in Ann Arbor, Michigan. The conference featured both scholars and business people with expertise on joint ventures and strategic alliances. We asked Dr. Cynthia Koch to edit the transcript from the conference and write an overview of the event. An overview by Dr. Koch is followed by an edited transcript of the four panels including comments from the audience.*

Overview

As part of its mission to study and promote the transition from central planning to market economies, the Davidson Institute invited managers and academic scholars from across the nation and around the world to share their research and experiences at its ***Conference on Strategic Alliances in Transitional Economies.*** Held at the University of Michigan Business School, where the Davidson Institute is headquartered, the conference, in Prof. Jan Svejnar's words, was designed to serve as "a launching pad for an extended research initiative." With the inclusion of business practitioners in the four-panel format, the conference promised to push the boundaries of the academic environment. As Prof. Jim Walsh noted, "rarely do we ever pull managers together into these conversations when we are formulating research agendas. We have done that today, and we have done that quite self-consciously. Our experience in transitional economies suggests that as much as we would like to sit in our windowless observatories and develop a research agenda for the next five years, the academic community cannot do it without a partnership with the management practice community."

Organized to explore "the why, the way and the how" of creating, structuring and managing strategic alliances, the sessions appeared to weigh heavily on the academic side with three of the four panels given to academic presenters. Professor Walsh's invitation to business managers to "reflect on their own experiences and to identify questions" for the academic community soon balanced the scales, however, as question after question following the presentations identified the challenges, conundrums, problems and perplexities confronting researchers and practitioners alike. The final panel further probed the complexities of creating alliances through cogent examples and explanations from representatives of the business community.

The following is an edited transcript of those presentations and conversations as they unfolded throughout the day.

Panel I: The Strategic Rationale for Alliances

Jan Svejnar begins with a broad view of transitional economies and the place of alliances. Pierre Dussauge and Harbir Singh pick up the conversation from a corporate strategy perspective focusing on the processes.

Jan Svejnar, Executive Director of the William Davidson Institute

Economic Transition, and the Influence on Strategic Alliances

Strategic alliances are among the most promising vehicles for successfully completing economic transitions. Nobody quite agrees on what transition means, so let's say that it is the process of transforming the economies of the former Soviet bloc, China and Vietnam to market-oriented economies. In 1990, they were quite a compact and homogeneous group. Now they are very heterogeneous because they have reached different stages of development to form an entire spectrum.

It is important to realize that strategic alliances of all sorts existed under communism as well. These alliances were highly centrally coordinated and managed on the part of the local government, basically because the government wanted to preserve control and have influence over how these alliances proceeded. There were certainly quite a few of them, sometimes proceeding hand in hand with very fierce ideological struggle. During that time, governments such as China or the Soviet Union would essentially let strategic partners from the West bid and select the alliances that were most advantageous to the government. Bridging the gap between East and West through various forms of alliances and alternative mechanisms proved to be quite difficult and became especially difficult after the imposition of the COCOM embargo on the transfer of high tech to the second world. In the 90's, transition meant major decentralization of economic activities. Suddenly, firms in these transition economies could negotiate agreements themselves.

Three models of transition have emerged so far. On the one extreme is China and Vietnam, which have introduced relatively limited market reforms but have grown very rapidly and have been very successful. In the Russian model, or New Independent States' model, in which there have been major reform measures, we see rapid privatization, mostly to insiders, managers and workers, and, at the same time, a severe depression, a decline in economic activity for five to six years in a row. Finally, the Central East European model, which has undergone major transformation measures, has encountered a short recession followed by varying degrees of economic growth. It is these countries in Central Eastern Europe that are increasingly classified as the emerging market economies.

For all three models, successful transformation depends on restructuring the firm in order to penetrate work markets. The limiting factors in doing this include technology, investment goods that embody modern technology, and various types of managerial know-how. Other problems include underdeveloped legal frameworks and enforcement. Also, the relevant decision makers in a number of these transitional economies have been very reluctant to offer attractive conditions to foreign firms and have actively discouraged their entry into the so-called strategic sectors. Yet quite a few features make these transitional economies attractive. They have a relatively well-educated labor force, and labor cost is still relatively inexpensive. Some countries, especially those in Central and Eastern Europe, have opened up remarkably to the world, to foreign trade and to capital flows, and they've introduced currency convertibility.

Many of these preconditions for strategic alliances raise questions. What makes these countries, at their current stage of transition, different from other developing economies and emerging market economies? To what extent can we transpose information about these other countries to transitioning economies? What are the most important constraints for the formation of strategic alliances? Can we identify four or five of the most important constraints as a way to structure a research agenda? Why has there been relatively little greenfield investment?

Pierre Dussauge, H.E.C.-School of Management

Alliance Types and Inter-Partner Learning

In general, alliances have been seen as a mechanism through which resources and capabilities tend to be transferred. So the very broad statement found in most of the literature is that alliances create significant learning opportunities and that learning, or the transfer of capabilities, is enhanced by similarity in the knowledge base of the partners. That is, partners can only learn if they know enough about what is taking place and can understand the intricacies of the new things they are seeing. While the partners need some closeness in capability bases for learning to take place, they also need significant differences for there to be something valuable to learn. If partner firms are too similar in many dimensions of their businesses, then there will not be enough to learn.

Based on these premises, we need to discover how to both capture these capability transfers and see what sort of consequences they lead to. I don't think you can generalize this idea that capability transfers will take place in all alliances in the same way. We have a very heterogeneous phenomenon, and if we don't try to clarify that heterogeneity, it is going to be very difficult to try particular conclusions. One classical way to classify alliances is to distinguish the kind of contribution firms make. Two broad kinds of alliances emerge. One is an alliance (link alliance) in which the partners contribute complementary assets, resources, or capabilities in order to build on synergies between these resources. This means that one partner actually lacks some of the capabilities or the resources, the other contributes, and *vice versa*. By joining forces, they get new opportunities to exploit new business opportunities. A very different kind of alliance (scale alliance) occurs between a firm which could carry out the entire business on its own but still chooses to form a joint venture because there is a problem of economies of scale, of critical mass, of critical resources, not in the sense of different resources, but of enough resources. Very broadly put, these sort of scale alliances assemble similar contributions from different partners. For example, the original partners of Airbus had the capability to make this plane on their own, but they were too small, without enough money, or enough engineers and market share. In link alliances, for instance, the

Japanese automaker forms an alliance with a U.S. automaker to actually sell a Japanese designed car in the U.S. The Japanese company contributes a car which is designed and manufactured in Japan and the U.S. firm contributes market presence. These alliances create opportunities for learning since each comes into contact with different ways of doing things and different technologies. So, if the contributions by the partner firms are different, the opportunities for learning are enhanced.

Learning is not something that you can just go out and look at, or observe. One way of [measuring] it is to actually look, not at the learning process itself, but at reorganization within the alliance. Organization of tasks in an alliance reflects different capabilities from the different partners. The distribution of tasks within the alliance reflects the relative capabilities of the partners and from that point of view, reorganization of the alliance signals that the capabilities of the partners have changed over time. Let's put it another way. If, initially, an automobile is imported from Japan into Europe by a European firm and, after a few years, that product is no longer imported, but actually manufactured locally, it signals that the European partner has managed to acquire enough of the manufacturing capabilities of the Japanese partner to produce reasonably good quality cars that are going to be acceptable for the market.

Link alliances tend to be reorganized much more rapidly and much more frequently than scale alliances, which means that when there is this complementary contribution to the alliance, reorganization takes place more rapidly, which signals the fact that learning has taken place in the process. If we take this one step further, then we need to recognize the competitive issues associated with learning, that is, if learning is important, we expect to see learning itself take on a competitive position over time. When we measure the evolution of the relative market share of partner firms associated in link alliances, and compare it to the relative market share of firms engaged in scale alliances, we find that the relative market share tends to vary significantly over time when the partners are engaged in link alliances. This means that when there is a link alliance, one partner gains market share compared to the other in a very significant way, whereas in scale alliances, it does not happen. Link alliances may be associated with fairly aggressive market share gaining type strategies, whereas share gaining is not as important in scale alliances.

Finally, do alliances result in takeovers and does this reflect the acquisition of capabilities? If, after a while, one of the partners can take over the joint venture, it suggests that that partner no longer needs a contribution from the other partner. Research tells us that termination by takeovers occurs much more rapidly and much more frequently in link alliances than it does in scale alliances. Our research does not tell us if entering partners end up being the acquiring or learning partner, or if the local partner ends up being the learning and gaining party.

Harbir Singh, University of Pennsylvania, Wharton

Understanding Outcomes of Alliances

My research does not come from transitional economies *per se*, but from teaching a program on managing alliances in China two years in a row and from the tensions surrounding what Chinese managers thought were key success factors at the end of each day. I am also basing my talk on a program in India on managing joint ventures.

I am going to talk about three perspectives on alliances: as cooperative relationships, as learning races or as strategic options. These are very different views of alliances. When you think about a cooperative arrangement, you are talking about trust, about collaboration, and a win-win situation. The idea has been advanced, however, that alliances are also learning races in which firms try to learn as fast as they can and cooperate while the incentives to cooperate are there. As an option for the future, alliances present high uncertainty. With high uncertainty, alliances become strategic options in which the firm makes an initial small investment and, if the environment proceeds in a good direction and the partner is living up to its promise, the firm scales up the investment, or exits if these criteria are not met.

In keeping with the four-panel format, I will talk about the formation phase, which has also been called strategic rationale, the structuring phase and management phase, and the outcomes of alliances. The literature seems to suggest that firms want to form alliances with complementary partners, perhaps with a certain threshold of capability where they will have the possibility of high commitment and compatibility. Chinese managers, however, raised some issues. The first was the importance of stakeholders. Many companies have been blindsided by the differences in different government agendas or have otherwise underestimated the capabilities of their partners or the cost of making a partner compatible. Further, as the locus of competition shifts, your partner may not be relevant to you anymore. This raises the question of transitioning from one partner to another.

In addition to high transaction costs, equity levels come into play. One study shows that companies with more experience in forming alliances seek equity less frequently. This indicates that companies find other vehicles to form alliances and to influence alliances other than equity. This is important because companies tend to spend a lot of time on the contractual factors which involve the amount of equity. Firms spend less time on the governance structure, which would mean that equity is seen as an enabler rather than as a determinant, and then really more time on the creation of a joint strategy than some operational performance involvement.

Regarding the management of alliances, one published study finds that trust is very important in terms of success, as measured by the degree of satisfaction, performance, commitment, communication, and conflict resolution. This also recognizes conflict, which is often left out of academic literature. There seems to be an emerging theme that rational capital is important and that this includes trust as measured through personal friendships between peers in the alliance. Perhaps we don't want to have a contractual view as much as a relational view of the alliance. The question arises, will empirical research down the road support this view? What is the best lens with which to look at alliances?

Panel I: Discussion and Questions

"How do we measure anything in these contexts? How are we going to know where these things are working or not, and are there better measures of know-how that we haven't yet discovered?"

– Jan Svejnar
William Davidson Institute

"I consult with companies that form strategic alliances all over the world. I am interested in the linkage between the lack of heavy Western investment in transitional markets [and] the lack of heavy investment in greenfield sites in these types of markets. Obviously, from the business perspective, these markets are prioritized with many other opportunities around the world. I think the relevant question might be, how do these markets compare with many other emerging markets? How can we use the lessons of many other places, such as India and Korea, which are not defined as transitional markets?"

– David R. Gunderson
Global Strategic Intelligence

"There is an overall level of dissatisfaction with many joint ventures. We all know that. But it's like democracy. It's still the best choice out there in many parts of the world. So, for that reason, a lot of companies are continuing to use both equity and unequity ventures."

– Paul Beamish
University of Western Ontario

"You go through and talk to managers of joint ventures and every case is somewhat different. Each one devises a separate strategy and most of them work and they've learned how to adapt to the current situation. Deriving some sort of general set of lessons might be the wrong direction."

– Robert F. Dernberger
University of Michigan Center for Chinese Studies & William Davidson Institute

"You shed some light on what the research shows as far as the success rate of alliances that are forced to restructure. I know that the outcomes depend on why alliances are forced to restructure, but is there some indication from the data that [restructuring] just prolongs the agony, or does it really turn out to be an opportunity to make a breakthrough towards success?"

– David A. Henson
Caterpillar, Inc.

"What's the difference? The first is that the privatization process is inherently corrupt and I think we miss that sometimes and all the consequences that that drives . . . .The second is that the firm is defined differently in all these countries and the distinction between the government and the firm and the different levels of the government and the firm is not very clear, and it's not always the same even within one country . . . .Third, transition by definition means change, and we who are entering don't really know where it's changing to and, probably even more importantly, the local companies, whatever that means, don't really know where it's changing to either. And so, your contract is really only the beginning, not the end."

– Bill Cook
Caterpillar, Inc.

"In establishing strategic alliances in transitional economies there are a couple of major obstacles to overcome. One, you may very well be negotiating with an enterprise whose only objective is to remain alive . . . and they have no other ambition or objective other than to find some foreign partner to keep them alive . . . and that's not to say that an alliance isn't possible in those circumstances, but you sure have to recognize that may be the only objective. Secondly, our company's experience has been that the companies really do not understand very much about the market or distribution. Finally, the reason there is not a lot of foreign investment in these transitional economies . . . greenfield investment . . . [or] strategic alliances . . . is that the world's investment community is waiting for the day when they don't have to use a strategic alliance to enter [a] country."

– Peter Walters

Guardian Industries Corp.

Panel II: Structuring Alliances

This panel addresses ways to structure alliances. Some of the challenges to structuring include issues of governmental alliances, the terms and the roles of each of the partners, the prenuptial agreement, resolving conflict and dissolving alliances, the legal or contractual understandings between the partners, compensation for managers and dividing up profits, and the value contributions made by partners.

Bob Kennedy, Harvard University

Competitive Shocks and Industrial Structure: Implications for Deal Structure and Governance

We have a project at Harvard that looks at competitive shocks, or policies that suddenly and significantly increase the role of market forces in determining industry structure. What we refer to as competitive shock is either internal or external liberalization and is a bit broader than the transitional economies defined here. Most of the academic research focuses either at the macro economic level, looking at fiscal policies and inflation, or on very micro issues, on the optimal design of a privatization program, for instance, and this micro level analysis often obscures commonalities across different economies. I've been looking at common trends in order to see beyond what's bobbing around on the surface to what's really going on underneath, the big structural changes that, hopefully, will take us below the surface.

After looking at three types of industry structural changes, patterns of entry, exit and turnover, we ask, in what types of firms are we going to see lots of firm formation and turnover, both in terms of numbers and in terms of rate? We've also been looking at changes in concentration levels and then, finally, changes in foreign presence, defined as imports, as a percentage of domestic output, and industry. In terms of entry and exit and concentration levels, there tend to be two generic industry paths that are relatively predictable. The business practitioners in the room know that it's important to understand whether Poland or China is fighting inflation or what they are doing with regard to their currency. I suggest that it's equally important to understand how the industry you are investing in is likely to evolve.

We tend to see fairly high entry rates in terms of numbers, extraordinarily high numbers of firms thinking about doing business in these markets. Is this industry going to become competitive in the West or in the world market? In high turnovers, industry restructuring is not the same as firm restructuring. There tend to be a lot of new firms and a lot of firm deaths. Over time, some of these state-owned firms will be able to adapt, but many will just die. Second, high barrier entry firms or industries tend to have low entry rates. There tend to be a small number of foreign direct investments, but they tend to be big dollar investments. The other thing to think about is, what is likely to happen in terms of foreign presence? This is a different dimension. How are foreign corporations likely to play a big role in the market, or not?

In R&D intensive industries, foreign presence tends to occur through trade, it tends to be centralized production and to ship exports into these countries. In advertising intensive industries, it tends to occur through foreign direct investments, so local market knowledge is pretty important. We've found through lots of deals and by making lots of big mistakes, the most important thing is to match the incentives with the ongoing industry environment to decrease the risk of an obsolescing bargain. Things may seem very attractive up front, but these people really want to stay alive, they want cash and once they have cash, they don't really need you any more. Ask yourself, what has the investor contributed? In many cases the investor is simply contributing cash. They're keeping the firm alive. They're not going to provide local management. In other industries, there is a kind of decreasing order of risk in which the investing firm will contribute specialized knowledge that can usually be technology or specialized management. Finally, you are at least risk as a foreign investor when you have access to imports, specialized imports, or distribution.

Many foreign investors are obsessed with equity. The need for equity control increases as the durability of the contribution declines, so it's most important to have equity control in cash-type deals. In deals where you are producing for export, continue either the imports or the distribution. Equity control is much less important because you don't have to worry about renegotiation. The other thing to think about concerning equity is that many foreign firms are really focused on the percentage of equity. We have found it successful to split percentage equity with specific covenants in the deal.

Most governments put controls on equity participation, but not on percentage equity ownership or what needs to be approved by the minority partner. Although minority shareholders legally don't have much protection, you can actually build a lot into the incorporation agreements so that the minority shareholders are required to approve any capital expenditures of over $100,000, or reappoint the management board every year. Therefore many local entrepreneurs will not be willing to give up equity control, but they will give the foreign investor veto power.

We have also found that debt seems to be a relatively low cost. Debt is incredibly risky in these volatile environments, but it does serve a pretty valuable function in particularly volatile industries where you are pursing value strategy. Debt allows you to throw the firm into default, and if you, the foreign investor, want to get out, then it creates a sharp decision point. It's often a useful hurdle.

Finally, what type of partners do you want to look for? Focusing on the split between rapid turnover industries and the firm restructuring industries, we found that local entrepreneurs are incredibly important in these high turnover industries because they have good local market knowledge, they tend to be hustlers, at least in the northern part of Central Europe where I have most of my experience. Government partners, or at least well-connected, or politically connected partners are very important, but entrepreneurship becomes much more important as you move down.

Joanne Oxley, University of Michigan

Governance of Technology Transfer Alliances in Transitional Economies: A Transaction Cost Economics Perspective

I am going to talk about a specific group of alliances designed for technology transfer. I want to talk a little bit about the governance officials in technology transfer alliances and the role of institutional environment. Transitional economies really are a kind of natural laboratory for this research. I want to focus on the interrelationship between the *what* and the *how* as I argue that how you structure an alliance is going to determine, or at least in part determine, what you are, and that what you intend to transfer in the alliance is going to have implications for the way you are going to want to structure it.

The challenge facing the transferor is how to structure an alliance to effectively transfer technology and effectively accomplish the learning that you want to perform, and yet safeguard these valuable assets, the proprietary knowledge or technology at the center of your own competitive advantage. The transaction cost perspective says that you have to look at the alternative governance structures available to you in this alliance and then start looking at the relative costs and benefits of each of these structures. No alliance structure is going to be perfect. That's self evident from the failure rate we see. But some structures are going to be more effective than others in particular situations and what you really need to do is to match the governance structure to the particular alliance and the particular activity that you want to achieve.

One of the basic tenets of transition cost economics is to use the simplest form of alliance available when it is possible to do so. In most cases, the simplest form will be a fairly simple contractual agreement. Unfortunately, when dealing with technology, setting up an alliance within the context of a contractual agreement raises a lot of difficulties. In order to create an effective and secure contract for the transfer of technology you need to be able to answer three questions in the affirmative. First, can you specify the project requirements in this technology transfer? Can you specify those within the contract? Is it actually feasible to define what it is we are trying to transfer in such a way that it can be put forward in a contract?

In general, when talking about creating new assets or new technology in technology related alliances, it's much more difficult to specify than if we're talking about existing, well codified technology. In the case of knowledge transfer into the transitional economies, a lot of times we will be talking about existing technologies. Or it may well be possible to at least specify, to write down the contracts that we will need to effectively govern a transfer. Then the question arises, can compliance effectively be monitored? Or can the performance of your joint venture partner, or your alliance partnership be monitored within a contract? If a firm chooses to rely on a contract, obviously it will need to be able to enforce that contract in the courts. Contracts can break down and when they do you have to think about additional safeguards or organizational or governance mechanisms to overcome some of these problems. Previous research that addresses these kinds of questions looks at a simple dichotomous choice between contracts on the one hand and then equity joint venture on the other. I want to put forward a very simple model of contracts versus equity joint venture and talk about how we might apply this model to look at these alliances.

This simple transaction cost model of alliance governance essentially argues that if you're dealing with well-defined, mature technology that can be well-defined, monitored, and enforced within a contract, then that contract is going to be your low cost alternative. As technology becomes more complex, or the scope of the technology being transferred increases, then the relative cost of contracts increases relative to an equity joint venture. As you get more complex technology while within a joint venture, it is much easier to both aide your partner in the way it performs its duties within the contract, and also to monitor what it is they are doing. As hazards increase, firms tend to rely much more on equity joint ventures. Looking at alliances in non-transitional economies, we find that equity is a lot more likely to be chosen in an alliance where there is a design as opposed to pure production, technology transfer for production. Joint ventures also occur more frequently where multiple products or multiple technologies are involved that are much more difficult to monitor. We are also more likely to see joint ventures when they are all partners in an alliance.

So, it really raises the question, how do you go about applying this model when you are going into a very different context, such as a developing country, or transitional economy? As a very first step, one thing we need to take into account is the institutional environment in which the alliance will take place. As an example, I've looked at the intellectual property regime to see how strong the patent protection or other intellectual property rights are, and what effect this one aspect of the institutional environment has on the choice between contracts and equity joint venture. Essentially, when a firm has weak intellectual property, it is much more difficult to rely on contracts and so, for a given type of alliance activity, we're more likely to see a reliance on equity rather than on contracts. This is a fairly simple argument, but one that is fairly well-supported today by empirical evidence. Even taking into account a lot of other differences, potential differences between country settings, I found that U.S. partners who partner with firms in different countries are more likely to use equity arrangements when they are partnering with firms in countries with weak intellectual property than they are when partnering with firms with stronger intellectual property.

Obviously, set habits or procedures have to be modified when going into a country with a different environment, but there are systematic elements to the way in which those can be modified. One lesson is that when going into a situation with weaker intellectual property regimes, the firm needs to put in place greater organizational safeguards, specifically to use equity in those particular alliances. Of course, intellectual property is only one small aspect of the institutional environment that might be relevant, but I would suggest that some of the most important things we need to look at are property rights, of which intellectual property protection is one example. Contract law, obviously, is another that will vary systematically across these countries.

Even if we look at the simple governance choice between contracts and equity, there are some things that we can look at that vary systematically across these countries which we need to look at to understand exactly how they change the relative costs of these different governance structures. There is actually very little work being done to assess and measure how the institutional environment varies across these countries. I think this is a really important first step in trying to understand how they are going to affect the way the alliance is structured. Finally, something that I haven't even touched on, but that is an important question is, what are the performance implications of alliance governance choices? What are the outcome implications? There's a huge range of questions here that reflects the vast opportunities for research.

Paul Beamish, University of Ontario

Equity Joint Ventures in China

In the words of Monty Python, "And now for something completely different." I want to talk to the practitioners about something that relates to joint ventures that, up until now, I have never focused on before. And I have done a lot of work over the years with practitioners. I've certainly interviewed well over five hundred joint venture general managers and CEOs about their joint ventures over the year. This has been my career for the last fifteen years, and the last eight years or so has involved understanding what is going on in China vis-à-vis joint ventures. Certainly, those of you who are practitioners know that there are now over a hundred thousand foreign local joint ventures operating in China, and so a lot of people are trying to figure out what makes these things work and what sorts of things cause them difficulties. I have been following, among many joint ventures, two longitudinally, and these two companies—both American, both very large joint ventures—are, frankly, going down the tubes because they do not understand compensation and motivation within their joint ventures in China.

The first issue relates to fairness, and here I am referring to expatriate versus local compensation packages. The second issue relates to reward management based models versus what I call hybrids. I want to start with two quotations, the first from a Chinese partner in a joint venture: "These eight American managers have total salary equal to the total salary of all four thousand Chinese people in this company." The second quotation offers a U.S. perspective: "We tried to introduce a salary incentive system whereby top producers could double their income. What was the result? Collective anger and a number of the best people leaving the joint venture. What's wrong with these people?" These quotations reflect the reality I have observed in some joint ventures currently operating in China, and I'm trying to figure out just what is going on that could lead to what is ultimately a very unhealthy situation.

The first thing I want to look at is the cost structure currently in place to set up a joint venture. Sending a middle manager over costs $75,000 in base salary, maybe higher. Then we start adding to it a series of items familiar to all the practitioners and some of the academics here today. In a place like Hong Kong, where housing costs have absolutely gone through the roof, you can get up to $300,000 in total costs of sending over an expat. My friends at Xerox, who have sixteen expats in Hong Kong, have a bill of $10 million U.S. for sixteen people. Contrast this with the use of a local manager, one of the top folks there, who may get as much as $10,000 or $20,000 in terms of income and a few allowances, and we find that, essentially, the cost for the senior person is 1/10th or less. Now here's the part that is not understood by people on the outside. If you are going to pay expats a big salary, you've also got to provide an equivalent salary to the Chinese equivalent who is the general manager. The general manager doesn't get that money because it goes to the government. In fact, it may cost more than $300,000, say $450,000, and the general manager only gets a little piece of that extra $150,000. So, the total cost of top management with one expat can very easily be half a million dollars. A lot of Chinese are, legitimately, very upset at what they perceive to be an absolute and complete imbalance between what's reasonable in terms of worth. Is one expat worth 100 or 200 of them?

I want to talk now about the problem of motivation. Is money the number one motivator? For you and me in North America or Western Europe, often a lot of it comes down to money and so we tend to use cash-based systems to try to achieve things. In China, money talks, but in a distorted voice. First, what does a $10,000 reward mean to your star performer in China? Well, what it can mean is a whole lot of grief. It can cause that individual a lot of problems because it sets him apart from all his colleagues, and when it sets him apart, you've ended up creating a very large wall between your star performer and all the persons that he has to work with. So, just handing somebody a bonus system gives you no guarantee that you will achieve the same kind of results that you might receive in the West. A lot of people don't seem to understand how payrolls work in China. There might be 30 categories, literally, of income sources for anybody in China. And then they get into all kinds of minutia with you, at least I would consider it minutia, and that's part of the problem. Who cares about what kind of extra bonus you get at spring festival. You don't care, and I don't care, but they care a whole bunch. Just try to simplify the system and you're missing the point. There are all kinds of things that in the United States or Canada we don't take much account of in terms of salary, but it's a different story in China and it gets reflected in some ways that are not well understood. There is a sense that money is a poor indicator of one's well-being. There is a spiritual, less materialistic element to [motivation] that a lot of us in the West have not well understood.

The other thing to keep in mind, and this will come as a revelation to some, is that there are no secrets about salaries. You may think that what you are paying somebody is a secret, but I've got news for you. Whatever company your manager works for, I can guarantee that I can find out in two days what he is making. If I can find out sitting in London, Ontario, just think how quick it is for somebody in Beijing to find out what everybody is making. So, if anybody is under the illusion that somehow you can pay someone a little bit extra and keep it from the other workers, forget it. It may as well be on page one of the *Detroit News*.

What can we do, if anything, about these issues? Let me just suggest a couple of things. One, in terms of fairness, we can aggressively localize, to go in with an attitude that says we are going to try to move as quickly as possible to more local management. This can be a very pragmatic, straight to the bottom line approach if we can find the right people. If you can explain your use of expats as a transition, that, yes, we have fourteen of these people here right now, but our objective is to get it down to three on an ongoing basis, and we have plans to localize as quickly as possible, that will play very well, particularly if you stick with the argument.

Some people are sent to joint ventures for development purposes. I suggest that you keep his or her cost at the parent company level. Don't add them to the burden of the joint venture, it will just bug the hell out of your partner. If the roles were reversed and they were doing the same thing to us it would be an issue, and I suggest that we utilize the overseas Chinese as a bridge between Western and Chinese management practices. To illustrate, at our business school we recently put together a résumé booklet of all of our students who speak Chinese. We sent it out to a bunch of organizations. Well, a guy from DuPont in Shanghai got on a plane, came over, and in twelve hours made five job offers. They are dying for people who can bridge two perspectives.

Now, in terms of motivation, here are a couple of alternatives we might consider. One, if we talk about reward sharing, reward motivation, talk about a bonus pool. And then understand that a lot of the incentives that we might utilize are ones that will play better than simply cash, things like trips, training, programs, recognition, promotion and titles. There are other things that are perceived as legitimate motivation tools.

Sonia, Ferencikova, University of Economics, Bratislava, the Slovak Republic
Structuring Alliances: The Slovak Experience

I am a special kind of personal strategic alliance, created between the University of Economics in Bratislava, the Fulbright organization, and the William Davidson Institute at the University of Michigan, and naturally I appreciate the contribution of the Business School and the William Davidson Institute very much. I am from Slovakia in the very heart of Europe. Today, I will speak about experiences from this part of Europe which have opened the door for foreign investors and have allowed them to create strategic alliances to a far greater degree than before. Many foreign investors have used these opportunities and they have entered this new market, especially through joint ventures created with the local companies. I would say that equity joint ventures have become the most difficult form of strategic alliance in the first stage of the transitional period.

Although comparatively low, levels of FDI into the Slovak economy have grown steadily since the early 1990s. The smallest absolute growth was recorded in the first year after Slovakia's independence after the division of Czechoslovakia (1993) because of investor uncertainty over the geo-political stability of Slovakia as a new state. I would say that during the Republic's first year, foreign investors preferred to share the risk, and so preferred to create joint ventures. With the growth of economic and political stability, they tended to establish wholly-owned companies more and more. This general rule has some limitations, especially in manufacturing, which only has a small amount of greenfield investment or investment in wholly-owned companies since foreign companies seek out existing capacities, a skilled labor market, etc. At the same time, manufacturing requires a much higher volume of investment and, because of this, it's riskier because companies need more investment. Also, the entrepreneurial risk is much higher in manufacturing than, for example, in hotels, or in the tourist industry. So, foreign companies prefer to share capital costs and entrepreneurial risk in the first stages and years of their activity when they test the environment and market. Many investors saw CEE as a prime site for access to new markets after 1989 and, therefore, tried to ensure this access by building upon the local knowledge of existing domestic firms. Furthermore, in many cases their entry into state-owned companies was allowed only under the condition of a joint venture.

However, recently we have noticed a new trend in investor strategy, especially of large multinationals. This trend is the incremental takeover of the ownership of joint ventures. In several instances in Slovakia during the last two to three years, multinationals have steadily increased their share in joint ventures. A number of reasons exist for it: the multinational's global strategy, conflicts between Slovak parent and foreign investors over joint venture strategy and over the control of key services such as energy, heating, etc., the inability or unwillingness of the Slovak parent company to match investment funds required to maintain the existing level of share ownership, and the problems in the Slovak parent company requiring quick money through the sale of its joint venture.

There are a number of reasons why multinationals got a big share or 100 percent in so-called joint ventures. For example, the biggest investor in the manufacturing sector is Volkswagen. Volkswagen entered our market in 1991, after winning a contest...with General Motors. In one year Volkswagen had 90 percent and now it is a wholly-owned, German company in our territory. The other case is Whirlpool. Whirlpool is the biggest American investor in Slovakia. Whirlpool entered or created a joint venture with the first local producer of washing machines in 1992, and Whirlpool got about 43 percent for capital transfer of about $5 million dollars. In one year, it had 49.9 percent shares. You can see from this number the effort of the Slovak foreign company to keep the majority, but in two years Whirlpool had 72 percent and declared its willingness to buy out the Slovak part of the ownership.

So, when we speak about foreign investors in our country, we have to follow two kinds of impact because foreign direct investments in joint ventures in wholly-owned companies have internal and external effects. Internal effects are very high. For example, they are doing well in increased labor productivity and export. As for the increase of employment, the results are a little painful because the impact has been just the opposite of what was expected. For example, the increase of labor productivity rose from about a hundred units per worker to more than six hundred units per worker three years later. At the same time, employment decreased.

On the other hand, the cases of many joint ventures in Slovakia show that FDI, while having important transformative impacts on individual companies, has had rather limited external effects on the host economy within which joint ventures have been established. We try to create networks of domestic suppliers for foreign investors because it's very important. Some companies are doing very well; some companies are totally separated from the domestic economy. For example, Volkswagen imports 90 percent of imports from German companies. They are doing a better job in this area because they want to decrease production costs and so they now have about 40 percent local imports. So we can say that the primary motive for foreign investors when they enter joint ventures in our country is the new market, a good position to a huge Soviet market and the existence of a low-wage, but skilled labor force. It's really incredible, but the average monthly wage in our country is about $250 per month. In Central Europe—in the Czech Republic, in Hungary, in Poland—there is no higher wage than $300 per month. So, because of production costs and the way they enter our market, foreign companies have become more competitive in world markets.

The role of joint ventures in establishing a deeper network of domestic supply linkages has also been limited. The Slovak producers have not seen many opportunities for increased production arising from FDI. Direct competitors of joint ventures (including Slovak parent companies) have even often been priced out of the market by more efficient production or by imports from a global network of foreign investors. In spite of the growing imports, the companies with FDI are mostly export-oriented. It means their activity should contribute to the surplus in trade balance under the condition that they don't import the majority of materials or components and that they involve domestic suppliers in their production to a broader extent.

Finally, in many cases the essence of joint ventures has been dissolved in Slovakia: when a multinational is a parent company it has used joint venture as a mechanism for the wielding of global corporate power over a relatively weak domestic producer and for its gradual takeover. A different attitude has been seen in cases where the foreign parent company is a medium-sized enterprise having no intention to buy out the Slovak share in the joint venture. The promotion of foreign medium-sized investors should be an alternative way along with the promotion of so-called big strategic investors into the Slovak economy.

Slovakia's joint venture experience is not long. At the present time there is not enough clear evidence that they play an important role in the Slovak economy as a whole. As mentioned in the UNCTAD report, Slovakia is the only country from the Visigrad group in which good economic performance has not been coupled with significant increases in FDI inflows. Incontestably, the FDI placed in joint ventures or in wholly owned companies have had many positive effects, but at this stage they look like islands of investments, separated from the domestic economy in which previous socialist dependencies are being replaced by new forms of global dependency.

Panel II: Discussion and Questions

"I was kind of surprised that you recommended choosing overseas Chinese to manage joint ventures in China. One, they cost just as much or they certainly want to cost just as much as the expatriates; two, they raise the problem of cultural conflict, perhaps similar to what comes with expatriates in the sense of resentment by local Chinese . . . .Plus, Chinese raised outside of China actually do feel that they have a very different mentality. So you have the same costs, intense conflict and the risk of enabling your Western company managers to avoid learning about the local environment."

– Linda Lim

University of Michigan Business School

"Certainly, I do not agree with you. I also have a lot of Asian and, in particular, Chinese students who have gone back to China over the last three years and they are not making the same total income as an expat."

– Paul Beamish

University of Western Ontario

"Actually, I want to second that. If you look at the list of expenses, at least half of those were things that would probably not apply to people who are thinking of returning permanently, i.e. wife's education, moving expenses, car, etc. . . . . Poland, where I do most of my work, was lucky because there was lots and lots of outbound immigration throughout the 80s. So there were people who hadn't been gone so long, and the total costs do go down if you get people who intend to go back permanently. Also, they tend to be better managers because they are plugged into local networks, or capable of plugging in."

– Bob Kennedy

Harvard Business School

"I agree with Linda's comments. I think we need to view these expats not just as high cost managers, but as transmitters of the corporate culture and technology from the foreign investor."

– Don Breiter

Venture China Associates

"There are two other factors that have to be remembered: First, are these second or third generation people coming back? Because this presents a slightly different situation to the student coming back. Second, most expats live in isolated enclaves and there is definitely resentment to that. Also, to Professor Ferencikova, in some of these countries in the Newly Independent States, I think unemployment is one of the things feared most. These labor intensive manufacturing systems are actually preventing unemployment, yet they are viewed somehow as partners who are cheating them. This has to be talked out to show that more people are employed because of these labor intensive devices and that, at this point, this is more important than the efficiency rate."

– Vera Andrushkiw

Wayne State University

Panel III: Managing Alliances

John Child from Cambridge, Karen Newman from Georgetown, and C.K. Prahalad from the University of Michigan and the Davidson Institute look at the management processes within the firms in the context of alliances.

John Child, Cambridge University

Trust and Management of Joint Ventures in China

I've been involved in studies of probably 120 joint ventures since the late 80s in China, but I am going to talk about something that I can't escape anymore because it seems to be so critical, at least in terms of what people in those joint ventures tell me in relation to how they manage them and try to make a success of managing joint ventures, and that's the question of trust.

First of all, I will try to say something about trust itself. Like culture, it is a very difficult concept to get a hold of. What is it? How do you get a hold of it? Secondly, I'll briefly suggest the role that trust can play in the formation, development and management of alliances, and then I want to turn specifically back to the case of China as a business environment. I consider what I will suggest to you as very broad options, what I call low trust versus high trust options, in regard to how much you rely on trust relationships if you're a firm operating in China.

There have been many definitions of trust, but they all seem to agree that trust relates to a situation in which you are in a position of some dependence on somebody else, where you're not certain about the extent to which you can control that relationship or the transactions you are involved in. So, the question immediately arises, on what foundations might people be willing to trust others? I think there are three. The first calculation being roughly equivalent to, "I'm prepared to work with you." The second prediction being roughly, "I'm getting to know you and I can, therefore, predict a bit about your behavior and I can understand where you are coming from and where you are going." And then the third some people would call bonding, "Well, we've now worked sufficiently long and, well, I'm actually getting to like you."

The idea of calculation is that you believe your partner faces sufficient deterrents to prevent him or her from reneging on the commitments or the expectations they've raised. One aspect of calculation, I believe, is that you believe your partner actually has the ability and the competence to deliver on his/her promises. This, I will suggest, is a particularly important basis of trust. Some people would also say it's economic, that it's so calculative that it's not really trust. It depends how you define the term. Once you start working with a partner, it's likely that another basis of trust starts to come into play without the first one going away. It's building up like a hierarchy, if you like, which has to happen with the knowledge of the partner. You begin to know enough about your partner to understand that partner, you start to know that that partner shares certain assumptions with you and you begin to feel the security that comes with being able to predict that partner's behavior. So knowledge, leading to prediction, may then start to build another kind of foundation for trust. At another stage, and here I'm suggesting that this is likely to be sequential, you trust the other partner because a personal friendship has developed, and that might involve a personal liking, identification with them, to some extent sharing the same values, and perhaps a sense of mutual, moral obligation.

Another thing I'd like to suggest, and I think this is relevant when we come back to China, is that there is a distinction between transactions and relationships that are based primarily on trust and those that are based primarily on what I call authority, or legal contract. It seems to me that both essentially involve some sort of codification or formalization of rights and obligations between people or maybe between groups of people, and people are expected to comply with this codification. Trust can substitute for codification, or it can substitute in a way that goes beyond codification. And this means that, potentially, it's a basis for transacting between parties that allows for flexible adaptation to uncertain conditions, because codes and codification have to be built on known conditions. Potentially, trust provides a basis for cooperation into the unknown.

Almost any executive you talk to who is involved in an alliance will say trust is important. No partnership will work without trust, but it is one of the most difficult things to achieve. There seems to be widespread agreement that trust is essential to or is an integral part of successful alliances, particularly, I think, those that are formed, as many are, to reduce and to share risk, to reduce uncertainty in order to facilitate learning. I think it follows from what I am suggesting that if the alliance is formed to "prevent uncertainties and to facilitate learning," then trust has to form a primary basis of relations between the partners while relying on authority, which would be the domination by one partner of the alliance.

It's interesting to speculate as to the correspondence of the different bases for trust with these different stages in alliance development. What I am suggesting, and this is a big issue which I haven't got time to go into, is that in the early stages, you need a basis of calculus that is sufficiently satisfactory for the partners to be willing to form the alliance in the first place. Once they start working together there's an element of predictability which comes into play and adds a further basis for trust. As the alliance unfolds, as it is successful and develops a rationale of its own, then you move towards elements of personal bonding and towards identification between the partners, or at least between the individuals who are working together on behalf of the partners.

If you manage to build up all these bases for trust in a relationship and things start to go wrong, such as some glitches in terms of the economic performance or the calculus, if you've achieved a degree of bonding, then you will probably be in a much better position to sort out the underlying problem rather than flounder on the first economic difficulty that comes across. On the other hand, it also suggests that if you don't get this initial calculation right, you will probably never give yourself much chance of building up other bases of trust, and that element of working together and personal bonding will never get a chance to develop.

The next question is, how relevant is this to understanding how this understanding of trust might work with China? China is a peculiar environment in the sense that it has certain elements of uncertainty that are perhaps not found in more familiar environments. Some of the distinctions that some complexity theorists make, especially Murray Gilman, occur between what he calls critical complexity, which simply means having a lot of elements in a system and a lot of factors in the environment, and getting to know them and taking account of them. Where there is effective complexity, there's a lot of variability and uncertainty in the relationship between those elements.

The next point is, by which sort of logic is this system being ordered? I think many people would say that China is a very complex environment because of what I call crude complexity. It has at least three different business systems and very important generational differences which become important for understanding the motivations of different generational groups. Once you take account of these, you can make predictions and find your way around the system. I think the more significant difficulties arise from elements of unpredictability in the system. So it's not just complex in that it's highly differentiated and it's a very big social and economic system because there's uncertainty, for example, as to who is the government. Because they are very much involved in business matters and in a way that is often unpredictable, you never know when they're going to put on an additional local tax. Finally, there are still significant shortages in the system. And if you consider how the Chinese deal with these things, they cope with them in a rather different way because rather than rely heavily on contract or authority, they're still relatively low on codification in the system. As a result, getting things done through relationships and mutual obligations tends to substitute for getting things done on the basis of contract and codification.

Now, I feel this is very, very speculative, but I see two options open to firms in China. The first option might be called a low trust option, but in terms of complexity theory, it is also equivalent to trying to reduce complexity rather than trying to absorb it or cope with it directly. In this option, the firm tries as hard as possible to impose its own authority, its own system of management, and its own contractual agreements with a Chinese partner or with the institutional government in the environment. This may mean they favor greenfield investment and a kind of greenfield investment in staff, selecting their own staff from scratch. This approach, as you may know, has been strongly advocated in the *Harvard Business Review* and recent issues of *MacKinsey Quarterly*. But people have quite rightly, this morning, raised the question of contingency, and this approach may not be feasible, for example, where a Chinese partner is still a key for delivering a market. Second, I think the low trust option raises very serious limitations as to how far a genuine transfer of business expertise can be made into Chinese managers, particularly expertise in terms of the strategic level, understanding how to do business.

Despite the fact that what I'm calling a low trust option appears to represent quite a strong trend at the moment, there is perhaps also a case for what we might call a higher trust option which aims to absorb the complexity of the Chinese system and the uncertainties by working closely with the Chinese partner. This approach suggests a joint venture rather than the earlier approach with a sizable, but not necessarily a majority,.of Chinese equity share. It implies that the Chinese partner has a meaningful presence on the board of directors and it actually shares actively in the management of the joint venture. It should allow for a lower proportion of expatriates and it certainly would involve the conscious cultivation of trust for a number of policies that will deliberately be followed.

To conclude, I think it's vital to consider the role of trust in any joint venture, but not the least in the China joint venture given the nature of the environment. And it's very important to consider what basis you are trying to put your trust on. Are you going to try to go right through that hierarchy and put it on the basis that's not just calculative, or are you going to leave it on a purely economic basis? So, I hope you'll help me struggle with this issue. It is clearly one we can't ignore, but it's not very well understood.

Karen Newman, Georgetown University

Organizational Transformation Through Strategic Alliances

I've been doing work in the Czech Republic for the last 5 years, building longitudinal case studies of formerly state-owned companies that are going through the transition process. Two of those companies have entered into strategic alliances. So, I come at strategic alliances not as the main focus of my investigation, but as one of the ways in which two of these companies have sought to transform themselves.

Prior to the revolution, companies had what would pass for a competitive advantage. Even though it was not a competitive market, they had resources and capabilities and, just like Western firms, the interaction with other firms combined to make those companies effective, given the planned economy, given the context in which they operated. Their capabilities in the Czech Republic included things like producing to meet demand, engineering the living daylights out of products, sometimes over-engineering them, and managing economies of scarcity by stockpiling. We call it "just in case" management.

The Czechs, and I think the Slovaks as well, have a tradition of "golden hands": they can fix anything. The good news is that they could get the product out the door; the bad news is it wasn't exactly to the customer's specifications all the time. Those were some of the capabilities prior to the revolution. Comes the competitive shock and all of a sudden those resources and capabilities are called into question with respect to their abilities to help the firm compete. So what we are looking at is how these resources and capabilities are transformed, yet again, to produce a new competitive advantage for these firms.

The first joint venture I'm going to talk about is between ABB and a company in the second biggest town in the Czech Republic, First Brno Machinery, or PBS for short.

This is a joint venture which, in fact, led to a purchase by ABB in February of this year. PBS is a boiler business that happens to know how to burn dirty coal better than most folks and, ABB, knowing that part of the world still burns dirty coal, wanted that technology. ABB also was a recognized brand name in Central and Eastern Europe, and they wanted access to those markets. PBS needed money and they needed management know-how. They also needed technology, specifically gas-fired technology rather than coal. They needed brand name recognition outside Central and Eastern Europe and they needed access to markets outside their traditional territory, which had been primarily the Soviet block countries. This alliance has worked reasonably well, but the PBS parent company was not happy with the joint ventures since it was not negotiated in terms favorable to PBS.

The second joint venture is a commercial arrangement between John Deere, the U.S. tractor company, and Zetor, which had the reputation for producing communist tractors. There was a conversation about a joint venture or an outright purchase in the early 1990's that did not come to fruition, so instead they signed an agreement with each other that Zetor would supply its small red tractors to Deere to be painted green and sold through the Deere distribution network. Until six months ago everyone said that it was just a question of when Deere would buy Zetor, not if. Deere's purpose in this was that they needed an inexpensive tractor for developing market economies and Zetor needed new markets, capital, and management know-how.

The question is, how do you transform human capital? How do you transform these companies, especially their capabilities and, at least, leadership ability? How do these two things change so that the company does indeed change and become competitive? I'm working with a framework developed by a guy in the Netherlands for thinking about how cultures differ. He says that country cultures differ on four dimensions. One is power distance, that is the extent to which we accept as legitimate and okay big differences between the "haves" and the "have nots," or the high status people and low status people. U.S. companies are low power distance; most Anglo countries are. We tend to try to diminish power distances. The Czech Republic is a higher power distance country than the U.S.

The second dimension, individualism/collectivism, refers to the extent to which an individual derives an identity from individual capabilities and achievements versus membership in a collective. The U.S. is off the charts on individualism; the rest of the world is much more collective. The last category is masculine and feminine. Masculine society places emphasis on achievement, work, merit rewards, whereas feminine societies emphasize things like the quality of working life, the quality of relationships, the meaning of life, and work as a means toward a good life, rather than the end in itself. The Czech Republic is more feminine than the United States.

Now, ABB is a big multinational/transnational company. The company itself is fairly decentralized; authority is based more on expertise than on position. Individual accountability is very important in ABB. There is a lot of willingness to take reasonable risks in ABB, and merit-based rewards are the norm. PBS is a very different kind of company. It is not nearly as multicultural and had a reputation as the Czech family silver, one of the good companies in the Republic. It is much more centralized and power is based much more on position. There is a tendency at PBS, according to their top managers, for people to actually hide in the collectivity. It's not so much that they derive their identity from the collectivity, but that they derive their safety from the collectivity and avoid individual responsibility. There is a real risk aversion and, just like a lot of other Czech companies, it follows a "just in case" mentality. So, the question is, how are we going to transform human capital in these companies and then, by implication, how are we going to make these strategic alliances work in the long run? Picking up on something Pierre said earlier today, these are cases in which the companies have very different capabilities and it's easier to learn if you've got similar capabilities. How can we get these companies close enough to each other that they can really benefit from this alliance and endure for the long run?

With respect to power distance, the Czech Republic is a higher power distance country than the U.S., so it's probably okay to use hierarchy more than you might use it in the United States for changing the way employees do their work. It's terribly important that you co-op management first and then hope, of course, that management will be a role model. Also, appreciate that people at least derive safety, if not identity, from the collectivity and use this to your advantage in managing the joint venture so that you allow people to develop new behaviors in the safety of a group. Reduce the uncertainty that's present in any transition to as knowable and understandable bits as possible. Try to create a series of small steps rather than giant steps so that people can take smaller risks rather than larger ones. Move as quickly as possible. Of course, this is very hard in an institutional context that keeps changing. Don't use job loss as a threat or punishment, except in extraordinary cases, because that is going to make people catatonic in countries where security is so terribly important and where tolerance of ambiguity is low. On the masculine/feminine side, individual merit-based rewards are not likely to be as effective in these countries as they are in the United States. Appeal to a higher purpose, a higher quality of life. In the Czech Republic, you might appeal to the next generation, to the history, or the grand culture of the country. Finally, in transitional economies, the Western partner tends to think that they've got it right and that there's not too much to learn from the local partner, and that's not necessarily true. So, the Western partner needs to appreciate the possibility that its corporate culture might not be the perfect corporate culture to try to transfer to the host company. Rather, the right set of management systems and corporate culture might be some kind of a hybrid between the two which appreciates the cultural characteristics of the host country.

C.K. Prahalad, University of Michigan Business School/WDI

The Role of Joint Ventures in India

I'm going to take a somewhat different perspective. The bottom line for me holds three things. First, all joint ventures and alliances in a transitional economy are inherently unstable. Any time you have discontinuous change, all the preconditions with which you start the joint venture change over time. So, if you don't start with the assumption that inherently joint ventures are unstable, then you are likely to be surprised. Second, anytime you have a joint venture in a transitional economy you should start with the assumption that it is a transition structure and, therefore, one of the two is going to be brought over. Third, you should not be surprised because joint ventures and alliances in the United States in high tech industries are unstable, too. It has nothing to do with the inherent trust and quality of the relationships; it is a structural problem and we have to come to terms with it.

My starting point is that you do not start with no history. Mulitnationals start with histories, so do Indian companies, so do Chinese companies, and so on. Understanding the backgrounds and the experience of these companies and the countries is extremely critical to understanding the relationship. I will use the Indian example of transition in the last 15 years to show this. Second, the starting assumptions of a relationship are critical because if you understand how those assumptions will evolve when changed, you know how the relationships will change. You can predict the evolution of these relationships if you understand the structure of the industries in which you are making the deal.

For the last 50 years, India has had an active public sector and a growing public sector, which is slowing down. It had enormous control of all industry by the government bureaucracies, and also a very viable private sector. It always had a multinational sector. Many transitional economies look like this. In China there is a public sector, a private sector, emerging private sector, and a multinational sector. The same thing exists in the erstwhile Soviet Union. So, at least one thing can be said if you want to understand what this world will look like when it goes through the transition. Institutions of market capitalism, the procedures that are required, the legal structure that's required in order for command economies to become market economies are going to go through a stage of lags and leaps, which are going to make it look like India. And if you want to understand all the confusion that can possibly take place, all you need to do is to understand India.

I am going to start by looking at the historical reality in the last 50 years in India. Phase one is 1960-1982. Most multinationals were not allowed inside the country, or only under stringent rules. Nor did India want to industrialize itself, or go abroad. Self-sufficiency was the key idea, and the Monopolies and Restricted Trade Policies Act made sure that no company grew to world scale and world class. But the interesting thing is you have low productivity, stagnations, scarcity of all kinds, little or no choice to consumers, sort of the Czech case. At the same time, there were several joint ventures, but multinationals looked at the joint ventures primarily from a local market perspective, and that made a huge difference. When the market is small and you have primarily a local market orientation, you do not really care too much about what happens in the place. You want to have a foot in the door. Now then, the country gets into a foreign exchange crisis and then they said, we are going to globalize India. What it meant was, how do we get multinationals into India, not how do we get Indian companies to world class. So, attracting foreign investment was a key idea and a large number of joint ventures were formed during this regime, but most focused on the Indian market place.

There is a learning phase and Indian joint venture partners were essentially escorts in that phase. That's not a flattering way to describe the Indian joint venture partner, but basically, the multinationals were saying to themselves that they had no clue how the Indian bureaucracy worked and that they needed a local person to navigate. When the system became clear and transparent, then they asked, why do I need this escort? And that's, I think, what is happening in most other countries, even though nobody wants to admit it. Escorts are less required and that is true in China as well.

In the last two years, India has had some very interesting new phenomena. The multinationals are willing to come into the market and to invest big bucks. They have been around for three to four years and understand how it works. It's a realistic market and it is going to grow. More importantly, they're finding India to be a fairly good source of talent and now feel that they can use these resources to create an export platform in the global marketplace. This is a very different perception and opportunity from saying that they will use India primarily for the local market. Most companies now can get 100 percent ownership in a transparent market place, so they don't want a partner. On the other hand, the Indian partner has worked with the multinational and wants to use the multinational system to enlarge its own scope, but it has a problem with control in terms of the technology used, transfer prices, scheduling, and a wide variety of things. Although the Indian partner is willing to invest, it can't match the multinational's funds. So, there is an effective dilution taking place so that the Indian partner has only two choices, either to quit, or drag its feet. I believe this is a natural progression that is not peculiarly Indian and it will happen in a large number of transitional economies.

Now you ask, has the world changed for Indian entrepreneurs? The answer for me is yes, it has. If you go back to the old system, the bureaucracy and the Indian entrepreneurs were very tightly linked. Publicly they always complained about each other; privately, they worked very tightly together to each other's mutual benefit. The multinationals were the bad guys and were left out. Now with the initial flush of joint ventures the Indian partner decided to use his knowledge of the politicians and the bureaucracy to leverage a relationship with a multinational. In fact, most entrepreneurs were smart enough, or thought they were, to keep the multinational away from a direct relationship with the bureaucracy or with financial institutions. Unfortunately, the world looks like this for them: The bureaucracy is becoming less and less powerful, so suddenly they find that P&G, for instance, can have degrees of freedom and independence from the Indian partner and suddenly the Indian partner finds that he doesn't have a point of leverage with a multinational because the internal connection used to be important, but has become less relevant. When this happens, the value of the local partner becomes less relevant, too.

So, my conclusion is this. If you look at MMCs and the Indian partners, they start with an assumption that there is a need for an Indian partner to work in India. This happens in China and Czechoslovakia. Then they ask, is one really needed? That's the question ABB is asking, and that's the question everybody else will ask once the system becomes transparent. Indian companies also ask, do we need a multinational to grow in our own market? Are we creating a market for multinationals? It's a very different position. To say, "I can benefit from working with a multinational," to saying, "I'm not benefiting, it is the multinational who is benefiting," is a very different position. What happens next? The multinational feels he has been used and the Indian partner feels even more sore about this because he feels used and about to be dumped by the multinational. The multinational thought it was going to be a very small piece of its global enterprise which it could afford to manage any way it wanted. If it's going to be 20% of its profit, that's a different game. So, the relative significance of the Indian or the Chinese to the global enterprise makes a difference to the kind of management attention you will give. The Indians, who thought they could go out and get 5 joint venture partners or 17 joint venture partners and somehow manage them, now find that it is not possible to manage them because the multinationals expect to get more control over what's happening inside India in their own operations.

So, there is a whole range of issues and maybe some of it is cultural, but not a lot. I don't think it is any different in any other transitional economy. The social climate says you are selling out and there is a tremendous sense of dependency and helplessness from the Indian partner's perspective. In other words, you are not only losing your company, you are losing your face, because you sold out to the multinational company and, therefore, visible divorce is, I think, more likely than otherwise. I believe that most of these joint ventures are dissolved or will be dissolved. So, I am not at all excited about these joint ventures because I think they are transition structures. They will get dissolved and the best thing to say is, let's find out how to make money in this process. And some Indian companies have figured this out. They will come to you and say, we are the best in showing you around. We don't want to manage it, we'll take equity position, and when you want to buy it, buy our stock and we'll make money.

Panel III: Discussion and Questions

"We talked about the transfer of knowledge and of culture in a one-way fashion. That is, we need to get people who can transfer American culture, management culture, to those countries. But one of the reasons to have expatriates is for them to learn about the markets in China, India, or wherever, and bring it back to the home company. I wondered if any of the companies here are doing that, or realize that they have to do that?"

– Linda Lim

University of Michigan Business School

"I'm from Dana Corporation. We've got 5 joint ventures in China and we've got some joint ventures in India with about 7 manufacturing plants, and that issue is certainly a struggle within our organization. First, we have a hard time finding good candidates who are adequately prepared for expatriate management jobs in these economies. Second, bringing them back to the U.S., or finding other challenges for them once they're through overseas, is another challenge. But we have enough success to have the money we need to do anything we want around the globe. The real limiting factor we have is finding the talent to undertake the jobs we have overseas."

– Glen Fillion

Dana Corporation

"We've made the assumption throughout the day that it's American or North American expats who go abroad and then perhaps learn something about the host country culture and come back to the United States or Canada and teach the rest of the corporation. Do any companies in here bring their Chinese top manager partners to the U.S. for one year to work side by side with their American counterparts, and to learn how it works in America hands on?"

– Karen Newman

Georgetown University

"We do at Caterpillar. We're putting together a program now that will start in August in which we will bring twelve Chinese managers from our joint ventures and joint venture partners in China to the U.S. for six months of combined classroom and on-the-job training."

– Bill Cook
Caterpillar, Inc.

"To me that's a big move forward, but it's still one step behind what I am imagining and what I see some companies doing. It is not bringing Chinese here for training, it is bringing Chinese to run American operations. I think that's where I believe that, given the sheer size and the differences in these markets, a significant amount of innovation is taking place in Asia."

– C. K. Prahalad
University of Michigan Business School
William Davidson Institute

"I think there is not only learning transfer from one partner to another, there is also opportunity for mutual learning. These opportunities may be triggered by relevant enlightened management action."

– John Child
Cambridge University

"Let's harken back to the Caterpillar discussion about the globalized mind set. It sounds almost utopian in the kind of world you envision, with Chinese managers moving into the U.S. and into Brazil and around the world and similarly for U.S. managers and British managers, yet coming in this morning there was the MFN debate kindling again. We have had war ships off the coast of China and we have counterespionage activity within the U.S. This raises an old question: Is the national state of friction in the move towards this utopian world, and is there some value there?"

– Jim Walsh
University of Michigan Business School
William Davidson Institute

Panel IV: Commentary by Practitioners

Members of the business community provide feedback and perspective on joint ventures and strategic alliances in transitional economies.

Peter Walters, Guardian Industries Corp.

Alternative Approaches for Strategic Alliances

I think it might be helpful to some of you to understand my perspective if you had a quick background on Guardian Industries and our international activities. We are a glass manufacturing company primarily. We manufacture raw glass, which needs a huge manufacturing plant that melts a variety of raw materials. We do hundreds of tons of glass a day and we also are a major manufacturer of downstream products, from automobile glass, which, worldwide, uses about 30 percent of all flat glass from mirrors to windows, to high rise office buildings, and so forth. One of the constraints on Guardian's growth internationally is that we can't build a small glass manufacturing plant to serve regional or local markets. Fabricating plants are considerably less expensive, but in our case we have found the actual float glass, as it's called, a more profitable enterprise. So we tend to first build a float glass plant and then we expand in the country where we build in the downstream fabricating.

I think we are all here today because strategic alliances in general are hard to create and manage, and in transitional economies they are even more difficult. Why create a strategic alliance in the first place? One of the reasons why these kinds of alliances are so difficult is because they frequently begin as forced marriages. We are asked to bid when a country is privatizing some segment of its economy or some individual enterprise. We bid against competitors and it can be an auction-type bid or it can be a negotiated sale. In some cases, we are handed partners because the government has decided that this is the company it wants to privatize. It has decided our company can in fact joint venture with it and we are to negotiate. So, the male/female spark is absent in these relationships.

The first decision, therefore, once you've decided to go to a geographic area, is whether you have to have a partner or not. The law may require it. If it's legally required, do you need a partner for market access? Is there technology that's useful in that country that you would like to transfer outside of the country? Do you need governmental relations assistance in order to get licenses to do business in the country, or do you need management capability in order to operate a business in the country? Do you have to have local language people to communicate to the workforce, and should they come from the joint venture partner? So, first the decision has to be made whether to have a partner or not. Assuming that the answer is yes, it is not so easy to identify the partner if it hasn't been handed to you.

We've struggled with this, quite honestly. Companies that have sold for many years in a country may well have a distribution system or a set of distribution relationships that allow it over time to learn a lot about, not only business practices, but who the movers and shakers might be in their own industry or some related industry that would be attractive. Those who do not have that luxury, if they have not sold into a market, probably have tended to identify partners through some form of grapevine approach. Typically, and this is certainly the case in the transitional economies, the first in are the banks and the law firms and the accounting firms, and it is inexpensive for all three of those to set up some kind of regional office.

The first step frequently is to visit those with whom one has relationships to ask questions about who's doing what to whom in the country. Who might be open to a joint venture? Who does the government favor? There is not, to my knowledge, a good source of information that can be used to systematically eliminate possible partners and identify those you ultimately choose. They have to go through a courting process with some dinners and walks on the factory floor until they find out how the manufacturing facilities are run and determine what kind of relationships they have with financial institutions in the country. Even then they end up relying on a gut feeling. It's not easy at all, and this is undoubtedly one of the reasons why a lot of the alliances don't last.

We happen to have done it in all different ways. We have been given a partner, negotiated joint ventures—roughly 50/50—with strong local partners, and we have negotiated joint ventures with more medium-sized companies that typically would demand less equity. Almost by definition, if you negotiate with a strong local partner, they will want 50% or 51%. It's pretty tough to get a prestigious company to take 20% or 15%. Today, Guardian would prefer 80/20 joint ventures. We have 3 basic 50/50 joint ventures and they are very, very maintenance demanding on our part. Each partner is continually jockeying for position—we do it, they do it—and this is pretty tough to manage. We don't enter into minority joint ventures ourselves because our technology is such that we have to protect it. With the exception of one of our 50/50 joint ventures, I'd have to say that Guardian's most successful joint ventures in transitional economies are ones in which we bought out the other partner, and we either spelled this out in the agreement to begin with, or understood that it was going to happen.

I'd also like to note that there was not a lot of discussion here today about how success is measured. Not many people today have talked about profits. Sometimes strategic means "lose money," and you do have to wonder whether or not our expectations are lower in strategic alliances than they are in our wholly-owned enterprises. You certainly can't ask how long a joint venture lasts as a definition of success because, as mentioned earlier, our most successful ones only lasted 4-5 years. Woefully lacking in all of this is much information on partners, not only the information to systematically identify partners, but once we've entered into a joint venture, we're pretty naive when it comes to information about these partners and, over time, we find out things that we wish we had known early on. There is a growing group of consultants who do in-depth, behind the scenes investigative analysis, and we have started to find that relevant.

I do have a criticism of my own brothers and sisters in the manufacturing sector that I think the academic community can help us with and that is that there is a real herd instinct with global investment. In 1990 and 1991 we were all fools if we weren't rushing to explore the opportunities in Russia, in Central Europe, and then afterwards there was a widespread sobering up. In 1992 and 1993, China became hot again and you had to be there or run the risk of being frozen out. And maybe in 1994 and 1995, as the Chinese economy started to slow a bit, a lot of projects that had started, stopped. There still aren't that many manufacturing companies who have money in China. India became the place to be. Well, you know, for my money, there is going to be a huge shakeout in India in the next few years, and you don't have to look any farther than the automobile sector. And now people have started to get off India a little bit and next year it looks like Brazil, because Brazil has figured out how to manage its economy and they've put hyper-inflation under control.

This is all unhealthy. It is not the way to go about creating strategic alliances and growth for your company. We all have to have a longer term perspective than this as we grow, even if our perspective in a strategic alliance is only 4 or 5 years. The reason why so much of this is problematic is that we haven't been at it very long. As difficult as strategic alliances are in Japan and Europe and the U.S., at least we've been at it for 30 years, so maybe there is some body of knowledge that we can look at, some case studies, even some systematic results that show that you can do this or you can do that in the transitional economies of Central/Eastern Europe, Russia, China, and India. A lot of joint ventures have only been in existence for 2 to 3 years, and that isn't much time on which to base evaluations.

Don Breiter, Venture China Associates

Strategic "Marriages" in China

I've been coming to the University of Michigan for many years and for the last 3 or 4 years working with the Davidson Institute. I worked at Cummins Engine Company for many years and it was my privilege to work with them as a founding partner of the Institute. I am now an independent consultant, focusing on working with businesses, primarily American businesses, who are trying to establish themselves in China.

I was eagerly waiting for someone to put up the line, "one bed, different dreams," on the screen because I am so used to going to conferences about China, and this is a Chinese expression that usually begins rather than ends the discussion as an example of the regrettable failure to communicate between partners on the front end of the process. That failure in this type of venture is inevitable. At Cummins 3 to 4 years ago, strategic alliances were and are still today considered the major vehicle for growth around the world. I believe there were only a few speakers today still speaking and treating alliances in that manner, and I found this somewhat surprising. In a way, however, it is in line with my own perceptions, having worked on trying to create these types of strategic alliances that are more than just marriages of convenience and recognizing how difficult it is.

Professor Singh touched on the fact that the two partners in the alliance, as in a marriage, should be complementary. It doesn't make sense if they are exactly the same, and yet they need to be compatible. The difficulty, as between the sexes, of finding people who are complementary and yet compatible lies in having come from different backgrounds with different experiences, which is what often gets in the way of being truly compatible. I think there is a sense of disappointment for many companies who have experienced trying to set up these joint ventures, on both fronts. Many companies find it difficult to establish the relationships of trust described earlier, so it makes it very difficult to jump into a venture on the front end as, perhaps, a naive lover or a young married person. This kind of trust is very hard to start with and build on. Trust is very hard to build over a negotiation table, whether it's the way the Chinese sit around it, or the way the U.S. people bring their lawyers. It's much better if you have an earlier relationship with a licensee relationship or supplier/customer relationship where, over a period of time of normal business practice, you develop some sense of trust and ability to predict how the others behave. In addition, I think U.S. companies, as they get into the ventures, have been disappointed with the complementary nature of their partner and the areas which they felt the partners were going to bring, whether that's access to local government and understanding how to get things done, or market access. This can lead to a sense of "why did I get into this anyway, if the foreign partner really does not, or is not able, to help us in the way we had expected?"

One more issue about compatibility. Whether it's in a marriage or in a relationship, it has something to do with a common vision and being able to develop that and having a sense of the future. Most Westerners going into a venture have a vision of China as a small part of their current business. They want to add that treasure to their global capabilities and they look at it quite idealistically as they look at its structure and discuss how best to organize around that, how to get the right people, the right equipment and the right facility. Of course, for the Chinese managers, the China market is not new for them. It's not the future for them and they seem to be much more preoccupied with the past and the present than our managers are as we shape the joint venture. The Chinese manager's point of view is to preserve power, control, prestige and privilege in this environment while absorbing the cash and technology. This difference in motivations is very hard to reconcile between the foreign managers coming into China, especially in the context of a negotiation table and contractual language.

Other opportunities for alternative ways of getting into the country, especially with wholly-owned entities and, in addition, holding companies which are wholly-owned, also allow a multinational corporation to create its own identity as opposed to being pigeon-holed into several different joint ventures. I've been involved in working in those paths and I see companies pursuing these as well. I think this is positive because you really can see the loosening up on the other side that will allow it to happen, whether it's local governments who are willing to give approval or the national government in China that is gradually relinquishing its power of approval. So, a company going in now is faced with the question, "well, should I jump into this old model or can I do it differently, or, if I wait another year or two, will those constraints have disappeared completely as they appeared to in Slovakia?" I feel somewhat positive that if companies have more choice as to how they choose to enter, they can now engage in strategic alliances that are truly strategic, that is, find partners who are truly worthy of that trust and can be compatible out of choice, not just because it's the only way into that society.

So, I think we'll see a greater mix and, as a result, I hope that the joint ventures formed in the future will be better for it, will not be solely marriages of convenience, but can be the kind of bed where there is one dream as well. Being able to enunciate a common vision and have a common management team that doesn't matter whether they're expats or locals, but the best people around the world pursuing a single vision, still makes sense to building strategic alliances.

Bill Cook, Caterpillar, Inc.

Transition to What? What We Don't Know

There's a story going around in Russia, for those of us working deals, that a foreigner is going to Russia looking for a partner with experience and the local manufacturer there is looking for a partner with cash. After a few years, the local partner has the cash and the foreign partner has the experience, so evidently it seems to be working.

We go out of our way to try to keep that from happening, so maybe we seem to be somewhat of a stubborn partner. Now let me begin by talking about process. We start our value chain with marketing and distribution. We normally start out importing into a country. We build a dealership organization and we invest a lot of time and money and managerial expertise in making that world class. This process has worked for us everywhere in the world except China, Russia and India, so far. We build a product support capability and local leadership turns us from a global company into a local company, and it's a critical function that they play for us. We have four major bases of manufacturing that are world class in every way: in Western Europe and Japan, where it's a 50/50 joint venture and has been in existence since 1964; then, of course, in the United States, and also in Brazil, where we have pretty much gone through this process. So we begin manufacturing really as market access and that turns into developing local content through suppliers, and then out of that we start to find some core competencies that make sense, and we export into our global infrastructure. We start to integrate the local leadership and we start through training, but it takes a long time to get the local managers to the point where they understand our whole global infrastructure, and so they stay outside for a while and eventually get integrated.

Our products are the same around the world, in North America, Europe, Brazil, Japan, and now in China, and we would expect in Russia as well. Ultimately, we develop local design capability, which is the last piece of the puzzle. Now that brings us to the process of putting in place a value chain, an infrastructure, a business infrastructure as we go into new markets. This whole value chain is relevant to China and Russia. Whether it is to India, we are not really sure, but as we look at China and Russia, particularly in the context of strategic alliances, what we see are competing value chains. With any partner we talk to, and you need to understand that in our business we're in that core Communist sector of the military industrial complex, our competitors are state companies, their suppliers are state companies, their partners are state companies and, for the most part, many of our customers are state companies. No matter how good we are, until that starts to change, we can't really compete and we haven't figured out how to do it. As we look at the value chains of those companies, the Chinese and the Russians are concerns today. We know how to compete with the Japanese and Europeans and we're getting our share of that business. The question is, how do we get the bigger piece of the business, the 80 percent to 90 percent that the Chinese and the Russians have? We don't know how to do it.

We sell differentiated product to discriminating customers. The Chinese don't know what that means, and we have to be able to teach them. That's the only way we know how to do business. We go down to entrepreneurial leadership and lots of time, particularly in Russia, they've got a completely different agenda. In effect, the Chinese do too, and it takes a lot of work. Our concept of distribution is illegal in China. We have dealers who are investing millions of dollars who cannot buy and sell. They have a workshop license and we pay them a fee, but it's a work around, and we are working through that and we're investing in that and we expect it to change, but we're betting on the outcome.

In terms of manufacturing, we insist on quality, the same quality everywhere in the world if we're going to put our name on it. The supply base, more so in China than in Russia, just simply is not there to deliver that kind of quality, and it takes lots of work and lots of investment. In addition, when you look at manufacturing, the Russian companies, which are essentially monopolies, are very vertically integrated in a very closed economy. So, the whole concept of being globally competitive, forming alliances and creating value chains is very foreign to them. Trying to tap into that resource gets real tough.

All of this understanding is starting to raise questions about whether or not we can do business in China and Russia the same way we do business everywhere else in the world. Is the value chain most appropriately structured in China and Russia the same way we structure it other places in the world? We like to think of ourselves as a truly global company, looking from a global perspective, learning from each other, so it's important to integrate the value chain we put in place in China and Russia so that we can learn from that, too. But is it appropriate? Our partners consistently tell us it isn't. And we tell them, "well, we're not too sure."

We have a whole bunch of studies underway to try to find answers to some of these questions. First, you have to start with the market. What does it want now and what will it want in the future? How and why will it change? Second, how much control do we need over our distribution, and how do we get competitive products to the dealers to sustain them? If we are only supplying product that we build our way, with our prices and premiums and quality, is that enough to sustain that distribution? We're liable to have a hollow shell. Is local manufacturing required to be competitive? What local supplier base exists and what development is required? Should we offer only international products or should we develop local brands? For us, that's heresy to even ask the question, but we are, and we are asking it very seriously. Why aren't international products competitive today and are local products really competitive? Will they be in the future? The local products we compete with sell for less than half of ours, and we don't really know why. Our partners and other companies we've talked to say that they are profitable, but we don't really believe them, and we have a number of studies under way to benchmark our product to Chinese product, and our product to Russian product, and we don't really know how they do it.

How will the local competitors transition and how will they survive? Where does the entrepreneurial leadership, the capital and technology come from? Why and how long will the transition take? If the transition process takes a very short time, and these companies lose their support and eventually fail, then can we just muscle through with our approach? If the transition process takes ten, twenty, thirty years, and there's nothing to say that it won't, it's not given that these two countries will, in fact, become global and integrated into the world economy. That's very much in question. How will the local political leadership allow local companies to fail while foreigners succeed and gain market share? Why won't they do that? It's a big concern. A global company looks at the value chain through the eyes of efficiency, and within that value chain there are a lot of places and opportunities for permanent alliances, as long as we control the value and are able to make the moves that we have to make from time to time to keep that value chain competitive. Within the context of these two national economies, however, we may not be allowed to do that and be competitive. And do international competitors see the opportunity the same way we do? If so, why do they act differently? In some cases, we are doing a lot of the same things, and in some cases, we aren't.

Zbigniew Latkowski, PTK–Centertel

The Role of Joint Ventures in Poland

What I am going to talk to you about today is based on my observations of the person who works and lives and operates in the Polish economy right now. I would like to talk about what differentiates joint venture companies in Poland from the Polish companies and especially about their strengths.

The first aspect that differentiates them is the properly worked out business plan. Unfortunately, mistakes happen. One company, a foreign trade company, did not understand and research our market and ceased to exist after two or three years. What is especially interesting about this company is that it was extremely successful in all the other markets. In Poland, however, it found an unexpectedly strong competitor. Also, the competitor was not visible because it included about 500 very small, local businesses. Another factor that differentiates those companies is the implementation of state-of-the-art technology. Those companies are also backed up with full investment, the financing from companies. I cooperated and worked at about 4 companies, and this is the first company that was really extremely successful. Finally, the large scale businesses also vary. I would like to add that foreign companies are well perceived by our local workforce. These are the companies that provide good income, good advertising and good product.

Now we will talk about the weaknesses of joint venture companies. The culture and business differences between, or among the partners result in misunderstandings and disagreements. If the scope is really big, then those differences might cause some serious political problems. There are significant differences in experiences as well as qualifications of executive members coming from abroad. Also, members of executive boards do not always work as a team. Differences in culture and divergence of objectives result from the problem that some companies' top managements influence the decision-making process of the partners who are there locally. The more partners, the bigger the problem. There are often serious problems with communications, and that is the language capability, but also the knowledge of relationships in the particular company. Some companies form joint ventures with already existing companies. In this case, those local companies have already hired a workforce and it's a problem of managing those existing workforces. Sometimes, the joint venture is started from the ground up and then it can design the policy, the human resource management, and the policy governing those according to its own needs.

In Poland, joint venture companies are counting on young men and women who are usually well-educated young people, with big intellectual and physical potential and high motivation to work for potentially high earnings. The weaker side of this kind of recruitment effort lies in recruiting inexperienced employees. We can't expect teams to stabilize. In order to stabilize they need experienced and mature management. Very often, these employees are overqualified and overeducated for the positions. Another interesting observation is that some managers coming from abroad have a very tolerant policy towards their employees. So, if there is some kind of misconduct, and if I ask whether this would be tolerated in their country, they say it would not. So the question is, why are they acting quite differently in Poland? Finally, there are difficulties with compensation, because the compensation market is not stable.

Many of the consultants I have talked to mention that there is a problem of inadequate selection of managers sent over to Poland. Many managers have lacked adequate knowledge and understanding of the country and its culture. One of the reasons might be that managers are coming over for short-term assignments.