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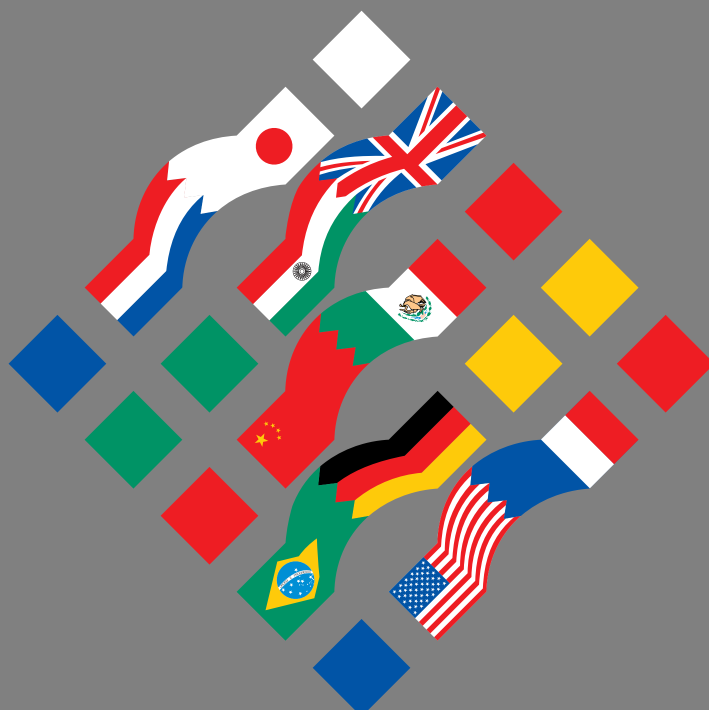
An Asian Perspective on Cross-Border Alliances:



Supplement to the Cross-Border Alliances Viewpoint

An Asian Perspective on Cross-Border Alliances: Different Dreams

by Ian Buchanan, Kevin Jones, Gerald Komlofske, Doug Ng

Multinationals' interest and activity in Asian alliances has increased dramatically over the past few years, driven by the realization that in many industries Asia holds the greatest promise for growth. In many cases, multinationals have found alliances to be the necessary vehicle for market access.

The two critical challenges in Asian alliances, are the successful negotiation of the objectives and the initial implementation. Western companies focusing on building or reinforcing their positions in Asia are faced with potential partners whose goals may be quite different: for Asian partners, the alliances often represent opportunities to supplement their own capabilities. And the goals of the partners often vary greatly from country to country across the continent. This makes it absolutely imperative to understand the motivation and the cultural background under which the potential partner is operating.

Implementation in Asia provides unique challenges because this is precisely the point where the differing objectives between partners, if not clearly resolved in the negotiations, come to light. Western partners must continue to "keep their eye on the ball" to ensure that the alliance achieves their goals and remains competitive.

Agreeing on Objectives—Different Dreams

One key to agreeing on objectives with Asian partners is recognizing that their goals are driven in large part by the stage of economic development of their home country,
as well as by perceptions of strengths and weaknesses relative to Western countries.

China

Beyond all other factors, Chinese companies are seeking technology. They see technology as a design or a blueprint; they view its acquisition as a panacea for "catching up" with the industrialized world. Often, however, when they acquire technology they have a difficult time making it work. While China has many engineers highly skilled at understanding product technology, they have a more difficult time wrestling with process technology. That is because process depends on mastering and embedding potentially imprecise operating philosophies, rather than more precise technical specifications.

South Korea

Western companies often find a similar emphasis on technology in South Korea, but for different reasons. In many industry sectors, the chaebols have chosen not to be technology leaders, preferring to obtain the technology from elsewhere. The chaebols use their highly refined process skills to produce the products more cheaply and more quickly and in some cases with better quality than their rivals do. As a result, they
prefer alliances to take the form of technology licenses, which provide them a base technology on which they can later build. Samsung and LG have been masters of this strategy and are viewed as models by other chaebols.

Japan

Japanese firms generally believe that they have sufficient product and process technology. The challenges they face involve maintaining their competitiveness as they continue to expand their global reach. Issues such as high factor cost, local content restrictions and currency fluctuations need to be dealt with—and become increasingly complicated. Japanese firms have responded by placing greater emphasis on gaining access to global manufacturing and distribution networks. For many, alliances are the most practical and expedient way to gain network access.

Smooth Implementation—Pitfalls to Avoid

The biggest pitfall we have observed is that the key success factors and sometimes even the rationale for the alliance are often lost during the negotiation process because of the urgency to consummate a deal.

The emphasis on understanding partner motivations is important beyond the structuring of attractive terms that can prevail in the competition to form alliances. Such understanding is also important to ensure that the alliances are formed in such a way that the appropriate capabilities are built and that the Western partners' own interests are met. Among the examples we have encountered in different places are these:

China

The common lack of process capabilities in China means that the Western partner must ensure that such capabilities are built into the new entity. This is especially critical in the many cases where a joint venture is developed by absorbing an existing local operation. Building the process capabilities involves an honest assessment of the number of expatriate production engineers and supervisors required as well as the duration of their stay, adequate training — overseas if necessary — for local engineers and production workers, and phasing in different stages of operations. At one of our clients, the technology agreement specified that certain quality targets needed to be met before more sophisticated operations would be transferred to the new venture.

South Korea

Given the ability of many South Korean companies to take a basic technology, duplicate it and improve upon it, a critical issue for many Western firms is to maintain control over their technology. Western firms that have been lax in this aspect have found that they ended up contributing to the emergence of new competitors. Among the precautions often taken are limiting the transfer of critical components and design capability, restricting local access to technical documentation and excluding source code from the technology transfer.

Japan

The challenge in Japan is often to ensure that the venture agreement allows access of the Western firm to the Japanese market. In one venture negotiation where we assisted a client, the motivation of the Japanese partner was to create another worldwide node that would allow it to sell to Japanese auto transplants in the United States. While this was a rational economic move, our client had to ensure that it was provided opportunity for access to the Japan market. In addition, capabilities development had to include what would be required for successful competition in the domestic Japanese market.

In addition to differences in respective goals, other "pitfalls" — what we think of as "frictional" losses — can occur between Western and local partners. Negotiators often describe these "frictional losses" as communications problems with the potential partner: "Every point, even minor ones, seemed to take forever to discuss because we have different frames of reference," or, "I would never have guessed that was the driver behind the problem — too bad it took so long to figure out."

These inefficiencies are rooted in different definitions and perceptions regarding competitiveness. In less-devel-oped markets such as China, for example, the local partner may view relationships as a key to competitive success. Indeed, in some cases it may appear that a Chinese partner may want to do the deal for the deal's sake. After all, forming a joint venture may mean instant pay raises for all local employees and substantial living benefits for the local managers. The Western partner needs to identify such issues quickly and find ways to address them without damaging the ultimate competitiveness of the alliance; they need to find a way to negotiate a venture that has a rational economic structure.

In our experience, many Western firms start by placing heavy emphasis on understanding and bridging the local culture in order to reduce "frictional loss." They tend to undo this effort, however, when they limit expatriate terms of service — constantly rotating staff in and out of the venture. In one case where we assisted in the restructuring of a joint venture, we discovered that such rotations were the cause of local employees' unwillingness to embrace new concepts. They resisted taking on the task of breaking down existing organizational barriers, because they felt the Western partner would not be around long enough to protect them against potential retaliation.

Ten Success Factors for Doing Business in Asia

The Vision Thing: With 55 percent of the world's population, more than 20 percent of global G.D.P. and nine of the fastest-growing economies, Asia warrants corporate-level attention. Success in the region requires a clearly articulated top-down vision for the region that is consistent with broader corporate objectives. This vision should establish clearly where the firm intends to go in the region, why, and what level of resources will be committed to getting there.

Look Before You Leap: There is no "Asia Pacific." Asia is a diverse portfolio of countries in terms of culture, size, stage of economic development, as well as local "business system" and "style." Translating a global strategy into an Asia-Pacific strategy therefore requires significant planning, research, analysis and insight in order to prioritize where, when — and how — to enter.

Be a Farmer, Not a Hunter-Gatherer: One species of Chinese bamboo takes four years to sprout, then grows 90 feet in six months. Such is also the case with much of the corporate growth in Asia. Building a sustainable position in most Asian markets requires a network of in-country relationships with the business and the government communities. These relationships take time to nurture but once in place can enable rapid growth.

Know-Who vs. Know-How: Relationships are strategic assets of the corporation. Decision processes, decision-makers and key decision influencers are not always apparent to outside observers. They need to be identified, cultivated and managed as a critical resource and a source of competitive advantage.

Build a Capability to Manage Alliances: Influencing decision-making on major projects or gaining access to otherwise "closed" components of the business system (e.g., distribution) requires subtle relationship management at multiple levels. This may be beyond the ability even of empowered country managers, so temporary "gap filling" can be achieved, without forcing permanent partnerships, by a variety of well-managed alliances. "Best Practice" alliance-management capabilities—including creation, maintenance and dissolution—need to be planned for, and developed, in the region.

Promise Only What You Can Deliver, and Deliver What You Promise: The small number of decision-makers and influencers, and the close links among them, means that both good and bad news travels fast. Over-promising or under-delivering anywhere in the country or the region can adversely affect a firm's overall image and credibility.

Empower the People Closest to the Market: While the degree of "coordination" across the region needs to be carefully defined, as a general rule the complexity of each market and the importance of local relationships require significant empowerment of the country manager within a pre-agreed strategic framework.

You Never Know Who Can Play the Violin Until You Ask: Finding the right people is hard, so cast an internal net widely. Often there are hidden pockets of expertise within the firm, where an "old-timer" has a past affiliation with the region, plus the benefit of maturity and an intra-firm "old boy" network.

A Contract May Be Just the Beginning: Prepare for uncertainties and surprises. In such dynamic environments, there are often unexpected changes in the course of the negotiation or approval process. Don't take a "yes" to mean "yes"; a memorandum of understanding should not be viewed as the beginning of closing the deal but as an invitation to start a long, interesting and challenging journey.

Value the Ride as Well as the Destination: Inevitably, there will be frustrations along the way. The key is to remember that the journey itself is full of learning opportunities. This learning can help to refine a strategy and remembering the lessons can enable future alliances to proceed much more smoothly.

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