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WHEN BUILDING INTERNATIONAL JOINT VENTURES, SET-UP MATTERS

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JOINT VENTURES REMAIN POPULAR as a valuable approach to global business alliances, but with a distinctly new look. Previously, they were viewed primarily as a way to reduce risks or costs, or to expand into new markets. Today's international joint ventures often involve established and emerging market players—a combination of mature companies and start-ups—joining together to pool their distinctly unique capabilities and resources to create something truly innovative.

For example, SoftBank, Alibaba, and Foxconn announced in 2015 that they had created a joint venture that would combine their expertise in artificial intelligence, manufacturing, and e-commerce to produce and commercialize humanoid robots. Similarly, global automotive giant VW and Cymotive Technologies, an Israeli cybersecurity start-up, announced a joint venture the following year to develop data security solutions for the next generation of VW vehicles.

Joint ventures can provide a relatively agile model for partnering in an increasingly digital and dynamic world. BCG's dedicated joint venture team—spanning geographies and including BCG specialists, seasoned joint venture managers, and academics—conducts ongoing research in this important topic.

The Pitfalls Of International Joint Ventures

Make no mistake: Despite their popularity, joint ventures are not without risk. Their advantages can be offset by misaligned interests and business objectives, lack of commitment, unclear governance, problems with talent, and operational inefficiencies.

BCG's own research indicates that 19% of joint venture managers were dissatisfied with the value created, and 73% thought the venture could have been better.

International joint ventures can go off track in a number of ways. And while it is important for joint ventures to be carefully planned and managed at each stage of their life cycle, the initial set-up phase is the most important of all. While a sound set-up can't guarantee a joint venture's success, a poor set-up will inevitably lead to failure. Any issue overlooked during the initial design will certainly surface later on, possibly when it is already beyond repair.

In short, the set-up is the cornerstone of every successful joint venture. A successful set-up covers the fundamental design of the joint venture, aligns all partners from the outset, and ensures a functional organization throughout the partnership.

Bcg's Framework For Successful Joint Venture Set-Up

To help organizations address the critical questions that ought to be raised as each joint venture is designed, BCG has developed a detailed playbook that identifies the 13 essential building blocks for successful joint ventures. (See the exhibit, BCG's Playbok Takes A Comprehensive Approach to JV Set-up.") We can help multinational companies—and, in particular, those planning to partner with firms in emerging markets—to set-up strong joint ventures based on the careful design of each key element:

- **Business Strategy.** Align the fundamental business objectives and scope of the joint venture and define exit mechanisms
- **Governance.** Assign decision-making responsibilities and set-up decision-making processes; decide on the optimal size, roles, and composition for both the joint venture's board of directors and the board of management
- **Organization.** Address HR challenges and cultural differences typical in a joint venture; instill a distinct culture in the joint venture; determine how the joint venture will be organizationally linked to, and steered by, the parent companies
- **IP Protection.** Define the strategy for sharing IP and establish IP protection measures
- **Operational Control.** Agree on the collaboration model for various functions and define which assets and resources each party contributes.

EXHIBIT 1 | BCG's Playbook Takes a Comprehensive Approach to JV Set-UP

BUSINESS STRATEGY	1	Business objectives and scope
	2	Exit
GOVERNANCE	3	Decision making
	4	Board of directors set-up
	5	Management board set-up
ORGANIZATION	6	Human resources for the joint venture
	7	Culture of the joint venture
	8	Internal organization of the MNC
IP PROTECTION	9	IP protection
OPERATIONAL CONTROL	10	R&D
	11	Supply chain
	12	Production
	13	Sales & marketing

Source: BCG analysis.

Crafting each building block requires thoughtful consideration of alternative solutions. Here are a few examples of some of the most critical challenges companies face, and the kinds of solutions they've developed as they've set-up new international joint ventures.

Designing Governance

Without exception, executives designing new joint ventures must deal with core questions of governance: How will decisions be made? How large should the board of directors be, and how should it be composed? Which executive positions should make up the board of management, and how should they be filled?

Some of the most important decisions involve the management board. (See the exhibit, Management Board Options Can Range from Lean to Comprehensive.") Such decisions must be made within the context of the joint venture's envisioned degree of autonomy. And they must take into account whether the joint venture places greater priority on operational efficiency or on merging broad capabilities and local knowledge.

The particular circumstances of each joint venture, of course, will result in different challenges during the set-up period. For example, going into a 50-50 joint venture involving a large German car manufacturer and an Asian auto producer, the German partner was interested in a governance structure that would provide a leading position while maximizing the transfer of knowledge and skills between the two companies. The joint venture achieved these goals by:

- Designing a 9-member board of directors, on which 5 seats were filled by German executives and four by their Asian counterparts

- Creating a board of management on which the key positions of CEO, head of sales & marketing, and head of technology & manufacturing were held by German managers—while the HR and finance functions were led by their Asian counterparts

- Ensuring that middle management positions were staffed by German executives, while other management staff roles were filled predominantly by local employees.

Over the years, BCG has developed a rich database of organizational structures for

EXHIBIT 2 | Management Board Options Can Range from Lean to Comprehensive—Most Are Lean+

Size of management board	0–2	6	8
	Lean management board set-up	Lean+ management board set-up	Comprehensive management board
Description	GM/Chairman (CEO) and CFO JV's agenda fully driven by parent companies	GM/Chairman (CEO) and CFO and key functions Some operational autonomy from parent companies	Most to all functions represented High functional competence in management board as basis for autonomy
Transparency and control	●	◕	◔
Local market knowledge	◔	◕	●
Efficient operation	◔	●	◔

● Facilitates target dimension   ◕ ◔ Does not facilitate target dimension

Source: Expert interviews; BCG analysis.

joint ventures that encompass a variety of industries, geographies, and deal configurations. The database can provide great examples and a useful starting point for discussions about governance design.

Planning An Exit

Some joint ventures are designed to accomplish a specific task, in a specific context, and then end. Others, like marriages, are created for an unspecified time frame. Either case requires an exit strategy, and every partner in a joint venture should have one.

More specifically, companies need to define triggers for an exit, exit mechanisms, as well as a methodology for valuing the stakes when dissolving the venture. Situations that might trigger an exit could include change of control of a venture partner, material violation of an agreement, inability to operate, bankruptcy or insolvency of one of the partners, or a material change in the scope of the business. In other cases, an exit is initiated when the joint venture's task is fulfilled or the context changes. Different conditions might trigger a variety of exit mechanisms, ranging from options for one party to sell its stake or buy out its partner to simply dissolving the joint venture.

Consider the example of a pan-Asian telecommunication joint venture that was suffering from poor performance. The minority partner unsuccessfully sought an external buyer for its shares. However, thanks to the "put option" that was written into the joint venture exit strategy, the majority owner was obligated to buy those shares at a preset price. Without an explicit exit strategy, the minority partner could well have faced an unappetizing choice between sticking with a losing venture or simply eating its investment.

Protecting Ip

IP protection is emerging as another key topic in setting up international joint ventures. Both the benefits and risks associated with IP can be enormous because IP protections can literally decide a partnership's failure or success. Indeed, the risks can transcend the joint venture; there have been situations in which a company has stolen its partner's IP and then used it to compete globally against the partner's parent company.

Despite such significant risks, IP is often a cornerstone of the joint venture, and IP sharing is a common feature in the process. It is used variously to convince a partner to join the venture, to improve the value creation of the venture, or to commercialize the IP as an outcome of the venture. However, the vision for sharing IP must be accompanied by measures for protecting IP ownership throughout the life cycle of the joint venture.

IP protection was a major concern for a mature-market-based engineering company that set-up a joint venture in China to produce and commercialize power distribution products such as switchgears and transformers. The European partner transferred its core R&D know-how into a separate entity, in order to maintain full control of its valuable proprietary IP and to strictly limit the type of information being shared with the partner. At the same time, less-valuable IP at the application level—involving manufacturing, assembly and engineering know-how—was readily transferred to the joint venture to increase its efficiency. Additionally, some key components were imported from Europe or sourced from a separate joint venture in China, as a further protective measure.

The ultimate goal is to ensure that IP protection receives thorough consideration from the outset of the joint venture planning.

There's no doubt that companies stand to reap tremendous benefits from international joint ventures. The opportunities can be hugely attractive both for established companies and for new start-ups in emerging markets. But the potential for failure should not be underestimated. The best way to enhance the odds of success is to draw upon the experience of others to design a solid set-up.

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