Strategic alliances and joint ventures

As economies become more globalised, the use of strategic alliances and joint ventures is rapidly becoming popular with a growing number of companies.

What is a strategic alliance?

An international strategic alliance is an agreement between two or more firms from different countries to cooperate in any value-chain activity from R&D to sales.

Collaboration can allow organisations to partner with an existing business to share the risks and opportunities in a new market through:

- Technology transfer/knowledge sharing
- Purchasing and distribution agreements
- Marketing and promotional collaboration
- Joint product development

Each partner in an alliance usually retains their independence while contributing towards a mutual shared goal.

The creation of a strategic alliance may turn actual or potential competitors into partners working toward a common goal.

What is a joint venture?

A joint venture involves a potentially long-term investment of funds, facilities and resources by two or more companies in a partnership venture, which benefits all companies.

All involved will have an equity stake in the new venture.

A joint venture may be formed to:

- Run production facilities in another country
- Set up a marketing and distribution presence
- Use complementary technologies held by each participant.
- Access new markets and distribution networks
- Increase capacity
- Share risks and costs with a partner
- Access greater resources, including specialised staff, technology and finance
International partnerships

Forming a joint venture or strategic alliance in the international marketplace adds a number of challenges including differences in language, culture and business practices.

Other factors to consider include:

- Intellectual property rights
- Financial considerations
- Potential for political instability
- Impact of local law

Intellectual property rights (IPR)

IPR includes technology transfer as well as patent, trademark, and copyright protection. IPR is often transferred or shared in the context of an international joint venture.

Protection of patent, trademark, copyright, trade secrets and knowhow, as well as future modifications or improvements, should be dealt with in the venture agreements and protected under local law.

Financial considerations

- Exchange rates may fluctuate dramatically so you'll need to decide which form of currency is to be used in payments between companies
- Potential for varying rates of inflation in the countries involved and sources of loans
- Interest rates can be affected by financial instability
- Domestic and foreign tax regimes applicable to the venture could significantly impact earnings, both positively and negatively

Potential for political instability

Political or social unrest mean that prudent firms should consider insuring against insurable risks, foreign exchange hedging and how best to repatriate earnings.

Impact of local law

The difference in legal tradition and rules between common law countries (such as the UK) and civil law systems (such as those of most of the members of the European Union) can give rise to real difficulties.

Legal points to consider include:

- Creation of a formal entity for the venture is often necessary or desirable, the subsequent entity being subject to local law
- It may be necessary to apply for permission to establish such a venture
- Employment laws may strongly favour employees with the result that termination of employees and/or distributors can be a difficult and expensive process
- Environmental laws and regulations must be reviewed in advance since permits are often required, while the consequences of violation can be disastrous
- Antitrust or competition laws and regulations may require attention
Why consider a strategic alliance or joint venture?

The decision to form a strategic alliance depends on the objectives of the companies involved and on the laws of the countries in which they are doing business.

The ideal partnership takes advantage of your core expertise while strengthening weaker areas of your business.

Well chosen partnerships can provide advantages such as:

- **Sharing the risks** – working in partnership allows you to offset your market exposure. A strategic alliance will probably work best if the firms involved complement but do not compete directly with each other.
- **Shared knowledge** – when partners contribute skills, brands, market knowledge and assets, there is a synergistic effect. The result is a set of resources that is more valuable than if the firms had kept them separate.
- **Opportunities for growth** – access to your partner’s distribution networks while taking advantage of a favourable brand image may help you gain market share faster than if you go it alone.
- **Focus on your core strengths** – a good partner will offer complementary strengths which can free you up to focus on the areas your business does best. For example, you can focus on product development while your partner focuses on sales and marketing.
- **Access resources** – your partner may be able to help by giving you access to resources (such as specialist staff, finance and technology) which, in turn, can help firms produce more efficiently or at a higher quality.
- **Access the target market** – working with a local partner may be the only way you can access your target market, particularly in developing countries aiming to avoid being exploited for their resources.
- **Economies of scale** – achieved when two or more firms pool their resources, co-operative strategies also allow small companies to join together to compete against larger competitors.

Ways to lower joint venture risks

International partnering with another business can be complex as it takes time and effort to build the right relationship.

- **Set clear objectives are unclear** – Ensure the objectives of the venture are totally clear and communicated to everyone involved. A venture will not succeed if the objectives are in conflict, however the objectives do not need to be identical.
- **Set mutual objectives** – If partners have different objectives for the joint venture and, as profits will be split between partners, it may take longer to make a return on your investment.
- **Find balance** – for example, in the levels of expertise, investment or assets brought into the venture. To make the partnership work requires a high level of commitment both in terms of finance and management time while, if the relationship breaks down, ownership of IP and jointly developed products can be an issue.
- **Ensure smooth integration of work practices** – Working with an overseas company can result in poor integration and co-ordination due to cultural issues and different ways of doing business.
- **Provide sufficient leadership and support early on** – Partners need to provide sufficient leadership and support in the early stages, particularly if you’re partnering with a larger company where you can be pressured into going in the direction the larger partner wants to take.
- **Mutual trust and commitment is not agreed** – Participants fail to build mutual trust and commitment.
Selecting a partner

After the decision is made to enter into a partnership arrangement, your business will need to consider factors relating to management structure and the law.

Management structure

Management structures used by companies for their joint ventures and strategic alliances fall into five broad types:

- **Dominant parent** – generally the majority owner of a joint venture, in cases where there is no majority owner, the dominant parent may be the company that contributes the most valuable resources
- **Shared management** – an equal number of managers from each company (board of directors, top management, and functional management) assume controlling positions but this requires a high degree of cooperation
- **Split-control management** – one company may hold most (or all) positions due to differences in expertise or because one firm may not want to share its knowledge or technology
- **Independent management** – found when the partners do not get involved in day-to-day operations but hire executives to run the joint venture instead
- **Rotating management** – key positions rotate between firms with each partner assigning a person for a period of time

Legal requirements

A joint venture or strategic alliance will need to change with circumstances. Agreements should anticipate these changes and provide a method for change, termination and dispute resolution.

Once a partner is selected, generally a Memorandum of Understanding (MoU) or a Letter of Intent is signed by the parties (after consulting lawyers well versed in international laws and multi-jurisdictional procedures) highlighting the basis of the future joint venture agreement.

Before signing the joint venture agreement, however, the terms should be thoroughly discussed and negotiated to avoid any misunderstanding at a later stage. Negotiations require an understanding of the cultural and legal background of both parties.

The three basic legal structures are:

- **Limited liability company** – a legal entity established to carry out a common activity. In this case, the cooperation of the parties requires further legal instruments, usually articles of incorporation of the company, by-laws and a shareholders’ agreement.

The advantages of establishing a legal entity include:

- A company is a universally recognised medium and gives a strong identity for dealings with third parties
- It allows for a management and employee structure to be put in place
- The participants have the benefit of a limited liability and the flexibility to raise finance
- The company will survive as the same entity despite a change in its share ownership

- **Co-operation agreement** – a legal entity is not created but a collaborative group exists. This type of agreement is suitable where the parties wish to avoid the formality and permanence of a corporate vehicle.

Although no legal entity exists it is still possible for the partners to be exposed to claims and liabilities because of the activities of their co-participants.
Therefore, an indemnity should be included in the agreement under which one party will indemnify the other for any losses that are caused through the actions of the co-participants.

Limited liability partnership – effectively a “hybrid” arrangement which can include characteristics from either of the categories above

**Documentation required**

Joint venture transactions call for clear, well drafted documentation. The provisions of these documents will vary from case to case but should, at the very least, cover:

<table>
<thead>
<tr>
<th>Joint venture/shareholders’ agreement</th>
<th>Memorandum and articles of association</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Object and scope of the joint venture</td>
<td>• The rights to appoint and remove directors; quorum provisions at both director and shareholder level</td>
</tr>
<tr>
<td>• Capitalisation/financing of the company</td>
<td>• Procedures for shareholders’ meetings</td>
</tr>
<tr>
<td>• Composition of the board and management arrangements</td>
<td>• Pre-emption provisions on share issues</td>
</tr>
<tr>
<td>• Provisions for distribution of profits</td>
<td>• Possibly pre-emption provisions on the transfer of shares</td>
</tr>
<tr>
<td>• Transferability of shares in different circumstances</td>
<td>• Division of shares into separate classes to which the parties’ respective rights can attach</td>
</tr>
<tr>
<td>• Provision for protecting minority shareholders</td>
<td>• Chairman’s casting vote (or its exclusion)</td>
</tr>
<tr>
<td>• Provisions for remedying a deadlock</td>
<td>• Appointment of alternative directors, flexible provisions for resolution by agreement and notices</td>
</tr>
<tr>
<td>• Provisions relating to termination</td>
<td>• Restrictive covenants on the company and the participants</td>
</tr>
<tr>
<td>• Restrictive covenants on the company and the participants</td>
<td></td>
</tr>
</tbody>
</table>

**Making the partnership work**

There are some simple steps that can reduce the potential of your partnership running into problems:

- Make sure you take time to research and evaluate any potential partner. Check to see if their goals and values align with your own business.
- Develop a personal rapport between yourself and the other party. Make sure you get to know and understand your potential partner.
- Ensure a management voice for all partners on the direction of the partnership. Make sure communication channels are kept open.
- Decide on reporting methods, milestones and goals for the partnership. Agree in advance how the partnership will proceed if these goals are not being met.
- Agree in advance on what arbitration methods you will use if there is a dispute between the partners.
Joint venture planning checklist

A checklist can be useful when you are planning a joint venture covering areas such as:

- Whether your business is prepared
- Choosing the right partner
- Finance
- Steps to implement the joint venture
- Legal models
- Bank accounts
- Sourcing business together
- Terminating the joint venture

Getting advice

Overseas partnerships can be complicated and potentially costly if things go wrong. Make sure you secure the necessary advice before entering into any partnership arrangement.

Research your markets

Our overseas market support is delivered in partnership with UK Trade & Investment (UKTI) to provide a deep analysis of international opportunities and routes to market. Services include:

- **UKTI’s Overseas Market Introduction Service (OMIS)** – a highly tailored package that uses their network of international employees to provide a localised snapshot of opportunities
- **UKTI’s Export Marketing Research Scheme (EMRS)** – helps you carry out export marketing research on all the major aspects of any export venture

More about SDI’s overseas market support and how to apply:

[http://www.sdi.co.uk/export-from-scotland/services/overseas-market-support.aspx](http://www.sdi.co.uk/export-from-scotland/services/overseas-market-support.aspx)

Preparing for international growth

Learn how to overcome more complex business challenges to prepare for global investment and expansion.

Enrol on our Preparing to Export programme – a one to four month service that helps companies plan for international trade or develop existing export markets.

Our Advanced level programme covers six to eight of the following topics:

- Finance and international value pricing
- Distribution channels and contracts
- E-Business
- International sales skills
- International communication/marketing skills
- Getting the best out of exhibitions and missions
- Licensing/franchising deals
- Strategic alliances/joint ventures
- Acquisitions
- Managing overseas operations
- Presenting an international market development plan
More about our how to enrol on our Preparing to Export programme:

http://www.sdi.co.uk/export-from-scotland/trade-and-export-guide/build-your-export-skills/how-to-prepare.aspx

Plan your trade and export strategy

With our support we can provide you with the focus and drive needed to make your company an effective player on the world stage. Over 100 Scottish businesses have already benefited from our support in developing their export and trade strategy.

What are the benefits?

- Expert guidance and support to achieve best practice
- Networking opportunities, both at home and abroad
- Global knowledge base supported by the latest technology
- On-going support with implementation of your strategy

Join our export strategy workshops to take your senior management team through strategy sessions that help identify opportunities, anticipate risks and plan for international trade.

Our series of workshops are delivered over one month and include a planning session, a full day with the management team and a follow up meeting.

More information on how to join an export strategy workshop:

www.sdi.co.uk/export-from-scotland/services/Export-and-trade-strategy-workshop.aspx

Our advanced international strategy development programme provides consultancy support to find and test best routes to international trade. It builds a core management team with export experience to take the business through initial trade stages and further growth plans.

Find out more about the benefits of our advanced international strategy development programme:

http://www.sdi.co.uk/export-from-scotland/services/Strategy-development-training.aspx

Mentoring and HR support

We can assist in finding and training an export manager to add to your workforce and help realise your exporting plans.

Find out if your company is eligible for funding for an export manager to support your export strategy:

http://www.sdi.co.uk/export-from-scotland/services/Funding-for-an-export-manager.aspx

Enterprise Europe Scotland (EES) is your local gateway for help on doing business, finding collaborative partners and raising your competitiveness in Europe.

EES can help you find a variety of business and academic partners, linking demand with supply of innovation across Europe, whether it’s for distribution of products, licensing a technology, manufacturing or joint venture.

We can work with you to define your needs, proactively look for suitable partners, qualify potential leads and support the negotiation process.
Learn more about European business opportunities:

http://www.sdi.co.uk/export-from-scotland/services/European-business-opportunities.aspx

International trade legislation and documentation

For further information on international trade regulations, customs procedures, export licences, transportation documentation and tax go to the Business Gateway website:

http://www.business.scotland.gov.uk

Read our guide for an overview on how to manage intellectual property, licensing and franchising:


Negotiating an agreement

Seek legal advice from lawyers specialising in international contract law. Look for a firm with experience in the country you are looking at doing business.

Note: This guide is provided to give an overview of the principal areas when considering joint ventures. Always seek detailed legal advice.

Contact us

For more information or to speak with our Smart Exporter advisers call 0800 019 1953 or email enquiries@smartexporter.co.uk