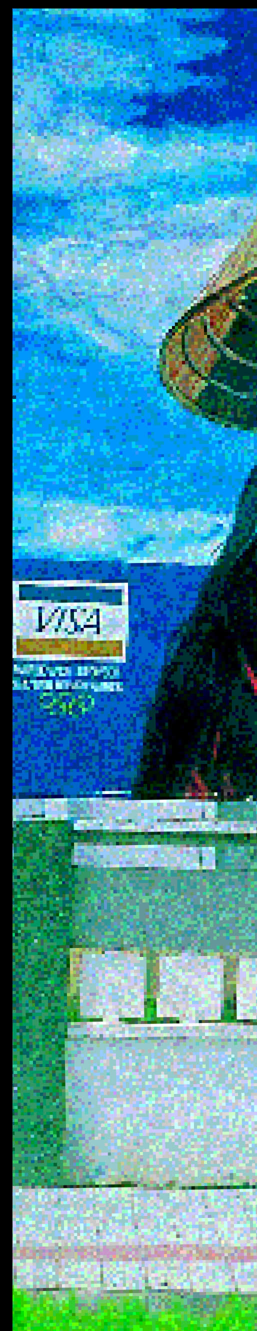
EMERGING MARKET ALLIANCES: MUST THEY BE WIN-LOSE?



"Marry in haste, repent at leisure"

Both sides, global and local, need to understand how power could shift

Managing partner differences

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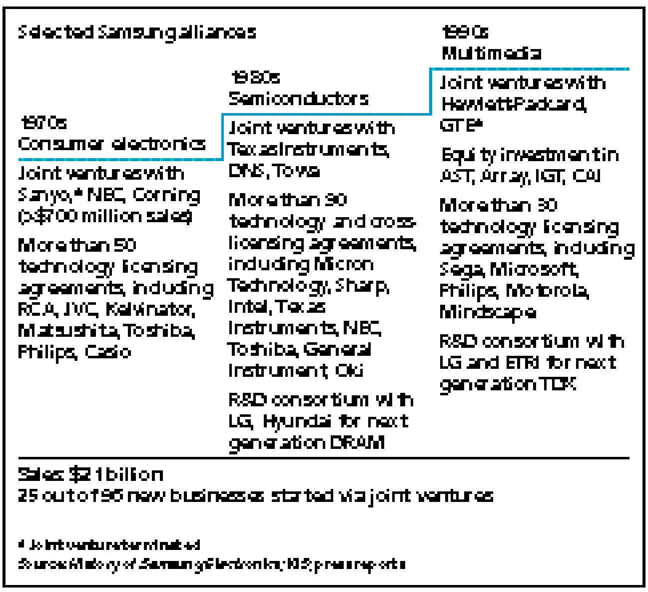
GLOBAL COMPANIES ARE LOOKING to emerging markets for growth. Companies in emerging markets are looking for ways into the burgeoning global economy. Alliances can seem the obvious solution for both sides.

For global companies, limitations on foreign ownership make an alliance the only route into some markets. In other markets, alliances provide an appealing way to accelerate entry and reduce the risks and costs of going it alone. The US company Aetna Insurance, for example, recently announced a joint venture with Sul América Seguros, Brazil's largest insurance company. Aetna is reportedly investing $300 million, with a possible $90 million more to follow, for a 49 percent stake in the joint venture. The aim of the Brazilian-based alliance is to accelerate growth and introduce new products in health, life, and personal insurance and pensions. Aetna contributes expertise in products, information technology, and servicing, while Sul América brings local knowledge, an extensive distribution network and sales system, and its leading market position.

Exhibit 1

Allying for technology and skills



Companies in emerging markets can find the idea of an alliance equally attractive. For those in a position of strength, it can be a powerful vehicle for growth, or a way to leverage low-cost manufacturing or a unique distribution network. Samsung of Korea has used several hundred technology licensing arrangements and joint ventures as vehicles to build a world-class electronics company (Exhibit 1). Of almost 100 new businesses it set up between 1953 and 1995, a quarter were initiated via joint ventures. For other local companies in emerging markets, alliances may appear to be the only way – short of selling the company outright – to survive once the home market has opened to new entrants bringing global brands or technology.

Given this pattern of mutual benefit, it is not surprising that alliances account for at least half of market entries into Latin America, Asia, and Eastern Europe (Exhibit 2). Some are successful. Nintendo and JVC both have alliances with Gradiente, Brazil's leading electronics company, to manufacture and/or market products under their own brand names as well as under the Gradiente brand. The alliances have helped Nintendo and JVC

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FACTORS DRIVING ALLIANCE RESTRUCTURING

A wave of alliance restructuring is just beginning to ripple through emerging markets, and is likely to persist. It is driven by five principal factors.

First, the expansion of free trade zones such as Mercosur and the Andean Pact promotes a regional approach to business, undermining national joint ventures. One alliance producing auto parts in Latin America, for example, has been restructured to cover a broader geographic region, with the aim of achieving scale economies.

Meanwhile, a consumer products company in China has rationalized several regional joint ventures in order to implement a national distribution strategy. This type of restructuring will be most pronounced where multinationals have invested in subscale manufacturing after being lured by hopes of privileged treatment and tariff protection.

Second, consolidation between local companies can lead to a situation in which two multinationals find themselves in partnership with the same local company, or *vice versa.* After a series of mergers within China, one local company is now in joint ventures with no fewer than five head-to-head global competitors. Similarly, mergers and global alliances between multinationals can expose joint ventures with two competing local partners in an emerging market.

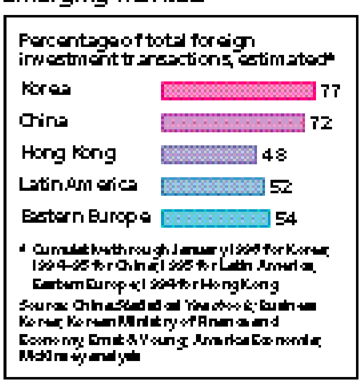
Third, many multinationals have overestimated their partners' strength and now want to increase control. Fourth, as emerging markets become more important, global concerns are reevaluating their historic licensing and distribution alliances and considering how to expand (or break) these relationships. And finally, many family-owned businesses are reviewing their portfolios and seeking to restructure alliances in order to divest or to improve performance.

build volume rapidly in an important market, while Gradiente has become a profitable company with revenues of over $1 billion and its own skills, market position, and manufacturing capacity.

Yet the popularity of alliances between emerging market and global companies, and their apparent "win–win" character, can mask their difficulty. They are hard to pull off and often highly unstable – much more so than alliances between companies from similar economic and cultural backgrounds. Many have failed to meet expectations or have required extensive restructuring. Indeed, in recent years, numerous high-profile joint ventures in Asia and Latin America have been dissolved, restructured, or bought out by one of the partners.

Exhibit 2

Importance of alliances in emerging markets



Why are joint ventures in emerging markets proving so difficult? The answer lies in the fact that multinationals and companies in emerging markets must overcome formidable differences if they are to develop successful alliances.

First, most global companies are considerably larger than their emerging market partners, and possess deeper pockets and, often, broader capabilities. This makes it hard to find equal, complementary pairings – a balance that is the hallmark of successful and enduring alliances. Our research indicates that among alliances undertaken in India, the global company typically has 30 times the revenue of its local partner. One case makes the implications clear. A multibillion-dollar worldwide leader in the consumer non-durables industry and a $70 million Indian company enjoyed a successful joint venture that trebled its market share in four years and became the third-largest competitor in its industry. But the global partner then wanted to add capacity and make India a regional supply source for Asia and Africa. The local partner's share of the necessary investment, about $17 million, represented almost a quarter of its annual turnover. When it declined to invest, the global partner ended up buying out the venture.

Other differences result from ownership structure, objectives, culture, and management styles. State-owned enterprises can make frustrating negotiating partners for multinationals because they have no single decision maker; instead, they have to seek approval from a range of political constituencies. But a multinational can be an equally frustrating partner for a family-owned business if its country manager has to seek approval for decisions from other senior managers, while the patriarch or matriarch of the family business can make decisions unilaterally. Different types of company also have different agendas. The family-run business may be more interested in ensuring a steady stream of dividends for shareholders than in maximizing growth or short-term shareholder value.

A reasonable (but rarely asked) question is: "Why are we forming an alliance in the first place?"

These challenges do not mean that emerging market alliances should be avoided. But they do raise the stakes. Before entering these deals, therefore, prospective partners should ask three questions. Is an alliance really necessary, or would an outright acquisition, direct investment, or contractual relationship suffice? How sustainable will an alliance be, given the partners' ambitions and strengths? And how should the strategy and tactics they adopt reflect the distinct challenges of alliances between global and emerging market companies?

Is an alliance really necessary?

Given the differences between partners and the complexities of managing a relationship, a reasonable (but rarely asked) question is: "Why are we forming an alliance in the first place?" If the main benefit of an alliance would be inside knowledge of customers, government, and suppliers, for example, the global company should ask whether it might be possible instead to hire five or ten key people who would bring those relationships.

In China and India, acquisitions and direct investments by overseas companies have increased, although alliances are still the main vehicle foreign companies use to enter the market. The proportion of wholly foreign-owned enterprises in China rose from less than 10 percent of incoming investment in 1991 to more than 30 percent in 1995.* In India, the figure grew from 5 percent in 1992 to 25 percent in 1995. Many global companies have operated as wholly owned entities in Latin America for decades.

Acquisitions can be equally effective for emerging market companies. Many companies have responded to globalization by looking to joint ventures or broad-based technology licensing arrangements with international partners, particularly when they needed to bridge a technology gap. But India's Piramal group, for example, has expanded its pharmaceuticals business at a compound annual growth rate of almost 60 percent since 1988, largely by acquiring other local pharma companies that already have non-equity licensing arrangements with global concerns.

Achieving an equal balance in an emerging market is challenging because of differences in size, culture, skills, and objectives

Other emerging market companies are experimenting with "virtual" alliances – piecing together the technology or abilities they seek without forming an alliance. One large Indian textile manufacturer aspired to enter the clothing business, but lacked manufacturing technology and marketing expertise. Rather than form an alliance, it cobbled together what it needed by hiring experienced people, persuading the equipment manufacturers to serve as technical consultants, and licensing certain technologies. Since embarking on the program four years ago, the company has grown by 150 percent. Such a strategy would not suit all companies, however; the learning and coordination of relationships it involves call for highly developed skills and consume a great deal of management time.

These alternative approaches are especially relevant when technology is readily available and global brands are not needed. Cheap, double-edged razor blades based on a common technology continue to take 83 percent of the Indian market, for example, despite the introduction of high-quality blades by Gillette in 1993.

Will the alliance last?

When an alliance *is* deemed necessary, both companies should assess at the outset how the partnership will evolve – whether it is a marriage of equals

* "Multinationals in China: Going it alone," *The Economist,* April 19, 1997.

HOW ALLIANCES EVOLVE

Alliances tend to follow the pattern set by the deregulation of an industry and the opening of national markets. As regulations change, so do the options available to multinationals and local companies, with the result that alliance structures established under one set of rules can quickly become obsolete under another. Pressure to restructure or dissolve partnerships may ensue.

Emerging markets typically go through four evolutionary stages: nascent, frenzied, turbulent, and mature (*see* exhibit). In the **nascent** phase, strict regulation and lack of market transparency limit alliance activity to non-equity technology licensing and distribution arrangements. When the deregulation of an industry or a country gets under way, it can trigger an alliance **frenzy** as global companies seek to gain access to a new market, influence government policy, or build a portfolio of options, and local players attempt to acquire world-class skills. Many alliances formed in this stage are created to comply with local ownership provisions.

Further deregulation, and multinationals' growing familiarity with the local environment, lead next to a period of **turbulence.** This is characterized by the restructuring and dissolution of alliances as alternatives become available. Foreign partners can now decide to go it alone or increase their ownership stakes. As the market for corporate control develops, merger and acquisition activity commences.

When regulations unravel, those alliance structures driven by regulation rather than business economics become especially fragile. Until 1992, for example, India's Foreign Exchange Relations Act prohibited non-Indians from holding a stake greater than 40 percent in any Indian company. Since liberalization, this limit has been eliminated or raised to 51 percent in most industries. The result is that existing shareholder agreements are coming under strain as foreign partners attempt to increase their holdings.

The risk of conflict deepens if a multinational launches a wholly owned subsidiary that competes with its partly owned subsidiary. Questions then arise over where the parent company will want to launch its new products and focus its investment. The potential for trouble is obvious.

Eventually, as the market stabilizes, the **mature** stage is reached. At this point, the environment starts to resemble that of developed markets, in which alliance structures are driven primarily by business logic.

that will endure, or something else. Achieving an equal balance in an emerging market is particularly challenging because of the differences in size, culture, skills, and objectives that we have mentioned. Such alliances are also vulnerable to rapid regulatory change (*see* text panel, "How alliances evolve").

Two factors influence the sustainability and likely direction of an alliance: each partner's aspirations – that is, the will to control the venture – and relative contributions. Aspirations can tip the balance. Does the global partner desire full control in the long run? (If it does, the alliance is likely to wind up in acquisition or dissolution.) Or does it want a permanent alliance in which the local partner provides specific elements of the business system, as with Caterpillar's long-standing relationships with its local distribution and service partners? Is the emerging market player's focus on the home market, or does it harbor global ambitions? If it does, and it wants to compete on its own against the multinational, conflict will be inevitable.

Four stages of market evolution

	Nascent	Frenzied	Turbulent	Mature
Market structure				
Regulations	Minimal regulatory freedom • Strict controls on ownership/capital repatriation • Strict regulatory oversight	Regulations relaxed • Near majority or majority foreign stake allowed • Operating restrictions still exist (eg, bureaucratic approvals)	Regulations liberalized • Fully-owned subsidiaries allowed • Operating controls eased • Market for corporate control emerges	Market deregulated • Free equity and capital flows • Operating freedom • Active market for corporate control • Shareholder orientation
Transparency	Unfamiliar to outsiders "Outpost" mentality	Many global players present Few can replicate locals' market knowledge and government relationships	Many global players present Many global players have "insider" knowledge	Market integrated with global markets
Alliance focus				
Global players	Market skimming • Limited involvement • Technology licensing/distribution agreements	Market access • Build options • Understand local market • Influence government	Market growth • Prune options • Invest in winners	Market integration • Optimize global business system (eg, by outsourcing) • Improve performance • New opportunities
Local players	Local game, local players	Upgrade capabilities • Products • Technology • Capital Provide "escort" service	Survival of fittest • Restructuring • Players without long-term advantage forced to exit • Strong locals go it alone	Genuine alliances • New markets • New products
Characteristics of alliance environment	Low-profile, non-equity-based collaborations	Rapid formation of many joint ventures	Dissolution of joint ventures; emergence of cross-border M&A, fully-owned subsidiaries	Full set of vehicles exist
Examples	Brazil (telecom)	China	India	Brazil (retail banking)

Ultimately, though, the evolution of an alliance will be driven by each partner's strengths and weaknesses, and by the relative importance of its contribution. Examples of valuable contributions might include privileged assets (ownership of mining rights or oilfield reserves, for example); advantaged relationships such as access to regulators, operating licences, and exclusive distributor relationships; or intangible assets such as brands, marketing, manufacturing, technology, management expertise, and patents.

Usually, the global company contributes intangibles, such as technology, brands, and skills, that grow in importance over time. The local partner's contributions, on the other hand, are more likely to be local market knowledge, relationships with regulators, distribution, and possibly manufacturing – assets that may fade in importance as its partner becomes more knowledgeable about the market, or as deregulation undermines (sometimes overnight) the value of privileged relationships or licences.

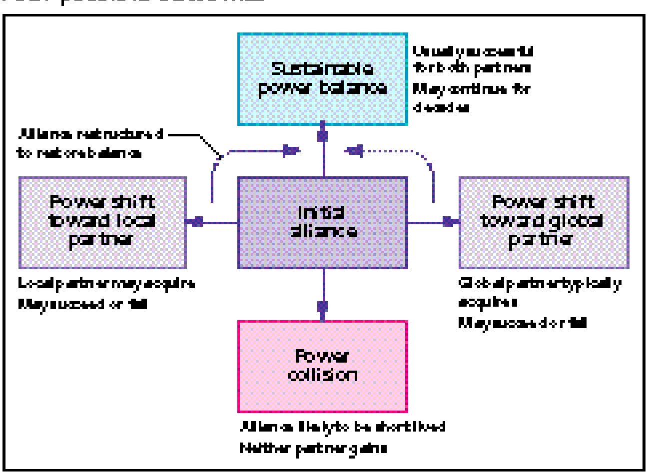
Exhibit 3

Assessing bargaining power

Determining factors	Importance of factor: High	Importance of factor: Low	Balance of power, Now: Us	Balance of power, Now: Partner	Balance of power, Future: Us	Balance of power, Future: Partner
Product or process technology						
Brand ownership						
Channel control						
Manufacturing capacity						
Ability to invest in the business						
Local relationships (eg, regulators)						
Global relationships (eg, global suppliers, global customers)						
Management control						

Exhibit 4

Four possible outcomes



Manufacturing cost leadership can also be fleeting in a globalizing economy. If the local partner essentially provides an "escort" service, it will almost certainly become less important. A survey of Chinese joint ventures indicated that Chinese partners systematically deliver less value than expected in terms of sales, distribution, and local relationships.*

To assess whether an alliance will be a marriage for life and how it will evolve, partners in emerging markets should catalog the current contributions of each partner, plot how they are likely to shift (Exhibit 3), and negotiate to ensure that the venture will be sustainable or to protect shareholders against a likely shift in power.

Four paths

Emerging market alliances tend to evolve along one of four paths (Exhibit 4). The first is that trod by **successful long-term alliances** such as Samsung-Corning, established in 1973 as a 50–50 joint venture to make CRT (cathode-ray tube) glass for the Korean electronics market. Samsung needed a technology partner to pursue its strategy of integrating vertically into electronics components and materials; Corning wanted to expand in Asia. The joint venture had about 20 percent of the global market, revenue of $695 million, and net income of $49 million in 1996, with investments in Malaysia, India, China, and eastern Germany. Heineken and Anheuser-Busch also have a number of successful alliances with brewers in emerging markets, in which the local partner continues to produce and sell its local brand for the mass market, while producing or importing and selling the global partner's brew as a premium brand.

* *See* Stephen M. Shaw and Johannes Meier, "'Second generation' MNCs in China," *The McKinsey Quarterly,* 1993 Number 4, pp. 3–16.

The second path involves a **power shift toward the global partner, often followed by a buyout.** Take the case of two consumer goods companies that formed an alliance to target the Indian toiletries market. At the outset, their contributions were balanced. The global company brought international marketing experience, world-class management systems, and additional volume to fill local manufacturing capacity. The local company brought the technology to make soap from vegetable fat (the use of animal tallow is banned in India), low-cost manufacturing, local market knowledge, and established products and brands. The global company wanted access to an enormous and potentially lucrative market; the Indian company aimed to increase its capacity utilization and enhance management and marketing skills and systems.

Gradually, however, the balance of power shifted. The global partner succeeded in getting an organization up and running and gained local acceptance for its product, whereas the Indian company was prevented from filling its capacity by slower than expected sales. Moreover, the expected transfer of skills and systems to the Indian partner never materialized, while its own brands, which had been transferred to the joint venture, suffered. The alliance was dissolved by mutual consent in 1996.

The way an alliance is structured and managed can determine its outcome. In one 50–50 joint venture, an emerging market company brought important relationships, brands, and distribution skills that might have led to a sustainable alliance had the venture been structured differently. But the global partner enhanced its own bargaining position by placing its people in key positions in marketing, manufacturing, and finance; introduced its own products and brands; built the manufacturing plant; and imposed its systems and culture on day-to-day operations. The venture reportedly lost money for several years until it was bought out by the global partner, whereupon performance improved. Notwithstanding this outcome, the emerging market partner may have rated the exercise a success, since it sold its 50 percent stake at a premium.

> Local partners do sometimes build their bargaining muscle, increase their ownership stake, and buy out their global partners

The third path sees a **shift of power toward the emerging market partner.** Local partners do sometimes build their bargaining muscle, increase their ownership stake, buy out their global partners, or exit the alliance to form other partnerships. Sindo-Ricoh illustrates how a power shift toward a local partner can lead to the restructuring and continued success of an alliance. Sindo has been Ricoh's exclusive distributor in Korea since 1962. It built low-cost manufacturing capability, expanded the relationship to a 50–50 joint venture, then took majority ownership with a 75 percent stake. In 1996, it boasted sales of $309 million and net income of $38 million.

The fourth path is **competition between partners, followed by dissolution or acquisition of the venture by one of them.** A 50–50 joint venture between GM and Daewoo to manufacture cars in Korea lost money until Daewoo acquired it outright. The partners had incompatible strategies: GM wanted a low-cost source for a limited range of small cars; Daewoo aspired to become a broad-line global auto manufacturer. Conflict and collision often result when the partners fail to agree on whether the joint venture or the parent companies will compete in related product areas or in other countries.

Finally, although alliances are often likened to marriage, a successful alliance does not *have* to last. Success is measured not by duration, but by whether objectives have been met. Take the joint venture between GE and Apar to make light bulbs for the Indian market. The arrangement was dissolved after only three years, yet GE emerged from it a leader in the Indian lighting industry, and Apar was handsomely remunerated.

Recognizing what path an alliance is following and how its balance of power is shifting is critical to ensuring that both partners have the opportunity to satisfy their objectives. Our research in Asia and Latin America – and a growing body of experience – identifies some practical steps that companies can take to address the challenges of emerging market alliances.

Alliance strategies and tactics for emerging market companies

Companies in emerging markets must recognize that they may be vulnerable over the long term because of inherent power imbalances. Indeed, our research suggests that global partners are more likely to wind up with control when the balance of power shifts. On the other hand, emerging market partners may possess sources of value that cannot easily be replicated in the short term, such as customers, channel control, local brands, control over key supply sources, manufacturing capacity, and relationships with government officials and regulators. They should make the most of these bargaining assets. Above all, they should invest to ensure that they last.

Before a company can develop a strategy to build power, it must set objectives for the alliance that reflect its aspirations and a hard-nosed assessment of its own strengths. Is its goal to become a world-class operator able to compete in some areas with global companies on their own turf? Is it to develop a sustainable home-market alliance based on an enduring source of strength? Or is the alliance a defensive measure to protect the business against threats from global brands or technology? And is it acceptable – or even inevitable – that the alliance will evolve toward a sale?

When the aim is to develop a genuine alliance or build a platform for growth, strategies to maximize power include:

Invest today to build power for tomorrow. The most critical issue for local companies is how to establish a sustainable source of value and thus maintain the balance of power. There are a number of ways to do this:

Develop your own brands. Recent experience suggests that local brands can be more powerful than their owners tend to believe. In Brazil, electronics producer Gradiente has laid the foundation for more balanced partnerships by building name recognition and sales volume that match those of global brands. A Venezuelan building products manufacturer entering a joint venture with a global partner retained its own brands in several segments in which global technology was not required, and where craftsmen trusted the local product.

Control distribution. Distribution is an area in which emerging market companies typically have initial advantages that can be extended to enhance their bargaining power. One industrial equipment manufacturer in Latin America increased its influence over distributors – and its clout with its global partner – by offering inventory management systems, financing, and extensive technical support. Investing to keep the advantage is crucial. Rallis, an Indian agrichemicals company, owns the country's leading nationwide agricultural inputs distribution system and has distribution agreements with several global chemical companies. But though it may command the dominant dealer relationships today, new market entrants are beginning to go directly to the farmer. If direct distribution should take hold, what will happen to Rallis's power? Perhaps anticipating this, the company is itself experimenting with direct distribution.

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Secure proprietary assets. Most industry value chains in emerging economies have "chokehold" points – privileged assets in short supply. Locking these in can establish a continuing source of value. Indian Hotels owns the best properties near all the country's main tourist destinations, for example. And one metals company in Brazil entered a long-term arrangement with a key supplier for a crucial input that was in short supply.

Preemptively acquire local competitors. Provided that these acquisitions make sense in their own right, they can strengthen a local company's negotiating hand by limiting the entry options for would-be players.

Become a regional hub for your partner. Many multinationals have their hands full exploring the larger emerging markets such as China and Brazil. Few have the time and management capacity to concentrate on smaller but still important economies such as Chile or Peru. Local partners can improve their market position and their long-term stature in a partnership by becoming a regional hub. One Indian engineering consumables company expanded its joint venture with a European manufacturer to distribute products throughout Asia. Similarly, a Colombian industrial concern acquired its counterpart in Peru and is expanding in Venezuela, thereby not only increasing the contribution it makes to its alliance with a European company but also strengthening its own position by attaining economies of scale in regional distribution.

Autonomous ventures – or, worse still, ventures in which a local partner calls the shots – can be anathema to truly global players

Think twice before allying with a global leader. Global market leaders are often the most obvious partners because of their products, skills, capital, and prestige. But they usually have global aspirations too, and may well seek to tighten their control over any alliance they undertake in order to optimize purchasing, pricing, product development, manufacturing, and brand strategy. Autonomous ventures – or, worse still, ventures in which a local partner calls the shots – can be anathema to truly global players. In the words of one chemical industry executive, "How can we serve our global customers in the same way across 20 or more countries when our partner operates the business? We can't even assure our customers that they can buy the same products with the same specifications from one country to the next."

Emerging market companies should ascertain whether a prospective partner is pursuing a "global" strategy – same brands, centralized decision making, global purchasing, unified R&D, consistent product portfolio and pricing – or a "global/local" strategy with, for instance, local and global brands, strong country or regional managers, and regional product development.

Considering alternative partners is especially important if the leading global players in an industry are inclined to swallow up local partners' stakes. A pattern has emerged in the behavior of one global consumer goods company in key emerging economies in Latin America and Asia. It enters a market by allying with a leading local consumer goods company; introduces its own brands, systems, and managers; becomes embroiled in conflict with its partner; and finally buys out the venture. An analysis of joint ventures in India indicates that majority control in 60 percent of Indo-American alliances lies with the US partner, while Asian partners have control in only 10 percent of their ventures with Indian companies. Europeans fall between these two extremes in their hunger for control.

Consider less obvious partners. A smaller, non-global company may present less of a long-term threat to a company from an emerging market. One Latin

American metals producer decided to form an alliance with a medium-sized German firm rather than a world leader. The alliance has prospered for 20 years, with neither partner aspiring to take full control. YPF, Argentina's privatized petroleum company, and Petrobras, Brazil's state-owned energy company, have proposed a $750 million project for the joint development and operation of a network of 1,500 gas stations, principally in southern Brazil, over five years.

An alliance with a global leader from a different industry is another possibility. Telecom companies from emerging markets could consider allying with information technology providers to build their capabilities, instead of entering more predictable arrangements with global telecom service companies.

Emerging market companies seldom consider taking a "financial" partner, yet this may make sense if they can build the internal capabilities to compete over the long term. Companies with attractive business propositions can win funding from sources as diverse as private equity funds, offshore Chinese holdings, and industrial investors.

Protect your future by securing access to key intangible assets. Emerging market companies should consider locking in key assets such as brands, technology, or distribution rights for 10 to 20 years if possible, rather than risk losing them within a short period or being forced to renegotiate the venture. They should also think how they would survive termination of the alliance. This risk is highest when the local partner contributes physical assets and capital that rely on the intangible assets controlled by its global partner. One Andean Pact manufacturer of transport equipment would have faced the loss of a $200 million business had its partner rescinded the licence agreement on which their joint venture was based. It therefore insisted on a clause stipulating three years' notice of termination. A less canny Latin American industrial company had to consider a shotgun wedding with a new partner when its original partner quit before it had internalized the skills to operate the business alone.

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Create world-class alliance capabilities. For multibusiness companies that may form as many as 20 alliances across unrelated industries, it is better to employ a few experts with well-honed negotiating skills than 20 gifted amateurs. Mahindra & Mahindra, a leading Indian business house, has designated a single senior executive to work with the leaders of each business unit as they develop and manage their alliances to ensure that the lessons each one learns are transferred to the rest of the company.

We have assumed so far that emerging market partners do not wish to sell their share of the business. In actuality, they frequently do. The problem is that potential buyers can be unwilling to acquire joint ventures outright because of the importance of local operating knowhow and relationships, or because of capital constraints. In this situation, a joint venture can be an effective step toward a sale, but the negotiations should look more like an auction than a typical alliance discussion. The local company should pursue simultaneous discussions with several potential partners or buyers, each of which should be asked to develop a proposal that includes an initial valuation for a controlling shareholding, proposed dividend flow, and terms for ultimate sale.

Alliance strategies and tactics for global companies

Global companies, like locals, need to adapt their alliance approaches to succeed in emerging market alliances.

Position early. Alcatel, VW, and AIG are leading operators in China today partly because they were early entrants into the telecommunications, automotive, and insurance industries, respectively. Procter & Gamble leads the Chinese detergents market because it secured access to production assets through majority ventures, then moved quickly to establish local sales and distribution. Early entrants frequently have more opportunities to lock up the most promising distribution channels, gain access to attractive production assets, and invest to build the business before competition intensifies.

In many product categories in emerging markets, the desirable assets, brands, and distribution systems are controlled by a handful of attractive partners. Once they are spoken for, competitors may be locked out, especially if the cost of setting up alternative distribution is prohibitive (as it is for many consumer goods), and where adding capacity (in chemicals, for example) would create overcapacity. India's health insurance market, which is about to be deregulated, is a case in point. In effect, India has a single government insurer, one hospital group with locations in various metropolitan areas, and no provider groups. The partner options are limited, even for early birds.

In many product categories in emerging markets, the desirable assets, brands, and distribution systems are controlled by a handful of attractive partners

Shape the market. The "toe in the water" approach of seeding dozens of growth options at low cost in many markets may seem appealing. In reality, however, joint ventures established in this way often perish from a lack of time or commitment. The global companies that do best in emerging market joint ventures invest heavily and act to shape the market by introducing new business approaches or products.

Think broadly about your partner's capabilities and consider the overall set of relationships that it can bring, not just the immediate joint venture or licensing proposition. The flow of opportunities that local partners, especially conglomerates, can contribute may exceed the value of the initial deal. When a multinational wants access to local relationships, it may be wise to consider companies outside its industry that could play an advisory or ambassadorial – rather than operating – role. It is in this light that Camargo Correa, one of Brazil's largest family-owned conglomerates, views its role in its long-standing alliance with Alcoa. Camargo encompasses one of the country's leading construction companies, and has widespread relationships with industry and government at all levels. It is also involved in related industries such as the development of power projects and infrastructure. Alcoa has the clear leading role in their aluminum smelting joint venture, while Camargo has, over time, assisted in negotiations with government authorities, built manufacturing facilities, and provided capital.

The flow of opportunities that local partners, especially conglomerates, can contribute may exceed the value of the initial deal

As most emerging economies are still at the nascent stage, industry experience may not be of lasting value in an alliance. Consider the case of a multinational seeking to join forces with a local company to enter India's non-durable consumer goods market. The key asset to acquire is distribution, but India's distribution system is archaic and will probably change dramatically over the next decade. The multinational could select the local market leader (and perhaps thereby educate a future competitor), but a more interesting choice might be a tobacco company, which is likely to have extensive retail distribution systems in India.

Identify the key decision makers and involve them early. This is especially critical when dealing with a state enterprise. In China particularly, proposals to establish joint ventures must often be approved by a dozen or more government or quasi-government entities.

Bring all your global capabilities to the table. Global companies have a strong suite of technical skills, geographic presence, business units, and systems, but rarely bring their full power to the negotiating table. The losers in several recent joint venture negotiations in the Chinese automotive and machine tool industries offered a solid but narrow manufacturing partnership; the winners offered technology, local parts sourcing, and substantial capability building. One Latin American state enterprise selected its partner because it could provide technical expertise on the ground to improve the business. Another Latin American company places as much weight on how potential partners might help it secure growth opportunities as on the immediate business they could do together.

Recognize that a "51 percent or nothing" mindset will close off opportunities. Having 51 percent ownership does not guarantee control. Effective control has more to do with management structure, ownership of key intangibles such as technology and relationships, and knowledge. In fact, a 49 or 50 percent stake can provide an opportunity to gain full control later, with less risk and more flexibility.

In one emerging market joint venture, the global partner owns the brand, controls the patented process technology, and is rapidly building its knowledge of the local market – yet it has only a 50 percent stake because its local partner, while recognizing that it needs an alliance in order to introduce new products, is unwilling to sell the "family silver" by giving up 51 percent. The 50–50 venture has none the less proved attractive for the global partner, given that its other options were to sink $200 million into a greenfield operation, form a partnership with a second-tier player, or forget about entering the market. It will, after all, have effective control over the most important business levers, and be positioned as the logical buyer of the business should the partners fall out or the family owners decide to sell.

Emerging market alliances pose different challenges from those faced by alliances in mature markets, and are often less stable

It is often worth asking, "What do we really need to make sure we can protect our interests in a 50–50 deal?" The notion of control can be broken down into rights to determine specific issues – capital expenditures, dividend policies, production volumes, and human resources, for instance. Some multinationals have found creative ways to address particular issues. One leading international oil company signed a 50–50 joint venture in the Indian market after concluding that a casting vote on capital expenditures was enough to protect its interests. Another global company agreed to a 50–50 joint venture with the proviso that it would have the right to build additional capacity if its partner vetoed expansion by the joint venture.

Beware of entering long-term licensing arrangements without performance contracts. Many global companies have granted licences because they had no other way to enter a market, or because at the time the market was negligible. In so doing, some have tied up the value of their intangible assets without any exit mechanism or promise of fair value in return. One US manufacturer granted a 20-year exclusive licence covering several large emerging markets to a single company in the region, with royalty fees set as a percentage of revenues. When its partner underperformed and competitors proliferated, it had little leverage to renegotiate the arrangement.

Recognize that the aims of family owners may differ from those of public companies. For one family owner of a profitable business, assuring an annual dividend of $20 million was one of the key terms of its alliance agreement – far more important than maximizing the value of each partner's contribution. Other family owners may be concerned that their name will stay with the business and that the deal should not be seen as a sale, even when they want to transfer control. And there is usually some sensitivity about preserving operating roles for qualified family members. Acknowledging these wishes may cost little, but can be worth millions. It can make the difference between being the chosen partner or one of the runners-up.

Emerging market alliances can create sustainable growth platforms for both local and global companies. But they pose different challenges from those faced by alliances in mature markets, and are often less stable. Before getting caught up in the heat of negotiations, companies should ensure they have a clear strategy and endgame in mind. They should also determine not only how many chips prospective partners bring to the deal, but how the value of those chips will evolve.