

KEY SUCCESS FACTORS OF INTERNATIONAL JOINT VENTURES OPERATING IN CHINA – A SINO-GERMAN PERSPECTIVE

Tim Gewiss ¹

Fresenius University of Applied Sciences, Germany

Jonas Oestersporkmann ¹

Fresenius University of Applied Sciences, Germany

¹Both authors contributed equally

Abstract

International Joint Ventures (IJVs) are one of the main models of multinational firms entering foreign markets and China in particular. Despite benefiting from various advantages, many partnerships eventually fail. Accordingly, it is of great importance to study factors that determine success of IJVs. Substantial research has been conducted on success factors in the past. However, it has been mainly concentrated on partners from the USA and Asian countries where a Central European perspective has been mainly neglected. This research attempts to fill this void by identifying key factors that determine success of a Sino-German Joint Venture in China. For this purpose, a conceptual model is developed which will be applied to a single-case study of SAIC Volkswagen. The research revealed that the internal factors of balanced control as well as similar commitment, and the external factor of a well-developed infrastructure are the crucial key success factors from a Sino-German JV perspective. At the end of this study, limitations are discussed and conclusions of the research are drawn.

Keywords: Success Factors, IJV, Sino-German, China

JEL code: F21, F23, L62

1 Introduction

In the progress of globalization, firms from all over the world seek for new markets to conquer, profitable investments and further optimization of their value creation processes. Since their market reformations in 1978, the People's Republic of China has become a protagonist within this framework. During the last three decades, China has attracted increasing amounts of Foreign Direct Investments (FDIs) (Yang, 1998). An essential source of FDI originates from the establishment of IJVs, which are one of the preferred market entry models for multinational enterprises wishing to expand to China (Luo & Tan, 2003). One reason for the popularity of IJVs in China is the need for companies to satisfy the governmental restrictions regarding foreign investments and ownership structure (Vanhonacker, 1997). Groot and Merchant define JVs as “separate entities owned by two or

more partners” (1998, p. 579).

A JV can be classified as an IJV, if it involves firms from more than one country (Geringer & Hebert, 1988). Despite creating the possibility for firms to combine their complementary resources (Luo, 2002 b), IJVs tend to have relatively high rates of failure and instability (Kogut, 1988; Hambrick, Li, Xin & Tsui, 2001) as well as unsatisfactory performance (Geringer & Hebert, 1991). Consequently, it is vital for firms to identify potential factors that positively influence the IJV performance, subsequently referred to as success factors.

The majority of the research on success factors of IJVs in China have adopted a Sino-American view. However, a Sino-European, and especially a Sino-German based analysis has been largely neglected in previous studies. This study will fill the void by examining the key success factors of Sino-German IJVs operating in China, with the help of a comprehensive case study on SAIC Volkswagen.

After outlining the determinants of the IJV performance, the third section provides an extensive overview over the automotive industry and SAIC Volkswagen. The fourth section is concerned with data collection and applied research methods, followed by the analysis of the collected data. The paper will conclude with a summary of the main findings and related limitations.

2 Literature Review

Some significant factors influencing the IJV performance have already been identified in the literature and cover a wide range of dimensions. According to Zheng and Larimo (2014), the determinants of IJV performance can be subdivided into three specific dimensions. Determinants of IJV performance can be examined by analyzing the situational factors at the IJV formation stage, factors related to the IJV operation stage, and lastly, by assessing the environmental factors in the respective local market (Zheng & Larimo, 2014). This study will exclusively focus on the latter two dimensions.

Control can be considered as one key factor that determines the performance of IJVs (Geringer & Hebert, 1989; Mjoen & Tallman, 1997). In organizations, control can be described as a process of monitoring, evaluating and adjusting the behavior and output of an entity (Ouchi, 1975). Companies mainly exert control through the use of power, authority (Etzioni, 1965) and three main mechanisms: market, bureaucracies and clan control (Ouchi, 1979). There are existing controversial empirical studies on how much control the parent company should seek to hold. Killing (1983), Mjoen and Tallman (1997) as well as Ding (1997) suggest that one JV partner should seek a dominant position in order to reduce the conflict potential. However, other studies (Beamish, 1993; Yan & Gray, 1994) emphasized the importance of balanced control since both IJV partners can benefit from the other partner's strength. Especially when considering IJVs, it is important to note that ownership does not consequently correspond to control (Behrman, 1970; Friedman & Beguin, 1971). Closely related to the factor of control, bargaining power represents another determinant of IJV

performance. According to Yan and Gray (1994), an interdependency exists between the degree of bargaining power and the related scope of control. Therefore, the respective bargaining powers of the partners indirectly influence the performance of the IJV.

Moreover, scholars identified a positive relation between the level of partner commitment and the performance of the IJV (Killing, 1983; Hu & Chen, 1996; Newman, 1992; Zheng & Larimo, 2014).

According to Morgan and Hunt (1994), relationship commitment can be defined as the partner's intention to persist and foster a relationship. In addition to control, bargaining power and commitment, trust has been identified as an additional determinant of IJV performance by many researchers (Madhok, 1995; Yan & Gray, 1994; Currall & Inkpen, 2002; Krishnan, Martin & Noorderhaven, 2006). A study on 293 IJVs in China by Luo (2002 a) further identified that cooperative behavior between the JV partners stimulate the performance. Lastly, the presence or absence of conflict resolutions influences the IJV's performance (Lin & Germain, 1998; Parkhe, 1991). Having conflict resolution strategies in place consequently positively stimulates performance of the IJV (Madhok, 1995).

In addition to the studies on determinants of IJV performance at the operation stage, further studies have identified factors of the local environment that influence the performance of IJVs (Isobe, Makino & Montgomery, 2000; Barkema & Vermeulen, 1997; Li, Lam & Qian, 2001; Zeira, Newburry & Yeheskel, 1997; Luo, 2002 b). The identified factors include the supporting infrastructure (Isobe, Makino & Montgomery, 2000), the regulatory and institutional environment (Luo, 2002 b), the human resource factors (Zeira, Newburry & Yeheskel, 1997) and the most extensively studied factor culture (Barkema & Vermeulen, 1997; Li, Lam & Qian, 2001).

Figure.1 provides a better overview of the determinants of IJV performance that were identified beforehand. IJV success can result from internal (within the organization) and

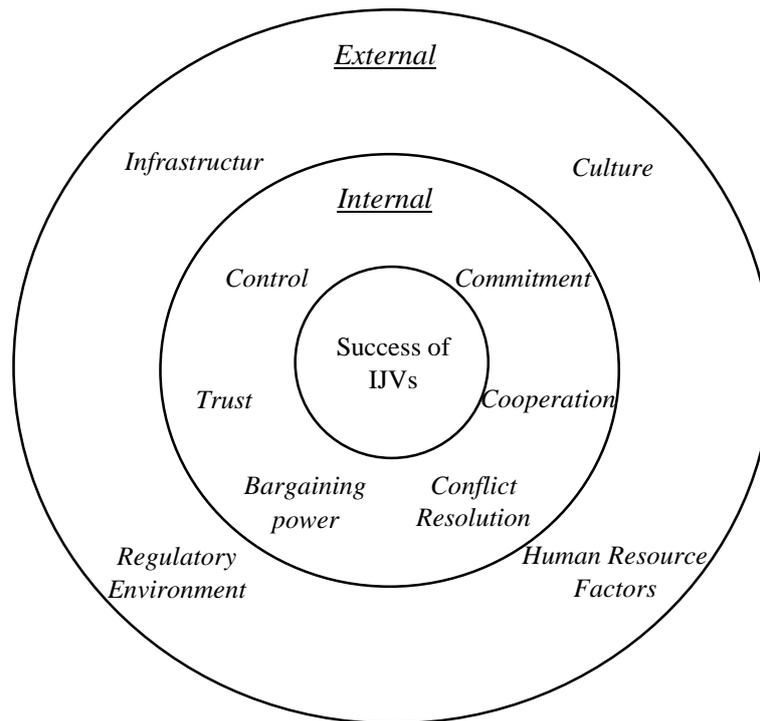


Figure 1. Key Determinants of IJV performance at operation stage

In order to identify which determinants of IJV performance are essential for success, scholars consider a wide range of measures (Demirbag & Mirza, 2000), ranging from instability (Blodgett, 1992), to profitability and growth (Artisian & Buckley, 1985). However, solely using “financial and objective measures embody potential limitations that are critical to evaluation of IJV performance” (Geringer and Herbert, 1991, p. 250).

Therefore, studies also tried to assess IJV performance by considering satisfaction and fulfillment of expectations (Geringer & Hebert, 1991; Artisian & Buckley, 1985). In order to prevent any biases and increase validity, this paper will use both, subjective as well as objective measures.

3 Chinese Automotive Industry

A comprehensive display of the Chinese automotive industry is an essential prerequisite for identifying the key success factors of SAIC Volkswagen. China’s automotive industry originated in the 1950s, however, the modernization and development took place in the 1990s due to decreasing trade barriers (Zhu, Sarkis & Lai, 2007). In 2009, China overtook the United States (US) to become the world’s largest automotive market in new car sales and is growing incessantly. Simultaneously, the sales in well-known automotive manufacturing countries like Germany, Japan and the US almost stagnated or decreased (International Organization of Motor Vehicle Manufacturers, 2017).

Since the entry into the 21st Century, the market landscape changed dramatically with many domestic competitors developing successful market positions and reaching notable market

shares. While in 2004, only one Chinese car manufacturer (SAIC Motor) made the list of the Fortune 500, (Time Inc., 2017 a), six Chinese manufacturers appeared on the list ten years later (Time Inc., 2017 b).

There are two key drivers for the automotive industry growth in China. One important factor is the GDP growth and the emergence of a greater middle class. Studies show that in the year 2000, only 4% of China's urban population possessed the according disposable income (\$ 9,000 - \$ 34,000), yet, 68% fitted this criterion in 2014 (McKinsey Quarterly, 2013). Moreover, the Chinese automotive industry has to be understood within the context of government interventions and stimuli, which function as the second important driver. In the last decade, many policies aimed to support the development of the automotive industry. For instance, the Plan on Adjusting and Revitalizing the Industry, which was in effect from 2009 to 2011 and aimed to counteract the industry slowing due to the financial crisis in 2008 (China Law Info, 2017). The market could keep up its pace and continued to grow even after the termination of the plan.

The Volkswagen Group is one of the most successful companies operating in the Chinese automotive market. In the following paragraph a short overview of the company's operations will be presented.

3.1 Volkswagen Group China

The Volkswagen Group was one of the first foreign automotive companies starting operations in the Chinese market. In 1984, the company from Wolfsburg, Germany started its cooperation with Shanghai Automotive Industry Corporation (SAIC) in Shanghai. Six years later, Volkswagen joined a second JV with First Automotive Works (FAW), located further north in Changchun. Since its entrance into the market, Volkswagen has played a leading role and now manages 29 plants throughout China. It managed to introduce all its brands to the market, which include Volkswagen, SKODA, SEAT, Bentley, Bugatti, Lamborghini, Porsche, Ducati, Volkswagen Commercial Vehicles, Scania and MAN. At the end of 2015, Volkswagen Group China (VWGC) employed approximately 90,000 people. In addition to that, VWGC plans to invest more than 22 Billion Euros from 2015 to 2019 in order to sustain and increase their competitiveness and further develop their sustainable performance (Volkswagen Group China 2017, a).

3.2 SAIC Volkswagen

For the purpose of this research paper, the JV with SAIC Motors, SAIC Volkswagen (SVW), formerly known as Shanghai Volkswagen, plays a special role since its operation will be analyzed in order to determine factors of success of a Sino-German IJV in China. SVW is headquartered in Anting and 50% is held by SAIC Motors, while the Volkswagen Group and Volkswagen China Investment Co., Ltd. hold 40% and 10% respectively. The JV is focused on delivering the two key brands Volkswagen and Skoda to its Chinese costumers (Volkswagen Group China 2017, b).

4 Research Method and Data Collection

Case studies have been widely adopted as a common research method in business-related studies. Likewise, this study will focus on identifying the key success factors of Sino-German IJVs operating in China by the use of a single-case study on SVW. Yin (2014) emphasized the need for case studies in order gain profound knowledge of a real-world case.

Qualitative data was collected through an intensive interview with a top-level-manager of the Volkswagen Group China, who has in-depth expertise and knowledge of the processes and the current situation within SVW.

The conducted interview lasted 45 minutes, employing a focused manner, and can consequently be classified as a shorter case study interview. Moreover, the case study research will be underpinned by a conceptual model, which will provide guidance for the data analysis and support conclusions and generalizations (Yin, 2014).

The case was selected based on the fact, that the JV of SAIC Motors and Volkswagen has been operating in China for several decades and therefore provides access to comprehensive data. Due to the past success of the JV, it is furthermore worthwhile to identify success factors with the aid of SVW.

A conceptual model was developed in order to allow a more systematic approach to the analysis and identification of key success factors at the IJV's operation stage. The already educed overview of determinants for IJV performance (Fig. 1) will be augmented and adapted in order to create the conceptual model (Fig. 2). The developed "Ice Cone model" includes the earlier mentioned internal and external dimensions which determine an IJV's performance.

After having identified factors that predominantly affect IJVs, there is a need to combine them with an IJV's performance. The model suggests to use both, objective as well as subjective measures in order to avoid any biases and enhance reliability. Based on this, key success factors of IJVs at the operation stage can be determined. Subsequently, the study will apply this model from a Sino-German perspective.

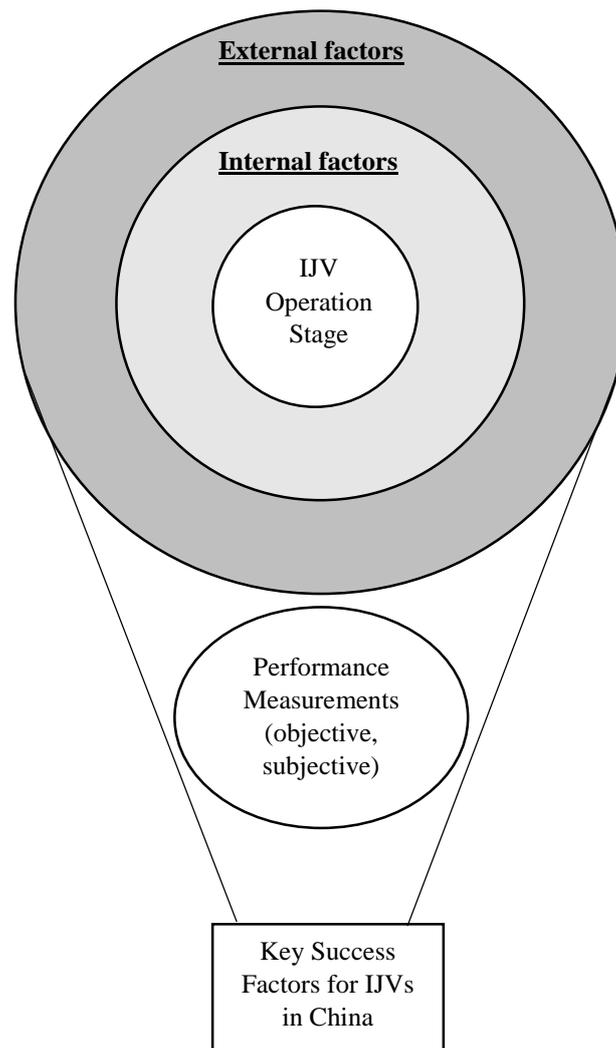


Figure 2. The Ice Cone Model of IJV success analysis

5 Data and Analysis

The interview analysis strictly follows the underlining conceptual “Ice Cone model” (Fig. 2), which was developed beforehand. Determinants of IJV performance that have found wide recognition in prior research (Fig.1) were examined according to the response of the interviewee. As mentioned before, the internal factors comprise control, trust, commitment, cooperation, conflict resolution and bargaining power, while the external determinants include the supporting infrastructure, regulatory environment, human resource factors as well as culture.

The conducted research revealed that balanced *control* in general and over crucial strategic decisions is prevailing within the JV.

This was mirrored in all the researched elements of control: control of investment decisions,

control over strategy formulation and implementation, as well as control over key management positions. The latter element will serve as an example to display this factor and the established process structure.

Question: How great is Volkswagen Group's (VWG) control over key management positions in the JVs?

Answer manager: Certain key positions are filled by Volkswagen Group Germany and others by our Chinese partners. Top-positions are staffed by two co-partners one from each side, which both cooperate and validate important decisions. In the case of executive positions, one person holds the leading position, yet, a representative is assigned by the partner. This secures working closely with each other and that the partners have an insight in all spheres of the operations, even if the division is in the partner's hand.

The research further exposed that a similar level of *commitment* is pursued by both partners. Initiatives and efforts originate from both sides and are in balance as shown in the following.

Question: Would you say, VWG puts more effort and initiative into reaching the agreed upon goals than your Chinese partners?

Answer manager: I believe, the partners in Shanghai contribute equally. Shanghai as a location coins the local cosmopolitanism and business mindset. The processes at SAIC Volkswagen are therefore rather operated in a cooperative manner.

Moreover, *cooperation* especially prevails in predefined shared work processes. It is limited when it comes to the cooperation regarding the exchange of core technologies and know-how in order to secure the company's competitive advantages. The *bargaining power* of Volkswagen is considered to be relatively low due to the high dependency on SAIC Motors concerning market access and subsidy funds. The performance determinant *trust* shows that the need of staying irreplaceable and securing the company's competitive advantages leads to a certain skepticism and according preventive measures. The pursuit of globally differing goals lead to a relatively low form of trust.

Further, the factor of conflict resolution was analyzed. In general, distribution plans and conscientious planning of tasks and responsibilities usually prevent the emergence of conflicts within the IJV. However, differing organizational interests occasionally cause challenges that need to be resolved accordingly. As seen subsequently, the interviewee indicates that conflict resolution strategies are hard to attempt at SAIC Volkswagen, since Chinese employees usually do not communicate disputes in a direct manner.

Question: Are conflicts communicated openly?

Answer manager: This depends on the person and the situation. In general, in the Chinese culture conflicts are not discussed openly. This is much more likely to happen within a small group than a larger one.

Subsequently, Table 1 gives a comprehensive and simplified summary on the results that were identified.

Table 1. Results of IJV Internal Factors

Internal Factors	
Control	Balanced
Commitment	Similar Level
Cooperation	Limited to predefined work processes
Bargaining power	Relatively low
Trust	Relatively low
Conflict Resolution	Hard to attempt due to cultural differences

The analysis of the external factors reveals that general cultural differences between China and Germany are huge. Notwithstanding, organizational cultural differences between the employees in the JV itself tend to be smaller, however still creating minor interpersonal conflicts.

Question: How big or small do you perceive the general cultural difference to be between China and Germany?

Answer manager: In the core of the matter, the differences are huge when considering cultural dimensions of for example Hofstede, including the position of the family and hierarchical structures. However, this is highly dependent on the region. In the offices in Beijing and Shanghai, a Western intercourse is prevailing, including the mindset of the Chinese colleagues.

Moreover, research suggests that the regulatory environment tends to have a great impact on the IJV's operations. Maintaining good relations between the IJV and the government is essential for effectively doing business in China. Furthermore, according to the interviewee, the Chinese infrastructure has developed greatly in the past and the JV benefits from the road and train track advancements. The distribution and production plants are in this sense well connected and organized, which is highly valued by SVW.

Question: How do you perceive the logistical infrastructure and connection to your production plants and distribution locations?

Answer manager: Nowadays, the logistic network is well organized and the many production locations in the center and the south are well connected, even through train tracks and well-built roads, of which the VWG benefits.

Lastly, the various recruitment channels of the IJV allow them to employ highly skilled students from top-universities in China. A summary on the analysis of the factors associated with SVW's local environment is displayed in the following table.

Table 2. Results of IJV External Factors

External Factors	
Culture	Great disparity in general, smaller within organization
Regulatory Environment	Big impact, good relations with government
Infrastructure	Well-developed
Human Resource Factors	Well-developed recruitment strategies provide access to capable employees

The prior analysis exposed a variety of different executions and natures of determinants that are attributed to impact the performance of SVW. Efforts are now concentrated on measuring the performance of the IJV in order to identify which of these determinants can be declared to be a success factor of a Sino-German IJV in China.

For this purpose, a conceptual analysis was conducted. A conceptual analysis is a method for analyzing content and “used to determine what words or concepts are present “(Carley 1990, p. 2). It aims at identifying the manager’s level of satisfaction regarding each determinant of IJV performance. Consequently, the level of satisfaction will serve as a subjective performance measure, while only the factors that reveal a high satisfaction will be chosen as potential success factors.

In order to determine the interviewee’s satisfaction regarding the nature of a determinant, two pre-defined categories are set-up. Subsequently, the interviewee’s answers to each determinant of IJV performance are analyzed and coded for the existence of words with an either a positive or negative connotation. The coding is repeated in the same way for each identified performance element like control, commitment etc.. Words that add nothing to the content, and thus cannot be valued, will not be considered in the analysis. This includes words and prepositions like “and”, “for” or “the”, etc. (Carley, 1993).

In the case the answers concerning a certain performance determinant has a preponderance of words that fit into the positive category, we imply that the interviewee is satisfied with the nature of the performance determinant. However, if an answer has a tendency towards the negative category, we implicate a lower satisfaction. The manager’s satisfaction will be displayed subsequently and is separated into five different levels (high, relatively high, medium, relatively low, low).

Table 3. Classification of Interviewee's Satisfaction

	Low	Relatively Low	Medium	Relatively High	High
Control					X
Commitment					X
Cooperation			X		
Bargaining Power		X			
Trust		X			
Conflict Resolution			X		
Culture		X			
Regulatory Environment			X		
Infrastructure					X
Human-Resource Factors				X	

The additional objective performance analysis will complement the conceptual analysis and further increase the reliability of the results. This study considers sales and profit as essential objective performance measurements. Sales and profit grew by an average of 7.5% between 2013 and 2016. Despite slightly lower growth rates in the last years, the performance of SVW can still be considered as excellent, because both partners managed to create a JV with stable growth rates, a great level of brand awareness as well as a dominant and stable market position (Volkswagen AG, 2014; Volkswagen AG, 2016).

Key success factors of the IJV SAIC Volkswagen are determined by combining the subjective and objective performance measurements. Due to the good financial performance of SVW, all factors (internal and external) that scored high in the manager's level of satisfaction can be considered as being key success factors. Therefore, a balanced level of control as well as a similar level of commitment are key internal success factors. In addition to that, the well-developed Chinese infrastructure positively influences the performance of the IJV and is considered as an external key success factor.

6 Conclusion

The market entry model of JV is commonly used by international firms expanding to Mainland China and represent a significant source of FDI. Nevertheless, inferior performance causes many companies to generate low profits and to eventually abandon the market. Thus, many scholars showed interest in the determinants that positively impact the performance of IJVs in China. However, the research thus far mainly encompasses parent companies from the USA and Asian countries and is not entirely conferrable to the Central European perspective. The research undertaken in this paper attempts to fill this void and reveal success factors of IJVs from a Sino-German perspective operating in China. For this purpose, a case study of the JV of Volkswagen and SAIC Motors was utilized. The review of the literature, first presented a wide range of significant IJV performance determinants and employed a subdivision after Zheng and Larimo (2014). Accordingly, the determinants of IJV performance can be

examined by analyzing the situational factors at the IJV formation stage, factors related to the IJV operation stage, and external environmental factors in the respective local market. This paper concentrated its efforts on investigating the determinants of performance during the operation stage and incorporated the analysis of external factors. The automotive industry in China was presented, revealing its main drivers and specific current circumstances. Within this framework, Volkswagen and its JV with SAIC Motor play a major role and record sustained success, which together with qualitative measures represent an important premise for determining key success factors. This circumstance was combined with the external and internal dimensions to form a comprehensive model. This model was subsequently applied to the primary research on the case study SVW. The research exposed that balanced control as well as a similar level of commitment are key success factors in the internal dimension, while the well-developed Chinese infrastructure can be considered as an external success factor. Respectively, these factors should be viewed as particularly important for Sino-German JVs at the operation stage in Mainland China and efforts should be focused on attaining these circumstances, if not yet incorporated.

As for all research, this paper includes various limitations. For one, the case study comprised only one exemplified IJV and the results should rather be viewed as a first approach to this specific topic. This is especially the case, since the automotive industry embodies a unique and dynamic environment and cross-industry generalizations should be treated with caution. Secondly, due to the fact that qualitative data was collected through only one in-depth interview, the research could include biases. There is a need for further research to either validate or disprove the identified success factors.

In the light of globalization, and as more research will be conducted on this topic in the future, there is a possibility to compare the success factors of Sino-European IJVs in China with each other, which could reveal interesting and valuable results for international business relations.

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