



# Internationalization of Swedish SMEs in Indian market through joint ventures

*How to make the marriage work?*

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*Subject:* Joint ventures

*Level and semester:* Master's Thesis, Spring  
2010

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# Preface

This thesis is written at Linnaeus School of Business & Economics in Linnaeus University during the autumn term of 2009 for the program of Master in Growth through Innovation and International Marketing. Hereby we would like to express our gratitude to our supervisor Sandara Kilkanite. She guided us when we need guidance, she supported us when we feel depressed and she motivated us when we lost energies to continue work. We honestly believe that without her active contribution we would never be able to complete this thesis.

We are thankful to Professor Dr. Hans Jansson for his valuable guidance. We visited him often and he was so kind that he never refused in spite of his busy schedule.

We are really thankful for the valuable contribution of Mr. Henrik Blad, Mr. Nils Marcks Von Wurtemberg and Mr. Ricky Dhillon. They always welcome us with smile and provide guidance beyond our expectation.

We can never forget Assistant Professor Dr. Joachim Timlon, who makes us feel that success comes to those who struggle for it.

Last but not least, we would like to thank our families, friends for their support during our lives.

Kalmar 25th May 2010

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# Abstract

India as a fast growing economy provides great business opportunities. It is considered as one of the most attractive emerging markets. Due to globalization, international business expands and international market is continually converting into boundary less environment. These conditions also affect SMEs. The SMEs are traditionally considered as home based industry but their survival is no more possible with local business. Joint venture is a type of entry mode to foreign markets. This thesis is an attempt to investigate how to improve joint venture relationship between foreign Swedish SME and local Indian firms by identifying and investigating the effecting factors. Throughout our study, the experience of case company Amokael remains focal point. Indian government is still imposing restrictions on certain industries in which foreign firms have to establish business through joint venture. Joint ventures of Swedish SMEs with Indian partners on Indian soil are considered to be critical due to the cultural and societal differences.

**Key words:** Joint ventures, SME, India

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# 1. Introduction

This part is written to introduce the reader about the purpose of the thesis. It will enhance the understanding of the reader that what is presented in the thesis, why it is presented in the thesis and how it is presented in the thesis. The thesis is about the internationalization of Swedish SMEs through joint ventures in India. The thesis is based on the failure joint venture of a Swedish SME Amokabel in India. We have made our research and obtained result generalize to make our thesis more valuable and to give benefit to as many companies as possible.

## 1.1 Background

Globalization has been a major trend since last decade and firms that felt secure with international boundaries are now facing competition. Due to the continuous growth in international trade, firms become more international in outlook and committed to international market. (Kirby & Kaiser 2003). The third wave of internationalization increased importance of emerging markets. Now the firms from mature countries try to establish themselves in emerging markets. Internationalization is a stepwise process where firms learn how to do business in foreign market by a gradual learning process (Jansson 2007).

One of the two major issues that firms face in their international growth concerns the entry strategy. Mainly how firms get access to new customers in new geographic markets? Also how firms should initiate their business and market in order to establish a strategic position in the host country and to maintain such a position. The second issue concerns the internationalization strategy. It deals with the globalization of business by the expansion of the firm to a number of countries (Jansson 2007).

The attractiveness of internationalization and consequently possible profitability encourage not only MNC's but SMEs to focus and increase its international business activities. SME's normally have limited resources like finance, product range and administrative capacity to enter in foreign market (Jansson & Sandberg 2008). More home oriented small and medium sized enterprises (SMEs) are internationalizing their business operations, becoming more global. The reduced physical and psychic distances make it less risky to operate in the foreign markets (Jansson, 2007).

Internationalization is seen as a gradual proceeding via a number of small steps. It is noted that first firms move towards the similar and near markets and then gradually towards other distinct and unfamiliar markets. Firms usually start with intermittent exports are later organized by independent agents or other intermediaries in the market and finally establish own subsidiaries (Forsgren & Holm & Johanson. 2005).

When Western firms enter and expand in emerging country markets, they need to learn many new things. Therefore, knowledge and learning are key factors in internationalization. New stages of internationalization are established with the firm extending its business from one major type of market to another major type or from one type of foreign environment to another. These foreign country market environments or contexts are defined as institutional settings. The internationalization process is therefore determined by the institutional distance between country markets. This concept involves major differences between how societies are organized. It is a broader concept than psychical distance or cultural distance. Rather, it improves cultural distance as a concept for international business research being changed from a country-level characteristic to a country institutional profile based on institutional theory. The institutional distance is assumed to be large when internationalization processes take place from old EU countries to new members as well to Asian countries (Jansson 2007). Firms can benefit from other internationalized firms and learn how they become internationalized what problem others face and how they over come. But this provides only limited benefit. Foreign business skills and knowledge is experimental knowledge and is associated with the specific situation and the contexts in which they have been developed. It is difficult to transfer that kind of knowledge. This type of knowledge can be divided into two kinds one is market specific experience and the other is operational experience. Market specific experience is developed by operating in a specific market and it is hard to use in other markets. The operational experiences are the ways of organizing and developing international business and it can be transferred more easily from one market to another. Generically operational experience can also be considered as experimental knowledge about to use the different modes of operations in the internationalization of a firm (Forsgren & Holm & Johanson. 2005).

The country market is a specific bounded entity. The country markets are surrounded by fences corresponding to economic, institutional and cultural barriers to business. Institutional and cultural barriers are major obstacles to foreign market entry and management. It is generally assumed that the form of organization is used in a foreign country is chosen with a

view to overcoming the psychic and cultural distances in an appropriate way. For instance, direct export differs from acquisition or green field investments in this respect (Forsgren & Holm & Johanson. 2005).

SMEs choice of an entry mode can highly affect the performance of companies. The choice of entry mode is affected by the firm resources; larger firms tend to have larger economic and managerial resources for the investments demanded for own representation in the market of entry than smaller firms (Jansson 2007). Entry strategy for international market is a comprehensive plan where evaluation of alternative entry modes plays major role to choose the best entry mode for the particular market (Backlund & Suikki 2005). The firms can enter into foreign market through intermediation or by establishing its own subsidiary which provide an option of exporting, FDI or joint venture (Jansson 2007).

## 1.2 Research background

Amokabel expanded its international business and entered in the Indian market. India is an emerging and growing market and Amokabel decided to enter in the market through joint venture. The joint venture was supposed to reduce the risks but unfortunately this joint venture ended in a total collapse and Amokabel had to close down its operations in India. The research is based on the failed business move of the Amokabel and is supposed to reduce the risks for any SME to avoid this kind of failure in future.

## 1.3 Problem Definition

In this section the main research problem and research sub problems, deriving from the main problems are described.

Joint ventures are not new creations. It is an older form of business structure; it was a vital mechanism during the first half of the 1800's. The development of new industrial technologies and economic growth in a risky environment bring them back. (Lynch 1990).

Joint ventures are like marriages and according to old English saying "Marry in haste, repent at leisure". Joint ventures are particularly problematic to manage, because by preserving the separate identity of their parent companies, they incorporate inherent sources of conflict. Joint ventures are critical when it cross borders because cultural differences and management philosophy come into play and challenge can be hard to achieve. It is management responsibility to overcome the differences in order to achieve the objectives and make a joint

venture successful. The instability rate is evidently high and the failures are often cited. This leads many observers to wonder why so many joint ventures are continued to establish (Yan & Luo 2001).

Although joint venture is a good option but it is hard to manage because both firms came from different backgrounds. The differences between firms point of view can distract from the objective. The situation becomes more complex when mistrust build between firms while sharing knowledge ((Brassington & Pettitt (2006), QickMBA (2010) and Backlund & Suikki (2005)).

The major challenge for joint venturing is partner selection, which is critical to both for foreign and local partner. Appropriate selection of the partner can improve a multinationals firm's advantage in foreign market. The firm can gain access to those marketing and distributing channels that are available only to local business (Lynch 1990).

Joint ventures are inherently design to address risky business. Therefore they are more prone to failure than traditional business structure (Ibid).

## 1.4 Main Research Question

Swedish SMEs can choose different entry strategies to enter in the India. Joint venture is one of the possible entry strategies. The idea is to find out the situations where joint venture is best entering strategy for the Swedish firms to enter in the Indian market.

*When JVs is the most appropriate entry mode for Swedish SMEs to enter in India? Or identify the situations where joint venture can be the best entry strategy for Swedish SMEs to enter India?*

### 1.4.1 Research problem 1

*How to choose the right partners for JVs?*

Joint venture is the working arrangement between two partners. Joint ventures are usually established to combine different strengths of two firms in a field. It is really important for the firms to choose right partner. It will help the SMEs to find the best partner.

## 1.4.2 Research problem 2

### *How to overcome the cultural differences between the partners?*

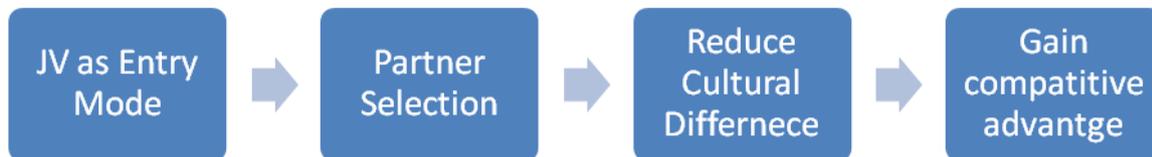
The communication gap between the partners due to the geographical cultural differences can mislead the partners, resulting in the total collapse of the joint venture. This is to help the Swedish SMEs to avoid this type of situations. The importance of this issue is specially increased as we deal with the joint ventures between Sweden and India where great cultural differences exist.

## 1.4.3 Purpose

Considering all the information above the main purpose of the research can be identified as to help Swedish SMEs to expand their business in emerging market of India through joint ventures, by critically analyzing the case of Amokabel. This study will try to explain what problems Swedish SMEs face when they establish in a joint venture with an Indian partner and also what they need to do to overcome these problems?

## 1.4.4 Summary of Research Problem

The overall aim is to improve the joint venture relationship and in the figure it is seen how problems are interlinked and improved the business relationship



We will start with the identification of the situations where joint venture is the best entry mode for the Swedish SMEs to enter in India. We will discuss different types of entry modes but our main emphasis will be particularly on Joint venture. Then we will move on with how Swedish SMEs can find best Indian partner. In the end we will find out that how inter partner compatibility can be increased by reducing the cultural differences.

## 1.5 The case company

The Swedish family-owned company Amokabel Group is located in Alstermo. Amokabel Group was started in 1992 with the formation of the first company, Alstermo Produktion AB. The continual passion for growth resulted in the enhancement of group with the establishment of new companies in the group as well as in new sectors like hydroelectric

power and the real estate. The turnover of Amokabel group for the year 2008 was equivalent to 50 million Euros and the group now consists of three cable manufacturing companies with subsidiaries companies. The group diversifies its investments by investing money in hydroelectric power and real estate.

The group is producing everything from automotive wires to covered conductors. The core business includes the ability to manufacture thousands of different types of wires and cables. The group also offers to design and produce a large variety of custom made Cables. Top performance in flexibility, quality, lead-time, product groups with minimal administration, technical specification and environmental thinking are the core values of the company.

Amokabel Group prides them on their delivery time. They guarantee deliveries within five days and in emergency cases they can reduce the supply time up to 24 hours. Last minute customer orders can be handled easily some of the production machines are reserved for the last minute customer orders and are not used in daily routine production process.

Simplicity and long-term thinking are the basic pillars of the corporate culture which enable the group to continuously innovate and improve the products and processes.

Amokabel Group is an international company with sales offices in Denmark and Norway, the representatives in China, Thailand, Hungary, Finland, Holland and Belgium and a joint venture in India.

Amokabel started a joint venture “Amelco Kabel Pvt LTD” in India with a local Indian company Elcomponics in May 2008. Elcomponics owned 51% shares of the joint venture and Amokabel owned 49% shares. The responsibility of the Amokabel is to transfer technology and the responsibility of the Elcomponics is to sale the product in the local market. The joint venture turned into a total disaster and Amokabel left India in May 2009. The Amokabel still owned the 49% shares of the joint venture but never claimed the profit or the actual investment back.

## 2. Methodology

In this chapter, the methodology for this research will be presented. Begin with the discussion of research design, followed by the scientific approach. Later on research method and data collection method will be under discussion.

### 2.1 Research Design

Yin (2003) described five types of research strategies to deal social sciences. These ways are experiments, surveys, histories, case studies and analysis of archival information. Each strategy has its own advantages and disadvantages depending on different conditions. Mainly there are three types of conditions: the type of research question, how much control investigator has over actual behavioral events and the focus on cotemporary as opposed to historical phenomena. The main difference between these research strategies are the ways of collecting and analyzing empirical evidence. Yin draws a table to show how these three conditions relate to all research strategies.

**Table Relevant Situations for different Research Strategies**

Strategy	Form of Research Question	Require Control over behavioral events	Focus on Contemporary events
Experiment	How, Why	Yes	Yes
Survey	Who, What, Where, How many, How much	No	Yes
Archival Analysis	Who, What, Where, How many, How much	No	Yes/No
History	How, Why	No	No
Case Study	How, Why	No	Yes

Source: Yin (2003), Case Study research: design and methods.

Every strategy has its distinctive characteristics but a large overlap can be found among them. Therefore, our main goal is to avoid the overall misfit. The experimental study can be done under laboratory settings (it is conducted in controlled environment). The main focus is on few variables. History does not deal with contemporary events. Survey study deals with phenomena and context but its context is very limited. Generally survey can be done through questionnaire and archival analysis. Case study is based on empirical study that investigate contemporary phenomenon within its real life context especially when boundaries between phenomenon and context are not clearly marked. (Yin 2003) (Jansson 2010).

According to Dubois & Gadde (2002) case study is considered a soft approach. It is hard to conduct but remain a common method of research in many scientific fields like psychology, sociology, political science, economics, management, public policy, social work etc.

In our study of joint ventures the choice of case study as a research technique is based on the facts that, we will deal with how and why type of questions we have no control over events and our focus is on a contemporary phenomena with real life context and according to Yin these all are the requirements where case study is the preferred strategy. Case Study will be helpful to understand the soft factors like culture as Yin (2003) described that case study is not just a data collection technique or a design feature but a detail research strategy.

## 2.2 Scientific Approach

According to Yin (2003) three types of scientific approaches can be used exploratory, descriptive and explanatory. These three techniques can be used at different stages of the research.

We used exploratory approach at the beginning of the study to identify and define the problem for further study. We studied an example of failed joint venture under exploratory approach. Then we used descriptive study for in depth study of events and scope connected to the thesis like social and cultural effects on JVs. Finally in explanatory approach we explained the cause and effect relationship after collecting information and knowledge.

There are two approaches for research problem namely inductive and deductive. Inductive approach applied to work with new things and trying to put them into theory and the deductive approach used to explain theory based events.

According to Dubois & Gadde (2002) inductive approach applied to work with new things and trying to put them into theory and the deductive will be used to explain theory based events. Primarily, deductive approach strongly emphasizes on theory. The weakness of this approach is having a distance from induction which is relatively based on empirical data.

Gadde and Dubois believe that the coherence of both approaches provides a detail and strong research background to analyze the findings.

Gadde and Dubois describe abductive approach as a way of conducting research. This approach is a systematic way of combining theory and empirical data for the analysis of research problem. Since our research problem is based on joint venture in international context we position to use abduction approach for our study. The reason behind this choice is the metaphor of case study which is in real life context and the way Gadde and Dubois define abduction as “investigating the relationship between everyday language and concept”.

Theory with the combination of empirical data provide further clarification of the situation and increase the chance to explore the factors which previously remain unrevealed. According to Gadde and Dubois matching between theory and real context is very important for case studies it helps to improve the study in future. The ideal way is to bring the problem from real life and examine it in the eye of theoretical frame work to know the areas where improvement required and how? Abductive approach claims that the theoretical Framework should be concrete and strict in order to provide guideline and observe empirical data in focused way. Abductive approach provides a way to refine the existing theories with the help of empirical findings.

We are using abductive reasoning for our case study because it provides an open space for work with the unique combination of inductive and deductive reasoning. In our research problem we are not testing theories or developing new one but figure out the important aspects with the help of empirical data and theoretical framework.

### 2.3 Research Method

Research Method can be distinguishing between qualitative and quantitative. According to Merriam (1998) researchers can adopt qualitative or quantitative methods to do a case study. According to Yin (2003) quantitative research deals with hard data, like statistical or numerical data where outcome are highly figured oriented and truly scientific. Qualitative research deals with soft data like social sciences where attributes, perception and human behavior involved.

Our study is merely based on qualitative research method. The reason of this choice is based on the research problem which deals with the joint venture issues between Swedish and Indian firms. Due to the importance of social and cultural factors the qualitative method considered more relevant because it is hard to get quantitative data on soft factors.

## 2.4 Design of Case Study

According to Yin (2003) case study design work as a blue print for researches and deal with four basic questions. What problem to study, relevant data, what to collect, and how to analyze results. The main purpose of research design is to avoid the unnecessary and irrelevant data and keep align with the research problem. The case studies are classified into four types known as single case (holistic) design (Type 1), single case (embedded) design (Type 2), multiple case (holistic) design (type3), multiple case (embedded) design (type 4). Each design has its own boundaries and can be used under different circumstances. Type 1 and type 2 are used for a single unique case discussion. Type 1 is used under single unit analysis and type 2 is used under multiple units. Whereas type 3 and 4 deal with multiple cases against single unit or multiple units. Single case design provides a thorough and concrete study because of its boundary limit.

	Single-case designs	Multiple-case design
Holistic (Single-unit of analysis)	Type 1 Single case in one unit	Type 3 Multiple cases in single unit
Embedded (Multiple units of analysis)	<b>Type 2</b> Single cases in multiple units	Type 4 Multiple cases in several units

Source: Yin (2003), Case Study research: design and methods

We consider Type 2 as an appropriate option as we discussed joint venture in international context where partner join each other from different continents to achieve single objective. Our case company Amokabel worked in India with an Indian company named Elcomponics. It was a joint venture and we studied this joint venture under Swedish prospective to improve the relationship between Swedish and Indian partners.

## 2.5 Data Collection

Mainly data can be distinguished into primary and secondary. We collect data from both primary and secondary sources. The primary data directly collected through interviews and articles, books and internet are the sources of secondary data.

### 2.5.1 Primary Data

We conducted interviews as a primary source of collecting data for this research paper. One advantage of interview is the reliability and authenticity of data. The interview was conducted in English language because of its international importance in joint ventures. The interviews were semi structured to get as much information as possible. To get a wider view, we interviewed experts who have strong knowledge on joint ventures.

We designed two types of interviews one for Amokabel representative and other one for experts.

We ask 43 questions to Amokabel representative during interview which covers company experience in India and what they recommend to SMEs who are interested to exploit business opportunities in India. The interview contains 15 questions which we asked from our experts. Our experts also provided us data regarding our topic.

### 2.5.2 Secondary Data

We collect the information from books, scientific articles and internet and use it as a secondary data.

The main source of our secondary data is based on the books from the library of Linnaeus University, Kalmar Campus. We also use university internet E-library to get access to the online books, thesis and research papers. For this purpose ELIN search engine remained helpful.

We also used internet for data collection as it is the major source of information and newspapers, articles and research studies easily available in WebPages.

### 2.5.3 Respondents

The introduction of the different respondents is given below.

#### 2.5.3.1 Swedish Trade Council Representative

The Swedish trade council (STC) is an expert body. Its job is to facilitate the Swedish firms at foreign soil and provide guidance about market information and strategic advice. STC also encourage foreign investors to invest in Sweden .Swedish trade council (STC) is a government body and its support is available at government and industry level.

We interviewed Rickey Dhillion who is the representative of Swedish trade council (STC) about the current situation of Indian market, problem and issues and the best strategy to enter in Indian market.

As a requirement of his job he deals with the day to day problems of Swedish business people in India. He is practically involved with the business problems and their solutions. On the basis of his knowledge we consider him the valuable source of information for our research thesis.

### **2.5.3.2 Amokabel Representative**

Henrik Blad is a young energetic Swedish business man. He is the Managing Director of AmoKabel (the case company). Henrik was practically involved in the joint venture of AMO Cable in India. He was the vice MD of Amelco kabel Pvt Ltd India. He is not only the witness of all the incidents but also practically involved in all the business matters. As a member of the traditional Swedish business family and the active partner of the JV company Amelco kabel Pvt Ltd India. We consider him as best source of information.

### **2.5.3.3 Swedpartnership Representative**

Swedpartnership provides expert guidance and financial support to SMEs to exploit the business opportunities in developing countries. The ambition is to take advantage of industry experience and expertise and to simplify the Swedish company's opportunities for contacts and business with companies in developing countries. The idea was also to bring together the efforts involve support and cooperation between Swedish companies and companies in emerging markets. Nils Marcks von Wurtenberg is working in swedpartnership as a program officer. He has experience to work in Arthur Andersen, KPMG, SEB, Swedbank and many other big Swedish organizations. He is working with swedpartnership since October 2009.

## **2.6 Reliability and validity**

Reliability is generally used in terms of consistency or quality. According to Yin (2003) the goal of reliability is to minimize the errors and biasness. Validity deals with research measures to determine the truthfulness of research results. To increase the validity of the thesis we ensure both external and internal validity. We use the triangulation technique by applying multiple sources of data and methods for confirming findings. We collect information on a common issue by different sources and then compare the information that weather it resembles with each other or not. We conduct interviews from different persons and verify information with collected data by cross examination. We also verify information from European commission survey and STC provided data. Furthermore, we use books,

articles and websites for the verification of data. Like we find out a fact that legal proceedings are slow and costly in India we asked about the case company representative about his experience then we asked from the STC representative for his expert opinion and then we further confirmed this issue by using secondary data from different books, articles and web sites.

This technique helped to check strategies to enhance internal validity. The data and interpretations will be driven back to the people (sources) to confirm the plausibility. In the end the method of peer examination used where our some colleagues comment on our findings (Merriam, 1998).

For this particular reason we conducted interviews to analyze the empirical study of joint ventures between Sweden and India.

As Merriam (1998) and Yin (2003) discuss the importance of external validity by elaborating the fact that study should be generalize. We want to give benefit to as many companies as possible from our research so we try at our best to make our findings generalize by increasing its external validity. We also used rich thick description so that other can compare their situation with the situation described in our thesis.

According to Merriam (1998) in social sciences the reliability is problematic because human behavior is not static so we tried to make results as consistent as possible with the collected data rather to think about that whether the findings will be found again.

According to Yin (2003) reliability means to verify that results are actually come up from the relevant data. We tried to implement sources of evidence and followed the rules of data collection described. We make our documentation strengthen by reviewing it repeatedly and by including exact names, references and details of the events and avoid its weakness by avoiding the blurred information. The second source of evidence “archival records” was used sensibly by avoiding the blurred information. Interviews as third source of evidence remained semi structured to get maximum information and to remained focus on the topic, we recorded these interviews to avoid any loss of information.

## 2.7 Methodology and Criticism of the sources

All respondents in this study are Swedish and it can be perceived that study shows only one side of the problem. Although it is somehow true but our aim is to study joint venture in Swedish prospective and how Swedish firms overcome the problems in Indian market. Therefore, we do not see it as a problem.

### **3. Theoretical Framework**

The models and theories used to answer the research questions are discussed in this chapter. The internationalization process, different options for firms in the journey of internationalization and the important factors affecting this journey will be discussed. The challenge faced by firms in the host country, model to scan the host country environment and to make appropriate strategy. The silent features of host country (India) are as well under discussion in a portion. Different aspects of joint ventures are comprehensively discussed like the types of joint ventures, driving forces for joint ventures, benefits and limitations and the critical features for their success. The appropriate partner selection criterion for joint ventures is also comprehensively discussed.

#### **3.1 Internationalization Process**

According to Jansson & Sandberg (2008) and Jansson, Hilmersson & sandberg (2008) internationalization of SMEs is a gradual and slow process where firms learn how to do business abroad. Longer a firm stays in a market more experience and strong place it gets in market. Internationalization process can be discussed under five stages model. This model describes how firms increase its international business and relationships from low to high. The increase in market knowledge and business relationship provides a strong hold to firms in foreign market. Internationalization process also depicts the objective of a firm in certain market.

Mainly the choice of entry mode is based on firm's internationalization exposure and their willing to expand. Joint venture is an option for firms having long term objective in a particular foreign market.

#### **3.2 Different Modes of Internationalization**

The firms used different modes to enter in international market like exporting, licensing, subsidiary, joint venture or strategic alliances (Lu & Beamish 2006). We discussed different possible entry modes here but our main emphasis will remain on joint ventures because it is the area of study for this thesis.

##### **3.2.1 Export (Intermediaries) (producer/customer relationships)**

Export can be of two types one is through intermediaries and other is through producer customer relationship.

In exports through intermediaries an exporter/importer network is established. It is established for the task of marketing/purchasing a product/service package. This international marketing and purchasing of products and know-how through this direct exporter/importer network means that a vertical network in the exporting region (for example a supplier's supplier network) is indirectly connected to another vertical network in the importing region (for example a buyer's buyer network) (Jansson 2007). According to Jansson & Boye (2010) agent or distributors are generally independent representative and considered an indirect link between supplier and customers.

SME's with limited resources use this intermediation way to enter in new markets. It is less risky and does not required SME's self presence in the market. Agents or distributors are helpful with market information and contacting with customer where language and culture is considered a barrier especially in emerging markets. It requires limited investment to enter in the foreign markets through intermediation (Jansson & Sandberg 2008).

The problem in this relationship is having no control on performance of intermediary because firms are fully depended on intermediaries for sales. It is hard to stop agent or distributor to involve in another business activity because it decreases its focus on SMEs business. Intermediary never provides the exact information about the customer or market development because it's in his own interest to create a gap between supplier and customer (Jansson 2007). Intermediation is good in the beginning of internationalization process but not helpful in the longer run (Jansson & Sandberg 2008). More risks are involved than benefits in this mode of internationalization.

The second type of export is the direct producer/customer relationships. In this the experiential knowledge of the parties is high. Direct producer/customer relationships do not suffer from the lack of direct contacts customers. They are highly committed and extensively adaptive. Supplier change, alter or develop the production and logistic system to fulfill the demand of the customer. The customers transfer the knowledge to buyer to improve the products. This amount of transfer of the knowledge show the trust of parties on each other (Jansson 2007).

The relationship develops mainly because the suppliers willingly adapted the production system and the logistic system to the demands of the buyers. To make it possible for the supplier to improve the quality of the products, the buyers share their knowledge with them. This is especially true for relationships involving outsourced products, where the knowledge

gap is large at the outset of the relationship. Communication through the information and know-how linkages played a critical role. The social linkage is very important in these relationships, otherwise the communication would not work properly. The social linkage is closely related to the information and know-how linkages. When the parties trusted each other, the exchange of information and knowledge became more open and reliable. Social relationships tend to become underdeveloped when barriers like these exist (Ibid).

To overcome these issues, firms can look for establishing subsidiary or joint venture which are more suitable and long lasting way to enter in foreign market.

### **3.2.2 Subsidiary**

When firms need to increase their control on business in foreign market, they consider different business structures to support business activity in foreign market such as subsidiary. According to Jansson & Sandberg (2008) subsidiaries not only provide strong business presence in foreign market but also effective in dynamic business environment where competition is extensive. The business through own subsidiary provide a direct contact with customer where firms have the great opportunity to build trustworthy relationship with clients and also learn the market tacit knowledge. Firms reduce cultural differences, geographical distance by establishing subsidiary although it takes time but it is in the longer interest of an organization. Firms can take advantage of low labor cost by placing production unit in emerging markets. Establishing a subsidiary in a foreign market shows firm's commitment towards internationalization in particular market. Direct contact with customer provides firms the opportunity to build trust between customer and supplier, once this relationship established the barriers start to reduce.

Although subsidiary has its own benefit but some demerits also present. As described in Johanson & Vahlne (1977) one problem with subsidiary is that a firm needs resources to establish it, which is good for MNCs but SMEs don't have enough resources to establish their own subsidiary. The risk rate is high because SMEs invest in a foreign market where conditions are different from home market.

The business opportunity converts into a great loss, if company unable to manage the things. In dynamic business environment where firms need to increase their control and want direct customer attraction the subsidiary is the best option (Jansson & Sandberg 2008). The problem with the subsidiary is that it require massive investment which may be possible for MNC but it is hard to manage for SMEs (Johanson & Vahlne, 1977).

Both business styles have merits and demerits in first way the risk and profit both are low, company is highly depended on intermediary. The later provides strong control over business on foreign market with high profit margin but the risk ratio increased at maximum level.

Two more entry strategies which can be used as an alternative to subsidiaries are acquisitions and joint ventures.

### **3.2.3 Acquisition**

Acquisitions of other firms are to secure critical relationships when there are threats from competitors. It can also help to establish relation with suppliers and customers. By acquiring a company the firm thus becomes involved in a set of business relationships and by way of interaction in these relationships it gradually develops in response to the value generated by these relationships (Forsgren, Holm & Johanson 2005). As discussed above that the SMEs have limited resources and it is hard for them to acquire any foreign firm.

### **3.2.4 Joint Venture**

International joint ventures normally defined as JV's that involve firms from different countries cooperating beyond national and culture boundaries. The majority of international joint ventures involve two partners, one from a foreign country and the other from local country. Joint ventures are legally and economically independent organizations operate as standalone firms who engage in regular business activity like any other independent firm (Yan & Luo 2001).

Firms seek partnerships to stay ahead of the competition in today's global economy. There are multiple uncertainties a firm can get through joint ventures including lack of knowledge of local market, risk sharing, and ability to combine different value of chain strength. Joint venture with local firm help to reduce this gap, on the contrary it is also a good option for local firm to learn foreign technology (Byung 2008).

According to Jansson & Boye (2010) SME's traditionally home market oriented so they have a disadvantage in international trade. Therefore, these firms considered as low degree of internationalization. This problem can be resolve by developing a joint venture where two or more than two firms work together in order to get competitive advantage. This can be achieved by sharing resources. Joint ventures open new business opportunities.

According to (Brassington & Pettitt (2006), QickMBA (2010) and Backlund & Suikki (2005) SME's looking forward for joint ventures due to their limited resources. The intension of doing business in cooperation is using external resources of partner to increase the proximity.

It also helps for establishing relationship. Joint venture is a beneficial tool in those markets where uncertainties high or trade barriers gave advantage to local firms over foreign firms. Joint venture not only able to reduce to cultural differences but also helpful in those markets where political instability effect the business performance. The potential of high sale volume increase the importance of joint venture in such countries like India and China. Joint venture is a favorable option in those countries where cheap labor force and good raw material available. Foreign companies just provide the technical facilities in that case. Under the umbrella of joint venture, two firms merge its resources in order to obtain the benefit which is helpful for both firms; one can learn the market knowledge and other can get the technical knowledge. Foreign firms can work as a local business entity in this way and get the inside knowledge of market. It is also favorable in investment point of view because SMEs has limited resources so joint venture will be the good option for firm to enter in international market.

Joint ventures are the most common and secure way to enter in international markets for SMEs due to limited resources (Kirby & Kaiser 2003). It is considered the best entry strategy for SMEs that minimize the risk of the firm in foreign market and increase the productivity. JV is a beneficial tool to learn new market knowledge while having a direct interface with customer.

Normally there are five main reasons for a firm to choose joint venture as entry mode: market entry, risk sharing, technology sharing and joint product development, as already discussed it also helpful to conform according to government regulations. Joint venture provides an opportunity to build political connections and business relationships (Kirby & Kaiser 2003).

#### **3.2.4.1 Types of Joint Ventures**

Hewitt (2005) divided joint venture into two groups. This classification is based on practical way of working rather than based on legal entity.

##### **3.2.4.1.1 Equity Based Joint Venture**

This form is used where partners willing to contribute capital to a joint venture that has a separate entity from its parent companies. Both Parties share the profit and loss on the basis of their share in the business.

##### **3.2.4.1.2 Non Equity Collaboration**

These types of alliances are not generally based upon establishing a separate entity from its parents and not deal direct profit based activities. The main focus remains on sharing

resources like R&D, joint productions and network alliances. These types of ventures are merely contractual.

Both types have differences on the basis of degree of control and motivation of partners. Generally a new entity of organization established under Equity Joint Ventures.

### **3.2.4.2 Driving Forces for Joint ventures**

Peter Drucker, the world famous economist considers joint venture as an important pillar of the business in future. He elaborate it more by saying that no company hold total control under current climate and firms will be mutual depended to each other to survive. According to Lynch (1990) there are several competitive forces that play an important role for the growth of joint ventures and strategic alliances. His classification is as followed;

#### **3.2.4.2.1 Hybridization of Technologies**

The development of new products may require expertise in diversified technologies. The firms usually have expertise in one particular area and failed to do new developments. This dilemma is a driving force for firms especially in technology sector to think about joint ventures for making new products. Current international markets require integrated system where different technologies available in one component. Firms can analyze and choose the joint venture partner by considering the lack area (Lynch 1990).

#### **3.2.4.2.2 Need to Bring Products to Market Faster**

Current economic world open a window where early introduction of product in market play a major role for competitive advantage. A partner having massive marketing and distribution channel can play a major role to get competitive advantage in foreign market and sometime even first mover advantage. Firms often adopt this strategic option to grasp the market at deep level in foreign market (Lynch 1990).

#### **3.2.4.2.3 Sharing Risks of Enormous Capital Expenses**

The joint venture help firms to produce and develop products by reducing cost factor by combining their expertise. New products or technologies often cost a lot but there is a threat from competitors to come in market with same type of product. So, by combining expertise of partners in joint ventures possibly decrease the risk factor on single arm. Good joint ventures will possibly the cause of complement each other weakness (Lynch 1990).

#### **3.2.4.2.4 Problems of Insufficient Management**

Companies often lack of sufficient management skills when it comes to extremely complex task for example construction business. The problem become intensive when firms want to enter in new market or new industry where previous experience consider little value. It is hard to have all skills in one hand so firms work jointly to overcome the weak areas (Lynch 1990). Partners pooled their skilled managers in joint venture in order to achieve the objective. Due to the criticality of the feature a functioning combination of people is very important.

#### **3.2.4.2.5 Insufficient Capital**

Smaller firms have financial problems but growth potential. Joint venture help firms to overcome the financial problems because investment shared by partners which allow firms to keep focusing on its expert areas (Lynch 1990).Sometime firms looking for an acquisition and it is impossible for them to go for it alone due to financial issues. Joint venture is rather considerable option to increase financial strength and make deals affordable (Hewitt 2005). Potential partner with sufficient cash flow is needed for future plans.

#### **3.2.4.2.6 Disappointing Merger and Acquisition Results**

The result of merger and acquisition during 1980's firms learnt a lesson that it is very hard to manage. One of General Electronics study shows that 95% of acquisition gave disappointments to the parent company. During last decade companies adopt and formulate a new strategy to go for joint venture rather than acquire a company. Joint venture is a less costly and less risky option for not only SMEs but MNCs as well (Lynch 1990).

#### **3.2.4.2.7 Cost of Communication**

International Joint Ventures possibly able to reduce the communication gap between two different cultures especially when the distance is high. Firms face troubles to manage business in foreign markets alone, joint ventures helps firm not only to reduce the societal gap but provide a good management skill. Due to the cultural distance many authors consider JV a better tool than wholly owned subsidiary (JIBS 2009).

#### **3.2.4.2.8 Enter to Restricted industries**

Joint venture is the only option to enter in such industries where government policies discourage or forbid full ownership of foreign investor. International firms got success to resources that controlled by local firms in particular industry (Gocmen 2004).

### 3.2.4.3 Limitations of Joint ventures

There are situation when choosing joint ventures as an entry mode results off track or great loss in market. Few limitations discussed by HM Treasury (2010) & Jamil et al. (2008) & rpemery.com & Gocmen (2004) are as follows;

- JV established when partners have common interests or shared objective. It is the primary need to establish joint ventures. JVs turned into great failure and not a suitable option if the interests and objectives not aligned.
- Companies just look for business opportunities and enter without any Business plan.
- Joint Ventures will not be fruitful if firms did not consider local demands of a foreign market and just enter with its own expertise.
- Partners must define each other responsibilities before running operations and show commitment with it. Many firms failed due to unclear responsibility issues.
- Firm must identify the ways in case of conflicts between partners.
- Foreign firms dependent on local partner in foreign markets, so the trust issue between partners remains very important for the success of joint venture.
- Difference of culture and management style results poor performance and coordination.
- If parent firms enter in different industry where both companies have no prior experience and require cross product strategy. The need of learning new skills, technologies and resources require high motivation. The risk of abnormal return increase significantly.

Now we will analyze different factors that are important for the firms while choosing entry mode for foreign market. These factors determine which entry strategy a firm should adopt according to its need and circumstances.

### 3.3 Factors effecting Inter partner compatibility (*Partner Selection Criteria*)

Inter partner compatibility is the key foundation for the successful joint venture. The collective and individual gains from joint ventures for the partners are dependent on it. Culture, strategy, organization capabilities and financial traits are most important areas for inter partner compatibility (Yan & Luo 2001).

Selection of both local and foreign partner is important for a successful joint venture. The local partner from host country can reduce the risk and increase the capability of the joint venture to use local networks and market resources. A foreign partner can bring advance technology, international know how and management expertise for the joint venture.

The appropriate partner selection criteria should be defined before the formation of JVs. The two broad types of criteria for partner selection are operation related and cooperation related. The strategic competitiveness and skills of the partner like absorptive capacity, product relatedness, market position and industrial experience are included in operation related cooperation. While cooperation related deals with the organizational or inter organizational traits like previous inter partner collaborations, experience in overseas operations, organizational form and firm size (Yan & Luo 2001).

### **3. 3.1 Cultural traits**

Achievement of cultural synergy is necessary for the development of mutual trust. The mutual trust is necessary for the success of joint ventures. Therefore, thorough research study of both types of cultures is important; national and organizational. The problems usually start when a partner unilaterally imposing its culture without considering the others. This includes both national as well as organizational culture. The organizational structure, business strategy, decision making process, management flexibility and conflict management are vitally important while developing organizational culture compatibility (Yan & Luo 2001).

### **3. 3.2 Strategic Fit**

The different aspects of the strategic fit which plays important roles are discussed below.

#### **3. 3.2.1 Absorption capability**

The absorption capability of the partners and their skill to exploit new knowledge while combining it with existing knowledge is important. This capability works much better when partners have different skills. The skills of one partner can help other to overcome the deficiencies of skills of other and vice versa (Yan & Luo 2001).

#### **3. 3.2.2 Market Power & market experience**

The joint venture can be immensely facilitated by already established parent firm in the local market. An appropriate local partner is the one that brings strong market power to the joint venture. If chosen properly it can improve the skill of the joint venture to use local networks, increase local market commitment and give more bargaining power to negotiate with government and other stake holders (Yan & Luo 2001).

### **3. 3.2.3 Product Relatedness**

Product relatedness between the foreign and local partner can create some unique benefits which is not possible in the case of diversified products. The existing marketing channels, distributors, agents and suppliers of the local partner can be used. The customer loyalty with the local partner can be exploited and the relations with the government agencies can be used (Yan & Luo 2001).

### **3. 3.2.4 Firm size**

The capability of a firm to contribute in the survival of a joint venture is clearly dependent on its firm size. Large firms can contribute more in removing the entry barriers, reducing risks and achieving economies of the scale for joint venture. The managerial perspective is different the large firms in the form of over sea conglomerate may not give as much strategic attention and importance to the joint ventures as by smaller firms (Yan & Luo 2001).

### **3. 3.2.5 International business experience**

The way of doing business and commercialization is different in different parts of the world. Therefore, lack of trust and misunderstanding may occur between the partners. The international experience of partners can help them to understand each other and helps them to adjust with each other (Yan & Luo 2001).

### **3. 3.2.6 Previous corporative experience**

The previous experience between the partners certainly increases the chances of the success. It will strengthen the relationship if partners already know and understand each other. The embedding of this power to the joint venture increases its chances of success (Yan & Luo 2001).

## **3. 3.3 Financial Traits**

The different aspects of the strategic fit which plays important roles are discussed below.

### **3. 3.3.1 Investment assessment and capital budgeting**

The effective investment assessment and capital budgeting is critical for the success of joint ventures. It is necessary for the local partner to understand the effective allocation of the financial resources in the host country as these capabilities are highly country specific. The complexities of investment increase in cross country relationship so it heavily depends upon the ability of the local partner to understand the investment opportunities in the local country and act accordingly (Yan & Luo 2001).

### **3. 3.3.2 Financing Ability**

It is difficult for foreign investor to get financial resources in the local market. Therefore, the ability of the local partner to maintain relationships with local financial institutes is really important. The foreign investor investigates the ability of the local partner by checking these

three areas. (1) Cost control ability, to increase revenue and reduce taxes and expenses and maximize operational efficiency. (2) allocation and utilization of capital which includes the ability to allocate and use working capital, attain local financing, use and control debts, and managing risks (3) assets management, including the ability to optimally deploy assets and resources, manage accounts receivables and cash flows and manage fixed and intangible assets (Yan & Luo 2001).

### **3.3.3.3 Exposure Hedging**

In dynamic and volatile host markets it is difficult to operate business. It is especially difficult for any foreign firm to maintain its cash flow and all the sources of income in such an environment. In these circumstances a local partner with the capabilities to handle these circumstances and reduce risk for the joint venture is desirable (Yan & Luo 2001).

### **3.3.3.4 Risk management**

International joint ventures stability and pattern of growth depends on the risk sharing ability of its partners. For example the currency rate fluctuation can effect on earnings and cash flows.

Management of currency rate fluctuation is really important because its area of effect is really large. It affects the return value to the international partner. It involves timely, frequent and sometimes even strategic decisions. Like the decision to adjustment of operation variables like pricing output and sourcing. The bigger decisions like altering assets ownership structures, relocating plants, and restructure the entire organization sometimes needed to be taken to cover this risk. To understand and handle such crucial risk partners need each other's ability of risk management (Yan & Luo 2001).

Inter partner fit is necessary for the success of joint venture. Strategic organizational and financial traits of the partners should be complimented and congruence for the inter partner fit. All strategic, organizational and financial traits are necessary for joint venture success. Any partner lacking in any of them can make the joint venture unstable and resulting in the failure of the business (Yan & Luo 2001).

### **3.3.4 Inter partner fit at the operational level**

It is advisable for the firms to look at the above described static characteristic of their future potential partners before going into a joint venture but these only are not enough. It is also of equally important to see that how the partner firms work together in their daily operation. It

has been said in the literature on the internationalization of the companies that the companies from similar country culture are more successful in joint ventures. But even the joint ventures between the countries like America – Britain, China – Japan and France – Italy have operational problems. To ensure the success of the joint venture by ensuring inter partner fit we need to look at the operational level criteria for partner selection (Yan & Luo 2001).

Operational level criteria for inter partner fit includes: compatibility of partner goals, complementary resources, commitment of the partners, and partner compatibility (Yan & Luo 2001).

### **3.3.4.1 Goal Compatibility**

The difference or resemblance between the partners about their goals affects the performance of the joint venture. The issue that how well-designed the considered deal concepts are behind a joint deal or how talented the participants are, is of less important than the ability of the allies to be competent enough to work together. Goal consistency harmonizes the interests between the firms that would otherwise give way to opposed sub goals pursuits. The firms should evaluate the goals of other firms to be in joint venture and dig out whether they are compatible with their own goals or not. The more similar goals increase the cooperation between the partner it is easy for one partner to predict the behavior of the other in any situation. It will increase the financial and operational synergies between partners. This will certainly increase the commitment of partners that will certainly increase the possibility to invest more resources into it (Yan & Luo 2001).

The conflict of goals ultimately arise the conflicts between parent organizations which will harm the performance of the joint venture and put a question on the stability of the joint venture. The firms may come into the joint ventures with different intentions. The firms from a specific geographical area usually have common needs to go into the joint venture. The firms from Japan seek joint venture to learn product innovation from Western firms while western firms want to learn process innovation or want market expansion. The firms from China take joint venture as a source to learn and acquire new technologies and the foreign firms wants to explore the market expansion opportunities in the Chinese home market. These goal differences convert into inter firm conflicts. This clash of goals discourages the partners to share their resources and this is one of the major reasons of joint venture failure (Yan & Luo 2001).

This is not necessary that only identical goals are the sign of compatibility. The firms usually go into the joint ventures to overcome their weak areas. It is natural for the firms to have different expectation from joint ventures. As long as the firms respect each other's goals and

the goals of one firm are not in direct conflict with other firms goals .The firms with different sets of goals can form a successful joint venture and the strategic expectation of both the companies can met simultaneously (Yan & Luo 2001).

#### **3. 3.4.2 Resource complementarily**

The more resource complimentarily between the parent firms the higher will be the functional and operational synergies in the joint venture. Resources complementarily also reduces governance and coordination cost stimulates information and most importantly improves the learning curve (Yan & Luo 2001).

#### **3. 3.4.3 Commitment**

Commitment of partners within joint venture is most important element. All other things have nothing to add if commitment is missing. It means that how much consideration a partner gives to the joint venture. The joint venture is a continuous journey of trust building among the partners. The lacks of commitment from partners disturb this trust building process. If partners are not committed then the minor conflicts may convert into big problems and disturb the entire joint venture (Yan & Luo 2001).

#### **3. 3.4.4 Capability**

Any partner who can help the firm to overcome its weakness to achieve business objective is a desirable partner. The partners with multi faceted and distinctive capabilities are welcome, without distinctive capability it is not possible for the partner to create value for the joint venture.

Firms may be weak individually lacking in different skills but collectively they can be powerful. Partners need to determine which particular capability they require from each other. The managers must seeks uniqueness in the relationship and this uniqueness is of three types “(1) unique capability that cannot be traded easily across companies (2)unique capability that cannot be easily substituted (3) unique capabilities that cannot be easily developed or replicated with a reasonable time frame” (Yan & Luo 2001).

#### **3.3.5 Guiding principles of partner selection in a joint venture**

Success of the joint venture depends on partner selection process. The more meticulous and regimented the partner selection process, the more successful the joint venture. According to Emerson Electric’s Chairman and C.E.O, Charles F. Knight, “when certain rigorous pre and post venture guidelines are followed you can succeed where others have failed” (Yan & Luo 2001).

Seven guiding points which should be considered by any firm going into the joint venture while selecting a partner are;

1. The capabilities of the potential partners should be judged by a team of professionals. This team of professional contains persons from every field like financial, operational and marketing professionals (Yan & Luo 2001).
2. Partners assessment should not be based on partners own description. Some companies like Emerson Electric form two teams one is in the favor of joint venture and the other is to oppose the joint venture (Yan & Luo 2001).
3. Partner selection should be incorporated with the focal company's strategic goals (Yan & Luo 2001).
4. Potential joint venture firms should obtain as much information as possible about their potential partners (Yan & Luo 2001).
5. The existing corporative relationship should be preferred in the quest of joint venture partner (Yan & Luo 2001).
6. It is advisable to collect first hand information during site visit. The employee mindset, morale of managers, operational efficiency, technology, equipment, cash flow, over all financial health and the effectiveness of the management system should be observed immaculately. Several candidate firms should be visited to increase the bargaining power. The government officials if involved should be visited early for the collection of first hand information (Yan & Luo 2001).
7. It is important to understand as early as possible the intention of the other partner about the joint venture. Why the other firm wants to be in joint venture, what are its goals and dose its goals collides with ours or partnership joint goals (Ibid)?

### 3.4 Factors effecting entry modes

The numerous factors which affect the entry mode of the firms for internationalization can be generally divided into two groups.

1. External Factor
2. Internal Factor

These factors are further explained below.

#### 3.4.1 External Factors

The firms should consider these external factors while choosing the entry modes are discussed below.

##### 3.4.1.1 Socio-cultural Distance

Socio-cultural difference is one of the most considered areas as Jansson (2007) and Backlund & Suikki (2005) suggests that countries having greater cultural difference often give a thought to firms not to enter through direct investment but joint venture. Companies tend to choose entry mode that have low risk and provide flexibility.

#### **3.4.1.2 Country Risk & Demand uncertainty**

Stability and return on investment are the most important issues for any investor investing in business. Country's political situation is an important factor while choosing entry mode because it forecast not only the return of the investment but future stability in business. Company normally restricts their investments in high uncertain areas and goes for joint ventures to make sure the return of investment (Jansson 2007) and (Backlund & Suikki 2005).

#### **3.4.1.3 Market Size**

Firms seek new markets to invest to grow their business. In the hunt for the new opportunities firms usually prefer big markets. The firms should not leave small markets because one day they will grow and turn into be big markets. Moreover small markets should be preferred because of the less competition (Huyett & Viguerie 2005). The size of market is an important constraint for the decision of entry mode. Low size markets often handle through intermediaries. Firms increase their investment in large size markets through establishing subsidiaries or joint ventures (Jansson 2007).

#### **3.4.1.4 Trade Barriers**

While entering in foreign markets the trade barriers can affect the entry mode selection decision. The examples of trade barriers include government restrictions and quotas system also affect the decision making of entry mode. For example if a country restrict wholly owned business by FDI then firms choose alternative options like joint ventures to enter in market (Jansson 2007).

#### **3.4.1.5 Competitive Environment**

Competition in the market is natural and firms have to look on it while deciding the entry mode to enter in foreign markets. Market with high intensity of competition limits the investment choice of a firm. Generally, firms avoid heavy investment in those markets where competition is already high (Jansson 2007).

#### **3.4.1.6 Geographical Distance**

The world is turning more and more into global village but geographical distances are still here and needed to be considered. They influence every day business transactions. According to Backlund & Suikki (2005) geographical distance between home country and foreign market play an important role on the choice of entry mode. Like if the distance is high, the cost of transportation increase which helps firm to plan to open a subsidiary or joint venture in foreign market. This factor becomes highlight when it comes to emerging markets where labor cost and raw material cost is quite low.

#### **3.4.2 Internal Factors & Foreign Entry Mode**

Now we will discuss some important internal factors and see how the firms are being affected with them while taking the entry mode decision.

##### **3.4.2.1 Cost & Pay Back**

Firms especially SMEs have limited resources. According to Backlund & Suikki (2005) the cost of an entry mode is critical because firm's financial budget effect the decision. This is one of the reasons to avoid SMEs by establishing a subsidiary in foreign market.

##### **3.4.2.2 Long term Profit Objective**

Firms want to establish their business in the market for a long time specially when they are moving to a foreign market. Intensions and expectations from future in foreign market act as a guide line for firms to choose entry mode.

##### **3.4.2.3 Company Size**

SMEs as being small in size have to face some unique restrictions in the decision of choosing entry mode for the foreign market. According to Jansson (2007) and Jansson & Sandberg (2008) SMEs consider lack of necessary resource to enter in foreign market because of small size of the firm. As an SME, the choice of entry modes for foreign market becomes limited.

##### **3.4.2.4 International Experience**

Internationalization experience acquiring is a gradual learning process. SMEs generally adopt certain pattern to acquire knowledge regarding international experience before exposing to foreign market. The internationalization process considers a detail method to understand the way firms think while doing business in abroad. Having low experience of

internationalization, may bring firms in a situation to go for intermediaries (Jansson 2007) (Jansson & Sandberg 2008).

#### **3.4.2.5 Control**

As discussed that intermediaries does not provide a strong control over customer or market. Intermediaries want foreign firms to remain dependent on them. If firms want to increase their control in foreign market and direct contact with customer then the option of entry mode is joint venture or subsidiary. On the other hand joint venture provides the liberty to limited control due to more than one parent company (Jansson 2007) (Jansson & Sandberg 2008).

#### **3.4.2.6 Risk**

If firm unable to take too much risk which is obvious when entering in foreign market than joint venture or intermediaries are the remaining options because in subsidiary the risk ratio increases significantly. Although great risk come up with large returns but sometime things end up in different ways (Jansson 2007) (Jansson & Sandberg 2008).

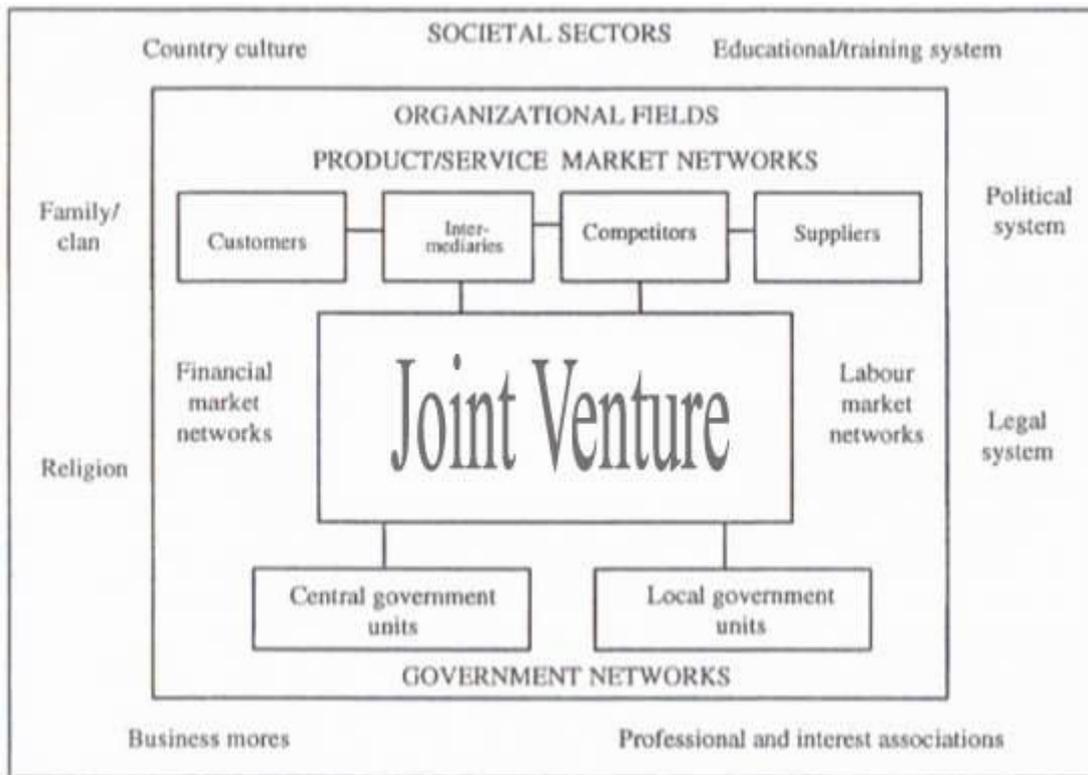
#### **3.4.2.7 Relationship**

If a firm wants a close relationship with its customer in foreign market, the choice of entry mode might be sharing the resource with other firms like in joint venture or building a subsidiary. First option provides benefit to SMEs (Jansson 2007) (Jansson & Sandberg 2008).

### **3.5 Scanning the Host Country Business Environment**

The global surroundings are turned into a playing turf consisting of institutions where market and societies are looked upon as rule systems that the business firms follow. The firms looking to develop their business in foreign markets have to deal with two types of rules in the host country. One is the official set of laws set by the governments and the other is the unofficial set of laws set by society (Jansson 2007).

The International Business Marketing model by Hans Jansson is helpful for the firms to scan the host country environment and make them able to plan the most appropriate strategy. We made some small modification in the model to use it for the joint venture study in India. It will help us to conclude in the coming parts that how firm can be affected by the different actors surrounding the business environment of the firm. It is important for the firms to scan the host country business environment because the rule systems of a specific market might facilitate or hinder the establishment and flourishing of the firm business (Ibid).



Source: Jansson (2007), International Marketing Business Model (Modified version).

### 3.5.1 Institutions

The society is composed of different social groups. These social groups characterized to form institutions on the basis of different rules. The behavior follows the specific rules innate in it. The organization of different parts of the society is influenced by each other. The reason of this is that the behavior of a specific group is not only influenced by inside rules but also by those of other social groups.

Institutions are viewed as different kind of rules that govern business marketing in a certain country market. The examples of important rule system are culture, political system, trade unions, business network actors that is in direct contact with Firm. The regulations, laws and the religious norms or rules might encourage or hinder incentives for innovation and commercial activities (Jansson 2007).

### 3.5.2 Firms Strategy and importance of Institutions

The firms need to learn about the institutions to predict about the behavior of the different actors of the market. This is important for the success of all the firms. The importance of this learning is tremendously high for the firms moving from mature to emerging markets.

The institutional factors influence the strategies between actors. Business judgment process is linked and bound by different actors in specific managerial fields for example product/service market is linked with customer, competitors, financial markets and governments. In this inter play the institutions and business markets both influence each other (Jansson 2007).

### **3.5.3 Basic rules and country culture**

The four major rules norms, values, thought style or cognitive factors, and enforcement mechanism or regulations governs the behavior within an institution. Basic rules such as valuations, norms and cognitive structures in organizational fields are therefore influenced by such basic rules of societal sectors, for example the national culture of the country. The culture can be divided into four factors: country culture, family/clan, religion and business norms (Ibid).

### **3.5.4 Indian Economic Conditions**

India is the fifth largest economy and has the third largest GDP in Asia. The GDP has touched US\$1.25 trillion. India with this growing GDP is included in 12 elite countries with trillion economies. The growth rate in GDP was 6.4% during last 10 years. India is the second largest country among emerging nations. Due to its large size of market, India provides high prospects for growth and earning potential in business. India is one of the BRIC countries. These BRIC countries Brazil, Russia, India, and China are known for their fast growing economies. India is a politically stable country and provides high rate of return due to government liberalized policies toward foreign investment (rediff.com). The labor pool of the country received significant attention from multinational organizations due to its quality. Indian government formed a policy for setting up special economic zones (SEZ). The purpose is to increase the investment in India by providing tax incentives, protection against anti business labor laws and regularity requirements (tradechakra.com) (sezindiainvest.com). U.S Department of Commerce named India as one of the big emerging markets where skilled and English speaking labor is easily available. According to Jeff Immelt chairman of General Electronics, India's actual treasure is its strong intellectual capital (Rathinasamy, mantripragadaKrishnan & Shivaswamy 2003).

### **3.5.5 Political Risk in India**

India is a politically stable democratic country where transition of power remains smooth. The business policies continuously improved in every government era. Good friendly Political contacts consider a benefit in Indian society and provide help to resolve the issues at official level (Rathinasamy et al. 2003).

### **3.5.6 Social, religious and culture climate of India**

India is the second largest country of the world after China having diverse cultures, languages and religions. Hinduism is the dominant religion practiced by 80% of the population. There are several minority religions like Islam, Christianity, Sikhism and Buddhism. Even though the dominant population is Hindu, country has no religion at state level and provides equal security and human right to every citizen of the country without considering religion. There are some occasional violent encounters between different communities especially between Hindus and Muslims but never represent the image of whole society where coherence can easily be found (Rathinasamy et al. 2003).

India has many languages and country is actually divided into different states on the ground of language. The national language is Hindi and official language is English. Both languages Hindi and English are easily understandable all over the country which provides a strong benefit to foreign companies to do business without facing any language problem (Rathinasamy et al. 2003).

Indian Culture is one of the oldest cultures and based on traditional values. Despite of old traditional, people are easily adoptable to modern business practice. Even though people are generous but it is important for foreign investor to understand the local values like attitude toward religion, respect of women, greeting people with folded hands. People are more family oriented. Foreign firms must understand the behavior and preferences of people for example initially American firms make a mistake to consider that taste and preferences are universal (Rathinasamy et al. 2003).

### **3.5.7 Indian Management Style**

India is a hierarchical society and management style is influenced by this hierarchical system which slows down the decision making process. Respect to seniors and old age people remains valuable asset for the people. Decisions come from managers and subordinate have to oblige them even if they know that it is wrong. Indian system is based on close ties between individualism where people like to work in groups. Authority is based on seniority and inequality between different individual can be seen on work place. (Soderlind & Kidby 2005).

Time is not a very important and prestigious standard in Indian business system. People normally didn't take it seriously and feel that they have lot of time. They consider timeline as a guideline and being late is not considering a big deal (Soderlind & kidby 2005).

Indian system is more trust oriented and people consider less importance to legal system. The word of mouth consider sufficient for an agreement. Managing Indian people need micro level management where manager closely observe and control the work of its employees. Indian people try to know each other before starting business dialogue and believe on face saving (izzat). Practically people tend to go for long term business relationships and building trust is essential between partners. Gift or reward culture is very common in Indian society and people use this technique for personal service and generally not regard as corrupt. Indian system is very slow and one must have the patience to get the benefit. Most of the foreigners take it hard to understand. Nepotism is widely seen as positive and people openly practice it (Owen & Purohit 2007).

The great cultural difference between India and West require a great deal of consideration before entering particular market.

## 4. Empirical Study

This section contains empirical facts about joint venture problem and current Indian Conditions both from the primary and secondary sources. This chapter is neutral collection of data. The data about a common issue is collected both from primary and secondary resource without any own value or stand point.

### 4.1 FDI in India

Indians welcome foreign investor to invest on their soil. Indian authorities allow foreign direct investment in four ways. These four ways include financial collaboration, joint venture and technical collaboration, capital markets via euro issues and through private placements or preferential allotments. Foreign companies can hold equity up to 100% like wholly owned subsidiary depending on the industry. Foreign investment can come in any sector depending on the equity except retail trades type of single brand retail, atomic energy, lotteries, gambling and betting, housing and real estate business and certain types of agriculture (investinindia.in) (GOA 2008).

#### 4.1.1 The FIPB approval

The foreign investor has to take approval from FIPB for investment in India. FIPB stands for Foreign Investment Promotion Board which process and deal all non automatic approval cases. Board takes 4 to 6 weeks for processing. Once investor receives approval from the board he/she must notify RBI in 30 days of receipt of inward remittances and within 30 days of issuance of shares to foreign investor (investinindia.in) (GAO 2008) (madeingermany.de).

#### 4.1.2 The approval by Reserve Bank of India

The Reserve Bank of India is the appropriate authority to grants approvals for FDI after the approval of Foreign Investment Promotion Board (FIPB). It takes two weeks and foreign equity up to 24%; 26%; 49%; 50%; 51%; 74%; and 100% can be granted depending on the industry and sector. Investors have to notify RBI within 30 days of completing the transaction, regardless of equity percentage (investinindia.in) (GAO 2008) (madeingermany.de).

### 4.2 Foreign Investors Business Formats

Foreign investors have five possible formats to setup business in India. These options include wholly owned subsidiary, Branch Office, Project Office, Liaison Office and Joint Venture.

Indian law allows joint venture to register as a new firm in the form of public or private limited. Investors find it more appropriate to remain as private limited company because private limited company is exempted from many legal obligations. The Private limited joint ventures secure the controlling interests and rights of both Indian and foreign investor better than public limited joint ventures.

### 4.3 Indian Laws and Regulations

The government of India (GOI) liberalizes its foreign investment policy since 1991. Government realizes the importance of FDI and develops detailed policies to attract foreign investors (GAO 2008).

#### 4.3.1 Foreign Exchange Management Act (FEMA)

The Foreign Exchange Management Act (FEMA) considered as the set of primary laws for foreign investment. These laws provide legal authority to Indian government to restrict foreign investment. It was not a complete document to deal with implementation so Government Issue press notes separately for each sector (GAO 2008).

#### 4.3.2 Department of Industrial Policy and Promotion (DIPP)

These press notes released by department of Industrial Policy and Promotion (DIPP), subsection of ministry of commerce and industry. These press notes decide how much equity a foreign company can have. The percentage is varies sector to sector (GAO 2008).

#### 4.3.3 Government officials interference

Foreign policy restricts foreign nationals to invest in Indian stock markets. Although Indian foreign investment policy based on legalized frame work but ministries can interfere and influence on decision of the approval especially when it comes to FIPB, this issue is often happens when investor belongs to countries of concern try to invest in sensitive sector, this intervention is on ad hoc basis (GAO 2008).

#### 4.3.4 Joint Venture Law Discrimination

Any foreign company can register itself in India under approved equity and operate under same laws and regulations as any Indian owned firm would. There is no discrimination in law against foreign company's registration process. There is a small restriction for the companies who enter in business through joint venture with an Indian partner. If foreign firms want to set up another company in the same sector it must require a no objection certificate from its JV partner (Foreign Investment India 2002).

Although Indian legal system allow 100% foreign equity but a joint venture with a local partner is preferred especially for SMEs due to the organization needs, local partner awareness of local market, natural and human resources and most importantly easy exit.

#### **4.3.5 Flaws of legal system**

The Indian legal system is considered a better system but sometimes formal procedure takes too much time to make a decision. Companies face trouble of tax levied, transportation goods from one state to another where cost and time delay occurs in the form of loss (Foreign Investment India 2002).

### **4.4 Intellectual Property Rights in India**

GOI considers IPR as an important issue and continuously improve the enforcement of laws about IPR. India is a member of World Intellectual Property Organization (WIPO) UN agency and World Trade Organization Agreement which contain agreements on Intellectual property as well. India is also the member of few major treaties namely as Paris Convention for the Protection of Industrial Property, Berne Convention for the protection of Literary and Artistic Works and Patent Cooperation Treaty (PCT) to deal with IPR (<http://dipp.nic.in/ipr.htm>).

#### **4.4.1 Department of Industrial Policy & Promotion**

The Department of Industrial Policy & Promotion (Dipp) control and approved IPR applications through Office of the Controller General of Patents, Design and Trade marks (CGPDTM). Dipp also setup an Intellectual Property Appellate Board (IPAB) to hear the appeals against any decisions made by CGPDTM. Indian court show proactive measures since 2005 against counterfeiting. Courts give protection to trade marks even if they are not registered in india (<http://dipp.nic.in/ipr.htm>) ([http://www.indianembassy.org/policy/ipr/ipr\\_2000.htm](http://www.indianembassy.org/policy/ipr/ipr_2000.htm)).

#### **4.4.2 Flaws of Intellectual Property Rights implementation in India**

The Government took strong measures regarding IPR issues but loop holes are still present in the system. The proceedings take too much time which causes the loss of time and money. The lack of trained officials regarding IPR issues create problem which also effect the enforcement of IP regulations. The presence of corruption highly effect on the decision making and performance of the system([http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc\\_143739.pdf](http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc_143739.pdf)).

The overall condition of IPR improved due to the amendment in the patent act during last decade. Due to progressive involvement of Indian government, country consider favorable for foreign investors.

#### 4.5 International property rights index

The international property rights index considers India as an average country and in green zone. The index is primarily based on three core components legal and political environment of the country (LP), Physical Property Rights (PPR) and intellectual Property Rights (IPR). Legal and political environment play a major role for the legislations and implementation of any rights and consider a much broader term of rights. The other two components are the share holder of economic growth. The index discusses the 11 major areas of any country including corruption, rule of law, stability, judicial independency, all kind of protection to IPR and PPRs. Sweden is positioned second ranked with 8.5 grading with Denmark in this index after Finland. India is holding 53<sup>rd</sup> position in this index with 5.5 grading and providing a strong argument of economic growth in the country. However the document considers the situation is negative compare to last year ([www.internationalpropertyrightsindex.org](http://www.internationalpropertyrightsindex.org)).

#### 4.6 Exporrådet / Swedish Trade Council India: Swedish Official View

Swedish Trade Council provides support to Swedish companies to grow internationally since 1972. STC consider as official entity of Swedish government for business and commerce in India. STC has detailed market knowledge regarding Indian market therefore, hold a strong view point based on its experience. Ricky Dhillon is the representative of Swedish Trade council in India. His every day job is to deal with the problems faced by the Swedish Business community in India below is his comments on problems and opportunity in India.

##### 4.6.1 India as a soil of opportunity

Ricky said that in spite of the Nemours problems faced by Swedish business community with regards to culture, legal problem and bureaucracy STC didn't find any single person who wants to leave India rather people wants to expand their business in India. STC considers India as the land of opportunity.

##### 4.6.2 Joint Ventures as an option to do business in India

STC did not recommend Joint venture as a good option for Swedish firms in Indian market. STC considers joint ventures are much risky, conflict oriented and lack of control. Swedish investor faces problems while working in India in joint ventures due to cultural difference

and management style. Moreover, STC considers Indian market as a great opportunity for Swedish while opposing joint venture as an entry mode.

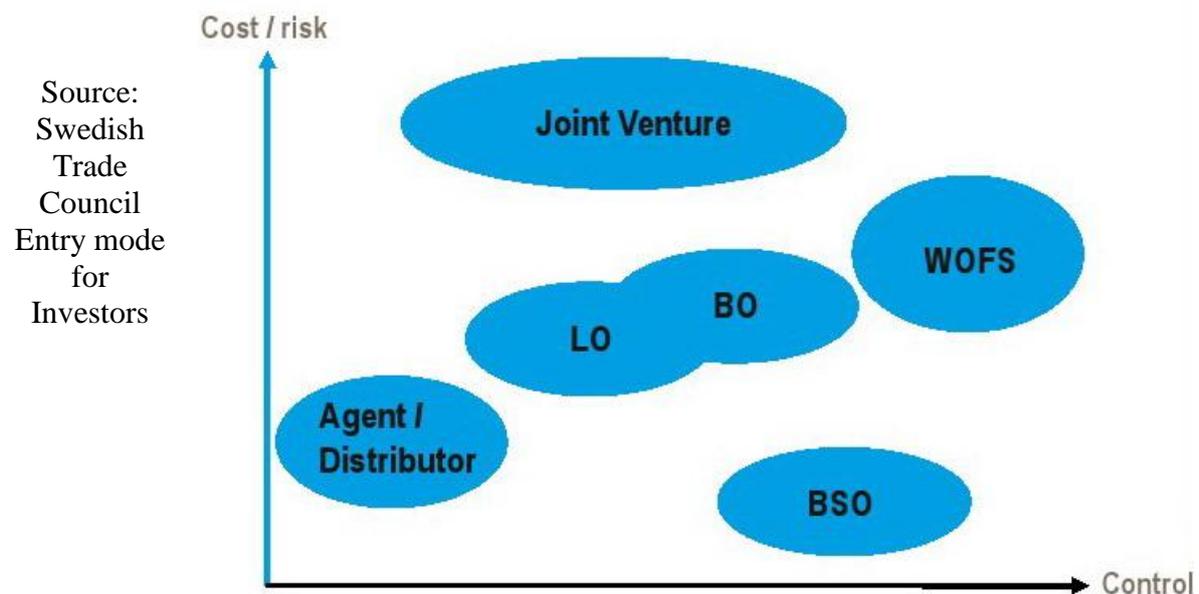
#### 4.6.3 Subsidiary as an option to do business in India

According to STC representative Ricky, wholly owned subsidiary is a good choice for Swedish firms to have full control and get pros and cons of the market. Rickey further describes that by establishing wholly own subsidiary Swedish investor will avoid problems because of cultural and management style differences.

#### 4.6.4 Business Support Office (BSO)

Furthermore Swedish trade council launches a program named Business Support Office (BSO) for Swedish companies in India. That is a new phenomenon and provides all kind of supports (sale support, virtual office in India, Sourcing support, Employment service etc.) to Swedish investor in Indian market. The responsibility of STC is to evaluate the entry mode according to the need of investor. STC regard joint venture highly risky and therefore, consider the last entry option.

### Entry Modes Comparison between risk and control



#### 4.6.5 Major

##### Problems in India for Foreign Investor

According to STC representative, three major problems Swedish companies face in India are bureaucracy, corruption and the taxation system. Bureaucracy have high influence on

procedures and responsible for slow process. Indian business style is different from Swedish, so it is important for firms to understand the local market and people behavior.

#### 4.7 Taxation problem with joint ventures

According to the Swedish-India Business Guide 2009-10 Published by SCCI Joint venture is slowly becoming less prevalent due to other options of business. Joint venture is treated as local company for tax purpose. The tax rate is currently 30%+10% surcharge

#### 4.8 Employment cost in India

In case of employment cost India is very cheap for production and other labor works for example employment cost is US\$ 1.12 per hour which is quite low and skillful as well. It is analyzed that those Swedish companies work in India less affected by current economic crisis due to the big Indian market size (<http://scci.aallton.se>).

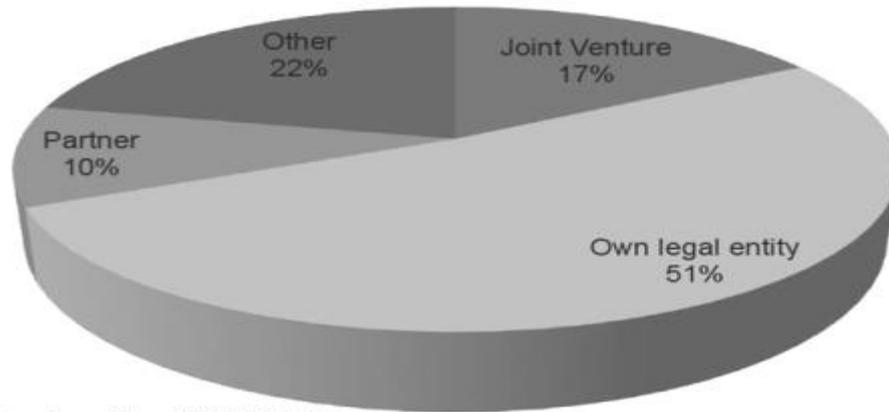
#### 4.9 Business Climate Survey (2009)

Below are some facts about Indian business environment. These facts are taken from the Business Climate Survey (2009) jointly published by Swedish Chamber of Commerce and Industries and Swedish Trade Council.

##### **4.9.1 Swedish Business Situation in India**

According to Business Climate Survey (2009) report jointly published by SCCI and STC shows that 108 new Swedish subsidiaries established in India till may 2009 and 775 Swedish firms involve in import/export business.

India is the 19<sup>th</sup> largest market for Sweden. Report concluded that Swedish companies choose wholly own subsidiary as a prominent option to enter in India and only 17% firms engage with any type of joint venture. Report also conclude that every second Swedish firm choose wholly own subsidiary as entry mode.



Source: Survey Climate 2009 SCCI & STC

#### 4.9.2 Cultural Problem

According to Business Climate Survey (2009) corruption rate is very high in Indian society. Companies must be aware of that issue before entering Indian Market. Foreign Companies need great patience in Indian market because response time is not so quick in India from officials. India is a large country and having different dynamics; companies need a detailed market research including regional difference inside the India. Although English is the official language and everybody understand it but local people and advisor required when companies want to establish business in India. People are price conscious and demanded to lower down the price even if the prices are mentioned on product.

#### 4.9.3 Major Problems in India

According to the Swedish-India Business Guide 2009-10 Document concludes about the major obstacles in Indian market faced by Swedish companies. Most importantly companies dissatisfied because of bureaucracy, corruption rate, complex labor, high tax rates, complicated legal and regularity system.

Regularity and tax regulation varies state to state which results situation into complicated. Indians are very slow mover and foreign companies often face problems working in India due to cultural difference. Document suggests that patience is very important to do business in India. Companies prefer to do market research before entering Indian market. Moreover foreign companies need to understand socio economic values and difference of culture in different states. Infrastructure and environmental conditions are very poor and need attentions during transportations.

#### 4.9.4 Growth Potential of India

India has a huge growth potential due to its market size. Foreign investor must have long term planning to exploit the opportunities. India is the source of highly skilled and cheap

labor provides great production facilities. People are very price conscious but market climate is profitable. Foreign companies can establish their business and maximize the profit by developing India specific strategies and solutions.

#### 4.10 Interview with Amokabel (Case Company) Representative

##### 4.10.1 Amokabel in India

Amokabel is one of the leading cable manufacture of Sweden formed a joint venture in India with Elcomponics. Elcomponics is one of the leading harnesses manufactures in India and old customer of Amokabel invites company to establish business in India under mutual cooperation. Amokabel was also interested to remain close to its Asian customers. At that time cable manufacture companies were not allowed to enter in Indian market with wholly owned subsidiaries. Joint venture was the only possibility for Amokabel to enter in Indian market. Amokabel had 49% shares of the jointly owned company. The ambition had always been to increase the sale volume and make money. The joint venture ends up with failure due to various reasons. Henrik Blad worked as the Vice MD of that Joint venture firm and shares his experience with us below is his comments:

##### 4.10.2 Advantages and disadvantages of Joint Venture

According to Amokabel, joint venture is the worst form of doing business and should be consider as the last option. But at the same time Indian situation is restricted European and American companies to enter in business with wholly owned subsidiary in most industries and joint venture remain a strong option. The advantage of joint venture is to provide a chance to enter in Indian market even for small medium enterprises having limited resource. It will also helpful to divide the responsibilities and exploit the local market knowledge. The disadvantage of joint venture is having lack of control and foreign companies always dependent on local partner. The difference of culture and working style results worst outcomes.

##### 4.10.3 Partner Selection

According to Amokabel, partner selection is very important in joint venture. Foreign firm should do home work carefully to verify partner's strength. Finding a good partner is important in this process.

##### 4.10.3.1 Public & Private sector partnership

According to Amokabel, Joint venture with public limited company is different from the venture with private limited. Public limited firms use modernize way of working and know the international requirement instead of private limited firms that consider old fashioned.

#### **4.10.3.2 Goal Compatibility**

According to Amokabel representative, it is important for partners to have same strategic goal. In Amokabel case bad selection of partner and having different business motives ruined the joint venture.

#### **4.10.4 Role of consultancy firms**

Companies can hire consultancy firms to write down each and every detail in agreement. So both parties clearly know the responsibilities. Partner should be fair to each other and transparency must be present there in order to make joint venture successful.

#### **4.10.5 Managing Responsibilities**

According to Amokabel, The management responsibilities should be clearly defines between the parent firms. Once the responsibilities are decided every party has to fulfill his part. Major decision took place by board of directors. In case of Amokabel joint venture, local partner did not market the product and failed to fulfill his responsibility.

#### **4.10.6 Decision making process**

According to Amokabel, important decisions should be taken collectively with the concern of all partners. Company have a very bad experience of decision making process in India where the senior partner takes the decision without concerning middle or top management. This issue will be further discussed more in the next coming parts of Henrik interview.

### **4.11 Indian Culture & Management Style**

Indian culture is very interesting and Henrik wishes to go India again but at the same time Amokabel suggests that the foreign investors going to India should be aware of Indian business behavior.

#### **4.11.1 Written agreements**

According to Amokabel, culture and business behavior is very important. If any firm want to enter in joint venture in India they might face difficult to control. Indian people try to manage things in Indian way. They did not really care about written agreements. One man show in private limited companies can easily be seen and effect on decision making process even in joint venture.

It is important for companies to have knowledge of Indian behavior and culture before entering in India. As Amokabel shares its own experience that according to the written

agreement their part of the responsibility was to manufacture and marketing was the responsibility of the other partner. Henrik said that when we manufacture the product we came to know there was no customer. In Amokabel point of view communication and transparency can save the relationship.

#### **4.11.2 Middle management**

Amokabel considers Indian middle management as hard working and committed. Henrik Blad, The MD of Amokabel still remembers and loves his staff in India. He feels sorry for them that they work even double than the Swedish middle management but their salaries are less than half of Swedish middle management salaries. He considered that top management was the trouble maker and did not follow the procedure. He again suggested that it is important to choose right partner.

#### **4.11.3 Poor time management**

In Amokabel view Indian people do not give due importance to time. Indians have time wasting habits like they waste too much time in doing unnecessary paper work and long meetings end up with no results. Henrik shares his own experience that he has three or four meetings with MD to improve the situation but result was none. “He left us alone to do all things in Indian market”.

#### **4.11.4 European Indian business norms conflict**

Henrik thinks that European people are organized and rule oriented and most of the time faces difficulty to work with Indian partner. Even the big firms like Electrolux face the same problem. Indian partners make decision out of the office especially in private or family owned companies.

Amokabel do not consider language or communication as a barrier or hurdle to do business. Company considers other conflict of preferences as a major hurdle. The examples of these conflicting areas are in terms of policy, control, authority, responsibilities and commitment to the business and work.

#### **4.11.5 Legal System**

According to Amokabel, the bureaucracy is very strong in India that is the big problem. The legal formalities took lot of time. That is one reason of having less importance of agreement in joint venture. It is hard to contact and hire legal service in India if foreign companies have any dispute with its partner because. It took lot of time and money and SMEs do not have that many resources to stay and look for the results.

#### **4.11.5.1 Exit Strategy**

Amokabel suggests that foreign firms should decide an exit strategy with its partner before establishing business. In Amokabel case, company still owns 49% shares of joint venture in India. Amokabel left all invested money and resources in total loss in India because of having no exit strategy and it is really difficult to involve and handle legal matters in India because of Indian legal system.

#### 4.12 Interview with Swedpartnership Representative

According to Swedpartnership program officer Mr. Nils Marcks Von Wurtemberg doing business in subcontinent require cultural knowledge. The study of culture before entering in Indian market is strongly recommend due to the great difference between Swedish and Indian way of perceiving things. Many people live in one house as a family represent the close ties between people and increase the expectation of favoritism in the society. Indian people are quite humble, friendly and generous and want to communicate. People are much socialized and tend to believe that people who come in India want to see Indian traditions.

Nils while sharing his personal observations told that hiring women on jobs is quite hard and did not consider as long term planning for any business. One reason behind this mind set is women quit jobs after marriage which is typical Asian way to look up at things. In Asia and especially men consider responsible for the earning and women consider responsible for managing houses. It is odd for women to do jobs after marriage. Again, it depends on area because in modern area like Mumbai, Delhi women are more involve in jobs than other cities. He considered Indians less materialistic than Swedish and think that it is a reason that Indians waste too much time.

#### 4.13 European Commission Survey about Business Climate in INDIA

The survey was conduct in 2008. It is based on responses from different foreign firms, representative offices, European Delegations and Member states Embassies. This Survey mainly covers the area of IPR and the bureaucracy process in India and describes the perception of foregin investor ([http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc\\_143739.pdf](http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc_143739.pdf)).

Few findings from this survey about current situation of Indian business environment are mentioned below.

##### 4.13.1 IPR Issues

India is improving in protecting IPR however few responses show that firms some time face IPR infringements. These infringements mostly seen in the terms of patent, trademarks design and copy right which effect company's local sales and production. Companies experience that most of the time infringements happens against the registered IPRs inside the country. In most cases it is easy to identify the infringer. Although government policies are very clear about IPR issues and companies legally have the protection against infringements but the commitment and efficiency rate is below average. Foreign companies face problem to deal with bureaucracy and judicial system because the cost of proceedings and slow process. Which is overall flaw in the system and there is no preference between local and international firms in this regard. However companies did not provide any information about the quantification of their losses due to counterfeit. It is also reported that the penalties are not enough to the counterfeiter and more initiate should be taken to protect the rights.

#### **4.13.2 Cultural Effect**

It is strange to know that the vast cultural conflict exists even between the different states. Companies mentioned that the official response varies between states which encourage the criminals. Police response is also varies and depend on the states. Time is not considered important in Indian system.

#### **4.13.3 Main Weakness of Indian System**

Documents conclude the main weakness of the Indian system in context of foreign investor is as follows;

- Corruption
- Cost of Proceeding
- Length of Proceedings
- Lack of trained officials
- Response time from Bureaucracy
- Political Will
- Deficient enforcement of IPR regulations
- Improvement required in IP legislation

## 5. Analysis

In this chapter the empirical findings described in the previous part of the thesis will be analyzed following the theoretical framework. The theoretical framework and the empirics will be connected into a discussion that aims at giving the answers to the formulated problems: When Joint Venture is the most appropriate entry mode for SMEs to enter in Indian market. The right partner selection and the reduction of the cultural differences between the partners.

### 5.1 Entry Mode for Indian market

The most common reason for firms to choose joint venture as an entry mode in Indian market is the legal regulation. Government in some sectors bound foreign investors to work independently and foreign investor have to work jointly with local partner. As in the case of AmKabel the government didn't allow foreign direct investment in the cable manufacturing sector.

SMEs with limited resources preferred joint ventures. Another reason is firms don't have market knowledge especially in case of SME. The other important reason for the firms to form a joint venture in the Indian market are due to the organization needs, local partner awareness of local market, natural and human resources and most importantly easy exit.

According to Henrik Blad foreign firms choose joint venture because of legal obligation and second having no knowledge about market. He further describe that foreign firms need sales and having local partner means that the local partner will be responsible to bring customers to joint venture.

The liberation of Indian economy after 2005 and the risk involved in joint ventures make it a less popular option. The high risk involvement, the inefficiency of Indian legal system, the cultural differences, the European and Indian business norms are the major causes of the reduced popularity of joint ventures in India. Most people now consider joint ventures as the last possible option of doing business in India. The survey of Swedish Indian business guide for 2009 clearly indicated the increasing popularity of own legal entities of Swedish firms in India than joint venture. The own legal entities of Swedish firms in India are 51% and the number of joint ventures are 17%.

The Swedish Trade council considered joint ventures in terms of money as most costly and risky and in terms of control as an average option.

The unique business problems associated with Indian business environment like bureaucracy, corruption rate, complex labor laws, high tax rates, complicated legal and regularity system, the difference of laws between different states and the lack of ability of foreign firms to use local business networks provide Joint ventures edge over other possible entry modes.

The joint ventures are now not only available option to handle above mentioned problems. The introduction of BSO by Swedish Trade council has challenged the edge of joint venture. The Swedish trade council Business Support Office (BSO) provides all kind of supports (sale support, virtual office in India, Sourcing support, Employment service etc.) to Swedish investor in Indian market.

The problem with these BSOs is that the foreign business skills and knowledge is experimental knowledge. As explained by Forsgren, Holm & Johanson (2005) this type of knowledge is associated with the specific situation and the contexts in which they have been developed. It is difficult to transfer that kind of knowledge. Unless or until the SMEs practically involve in the business they cannot acquire the required skills for doing the business in a particular market.

## 5.2 Partner Selection

The firms form joint ventures to replace their weakness with the strength of their partner. JVs turned into great failure and not a suitable option if the interests and objectives of the partners are not aligned. Selection of the local partner from host country can reduce the risk and increase the capability of the joint venture to use local networks and market resources.

The success of a joint venture is dependent on the inter partner compatibility. This inter partner compatibility is dependent on the issues of Culture, strategy, organization capabilities and financial traits.

### 5.2.1 Cultural Traits

Indian culture is based on old tradition values. The roots of these traditions are based on centuries. These values and traditions are very different from west. It is important for foreign firms to understand this difference before entering Indian market. According to Henrik Blad Swedish companies want to work in Swedish way and Indian try to work in Indian way and then conflict rise. The foreign partner need to understand this that he has to adjust on the foreign soil and all the things can't go like he/she wants.

Nils said in his interview while giving his views about Indians that the Indians are not as materialistic as west so they can't understand the importance of the time in western way of living. Patience is the primary key to work in India and one must have to understand it.

### **5.2.2 Management Compatibility**

It is important to have local management who understand market. According to the Amokabel the importance of local staff in joint venture is critical due to the understandability of market and customer mind set. Henrik also express the importance of finding skillful people because one wrong choice can damage the shape of joint venture. Partner should be transparent to each other and clearly practice what they aim to do in joint venture. Foreign companies normally responsible for providing the knowhow and local partner are responsible for marketing, sales and local operations. Henrik Blad positioned that the compatibility is based on having same objectives, if one company lose its motivation. The joint venture must be terminated.

Managers are very authoritative in India that means people try to avoid arguing with managers and willing to accept their decisions which is quite different for Swedish people who work and express their opinion freely in work places. It feels that foreign companies try to bring their business culture in India which is not a successful option.

In India the structure of organizations is hierarchal middle management usually look towards the top management for further instructions. Swedish people usually find it difficult to manage these types of situations and may lose patience because they need to tell middle management again and again what to do.

Due to the authoritative style of top management sometimes it is really difficult to reach at a collective decision with local partner. The local partner may take decision independently that can create problem in the joint venture. The only solution to this problem is transparency.

### **5.2.3 Financial Traits**

All respondents and secondary sources focus the importance of financial traits investigation of partner. Henrik Blad mentioned this as one of the mistakes of Amokabel. AMOkabel did not take this issue seriously and not investigate about the financial traits of the partner and in the end suffered badly because of this mistake.

Ricky Dhillon mentioned the financial screening while choosing partner as a mandatory process. Swedish Trade council has several studies mentioned financial screening is important.

The financial traits scanning of the partner should be done comprehensively. Financial strength is not only important just in terms of money matters but how actively local partner can participate and perform in joint venture. In most cases the local partner is responsible for marketing and sales because of having market knowledge. Foreign firms have problem in risk management due to the way of implementation of rules and regulations in Indian system.

Foreign firms must verify how really this joint venture matters to local partner. Sometime local partner involve with more than one companies and did not take things seriously. Partners have clear contract in regards of risk sharing so everybody must understand his clear role in JV.

The partner must possess three abilities. The first ability is to increase revenue and reduce taxes and expenses and maximize operational efficiency. The second ability is to allocate and use working capital, attain local financing, use and control debts, and managing risks. The third ability is to optimally deploy assets and resources, manage accounts receivables and cash flows and manage fixed and intangible assets.

Our case company Amokabel did not evaluate its partner's financial strength. In some areas over trust of Amokabel on its local partner created problems. The one example of that is that Amokabel tend to believe that local partner will generate sales which were not actually happened.

#### **5.2.4 Goal Compatibility**

It is natural for the firms to join joint venture with different goals. Conflicts of interests and goals are the major reason of failure in joint ventures. The firms from two different geographical areas have different needs. Indian partner will look at the joint venture as a source to acquire and learn new and advance technology while the Swedish partner will be interested in the expansion of his business in Indian market.

The goal compatibility will increase the synergies between the partners. The firms with different sets of goals can form a successful joint venture and the strategic expectation of both the companies can met simultaneously. Firms need to respect each other's goals and the goals of one firm should not be in direct conflict with other firms goals.

Amokabel, Company failed to develop goal compatibility with their Indian partners. They wanted to increase their market share. The Indian partners need was the transfer of technology. Once Amokabel was done with their part the Indian partner was failed to fulfill their responsibility. The goal of the Indian partner was accomplished so they did not show respect for AmoKabel goals. Henrik said in interview that "if top management does not show the interest and commitment in business, things go wrong".

It is really important for the firms to dig out the information about the partner that wheatear they will respect the goals of the foreign partner or they are only interested in their own requirements.

#### **5.2.5 Controlling Issues**

Another major issue in joint venture is regarding the controlling body. Many joint ventures failed due to the controlling and managing issues. Foreign firms try to control and run things in their own way which is quite difficult in India. On the other hand Indian partner think that foreign partner don't know anything about India, so it is our duty to control and manage everything. According to Amokabel, it should be clearly mentioned in agreement that how to control. Most of the time board of directors are responsible to make decisions in joint venture but in Indian culture people make decisions outside the board. It is important while choosing partner that he must know how foreign firms work. It is important for foreign firms to make sure that everything is according to agreement. Amokabel had agreement with its partner that all decisions will took place in board of directors meeting but actually it wasn't happen. Again the seriousness of partner is very important. Henrik argues that firms must have full control in order to work freely and that is the reason he prefer wholly owned subsidiary over joint venture. In his opinion foreign firms can hire local employees to market and sale the product but prefers to has control in his own hands.

### **5.2.6 Firm Size**

Our respondent mentioned that whatever the firm size is or the share size a firm have in joint venture the important thing is commitment. Authors mentioned in literature that small sized firms are more committed because both have limited resource and unable to perform without cooperation. The large firms may be less committed with the joint venture.

## **5.3 Laws and Regulation**

India is very liberal country in terms of FDI. In spite of the fact that there are different restrictions for international firms to choose local partner in India in specific sectors. The government policies after 2005 provide more space to foreign firms to do business.

There is no discrimination for Foreign and local firms in Indian law while dealing with the local law. The problem which foreign firms faced is the slow proceedings of the courts and the heavy and useless paperwork involved. The slow and influenced bureaucracy makes the things more difficult for foreign firms.

The foreign firms usually avoid legal proceedings as they are so costly and time consuming that the SMEs with limited funds can't afford it.

In our case company scenario Hanrik Blad share his experience and said that due to the slow process and so much wastage of money they left their 49% shares and don't claim them in

court while the local partner refused to pay anything. Henrik further said that the written agreements are just a formality because it is difficult to get justice from the court on the basis of these agreements. He considers moral obligation more important than legal obligations for firms to follow the agreements.

He suggested that the “*exit strategy*” should be defined in the written agreement. That if joint venture will be needed to dissolve then it should be clear to each firm that what will be owned by each firm and what will be the obligation of the each firm. If firms don’t decide this strategy in the beginning it is nearly impossible to resolve this type of issues in courts.

However it is important for foreign firms to aware of laws and regulations as government provide different facilities to companies like SEZ. Although the process is slow but even then the courts play their role for effective implementation of IPR. The lengthy process is the drawback of Indian legal system. Tax rate is quite high in India which is a concerning issue for foreign investors.

#### 5.4 Government Interference

Indian Government continuously improves its policies to attract foreign investors. The main problem as our empirical study finds out the complex bureaucratic system in India. Politicians are involved in different decision makings by the authorities. The relations with politicians can expedite the procedures of approvals and sometimes companies can have out of the way favors from the authorities on the decisions.

The bureaucracy tries to protect the local industry by limiting the foreign firms which is not a healthy sign for investors. However the condition is far better now compared to decade ago.

#### 5.5 The IPR Situation

The Official Indian policy about IPR issues is very strict. Apparently on papers the situation is very good for companies and they have strong protection against IPR violations. However companies seem uncomfortable in reality. It is because of low level of commitment and lengthy process of the legal system. Companies try to adopt new technologies to save IPR which is hard to copy itself like hologram and barcodes but still infringements are present.

India is forcefully active in the implementing IPR during last decade and since then the progressive improvement can be observed.

#### 5.6 Tax Rate and Corruption

Many foreign firms have serious concerns on the issue of corruption and high tax rate. STC considers these problems as two major problems for foreign investors in India. STC suggests

that the foreign investor must understand and study high tax system and bribe culture in India. Even the people holding most senior positions are involve in corruption. Bribe culture is very strong and nepotism and favoritism is also common phenomena in Indian society.

Bribe in local terms consider as gifts and many companies use these techniques to get benefits. One reason of Bribe culture is having 29 states under one federation which is quite hard to control and even central government has no control in few areas far from capital. Taxation system is really complex as the goods move from one state to other state. Every state has its own laws and regulations for a single commodity which may differ from other parts of the country. Local Politicians become stronger and has great influence on official departments like police and taxation authorities.

## 6. Conclusions

In this chapter we will conclude the main findings of our research. The purpose of this conclusion is to answer our research question.

Our main research question was:

***When JVs is the most appropriate entry mode for Swedish SMEs to enter in India? Or identify the situations where joint venture can be the best entry strategy for Swedish SMEs to enter India?***

Our conclusion for this question is that the Joint ventures are very difficult to manage. Joint ventures are full of obstacles right from its formation to the everyday operations. Situation becomes much worse when long geographical and big cultural distances exist as in the case of Swedish and Indian firms. Joint venture is not a popular option for Swedish firms in India due to lack of control and if possible they preferred to form own subsidiary.

Although with all these problems the joint venture is still the best option for Swedish SMEs to enter in Indian market. It requires less resources and it is the most effective and secure source to get experimental practical market knowledge. All other entry modes either provide limited market knowledge like intermediaries or too costly or risky for SMEs like acquisition or a subsidiary at foreign soil.

As far as the failure of Amokable is concerned we find out that the proper home work was missing. The case company decided to go in joint venture on the invitation of their Indian client. The problem was not with the choice of the joint venture as an entry mode. The reason of failure of the Amokable on Indian soil was that they looked at the opportunities but failed to identify the involved risks. The plan of Amokable missed the answers of basic questions that how to enter in the market, how to build up business in the market, how to build up relation with the partner and how to survive with typical Indian conditions?

The key to success for a SME in a joint venture is the early and complete awareness about all the potential problems of the joint venture and the plans to avoid or manage them properly. The scope and planning of the management of these problems will start before the formation

of joint venture. The scope of this problem management planning will continue to expand through the everyday operations of joint venture.

SMEs can have a great advantage of having a local Indian partner on Indian soil. The continual business reforms in India started from 2005 are turning India into a friendly environment for FDI. These changes can only lead to a better climate for foreign firms wanting to do business in

India. Even then in some specific industries the government of India bound foreign investor to work with local partners and joint venture is only available option.

Our first sub research question was:

### *How to choose the right partners for JVs?*

We concluded for this question is that the joint venture is the working agreement between two partners. The choice of the partner is the basic building stone of the joint venture. If this building stone will not be laid properly the joint venture can never be successful.

The firms must investigate external and internal factors while choosing partners. The one reason of the failure of Amokabel is to ignore research about partner. Amokabel never investigate about their partners. Both the Amokabel and its partner were not able to develop working cooperation with each other. The basic reason for this was that they did not know about each other. The weakness and strengths of both were hidden from each other. This lack of information about each other turned the joint venture into a failure.

Joint venture is long term business relationship so investigation about the partner should cover all aspects from its financial capabilities to operational capabilities. The purpose of the joint venture for the firms is to replace their weakness with the strengths of their partners. The firms must collect all the information about their potential partners. What are the strengths and weakness of the partners and either the potential partner firm will fulfill their requirement or not?

The goal compatibility is really important for the joint ventures. Firms with conflicting goals can never make a successful joint venture. It can often be difficult for a Swedish firm to know what to expect from an Indian partner and to know in what way they think. An Indian might say one thing and mean another. Most of the Indian firms form joint venture with Swedish firms to learn new technologies. Swedish firms who are just able and wanting to see things from their side might very well find themselves in a shock when they realize that the partner wants something totally different.

Financial capabilities must include the investigation about current market reputation, the past market performance, ability to finance the joint venture to cover financial risk and the ability to manage financial resources efficiently.

Our second sub research question was:

*How to overcome the cultural differences between the partners?*

Swedish and Indian cultures are different from each other having different values. It will be strange if the natural collision between these cultures in different situations don't occur. The conflicts between partners may arise because of the cultural differences. Swedish firms should understand Indian cultural values and the habits of Indians based on their culture. It is important for Swedish firms to have its business culture but it is also important to respect the Indian culture in the country. A company can still be Swedish and have Swedish core values at the same time as it adapts to the local Indian business climate. Once a Swedish firm understands this it can easily predict that what can be the possible move of their Indian partner in a particular situation. This will surely decrease the possibilities of misunderstanding between partners.

This cultural understanding will not only helpful in dealing with partner but it is also helpful to understand the mentality of the managerial staff and how to deal with them.

## 7. Recommendations

This is the final part of the thesis; we end up here with our recommendations for the Swedish SMEs who want to expand their business in India through joint venture. These recommendations will be helpful to avoid failures.

Firms must have a proper plan to enter, establish and grow joint venture business. This plan should cover the issues from formation of the joint venture to the everyday operations till the exit strategy. It is important to look at the opportunities but it is also important to identify the involved risk and plan accordingly.

When choosing a partner the most important thing is to know who is your partner and what are his intentions to be your partner? The existing corporative relationship should be preferred in the search of joint venture partner. Partner assessment should not be based on partners own description. The capabilities of the potential partners should be judged by a team of professionals. This team of professional contains persons from every field like financial, operational and marketing professionals. It is batter to check the market reputation and past record of the partner.

It is important to collect the potential partner's information on the issues of employee mind-set, morale of managers, operational efficiency, technology, equipment, cash flow, over all financial health and the effectiveness of the management system.

It is important for SMEs to know that what they want to gain from the relationship and it is equally important to know what their partner wants to gain from it. As long as both parties have resources to contribute to the joint venture there should be some kind of dependency on each other. The transfer of technology by Swedish firm should be related with the expansion of the business in the Indian market. In this way the Swedish firm will remain at a safe end.

To avoid future financial risks complete investigation of the partner in the appropriate manner should be done. This financial investigation should cover all the aspects from financial standings to market performance and utilization of resources.

Swedish firms should understand Indian cultural values and the habits of Indians based on their culture. It is important for Swedish firms to have its business culture but it is also

important to respect the Indian culture in the country. This will surely decrease the possibilities of misunderstanding between partners. This cultural understanding will not only helpful in dealing with partner but it is also helpful to understand the mentality of the managerial staff and how to deal with them.

The cultural understanding can be increased by social gathering. Organize social gathering on local Indian cultural events. Try to involve local and foreign staff and encourage them to participate. It will decrease the cultural differences and will not only increase the firms understanding about the Indian culture but make the firm popular in the local staff too.

Indian business persons have authoritative style and problem may arise because of this style. To avoid this type of problems the managerial controlling activities should be define clearly in the binging. Every partner must know his responsibility and authority. It means the decision making process should be clearly define, what type of decisions partner can take independently and for what kind of decisions both the partners have a joint session to reach on a collective conclusion.

The firm size really matters, it is not recommended for SMEs to establish joint ventures with very big or very small firms than its own size. It is good to have relatively small firm as compared to foreign firm as a partner because they will show more interest in joint venture rather than big firms. The partner firm should not be so small that it cannot cover the financial risk to the joint venture.

The Swedish SMEs should be aware of the poor implementation of law in India as compared to Sweden. The contracts are not so much important for Indians. Written agreements are in no way provide assurance that everything will go accordingly. To avoid future problems SMEs should try to engage its Indian partner in moral obligations than legal. The “*exit strategy*” should be defined in the initial agreement. The agreement should be written comprehensively with the help of international and local business law experts.

The political and governmental influence should be handled properly. The local contacts with political and influential government officials should be established. It is important to get help from local people who knows the way to interpret the law.

## Glossary

FDI	Foreign Direct Investment
SME	Small Medium Enterprise
Joint Venture	A foreign and local company establishes a new business entity by agreeing to share resources and risks on the basis of their contribution.
Wholly Owned Subsidiary	A foreign Company establishes a new enterprise in India and hold 100% capital of new enterprise.
STC	Swedish Trade Council
WTO	World Trade Organization
IBM Model	International Business Marketing Model
GOI	Government of India
FIPB	Foreign Investment Promotion Board
FEMA	Foreign Exchange management Act
DIPP	Department of Industrial Policy and Promotion
WIPO	World Intellectual Property Organization
PCT	Patent Corporation Treaty
CGPDTM	Controller General of Patent, Design and Trade Marks
IPAB	Intellectual Property Appellate Board
LP	Legal and Political environment of a country
PPR	Physical Property Rights
Nepotism	Favoritism shown patronage granted to relatives
SCCI	Swedish Chamber of Commerce India
SEZ	Special Economic Zone

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### **Interviews:**

Henrik Blad  
MD, AmoKabel  
Ricky Dhillon  
Swedish Trade Council, India  
Nils Marcks Von Wurtemberg  
Program Officer, Swedpartnership



## Linnaeus University – a firm focus on quality and competence

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On 1 January 2010 Växjö University and the University of Kalmar merged to form Linnaeus University. This new university is the product of a will to improve the quality, enhance the appeal and boost the development potential of teaching and research, at the same time as it plays a prominent role in working closely together with local society. Linnaeus University offers an attractive knowledge environment characterised by high quality and a competitive portfolio of skills.

Linnaeus University is a modern, international university with the emphasis on the desire for knowledge, creative thinking and practical innovations. For us, the focus is on proximity to our students, but also on the world around us and the future ahead.

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