

8 Strategic Alliances and Foreign Investment Opportunities

If your company is interested in delving further into the international trade arena, licensing, joint ventures and offshore operations might be explored. While direct exporting may be a profitable method of market entry for some businesses, licensing your company's manufacturing rights to a foreign company or setting up a foreign manufacturing joint venture may be viable alternatives.

In comparison to exporting, setting up offshore manufacturing operations may be a more economical way of doing business. Firms choosing to set up operations in different countries should check for local incentives. Government agencies usually will assist foreign businesses to set up operations and will provide a wide range of grants and taxation incentives, both for the corporation and its expatriate employees.

This chapter will discuss the relative advantages and disadvantages of alternatives to direct exporting, how to find licensing and joint venture manufacturing partners, and how to finance overseas investment.

Strategic Alliances

Licensing

Licensing involves a contractual arrangement whereby a company licenses the rights to certain technological know-how, design and intellectual property to a foreign company in return for royalties or other kinds of payment. Licensing offers a small business many advantages, such as rapid entry into foreign markets and virtually no capital requirements to establish manufacturing operations abroad. Returns are usually realized more quickly than for manufacturing ventures.

The disadvantages of licensing include a lack of control over manufacturing, quality, and marketing. More importantly, that the licensee may become a competitor if too much knowledge and know-how is transferred. Always make sure to carefully protect your trademarks and intellectual property when undertaking any licensing agreement.

One way to help ensure that your intellectual property is protected is to secure proper patent and trademark registration. In the interim before your patent is filed, you may ask a potential licensee to sign a confidentiality and non-disclosure agreement barring the licensee from manufacturing the product itself, or having it manufactured through third parties. Make sure such agreements are not in violation of laws in the host country.

Patents should be filed with the appropriate foreign government within one year of U.S. filing, in order to obtain patent protection under the Paris Convention, the international agreement on patents. Patent rules vary from country to country, so it is important to consult a competent international patent and trademark attorney.

Licensing the rights to your product to a foreign company will require a carefully crafted licensing agreement. Consulting an attorney is critical since rules on licensing also vary from country to country. Be careful that the agreement does not violate host country antitrust laws. Under the antitrust laws of many countries, the licensor cannot set the price at which a product will be resold by the licensee.

Check with the United States Trade Representative's Office (USTR – www.ustr.gov) for current information on intellectual property rights (IPR) protection in different foreign countries or refer to the Country Commercial Guides available from the U.S. Department of Commerce at www.export.gov.

Foreign Manufacturing Joint Ventures

In contrast to licensing arrangements, foreign manufacturing joint ventures allow for the U.S. company to have a stake and management role in the foreign operation. Joint ventures require more of a direct investment than licensing and typically include the need for training, management assistance, and technology transfer.

Joint ventures can be equity or non-equity partnerships. Equity joint ventures are contractual arrangements with equal partners. Equity joint ventures are contractual arrangements which may, or may not, involve the host country partner in an arrangement in which joint activities (marketing or R&D) are formalized, although ownership is not shared. Laws often require that a certain percentage of stock belong to a citizen of the host country.

Foreign manufacturing joint ventures are risky in that geographical and cultural factors may interfere with the smooth running of operations. You will have to deal with entirely new management, located in a different country, whose first language

may not be English. Despite the drawbacks, using a foreign partner can have several benefits, viz. the partner likely will have intimate knowledge of the target market and may have business and political contacts to make market entry faster and more successful.

Partner Selection Issues

Finding a suitable partner is critical to the success of any licensing or manufacturing joint venture arrangement. However, the selection process can be time-consuming and difficult without proper assistance. The United States government has developed a number of special programs to assist U.S. companies to select overseas partners.

Established in 1994 as a United States Agency for International Development program, the Global Trade and Technology Network (GTN) has worked to facilitate sustainable economic growth in developing countries and emerging markets through business linkages and technology transfer. In 2002, GTN launched an Internet-based trade facilitation platform (www.usgtn.net) to further spur trade between companies located in the United States and developing nations. Since that time, the GTN trade platform has become a leading worldwide provider of international trade leads services. GTN's trade services include trade and investment business matching services, technology transfer, trade lead follow-up services, trade financing referrals, and market information. You can register online for this service.

The U.S. Department of Commerce's Commercial Service sponsors a number of trade missions throughout the year that could serve as an excellent venue for meeting potential joint venture or licensing partners. These missions provide one-on-one, pre-screened business appointments with foreign businesses for delegation members, arranged by the overseas staff of the Commercial Service. For company representatives that cannot join an organized trade mission, but that can visit a targeted country, the Commercial Service can provide a "Gold Key Service" to help you locate appropriate business partners. The Commercial Staff in that country will meet with you, provide an orientation briefing, advise you on market entry strategies, set up pre-qualified meetings for a day or more (changes are by the day), provide an interpreter for meetings if needed, and help with follow-up planning. Fees vary by country. If you cannot visit the country initially, you can arrange for an International Partner Search, by providing your company literature and partner requirements to the Commercial Service, which will identify partners for you. Both services can be arranged through your local Export Assistance Center.

The following steps should be followed in selecting an overseas partner:

1. Contact your local Export Assistance Center to discuss your target market, market strategy and the type of partner you are seeking. Determine whether a trade mission, a Gold Key Service, or an International Partner Search makes the most sense at this time.

2. Either as a result of your in-person appointments or from the information forwarded to you by the overseas Commercial Service staff, you will have a list of potential business partners to evaluate.
3. Conduct a financial and business background check on the most qualified candidates, weighing the respective strengths and weaknesses of the various potential business partners. You will probably want to use a credit reporting firm to assist you with this step.
4. If you haven't yet gone abroad, make sure you do so at this point to get first-hand information and to meet face-to-face with potential licensees or joint venture partners. There is no substitute for one-on-one meetings held on their turf, to get a proper read of their capabilities, and to clarify individual and mutual objectives and benefits for both parties.
5. As you finalize your selection and begin negotiating an agreement, make sure to involve the assistance of legal counsel. Commercial laws vary around the world, so make sure you understand and make adjustments for the foreign legal framework before consummating any deal.

Foreign Investment Opportunities

Establishing a manufacturing facility abroad requires a greater investment than licensing or joint venture manufacturing, but it also affords the greatest amount of control over your product and operations. Additional factors to consider include foreign government investment incentives, the need to eliminate high transportation and/or tariff costs, and the desire to lower production costs.

If you are considering setting up an offshore manufacturing plant, you will need to assess whether or not to acquire an existing facility or to construct a new one. Key factors in this decision include legal and tax ramifications, location and how to finance the foreign investment.

Legal and Tax Implications

Much of the decision-making process surrounding joint ventures or offshore manufacturing involve legal and tax issues. Since some countries actively pursue foreign investment, they have relaxed their laws on some types of investments and the amount of equity required. In addition, many offer tax incentives. Consequently, U.S. and host country attorneys and accountants need be an integral part of the team to assess whether and where joint venture or offshore manufacturing would be most profitable.

Overseas Private Investment Corporation (OPIC)

Investing overseas requires a substantial commitment of a company's time and money, and a certain amount of risk. To provide investment assistance and to address the risk insurance needs of U.S. companies, the U.S. government created OPIC, a separate

business-oriented agency to support American investors entering developing country markets. OPIC (www.opic.gov) is the lead agency assisting U.S. businesses interested in making direct investments overseas. OPIC programs are available if the project:

1. Is a new venture, or an expansion of an existing business,
2. Is located in a developing country where OPIC operates (OPIC operates in 150 countries),
3. Will assist in the socioeconomic development of the host country,
4. Is approved by the host government, and
5. Is consistent with the economic interests of the United States and will not have a significant adverse effect on the U.S. economy or U.S. employment.

If your potential overseas investment fits these criteria, OPIC can be an extremely useful resource. OPIC offers a variety of programs, including financing and political risk insurance to help protect your investment and several pre-investment services.

Pre-investment Assistance

OPIC sponsors investment missions to introduce U.S. business men and women to key foreign private sector leaders, government officials, and potential joint venture partners. Since 1971, OPIC has accomplished its developmental mission by supporting more than 3,100 projects throughout the developing world. Over the agency's 34-year history, OPIC has supported nearly \$150 billion worth of investments that have helped developing countries to generate over \$11 billion in host-government revenues and create over 690,000 host-country jobs. These projects also have helped generate \$66 billion in U.S. exports, creating 257,000 at home. In addition to pre-investment assistance, OPIC provides financing to assist in the setup of overseas operations and risk insurance to mitigate some of the problems associated with investing in developing countries.

Financing

In July 2003, OPIC announced the establishment of a new department and business center focusing on small and medium-size businesses, to help ease their entry into new markets. The Small and Medium Enterprise Department and the Small Business Center are responsible for OPIC's direct loan program, which provides financing to businesses with revenues under \$250 million and \$35 million per year, respectively. Direct loans between \$100,000 and \$10 million are available for overseas investment projects that involve at least a 25% equity ownership by a U.S. small business. Finance activities for larger corporations are housed in the Structured Finance Department, which is responsible for the Investment Guarantee programs, as well as special initiatives. OPIC's Small Business Center can be reached at 1-800-225-5722.

Insurance

Private investors may be hesitant to undertake long-term investments abroad, given the political uncertainties of many developing nations. To alleviate these concerns, OPIC insures U.S. investments against three major types of political risks: inconvertibility of currency, expropriation and political violence, including civil strife.

Foreign Governments

Foreign governments, particularly in developing countries, often sponsor special agencies to aid and facilitate foreign direct investment. Some examples include the Mexican Investment Board (MIB), the Portuguese Trade Commission and the Bahrain Promotions and Marketing Board. These foreign investment promotion agencies can provide detailed market information, joint venture leads and contacts with key officials. They often maintain offices in the United States.

Some countries also may have special funds or financing arrangements to spur foreign investment in particular sectors or geographical areas. Foreign investment promotion agencies can lead you to these sources. Contact the appropriate foreign embassy in the United States for the name of the agency that can assist you.

A Final Word on Going Global

How you decide to enter overseas markets will depend on a variety of factors unique to your own small business. Going global can be a challenging experience for a small business, but the rewards can be substantial. Let optimism and enthusiasm be your guide as you go global. The U.S. Small Business Administration, as well as numerous other government agencies at the state and federal level, support and encourage your entry into the international arena.