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The determinants of foreign partner's equity ownership in Southeast Asian joint ventures

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Abstract

Using a sample of 375 equity joint venture agreements between 2 partners in 6 Southeast Asian countries, we document the active role of Asian companies in driving the flow of joint venture activity in this region and provide a comparative analysis of joint ventures in transitional and non-transitional Southeast Asian countries. Specifically, we analyze the relationship between the foreign partner's equity ownership and partner uncertainty, the types of joint venture activities, and the frequency of transactions between the joint venture partners. In addition, we show that the relationship between the foreign partner's equity ownership and partner uncertainty, as proxied by cultural dissimilarity, depends on the types of joint venture activities. In the case of Vietnam, a transitional economy, the evidence suggests that, in the presence of a weak legal and regulatory system, foreign firms are entering the country on a smaller scale and are more prone to informal, relational contracting as a substitute for legal enforcement.
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1. Introduction

Fortune 500 companies frequently use joint ventures as a form of organizing economic activities in developed countries (Harrigan, 1985; Janger, 1980).[1] Multinational corporations

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[1]Lynch (1989) defines a joint venture as "a cooperative business activity formed by two or more separate organizations … that creates an independent business entity and allocates ownership, operational responsibilities, and financial risks and rewards to each member, while preserving their separate identity/autonomy".

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also use joint ventures when operating in developing countries Vaupel and Curpan (1973), even when the host country does not require the use of joint ventures with a local company as a condition of market entry (Beamish, 1984). The joint venture literature maintains that a joint venture formation is justified when synergy exists between the 2 contracting parties (Contractor & Lorange, 1988; Root, 1988) and there are transaction costs or information asymmetry problems that make outright acquisition of the other party economically infeasible (Balakrishnan & Koza, 1993; Buckley & Casson, 1988, 1996; Gomes-Casseres, 1996; Hennart, 1988).

Despite the popularity of joint ventures as a form of economic organization, there is limited study of joint ventures in the emerging Asia Pacific countries. Most joint venture studies in the emerging markets of the Asia Pacific region focus on China as the joint venture location (Chen & Hu, 2002; Chen, Hu, & Hu, 2002; Chen, Hu, & Shieh, 1991; Hu & Chen, 1993, 1996; Li, Lam, & Qian (2001); Luo, 2002; Meschi, 2004; Pan & Li, 2000; Pan, 1996, 2002; Tsang, 2002). Other emerging countries in the Asia Pacific region have received very limited attention (e.g., Aswicahyono & Hill, 1995; Lasserre, 1999).

Three factors motivate our focus on the Southeast Asian economy. First, when venturing overseas, companies tend to pay special attention to the size of the foreign markets. Feldman (1992) reports that 76% of 110 Asian–American ventures surveyed mentioned that access to new markets is the primary objective. As a result, the substantial focus on China is understandable considering the potential size of its market. Academic interest in China largely follows from this increasing business focus on China. However, Schlosstein (1991) argues that Southeast Asian countries—more specifically, Indonesia, Thailand, and Malaysia—represent the New Little Dragons, as they were laying a solid foundation for economic takeoff, to follow the previous Little Dragons (Korea, Taiwan, Singapore, and Hong Kong). Indeed, the World Bank statistics on average GDP per capita growth for over 200 countries over the 1990–1999 period indicate that of the top 15 countries for which complete data is available, 5 of them are Southeast Asian countries (Singapore, Thailand, Vietnam, Indonesia, and Malaysia). The high GDP per capita growth of the Southeast Asian countries implies an increasing standard of living that potentially gives these countries' citizens greater purchasing power. As such, the Southeast Asian countries are likely to represent significant business opportunities.

Second, despite their geographical proximity, the Southeast Asian countries are quite diverse in terms of their economic development, political system, culture, and ethnicity (Lim, 1996). As a result, the Southeast Asian countries offer a rich laboratory to study the ownership structure of joint ventures with foreign partners. Third, anecdotal evidence suggests that developing nations in Asia that previously benefited from foreign investment are becoming foreign investors themselves. For example, Biers (1994) shows that Malaysian, Thai, and Indonesian companies started to invest in China and Vietnam. In fact, as of 1994, Malaysia was the 6th largest investor in Vietnam, while Thailand and Indonesia ranked 12th and 13th, respectively, ahead of the US The growing economy of India has also attracted investments from the Southeast Asian countries (Day, 2004). As a result, the Southeast Asian countries may represent, not only a significant business opportunity, but also the drivers of economic growth in Asia. Only recently, have academic researchers started to focus their interests on these Southeast Asian countries as important foreign investors in China (Chen, Hu, & Hu, 2002).

In this study, we empirically examine a sample of 375 joint ventures established in 6 Southeast Asian countries between 1990 and 1999. We focus on joint venture agreements

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