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# Country risk, national cultural differences between partners and survival of international joint ventures in Brazil

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**Abstract**

This article aims to identify the main and interaction effects of two country-level variables, namely national distance and country risk, on the survival of international joint ventures in emerging markets. Research hypotheses predicting the negative impact of national distance and country risk on survival of international joint ventures are formulated in this article. These research hypotheses are examined in a sample of 234 international joint ventures formed in Brazil between 1973 and 2004. These international joint ventures were subjected to an event history analysis over a period of time ranging from 1973 to 2006. The empirical results show that large national cultural differences between local and foreign partners increase the instability of international joint ventures, whereas the survival of these alliances does not seem to be affected either by the economic and political uncertainty of Brazil. Furthermore, the national distance between local and foreign partners has effects on survival that are variable according to the life cycle of international joint ventures.


*Keywords:* Country risk and national distance; Emerging market and Brazil; Event history analysis; International joint venture; Survival

## 1. Introduction

International joint ventures (IJVs), which are organizational entities created and managed jointly by foreign and local firms, have largely contributed to the foreign expansion of many US, European and Japanese firms. This central role of the IJV in the internationalization strategy of firms, particularly multinationals, was identified and stressed by Franko (1971) in his book, *Joint Venture Survival in Multinational Corporations*. However, since 1971, the scope of IJVs have widened considerably, to the point where their initial objective has become secondary in relation to new objectives such as achieving economies of scale and size effect (Garrette & Dussauge, 1995; Hennart, 1988; Kogut, 1988), learning and transferring competence and knowledge (Hamel, 1991; Hamel, Doz, & Prahalad, 1989), or refocusing and restructuring a business portfolio (Nanda & Williamson, 1995). At the same time, the opening up of new geographic markets accelerated, the WTO was set up, and local regulations favoring foreign direct investment were introduced widely in various

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developing countries. These trends motivated the multinationals to replace the IJV by other entry modes, such as wholly owned subsidiaries and acquisitions, which ensured them total control of local operations and resources, rather than the shared control associated with IJVs. These two combined movements led to a slow but inevitable decline of IJV as a mode of entry.

In the late 1990s, however, IJVs expanded once again. The spectacular growth of the BRIC countries (Brazil, Russia, India and China) in particular and emerging markets in general gave new momentum to IJVs. It was the political and economic uncertainty as well as the specific cultural features of these countries that made IJVs so popular among foreign firms (Farrell, Remes, & Schulz, 2004; Yan, 1998). US, European and Japanese firms tend to prefer IJV as a mode of entry whenever the country risk and the national cultural distance (or national distance)—known as *country-level variables* (Kogut & Singh, 1988)—are high and difficult to handle.

By collaborating through an IJV with a local partner in the emerging market, the foreign firm may protect itself against the adverse impact of these variables. It is the IJV's very structure, and more particularly the nature and complementarity of each partner's contributions, which make it so attractive (Farrell et al., 2004). The foreign partner provides the IJV with upstream resources such as brands, investment and production technology (Connolly, 1984; Pan, 1996; Tsang, 2005). The local partner provides downstream resources such as access to local markets and distribution channels, personnel (Inkpen & Beamish, 1997; Kale & Anand, 2001), knowledge of local regulations and preferential access to the government (Kale & Anand, 2001). Thanks to its IJV with a local firm, the foreign firm does not deal directly with the market, distribution channels, regulations and political stakeholders of the emerging market. It is the local partner which is in charge of them. Thus, the IJV allows the foreign partner to reduce its *liability of foreignness* (Rodriguez, Uhlenbruck, & Eden, 2005; Zaheer & Mosakowski, 1997). Liability of foreignness pertains to the costs of doing business abroad. These costs can be defined as *all additional costs that a firm operating a facility in a market overseas incurs compared to a local firm* (Zaheer & Mosakowski, 1997, p. 445). They vary greatly across host countries. As a consequence, foreignness is a liability, especially in emerging markets where political and economic uncertainty is high and where national cultural differences are marked (Yan, 1998).

The IJV is also a source of learning for the foreign partner, which takes advantage of the period of collaboration to observe the local partner's *modus operandi* and to transfer its downstream resources and market knowledge. Apart from the learning outcomes, a foreign firm involved in an IJV benefits from an institutionalization process on the part of the local consumers and political stakeholders (Scott, 1995; Zaheer & Mosakowski, 1997) and gradually acquires the status of a "quasi-local player."

While the IJV is a frequent mode of entry into emerging markets, its concrete outcomes do not always live up to its promise and potential benefits. Empirical studies on IJV survival in emerging markets show that between 30% and 50% are sold off, bought out or dissolved by the partners in the first 5 years (Kale & Anand, 2001; Lee & Beamish, 1995; Leung, 1997; Meschi, 2005; Nakamura, 2005; Pan, 1996; Yan, 1998). Some studies have linked this high instability rate to the specific nature of country-level variables of emerging markets, namely, high country risk and large national cultural differences: "for IJVs formed in developing or transforming economies, the turbulent political and economic environments together with the intercultural and interorganizational dynamics have made managing international joint ventures particularly challenging" (Yan, 1998, p. 773). In other words, the two country-level variables—country risk and national distance—which lead to the formation of IJVs in emerging markets are also those that cause their dissolution. This is a paradox inherent to IJVs formed in emerging markets.

However, empirical studies of the impact of country risk and national cultural differences on IJV survival have produced inconclusive results. Furthermore, the impacts of these variables on survival have been only examined individually, and not jointly. The objective of this article is to study in-depth the relationship between these country-level variables—taken individually and in interaction—and the survival of IJVs. More precisely, this article aims to answer the following questions: what is the impact of country risk and national cultural differences between local and foreign partners on the survival of IJVs? Is country risk a moderating variable, or does it amplify the impact of national cultural differences on IJV survival? Does the longevity of IJVs affect the impact of national cultural differences on survival? It is important to note that these different research questions will be addressed solely in the setting of one emerging market, Brazil. We are aware that these issues may also be faced by IJVs formed in developed countries. Similarly, the theoretical argumentation