

Incentives for Co-Ventures

Governments can offer incentives to encourage small and medium industry to enter developing countries; both sides benefit

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I have been challenged to discuss the incentives that developed and developing country governments can offer to enhance the co-venturing process, especially for small and medium industry which wishes to enter developing countries.

I would like to offer two caveats. I cannot, of course, assess country-by-country the various incentives — or disincentives — each offers. Also, there are compendiums of legislation and evaluations thereof, at least for the major countries. Whether such legislation is good or bad often depends on individual political and economic circumstances, on the nature of their economic objectives, and on the success they have in achieving their objectives.

I appreciate the difficulties inherent in referring broadly to "developing" and "developed" countries in general. Obviously, there are important differences between countries in each group, but — also obviously — one can only generalize in a commentary of this sort.

As I prepared the following comments, which are perhaps more exploratory than definitive, I was struck by one important contrast. This paper, and indeed, most literature concerning the problems of doing business through licensing and co-venturing abroad, basically deal with relationships *within* the private sector.

And yet, as everyone is aware, there are increasingly more than two parties of the private sector involved in the co-venture process. Almost as a matter of course, there are three or even four parties to a transaction. There are the two venturers themselves and one or two governments — at least those of the technology transferor and of the technology recipient.

Another Element

And even another element is surfacing — the international organization which is seeking to inject multinational influences into a process which historically was considered to be private and predominantly bilateral. The United Nations Conference on Science and Technology in Development held at Vienna in Au-

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gust, the discussions at the UNCTAD, the support in some quarters for the development of a binding and so-called "Code of Conduct", and the oft-repeated call for a New International Economic Order — all are evidences of the pressures for the multilateralization of issues related to the co-venture process — to all forms of bilateral technology transfer. I believe these pressures could in time have marked effects on the private sector, and especially on the activities of small and medium enterprise, which may not have the capacity of the transnational to withstand or deal with such pressures.

Regrettably, it seems to me that increasing government involvement in technology transfer does not always carry with it the certainty of either informed or improved involvement, at least from the venturer's viewpoint. It may or it may not. Definable, worthy — and attainable — economic goals may be overridden by less worthy but pressing domestic political considerations. Governments may not have developed fully the capacity to understand their own technology needs or to negotiate intelligently to locate and acquire needed technology. The disadvantages of technology transfer, and, for that matter, the advantages of technology transfer, may not have been fully evaluated.

In dealing with the question of incentives in a more general context, then, I should like to suggest what may be truisms, albeit important ones.

If the purpose of government incentives is ostensibly to encourage co-venturing, I would conclude that they will tend to become favorable for the process primarily only when governments understand why companies will use that mechanism to enter foreign markets.

Voluntary Act

Incentives will tend to become favorable when governments understand that co-venturing is ultimately a voluntary and economically-motivated act taken by a private company.

Incentives will become favorable when governments understand that acquiring technology through the co-venture process can truly become acceptable public policy but that it must be carried out through reasonable negotiations with all concerned to establish the terms of agreement on such policy.

Probably then, and only then, will terms be established which will encourage and stimulate co-ventures for mutual benefit rather than be deliberately — or unintentionally — counter-productive, as many are today.

As governments acquire this understanding, it will also become clear that co-venturing is only one of several ways by which private enterprise can enter a

foreign market. It involves considerable risk, but it may also provide considerable return. And, properly organized, it may be one of the best forms of business organization for reducing the risks of going overseas. It can provide for a blending of domestic and foreign technologies, for acquiring the expertise to penetrate a given market, for the sharing of production costs. It may even stimulate the acquisition of new technologies and help reduce ever-soaring R&D costs.

But one factor about co-ventures becomes especially important in terms of the kinds of incentives to be made available.

The decision to enter into a co-venture is one which leads to a commitment of substantial resources over a substantial period of time. Therefore, it should be taken with considerable understanding.

Ideally, it should be made on the basis of mutually reinforcing relationships. Much like a marriage, a decision to enter into co-ventures should not be taken to achieve short-range benefits or advantages — these can be handled in other ways. As many commentators have noted, because of the longer-range commitments of money, time, and technology, a decision to co-venture should have been made as an integral part of a company's long-range planning strategy. It should reflect the way a company looks at the total overseas market and its own relation to that market over a period of several years. This is true whether one looks at the co-ventures from the point of view of entering the market or venture or, equally important, from the viewpoint of *leaving* the venture.

At this point, the relationship between how the private sector considers the venture process and the issues of incentives to be offered by governments should also begin to become apparent.

Biggest Risk Category

Since co-ventures are long-range commitments, undertaken voluntarily, the biggest single risk category for the venturers is the possibility that the terms under which the venture was entered into will not or cannot be maintained for the life of the agreement. Changes in terms could mean that the original estimates on which the profitability of the venture was based will have been significantly modified.

Hence, the most significant single incentive which can be given by a developing country to a joint venture from a developed country will be the maximum possible degree of assurance, preferably by law or regulation but also by attitude, that the rules of the game will not be changed in midstream and that reasonable and equitable conditions once agreed to will be honored as set.

Let me elaborate.

Undoubtedly, partners to a venture process would prefer the kinds of incentives which would permit the highest absolute profits possible. They include assurances against expropriation, provision for high levels of repatriation of capital and earnings, freedom to use foreign personnel in unlimited numbers, patent and/or trademark protection, nondiscriminatory local tax treatment, favorable treatments re-imports, and so on. Obviously, the greater the profitability to a venturer from these kinds of incentives, the more pleased it will be.

However, it seems to me that the real bottom line may be what I mentioned earlier — the elimination, or at least minimization, of risk, both political and economic. This in turn equates with the elimination of uncertainty, and this, in a very positive sense, equates with the establishment of predictability as the major consideration in going abroad.

Then, for example, a government may, for policy reasons, permit repatriation of only "x" percent of earnings, as against a foreign entrepreneur's desires for a higher "y" percent. However, if the venturing company has reasonable certainty that its earnings over the life of the agreement can be repatriated even at the lower level, it acquires a sound basis on which it can determine whether to come in or stay out. Though its total repatriation of earnings may be less than it desired, it may also be able to make up its losses through other measures. In any event, it is not making an important decision blindly.

Risk Disincentive

On balance, then, the biggest disincentive to co-ventures can broadly be described as that of "risk". "Risk" can be defined in a number of ways, but generically it is encompassed in the term "uncertainty". Therefore, the best incentives are those which tend to eliminate uncertainty, permit the greatest degree of predictability, and offer the venture partners the greatest opportunity to undertake reasonable and informed calculations concerning the longer-term benefits to them of co-ventures. These factors may become even more important for small and medium co-ventures which have less margin for loss than for the transnationals which perhaps can more easily write off losses.

In comparing the incentives which might be offered by developed countries, as compared with developing countries, the picture with regard to the former seems somewhat different. Developing countries through their regulations *actively* affect and control the ways in which technology is received and utilized. However, if the United States can be taken as an example, it would appear that market-oriented developed countries generally may not control much of the technology which would normally be subject to transfer through the co-venture process.

There are exceptions, but a major portion of the technology, at least in the United States, is regarded as being proprietary in nature, and is therefore not in the public domain. This seems particularly true if the all important "know-how" and management and production skills and techniques are included.

Thus, at best, developed countries may be able only to establish conditions which either encourage — or discourage — private enterprise on its own to consider technology transfer through the co-venture process or in some other mode. They (the governments) cannot transfer that technology themselves, or force transfer of technology by the private sector. It's relevant also that the private sector in many developed countries has to be regarded as believing that it has alternatives to investment overseas, particularly if risk is high. It does not need to go overseas.

Clearly, the foregoing are factors which must be taken into account by *both* developed and developing

countries if incentives are to be taken which encourage technology transfer to developing countries.

Political Overtones

Parenthetically, it is perhaps a commentary on the nature of the political as well as the economic overtones of the technology transfer issue that even governments and businessmen of developed countries may not be sure of their own attitudes toward these problems. Some, whose livelihood is clearly perceived as depending on overseas business, see their incentives policies as being clearly defined and have developed supportive law and organizations. Others are ambivalent.

I have met many U.S. businessmen who are uncertain about either the long-term or short-term advantages of technology transfer. It is interesting, however, that they did press for "clear and consistent technology transfer policies" even in this country. I would suspect this same concern for "predictability" could be heard from businessmen in most developed countries — just as I believe it reflects a major concern about doing business with developing countries.

Now, a final point of this over-all exploration — one which may serve to raise more questions than it answers: I've suggested the expanding pervasiveness of government involvement in technology transfer and the general effects of the regulatory process on entrepreneurial decisions to use such mechanisms as the co-venture process to go abroad. Implicitly, if not explicitly, the discussion has been cast in terms of the decision-making on relevant incentives policies as coming only from national governments.

The question I'd like to raise is whether there is anything that the private sector — the potential co-venturers themselves — can or should legitimately attempt to do to affect the way government decisions about incentives policies are made, or the substance of those plans, particularly as they relate to small business. If governments become more and more demanding in the conditions they impose on foreign investment, it may be that the private sector may have to consider various courses of action in its own interest to help make those conditions the most favorable possible.

First, of course, conferences and LES meetings offer an excellent vehicle for bringing to the attention of governments the kinds of issues those governments really need to address and the kinds of pragmatic measures which should be taken if technology transfer is to be enhanced. Throughout the United States, there are numerous organized groups of business interests seeking to contribute to these efforts, and their work should be supported.

Second, the failure — or unwillingness — of governments of developing countries to provide incentives may often stem as much from the mistrust of corporate motives as from misunderstandings about the economics of the co-venture process. (A company's motivation

to go abroad, where environmental antipollution controls may yet be slack or nonexistent, is an example of an action which could strengthen that mistrust. The company ends up avoiding costly antipollution controls in the U.S. However, at the same time it is transferring its technology abroad, it also imposes its own pollution-generating activities on the foreign country!)

Improve Images

Is there, then, something that potential co-venturers should be doing to improve their corporate images abroad, be they large or small? Should they be considering become better "corporate good citizens" to lessen mistrust and to reinforce their own views that their expanded presence is mutually beneficial to both developing and developed countries? Much is already being done in this regard by members of the private sector, but perhaps they and others, both individually and collectively, could do more to increase their responsiveness to government requests to help meet specific economic — and social — needs of developing countries.

And third, can the private sectors in developing and developed countries find better ways to work with both national governments and international organizations? Can they help to improve the capacity of developing nations to understand the economics of co-ventures and therefore to negotiate for the entry of such activities on terms mutually beneficial for the private sector and for governments?

Certainly, there are many considerations which argue for greater attention to the proper utilization of the co-venture process, as well as other modes of technology transfer, to encourage small and medium enterprise to participate more effectively in this activity.

At the same time, it is clear that there may be a fundamental conflict shaping up between governments and the private sector. Governments most frequently consider the development of incentives from the "macro"-level of policy. For the small and medium industries, however, it is the "micro" considerations which become immediately significant. There can be no doubt that the perspectives of each are different and that a real communications gap generally exists between the two.

The forthcoming task, then, is one of narrowing that gap, with understanding, without rancor or polemics, and with realistic compromise. The gap is, unfortunately, always a shifting one. It is never the same for companies or countries or for products. Lines cannot be drawn cleanly, and both parties to the issue can present valid arguments on their own behalf.

However, if the gap can be narrowed, the result can only be a vastly more positive contribution by small and medium enterprise, through the adaptation of its technologies, to meeting our global needs and, indeed, perhaps to our survival.