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COMMENT: A BUSINESSPERSON'S PERSPECTIVE CONCERNING JOINT VENTURES

Daniel F. Austin[†]

It is my pleasure to be here today and thank you Professor George Dent for including me on the Panel. I represent the businesspersons' perspective concerning joint ventures. I am not a lawyer and I hope that before the day is over I will learn the meaning of the words "punctilio of honor."

I intend to discuss joint ventures from a broad perspective and from a businessperson's view point. Certainly, joint ventures include the largest companies, such as Proctor and Gamble, aligning with either a smaller or larger company. Today, I would submit that there is a whole spectrum, or range, of joint ventures for companies of all sizes. From the perspective of the business that I run at McDonald Investments, which is essentially a service business dealing with corporate customers and investment banking clients, for example, we have tried to change our thinking in terms of how we provide those services to become the most meaningful and relevant to our clients.

Why do companies enter into joint ventures in the first place? Stephen Fraidin[1] talked a little bit about this earlier. I think there are a number of reasons why they choose a joint venture but I will explain on a personal level why we might choose to do that as an organization. We have gone from saying: "We have a series of products, and we are going to deliver them to whoever may choose to buy those products or services?" to a model of saying, "You are my customer, and what is it that I can do to try to own as much of your wallet and become more important to you." Then we try to do our best to come up with all those services that our client cares about. Some of the services I already provide. Some of the services I really do not have the resources to be able to provide right now. So, I am left with three options. For instance, I can choose

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1 *See* Stephen Fraidin & Radu Lelutiu, *Strategic Alliances and Corporate Control*, 53 CASE W. RES. L. REV.865 (2003).

not to ever provide those services. But if I want to fill the client's needs, I may choose to go out and buy a company that can help me be more important to the client. Or, and this is the third option, I can form some kind of an alliance with somebody. This option may end up being a joint venture.

A few years ago, after the start of the Internet explosion, KeyCorp decided to leverage its great relationships with middle market customers – i.e. companies that make things and companies that provide services. The bank reasoned that it ought to be able to find a way to take its strong technology base and create a system allowing those small businesses to procure products through a website which we would create. The service platform was named "Key Next," and it is a simple way for businesses to buy things ranging from complicated services to office supplies. I remember when I first heard of this initiative, I worried that Key would now have to compete with a number of nimble, small, agile, entrepreneurally driven Internet businesses that could be a lot better at hitting that target. But instead of hooking up with the right entrepreneurial company to execute the plan, Key made the decision to build its own platform. A better decision in retrospect would have been to form a joint venture with a technology company. KeyBank's core strength was its relationships with middle market companies. Someone else had strength in knowing how to put together the right web page and have the right technology and was entrepreneurial. Key could provide the leads, the sources, and perhaps the capital. The other company could provide the technological know-how.

After two and a half years of unsuccessfully trying to make Key Next work, the bank essentially dissolved the unit into the other lines of business. One of the reasons why I think joint ventures or alliances are so relevant today is that they allow companies to be more important to their clients by providing more services that are important to their clients. By having seven products or services touching that client or customer instead of two or three, a company can enhance customer relationships and become more profitable.

We have a client in Cleveland that has another totally different reason for forming a joint venture. The Company is a manufacturer and distributor of consumer and industrial products. They have formed a joint venture in China because the best and cheapest way to manufacture their product is in China. If you are dealing in China the most efficient way for U.S. companies to manufacture products is through government-owned manufacturing businesses.

So, this local company has effectively formed a joint venture with an entity in China. They have an ownership interest in the Chinese entity, but the rest of the ownership resides over there, and it is a sizable manufacturing operation. The Chinese entity is primarily concerned with putting people to work, as the entity's overriding objective is employment of the people; for the U.S. company, it is about getting a high quality and inexpensive supply source. These are very different objectives.

If you have two parties that both have the same objective of maximizing profits, then you may run into some of the problems that were talked about in the two earlier presentations. Picking up on Stephen's remarks, I would stress the point that in all forms of joint ventures and alliances, it is important to plan and think through and appreciate all of the potential outcomes, and to try and discuss as many of those situations upfront as possible. I also agree with Stephen that you do not want to over-engineer things in advance because that is also a mistake. But, some problems do require forethought; for instance, it's often necessary to have people begin to think about whether there is a need for capital and about which party is going to be providing it and on what terms. If that capital cannot be provided, what happens next? I think to the extent that you can begin to think about who is contributing what to the joint venture, how will it work, and how will it be governed, I think you go a long way in solving many of the problems. I happen to think joint ventures are tough.

Why do mergers of equals very often fail? In a merger of equals we found that when you have two constituents it was very difficult, especially when times were tough, to be able to make difficult decisions. I just think it adds an extra burden and challenge not knowing exactly what might happen down the road when you put a joint venture together. Thank you.