FDI Success Factors: Evidence from a European Manufacturer in the Chinese Automobile Industry

Halia M. Valladares Montemayor
Mount Royal University

Radu Pirvulescu
Mount Royal University

When considering expansion to new markets in emerging economies, companies need to focus on planning a manufacturing strategy, including facility location, cost efficiencies and competitive advantages. The objective of this research is to describe Renault's FDI strategy for entry into the Chinese car manufacturing industry; to explain how a car manufacturer can be successful in a new market. Additionally, critical success factors were identified through the qualitative research, including: numerous foreign direct investments, willingness to help the partner to become a more competitive manufacturer, and the ability to build strategic relationships (Guanxi) with the Chinese government, suppliers and local dealerships.

INTRODUCTION

This paper explores, studies, and presents Renault S.A.'s FDI strategy to succeed in the Chinese market. This research analyzes the potential success factors for the future growth of the company as a late entrant to that market. The data gathered was analyzed against the company's strategic objectives to pursue new markets in order to increase sales and brand recognition outside of Europe, South America, and the Middle East. The country's market, industry characteristics, and the impact that it has on Renault's future development are compared and contrasted in this article.

The automobile industry in China is the fastest growing in the world and it had numerous foreign automakers trying to exploit it. We draw on Foreign Direct Investment theory (FDI) to understand the motivation of Renault and the choices the company made, along with the implications FDI has for its future. Plausible factors that affect Renault's decisions in an overcrowded market will be looked at as well as the motivation along with critical partnerships. The research questions are: "How can a late market entrant benefit from an overcrowded market?" and "Which strategies helped Renault to achieve its goal?". The relevance of this study is that no data exists on the success factors for late market entrance into a developing country. The research is based on secondary data from renowned journals such as the Journal of International Business Studies and the Journal of Knowledge Management Practice.

LITERATURE TO REVIEW

Chinese Automobile Market

Since its acceptance in the WTO in 2001, China has aggressively started producing and importing more cars. By 2010, it set a new world record of selling more cars annually than any other country in history (China Auto Web, 2011). The total numbers of new vehicles reached 18,061,900; out of this number, 13,757,800 units were passenger sedan cars. The number of registered cars, buses, vans, and trucks on the road in China reached 62 million in 2009, and is expected to exceed 200 million by 2020 (China Association of Automobile Manufacturer, 2012). With such a high population, China is seeing more and more drivers on the road (China Association of Automobile Manufacturer, 2012). McKinsey & Company estimates that China's car market will grow tenfold between 2005 and 2030 (Watts, 2009). The automobile market in China is very strong and the recent numbers suggest that it is nowhere near being saturated. Passenger sedan cars have been the most widely sold cars in China. These are generally broken down into small sized and medium sized cars. Unfortunately, due to the privacy of the Chinese Car Association, exact numbers were not found on the small sized car market. However, in recent research conducted by Roland Berger Associates, Chinese demand for small cars will rise 30% worldwide over the next decade (Berger, 2011). The Chinese government is looking to introduce incentive programs to help small sized cars sales (any car with an engine capacity of less than 1.6 liters). Because smaller cars are priced more affordably, this segment of the market is more appealing to the Chinese consumer.

In China, medium sized cars have been doing very well, as this segment complements the small size segment of vehicles to form the big passenger sedans section. For the past two years, publications in China showed that medium sized cars have been selected as China's Car of the Year, since they match the tastes of Chinese buyers (Wang, Lio & Hein, 2012). This demonstrates that customers see a lot of value in medium sized sedans.

The medium size passenger segment in US, for instance, is 49.76% representing 304,601 per 612,145 sedans sold (WSJ, 2010). It creates the biggest majority of sedan passenger sales, followed by small size cars. The main competitors are FAW Volkswagen and Shanghai GM as they both have really strong positions in the market. Those two companies have come to develop and sell both small sized cars as well as medium sized automobiles. Among the top competitors there is another French car manufacturer that has managed to become profitable in the Chinese market. Peugeot's track of success indicates that French cars are appealing to the local market and have a strong possibility of succeeding with local consumers. Opportunities for market expansion exist in China. Given that there are 58 cars per 1,000 people, there is lots of potential for increasing sales (The World Bank, 2013).

The industry in China works best if a car manufacturer partners and creates a joint venture with a domestic brand (Harwit, 2001). Renault already has a partnership with Nissan which has the potential to create new opportunities in China. This will make for easier access into the market and the opportunity to share valuable insights from Nissan's experience. Furthermore, Formula One racing has operations in China at the Shanghai International Grand Prix; Renault has been a long time participant there. The company's reputation in this race may have an impact on its future sales due to brand recognition. Recent decisions allowed the Grand Prix to be renewed for a further seven years, until 2017 (New Zeeland Herald, 2011).

Alliances

A major factor for business when expanding in any industry is its ability to mitigate risk and ensure smooth operations. Renault is a company that engaged in alliances in Europe as a way to really differentiate itself from competitors and provide quality products. Since it has previous experience with alliances, Renault learned that it helped to learn and acquire new skills and knowledge from its partners while maximizing the utility of its assets (Lei & Slocum, 1992). The motivation to pursue late entrance into China is based on the Synergistic Knowledge Networks, where the two partners are involved in developing synergies of knowledge. The alliance most likely provided a win-win situation where spin-off of new innovations and process improvements promote better overall performance (Nielsen, 2002).

The alliance between Renault and Nissan has seen the two companies open a new, joint China Warehouse in Shanghai. It is a new step in the relationship between the two manufacturers with regards to after-sales and service in the country. This inauguration will provide high quality parts to dealers and car owners in the country. It will operate under the alliance and copy its performance models from where it currently operates smoothly: Hungary, the UK, and Russia (Renault Nissan Alliance, 2011). The alliance saw this opportunity, with China providing the largest auto market, and decided to expand globally. The China Warehouse will cover 8,000 square meters and will provide a full range of auto parts. Around 3,000 are scheduled for Renault and around 10,000 will cover the Nissan models. According to Renault China's Managing Director, Mr. Robert Chan, Renault (Beijing) Automobile Co., Ltd is now officially in operations (Renault Nissan Alliance, 2011). The operations coupled with the Renault-Nissan China warehouse will bring confidence to the consumers and will reflect the high quality services offered. The plant is based on extensive communication and resources system optimization through sharing technical platforms. The platform is based on Nissan's original mature platform and has undergone several modifications and upgrades from Renault. This will lead to the simplification of the internal process and reduce costs, shorten delivery time, and increase satisfaction for the consumer. (See Appendix 1). The special relationship between Nissan and Renault allows the two companies to engage in a joint venture rather than a loose agreement or contract. China bases a lot of its business on Guanxi where the parties involved take time to develop relationships (Browaeys & Price, 2011).

Relationships

Renault can "piggyback" and use Nissan's product and strategy in its entry into the Chinese market. Renault and Nissan have been engaged in a global alliance since 1999 (Renault, 2013). Interestingly enough, Renault will position itself as an affordable luxury brand in China. The original agreement signed between Nissan and Dongfeng in 2003 includes a provision to integrate Renault into what officials in the three companies refer to as a "prosperous triangle" in China. It seems that, in China, the only way to succeed is through synergies and alliances, according to Jeremie Paping, Finance Director of the Renault Nissan alliance (Foy & Sthothard, 2013). Dongfeng achieved the reputation of being China's best-known carmaker outside the country due in part to joint ventures with Honda, Nissan, Peugeot, Citroën, and Renault. Nissan sold 1.25 million vehicles in China in conjunction of course with Dongfeng. This accounted for almost 60% of the Chinese company's net profit in the first six months of the year. (See Appendix 2 & 3)

METHOD

Research Objectives

This paper's research objectives focus on understanding how a later entrant into an oversaturated market can still create enough value for itself and be profitable. We analyze the manufacturer's long term objectives and the motivation for expansion. We take a look at the landscape environment of its existing market and the prospect of China to understand the key differences and similarities. Lastly, we try to uncover the critical factors that will help Renault succeed in the overcrowded automobile industry.

Research Design

Our research into Renault's expansion was initiated by engaging in exploratory research. There are two reasons for this. First of all, there is a very limited amount of accurate information with respect to the manufacturer's operations; this is combined with the host country's low levels of transparency. Secondly, Renault is in the process of executing its strategy and building its power plant. Since so little has been disclosed so far by the company, designing the research to be an exploratory in nature allows us to gain new ideas and perspectives on Renault's car manufacturing processes. Also, we aim to learn about the impact of the factors at the level of the economy and how Renault can adapt to them.

We designed the research to give us accurate historical information about the firm. Once we had this information, we looked to understand the automobile industry in China. Analyzing Renault's historic international business strategy and past records enabled us to identify key aspects of its new expansion strategy. Once the industry analysis and the strategy factors had been investigated, we were able to uncover the main factors for Renault's potential success in China.

Qualitative and quantitative data collected for the purpose of this research were obtained through secondary data from the most reliable sources possible, including reputable websites such as the Chinese Association of Automakers, CIA World Factbook, peer reviewed journals, and various qualified news sources. Publications and the date when published were checked to ensure a recent and relevant documentation was available. The data was chosen based on the relevance it had in relation to Renault's market entry into China and based on its accuracy. The currency conversation is all standardized and dealt with in US dollars or Yuans. Given the fact that the venture is in the approval process by the Chinese Ministry of Industry and Information Technology, very little detailed information is available from China about Renault.

Renault carries the following strategic objectives with it when capitalizing on new markets. Renault likes to penetrate areas where its brand does not yet have a strong presence. It wants to access markets where small and medium sized cars demand has been stable or is on the rise. Renault could capitalize by ensuring that its local strategic alliances can further its development along with sharing of ideas and knowledge. Our research questions were the following: is Renault's FDI strategy in line with its strategic objectives? How can a manufacturer such as Renault be successful in a new market as a late entrant?; and what are the critical success factors to market entrance in China? Our research focused on factors at the levels of the economy and the firm.

The economic level includes the business environment, political, and legal factors all of which contribute to a clear picture of aspects that can harm or accelerate market entry. The research will present the specific characteristics of the country and identify key aspects that are not in Renault's control. To develop an understanding of the industry in the new market and the need for Renault's offering, a broad and multi-perspective view is used. As mentioned above, the factors at the firm level are studied, including the examination of key competitors, their market share and competitive edge along with Renault's available resources. Critical trends and factors are also examined. The concept of a late entrant into a crowded segment plays a big part on the firm's strategy. The construction of facilities so that the corporation produces high quality products at an advantageous cost was a key objective of Renault. The FDI strategy that the firm chose to undertake played a vital role in its ability to do business successfully in China. Investments from the French manufacturer were important to establish an interest in the local Chinese partner. Because of the FDI displayed towards the local partner, Renault could start developing serious milestones in laying a strong foundation for the manufacturing and assembly lines of the automobiles. The willingness to contribute time and financial incentives to minimize the cost of the start-up was only one of the stepping-stones for the joint venture. Because this level of commitment had been established, Renault and Dongfeng could now expand their relationship further by engaging in sharing successes from their own experience. The FDI strategy opened the doors to the possibility of creating a successful partnership where information sharing is a key aspect of the partnership. By engaging in this strategic plan, Renault could benefit by deploying a proven system that it had used in Europe with Nissan and expanding it with its new-formed partner, Dongfeng.

RESULTS

Factors at the Economic Level

China is in a period of economic boom and was not hit as hard as the US in the worldwide recession. China is a strong partner of the emerging "BRICS" (Brazil, Russia, India, China and South Africa) alliance and is looking to prosper in the years to come. A potential issue concerning China is the possibility of a great deal of red tape and the implications it can have on slowing down the process of any outside firm looking to engage in a foreign partnership (Qi, 2014). This could indicate that there will be less transparency when doing business in China and more time might be allocated to persuading the government to be receptive to new business. In China, the government has supported grants and tax cuts for the automobile industry (The World Bank, 2011). Exporters benefit by having joint ventures with local car manufacturers and have access to some advantageous supply chains (Current Trends Now, 2011). The Chinese government wants the automobile sector to create greener and more efficient cars and, as such, is willing to help different local carmakers.

The country has a somewhat complex tax regime and Renault will require further consultation with local tax specialists. In China, Renault could benefit tremendously by engaging in a joint partnership or joint venture as it will be taxed more favourably. Having local connections would speed up developments and make sure the company does not end up paying more than necessary in start-up costs.

While the Chinese environment dictates that car manufacturers establish 50:50 joint venture partnerships, Renault's intention wasn't exclusively based on the law (Kohler, n.d.). When a company uses an already successful existing alliance (Renault-Nissan) to wisely choose a local manufacturer, it goes beyond the mere bare minimum of having a partner to qualify for a license. Dongfeng is China's second largest car manufacturer. Dongfeng has been engaged with Nissan in manufacturing cars in Asia and has a very successful platform for delivering quality cars. Since Renault and Nissan also share their own successful platform in Europe, the formation of the "three star alliance" (Renault, Dongfeng, and Nissan) must be formed with the purpose of speeding up the process of value creation, sharing technologies, and dominating the supply chain channels. Because Nissan acts as the intermediary party and has engaged in previous business with both Renault and Dongfeng, the alliance points towards a very strong relationship and strategic objective. Using each company's core competencies to create lasting competitive advantage, the joint venture between Renault and Dongfeng seems to be a well thought out and executed plan.

In China, income disparity is higher and the spending budget of the middle class is nowhere near linear (English People's Daily Online, 2011). Even so, the Chinese market allows Renault to grow dramatically if it manages to impose itself as a high quality car manufacturer while keeping costs down. France managed to maintain positive relations with China. Over the years it grew its foreign direct investment and export/import relations (Lee, 2013). In China, cultural and language barriers may be more of an issue, but the engagement in a partnership or joint venture with a local company will allow Renault a smoother transition. China has most of the majority automobile segments dedicated to passenger cars; small and medium being the most lucrative (China Association of Automobile Manufacturers, 2012). The industry is still developing but holds a large number of competitors with proportionately smaller market shares. The need for both local and external expertise and knowledge in China is to be emphasized, as a partnership without these critical ingredients is bound to fall behind in technology advancements and quality offerings. For example, the truck and safety utility vehicle segment is notably smaller compared to the passenger car market (China Auto Web, 2011).

Factors at the Firm Level

The executive president of Renault China is Chen Guo Zhang. According to him, the French car manufacturer is set to launch 10 new models in the next 4 years (Shanghai Daily, 2013). The number of dealers will by increased by 60% to a total number of 185 in the following two years. Renault passed one of its main tests in receiving the green light from China's Ministry of Environmental Protection. However, it is waiting for approval from the National Development and Reform Commission and the Ministry of Industry and Information Technology. Because it already got approved by one of the ministries, it is well on its way to see its investment develop. The factory will have a capacity of 150,000 passenger vehicles per year and 150,000 engines per year. Based on the internationalization theory, Renault is moving to China to capture nation specific advantages in China to complement the firm's specific advantages (Buckley & Casson 1988; Dunning 1988).

This is amplified by the Internationalization Theory which states that firms will gain in creating their own internal market such that transactions can be carried out at a lower cost within the firm (Morgan & Katsikeas, 1997). The gel that moulds the Renault – Dongfeng alliance is derived from the commitment and relationship building between the two car manufacturers.

Renault is positioned to have a favourable, if late, start in penetrating the Chinese market. In terms of car sales, China shows great potential when it comes to meeting Renault's strategic objectives of expanding outside of Europe, Latin America, and the Middle East in order to maximize profits. China's automobile market is said to be expected to grow tenfold between 2010 and 2020. This is an immense market opportunity in which any carmaker might establish itself and increase sales. On paper, Renault products match quite well with the car demand that Chinese customers are asking for: affordable, good quality, sedan cars, while offering a choice of eco-friendly automobiles. The history of an alliance of Renault with Nissan, Nissan and Dongfeng, and Dongfeng and Renault is one of the key aspects as to why the French carmaker will be able to be successful in the Chinese market. The alliance between the three companies will ensure high quality products at lower manufacturing costs. The plant is based on extensive communication and resources system optimization through sharing technical platforms. The platform is based on Nissan's original mature platform and has undergone several modifications and upgrades from Renault. This will lead to simplification of the internal process and reduce costs, shorten delivery time, and increase consumer satisfaction. (Renault Nissan Alliance, 2011). The ability to piggyback on Nissan when entering the Chinese market is key to Renault's success. FDI in the Chinese economy is a major reason why Renault has the chance to capitalize on new sales for years to come. Dongfeng contributes to the alliance through the sharing of knowledge and improvement of its manufacturing processes, while Renault gets access to critical local expertise. FDI into the new jointly owned plant between Dongfeng and Renault allows for the new partnership to take advantage of numerous supply chains that combine the external and internal experience of the two car manufacturers. The qualitative data suggests that the success of the new partnership is due to a long process of relationship building between the firms. The success of the partnership boils down to two aspects: the creation of relationships where FDI will create the most value, and the facilitation of sharing of processes, supply chains, and knowledge to benefit both parties. Nissan provided a short-cut for Renault into this alliance by introducing Dongfeng and Renault. With the help of Dongfeng, which has built cars with Nissan in China for the past ten years, the French carmaker is set to start building its $1.3 billion dollar manufacturing plant.

CONCLUSION

This research indicates that, given the saturated car market in Europe for Renault, China can prove to be a great marketplace for developing the brand if certain steps are taken into consideration. The Chinese landscape can prove to be the best opportunity for Renault as the country becomes the largest car manufacturer in the world, even overtaking Japan (Jie, 2010). Serious determinations to engage in further cross platform sharing and helping Dongfeng advance its operations are key aspects of the alliance. This usage of strategic partnerships in the foreign market can contribute to a lucrative deal for Renault as long as the Guanxi relationships are maintained throughout the business venture. As a late entrant to the market, Renault can take advantage of a longer time frame in which it can engage in FDIs. Because it did not rush into the new market early on, Renault waited to see if the alliance between Nissan and Dongfeng stood the test of time. Once this was proven, Renault engaged in the alliance bringing to the table new technologies and knowledge, along with the capital required. The findings reveal that relationship building is a key aspect to any FDI in China and the way Renault approached it through Nissan will prove vital to the company's success. Few joint ventures can succeed in China, especially given the competitive field; Renault is on the brink of positioning itself, along with Dongfeng, to reshape the car landscape in China.

This research study has the following limitations. The study is focused in only one sector or industry; this does not allow the analysis of the causal relationships between different variables. According to Young (1996), causality cannot be evaluated in studies of sectional type conducted in one determined timeframe, and this is how this research has been approached. The biggest disadvantage in researching only one unique sector is that the generalization of the results should be approached with caution (Prieto Moreno, Santidrian Arroyo, Valladares Montemayor, 2007).

We used a positivist approach which critics argue cannot explain the whole observed universe of the industry. Critics suggest that the positive approach is reductionist because it only studies economic factors and leaves complex social factors out of the study (Larrinaga-Gonzalez, 1999). However, in our research we do consider socio-cultural implications at the country level in the discussion of Guanxi. Furthermore, it is important to mention that no theory, in any discipline, explains the total universe observed. Therefore, the fact that we cannot explain all reality in this research does not invalidate the findings. Prieto and Perez (1992, p. 652), and Monterrey Mayoral (1998, in Valladares Montemayor 2009, p.190) note that "one methodology should not be abandoned simply because it cannot explain and predict the entire observed phenomenon".

This paper studied the very rare case of a late entrant into a developing country's automobile segment. It presented information about how and why Renault was interested in being a late entrant into the Chinese market and put emphasis on the firm's FDIs and alliance formation process. Further research should be conducted in both the short term and the long term to see if Renault's decision was a rewarding one. We suggest that further investigations look closely at the return on investment that the company gains through these FDIs. A development of the alliance between Renault – Dongfeng; Nissan – Dongfeng, and Renault – Nissan should be analyzed to see if transfers of technological knowledge and production platform are benefiting one party more than the other, since literature supports the idea that alliances are built on win-win situations.

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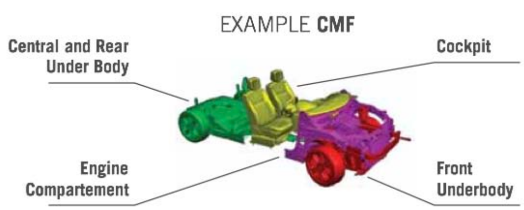
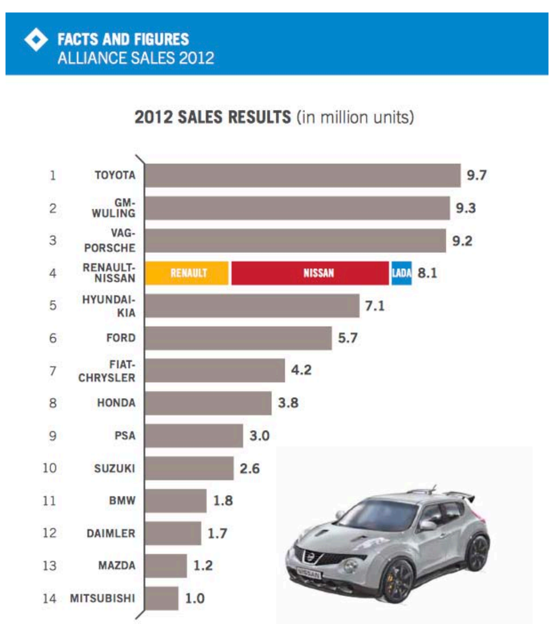
APPENDIX 1



Source: Renault S.A. (2013)

APPENDIX 2



Source: Renault S.A. (2013)

APPENDIX 3

Source: McKinsey & Company (2012)