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Piggybacking: A successful road to the Chinese market?

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**Wirtschaftswissenschaftliche Fakultät
der Eberhard-Karls-Universität Tübingen**

**Piggybacking -
A Successful Road to the Chinese Market?**

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1. Introduction

The Chinese economies of Hong Kong, Taiwan and the People's Republic (PR) of China belong to the most successful developing markets of recent decades. Greater China has increasingly attracted imports, foreign direct investment and "new forms of internationalization" (Borner, 1986). The latter encompass such market access strategies as the so-called "piggybacking", whose analysis will be subject of this paper.

Piggybacking is generally defined as a strategy to penetrate foreign markets using the specific knowledge of a local partner in order to minimize market entry costs. More precisely, it is "a non-equity arrangement wherein one producer markets the products of another producer" (Terpstra/Yu, 1990). The local firm (carrier) performs as a distributor and marketing agent for the products of the foreign firm (rider).

While this cooperation reduces the rider's cost of market entry, the carrier may gain essential knowledge of the rider's intellectual property which determines the rider's competitive position. Therefore, firms from developed countries that engage in piggybacking undertake the risk of the carrier possibly using the newly acquired valuable information to compete in their own market. Thus, there is a tendency towards disruption of cooperation agreements.

The following essay deals with this kind of conflict as a possible consequence of the piggybacking strategy, presenting a theoretical part (chapter 2) followed by an empirical analysis (chapter 3). The latter is based on an opinion poll among German firms that have been asked to evaluate the relative importance of various advantages and disadvantages of international cooperation in Chinese markets. The questionnaire was sent out in October 1997. Finally, some conclusions will be laid out.

2. Piggybacking and the Theory of the Firm

In this paper we will derive the decision making problem of firms engaged in piggybacking from the transaction cost approach for Multinational Enterprises (MNE). According to this approach (Dunning, 1981) the MNE is in possession of specific knowledge, which is used to offer differentiated goods in monopolistic markets. Specialized knowledge may also become part of the production technology and allow the firm to assume a leader's position among its competitors.

These so-called owner-specific advantages (Caves, 1992) are not confined to new products or a technologically superior production function. In many modern industries, specific advantages derive from highly specialized knowledge in all spheres of internal and external firm activity. Often these "pieces of special know how" develop their complete economic value only by combination: Both the firm-specific organization of a heterogeneous set of skills and specific knowledge in a unique web of intra-firm relations determine the value of a modern firm.

Knowledge and skill-determined intangible assets are of outstanding importance because they decide on the firms relative position in the process of innovative competition. Intangible assets lose this property instantaneously, if the specific knowledge becomes available to the competitors. The reason is that inherent to knowledge are some characteristics of a public good, i. e., its economic value declines as soon as it becomes freely available. In other words, the economic value of specific knowledge derives from its exclusiveness. Exclusiveness of knowledge is a precondition for the establishment of market power which, in turn, enables the innovative firm to generate the funds necessary to secure the profitability of its investment in new products and production processes.

One of the crucial points of any cooperation agreement or any joint activity with a potential foreign competitor stems from this role of specific knowledge. In the case of piggybacking the risk is twofold: The carrier has to unveil its specific knowledge of the foreign market to the rider, while the latter may be forced to dismantle (at least partly) its intellectual property to the former. Therefore, any joint economic activity with a foreign competitor is fragile because it is open to abuse.

The "modern theory of the firm" is helpful to gain more insight into this problem. According to the transaction cost approach to multinational firm behavior international firms evaluate the cost-benefit balance of an international engagement. While benefits of internationalization are determined by the ability to utilize specific ownership advantages in large foreign markets, international engagements might be confined by additional transaction costs.

If the expected benefits outweigh additional costs the question arises of *how* to penetrate the foreign market. The options are exports, foreign direct investment (FDI) or an intermediate form of action. To a large degree this decision depends on the relative attractiveness of foreign and domestic markets. The environment envisaged by the transaction cost theory takes into account several factors such as artificial and natural trade barriers, institutional settings and economic policies at home and abroad in order to determine the decision-making¹.

This approach has been most convincingly demonstrated in Dunning's OLI paradigm (Dunning, 1981). Dunning combines the theory of the firm with elements of trade and location theory using the criteria of ownership (O), internalization (I) and location (L) advantages. Ownership specific advantages are assets and rights which are assumed to be exclusive to the enterprise which owns them. Some of them, at least, can be transferred across national boundaries. The firm possessing the assets decides whether to internalize their use or sell this right (not the assets) to other companies. Location advantages depend on the attractions of location specific endowments, which are not transferable across national boundaries, offered by the home and the foreign country. The decision-making problem is illustrated by a simple matrix as shown in *figure 1*.

¹ The simple trade model determines the attractiveness of a distinct industry by relative factor endowment.

Figure 1
OLI-Matrix

Route of servicing market	Advantages		
	ownership	internalization	(foreign) location
Licensing	yes	no	no
Export	yes	yes	no
Foreign direct investment	yes	yes	yes

A firm in possession of "specific ownership advantages" has the possibility to give out licenses to other producers. In such case, the success resulting from innovation (the investment in research and development (R&D)) is determined by the inflow of license fees. Usually, an innovation developed within a firm may also be applied successfully within this particular firm. Thus, the combination of "internalization" and "ownership advantages" is superior to mere licensing. The reason is that sufficient ex-ante information on the economic value of an innovative good (or process) is not available. The information deficit prevails on both sides. Therefore, the market price of the innovation is higher than the contracting price. Consequently, the innovator will be better off if he produces the new product himself.

If the decision is made in favor of internal use of the specific knowledge the question arises of where to produce a new product: At home or in a foreign market. This problem can be solved with respect to the parameters of location advantages mentioned above.

In order to introduce piggybacking into this model we emphasize the fact that the internalization advantage of a firm is expected to be the larger the more it covers the whole value added chain from market evaluation to production, distribution and marketing. Such a concentration of competitive strength may be quite normal as long as the firm operates on the local market. But the capability to organize distribution channels and acquire competence in marketing in foreign markets will often be restricted. A successful foreign market penetration then calls for either a comprehensive market entry strategy in order to generate new skills abroad or for cooperation with local suppliers that already dispose of these skills.

In terms of the OLI matrix this means that the ability to internalize the whole value-added chain may differ between the home and the foreign market. In particular, the "internalization advantage" must be split into a home and a foreign component. If the firm decides to enter a new market, the internalization advantage abroad must be achieved by acquiring skills and knowledge in all relevant fields. This strategy does not involve high additional costs, if foreign and home markets are similar. But the cost of market penetration rises with geographical, cultural and economic distance. Consequently, entry in the Chinese market is far more expensive for a Western European firm than for a firm originating from that region. Various economists believe that piggybacking is a useful strategy for the rider to overcome these entry barriers. The firm entering the market cooperates with a local partner already in possession of the relevant internalization advantages in the foreign market and thus, minimizes the cost of market entry.

The carrier, too, may have various motives for cooperation, for instance a possible increase of his market share, gains derived from a positive image conveyed by the foreign brand name or simply by technological and knowledge spill-over effects. These expectations can be summarized as the attempt to participate in "ownership advantages" of the rider. Thus, from the rider's point of view, the piggybacking arrangement is equivalent to trading ownership advantages (products, processes, organizational skills) for internalization advantages abroad.

An ideal constellation occurs if the carrier himself is bound to enter the rider's market due to similar motives. In this case, both carrier and rider trade their specific ownership and internalization advantages they possess at home with each other. Such a mutual agreement diminishes costs of entry for both partners and allows them to realize gains from mutual spill-over effects of specific knowledge.

Mutual benefits, however, are at risk, if one or both of the cooperating parties abuse information on the other's specific knowledge. On the one hand, the rider could acquire the carrier's specific foreign market knowledge and start its own market penetration strategy. Eventually, the rider might even evict the carrier from its home market. On the other hand, the carrier could misuse its knowledge of the rider's

specific product and production skills for re-engineering and start to compete with the rider in this field.

The latter case is of particular concern to MNE of industrialized countries entering emerging markets because these kinds of arrangements usually combine partners of different technological levels. As demonstrated earlier modern industrial and service enterprises rely heavily on specific knowledge to secure their competitive position on innovative markets. For this reason the partial unveiling of the production process is very critical in a piggybacking arrangement. Moral hazard is at hand when the rider's competitive position can seriously be threatened by dishonest conduct of the carrier.²

Apparently the rider's opportunity to prevent such moral hazard is determined by his capability of bundling knowledge and skill components to so-called "core abilities" (Porter, 1991). Such a web of firm specific abilities cannot be copied too easily (Borner, 1986), so that the risk of re-engineering is minimized and ownership knowledge can be transferred to the carrier without damage. Assuming that strong webs of core abilities more often prevail in larger-sized companies than in small and medium-sized ones³, the moral hazard problem is expected to have especially strong impact on the cooperation decision of smaller companies.

Summing up these theoretical considerations leads to the conclusion that technology intensive MNE trying to enter a foreign "low-tech" market have to take into account three major conflicting aspects: First, market penetration is costly and time consuming. The risk of failure is especially high when great distances (geographical, economical and cultural) exist. Thus, piggybacking may substantially facilitate market entry.

Second, as a consequence of piggybacking the rider partially transfers his specific knowledge to the carrier. This loss of knowledge is the price of cooperation and

² If the rider is an enterprise from a less developed country the situation is different. The focus here is on the first case.

³ Technologically advanced small and medium sized enterprises often rely on a relative small basis of highly valuable ownership specific knowledge. The "core abilities" are concentrated in a small number of workers, so that the re-engineer does not have to break up a highly differentiated system of knowledge interdependences.

should not turn out as a major problem as long as the carrier plays by the rules. If, instead of promoting its products, the carrier misuses specific knowledge to compete on the foreign (or the world) market, the advantage of applying the piggybacking strategy has to outweigh the cost of knowledge deprivation.

Third, the rider's risk of losing competitive strength due to a possible violation of its intellectual property rights appears to be crucial for small firms whose market power relies heavily on a small set of top technologies.

3. Empirical Analysis

3.1. General Results

Based on a questionnaire that was answered by 79 German enterprises (equaling 18% of the recipients), detailed information on firm behavior in the Chinese market has been achieved. These companies were categorized in large-sized (47 or 60%), medium-sized (11 or 14%), and small (21 or 20%). An enterprise belongs to the category of small firms, if either the sales volume is lower than 10 million DM or it has less than 50 employees. With sales of DM 10 to 42 million or 50 to 250 employees a firm is considered a medium-sized firm. Finally, large firms have sales over DM 42 million or more than 250 employees.

Most activities of German firms in the Chinese markets consist in exporting. 63% of the firms operating in Hong Kong use this option, 66% in the PR of China and 72% in Taiwan. While wholly-owned subsidiaries are rarely found in all three markets (5-6%), the significance of intermediate forms of cooperation, such as licensing and joint-ventures, differs remarkably between Taiwan and Hong Kong (13% and 9%) versus the PR of China (38%).

Asked about the motivation to enter the Chinese markets, 81% of firms correspondingly answered that they were primarily interested in aspects of demand. This was a clear result. For most enterprises the expectation of growing future

demand is stated to be the crucial factor for their engagement, rather than the actual size of the market itself.

The share of enterprises considering local production costs as an important factor influencing their decision is about 10%. German firms (or producers from technologically advanced countries in general) predominantly offer differentiated products that incorporate high degrees of human capital. As a result of monopolistic markets, factor costs are of minor importance because these products sell at a premium price. The need to secure specific ownership advantages increases with the firms dependence on the premium price⁴.

We now take a closer look at market entry. *Table 1* illustrates the relative importance of nine different aspects of market entry barriers. The lack of information about local demand and a nontransparent bureaucracy rank highest in the category of "very important" barriers (32% each). Insufficient information about the distribution possibilities ranks second (29%).

More than 40% of firms classify cultural barriers and the uncertainty of the political circumstances as "unimportant". Likewise, the quality of skilled labor is not a very high barrier to entry (14%). The results are even more striking when categories are partially aggregated. Summing up the categories "very important" and "important" as well as "less important" and "unimportant" reveals the structure of entry barriers even more clearly: Bureaucratic obstacles (66%), lack of distribution channels (63%), insufficient knowledge of local demand (62%) and legal impediments (59%) are perceived as the strongest barriers to market entry. Problems such as foreign culture (24%), uncertainty of the political circumstances (35%), inadequate level of education of the local work force (36%) and language (44%) are considered as minor obstacles.

⁴ Local firms (especially Hong Kong and Taiwanese firms operating in mainland China) are usually in a different market position. With the beginning of the course of economic reform in the PR of China, they followed a line of using factor cost differentials to their advantage. As a consequence, Chinese firms manufacture standard products and sell these at cost-pricing level on the local and the international market.

Table 1
Assessment of market entry barriers

Market entry barrier	Very important	Important	Less important	Un-important
Incomplete information about local demand	32%	30%	10%	28%
Incomplete information about the distribution possibilities	29%	34%	14%	24%
Inadequate level of education of the local work force	14%	22%	25%	39%
Competition	22%	20%	29%	30%
Uncertainty concerning legal regulations	24%	35%	9%	32%
Bureaucratic obstacles	32%	34%	11%	23%
Language	24%	20%	25%	32%
Cultural / social obstacles	5%	19%	29%	47%
Uncertainty concerning political circumstances	6%	29%	24%	41%

Producers located in markets for differentiated goods rely heavily on precise information on the market. They use diverse channels of distribution because their products differ from those of mass suppliers. Demand for such products is often small. For instance, special machines are of use only to a small number of clients. In an undeveloped market like the PR of China, producers might not even be informed about technical solutions to their problems, which are available on the global market. Then, demand for this good simply not exists, in spite of the innovation's value to potential clients. Marketing becomes a fundamental factor of economic success, but gaining access to the circle of potential clients in a large and unfamiliar market is an extremely difficult task.

Special distribution channels are of particular concern in entering these markets. They are the more important, the more the product requires repair and maintenance services. If these kind of services cannot be fully supplied the product becomes costlier to the client and may as well damage the producer's reputation. Last but not least, legal and administrative protection is an especially heavy burden for producers operating in differentiated markets. Fixed costs of legal approval for sophisticated products are high and levied on a relatively small quantity of products sold.

So far it is tempting to state that a cooperation agreement with a local producer, who is well positioned and familiar with the market, should represent an attractive market entry strategy. In fact there seems to be a high correlation between the strongest entry barriers (*table 1*) and the expected advantages of cooperation (*table 2*).

Table 2
Expected advantages of cooperation

Expected advantages	Very important	Important	Less important	Un-important
Utilization of the partner's market experience	56%	23%	6%	15%
Utilization of the partner's distribution network	54%	19%	10%	16%
Widening of the product range	3%	16%	29%	52%
Utilization of the partner's technological know how	4%	16%	29%	51%
Avoidance of misunderstandings due to culture and language	34%	23%	15%	28%
Support in dealing with local administrators	46%	27%	6%	22%
Reduction of the risk of market entry through limitation of commitment	24%	33%	9%	22%

In these cases 56% and 54% of firms report that the partner's knowledge of the new market and the provision of established distribution channels have the highest priority in cooperation agreements, followed by the capability to manage problems on behalf of foreign bureaucracy (46%) and misunderstandings due to culture and language (34%). The local partner's scope of products (3%) and his know how (4%) are of minor importance to most German firms. Again, when aggregating categories "important" and "unimportant", the result is even clearer. The positive impact of the partner's market knowledge, an effective distribution system and the familiarity with administrative procedures were important to most firms (79%, 73% and 73%) in their decision-making. The factors widening of product range and utilization of the partner's technological know how do not find much attention, they are not important to about 80% of firms.

The question arises why only few such cooperation agreements are implemented then. The reasons become prevalent when asking firms what they perceive as disadvantages of cooperation. *Table 3* shows the relative importance of five potential disadvantages. Obviously, the risk of technology transfer is considerable, with 65% of the firms classifying it as an important problem (among those 41% even marked: "very important"). Almost as important ranks the insufficient control about the local partner's marketing (58%), his business practices (61%) and legal risks (53%). Political risks due to the partner's provenance are of minor importance (23%).

Table 3
Expected disadvantages of cooperation

Expected disadvantages	Very important	Important	Less important	Unimportant
Undesirable (unauthorized) technology transfer	41%	24%	11%	24%
Insufficient control of marketing activities	20%	38%	18%	24%
Insufficient control of the partner's business practices	28%	33%	19%	21%
Legal risks	18%	35%	18%	29%
Political risks due to the partner's provenance	3%	20%	34%	43%

Obviously, there is strong uncertainty about the reliability of the local partner concerning the terms of the cooperation agreement and intellectual property rights. German firms seem to perceive disadvantages as outweighing the advantages of cooperation, despite their large number. As a consequence German firms often avoid cooperation.

Comparing these empirical results to both the theory of the firm and the modern theories of trade and growth⁵, they turn out not to be surprising. In the production process human capital is the crucial factor of high-value production and service activities. Therefore, firms from advanced countries are eager to protect this precious asset from potential competitors. Cooperation agreements leading to a

⁵ See for example Grimwade (1989).

partial transfer of such assets are successful as long as both partners benefit from the partnership. Both want to be sure that they can control the outflow of specific knowledge. Companies will probably be risk averse, facing the complexity of such agreements and the uncertainty about the partner's actual behavior. For this reason, the potential of a successful cooperation will not be exhausted completely.

3.2. Cooperation with partners from Taiwan, Hong Kong and the PR of China

In this chapter we examine our results according to the provenance of the cooperation partner. When asked about particular advantages and disadvantages of cooperation projects, the answers differed for potential partners from mainland China, Hong Kong and Taiwan.

While cooperating with a mainland Chinese partner German firms expect advantages in the utilization of the partner's market experience (65%), distribution network (53%) and knowledge of the cultural, commercial and social circumstances (53%). Although, these criteria are perceived as most important advantages of a cooperation with a partner from Hong Kong or Taiwan (43%, 35%, 39% and 38%, 30%, 35% respectively), when compared to the results given for a potential partner from the mainland they appear less important.

The advantage of an increase in technological know how and the enlargement of the product range are classified as unimportant. Remarkably, with a firm from Hong Kong (73% and 67% respectively) or Taiwan (the same) they appear to be relatively more unimportant for cooperation arrangements than with a firm from the PR of China (66% and 61% respectively). Another astonishing fact is that the familiarity with western business practices is perceived as relatively unimportant for potential Hong Kong (52%) and Taiwanese partners (56%) and even more so for mainland Chinese partners (62%). This could, to some extent, be considered a contradiction to the classification of the disadvantage "insufficient control of the partner's business practices" as very important.

Turning to the perceived disadvantages of cooperation, the risk of losing ownership advantages is a very important criteria when engaging in cooperation with partners from mainland China (44%), but less important for an arrangement with a firm from Taiwan (29%) and Hong Kong (19%).

In general, German firms only report a minor risk of negative impact on the quality level of their products through a cooperation with Taiwanese and Hong Kong firms (only 5% to 6% see this as a very important disadvantage of cooperation). In the case of a partner from mainland China, the figure amounts to 18%. The political risk pertaining to the provenance of the partner does not seem to pose a significant threat; 80% of the firms classified this disadvantage as "less important" or "unimportant" when concerning a mainland Chinese partner, 82% for Taiwanese partners and 89% for partners from Hong Kong respectively.

Taiwanese and Hong Kong firms seem to have a better chance to find a German cooperation partner than firms from the PR of China. Comparing the assessment of potential partners from Taiwan and Hong Kong, the latter perform slightly better.

3.3. Small and medium-sized enterprises

For most of the initial period of globalization, internationalization of production has been restricted mainly to big enterprises. Only recently, small and medium-sized enterprises have been engaging, albeit hesitantly, in international activities beyond trade. The reasons are obvious. International production requires large amounts of capital, a skillful and educated work force as well as considerable resources in order to evaluate foreign markets and the risk of entering them. Most small and medium-sized enterprises refrain from such an engagement because it exceeds their financial resources as well as their organizational capabilities. Any engagement beyond pure exporting will be subsumed under the term "new forms of internationalization", i. e. intermediate activities such as licensing or piggybacking.

Considering the limited resources of small and medium-sized enterprises, we expect exports to rank high and internationalization of production (i. e. 100% subsidiaries)

to be unimportant. Empirical data indeed confirms this assumption. Among small enterprises exporters to the mainland Chinese market make up for 55% to Hong Kong 52% and to Taiwan 71%. None of them chose the path of establishing subsidiaries. New forms of internationalization have some importance in the Chinese market (16%) but are almost completely absent in Taiwan (6%) and Hong Kong (3%).

The perceived entry barriers are quite similar to those derived from the whole sample. Incomplete information about local demand and distribution possibilities rank highest, the former being considered "very important" or "important" by 58%, the latter by 61%. Political risks (26%), cultural differences (6%), language (39%), bureaucracy (48%) and legal barriers to entry (45%) are less important on that scale.

The question of cooperation advantages and disadvantages revealed quite similar results. However, cooperation advantages are perceived more distinctly. 68% of the small firms consider the utilization of the partner's market experience as very important while only 56% of all firms in the sample do. The utilization of the partner's distribution channels account for 58% and 54% respectively. Small companies do not perceive bureaucracy and language to the same degree as entry barrier as bigger ones do (32% and 29% versus 46% and 34%). Potential disadvantages of cooperation do not differ systematically. While the assessment of the risk of unauthorized technology transfer (42%) and insufficient control of business practices (26%) is about the same (41% and 28% respectively for the whole sample), the danger of low-quality marketing (16%) and legal risks (13%) seems to be less prevailing (20% and 18% respectively).

On a broad scale, however, the assumption that small and medium-sized enterprises are more vulnerable to unauthorized technology transfer and insufficient control of the partner's activities does not hold. Such companies rather see a stronger entry barrier in insufficient knowledge of the foreign market and, therefore, highly assess the potentially positive effects of cooperation in this field.

Analyzing the data, two limitations of the questionnaire have to be taken into consideration. First, the sample for medium and small enterprises is small and may

suffer from non-specific answers. Second, there may be a qualitative difference between answers of large and small companies due to the possibility of the former having already gained more practical experience in the Chinese market than the latter.

3.4. Scope for Cooperation

In the last section we analyze possibilities to improve cooperation agreements. We asked the firms to evaluate the relative importance of six factors: Stronger commitment of the partner for common goals; better information about potential partners; improvement of the partner's technological capability; higher legal security of cooperation contracts; reduction of political uncertainties; better information about the political and economic development of the region.

Table 4 shows that three factors are of utmost importance. 44% of the enterprises find it "very important" to gain more information on a potential partner from the PR of China. 42% believe that cooperation could become more successful if the local partner were to put more emphasis on the implementation of common goals. 41% find it necessary to improve the cooperation agreements on a legal basis. Improving the technological capability of the local partner ranks next reported by 29%, but is far less important than the three main factors for better cooperation. Gaining further general information on the political and economic environment of the new market appears to be less important (16%).

For cooperation partners from Taiwan and Hong Kong the relative importance of these factors is quite similar, but each factor separately is of minor importance. Thus, better compliance of the partner with the common goals is "very important" to 27% of all firms in the case of a Hong Kong firm and to 28% in the case of a Taiwanese firm. Better information about the potential partner is "very important" to 27% when the partner is from Hong Kong and 23% when the partner is from Taiwan.

Table 4

Possible improvements of cooperation identified as "very important"

Partner from	all companies			small and medium-sized companies		
	PR of China	Hong Kong	Taiwan	PR of China	Hong Kong	Taiwan
Stronger commitment of the partner for common goals	42%	27%	28%	32%	26%	29%
Better information about potential partners	44%	27%	23%	35%	29%	26%
Improvement of the partner's technological capability	29%	11%	6%	16%	16%	6%
Higher legal security of cooperation contracts	41%	15%	15%	19%	10%	10%
Reduction of political uncertainties	20%	11%	6%	13%	6%	3%
Better information about the political and economic development of the region	16%	8%	8%	13%	10%	10%

Turning to small and medium-sized firms we do not find significantly different results (table 4). An exception is that these enterprises are less determined in their judgement of cooperation with a mainland Chinese partner. Thus, compared to the assessment in the whole sample, the three most important aspects of improving cooperation agreements are less clearly identified as "very important" in the small sample: 32% of the small and medium-sized companies consider stronger commitment of the partner for common goals as "very important", 35% want better information about potential partners and only 19% request higher legal security of cooperation contracts.

Again, the small sample only allows for cautious conclusions.

4. Conclusions

From the theoretical part of this paper we derived two major points. First, piggybacking is a successful market entry strategy for firms, which are not able to internalize their ownership-specific advantages abroad. Utilization of the partner's experience in the foreign market represents the predominant advantage of the rider. Its main disadvantage in a piggybacking arrangement is linked to the moral hazard of the partial unveiling of his production process including his intellectual property to the carrier. Therefore, the decision of the rider equals a trade-off between ownership advantages, which it exposes to the partner, and internalization advantages abroad, which it gains through the cooperation.

Second, small and medium-sized enterprises are more likely to engage in a piggybacking arrangement because they face more difficulties to internalize their ownership advantages abroad. At the same time, the risk of losing their assets is higher, because they are less likely to build up "core abilities", which can not be copied easily.

The empirical part generally supports the theoretical results. The PR of China is viewed as an important but difficult market. The German firms that answered the questionnaire stressed the fact that incomplete information about local demand and distribution possibilities are the main barriers to market entry. Consequently, they regard the potential partner's market experience and distribution network as the most important advantages of a cooperation arrangement.

The inherent risks of a cooperation are also estimated as expected. Unauthorized technology transfer and insufficient control of the partner's marketing activities are regarded as main disadvantages. Remarkably, political risks due to the partner's provenance are not considered a major disadvantage, i.e., German companies are generally not discriminating against companies from Hong Kong and Taiwan in their search for a cooperation partner in the Chinese market.

Empirical data for small and medium-sized enterprises, however, do not support the theoretical considerations. The assessment of market entry barriers, as well as advantages and disadvantages of a cooperation arrangement are roughly the same for small and medium-sized enterprises as for the whole sample. The assumption that small and medium-sized enterprises are more vulnerable to unauthorized technology transfer and insufficient control of the partner's activities does not hold.

The empirical results prove that cooperation arrangements are strongly considered by German firms as possible market entry strategy for the Chinese market. But the threat of unauthorized technology transfer still remains. German firms seem to trust companies from Hong Kong and Taiwan more than those from the PR of China. Comparing the assessment of potential partners from Hong Kong and Taiwan, the former perform slightly better.

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