

Joint Ventures in Construction Firms in Saudi Arabia

By

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A thesis paper summary

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Abstract

This paper is a summary of the research work done by Mr. Kamal Abbassi in fulfillment of the requirement of an MS in Construction Engineering and Management. The paper discusses the main problems facing the joint venture firms in the eastern province in Saudi Arabia. A survey of thirty firms For Saudi-Foreign Joint venture and twenty firms for Saudi-Saudi joint venture from the eastern province was under taken.

The survey includes different questions such as role in construction, type of construction, grade as specified by ministry of commerce, reasons for making joint venture and what type of joint venture. Also, the questionnaire includes seventeen different problems facing the construction joint venture firms. These problems are ranked according to the importance index, which measures there level of importance. A computer statistical package (SAS) was used to analyze the data.

A hypothesis that Saudi-Saudi joint venture and Saudi-Foreign joint venture agree on the ranking of importance indices was tested and showed not to be true. It was concluded that for Saudi-Saudi joint venture, payment delay from the owner, government regulation and lack of adequate study of partner before forming the joint venture are the main problems. For Saudi-Foreign joint venture, poor written contract, lack of adequate study of partner before forming the joint venture and government regulation are the main problems.

1. Introduction

As today's projects become more complex and sophisticated, one finds the need to give in-house expertise through an inter-professional temporary agreement of a joint venture where two or more organizations cooperate to meet the total needs of a project. Joint venture in this paper is defined as a union of two or more parties who agree to share the responsibilities, profits and losses of construction contract. The joint venture can consist of any type of agreement that two or more parties elect to share.

1.1 Statement of the Problem

Transfer technology and risk sharing are major items in forming joint venture business. Working together for success is the aim of the joint venture. So, joint venture will succeed when different nationalities participate in the project. This is true not only in business activities but also in trade relationships, since it concentrates on the combination of resources between two independent organizations in order to improve their market growth potential.

It is an unfortunate fact of business that many joint ventures fail. The failure cannot be attributed to a certain country or product area, but is due to the difficulties involved in handling a complex marketing tool. So the significance of this study is to identify problems faced by joint ventures in Saudi Arabia and to suggest ways to alleviate these problems in future work.

1.2 Previous Study

Many papers and books have been written about construction joint ventures. The literature does not reflect any studies concerning construction-related Firms in Saudi Arabia.

"Construction Joint Venture" is a paper presented by David Ashley. His study concentrated on the theory of joint venture partnership, formed primarily for sharing construction related risks. The theory for partnership or joint ventures involves simple but realistic assumptions about the individual participants' behavior. His conclusions were:

- a. Due to a reduction in total project contingency, a joint venture of contractors has a competitive advantage over any of the same contractors acting independently.

b. Increased liabilities by each contractor for the action of the others may produce competitive advantages.

c. When project shares are distributed, each partner will have same rate of return on cost.

d. Since optimal project shares may vary with bid amount, they should be jointly determined with the bid amount.

Black, in his paper entitled "To Joint Venture Or-Not-Is-It For Your Firm?" discusses the management system by pointing out many practical problems to help the reader to eliminate guess work, avoid pitfalls and reduce costly trial and error methods. The paper discusses marketing joint venture so he starts by listing major marketing items to be examined, such as required skills, background knowledge, and necessary contracts for the project. He concludes that after participation in a joint venture, the owner should summarize and analyze whether it is beneficial to get involved in another joint venture, and if so under what circumstances.

Lammie and Shah, in a paper with the title "Managing Joint Venture in Large Public Projects", discuss how joint venture helped to finish one of the biggest projects in the United States in a successful way. From many years of joint venture experience, Lammie and Shah summarize the following:

1. With the clear objective of achieving designated revenue, service and dates, all other considerations become secondary.

2. Major organization and staff change was an actual part of the project life style.

3. Each project is unique in itself with the only common denominators being challenge and risk.

4. Any new project starting up from zero bases would make a serious error to ignore the experience of other agencies developing comparable systems.

1.3 Objective of the Study

The main objectives of this research are to:

1. Undertake comprehensive analysis of joint venture in construction firms, particularly in Eastern Province in the Kingdom of Saudi Arabia.
2. Identify and analyze the problems which faced joint ventures in the construction Firms in Saudi Arabia.
3. Test the hypothesis that the Saudi-Saudi joint venture and Saudi-Foreign joint venture agree on the importance index ranking of problems facing joint venture

1.4 Procedure

The methodology of this research consists of the following steps:

Step 1: Study of all types of joint ventures. A literature search is focused on the problems of joint venture.

Step 2: Data is gathered through site visits, interviews and discussions with partners, the Saudi and the foreign joint venture and the Saudi - Saudi joint venture.

Step 3: From the preliminary interviews and the literature review, a questionnaire is formulated.

Step 4: The questionnaire is distributed to both ventures. The Saudi-Foreign Venture and the Saudi-Saudi Venture.

Step 5: Data was gathered from the questionnaire and analyzed statistically.

Step 6: Recommendations based on the analyses of results are suggested.

1.5 Scope and Limitation of the Study

This research is limited to construction Firms in Saudi Arabia, in the private sector only. This study will be restricted to the construction firms in the Eastern Province of Saudi Arabia.

1.6 Significance of the Study

The results of this research will highlight the main problems facing joint ventures. From the discussion of these problems, recommendations will be given to eliminate or reduce joint venture problems. Also, this research will be a base for future study in this filed.

2. Joint Ventures

A joint venture is a cooperation formed by two or more separate entities, usually corporations, which typically allocate ownership based on shares of stock controlled. This definition can be sub-divided into two, contractual and equity joint ventures. The contractual joint venture is an agreement between two or more separate firms for the exchange of performance, while an equity joint venture provides for future joint decision making in a jointly owned company.

2.1 Reasons for undertaking Joint Ventures:

- 1) To share the risk
- 2) To generate required binding capacity
- 3) To reduce the number of competitors

- 4) To satisfy the customer's desires
- 5) To give specialized treatment on a job requiring unfamiliar expertise
- 6) To give an additional source of manpower
- 7) To give an additional source of supervision
- 8) To give an additional source of financing
- 9) To provide more than one estimate of the job for comparison
- 10) To satisfy local customs and practices and provide local representation on a project in an unfamiliar area.

2.2 Types of Joint Ventures

- 1) Construction and land development joint ventures
- 2) Exploration and drilling joint ventures
- 3) Mining
- 4) Marketing and distribution joint ventures

2.3 Characteristics of Joint Venture Projects

Generally project characteristics which need to be joint ventured are:

- a) High risk projects
- b) Foreign work
- c) Large scale projects
- d) Projects requiring technology

3. Problems facing Joint Ventures

Since joint venture is a union of two or more parties, several problems will certainly occur. The problems can be divided into two parts:

- a) External problems
- b) Internal problems

External problems can be any of the following:

- 1) Poor written contract
- 2) Payment delay from the owner
- 3) Government regulations
- 4) Work termination

Internal problems are as follows:

- 1) Poor quality of venture work
- 2) Delay caused by the venture
- 3) Poor organization structure of venture
- 4) Financial problems of venture
- 5) Poor communication between parties
- 6) Inadequate estimation
- 7) Lack of adequate preplanning
- 8) Lack of attention and flexibility

- 9) Lack of policy agreement
- 10) Foreign venture headquarters are abroad
- 11) Too much paper work has to be sent to other party for approval
- 12) Lack of adequate study of partners before financing the joint venture
- 13) Reaching a decision takes a long time
- 14) Poor written contract
- 15) Payment delay from the owner
- 16) Government regulations
- 17) Work termination

4. The Survey

The questionnaire used for this research had two parts to it. Part “A” includes general information questions including the company’s name, the company’s nationality and respondent name and position. Also included is general information on the construction firms such as:

- 1) Role of the firm in construction
- 2) Number of employees in the joint venture
- 3) Type of construction
- 4) Grade of the firm

- 5) Reasons for entering joint venture
- 6) Joint venture type

Part “B” concerns the problems facing joint ventures in construction firms. This part includes seventeen different problems facing the joint venture, as follows:

- 1) Poor quality of venture work
- 2) Delay caused by the venture
- 3) Poor organization structure of venture
- 4) Financial problems of venture
- 5) Poor communication between parties
- 6) Inadequate estimation
- 7) Lack of adequate preplanning
- 8) Lack of attention and flexibility
- 9) Lack of policy agreement
- 10) Foreign venture headquarters are abroad
- 11) Too much paper work has to be sent to other party for approval
- 12) Lack of adequate study of partners before financing the joint venture
- 13) Reaching a decision takes a long time

The sample size determination for the number of Joint Venture firms to be questioned was calculated using a statistical formula. The scoring of the respondents' answers was done using the mean for questions in "part A" and an Importance Index formula for the answers in "part B" that relate to questions on problems facing the joint venture in the construction firms.

Data collected from the questionnaire was analyzed statistically using a computer program (SAS). The different methods used for calculating and presenting the survey results are as follows:

- a) Tabulation and Cross Tabulation
- b) Statistical Techniques (weighted mean, Std. Dev., Std. Error of Mean, Confidence Interval, Coefficient of Variation)
- c) Ranking (using the Importance Index)
- d) Correlation (The Spearman Rank, Partial Corr., Multiple Corr.)

5. Conclusion

Based on the results of this research, the following can be concluded:

I For Saudi - Saudi joint venture:

The following problems were ranked as important

1. Payment delay from the owner
2. Government regulations
3. Poor organization structure of venture
4. Financial problems of venture
5. Lack of policy agreement
6. Inadequate estimation

The following problems were ranked as somewhat important

1. Lack of adequate study of partners before forming the joint venture.
2. Poor communication between parties
3. Work termination
4. Reaching a decision takes a long time.
5. Poor written contract
6. Poor quality of venture work
7. Lack of adequate preplanning
8. Lack of attention and flexibility
9. Delay caused by the venture
10. Too much paper work has to be sent to the other party for approval.

The following problems were ranked as somewhat not important

1. Foreign venture headquarters are abroad

II For Saudi - Foreign joint venture:

The following problems were ranked as very important

1. Poor written contract
2. Lack of adequate study of partners before forming the joint venture,

The following problems were ranked as important

1. Government regulations
2. Payment delay from the owner
3. Lack of adequate preplanning
4. Financial problems of venture
5. Inadequate estimation
6. Lack of policy agreement
7. Work termination
8. Reaching a decision takes a long time.
9. Poor communication between parties

10. Lack of attention and flexibility

The following problems were ranked as somewhat important

1. Poor organization structure of venture
2. Poor quality of venture work
3. Delay caused by the venture
4. Too much paper work has to be sent to the other party for approval
5. Foreign venture headquarters are abroad

III For role in construction

The Following problems were ranked as important

1. Payment delay from the owner
2. Lack of adequate study of partners before forming the joint venture.
3. Poor written contract
4. Government regulations
5. Poor organization structure of venture
6. Financial problems of venture
7. Lack of policy agreement
8. Lack of adequate preplanning

The following problems were ranked as somewhat important

1. Inadequate estimation
2. Poor communication between parties
3. Work termination
4. Poor quality of venture work
5. Lack of attention and flexibility
6. Reaching a decision takes a long time.
7. Delay caused by the venture
8. Too much paper work has to be sent to the other party for approval
9. Foreign venture headquarters are abroad

IV for Type of construction

The following problems were ranked as somewhat important

1. Payment delay from the owner
2. Poor written contract
3. Government regulations
4. Lack of adequate study of partners before forming the joint venture.
5. Financial problems of venture
6. Inadequate estimation
7. Lack of policy agreement
8. Poor organization structure of venture
9. Lack of adequate preplanning
10. Work termination
11. Poor communication between parties
12. Reaching a decision takes a long time.
13. Lack of attention and flexibility
14. Poor quality of venture work

The following problems were ranked as somewhat not important

1. Delay caused by the venture
2. Too much paper work has to be sent to the other party for approval.
3. Foreign venture headquarters are abroad

V For grade

The following problems were ranked as important

1. Payment delay from the owner
2. Government regulations
3. Poor written contract
4. Lack of adequate study of partners before forming the joint venture.

5. Financial problems of venture
6. Lack of policy agreement
7. Inadequate estimation
8. Poor organization structure of venture

The following problems were ranked as somewhat important

1. Lack of adequate preplanning
2. Poor communication between parties
3. Reaching a decision takes a long time.
4. Work termination
5. Lack of attention and flexibility
6. Poor quality of venture work
7. Delay caused by the venture

The following problems were ranked as somewhat not important

1. Too much paper work has to be sent to the other party for approval.
2. Foreign venture headquarters are abroad

VI For reason for making joint venture

The following problems were ranked as important

1. Payment delay from the owner
2. Government regulations
3. Lack of adequate study of partners before forming the joint venture.
4. Poor written contract
5. Lack of policy agreement
6. Financial problems of venture
7. Inadequate estimation
8. Poor organization structure of venture
9. Reaching a decision takes a long time.
10. Lack of adequate preplanning

11. Lack of attention and flexibility
12. Work termination
13. Poor communication between parties

The following problems were ranked as somewhat important

1. Poor quality of venture work
2. Too much paper work has to be sent to the other party for approval
3. Delay caused by the venture

The following problems were ranked as somewhat not important

1. Foreign venture headquarters are abroad

VII For type of joint venture

The following problems were ranked as important

1. Poor written contract
2. Payment delay from the owner
3. Lack of adequate study of partners before forming the joint venture.
4. Government regulations
5. Financial problems of venture
6. Inadequate estimation
7. Poor organization structure of venture
8. Lack of policy agreement
9. Lack of adequate preplanning
10. Poor quality of venture work
11. Work termination

The following problems were ranked as somewhat important

1. Lack of attention and flexibility
2. Poor communication between parties
3. Delay caused by the venture

4. Reaching a decision takes a long time.
5. Too much paper work has to be sent to the other party for approval.
6. Foreign venture headquarters are abroad

VIII based on the hypothesis test the Saudi-Saudi joint venture and Saudi-Foreign joint venture do not agree on the ranking of importance of problems Facing joint venture Firms.

Based on the interview conducted for this research, the following can be concluded:

1. A high percentage of local Firms enter into joint venture on a project basis, so when the project is over, the joint venture gets over.
2. Market demand and the political situation greatly affect the joint venture firms.
3. It is difficult to find the right partner with similar objectives.
4. Joint venture by services involves taking payment for services.

6. Recommendations

To avoid the problems facing the joint venture, the following recommendations are worth considering:

1. A standardized form of the contract is strongly recommended. All points in the contract should be meaningful and reasonable. Expert people have to review the project contract and give their recommendations before the joint venture firms sign the contract.
2. Every party in the joint venture firm must study his partner in detail, his financial position, quality of work, organization structure, and where the Headquarters will be.

3. Drawings and specifications should be reviewed, engineers should make a detailed and comprehensive review of each drawing and specification.
4. The owner should recognize his liability and understand the financial implications of his goal.
5. It is recommended to mobilize the joint venture in the Kingdom of Saudi Arabia to save traveling and communication expenses.
6. Good relationship between parties in the joint venture is very helpful in executing the work smoothly.
7. Joint venture can be successful because they encourage teamwork and because they are free of taxes for an initial five year period.
8. Foreign exchange currency rate variations must be taken into consideration.
9. Local contractors mainly enter joint ventures for technology transfer to the project in the Kingdom, while the foreign contractor enters a joint venture to get into the Saudi market.
10. The management of joint venture must be from both partners, because when the foreign venture provides the management, he will take a fee for that plus his percentage in profit. So most losses to the joint venture will be faced by the Saudi partner.