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Challenges of joint ventures in the construction industry: Literature review

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Abstract

New opportunities are constantly emerging as a result of globalization which allows local firms to enter into international construction markets. As a result, joint venture (JV) construction projects are becoming common place which results in increased exposure of organizations to worldwide business markets. The formation of JVs between construction companies has become one of the recent efforts in combating contractors' problems as they are confronted with multiple challenges. Therefore, the current study sought to identify challenges or risks encountered by JVs in the construction industry. A literature search relative to challenges and risks of JV projects in the construction industry was conducted. Thematic analysis was conducted to establish the various categories of risks and barriers to JVs in the construction industry. Key findings reveal that challenges encountered in JVs formation are: inadequate staff training, the number of parties involved as well as collaboration of people from different cultures. Other challenges encountered by joint ventures that are less significant relate to the lack of clarity of the JV partner, unequal sharing of risks and benefits and an irregular pattern of operation as well as unstable relationships. The study highlights potential challenges involved in JVs. Consequently, by addressing these challenges, interested and concerned parties (contractors, consultants, owners) could improve the JV relationships before contracts are signed.

Keywords: challenges, construction industry, joint venture, projects

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1. Introduction

According to Fitzpatrick, Hecker and Hazard (2011:1), JVs have become increasingly common in the construction industry. Issues related to the formation and operation of JVs for construction projects have been the subject of considerable commentary. The Construction industry development board (CIDB, 2004:1) indicated that, the creation of joint venture will mainly depend on: the size of the project, where the project requires specialist skills or abilities, where the skills and expertise of emerging firms can be developed through their association in JVs with well-established experienced companies. Therefore, the use of JVs is a crucial weapon to alleviate projects issues particularly related to delays and disruptions, poor site management, time and cost variations, skills and competence issues.

Knowing that JVs are a useful vehicle for collaborative housing development and future private rented sector projects, it is regarded as a speculation for profit (Umunna, 2014:1) where the risks and rewards (benefits) are shared by two or more parties (Construction industry development board, 2004:1). Yet, Talman (2009:180), in his study undertaken in Swaziland, made an important observation, where, JVs make for a thought-provoking paradox as the popularity of joint ventures is as high as the %age failure of its operation. Similarly, Govindan, (1995:2) supported this previous argument by highlighting the fact that international construction firms have extensively used JVs as a vehicle to enter new construction markets, yet, the failure rate of such ventures has been quite alarming.

Indeed, risks are innate in JV construction projects and include the agreement of the contract, partner selection, potential financial distress, improper project feasibility study, project delay, inadequate forecast about market demand, loss due to bureaucracy for late approvals and design changes have been identified worldwide (Kwok et al., 2000:4; Shen et al., 2001:77). Thus, the main objective of this study is to identify the key issues that contribute to the successful delivery of JV construction projects. Observing these key issues or challenges will influence the increasing success of the JV construction projects performance. Hence, the researcher has decided to first highlight important aspects of JV and progressively identify the possible challenges faced by JVs.

2. Overview of joint venture

2.1 Definition of joint venture

A JV is the most common form of organizational structure where the partners wish to establish and operate a jointly owned business (Kale et al., 2013: 60). Thus, a JV, unlike a partnership, will have a distinct legal entity and also have a certain time limit. Kolbehdari and Sobhiyah (2014:373) further highlight that JV is a specific type of long-term alliance among the partners which creates an exceptional opportunity for combining distinct merits and complementary resources. Thus, it can be said that JV is a prospect to share the risks and costs in order to advance knowledge, to enter new markets, and economic saving. Moreover, JV provides strength in terms of achieving goals of construction companies, whilst offering a unique opportunity to combine the distinct competencies and the complementary skills of participating firms (Kale et al., 2013: 60).

In the same way, JV is commonly named partnering as it is a relationship between two or more companies or organizations which is formed with the express intention of improving performance in the delivery of projects (Azlan-Shah et al., 2010:328). Similarly, Matschulla and Rittmann (2012:6) emphasize that a JV takes place when two or more parties come together to take on a combined task

which can be a project or a series of works for a specific operation only or it can become a continuing business relationship. A JV is therefore, the commercial agreement between two or more companies in order to allow superior work quality and cooperation towards achieving a common aim, through the management of the appropriate resources.

2.2 Types of joint ventures in construction projects

Indeed, the selection of an appropriate legal form of JV needs to take into account the goals of the JV operation, as it would limit problems and thus reduce the exposures faced in such corporation. It is important to discover that there are numerous types of JVs encountered during the course of construction projects which include three common legal forms of JV, i.e. contractual or consortium joint venture, partnership joint venture and corporate joint venture which is the incorporation of joint venture as a limited company (Kwok, 2006:3). However, according to Zhang (2011:21), there are three types of consortiums: non-equity joint venture (non-integrated joint venture/ Project-based), equity joint venture (integrated joint venture/ Traditional type) and combination joint venture (Contractual type).

2.2.1 Non-integrated joint venture

This type of JV, on the contrary to the integrated joint venture, has as primary characteristic, not to be a partnership in that there is no sharing of profit and losses and each member is taken for a specific scope of work and is responsible for the profit and losses associated with that specific scope of work (Kale et al., 2013: 62). Furthermore, Hong and Chan (2014:5) and Zhang (2011:21) highlight that, the non-integrated JVs are usually used when parties to a JV each have isolated scopes of work and the JV is being formed simply to satisfy a particular requirement demanding a joint bid, where responsibility for the contract habitually has to be assigned to a JV board. The work and obligations making up the contract are broken down into discrete elements usually on the basis of locality, the nature of the work, or the capabilities and resources required where each element is assigned to a specific member of the JV who assumes full responsibility for its execution, under the direction of the JV (Construction industry development board, 2004: 63).

2.2.2 Integrated joint venture

Integrated JV according to Kale et al., (2013: 63) has as primary characteristic to represent a true partnership, in that the parties share profit and losses and the interest may be 50:50 and there may be two or more members. However, the integrated JVs may otherwise refer to jointly managed JVs (JMJs) where the parties fundamentally agree to perform their work as if it was performed by a distinct corporation having numerous stakeholders (Hong & Chan, 2014:5). In other words, the integrated JV is adopted when the parties to the proposed joint venture expect to perform their work on an incorporated basis. This type of JV is used in projects which are of an immense size and the task of splitting the work is very difficult (Kale et al., 2013: 64). As a result planning and programming can become complicated and requires highly structured and authoritative central management (Kale et al., 2013: 64).

2.2.3 Combination joint ventures

In addition to the types of JVs encountered in construction projects, there is the combination joint venture type which is used in larger and complex projects. It is a combination of an integrated and non-integrated joint venture (Kale et al., 2013: 64). According to Kale et al. (2013: 65), each member takes

on specified scope of work and is responsible for the profit or losses associated with that scope of work. But the member also agrees to act as a partner with respect to a portion of the necessary work, which may include sharing the preliminaries and general conditions necessary for each member's separate scope of work, as well as the actual performance of the portion of the work of the project (Kale et al., 2013: 65).

2.3 Reasons for forming joint ventures in construction projects

Zhang (2011:20) states that, a JV is constantly used as an essential means to conjoin contractors in construction industry. However, the motivations of entering into JVs in construction industry depend on the area of operation. For instance, in Japan, construction JVs are used to develop the chance of acquiring projects by small and medium-size companies. Moreover, in China, construction JVs are means for foreign companies to evade government policy. Just as in manufacturing industry, JVs are also used to expand market, to share risks, to reduce cost or access cheaper materials and resources as well as to transfer technology in construction industry (Zhang, 2011:20). Moreover, the motives of JVs formations are further summarized by Zhang (2011:21) in Table 2.1 as follows:

Table 2.1 Reasons for the formation of joint ventures (Zhang, 2011:21)

1	To partake in overseas project or to undertake the major project
2	To develop market
3	To spread financial risk
4	To reduce cost by accessing the cheaper manpower, materials and resources
5	To transport outside expertise/technology
6	To acquire management skills
7	To evade government policy about foreign investment constraints

3. Challenges or Risks of Joint Ventures

In general, JVs help firms in accessing new markets, knowledge, capabilities, as well as other resources. Yet, these operations could be challenging to achieve as they are owned by two or more parent companies (Beamish & Lupton, 2009:75). These companies may have opposing or dissimilar objectives, variances in management style as previously discussed in the previous sections of this paper. However, those challenges can be clustered under the following points when it comes to the challenges of JVs:

3.1 Ambiguity in each partner's responsibility

Lack of clarity of partner implies defining the extent of authority of each of the key individuals in the JV project (Kolbehdari & Sobhiyah, 2014:13). Some ventures require the active participation of both parents to be successful, while others do not (Kale et al., 2013:65). In the case of a 50-50 JV, which is the case of an integrated joint venture, matters are more complicated when the minority partner wishes to participate actively in the decision-making (Kale et al., 2013:65). To be more precise, the parents of a proposed partnership must articulate their assumptions and involve key people during the negotiations to define the contributions the partners will make and the benefits they expect (Kale et al., 2013:65).

3.2 Unequal sharing of risks and benefits

Indeed, it is very important to resolve issues dealing with the values generated by the venture before finalizing the project (Kale et al., 2013:64). Therefore, ensuring an equitable risk-benefit ratio is fundamental to the longer-term health of the alliance (Kale et al., 2013:64). As in a JV, the partners should cooperate to achieve the JV desired objectives and hence complete the desired value creation (referred here as: growing the pie) (Talman, 2009:188).

On the other hand, Talman (2009:188) emphasized that partners will almost obviously compete to share the anticipated benefits (referred here as 'getting the largest slice of the pie'). And thus, the competitive perspective would mean that, all partners would perform in order to learn from the other partner which would therefore have a damaging impact on the JV performance.

3.3 Irregular pattern of operation and unstable relationships

Kale et al. (2013:64) puts forward the idea that a JV will get off to a successful start as long as it settles into a normal pattern of operation and stable relationships. As a result, effective day to day routines need to be established and problems arising from the activities will be predictable (Kale et al., 2013:64). Conversely, it is further articulated by Talman (2009:188) that, the management of JVs is about creating good relationships between partners as well as enhancing trust; yet, the most difficult events in JVs are those that have the potential to put the parties against each other (Kale et al., 2013:64).

However, there should be exit mechanisms so that when conflicts escalate beyond a certain threshold and the parties no longer feel they can work with each other, this exit mechanism will be in place, thus avoiding costly and time-consuming litigation. Therefore, to avoid having to exit a venture that has by one measure or another failure, the partners need to step around the minefields.

3.4 Inadequate staff training & misunderstanding of partnering concept

In fact, inadequate staff training is the essential reason for JV failure, where the participants do not fully understand the concept of a JV and consequently are not able to implement partnering successfully (Kale et al., 2013:64). This problem causes further issues to the formation of joint venture construction projects according to Kale et al. (2013:64) which is the misunderstanding of the partnering concept as participants failed to understand how the partnering relationship could provide a competitive advantage. According to Minja et al. (2012: 34), limited experience in the partnering approach affects the understanding and knowledge of project participants.

3.5 Collaboration of people from different cultures & the number of parties involved

Indeed, the collaboration of people from different cultures with different attitudes may cause improper communication, which will result in conflict and may cause the collapse of the JV (Kale et al., 2013:65). Kolbehdari and Sobhiyah (2014:13) as well as Beamish and Lupton (2009: 85-86) emphasized that, it is important for the partners to be aware of cultural differences as it can affect the successful performance of the JV. In other words, the prospective conflicts in any JVs exists due to the differences of partners involved, which may be further amplified as a consequence of the different cultural backgrounds of partners (Hong & Chan, 2014:12). Moreover, with the issue of difference in cultures,

compatible objectives are difficult to inaugurate between partners who come from different cultures (Govindan, 1995:51).

It follows then that, the number of parties may be another challenge to the success of the JV construction project since the decision-making is normally slowed down (Kale et al., 2013:65). Moreover, Julian (2008:4-5) argued that the number of partners involve in JV operations may result in conflicting desires of parent firms for cooperation and their autonomy. As a consequence, there is considerable evidence to suggest that there is a significant inverse relationship that exists between the level of conflict and the performance of joint ventures.

Similarly, García-Canal et al. (2003:743) highlighted that the number of partners participating in a JV represents a dimension of complexity that may disturb its effectiveness, which is, the extent to which a main partner's goals for the alliance are fulfilled. In other words, García-Canal et al. (2003:743-744) expresses that the number of partners conditions the proper management of joint ventures as it could result in conflicting interests, operational asymmetries, poor coordination of the activities that would make it problematic for the firm to accomplish their full potential in the joint venture.

4. Methods

In the present paper, the theory regarding JVs and their general challenges are assessed and identified. Journals, theses, books and government reports which included authors such as Kwok et al. (2000), Kale et al. (2013) as well as Shen et al. (2001) were reviewed. The researcher then conducted a systematic thematic analysis. A thematic analysis is a systematic approach to the analysis of qualitative data that involves identifying themes or patterns of cultural meaning, coding and classifying data, typically textual, according to themes; and interpreting the resulting thematic structures by looking for commonalities, relationships, overarching patterns, theoretical constructs, or explanatory principles (Boyatzis, 2008:1; SAGE Research Methods, 2013:2). Thus, the researcher reviewed the data, took notes of challenges of JVs in construction projects and sorted them into specific categories or points with the objective to identifying the key issues that are encountered by JV partners when entering JV agreement.

5. Findings

Joint venture operations may encounter challenges during the course of execution of JV projects. Indeed, these challenges have repercussions on the JV operation and therefore they should be strategic in order to avoid collapsing of the JV agreement. Results from the existing journals, theses, books and government reports revealed that the highly perceived challenges in joint venture operations include: unequal sharing of risks and benefits; irregular patterns of operation and unstable relationships; as well as misunderstanding of partnering JV concept. However, the lack of clarity of your JV partner seemed to be considerable and finally, inadequate staff training; the number of parties involved; as well as collaboration of people from different cultures are considered not to make significant impact when it comes to the formation of JVs.

6. Conclusion

The objective of this study was to identify the possible challenges underlying the JV process. The literature review produced a list of those challenges. Indeed, the most important risks or challenges

influencing the formation of JVs were found to be unequal sharing of risks and benefits; followed by irregular patterns of operation and unstable relationships; as well as misunderstanding of partnering JV concept. Even though, the main purpose of JV operations remains the spreading of risk inherent in large projects and to pool resources in a way that permits the execution of projects, it becomes crucial for the partners to be aware of the possible risks or challenges and thus set procedures to resolve such problems as they could occur in the course of the execution of the contract.

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