

AN EXPLORATORY STUDY OF PROBLEMS FACING EMERGING CONTRACTORS IN THE NORTH WEST PROVINCE OF SOUTH AFRICA

Wellington Didibhuku Thwala¹ and Makgati Jacob Phaladi²

University of Johannesburg
Department of Construction Management and Quantity
Surveying
Johannesburg, South Africa

ABSTRACT

Purpose of this paper

The main purpose of this study was to examine the problems that are facing emerging contractors in South Africa focusing on the North West Province. Different studies have highlighted that there are different critical factors that influence the success or failure of contractors. They range from experience in the construction sector, technical and management skills, mentoring and access to finance. Since 1995 various contractor development programmes have been initiated in South Africa with little success.

Design/Methodology/Approach

A comprehensive literature study was conducted and it was supplemented by primary data gathering. A questionnaire was sent to over 100 contractors in the North West Province and 57 questionnaires were returned. The response rate was good as it was more than 50%.

Findings

¹ Department of Construction Management and Quantity Surveying

² Department of Construction Management and Quantity Surveying

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The main findings of the study was that the major problems contractors were found to be Government not paying on time, lack of capital and difficulty in arranging guarantees. Emerging contractors are failing due to lack of adequate capacity to handle the uniqueness, complexity and risks in contracting, lack of effective management during their early stages, lack of basic business management, poor record keeping and inadequate technical, financial and contract managerial skills.

Originality/Value of this paper

The importance of emerging contractors in South Africa has been recognised by many researchers. The contribution of these enterprises to the creation of jobs and to the alleviation of poverty has been recognized by many Developing World governments including the South African Governments. They have been given prominence in many development plans as well as in the strategies of many donors. The aim of the study was to examine the problems facing contractors in South Africa focusing on the North West Province. These will ensure that the programmes are relevant and effective.

Keywords: Emerging Contractors, Small and Medium Size, Emerging Contractor Development Programme, Enterprises.

1. INTRODUCTION

Micro and small enterprises are a major feature of the economic landscape in all developing countries today (Liedholm and Mead, 1999). The South African government has committed to ensuring that black-owned companies have access to the construction sector. Under its black economic empowerment (BEE) programme, the South African government has set targets for the percentage of each industry to be controlled by black-owned businesses. Large, predominately white-owned corporations have sold assets to achieve this objective, with the first sale occurring in late 2000. From 1995 the democratic government through its various departments has initiated some contractors' development programmes by which it awards certain levels of its construction projects to the historically disadvantaged black contractors in order to enable development of competent skills, build viable construction companies, create jobs and redistribute wealth (Department of Public Works (DPW), 1996).

A construction company's decision to expand into international markets must be based on a good understanding of the opportunities and threats associated with international business, as well as the development of company strengths relative to international activities (Luger, 1997). The study was done by surveying the executives in charge of international construction of large United States based contractors. The findings indicate that track record, specialist expertise and project management capability

are the most important company strengths; loss of key personnel, shortage of financial resources, and inflation and currency fluctuations are the most important threats relative to international markets; and increased long term profitability, the ability to maintain shareholders' returns, and the globalisation and openness of the markets are the most important opportunities available in international works (Luger, 1997). The vast majority of construction firms are small enterprises that rely on outsourcing personnel as required. According to the World Bank Survey (2001:44) of Small and Medium Size Enterprises (SMMEs) indicated that increased contracts from government and large companies were needed for them to expand their employment. This has severely affected skills training and the retention of expertise in the industry as construction workers become highly mobile, walking in and out of the industry, depending on performance in other sectors of the economy. The impact can be seen in the rigid adherence to management techniques and construction practices handed down from colonial times which have resulted in inadequate skills and capacity. Delays with interim and final payments, as well as onerous contract conditions faced by construction firms, can also impose huge constraints on the industry. Many construction firms have suffered financial ruin and bankruptcy because of delays in payment, which are common with government contracts (Croswell and McCutcheon, 2001).

2. RESEARCH OBJECTIVES

The main objective of this study was to establish the problems facing emerging contractors in the North West Province that leads to high failure rate. Another objective of the study was to find out on the gender and race composition of emerging contractors in the North West province. The majority of emerging contractors are owned and operated by men (Liedholm and Mead, 1999). It is imperative to find out how far is the transformation of the industry since 1994.

3. RESEARCH METHODOLOGY

One hundred (100) small and medium sized contractors were randomly selected from the database of the National Department of Public Works (NDPW), Mmabatho Regional Office: Emerging Contractors Development Programme; Local Municipalities: Contractors Development Programmes (CIP), and Construction Industry Development Board (CIDB) contractors register/database. The probability sampling method using simple random sampling was found to be the most appropriate for the study. The selection criteria adopted to form the target population included the following:

- Contractors from Grade 1 and 4 of the Construction Industry Development Board (CIDB) grading; and

- Emerging contractors located in North West province.

A total number of 100 questionnaires were distributed among small and medium sized contractors and 57 questionnaires were returned. The response rate was good as it was more than 50%. The research methodology for the study provided both primary and secondary data. The primary data collected formed the investigation using a structured questionnaire. The primary data was collected between June 2008 and September 2008. The scope of the study was delimited to small and medium size contractors operating in the North West province of South Africa. The Microsoft Word and Excel programmes were used to present the graphics. The statistical programme used for analyses and presentation of data in this paper is the Statistical Package for the Social Sciences (SPSS). This section consists of descriptive statistics which uses frequency tables and display charts to provide information on key demographic variables in the study.

4. LITERATURE REVIEW

Thwala and Mvubu, 2008, Dlungwana and Rwelamila, 2003; Crosswell and McCutcheon, 2001; have stated that contractors can be distinguished from each other by variables such as the size of annual turnover, capacity and capability. The challenges facing small and medium-sized contractors can be distinguished between those that affect small-scale contractors and those that affect medium-sized contractors. Some key features of small-scale contractors are that they are largely unregistered, operate in the informal sector of the economy and have very little formal business systems. The small-scale sector comprises the largest percentage of total contractors, although they employ very few permanent staff, usually less than ten employees. The conditions in developing countries present additional challenges, which include, amongst others, the lack of resources for training contractors, such as funds, poor construction procurement systems and lack of management capacity and resources to equip managers to operate their business enterprises effectively and efficiently.

5. CHALLENGES FACED BY EMERGING CONTRACTORS IN SOUTH AFRICA

The challenges faced by small and medium contractors can be distinguished between those that affect small-scale contractors and those that affect medium-sized contractors. Small and medium contractors are facing increased competition due to the long-term real decline in demand, and many contractors have responded by shedding labour. The larger

contractors have responded by moving into the international market. Small local contractors, in particular, are furthermore subject to volatilities due to the geographic distribution of construction and the peak workloads that characterise construction projects, which has further reduced their ability to build capacity. Emerging contractors are subject to the same market forces described above for small contractors. However, while emerging contractor development policies were intended for black economic empowerment, small government contracts have in fact been used as job creation opportunities.

Lack of effective management during their early stages is a major cause of business failure for small and medium sized contractors. Owners tend to manage their businesses themselves as a measure of reducing operational costs. Poor record keeping is also a cause for start up business failure. In most cases, this is not only due to the low priority attached by new and fresh entrepreneurs, but also a lack of basic business management skills. Most business people, therefore, end up losing track of their daily transactions and cannot account for their expenses and profits at the end of the month. During the early stages of some business start ups, owners were unable to separate their business and family/domestic situations. Business funds were put to personal use and thus used in settling domestic issues. This has a negative impact on profitability and sustainability. Some owners/managers employ family members simply because of kinship relations. In some cases, these have turned out to be undisciplined and ineffectual, a factor that has led to eventual and sometimes rapid failure of businesses (Rwelamila, 2002; Miles, 1980; Crowell & McCutchen, 2001; Mphahlele, 2001; Ofori, 1991); International Labour Organization –ILO- (1987); Wijewardena, H. & Tibbis, G.E. (1999). The relative lack of success facing emerging contractors in South Africa was a result of: inadequate finance and inability to get credit from suppliers; inability to employ competent workers; poor pricing, tendering, and contract documentation skills; poor mentoring; fronting for established contractors; lack of entrepreneurial skills; lack of proper training; lack of resources for either large or complex construction work; lack of technical, financial, contractual, and managerial skills; and late payment for the work done.

Since 1995, the Department of Public Works (DPW) has been actively involved in conceptualising and implementing programmes to promote emerging contractors in the built environment. Through these programmes, the DPW has increased participation of previously disadvantaged individuals in the mainstream economy. Moreover, it increased economic activity in an economically depressed environment. Previous contractor development programmes have focused on the under R500 000 range, which has been found not to be a sustainable market given the number of new entrants to the market. This resulted in few of the contractors being sustainable and the cost of contractor development consequently being extremely high compared to the sustainable result.

The challenges faced by the emerging contractors include: the coordination and management of the many facets of the different programmes; maintaining focus on sustainability against pressures to roll-out too rapidly; reaching target market with information about the opportunity; sourcing mentors with the requisite skills and experience; the large numbers of contractors targeted requires large numbers of trainers and mentors which are not readily available, and are costly; the available resources to effectively and efficiently monitor, evaluate and facilitate programmes are limited; an integrated development approach requires considerable support from senior management of public sector clients and considerable inputs from officials; programmes lack sustainability; while public sector clients have done a lot for contractor development, particularly in the area of policy, there are still many issues that must be addressed at operational level, such as late payment cycles; procurement policies should encourage longer contract periods and move away from frequent tendering which is both expensive and disruptive; more qualifications need to be developed that are targeted at the specific needs of small and emerging contractors; there is a lack of access to affordable finance; emerging contractors lack demonstrable credit and track records. The following are the major constraints faced by emerging contractors' development and growth.

6. FINANCIAL BARRIERS TO SMALL AND MEDIUM CONTRACTORS' DEVELOPMENT AND GROWTH

Efforts to promote SMME access to finance might have more impact on development and growth but access is limited and the cost of capital is high. While government has made some efforts to increase accessibility to finances, the targeted programmes have had limited success because awareness and usage of existing promotional programmes is very low. In addition to insufficient access, high interest rates also pose a constraint to micro enterprise growth. Moreover, Gounden (2000) reports that there are core difficulties seen in terms of discrimination by financial institutions against micro enterprises with little collateral, difficulties in accessing information and lack of market exposure. The inadequacy of external finance at the critical growth/transformation stages of micro enterprises deters the enterprises with growth potential from expanding (Nissanke, 2001).

7. LEGAL BARRIERS TO SMALL AND MEDIUM SIZED CONTRACTORS' DEVELOPMENT AND GROWTH

With regard to legal barriers, a commonly perceived constraint of micro enterprises is the labour laws which are said to raise the cost of employment artificially prolong retrenchments or corrective action and do not allow for adequate flexibility especially in wage settings and the arrangement of working time (Bhorat, H; Lundall, P & Rospabe, S., 2002). As a result, enterprises feel a profit squeeze and impact on the willingness to create jobs.

8. FINDINGS FROM THE NORTH WEST STUDY

The pie chart below shows that the small and medium size industry in South Africa is still male dominated with 78% male and 22% female owned. The age of the people interviewed ranges from 20 to 59 years old. 98.3% of the people interviewed were Black and 1.7% percent were Coloured people. The figure clearly shows that emerging contractors in the North West Province are dominated by Black people. 71.2 % of the people interviewed were managing directors; 6.8% were managing partners; 8.5% were Construction Project Managers and 10.2% were Construction Managers.

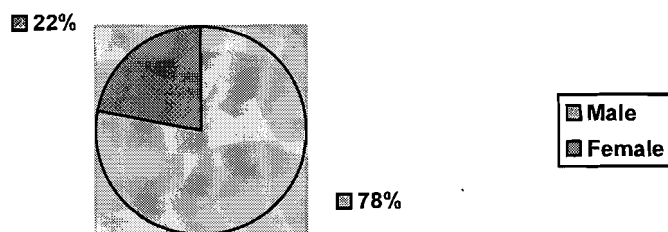


Figure 1: Gender in the North West Province

Table 1: A survey of Contractors' Qualifications, North West Province, 2008		
Qualification	Frequency	%
Grade 11 or lower	10	18
Grade 12	17	30
Post Matric Diploma/ Certificate	17	30

Bachelor's Degree	6	10
Post-graduate Degree	7	12
Total	57	100

The results also show that 18% of the owners of the contractors had a Grade 11 or lower qualification; 30% had Grade 12 qualification; 30% had a post-Matric Diploma or Certificate; 10% had a Bachelor's degree and 12% had a post graduate degree. The results also show that 45.7% of the owners had a qualification that is up to Grade 12.

Table 2: Contractors' track record in North West province as at 2008

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No. of Projects Managed	Frequency	%
0 - 2 projects	43	75
3 - 19 projects	11	19
11 - 15 projects	2	4
Above 20 projects	1	2
Total	57	100

The results show that 75% of the contractors manage between 0-2 projects; 19% of the contractors manage between 3-19 projects; 4% of the contractors manage between 11-15 projects and 2% of the contractors manage above 20 projects at a time. Most of the contractors at the lower grading lack the capacity to manage many projects at one time.

Table 3: Basic construction skills lacked by contractors, North West province, 2008

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Type of Construction Skills	Frequency	%
Construction Management	9	15
Business Management	11	20
Project Management	11	20

Health and Safety	6	10
Tendering	11	20
Site Management	9	15
Total	57	100

The results show that contractors lack basic construction skills with only 15% construction management; 20% business management; 20% project management; 10% health safety; 20% tendering and 15% site management. It is also clear that the majority of the contractors in the North West Province lack important skills that will enable their contractors to be successful. The results show that scarce skills in the construction industry is a main challenge, as most of the small and medium sized contractors cannot afford to hire qualified artisans and construction professionals due to the high demand of built environment professionals. And it leaves small and medium sized contractors with no option but to outsource their work to the well-established contractors.

Table 4: Contractors' years of experience, North West province, 2008

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Years of Experience	Frequency	%
less than 3 years	21	37
3 - 5 years	19	33.9
11 - 15 years	11	18.6
Over 15 years	6	10.5
Total	57	100

The research also found that 37% of the owners of the contractors have less than three years experience; 33.9% of the owners have between 3 and 5 years experience; 18.6 % of the owners have between 11 and 15 years and 10.5% have above 15 years experience in the construction sector.

9. CONCLUSION AND RECOMMENDATIONS

This paper has shown that after 15 years into the new democratic South Africa, the state of emerging contractors continues to be unsustainable,

even with existence of supportive programmes (i.e. contractor development programme and emerging contractor development programme). The South African construction industry will continue to provide jobs for Historically Disadvantaged Individuals (HDI) but without such an intervention, small and medium sized contractors will remain unsustainable and their performance unsatisfactory. The study finds that lack of effective management during their early stages is a major cause of business failure for small and medium sized contractors. Owners tend to manage their businesses themselves as a measure of reducing operational costs. Poor record keeping is also a cause for startup business failure. Lack of financial management; lack of entrepreneurial skills; lack of proper training; lack of resources; lack of technical skills, lack of contractual and managerial skills; late payment for work done which are common with government contracts; inability to get credit from suppliers and fronting for established contractors are also contributing factors for the failure of emerging contractors in the North West Province.

In order to address problems and challenges faced by emerging contractors in South Africa, it is critical for the government to review policies with regard to Contractor Development Programmes (CDP) to ensure that the government contributes to the success of small contractors in South Africa. The research had established that there is not one critical success factor that can make small and medium sized contractors to be successful but a combination of factors. In the North West Province case study it was found that some factors were critical and some were less critical. The authors recommend that the following factors to be considered as key to the success of emerging contractors in the North West Province:

- **Business skills:** Location of business premises is very important. Set specific targets for your business, carry out market research, employ qualified personnel and put them in position according to their skills. Know and understand existing skills needed and attend refresher courses on business management skills.
- **Management skills:** Financial management should be emphasized as well as networking with other people with similar businesses and keeping records of workers to help in evaluation of the performance.
- **Access to capital:** Merge with others that have similar businesses, negotiate favourable credit purchases from the supplier, source affordable loans from financial institutions and negotiate advance payments from the clients.
- **Good record keeping:** Financial records should be prioritised and a record of books of accounts on a daily, weekly, monthly and annual basis should be established.
- **Well managed Cash flow:** Prepare cash flow forecasts and budgets and prepare a cost-benefit analysis. Lease equipment and other financial assets to improve your cash flow, negotiate

outstanding loans through payment procedures and scale down operational costs.

- **Family/domestic situation:** Separate business activities and family obligations and look for alternatives sources of income to cater for the family's basic needs.

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