

**PROBLEMS AND DILEMMAS OF CLASS F CONTRACTORS'
PARTICIPATION IN LARGE PROJECTS**

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requirements for the award of the degree of
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MAY 2011

I declare that this project entitled “Problems and Dilemmas of Class F Contractors’ Participation in Large Projects” is the result of my own research except as cited in the references. The project has not been accepted for any degree and is not concurrently submitted in candidature of any other degree.

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Date : 20TH MAY 2011

To my beloved and respectful parents,
Allahyarhamah Hajah Zahrah Bt. Abdul Ghani (PBUH: Jan29, 2006) and
Allahyarham Haji Mohd Hanif Bin Ismail (PBUH: April6, 2011).
May Allah bless upon both of you in Jannah. Amen.
Al-Fatihah.

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ABSTRACT

The Federal Government of Malaysia has imposed several crucial moves, like the New Economic Policy (NEP), New Economic Model (NEM) and the policy of allocation of 10% of cost of contract of large projects to Class F contractors. The target is to address the issue of Bumiputra contractors in Malaysia. In order to steer the action towards the aim and the objectives, the Government, through several bodies will work together in monitoring and control of the construction industry in Malaysia. The aim of the study is to analyze the current problems or dilemmas of Class F contractors in participating in large projects. The objectives are to investigate the previous efforts done by the Government of Malaysia about the Class F contractors, to study the success and effectiveness of the policy of 10% job allocation to Class F contractors and to analyze the problems and dilemmas of Class F contractors in participating in large projects. The study involves the process of literature review and surveys administered by questionnaires. The study shows that the lack of expertise and experiences among the Class F contractors in handling bigger and tougher job of works has been the biggest problem and dilemma for the group. Lack of supplier networking and the financial limitations are other biggest hurdles. As conclusions, the Class A and Class F contractors must work together to benefit each other, in terms of expertise, experiences, cost, profit, networks, and even for the long term of good track records among the Government's project. The Class A contractors must play their role and responsibility significantly to help the Class F contractors to grow. The Class F contractors also must play their roles actively by seriously involved in projects given. Meanwhile, the Government must be able to continue in their efforts to assist and protect the rights of the majority of Bumiputra contractors in Malaysia, especially the Class F contractors.

ABSTRAK

Kerajaan Malaysia telah melaksanakan beberapa pelan tindakan seperti Dasar Ekonomi Baru (DEB), Model Baru Ekonomi (MBE) dan polisi pengagihan 10% dari kos kontrak bagi projek berskala besar kepada Kelas F. Matlamatnya ialah untuk menyelesaikan isu kontraktor Bumiputra di Malaysia. Demi mencapai tujuan dan objektif, Kerajaan dengan bantuan badan-badannya akan bekerjasama untuk memantau dan mengawal industri pembinaan di Malaysia. Tujuan kajian ini ialah untuk menganalisa keadaan terkini bagi masalah dan dilemma kontraktor Kelas F di dalam penglibatan di projek besar. Objektif-objektif kajian adalah untuk menyiasat usaha-usaha Kerajaan yang lepas berhubung Kontaktor Kelas F, untuk mengkaji kejayaan dan keberkesanan polisi 10% kerja diagihkan kepada kontraktor Kelas F, dan akhir sekali ialah untuk menganalisa masalah dan dilemma kontraktor Kelas F di dalam penglibatan di projek besar. Kajian ini melibatkan proses ulangkaji hasil-hasil kajian terdahulu dan kajiselidik menggunakan teknik soal-jawab soalan. Kajian ini menunjukkan bahawa kekurangan kepakaran dan pengalaman di kalangan kontraktor Kelas F dalam melaksanakan projek yang lebih besar dan mencabar, adalah merupakan masalah dan dilemma yang terbesar bagi kumpulan ini. Kekurangan jaringan pembekal dan kewangan yang terhad adalah antara halangan lain yang terbesar. Kesimpulannya, kontraktor Kelas A dan Kelas F mesti bekerjasama untuk kebaikan semua, samada dari segi kepakaran, pengalaman, kos, keuntungan, jaringan, dan juga demi rekod baik untuk jangka masa panjang di dalam projek Kerajaan. Kontraktor Kelas A mesti memainkan peranan dan tanggungjawab mereka secara penting untuk menolong kontraktor Kelas F agar berkembang maju. Kontraktor Kelas F pula mesti sanggup memainkan peranan mereka secara aktif melalui penglibatan secara serius di dalam projek yang telah dianugerahkan. Sementara itu, Kerajaan pula mesti sanggup meneruskan usaha murni untuk membantu dan mempertahankan hak majoriti kontraktor Bumiputra di Malaysia, terutamanya kontraktor Kelas F.

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CHAPTER 1

INTRODUCTION

1.1 Introduction

Malaysia's trend of major sectors like housing, industrial, commercial and infrastructures have been monopolized by the non-Bumiputra contractors, especially in the private area. The move by the Government of Malaysia through New Economic Policy or called NEP (Tun Abdul Razak, 1971) has saved millions of Bumiputra from poverty and inequality of national's wealth. According to NEP or New Economy Plan, it stated that the requisition of 30% of Bumiputra's participation in all sectors in which the real objective is to increased the Bumiputra's participation in all sectors in Malaysia. Needless to say, the involvement of Bumiputra towards a high level of technical and knowledge of contracts works is our Government's top priorities throughout the years, since the implementation of NEP by our former Prime Minister, late Tun Abdul Razak.

Today, Malaysia's construction industry becoming increasingly more complex partly because the complexity of the construction process itself, and the large number of parties involved including clients, users, designers, regulators, contractors, suppliers and others. The industry's fortunes tend to fluctuate with the general economy, and it has a cyclical nature and quick response to the changes in the economy (Olomolaiye et al., 1998). The industry, in the developed countries, is supported by the social and political infrastructure that are manifest, *inter alia*, in the legal systems, forms of contract, *de jure* responsibilities of specific aspects of the process and the formal accreditation of professional competence. Such supportive infrastructure systems do not exist in the developing countries which tend to rely on infrastructure and procedures that are borrowed from, or imposed by, the developed

countries (Drewer, 2001).

A number of scholars have addressed the industry's problems in the developing countries setting and discussed ways to alleviate such problems (Hillebrandt, 1997; Ofori, 1993, 1994; Wells, 1986; Turin, 1973). However, lack of progress was noted in solving such problems due to a number of reasons. These reasons include in-appropriateness of some of the recommendations, the initiatives adopted, poor executive capacity of the implementing agencies, lack of resources for implementation and initiatives, neglect of the construction industry by governments and their lack of commitment to solve its problems (Ofori, 1994). Ofori also added that another important possible reason for the lack of progress in construction industry development is the absence of measurable targets in programmes for improving the industry's overall performance.

Ogunlana et al. (1996) stated that the industry's problems in developing economies can be categorized into three areas: (1) problems of shortages or inadequacies in industry infrastructure, (2) problems caused by clients and consultants, and (3) problems caused by contractor's incompetence/inadequacies. Ogunlana and Olomolaiye (1989) indicated that the major problems faced by contractors in developing countries have been classified as problems imposed by the industry's infrastructure, problems of inaccurate information and frequent changes in instructions, failure to meet obligations on the part of clients and consultants, and problems imposed by their own shortcomings.

Therefore, the Federal Government of Malaysia has imposed several crucial moves, like the New Economic Policy (NEP), New Economic Model (NEM) and the policy of allocation of 10% of cost of contract of large projects to Class F, are to address the issue of Bumiputra contractors in Malaysia.

In order to steer the action towards the aim and the objective, the Government, through several bodies will work together in monitoring and control of the construction industry in Malaysia. The establishment of Ministry of Works or KKR, Unit Pendaftaran Kontraktor (UPK), Pusat Khidmat Kontraktor (PKK),

Bahagian Pembangunan Bumiputra (BPB), and Construction Industrial Development Board (CIDB) are to help promote check and balanced on the Malaysia's construction industrial environment.

1.2 Problem Statement

In Malaysia, Class F is considered as the lowest of the eight classes of contractors according to Unit Pendaftaran Kontraktor or UPK, 1997. However, it is the largest group of Bumiputra contractor in Malaysia, and perhaps in the world, as reported by News Straits Times in May 1, 2005.

In order to address the issues on Bumiputra contractors, the Government of Malaysia have implemented numerous moves, plan and policies to improve the economy and the level of competencies of this special group. Malaysia's 2nd Prime Minister, Tun Abdul Razak have introduces the New Economic Policy, NEP in 1971 to address the issue on Bumiputra. This is the very beginning of the Malaysia's social contract of 30% equity allocation on national's wealth for Bumiputra.

The Government through its body of Public Works Department, PWD have come up with several policies on Bumiputra issues. One of them is the policy of the allocation of 10% of cost of contract to Class F contractors. The policy has been first introduced in March 26, 2008. Nevertheless, the policy has been ordered for temporary stop on May 7, 2009 due to several mechanism issues. The latest guidelines on the policy have been issued on April 5, 2010. The circular on the guidelines called "Surat Arahan KPKR, dated April 5, 2010", dictates the latest mechanism on the policy of allocation of 10% of cost of contract of large project, which is over RM10 million, to Class F. However, as for the allocation of 10% of cost of contract, the guideline is still give limit to the maximum scope of work of RM200,000 for each of Class F contractor.

The requirements stated by Kementerian Pembangunan Usahawan are they need to be registered under Pusat Khidmat Kontraktor or called PKK in order to be entitled for projects under State and Federal Government of Malaysia. Initially, according to New Economic Policy, NEP, Class F are only given projects cost RM100,000 and below for every State and Federal Government projects. However, our former Prime Minister, Tun Dr. Mahathir Mohamed has made announcement through the 2003 Budget Speech that the entire allocation of maximum RM100,000 is not reliable anymore that it need to be increased to RM200,000, based current standard increment of cost and living. Meanwhile, the contracts works for statutory boards need to allocate a certain cost of 10% of the overall amount of the project cost for the Class F, whereby the award of the contracts are normally through tendering, quotation or requisition.

The mechanism on the allocation of the job of 10% to Class F contractors seems to have weaknesses. In the end, the Class F group seems to be blamed because of their lack of skills and knowledge in various level of construction, which lead towards further difficulties in segregating the job by the main contractors, and many more problems and dilemmas. The true and effective short and long term remedial remains unsolved because this lowest class are stills left behind without proper and organised method and mechanism of segregating the jobs given, especially the one that needs expertise. As of the weaknesses in the latest guidelines, there are items like 2.7.1, 2.3.1, 2.4.1 and 2.6.1 that need to be reviewed.

There must be a true and affective mechanism on the policy of the allocation of the 10% cost of contract to Class F contractors. This group needs a serious attention on monitoring and control of the work done by them as they need to undergo a real kind of on-job training and exposure, so that they can grow skilful and more professional. As per study, below are the several issues that need to be tackled:

- i) What have been done by the Government of Malaysia to address the Class F issues?

- ii) How are the success and the effectiveness of the Government's policy of allocation of 10% costs of contract of large contract to Class F contractors?
- ii) Why the Class F seems to face the problems and dilemmas especially in participating in large projects?

Therefore, a study needs to be carried out to explore the problems and dilemmas of Class F contractors in participating in large projects as imposed by the Government of Malaysia.

1.3 Aim and objectives

The study is to analyze the current problems or dilemmas of Class F contractors in participating in large projects. To achieve the aim, the following objectives are formulated:

1. To investigate the previous efforts done by the Government of Malaysia about Class F contractors
2. To study the success and effectiveness of the policy of 10% job allocation to Class F contractors
3. To analyze the problems and dilemmas of Class F contractors in participating in large projects

1.4 Scope of study

The scope of the study is on the Bumiputra contractors in Malaysia, which are Class F and Class A. As of recorded, there is a total of 44,580 contractors registered with the Contractors Service Centre or called Pusat Khidmat Kontraktor, PKK. Out of which 90% or 40,305 of them are Bumiputra. The number of Class F

contractors is the highest which is more than 50% out of total number of 40,305. The classification of the contractors is in accordance with the paid-up capital and also their experience. Therefore, the policy of procurement would be made through tenders are among the steps to ensure the equal participation of Class F contractors continue (Dewan Rakyat, 2010).

The Bumiputra contractors had yet to achieve satisfactory levels in company management, project execution, and financial strength had yet to fully utilise technology and human resources. The contractors were promoted from class to class, hence deriving experience. Such a few requirements in tenders such as price and technical ability are taken into account. The Government of Malaysia through its Public Works Department, PWD or called JKR, will monitor the technical criteria and do not any prohibit any contractors that have the ability and the capacity, to execute a purchase or projects. As per open tenders, such measure could overcome wastages compared to other.

Meanwhile, the Government identified new potential economic areas, under the National Key Economic Activity (NKEA,) for the participation of Bumiputra entrepreneurs. Malaysia's 6th Prime Minister, Datuk Seri Najib Tun Razak has mentioned that there are between 12 and 14 areas have been identified to be listed under the NKEA. Bumiputra entrepreneurs are encouraged to venture into new potential industries and avoid industries which already had many players. The idea of venture into businesses which had already reached a saturation point is discouraged. According to per capita, Malaysia has the largest number of Class F contractors in the world. The potential companies which had an edge over others will be given place.

Under the New Economic Model (NEM) only companies which are competitive and accredited based on merit would be considered for government assistance. For example, Ekuiti Nasional Bhd (EKUINAS) would only look for companies which qualify to be upgraded and will be injected with equity funds. The non-Bumiputra businessmen were also encouraged to assist their Bumiputra counterparts. (Bernama, 2010)

The study is also to cover the action taken by the Government of Malaysia to address the Bumiputra issues. One of the measures taken is the implementation of the policy of the allocation of 10% cost of contract of large projects to Class F contractors. The policy has been first introduced in March 26, 2008. The meaning of large projects is the project cost more than RM10 million, and only been given to Class A contractors. Regardless, there are still weaknesses in the mechanism of the policy on Class F contractors. Thus, the overall objective of the measure which is to enhance the experience and skills of the Class F contractors seems to be undermined. Under the NEM, the competition is great and tight. Nonetheless, the Class F contractors seem to be unprepared for the challenge, in terms of skills, exposure and experience to stay competitive.

Thus, the entire study is to cover the scope of contractors between the Bumiputra Class A and Class F contractors that operated within the area of Wilayah Persekutuan Kuala Lumpur only. They must be registered under LPIPM (Lembaga Pembangunan Industri Pembinaan Malaysia) or called CIDB Malaysia (Construction Industry Development Board Malaysia) and PKK (Pusat Khidmat Kontraktor) of Kementerian Kerja Raya, KKR or called the Ministry of Works.

1.5 Research methodology

There must be an effective method to ensure the success of the objective, whereby the entire process has been divided into three (3) categories and they are literature review, data collection and data analysis.

1.5.1 Literature Review

At first, the study will be based on previous database. The databases will carries from old thesis, journal, articles, newspaper cutting, e-zines, magazines,

books, websites, and circulars. The vast range of references will provide a better understanding on the entire study, the problem, the aim and the objectives.

1.5.2 Data Collection

Second is the collection of raw data. This is important as the exclusivity of the collection of data will bring significant impact on the finding of the study. As per the study, the collection will be based on distribution of several sets of questionnaires among the two (2) classes of targeted contractors which is Class F and Class A Bumiputra contractors. They must be registered by CIDB and PKK, and operate within Wilayah Persekutuan Kuala Lumpur.

1.5.3 Data Analysis

On data analysis, the entire raw database from the questionnaires will be process. The exclusivity of each data will be analysed, and converted into verifiable conclusion like graph and chart. The graph and chart will represent the entire finding of the study. Then, an appropriate recommendation will be given based on the latest finding and the current situation.

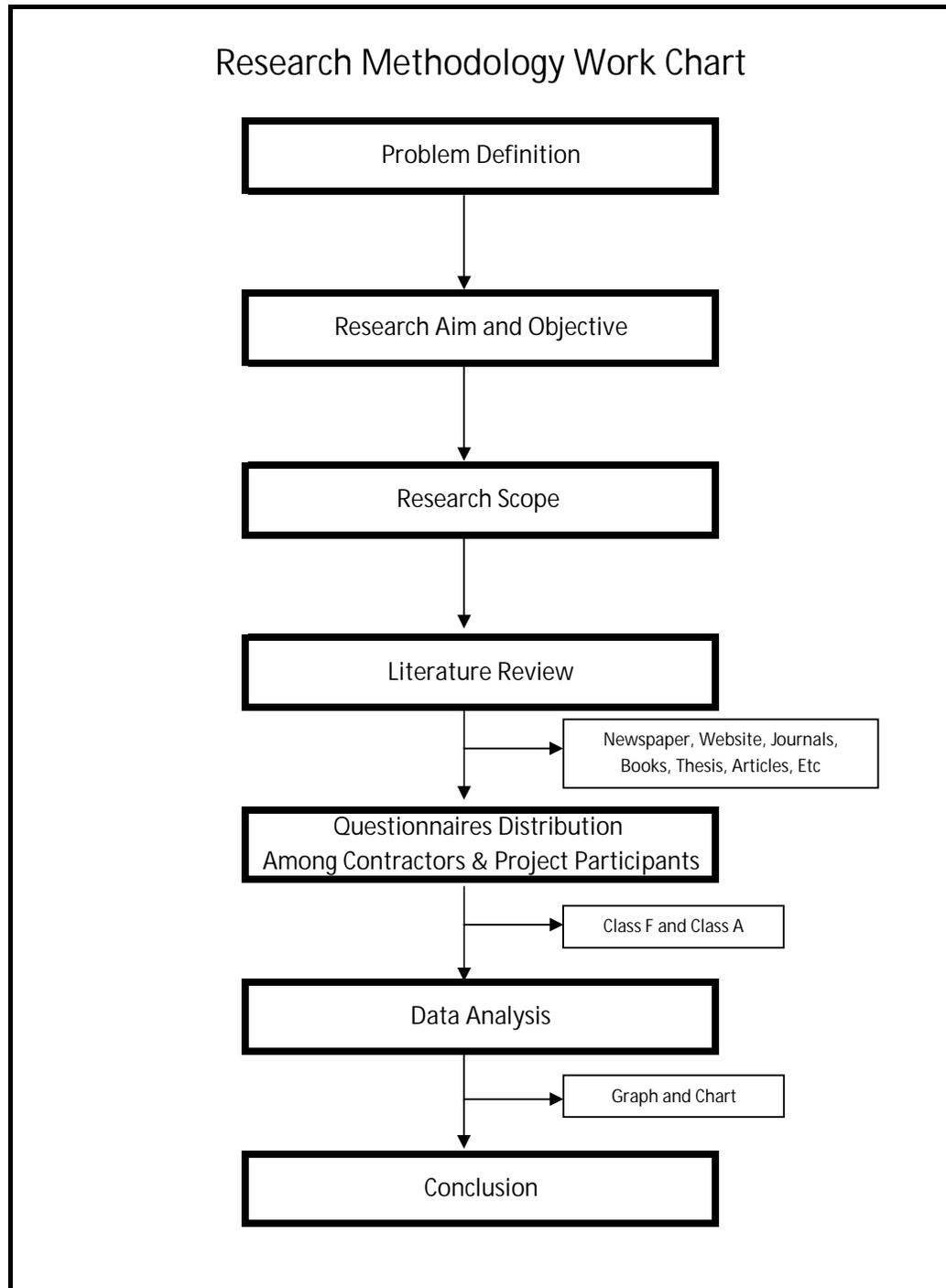


Figure 1.1 Work Chart of Research Methodology

CHAPTER 2

CONSTRUCTION INDUSTRY IN MALAYSIA

2.1 Introduction

ITALIA, An Overview of Malaysian Construction Industry (2009), dictates that the Malaysian economy contracted by 6.2% in the first quarter of 2009 (4Q 08: 0.1%) due mainly to a significant deterioration in external demand and the decline in domestic demand. External demand deteriorated significantly following the deepening recession in several advanced economies as well as slower growth in the regional economies. Domestic demand contracted, due mainly to weaker investment and private consumption activities.

On a sectorial basis, weaknesses were seen across all economic sectors, with the exception of the construction sector. The manufacturing sector recorded a sharp decline amidst significant deterioration in external demand as well as weaker domestic conditions. The services sector registered only a marginal decline, due to weaker growth in sub-sectors closely linked to the manufacturing sector and trade-related activities. The performance of the agriculture sector was affected by weaker production of palm oil and rubber, while growth in the mining sector continued to be sluggish on lower output of both crude oil and natural gas.

Meanwhile, the construction sector has recorded a GDP growth of -1.6% in the fourth quarter of 2008 in comparison to 3.9% and 1.2% in the second and third quarters of 2008. It turned around to register a small positive growth of 0.6% in the first quarter of 2009, supported by the higher construction of office space especially in the Klang Valley as well as, supported by increased activity