

INCO EASTCON 2000
The Modernisation of the Construction Industry in Russia and
Poland: Policy Conditions and Organisational Initiatives for
a Successful Transition toward a Market Economy

Russian Research Team Final Report
March 2000

1. Overall Objectives of the Russian Participation

The following overall objectives were set:

- To deepen the understanding of the trends in the modernisation of the construction industry in Russia with special regard to the conditions that could support a successful transition process towards a market economy;
- To identify, analyse and circulate information on critical success factors in the institutional, organisational and cultural reorganisation of construction companies to match the requirements of a new competitive market;
- To provide local policy makers with the necessary insight to promote policy recommendations on how to overcome the factors hindering the process both at the organisational and institutional level;
- To generate content and methodological expertise to be disseminated via the training activities of the Russian partner and to improve the capacity of local institutions to support the process of transformation of the construction industry.

2. Research Approach and Methodology

2.1. Research Approach

Critical success factors and policy conditions were identified on the basis of a systematic process of analysis and interpretation of qualitative and quantitative data regarding the most critical processes in the management of construction organisation in the transition toward a market economy.

The data was gathered in strict consultation with members of the construction industry with the use of a participative approach to the data collection. This was achieved in three ways:

- The data was collected on the basis of direct contact with the industry through in-depth interviews and site visits;
- The research included a number of consultation/feed-back cycles in the form of workshops aimed at testing the new emerging findings with the industry representatives and with a view to disseminating the results in the course of the project;
- The project was supported by a construction industry project advisory panel which in Russia was represented by Dr. Andrey Panibratov who is a deputy director of a local contractor and a senior lecturer in St. Petersburg University of Economics and Finance.

2.2 Methodology

The selected methodology of the research is to some extent represented in the description of work task activities (see Section 3). The following methods of research and analysis were used:

- contextual and background data gathering through literature review and interviews with local experts, entrepreneurs and government officers;
- data collection workshops (focus group technique);
- company case studies (field research);
- comparative analysis of field data on the basis of inductive cross-case analysis.

3. Overview of the Work Programme

The project was organized into six work tasks, each of which constituted a separate set of organisational and research activities and was aimed both at obtaining some valuable interim research data and the development of an organisational and research basis for the follow-on work task activities.

3.1 The Project Work Programme

3.1.1 Contextual and background data gathering (Work Task 1).

Collected data included

- overview of the construction industry in the period before 1992;
- construction industry development in the transitional period (after the year 1992);
- present status of the construction industry;
- typical ways of construction companies' reaction to the changes and the ways they used the new opportunities.

Data was collected

- thorough literature review (Russian National Library, Libraries of the State University of Architecture and Civil Engineering, St. Petersburg Technical Library);

- by interviewing local scholars and experts, as well as representatives of the construction industry in the city of St. Petersburg and in the town of Veliky Novgorod;
- by interviewing municipal politicians and government officers in the city of St. Petersburg and the town of Veliky Novgorod.

As the result of the above work, the Work Task 1 Report was issued by the GASU on the 4th of December, 1999 (a total of 19 pages, plus two annexes). The information contained in the report was the subject for review and discussion at the Project Meeting No.2 on 14th December 1998 in St.Petersburg.

3.1.2 Designing the data collection process (Work Task 2)

This task focused on agreeing specific data gathering methods and sources, methodologies of initial and in-depth analysis of qualitative data, and training of local research team.

The data gathering methods and methodologies of analysis were discussed and agreed during Project Meetings 1 and 2 in London and St. Petersburg, as well as at GASU in-house meetings. It was decided that the focus group techniques were to be used for the collection of qualitative data through five data collecting workshops.

As part of Work Task 2 the Russian research team took part in a training workshop run by Dr. May Pettigrew from The Tavistok Institute. The purpose of the workshop was to train members of the research team in the methodology of running focus groups, the preparation of questionnaires and in conducting an initial analysis of collected data. On January 28, 1999, the team ran a pilot focus group under the supervision of Dr. May Pettigrew. The data obtained was processed by the team and evaluated by researchers at the Tavistok Institute. Feedback from the Tavistock Institute proved to be very useful for the organisation of future focus group sessions and further analysis of the obtained data.

3.1.3 Identification of critical processes and prospect case studies (Work Task 3)

The key objective of Work Task 3 was to identify and to increase understanding of critical success factors for construction companies in St. Petersburg and Veliky Novgorod. The research activities were performed in the city of St. Petersburg and the city of Veliky Novgorod with the use of the focus group techniques. Four sessions were run in the period between February and April 1999. The total number of construction companies participating in the these groups equaled 23. The choice of participating companies made by the GASU research team was based on the following criteria:

- Current level of activity of a company in the construction market, “historical” data, that can prove that a company may be referred to as “successful”;
- Covering all the most important categories of construction companies with the special focus on main contractors, subcontractors and specialist contractors;
- Maintaining realistic balances between the big and medium-sized companies as well as old and new companies.

The results of Work Task 3 activities were discussed at INCO - EASTCON 2000 Project Meeting No.3 that took place in Poland on April 12-13, 1999.

The report on focus groups was submitted by the GASU team to the Tavistock Institute on April 30, 1999. It consisted of an analysis section, statistics report and a list of participating companies. Findings from Work Task 3 research activities formed the basis for further field research (case studies) which was carried out as part of Work Task 4.

3.1.4 Company case studies (Work Task 4)

Work Task 4 was implemented in two phases:

1. Preparatory Phase
2. Field Research Phase.

The following tasks were executed during the Preparatory Phase (April-June 1999):

- ✓ The programme of case studies was worked out and agreed
- ✓ The target companies for field research were identified in accordance with requirements set out in the Terms of Reference and augmented at the Project Work Task meetings
- ✓ A case study protocol was drafted
- ✓ Case study questionnaires were developed
- ✓ A pilot case study was carried out

During the Field Research Phase (July-October 1999) eight case studies were carried out, and the obtained data was translated into English. A preliminary analysis of the field data was made by the end of October, and a Work Task 4 report was prepared and submitted to the Tavistock Institute in the first week of November, 1999. At the final stage of the Field Research Phase Dr. D. Nicolini, the Project Co-ordinator, conducted a cross-case analysis briefing for members of the Russian research team, which proved to be very useful for the team's analytical work as part of Work Task 5.

3.2.5 Comparative analysis of field data (Work Task 5)

A cross-case analysis of the field data was carried out by the Russian research team during November 1999. This report contains findings and results of the analysis.

▪ Sectoral conferences on the best practices and policy innovation (Work Task 6)

4. Background data and its interpretation

Contextual and background data collected as part of Work Task 1 provided a good understanding of the ways to success of different kinds of construction companies and formed the background of further research activities. The main findings at this stage can be summarized as follows.

1. As the result of the local construction industry decentralization and privatization of the state-owned construction trusts that took place in the early 90-s, the following kinds of construction companies appeared:
 - construction trusts, DSKs and construction enterprises that managed to retain their structure and main assets and were transferred into JSC -public or limited. (further referred to as “old” and/or “big” companies)
 - construction companies that appeared on the ruins of those trusts that failed to maintain their position and split into a number of legal entities (“new” companies, both “big” and “medium”).
 - new construction companies which are limited liability companies or private enterprises established from scratch and which specialise in specific works in accordance with requirements of the growing market (further referred to as “new” companies – most of them are “medium” or “small” companies)
2. The key factors of successful development of construction companies in the period of transition to the market economy are internal factors, i.e. creation of an effective structure, good management, ability of a company to react to changing economic environment, etc.
3. The role of a director (and other top managers) in achieving the success of a company is very important. This is true for both kinds of the existing construction companies, “old” and “new”.

Analysis of contextual and background data helped the Russian research team to form the criteria for selecting construction companies for further research (Work Tasks 3 and 4 activities) and to create hypotheses that were checked during the project.

The initial hypotheses were as follows:

1. There are two kinds of construction companies currently in existence in the market that can very generally be defined as “old” (having existed in the soviet time) and “new” (established in the 90-s). Both kinds include successful companies, but their methods of achieving success differ and their practices in the market also differ.
2. The methods of achieving success to a large extent depends on the profile of the company.
3. Factors of success can be grouped as follows: “external factors” (political and economic situation, taxation, competition) and “internal or in-house factors”

(management, marketing and development, organizational and institutional issues). “Internal” factors of success must be considered as the most crucial for achieving/developing success.

Further research has not only proved that the above hypotheses were generally right, but has given a much deeper understanding of the reality and trends hidden behind the above assumptions.

For example, the differences in approaches of “old” and “new” companies towards the challenges of the emerging market economy were most obvious on the extreme ends of the scale. But between those there is a whole lot of companies that, being “old” in age, are more or less “new” in their development concept and practices. It was noticed that “old” companies are mostly the big ones, and “new” companies are medium and small companies. However, some of the “new” companies have grown substantially both in assets and in the number of staff, and must be referred to as big now (Company 2).

The scope of differences in methods of achieving success practiced by particular companies is a function of time. For example, the difference in approaches between the “old” and the “new” companies, that was very obvious and decisive in the period of privatisation and establishment of the market relations in construction (up to mid 90-s), appears to be less distinct nowadays.

So we came to the conclusion that, where appropriate, we were to look at things in their development, rather than just to investigate a “slice” of the present situation. To do that we identified two “historical” phases of development of successful construction companies (see Section 9 of this report).

The first phase which further in this report is called the “rocket boost” phase is characterised by what we call “effective use of company’s original advantages” whatever they are. In other words – all approaches are good for a particular company if they work for its success. “Old” companies would obviously take advantage of their name, monopolist/semi-monopolist status, expertise, permanent clients, lobbying possibilities, ownership of data bases, valuable basic assets and others, including improvement of management. “New” companies and some of those in between will benefit from better management, competitive environment, flexibility, small overheads and therefore the possibility to pay more to their staff, lack of unused basic assets, the use of up-to-date technologies and materials and following the “no job is too small” principle.

The second phase which in this report is called “survive and develop” phase, is taking place now and is characterised by more advanced market relations and therefore more common approaches and techniques used by the “old” and the “new” construction companies in order to achieve and develop their success - and those to a larger extent are market techniques. The economic crisis of August, 1998 has boosted this development even further.. The “survive and develop” approach to developing success has been discussed by companies subject to our field research and is summarized in Section 9 of this report.

It is also important to note that today most of the successful companies are creating conditions for their successful development from within their companies, treating the unfavorable economic situation purely as an environmental factor which is common to all market players.

*RUSSIAN CONSTRUCTION COMPANIES IN THE TRANSITIONAL PERIOD
COMPANY SUCCESS FACTORS*

Figure 1 *The beginning of transition to the full-scale market economy in Russia (early 90-s) The main factor of success is good use of companies' original advantages, plus profound learning efforts*

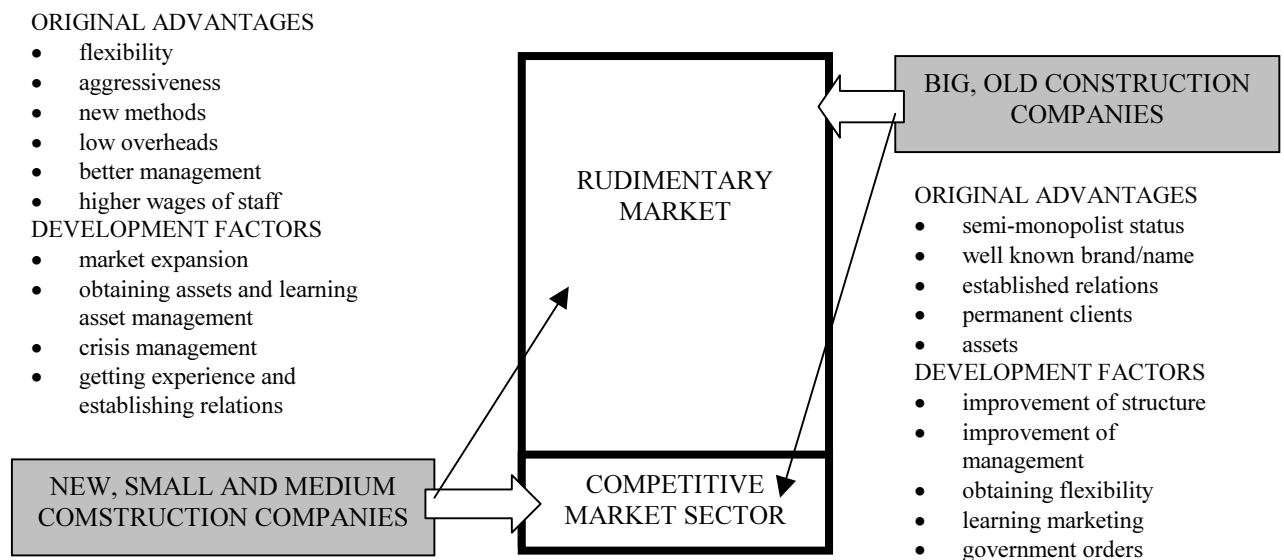
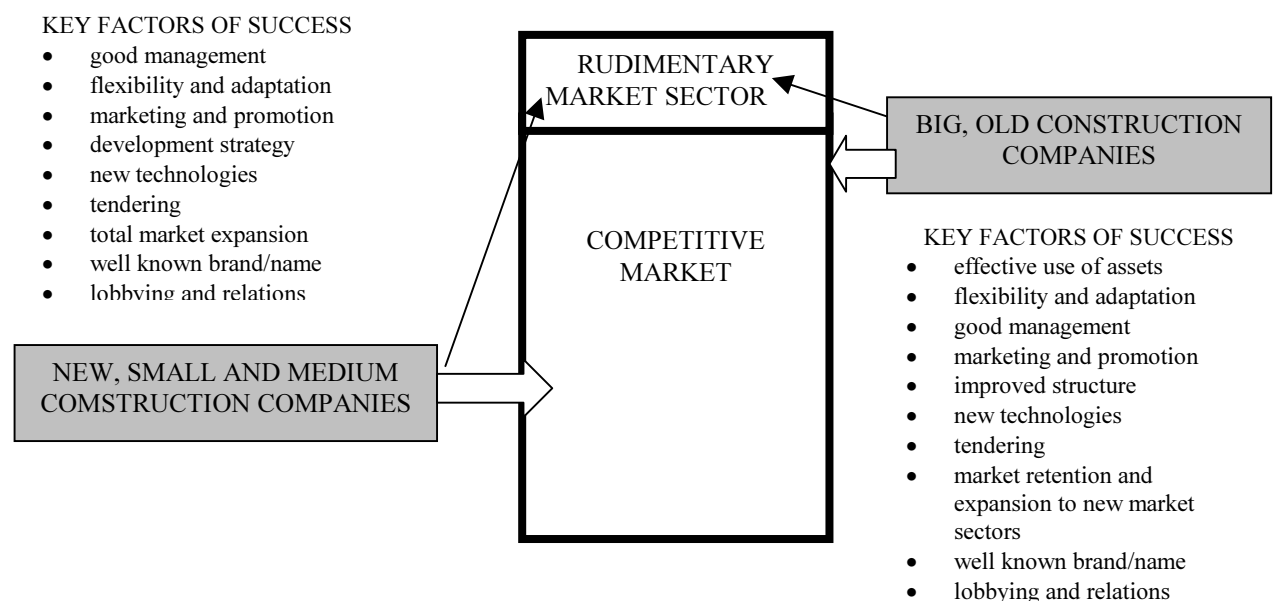


Figure 2 *Advancement of competitive environment in construction sector under unfavorable economic conditions (today). Factors of success of both kinds of companies have become much in common*



5. Selection of construction companies for focus group sessions and case studies

The selection of construction companies for focus group sessions and case studies was performed on the basis of criteria described in section 3.1.3. A total of 23 construction companies took part in the data collection workshops run by the Russian research team. Nine companies were the subject of in-depth research as part of Work Task 4 (case studies).

To summarise the description of selection criteria, we can say that the companies were selected in a way that insured full coverage of the local construction sector and adequate representation of the local construction market players.

6. The Definition of a successful company

According to managers of the construction companies under investigation, a successful company is a company that

- pays competitive wages to the staff and has the possibility of hiring the best professionals
- is a team of highly qualified professionals
- provides the highest quality services
- has a very good reputation among its clients
- constantly expands its share in the market sector
- introduces new methods and techniques

All the investigated companies claimed that they were *the* successful ones. Having been asked the question of how they could prove that they were really successful, the answers were as follows.

- *“Unlike a lot of other companies we pay our staff regularly. The wages of our staff are not very high, but they are competitive. We have a very good team of professionals. People are happy to work for the company because they are part of the team, part of our “family”. We must also stress that our reputation is one of the highest in Russia among the companies of the same kind”* (Company 1).
- *“We are developing very fast. Having started our business from scratch five years ago, we are now the most dynamic company in our market sector. We have survived the crisis of 1998 and even managed to expand our activities.”* (Company 2).
- *“Though being referred to as the ‘most successful housing construction enterprise in St. Petersburg’, we are not quite happy about our development. We are now in the process of modernisation and restructuring, that will help us to reduce costs and introduce new methods of construction that would meet the highest standards. The crisis hit us, but we have survived – that is why we think that we are a successful business.”* (Company 3).
- *“We participate in 100% of tenders for infrastructure development projects in St. Petersburg and we win a lot. We have won jobs in projects financed by EBRD*

and the World Bank. Wish we were able to pay our staff more, though we do try to keep the wages at a competitive level.” (Company 9).

- *“We are successful because we have survived last year’s crisis. Not all small contractors were able to do that.” (Company 5)*
- *“We are a very young company, so we did not make as many mistakes as our older competitors. We have a clear and realistic development strategy. We use Information Technology, and our staff is young and energetic.” (Company 8).*
- *“We have a share in the market and we know how to expand it. We have just finished modernisation of our manufacturing facility, so our elevators will be even more competitive next year. And our services are cheaper than that of Otis – our key competitor.” (Company 6).*
- *“We are proud to say that we have the largest share in the market of high-tech housing construction. Our success is based on new technologies and new construction materials. Good management and planning is also very essential.” (Company 7).*

It is interesting to notice that *“ability to pay competitive wages to company’s staff”* was treated as one of the important evidences of a company’s success by 100% of companies, both those that were subject to our field research and the participants in Focus Group sessions.

7. Main factors of success

As it was mentioned in Section 4, the key factors contributing to success of a construction company can be split into two groups: the **internal factors**, which are the most essential, and the **external (economic and legislative environment) factors**.

7.1 External factors of success

The most important factors that influence company business and the ways construction companies practice, mentioned by all investigated companies, are shown in the table below.

| <i>External Factors (NEGATIVE)</i> | <i>Influence</i> | <i>Company Reaction</i> |
|--|--|--|
| Federal and municipal tax policy | Taxes are extremely high and prevent business development | Tax management |
| Money surrogates, barter deals | Reduction of companies’ working capital, insolvency of clients | Hire specialists in barter deals and security operations, open barter deal departments |
| Economic instability | Economic and financial crises | Crisis management |

| | | |
|---|--|--|
| Political instability | Causes general unfavorable environment | Survive |
| Bureaucratic licensing certification and agreement procedures | Prevents fair competition | Use lobbying possibilities, hire appropriate specialists |

| <i>External Factors (POSITIVE)</i> | <i>Influence</i> | <i>Company reaction</i> |
|------------------------------------|---|---|
| Competition | Maturing of competitive environment that can both be advantageous for a company and dangerous, depending on the company's practices in the market | <ul style="list-style-type: none"> • learn to work in competitive environment • proper budgeting • commitment to quality • added flexibility and responsiveness |

It is important to note that all the companies under investigation considered competition to be a positive factor, even those who took advantage from their retained semi-monopolist position in their sectors of construction market. The attitude of company managers towards competition seems to be very important and must be considered as one of the indicators of a successful company. The typical comments of the companies' entrepreneurs about competition were as follows:

- A. *"we could only start our business due to the emerging competitive environment which 'till now unfortunately has not developed enough yet."* (Companies 2, 5 and 8);
- B. *"we stand for fair competition, we would definitely take advantage of it."*(Companies 4 and 6);
- C. *"we are for 'controlled' competition, which would help us to improve quality and teach us how to budget; but we would like to retain our semi-monopolist status and only allow our competitors a small share of the market* (Companies 3 and 9);
- D. *"competition is a good thing and we are not afraid of it, we try to take advantage of it."* (Companies 1 and 7).

Comments C and D belong to entrepreneurs of "old and big" construction companies that, unlike the "new" companies who took advantage of competition from the beginning of their establishment, had to learn hard how to act in a competitive environment.

All entrepreneurs agree that competition at present is still not fair enough due to the current legislation, bureaucracy and bribing, but they say that it is maturing.

Another external factor that causes lots of problems to construction (and any other) businesses is lack of cash due to insolvency of Russian clients. The result is flourishing of the non-monetary settlements, like barter deals, settlements on taxes,

tied-up securities, and other kinds of non-monetary settlements. These cause the following problems:

- lack of working capital
- inability to apply for bank guarantees and therefore inability to win international tenders for construction works
- diverting qualified personnel to handling barter deals.

All the investigated companies use non-monetary settlements with their clients, suppliers and subcontractors, some of them have managed to turn this to their advantage over the foreign and joint venture competitors (Companies 2 and 7). Some of the companies hire specialists to handle barter, or even establish specialist departments to handle barter/non monetary settlements.

Here is a typical comment on the external problems: *“The main obstacle to success is the fact that there is no money – our clients have no money to pay us, therefore we have no money to pay to our subcontractors, including our foreign partners for their services. Every year the requirement for renewing our license increases and the bureaucratic process instead of getting easier is getting worse. Current tax policy eats a huge percentage of our income from projects.”* (Company 1)

During the research the interviewed companies added a third dimension to the investigated issue (i.e. factors that contribute to success), by suggesting an additional, factor described by them as *“the ability of a company to survive in a hostile economic and political environment”*, which is not just good crisis management, but rather a specific approach to doing business in Russia. According to most entrepreneurs, this ability (or rather art) is crucial for achieving/developing company’s success in the current economic environment. It includes the ability to:

- quickly react to any minor changes (or expected changes) in the federal and local legislation, norms and regulations, and alter tactical plans accordingly;
- reduce costs by keeping wages and overheads low, and by finding more competitive suppliers;
- retain professional staff;
- accept and handle barter deals and non-monetary settlements, including the so called “barter chains”;
- use permanent and well known clients, suppliers and subcontractors;
- use locally manufactured construction materials;
- diversify business by adding new non-core activities and, where possible and appropriate, new core activities;
- use lobbying possibilities and personal relationships at all levels;
- use the “no work is too small” principle

All investigated companies use methods and approaches listed above in different combinations, in order to survive in an unfriendly economic climate. At the same time all the entrepreneurs stress that *just to survive is not enough for achieving success. It is crucial not to miss strategic development.*

Therefore, the summery is as follows: combination of adaptation and development (flexible tactics and good strategy) is the most important key to success in the current environment. Typical director of a successful company must be focused on taking advantage from competition or at least consider growing competition in company development concept.

7.2 Internal factors of success

As it was mentioned before, the internal factors were considered by entrepreneurs of the investigated companies as the most crucial for achieving/developing success. Some of those factors were already mentioned in subsection 7.1 of this report in connection with the art of surviving in a hostile economic environment.

The key internal factors that contribute to success were identified during the cross-case analysis (as groups of themes). They are as follows.

- GOOD COMPANY MANAGEMENT
- GOOD COMPANY STRUCTURE
- PERSONNEL DEVELOPMENT
- GOOD MANAGEMENT OF ASSETS
- MARKETING AND PROMOTION
- COMMITMENT TO QUALITY
- DEVELOPMENT STRATEGY
- PARTICIPATION IN TENDERS
- USE OF UP-TO-DATE TECHNOLOGIES AND MATERIALS
- GOOD TEAM, CORPORATE TRADITIONS
- USE OF CREDIT
- LOBBYING POSSIBILITY

8. Description of the internal factors contributing to success

8.1 Good company management

Five companies of the total of nine under investigation consider good company management as the most important factor of their success (Companies 1,2,7,8,9).

According to the interviewed entrepreneurs “good company management” means the following.

- *knowing the company’s objectives and having the courage to achieve them* (Companies 1,3,9)
- *creating a good in-house management system and structure* (Companies 2 and 8)
- *delegation of responsibilities to middle managers* (Companies 2 and 6)
- *using IT in management* (Company 8)
- *training of managers* (Companies 1,2,4,5,6,7,8,9)
- *collective decision-making* (Company 2)

All the companies stressed the very important role of their directors.

A number of companies connect their success wholly with their directors. For Company 1 the Director is everything: he is the sole decision maker, he personally brings in 50% of jobs for the company, he lobbies the company's interests in the municipal administration and among clients. The middle managers of Company 1 admit that such an important role of the director can make the company potentially vulnerable, and that to insure sustainable development of the company the management structure should be altered and more responsibilities delegated to lower management levels.

Company 3 still practices a very conservative and traditional management style (strong vertical management hierarchy, director is the key decision-maker). Being an "old and big" one, this company took advantage from this conservative style in the mid 90-s, but now the management system is being altered. Though the structure still remains vertical, more and more responsibilities are being delegated to the middle managers. According to the director of the company, "*new management methods and approaches are only introduced if there is an obvious need for them, but once the decision is made to make any alterations it is pushed forward very energetically under strict control of the powerful director*".

In the old companies (which are mostly the privatised big construction trusts) the important role of directors lies in their ability to effectively use the original advantages of their companies multiplied by their ability and their will to introduce changes that are dictated by the maturing market environment. In accordance with the current legislation, directors of such companies are elected by the company staff every five years.

The director's role in new companies is also very important, but for a slightly different reason - the director is most commonly the owner (or one of the owners of the business).

The management structures of successful companies range from vertical and hierarchical (Company 3) to very flat (Company 2). There is a general tendency of moving towards flatter management structures and towards delegating more responsibilities to middle managers.

Top managers of most of the successful companies have undergone management training in Europe (see Subsection 8.3).

8.2 Good company structure

According to the interviewed entrepreneurs "good structure" is:

- *flat* (Companies 2, 5, 6 and 8)
- *flexible* (Companies 1 and 9)
- *loose* (Company 4)
- *conservative, vertical structure* (Company 3)

All the companies have agreed that company structure, even when considered effective, should not be fixed. There are vivid tendencies of transferring to flatter structures and more flexible structures, allowing to easily modernise and add/remove structural units. The structure of Company 1 consists of two elements: administrative and operational. This adds flexibility and allows the company to effectively cover different regions of Russia. Companies 2 and 5, while expanding the range of their activities, think about transferring some of their operational departments to daughter companies. Company 7, being in the process of diversification of its business, creates a new daughter company for each new area of activity, thus actually becoming a holding.

8.3 Personnel development

As was mentioned in the previous subsection, most of the companies' top managers have undergone management training in the West (mostly during the "Perestroika" period of the late 80-s – early 90-s) or at management courses run by western training centres in St. Petersburg. A typical training course lasted about a week (some attended several courses of different kinds). The learned disciplines included company management, marketing, project management, estimating, tendering, international contractual relations. All the interviewed entrepreneurs pointed out that learning something about western methods of management proved to be useful though not enough for the successful running of their businesses. However, it can be concluded that a chief executive who has some knowledge about western methods of management and who is open to further training is an important asset for a company trying to achieve success.

The picture is different at the companies' middle management level. There are few middle managers who have a specialist knowledge in management-related disciplines. Most commonly people responsible for project management, marketing, tendering and company development are engineers by education and experience. Some of them are learning on the job, others just rely on the knowledge and wisdom of their bosses. Most of the interviewed young specialists holding positions of marketing managers and project managers are eager to learn more, but they have little opportunity to undergo formal training/education because companies are very careful about investing too much into personnel development.

It should be pointed out though that in the last two years all the companies under investigation made some investment into the development of their middle-level management personnel, mostly by sending managers on short-term courses and workshops. The response of those managers who have undergone such training is positive, but most of them say that it is not enough and that they would like to learn more.

When asked about the development of their middle managers, chief executives of the successful companies said the following.

- *"We take any chance of sending our middle managers on short-term refreshment courses, including management courses, but we can not pay a lot for such*

training. We are also unable to let our staff off from work for a long time. Not all the offered training courses are good, not all the western experience is applicable in Russia. So in each case we have to decide whether it is worth spending time and money, and I must say that very often I say: no, it is not."(Company 1).

- *"All our directors have undergone management training. As for our middle managers, we would rather hire a good professional than spend time and money for retraining of our engineers to convert them, let's say, into marketing specialists. There is a lot of good specialists out of jobs now, so it is not a problem to find one for a particular position. Such a newcomer can also train our staff, this is less expensive and does not distract people from their daily work."*(Company 6).
- *"We have to learn a lot about running business in a market environment. If I had funds, I would have sent my key middle-managers to training courses or to undergo some professional practice in a western company. "* (Company 9).
- *"We spend a lot of funds for training of our staff in new technologies and new materials, which is more important for us. As far as management is concerned, some of our middle managers already have some knowledge of western-type management and relevant experience, others learn at work. It does not mean though that we do not retrain our managers at all. We are working out a personnel development programme right now, which will definitely include training in marketing and project management."* (Company 2).
- *"Being a very young company we try to hire people who already have the knowledge and experience required for their positions. This will be augmented by the personnel development programme which will include training in management disciplines. We can be sure that the specialists that we have invested in would not leave, because we are able to offer them competitive wages and the opportunity to develop."* (Company 8).
- *"My key middle-level specialists do their job well. I always give them an opportunity to obtain new knowledge, especially in new methods of construction, new materials, estimating, those kinds of things. I would not invest much into retraining of my middle-managers now for two reasons. One, I can not offer salaries that can be comparable with those in the West, so a manager who I have invested in can move to a western contractor that can offer better wages. Two, little from the western management experience can be used here immediately. Our clients now are mostly Russian. If it changes in the future than we shall also change our approach."* (Company 3).

The company entrepreneurs are happy about the existing system of professional (engineering) retraining, the roots of which lie in the highly praised Soviet professional retraining system. For instance, the key specialists of Company 1 undergo regular short-term training to keep abreast with the fast changing market of technology (e.g. up-to-date computer software, like ACAD, etc.).

Most of the old companies (Companies 1 and 3, for example) are facing the problem of overstaffing. Although the numbers have been reduced drastically during recent years due to people voluntarily leaving the companies (In Company 1 the number of personnel has reduced from about 1000 in 1990 to 740 in 1994 and further to 320 in 1999), there is still surplus available staff and a lack of an understanding of what kind of staff is actually needed. The current Russian legislation makes it is very difficult to reduce staff and so optimize the staff structure.

8.4 Good management of the basic assets

One of the important distinctions between the “old” and the “new” construction companies is that the former have inherited a large amount of buildings and structures, land, plant and equipment, while the latter rent or purchase the basic assets in strict accordance with their immediate needs and further development plans. So it was a priori assumed by the research team that the “new” successful companies must have used their basic assets more or less effectively. This assumption has proved to be true during the research. For example, Company 2 successfully operates the following basic assets:

| | |
|----------------------------------|---|
| Office space and laboratory base | rented from their key partner – Research Institute of Materials; |
| Construction base | the company now owns facilities that previously belonged to its former mother-trust; |
| Plant and equipment | the company owns an inventory of up-to-date plant and equipment which has been purchased in accordance with the company needs; |
| Manufacturing base | the company bought a construction materials manufacturing business together with the manufacturing facilities 2 years ago; the company is considering buying another building in order to expand its manufacturing capacity. |

According to the chief executive of the company, they have just enough assets to run the business successfully and develop in the middle-term. The company also has a strategic development concept, which, if successfully carried out, may require more basic assets.

In the case of the “old” construction companies the situation is different. All of the old companies have inherited many basic assets (administrative buildings, workshops, garages, apartment houses, plots of land, underground infrastructure, social buildings like hostels and kindergartens) a large part of which is run-down and is actually not in use. The run-down assets are absolutely frozen, and yet require costly maintenance.

They are the real burden for the companies, so good management of such kind of assets is an important factor for their financial stability.

According to the entrepreneurs of the investigated companies that can be referred to as “old” (Companies 1,3,7,9), they use the following ways of handling excess basic assets:

- rent out office space, workshops and garages (Companies 1,3,7,9)
- use free space for running additional non-core activities in order to compensate maintenance and tax costs (Companies 1,3,7,9)
- sell liquid assets (Companies 1,9)
- refurbish office buildings and workshops and use them for expansion of core business (Companies 3,7)
- barter unused basic assets for other things (Companies 1,8).

8.5 Marketing and promotion

All of the companies under investigation consider good marketing as one of the most important factors of their success. Five of the nine companies under investigation have marketing departments, in others marketing is the responsibility of their directors. Only two companies (Companies 2 and 8) have professionals in charge of marketing, others rely on the experience of their directors or hire non-professionals which is less expensive.

The marketing and promotion methods that are most commonly used by the construction companies are as follows:

- advertising
 - in the press (all the companies under investigation)
 - on radio (Companies 3,5,6,7)
 - on TV (Companies 2,3,7)
 - billboards (Company 7)
- very good bi-lingual (Russian and English) company literature (Companies 2 and 7)
- direct mail (Companies 2, 5 and 7).

Below is a typical example of an approach to marketing and of marketing methods used by a big “new” construction company (Company 2).

8.5.1 Company 2 example

Marketing is considered crucial for the successful development of this company. From the first days of its existence marketing was the centre of attention of its Directorate. The marketing department was established in the mid 90-s with a staff of one which increased to five by 1999. Since 1995 the position of Marketing Director was established to plan and coordinate marketing and promotion activities of the company, its daughter company and trade representatives.

According to the marketing director, *“the company’s marketing strategy includes at least two main elements and approaches: one for highly competitive markets of St. Petersburg and Moscow, the other for the regional markets.*

In the first case the company is positioned as a high tech company successfully competing with Western contractors and offering flexible and high quality services with no compromise.

In the second case it is stressed that the company is the only available option – offering local prices and flexible settlement schemes, using Western materials and ensuring high quality of construction.”

Marketing techniques that proved to be successful:

- “Propaganda” of new technologies and materials, used by the company, in professional and specialist press

This is indirect advertising of the company’s activity aimed at attracting the attention of potential clients to the company. The activity is supplemented by a quick response to requests and inquiries.

- Direct mail campaigns
- Seminars
- Good literature, including company information sheets, description of particular technologies and materials, detailed specifications, references and records, etc.
- Offering “standard” methods of solving “standard” problems.

The most frequently occurring problems and requirements of the customers are analyzed and ways of solving them (covering the whole specter of options) are worked out. These can include low-cost immediate measures up to full-size design-and-build projects.

- Free of charge consultations
- Advertising

Here is a couple of examples of marketing and advertisement actions that have proved to be very effective:

- 1) Advertisement of waterproofing materials manufactured by “HYPROCOR” daughter company.

Slogan “Prepare to enjoy the sound of rain drops tapping – when you put your roof in order”

- 2) Direct mail campaign (the summer of 1998)

Information about the company was mailed to 4000 addresses all over Russia, to include potential clients, regional and municipal administrations, etc. By November 1, 1998 the effectiveness of this campaign was as follows:

$$\frac{\text{net profit from contracts}}{\text{cost of direct mail}} = 39,88$$

The marketing department maintains a computerized data base of customers, competitors, requirements, responses and products. The data base is made on the basis of "Microsoft Access" software.

This company is the "new" one and is acting in the market sector which is characterised by tough competition. So its approach to marketing is the most "western-like" among all the companies under investigation.

Here is one more example.

8.5.2 Company 1 example

Though the company has a marketing department, marketing and finding jobs is the key responsibility of the director general. 50% of all contracts are concluded by the director general who spends 70% of his time to achieve this end. *"We are successful, because I know the market, the competition and the percentage of risk involved"*. 40% of contracts are brought in by the company's regional project managers who operate in different regions and 10% from the marketing department. In 1999 the company acquired a portfolio of contracts worth 26 millions roubles (about 1 million UD Dollars).

The marketing department, apart from bringing in 10% of all work, is involved in advertising and in representing the company at exhibitions.

In this case Director General meant to say: "marketing is me". This approach looks effective at the present time because of specificity of the local and the world markets of engineering design, and also the specificity of relations in this particular company, where the company has delegated enormous power to its DG. But for the future, as it was mentioned by the senior and middle managers of the company this situation can be the source of danger for the company's development and success.

8.6 Commitment to quality

All the successful companies stress their commitment to quality. *"Good quality for modest prices"* – this is the most frequently mentioned advantage of a local contractor over a foreign one which usually offers "the highest quality for high price".

- *"We have developed our own quality standards, which are even stricter than the standard clients' requirements. Our clients must be aware of the fact that we offer*

the highest standards of quality, sometimes even better than that of the western contractors. We can offer better quality for a lower price” (Company 4);

- *“The company offers high quality services and products.. The company uses up-to-date technologies and western-quality materials and ensures the highest standards of work. It must be competitive to Western contractors by offering lower prices for the work of the same quality (due to lower overheads and manpower costs, and lower prices for construction materials, partly produced in Russia), and has to be competitive to the local contractors by offering higher standards of work” (Company 2);*
- *"The company’s mission is to perform good quality housing construction and to ensure comparatively low cost of construction, by means of the effective use of up-to-date construction materials and techniques.” (Company 3);*
- *“We are well known and respected in the market for our quality. We put in a lot of effort to ensure that the highest quality remains even in a smallest project. We are introducing a brand new quality system in our company, and we will certify our quality system to the ISO 9000 international quality standard” (Company 1);*
- *“Quality is very important, especially for such a small contractor as we are. Its a small world, everybody knows each other in the market, so one mistake can ruin one’s image. That is why we are so committed to quality.” (Company 5).*

8.7 Development strategy

All the interviewed chief executives stressed the importance of having a development strategy in a company. The most common comment on that was *“we spend a lot of time and effort just in order to survive, but we do not forget about development, as we know some of the companies who have forgotten – where are they now?”*. Only four of the nine companies claim to have development strategies formally adopted and documented. In the other five companies, development strategies are in the heads of their directors. The following strategic goals have been mentioned by the companies:

- geographical expansion (5 companies);
- ability to complete “turn-key” construction projects (4 companies);
- adding manufacturing capability (3 companies);
- increasing their share in the market sector (2 companies);
- diversification of core activities (2 companies).

Referring to the previous paragraph, companies that have formally adopted and documented their strategies are the “new” companies with more or less flat structures and holding companies (for example Companies 2 and 8). In Company 2 the company mission and Development Strategy in general terms are announced in the company literature. There is also the documented mid-term development plan which is an in-house classified document.

Much more important is what all entrepreneurs refer to as “development strategy in my head”. Taking into account the enormous role that director plays in a typical construction company today (no matter whether it is “old” or “new”) he often personally embodies the success of the business. As it was mentioned before in this report, entrepreneur with an appropriate development strategy in mind and the will and ability to implement it is one of the key factors of a company’s success so far. The most rapidly developing company (Company 2), which is the one that is active in the market sector with the highest level of competition, seems to have overcome this situation by having integrated their strategic development concept in the planning, operating and marketing activities. The current success of companies 1, 3 and 7 is still to the large extent relying on the wisdom and will of their directors. Example described in subsection 8.5.2 shows that the hidden danger of this situation is becoming clear to company’s top managers.

8.8 Participation in tenders

Tenders and tendering came into practice in the early 90-s in Russia. Now more than half of the construction jobs are awarded through competitive tenders, i.e.

- projects funded from municipal and federal funds - 100% awarded via tenders;
- international projects (World Bank, EBRD) - 100% awarded via tenders;
- private clients – competitive tendering has become more popular during recent years.

This makes it crucial for local contractors to obtain a knowledge of tender procedures and application, as well as to gain experience in tendering.

100% of chief executives of the companies under investigation have undergone training in tendering and estimating as part of the preparation to a tender.

Seven of the nine companies under investigation claim that they regularly participate in competitive tenders (Companies 1,2,4,5,6,7,9), five of them bid for all applicable jobs. Two companies have successful experience of bidding for international construction projects.

Here are some companies’ comments on the issue.

- *“We usually participate in several tenders for big jobs every year. Our company has qualified specialists that know the procedures and can prepare tender documents and make estimations. But participating in tenders and not winning is a bad advertisement for the company – that’s why we decline many opportunities and sometimes invitations to tender if I am not certain that we have a chance of winning. We have done well in Russia, but unfortunately I can’t say the same for outside of Russia – I put this down to the fact that we are not well known in Europe”* (Company 1);
- *“Participation in tenders is very important for us. We won our first big job in 1994 on a tender where our competitors were western contractors. We offered a*

better price and the same quality. I must point out that personal relationships are still very important in our sector of the construction market, so it is good to stand on two legs: good tender and good relations” (Company 4);

- *“We bid for most of the available jobs in our market sector and we win at least 30% of them. That is normal for us. By winning even a small tender and by having completed the job successfully we build a reputation for ourselves. So next time clients address us directly” (Company 5);*
- *“Our company has a tendering department that is responsible for tracing open tenders and preparation of tender proposals. We participate in tenders and win jobs not only in Russia but in C.I.S. For example, we have recently won a housing construction project in Kazakhstan (Company 7);*
- *“We have very little experience in tendering. This is because of the lack of competition in our cheap housing construction sector. But we are aware of the market requirements and of the fact that competition will be increasing, so we will be ready to bid for jobs in the near future” (Company 3);*
- *“We have just started to participate in international tenders in St. Petersburg. To be able to do this we have undergone specialist training and employed the service of a specialist consultant. Unfortunately we have not won international jobs yet, but it is the matter of time and gaining experience” (Company 9).*

8.9 The use of up-to-date technologies and materials

The use of up-to-date technologies and materials is considered very important for achieving and developing success by all the interviewed companies, due to the stiffening of standards and construction norms, growing competition and growing demand for good quality construction. The use of new technologies and materials is the cornerstone and one of the decisive factors of successful development of the “new” companies (like Companies 2,4,8). The “old” companies (Companies 3 and 7) are also trying to take advantage of this by introducing up-to-date technologies and construction techniques like cast-in-situ concrete construction, the use of better insulated prefabricated concrete panels, and the use of timber frame construction techniques for small housing construction.

8.10 Good team, corporate traditions

A good team and corporate traditions is something very special and important for most of the interviewed companies. A good team is referred to both as an important factor that contributes to success, and as an indicator of a successful company. The directors of “old” companies as well as the staff are proud of their corporate traditions. This compensates for their modest salaries. “New” companies on the other hand are also anxious about creating and developing their own corporate relations and traditions.

Here are some comments on the issue.

- *“We are a family of like-minded people and we are happy about it. The family always means loyalty. I consider loyalty to the company as the most important characteristic of my staff and it definitely constitutes a key to success, employees demonstrate this by their attitudes to work, their willingness to work overtime when absolutely necessary – this also shows that they are not indifferent to the success of the company (Company 1);*
- *“Our approach which is shared by most of our staff and which we are all proud of is the following “Tradition, realism and conservatism. Our competitors come and go, but we were, we are and we will be” (Company 3);*
- *“Our corporate traditions are changing from allegiance to the company to a team spirit” (Company 5);*
- *“There is good corporate spirit in our company. It can be strengthened even more by letting people better understand the mission of the business and our commitment to the highest standards of service” (Company 6).*

8.11 The use of Credit/Loans

Four of the nine companies (Companies 1,2,5,7) have experience in working with foreign/international banks and financing agencies, like TACIS and EBRD, as well as with the local banks. As it was mentioned before, it is very hard to get loans in the current local economic environment, so companies that manage to do this must have very good reputation and reasonably good cash flow.

8.12 Lobbying possibility

The possibility to lobby interests at the municipal administrative level, as well as close relations with potential clients, are both very important factors of achieving and developing success by a contractor. Those factors were particularly important for the big old contractors at the initial stage of their incorporation into a growing market economy. During recent years which are marked by the growth of competitive market relations, the role of direct relations with clients diminished, although it is still a factor. As far as the lobbying possibility is concerned, in recent years this factor became more important for creating a more favorable administrative and economic environment for construction companies at the municipal level, as well as a tool for defending interests of particular construction companies. It must be noted, that the most successful “new” construction companies in the process of their development and expansion also obtain lobbying possibilities, thus diminishing the principle difference between the “old” and the “new” companies. Contractors lobby their interests in the following ways:

- through public professional bodies and organisations (The Union of Contractors of St. Petersburg, The Union of Designers of St. Petersburg, etc.);
- by creating a “construction lobby” at the City Hall;
- by creating direct relations with relevant committees of the municipal administration

Here are some comments on the issue.

- *“We pay much attention to our relations with the city administration to be aware of the upcoming government funded projects. We also prepare proposals on the future development of the local construction sector for the city administration. But we do not just rely on our relations. We are one of the strongest market players in the city”* (Company 3)
- *“We are committed to competition, and we use all the legal opportunities to lobby the interests of our company and of the whole construction industry at all levels. At the municipal level we do it through the Union of Contractors and other local professional bodies, through direct representation at the City Hall; on the federal level we defend our interests through the federal bodies. We even lobby our interests at the C.I.S level, as we participate in construction projects in the C.I.S countries”* (Company 7)
- *“Being a contractor from the relatively small town of Veliky Novgorod, we have absolutely no opportunities to lobby our interests at municipal or federal levels. To get jobs we combine market approach (participation in tenders, including the international ones) with administrative approach (the use of personal relationships with particular clients)”* (Company 9)
- *“We value our relations with our main clients very much, but we win jobs via competitive tenders”* (Company 4)
- *“We are market players and we enjoy competitive environment. I must say that in our sector of construction market (roofing, insulation and our specialist jobs) competition is high, so no “special” relations or lobbying will help – just the quality and the price* (Company 2)

A typical example of using relationships at the municipal and city district levels is getting plots of land in the city for housing construction. To minimize construction costs and to attract private investors a developer/contractor would seek for sites situated in the existing housing areas, with all underground infrastructure readily available (contractor is to pay to the municipality for the infrastructure), close to metro stations, supermarkets, recreation areas, etc. Though the legislation regulating the land plots allotment is rather strict, there is a lot of opportunities for negotiating better deals.

A typical example of lobbying is continuous attempts (that may prove to be successful in the near future) of big housing developers/contractors and the local Union of

Contractors to introduce hypothec in housing construction. This would need alteration of both the Federal and municipal legislations. The Union of Contractors has achieved some success at the municipal level (St. Petersburg Administration) and even at the Federal level (Committee for Construction, Government of the Russian Federation), together with construction companies and their associations of Moscow and other regions of Russia.

8.13 Requirements to chief executive of a successful construction company

During the research it became obvious that originally the role of chief executive (chief executives) of successful companies, though having been noted during the analysis of background information, was underestimated. In all of the companies under investigation a Director is the main driving force of the successful business development (see subsections 7.1, 8.52, 8.7 and 8.12). The directors' role was especially notable and important at the "rocket boost" stage of companies' development (up to mid-90-s - see Section 9 of this report), and it also remains a factor at the current stage, though there is a tendency of gradual diminishing of this role while a company fits into the market environment. The table below shows the list of the key requirements to chief executive of a successful company, in a way they were described/mentioned by the participants in the current research.

| | Requirements to chief executive | Companies | |
|---|---|-----------|-----|
| | | old | new |
| 1 | An experienced professional that knows all ins and outs of the business | + | + |
| 2 | A person who has personal relations with authorities and clients | + | |
| 3 | A person who is respected in the company | + | + |
| 4 | A person who is focused on taking advantage from competition | | + |
| 5 | A person who considers competition in planning and operation | + | |
| 6 | A person who is familiar with Western approach to management | + | + |

9. Two phases of the way to success and the proposed integrative concept of success

During our research we came across the situation in which different kinds of companies at some stages of their ways to becoming successful used different, sometimes contradictory but nevertheless equally effective, ways of achieving their current success in the market. At the same time their approaches to business and ways of development have much in common. And they are definitely moving closer to each other in these aspects while the competitive environment in the construction sector of Russia is becoming more advanced.

The most important factors of success mentioned by all of the companies under investigation are described in detail in Section 8 of this report. These factors vary in their importance for each company, however, there is a lot of overlapping and common trends.

During our research we mostly concentrated on the current situation in the construction sector and the companies. But we also could not get away from looking at the processes involved in their development. The ways to current success of most of the successful companies cover the period between the beginning of the 90-s and 1999. This period contains two phases that are crucial for understanding the current status of companies and their success.

9.1 Phase 1. Privatisation of construction companies and establishment of a competitive market in construction sector (up to the mid 90-s)

The key to companies' success in Phase 1 was to boost their establishment and development in the market by means of the appropriate use of their original advantages (this development phase is referred to as the "rocket boost" phase in this report). For the big construction trusts that decided to retain their integrity (Companies 1,3 and 7) the original advantages were the following:

- retained semi-monopolistic status in their market sectors
- ownership of valuable assets like basic assets, plant and equipment, professional staff, data bases, know how and other intangibles, "historical" relations with clients and well known reputation.

The original disadvantages of those companies were as follows:

- monstrous structures that needed urgent alteration, overstaffing, run-down basic assets, lack of experience in competition.

The three companies under investigation (and some others in the local construction market) have managed to utilize the original advantages that they had inherited from the previous times (see previous sections of this report). They were also successful in neutralizing their original disadvantages, thus paving the way to further successful development.

The successful companies that were established in the 90-s on the ruins of the big construction trusts or from scratch (the "new" companies) have enjoyed and properly utilized the following original advantages:

- more effective structure, better flexibility, lower overheads
- better management
- better practices in the competitive environment

As it was numerously mentioned in this report, the role of Director of a construction company was extremely important at that stage, it is also important at the next stage of development (see 9.2), but to a less extent.

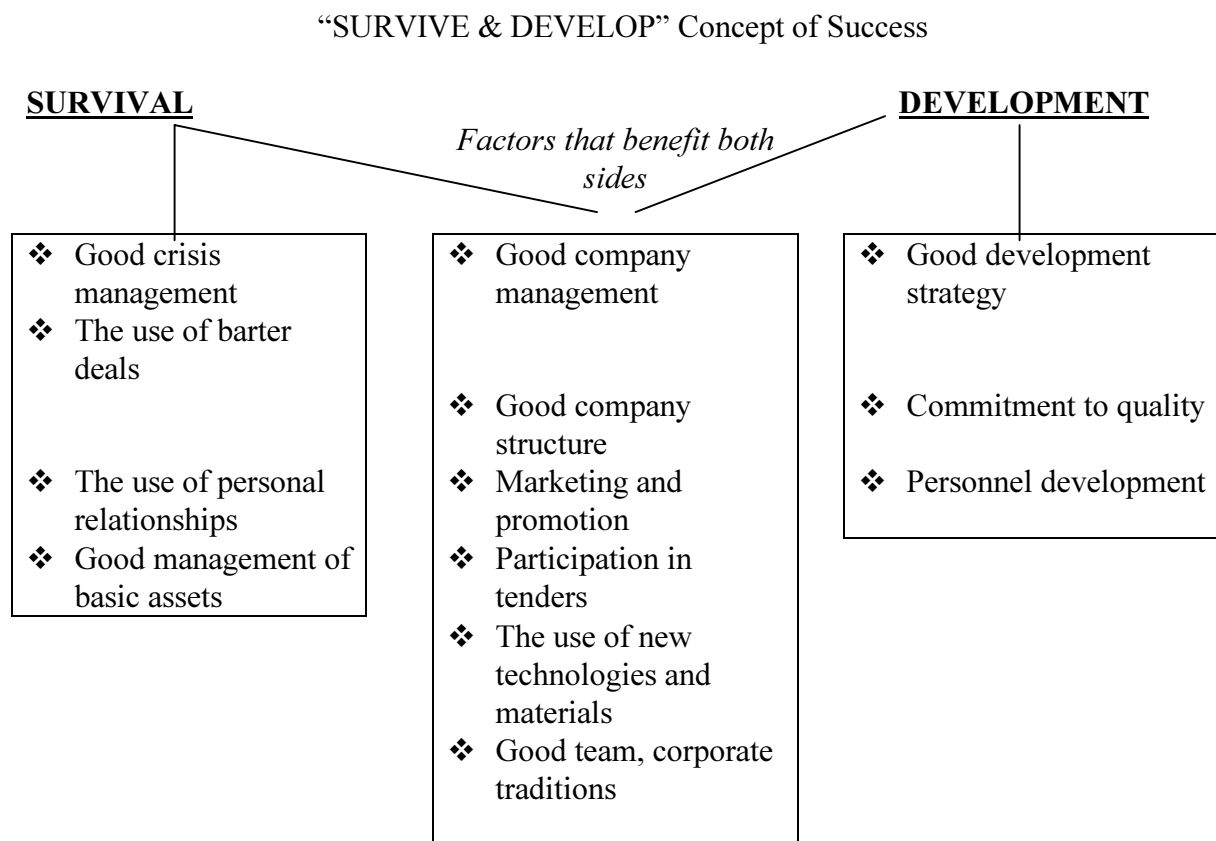
9.2 Phase 2 Advancement of the market economy in the unstable economic environment (ongoing from the mid 90-s till today)

This is an ongoing phase in which companies of all kinds that have successfully established themselves in the market during Phase 1, are developing now. This phase

is characterized by the economic and political instability in the country that caused the financial crisis of August 1998. At the same time the construction sector in St. Petersburg shows traces of gradual recovery, and the competitive environment is growing. Two crucial prerequisites of companies' success that comprise all the key factors described in Section 8, were mentioned by all the successful companies interviewed, and they are:

- the ability to survive in a hostile economical and political environment (also see Sub-section 7.1)
- clear vision of the future and development in accordance with good development strategy.

That is why the integrative concept of success in the present economical and political environment is called "survive and develop" in this report. The figure below shows how the key factors of success described in details in the above sections of this report fit into this scheme.



11. Implication of the findings

There are at least four groups that could consider findings of this research in their activities:

- Russian construction managers
- Western construction companies that are active in the construction markets of Russia and CIS
- Political decision makers

- Local and Western trainers providing training services in Russia and CIS

Russian construction managers

Identification of the critical factors of success in the local construction sector and their development in time, views of top managers of successful Russian construction companies about the ways and mechanisms of achieving and developing success, identification of trends and tendencies – these aspects can be the most interesting for managers of the local construction companies.

In view of the fact that during and after the Final Conference that was conducted in St. Petersburg on March 23, 2000, the Russian research team received the great number of requests from construction companies' entrepreneurs to have the research data published fully or partially, it was decided that it should be published (in Russian and in English) in the Internet on the official GASU and StPCP sites.

Western construction companies that are active in the construction markets of Russia and CIS

Features of successful local construction companies identified in this research would hopefully be helpful for the Western contractors in finding partners/subcontractors for the joint local construction projects. Findings of this research also disclose some useful details and peculiarities of the way the business is made in the local construction sector.

Political decision makers

It is worth mentioning that, according to the both official and independent statistical reports and analysis, construction sector is one of the most advanced industrial sectors nowadays in St. Petersburg and in a lot of other regions of Russia. This sector is one of those (together with telecommunications and some others) that have survived the crisis of August 1998 and is expected to develop fast in the near future. Municipal and Federal Governments' role in creating the favorable conditions for construction sector development and for attracting local and foreign investors is decisive. Entrepreneurs of the construction companies under investigation criticized the existing legislation and activities of policy makers both at Federal and municipal levels. The main targets for criticism were:

- tax laws and policy
- existing land laws that do not allow to sell, buy and mortgage land (although there are precedents for allowing those to some extent by municipal governments)
- time and cost consuming procedures of licensing and certification, including licensing of all types of construction works
- lack of experience (and desire) in attracting and managing foreign and local investments into the construction sector

- lack of desire and will to introduce hypothec, though there is a lot of legal schemes having been developed by associations of contractors and other participants in construction sector
- low average level of knowledge (by the municipal government's officials and staff) in market relations, management of projects and investments as well as public relations.

These are the main problems that construction companies would like policy makers to solve in order to facilitate successful construction sector development.

Local and Western trainers providing training services in Russia and CIS

According to this research, most of the companies are in need of management training and retraining of their middle managers. The most frequently mentioned training disciplines, that they experience lack of knowledge and practice in, are as follows: marketing, estimating, tendering, business planning, project management and quality management. Administrative staff of local municipalities also require management training. Most of those kinds of training can only be provided by the Western trainers or local trainers trained in Western management methods and approaches. There is some number of both kinds of training centers in St. Petersburg nowadays, one of which – StPCP – took part in this research. This report can prove to be very helpful to trainers in identifying the training needs of the local construction industry.