

CHAPTER ONE – INTRODUCTION

Sri Lanka is an island nation with a land area of 65,610 square km (sq.km). In 2010, the country had an estimated population of 20.65 million with an annual growth rate of 1 per cent. The country is located south of India and is surrounded by the Bay of Bengal in the North and Indian Ocean in the South and West (ICRA Lanka, 2011).

With the aim of sustaining over 8 per cent GDP growth rate in the next 10 years, the Government of Sri Lanka has laid emphasis on less developed regions, rural livelihood, infrastructure and reconstruction in erstwhile conflict zones as well as tsunami affected areas. Several plans and strategies announced by the Government indicate that the country's construction industry is poised for significant growth because of investments in sectors such as power, roads, ports transportation, housing, tourism and reconstruction (ICRA Lanka 2011).

The Sri Lankan construction industry is expected to grow at a rapid pace in the post-conflict scenario. The end of the island's ethnic conflict in 2009 has revived the economic activity and resulted in a strong focus on infrastructure development. The country's construction industry contributes to about 70 per cent of the Gross Domestic Fixed Capital Formation and about 8 per cent to the country's GDP, with growth since 2003. The industry ranks seventh among the 13 major sectors contributing to the country's GDP.

In 2010, Sri Lanka's construction industry recorded a growth rate of 9.3 per cent as compared to 5.6 per cent in 2009. Its contribution to the GDP was about LKR 423.4 billion, at constant prices. Greater construction activity was also reflected in 12 per cent annual growth of the building material industry. Acceleration of ongoing projects such as for development of power sector including mega projects and road development including expressways, interregional national highways is likely to generate large demand for companies in the construction industry (CBSL, 2010).

In 2010, disbursement of loans increased 39.6 per cent for construction of houses, business premises, other buildings, and property developments. The Sri Lankan construction industry is on an upward trend, due to the post-conflict scenario in the country. The end of the island's ethnic war in 2009 has revived the economic activity and resulted in an infrastructure building boom. Significant reconstruction activities are expected to be undertaken in the North and the East of the country. The other regions of the country are also expected to see significant development activities (Construction Industry Survey, 2011).

In 2010, Sri Lanka's gross domestic product (GDP) growth was 8 per cent as compared to 3.5 per cent in 2009. In the coming decade, the Sri Lankan Government aims to sustain economic growth rate at over 8 per cent. The construction industry occupies an important position in the Sri Lankan economy as in any developing economy (CBSL, 2010).

Various policies and plans of the Government of Sri Lanka indicate that economic growth acceleration focuses on less developed regions, rural livelihood and infrastructure development. Sri Lanka is considered as a developing country which shows a high potential on construction industry after 3 decades of internal conflicts is over. Construction contributes high percentage to GDP growth on a country and it further would help to curb inflation and reduce unemployment in the society.

Sri Lanka's construction industry has, historically, been supported mainly by housing, industrial and physical infrastructure. In the next 10 years, some of the key areas, which are expected to generate significant demand for construction, include power, roads, ports, water supply, sanitation, tourism, housing, and reconstruction of post-conflict and tsunami-affected regions. It has long been recognized that small and micro businesses have a vital role to play in the economy (Stanworth, 1991; Hay and Kamshad, 1994), generating employment, promoting innovation, engendering competition and creating economic wealth.

Druker and White, (1997) stated that, The definition of "construction" used here embraces a wide variety of organizations, including multinationals which have a product division concerned with construction activity and contractors whose main business may be within construction including building, civil engineering, mechanical and electrical services.

1.1 Background of the study

With the introduction of market economy in late 70's then government dominated construction industry become open to capable entrepreneurs who able to become contractors in the country. Few individuals who forecast growth of construction industry and potential of the market invested on forming construction companies in Sri Lanka. However with most of the mega scale construction projects launch like Mahaweli development scheme were handled by large scale international contractors. Local companies slowly emerged as labor suppliers, subcontractors, machinery suppliers and service providers later became larger construction companies in Sri Lanka. Few examples of them are ICC, Maga, Sanken Lanka, Thudawa, KDAW, SIERA who are leading in the industry as professional construction companies.

However after the initial construction boom subside the industries became highly competitive as a result of internal conflicts and low investment in infrastructure development in the country. The tendency to enter small scale contractors become a challenge as a result of the slow growth rate of the industry during internal conflict.

Kululanga, (2012) stated that, the state should play three roles in developing the construction industry, namely: (1) as a major client; (2) a provider to a general business environment; and (3) as a stimulant for a specific construction business environment. The general business environment if not enhanced will only perpetuate under development of the industry. Therefore, the enabling business environment represents the broad context within which the business climate becomes conducive for cartelizing capacity building of companies. For example, poorly conceived policies, an unstable political environment and high levels of corruption can result into a highly disabling environment with significant negative consequences.

Five competitive forces proposed by Porter (1980) cited by Budayan et.al, (2013) in the construction industry are considered, differentiation strategy can be considered as an effective strategy to impede these competitive forces and influence them in its favor, which in turn, creating and sustaining competitive advantage for the construction industry.

1.2 Small and Medium Scale Enterprises (SME)

There is no internationally agreed definition of Small and Medium sized Enterprises (National Strategy for Small & Medium Industries Development in Sri Lanka, 2002; OECD, 2009). The Small- and Medium-scale Enterprises (SME) plays a vital role in the developing economies by contributing to the national economic output and employment generation and is considered as engines for economic growth and development (Thiruchelvam et.al, 2003; Singh et.al, 2010). At present there is no clear definition of SMEs. This position has created confusion in identifying the SMEs for various programs; it also creates implementation problems for the national policy (SME Draft Policy, NEDA – 2009).

In Sri Lanka, the definition of the SME depends on following three variables namely number of full time employees or production turnover or total asset value. The industries categorized as fixed assets values not exceeding Rs. 20 million small industries and Rs. 50 million for medium industries. At the lowest end the small industry asset value identified as Rs. 1 million. The SMEs account for 80 percent to 90 percent of the total number of enterprises in Sri Lanka and contribute 30 percent in terms of value added and account for 32.7 percent of the employment from Agricultural sector, 26.3 percent of the employment from Industrial sector 41.0 percent of the employment from Services sector. Also 75 percent of SMEs are located outside the relatively prosperous Western Province (SME White Paper 2002).

One of the important SME strategies is to create an enabling business environment. This broadly covers access to finance, technology, regulatory framework, access to information and consultation, access to markets, business development services, industrial relations and labor, linkage formation and environment issues (SME White Paper 2002).

1.3 Problems encounter on small scale contactors development

The ICTAD classification of construction contractors are mainly on their financial capability on grading concerned. However there are contractors who are capable and managed by industry professionals be able to manage even large scale construction are facing sever burdens mainly in finance, quality and skills of employees.

1.4 Problem Justification

The above difficulties would restrict small scale contractors to grow up to middle scale and bridge the gap between large scale and small scale both are necessary to maintain sustainable construction growth of the country. Large scale projects which are undertaken by larger construction companies unable to find specialized sub-contractors who are capable of handling specialized work scopes. Therefore there is a gap between small scale constructor's capability and requirement of the construction field. The large scale contractors cannot fill this gap because of the following problems encounter in the small scale industry.

Since the majority of indigenous construction companies are small, lack capacity, vision and capital, these problems tend to be exacerbated by the volatile environment in which they operate. Hence, they may face a difficult growth path because they and their business environment are both underdeveloped. Given an opportunity, they can probably overcome their inadequacies, but they cannot change their environment.

The most convincing reason for providing a specific business environment to construction industry stems from the view that the business behavior, practices, products, structure of the organizations in the industry, low capital requirement for entry and high labor intensive make the industry unique from other industries. This is the reason that several countries have established formal national construction industry councils to facilitate interventions for construction industry development on behalf of the state. Therefore, the state as a provider of a specific construction industry environment should provide specific laws and regulations on one hand, and the necessary structures and institutions for enhancing capacity building such as incentives and a variety of controls. Accordingly the research question is defined as "what are the existing situations of competitive construction industry in Sri Lanka? and what are the barriers to enter and survive in competitive construction industry in Sri Lanka?"

1.5 Objective of the study

1. To find out existing situation to enter and survive competitive construction industry in Sri Lanka
2. To find out barriers affecting to enter and survive competitive construction industry in Sri Lanka
3. To propose a suitable policy implication to enter and survive competitive construction industry in Sri Lanka

1.6 Problem justification

Budayan et.al, (2013) stated that, based on a literature review, nine corporate management activities, which can affect the achievement of competitive advantage, was determined as the drivers of the differentiation strategy. These activities are strategic planning, business development, financial management, professional management, organizational learning, research and development, tendering, knowledge management, and marketing.

Encourage small scale contractors to pay more serious attention on the use of expertise of relevant professionals to develop companies in to stronger ventures. Highlight the importance of sustainable development of the construction industry which is a drive of any economy to enhance the confidence of investors subsequently create opportunities for potential contractors. Having identification of the problem encountered by the small scale contractors the study will be provided frame work to attract professionals and develop trust on small scale contractors that they have clear future if they manage themselves to match the market demand.

1.7 Significance of the research

Okpara and Wynn (2007) cited by Gill and Biger (2012) identified several factors that are responsible for small business failure in Nigeria: lack of financial support, lack of management experience; corruption, lack of infrastructure, lack of training, and inadequate bookkeeping and recordkeeping.

The importance of studying this research is to provide a benefit to the SME in construction industry. Also identify the possibility of new methodology for the betterment of the SME sector in construction study of focus theme. Government of Sri Lanka, ICTAD, construction companies, Universities and other likeminded institutions will also be benefited in this.

1.8 Limitation of the study

This study is limited to the Western Province which had a direct impact in both private and public development and research will focus only on analyzing the barriers of survival of small and medium scale construction. Implementation of policy for this sector will be taken as the applications compared to the current methods relatively modernize strategy for betterment of the industry.

At present ICTAD has taken the initiative providing guidelines for this sector and improve the industry norms. As such there is no national policy for this sector. By this research a uniform and equitable single policy for the entire sector could be developed to overcome the above stated issues.

1.9 Organization and Preview of the Thesis

This study report comprises six thematic chapters. Firstly this study report provided an introduction about the study which provides consensus for the survival of the small construction industry, focus, limitations along with other relevance and information. Secondly the report focused on the literature available. The literature were reviewed and gathered from Books, Journals, Articles, Research Reports and Websites. Thirdly the report revealed the case study areas with maximum possible information available and Research design followed thereafter. Analysis and conclusion arrived subsequently through fifth and sixth places. Citations and references have quoted where necessary to provide due respect to the Authors and Publishes.