

**SMALL FAMILY-OWNED CONSTRUCTION COMPANIES IN COLOMBIA:  
A BUSINESS STRATEGY**

by

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c Jaime A. Benitez

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**ABSTRACT**

The purpose of this thesis is to develop a business strategy for a small family-owned construction company, in the city of Bogota, Colombia. To do so, the market is analyzed in terms of price ranges, neighborhoods, and types of construction. The company is defined within this broad market; then the different forces that drive the subindustry, apartment buildings, are analyzed. In order to determine the actual capabilities of the company, its value chain, market share, present strategy, organizational structure, and culture are investigated.

Within this framework, a strategy proposal for future growth and continued profitability is discussed.

Thesis Supervisor: Professor Fred Moavenzadeh  
Title: Director, Center for Construction  
Research and Education

TO MOKINA AND MY PARENTS

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## INTRODUCTION

Construction is one of the industries that is most affected by economic cycles. In several countries the welfare of the construction industry parallels national economic welfare. Thus, economic change is one of the most important factor affecting the business strategy of a company.

In Colombia this is especially true, and the effect that Colombia's economy has on the strategy of small companies will be analyzed in this paper. Family-owned companies can be very successful in the Colombian economic environment; when this happens, they need to determine the best way to employ their capital and profits. Some builders believe that growth is the strategy to pursue, while others think that diversification or investment in other industries is more appropriate.

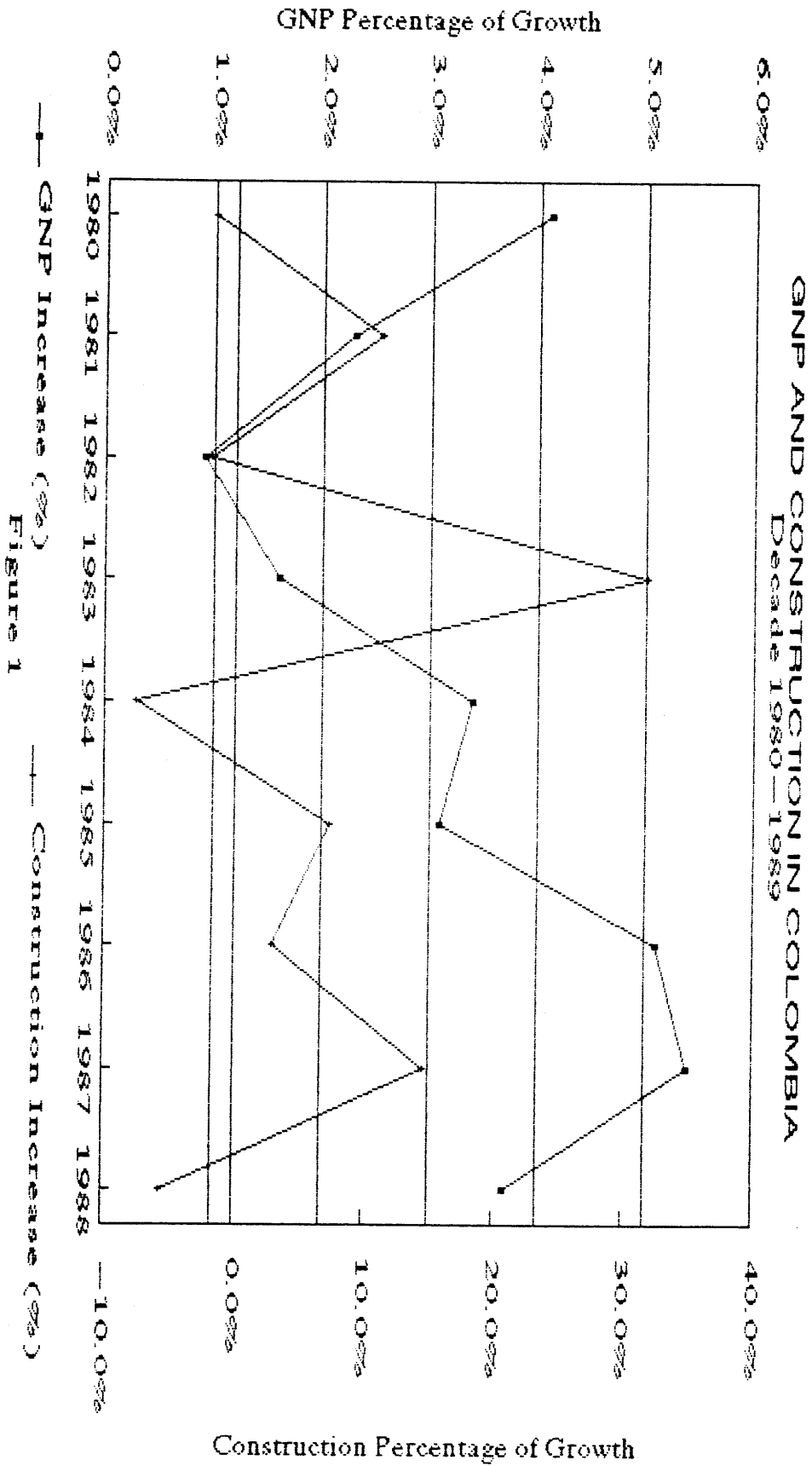
It is difficult to know which is the best strategy. However, a number of studies of family-owned corporations have been made by professors and graduate students at several business schools and by consultants in various management consulting firms. These prior studies are extremely helpful in defining and proposing a strategy for a family-owned construction companies.

## BACKGROUND

The following is a summary of the Colombian environment and the construction industry. It is followed by an analysis of the housing construction segment in the city of Bogota. With this background it will be easier to understand the circumstances in which a specific company has to work in.

**The Industry and Colombian Economy.** Construction has been considered by the Colombian government as a leader industry. The demands that construction places on other national industries is a multiplier for the growth of the whole economy. Construction itself represented a 6.2% of the gross national product in 1989 (2.15 billion dollars from a total GNP of 34.7 billion dollars). During the past four years percentage increases of GNP and construction had exhibited proportional changes (Figure 1).

Construction employs, directly or indirectly, 30% of the labor force in the country. 5,100,000 people are related to the construction industry or its suppliers. As a result, the welfare of this industry is politically important to the government. In 1989 national unemployment decreased to approximately 8.5%. Construction contributed to this



Construction Percentage of Growth

decrease by creating 415,000 new jobs.

Recessions in a labor-intensive industry, such as construction, have been linked historically with very high unemployment rates. This trend has begun to change because of the diversification of industries and the industrialization of construction. As a result the average construction worker is earning a better than minimum wage. However, even as this trend occurs, most construction in Colombia remains based on concrete structures and masonry walls, which will always be very labor-intensive activities.

**Industry Segmentation.** The construction industry in Colombia is divided into public and private construction (14.5% and 85.5% share of the total, respectively)<sup>1</sup>. Unlike the segmentation of the industry in other countries, private construction includes a big quota of housing built by the government. It is the author's belief that this segmentation is more accurate because it allows analyzing the government as a competitor of the private builder. An analysis of the construction industry, based on this pattern of segmentation, is contained in this chapter.

**Public Construction.** This segment of the industry consists

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<sup>1</sup> Public or private construction is defined statistically by the use of the building and not the proprietorship.



of the builders of infrastructure facilities (roads, aqueducts, sewers, dams, etc.) and of public buildings owned by the different levels of the government (Nation, State, or Municipality). The share of only 14.5% of the total construction industry is low compared with other developing countries where it ranges from 30% to 50%.

In Colombia, all the public services are owned by one or another of the government levels, who are responsible for their construction and operation. For most of the towns these services have become burdensome and very hard to manage; thus, a trend has evolved to change the policy of government ownership and turn public services over to the private sector. Several studies are currently being conducted this issue. It is expected that a private operator will make these services more efficient; however, in order to be profitable, prices will have to be increased in order to upgrade technology. Under these circumstances, it can be expected that the demand for the construction of public facilities will increase.

The construction of public projects is performed by Colombian companies, foreign companies, or a combination of the two. But for most of the big projects which demand highly experienced constructors, Colombian firms are bypassed and deprived of the opportunity to get the required practice (CAMACOL, 1990). This situation does not occur in the construction of roads where Colombian companies have the

experience in mountainous and rainy conditions which are characteristics of the most heavily populated regions of the country. These characteristics, which serve as an entry barrier for outsiders, have also created the need for expertise in geotechnical support of slopes and in permanent road maintenance.

Funding for public construction projects comes from international loans, taxes, and the income from international trade. In rural areas where coffee is a major product, the National Coffeegrowers Federation lends or builds roads and aqueducts. A tax that has been widely used in urban areas is called "valorization" and it charges those properties that are favored and whose values are increased by the existence of the project. This financing innovation has been responsible for the growth of this sector and for most of the decrease in unemployment.

Unfortunately, recent history has revealed that public constructors suffer from financial problems. The Superintendency of Societies has warned these contractors that their debt-to-equity ratios have increased to uncontrollable levels (El Espectador, 1989). In 1989 the Pinsky firm declared itself in bankruptcy, leaving several bridges and other structures half built. Bruges, another firm, fell into bankruptcy several years ago, even though it held a large number of accounts receivable from the government. Another problem has been the lack of interest

of Colombian contracting and consulting firms in working outside the country.

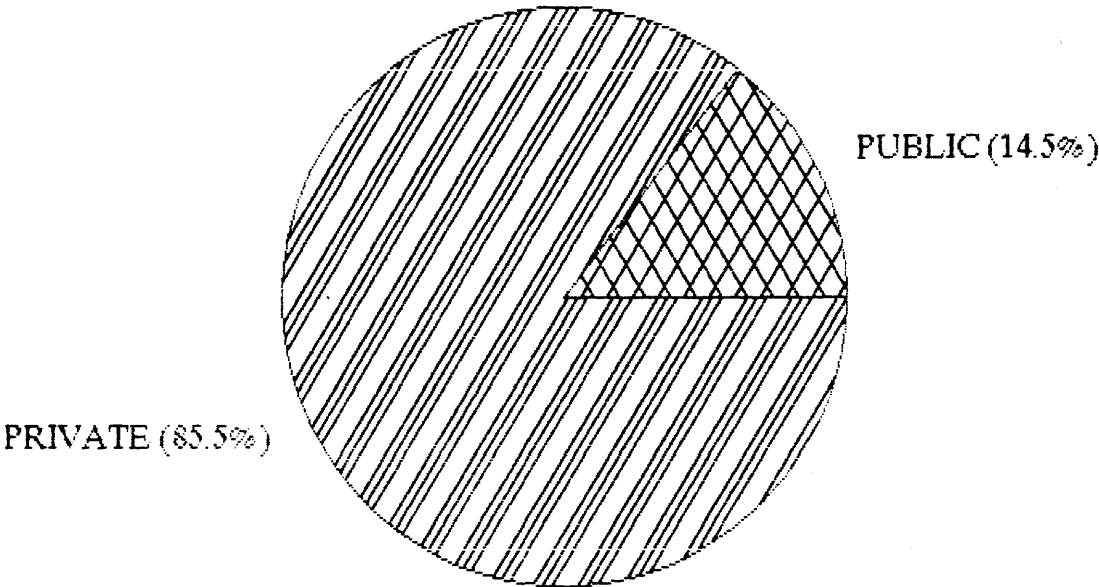
**Private Construction.** Housing is the most important segment of private construction in Bogota, with 79.0% share of the market. It is followed by commercial buildings with 9.6%, office buildings with 4.9%, warehouses with 3.5%, industrial buildings with 1.6%, and finally hotels, educational, and religious buildings with the remaining 1.4% (Figure 2).

The amount of square meters built during the last three years in the twelve most important cities is given in Table 1. Even though these numbers show a decrease in physical construction volume, other numbers indicate that the industry is not in bad shape. These numbers are the increase in jobs mentioned before and the amount of money invested in the industry. In 1989, 900 million dollars were placed in the housing industry; 300 million came from the buyers and builders and 600 million came from the financial system, indicating a real increase of 32% over the prior year (El Tiempo, 1990).

Housing itself is divided into individual family houses and multifamily projects. The latter consists of groups of houses and low-rise and high-rise apartment buildings.

This housing does not include the informal sector which is made up of remodelled structures and housing constructed without permits in suburbs or in rural areas. Informal

TOTAL CONSTRUCTION INDUSTRY DISTRIBUTION



PRIVATE CONSTRUCTION INDUSTRY DISTRIBUTION

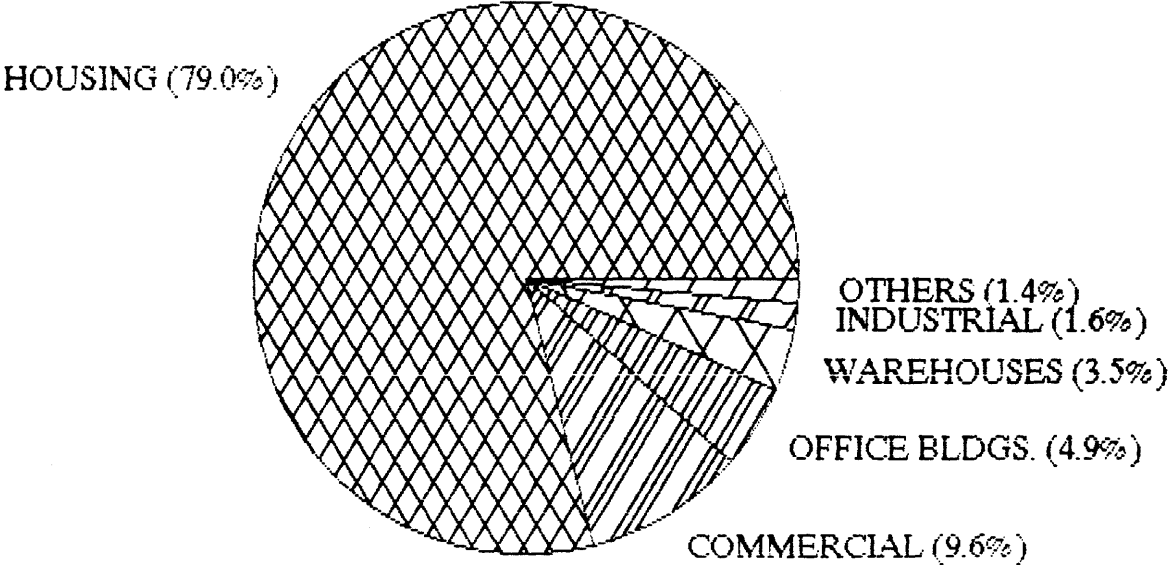


Figure 2  
12

BUILDING ACTIVITY DURING 1987, 1988, AND 1989  
(square meters)

CITY	1987	1988	increase	1989	increase
Armenia	68,020	116,515	71.30%	99,480	-14.62%
Barranquilla	199,708	148,958	-25.41%	251,376	68.76%
Bogota	3,918,919	3,457,714	-11.77%	3,270,676	-5.41%
Bucaramanga	331,315	325,052	-1.89%	354,846	9.17%
Cali	1,106,265	1,144,892	3.49%	1,126,046	-1.65%
Cartagena	277,230	230,025	-17.03%	305,262	32.71%
Cucuta	143,374	120,932	-15.65%	88,453	-26.86%
Ibague	112,914	121,510	7.61%	173,193	42.53%
Manizales	108,486	92,843	-14.42%	191,691	106.47%
Medellin	1,905,687	1,977,149	3.75%	1,230,827	-37.75%
Pasto	156,260	148,005	-5.28%	57,649	-61.05%
Pereira	276,064	239,163	-13.37%	304,843	27.46%
TOTAL	8,604,242	8,122,758	-5.60%	7,454,342	-8.23%

Note: These twelve cities are 90% of the nation's total construction.

Source: CAMACOL's report, Jan. 26, 1990.

Table 1

sector activities are not included in the accounting of municipalities, banks, or chambers of construction. Rough estimates indicate that an additional 40% of construction could be added to housing if there were a way to measure the informal sector.

Depending on its size, each town may have several different authorities that act upon the builder to regulate formal construction. Permission from City Planning is usually required in order to proceed with any construction. If the project involves urbanization, a permit from the local Secretary of Public Works is also required.

For the real estate process, an authorization from the Municipality or from the Banking Superintendency is necessary. The latter entity protects the buyer and the banking system from fraudulent construction. Its authority is feared more than the others since it can lead to a withholding of credit for the construction company or for its partners in any other industry. The Banking Superintendency is a national authority which has 5,000 construction firms registered. Unfortunately, the specialized contractors, the subcontractors, and "informal" builders do not appear on these records.

Another important entity is the National Chamber of Construction, CAMACOL, which represents the builders as an industry. Affiliation with the chamber is not mandatory, therefore the number of registered builders does not reflect

the exact number of firms in the construction industry.

Different from other countries, no specific requirement are imposed by the Fire Department or other authorities. No occupancy permit is required and sometimes buildings are never even visited by any local authority. However, the builder tries to stay within the law because of possible sanctions.

In addition, a law of 1989 requires a stability insurance bought by the builder, with the buyer as beneficiary. The insurance protects the buyer of a new house during a period of two years for any quality problem the house may have, and for a period of three years for any problem of stability. If any of these conditions occurs the buyer can make a claim to the insurance company, which is obliged to pay for the amount of the damages. The insurance company may take legal action towards the responsible of the sinister. The whole process assures a shorter repayment of the damages to the owner of the house than a normal sue against the builder. It also coerces the builder to do the needed repairs; else he would have to deal with a better structured legal system: the insurance company. To assure its enforcement, every notary that legalizes a sale of a house must demand a copy of the policy.

The only technical requirement that must be met is the Antiseismic Code, which defines a city's risk in case of an earthquake. And while there are no codes for foundations,

elevators, or any other mechanical device, designers take the American or European codes as guides. With respect to plumbing, sewage, and electricity, the local public service companies establish the requirements and impose their authority.

**Housing Supply and Demand.** As has already been stated, construction in Colombia is a cyclical business that depends on the welfare of the national economy. The duration of the cycles can be considered short in relation with the time the building projects can last. Periods of construction prosperity, like 1978-1980 ("Colombian Coffee Bonanza"), 1982-1985, and 1986-1987, coincide with high levels of Colombian exports. The cycles also correspond with changes in government policies and changes in the governments themselves. (Elections were being held in 1978, 1982, and 1986, coinciding with the beginning of prosperous periods.)

Even though the census is the primary basis for predicting housing demand, in Colombia it is barely used. Not only are the intervals between the census too great, but there is much mistrust of their accuracy. For example, the last census of 1985 reported results well below the predictions of population growth. Some consider that the census was very badly done, while others say that population growth rates have really decreased.

Even though construction demand generally follows the



above cycles, it can be different for different cities. Secondary cities, with populations of 500,000 to 1,500,000, have recently shown relatively greater population increases than have the two biggest cities, Bogota and Medellin. Migrants have shown a preference for these cities that, unlike some time ago, now have good services and transportation systems. A survey made by CAMACOL has given the effective demand for housing in the most important cities (Table 2).

During 1989 the housing construction demand in Bogota performed differently for different social classes. (Supply and demand for this city is found in Table 3 and Figure 3) The upper-middle income and high-income groups found a saturated market for the first time in the history of Bogota. This occurred because of the low entry barrier to the construction industry. Anybody (businessmen, medical doctors, lawyers) with some savings decided that construction offered a lucrative investment opportunity. 1987's show of high profitability is an example of how "high temporary profits in a cyclical industry are frequently misread as a long-term opportunity" (Porter, 1985), thus attracting many entrants. Also, savings institutions had excess reserves that they wanted to invest in construction and therefore encouraged construction borrowing.

The excess in housing supply is seen in development areas where new buildings finished in 1988 are still being sold.

EFFECTIVE DEMAND OF HOUSING IN CITIES WITH 500,000 PEOPLE OR MORE, 1989  
(Number of Families)

HOUSE PRICES		BOGOTA		CALI		CARTAGENA		TOTAL
UPAC	US \$	MEDELLIN	B/QUILLA	MEDELLIN	B/QUILLA	MEDELLIN	B/QUILLA	
1 - 700	5 - 3,558	5,190	10,938	9,129	5,455	1,680		32,392
701 - 1,000	3,563 - 5,083	4,932	4,687	2,808	5,134	1,680		19,241
1,001 - 1,500	5,088 - 7,625	8,298	2,787	2,107	2,187	2,671		18,050
1,501 - 2,000	7,630 - 10,167	8,088	8,740	2,956	854	2,671		23,309
2,001 - 2,500	10,172 - 12,708	4,632	4,302	5,454	440	5,039		19,867
2,501 - 3,000	12,713 - 15,250	7,042	4,904	1,658	434	2,015		16,053
3,001 - 3,500	15,255 - 17,792	4,416	3,481	1,403	272	1,506		11,078
3,501 - 4,000	17,797 - 20,333	2,492	2,085	386	208	891		6,062
4,001 - 5,000	20,338 - 25,417	2,036	3,456	318	156	491		6,457
5,001 - 6,000	25,422 - 30,500	1,397	1,974	409	296	37		4,113
6,001 - 8,000	30,505 - 40,667	1,422	2,462	394	264			4,542
8,001 - 10,000	40,672 - 50,833	919	1,250	351	128			2,648
10,001 - 20,000	50,838 - 101,667	999	1,668	602	256			3,525
TOTAL		51,863	52,734	27,975	16,084	18,681		167,337

Source: CAMACDL

Table 2

HOUSING SUPPLY AND DEMAND IN BOGOTA

October 1989

HOUSE PRICES		TOTAL SUPPLY		EFFECTIVE DEMAND		UNSATISFIED DEMAND	
UPAC	US \$	Units	%	Units	%	Units	%
1 - 1,000	5 - 5,083	0	0.0	10,122	19.5	10,122	28.2
1,001 - 1,500	5,088 - 7,625	216	1.3	8,298	16.0	8,082	22.5
1,501 - 2,000	7,630 - 10,167	1,233	7.7	8,088	15.6	6,855	19.1
2,001 - 2,500	10,172 - 12,708	945	5.9	4,632	8.9	3,687	10.3
2,501 - 3,000	12,713 - 15,250	1,275	8.0	7,042	13.6	5,767	16.1
3,001 - 3,500	15,255 - 17,792	991	6.2	4,416	8.5	3,425	9.6
3,501 - 4,000	17,797 - 20,333	936	5.8	2,492	4.8	1,556	4.3
4,001 - 5,000	20,338 - 25,417	1,837	11.5	2,036	3.9	199	0.6
	SUBTOTAL	7,433	46.4	47,126	90.8	39,693	110.7
5,001 -higher	25,422 - higher	8,570	53.6	4,801	9.2	(3,769)	-10.5
	TOTAL	16,003	100	51,927	100	35,924	100

Source: CAMACOL Cundinamarca

Table 3

### HOUSING SUPPLY AND DEMAND IN BOGOTA

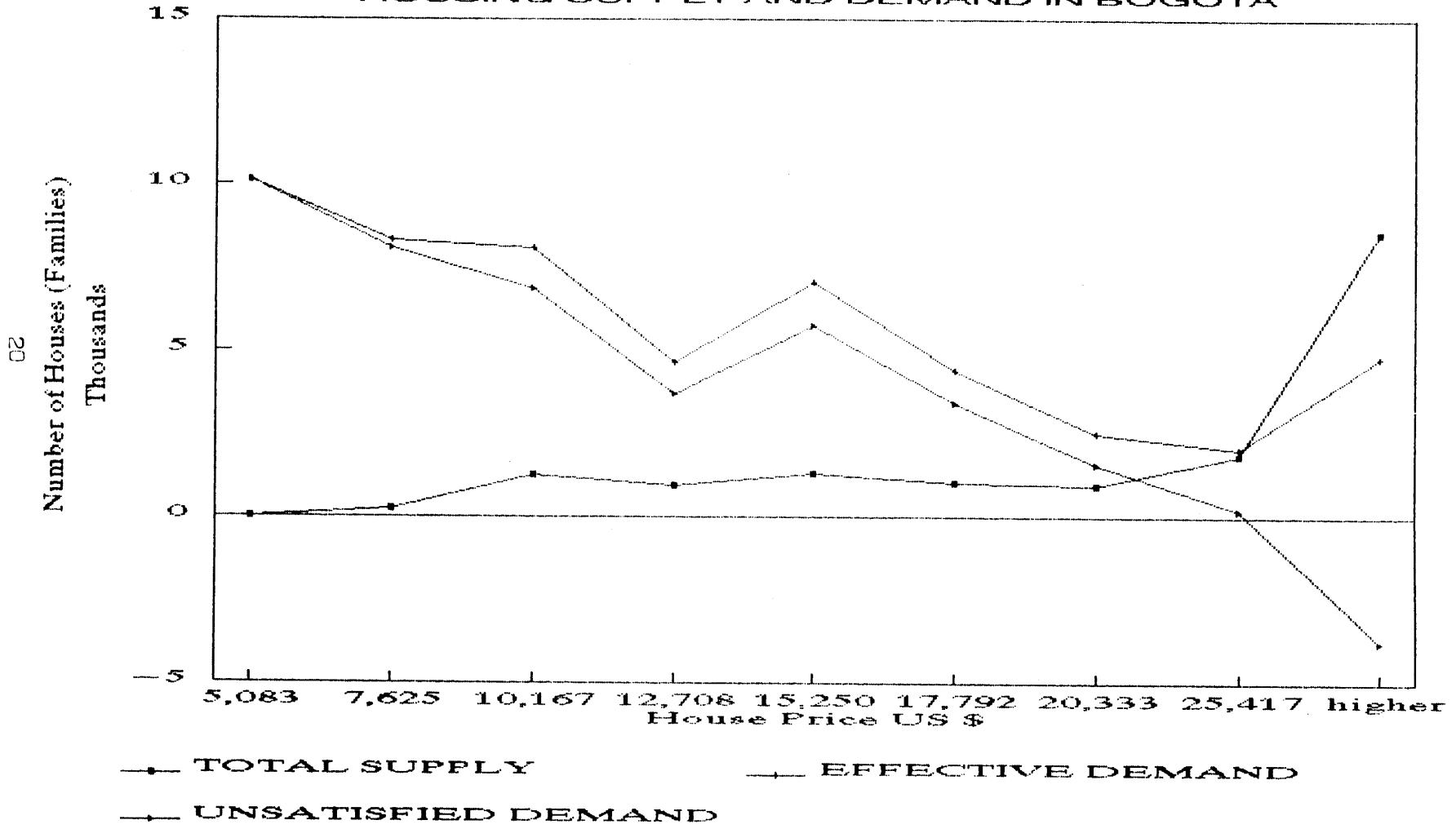


Figure 3

In addition, realtors are complaining of the slow movement of the housing market and the lack of profitability of rental housing. In 1989 the number of construction licenses given by the authorities in Colombia was reduced by 9.33% (for Bogota the decrease was 7.38%) (El Tiempo, 1989).

At the same time the ability of lower-income groups to pay for housing was being reduced by the very system that was invented to make housing available to the national population in the first place. The loans provided by this system had rising rates that were not followed by the incomes of lower-income employees. In fact, in 1989 pesos, the total income of an average family had fallen 9.1%, from US \$327/month in 1981, to US \$297/month in 1989. (EL Tiempo, 1989). This drop in average income should be viewed with caution because of the decrease of the average family size during the same period; some say that the real income per capita during the "Lost Decade" for Latin Americans was reduced by 0.1%. Nevertheless, a shortage of 50,000 houses has been estimated for the low-income class.

**Housing Finance.** Housing construction finance is provided by the special banking system described below. For some low-income projects, finance is provided by government institutes. These include: the Institute of Territorial Credit (Instituto de Credito Territorial - ICT); Central Mortgage Bank (Banco Central Hipotecario - BCH); The

National Saving Fund (Fondo Nacional del Ahorro); the Military and Popular Especial District Housing Funds (Caja de Vivienda Militar and Caja de Vivienda Popular del Distrito Especial); and several others.

A law which created a savings and loans system with a new unit of constant buying power (UPAC) was enacted in 1972. The system attracted most of the savings of the nation to institutions which although similar to banks, were able to offer higher interest rates. These institutions, Corporations of Savings and Housing, were charged with stimulating the industrial sector by giving loans, especially to the construction industry. The overall intent was to reduce unemployment, create housing, and circulate large amounts of savings that people were not investing.

The lending procedures of these corporations are different from other countries; the same lender provides loans to the builder and to the final buyer. After the property has been sold, the builder, with the approval of the corporation, transfers the credit to the buyer.

The national government has controlled these corporations very closely and has established minimum percentages of total loan funds going to loans for houses in different price ranges (Appendix A). When they are not able to reach these minimums they are obliged to acquire Titles of Constant Value from the Fund of Savings and Housing (Fondo de Ahorro y Vivienda - FAVI) for the amount they have not

been able to lend. These titles only gain the monetary correction, an approximate of the inflation established by the Monetary Board.

Some politicians blame UPAC for the high inflation rates, but others consider it the source of industrial growth. To continue or suspend the UPAC is always an issue for politicians during elections. However, a special poll is needed to determine if it is an issue to the average citizen. The most probable future president of Colombia for the 1990-1994 period, Dr. Gaviria, seems to be a supporter of UPAC; unfortunately, he has not announced his precise position on this issue.

In January 1989 an Urban Reform Law was enacted. One of its purposes is to get special sites (easily-accessible lots that are being left without use until their value is increased) to the construction market. On those sites, housing for low-income people can be constructed without the additional cost of infrastructure facilities. Another purpose of the reform law is to create a low-interest-rates lending system for buyers. The Savings and Housing Corporations are forbidden to give mortgages in UPACs for houses priced below 120 months of minimum wages. Unfortunately, until now, 1990, the corporations had no method of financing themselves to give the subsidized loans. Therefore, their resources assigned to low-income loans are being sent to the FAVI or to the BCH, which uses them for

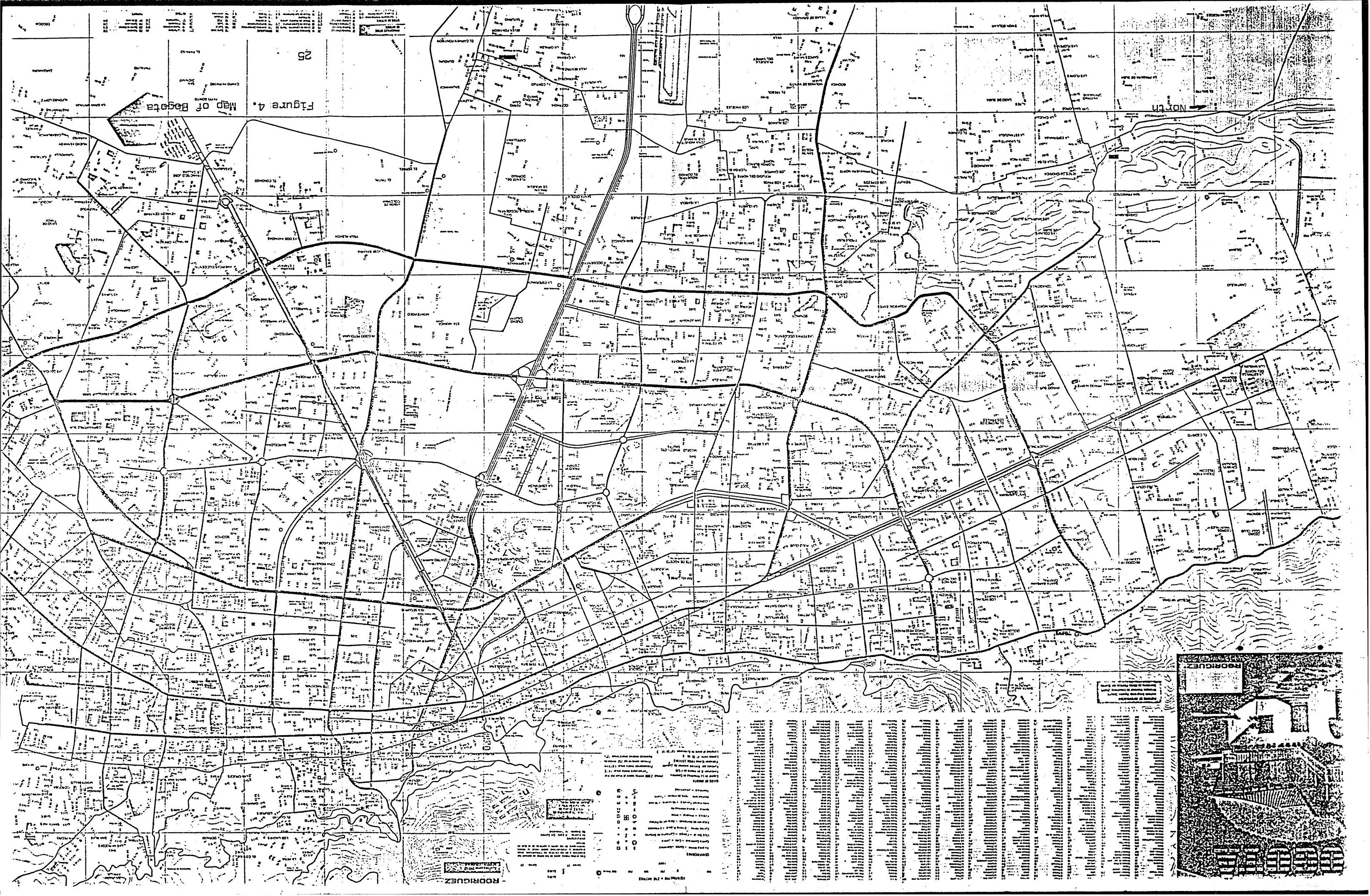
loans on UPACs for the same income level.

**Construction in Bogota.** The only physical barrier to Bogota's future growth are the mountains at the east of the plateau where the city is located (Figure 4). The public service companies have established another limit, Bogota river, beyond which they do not serve. Within these limits the amount of land to develop is still very large, but development has centered along the most important roads.

Geographical construction markets in the city of Bogota are defined by levels of income. Most of the neighborhoods at the north end of the city are high income communities. Studies made by the Colombian Chamber of Construction (CAMACOL), northern Bogota contains 74% of the construction in the city. This area also includes some highly active middle and middle-low urban developments. This geographic area is the construction market focus for the remainder of this strategy development study.

The lack of an efficient public transport system has increased the demand for housing projects near downtown and in the eastern hills. This has caused a problem of overdensification and high cost of land in these areas. The most northern zone of Bogota, beyond 134th street, became an area of high development. As a result of this development, over the past two years the neighborhood traffic has become terribly congested. Moreover, this zone of the city was the





Map of Bogotá  
Figure 4

NORTH

RODRIGUEZ

Scale: 1:50,000  
Date: 1960  
Author: Rodriguez

**LEGEND**

1. Major Road (Double line)

2. Minor Road (Single line)

3. Railway (Line with cross-ticks)

4. Canal (Line with short dashes)

5. Contour Line (Line with elevation numbers)

6. Building (Small rectangle)

7. Park (Area with wavy lines)

8. Water (Area with wavy lines)

9. Airport (Large rectangle with runways)

10. Stadium (Large rectangle with internal lines)

11. School (Small rectangle with 'S')

12. Church (Small rectangle with cross)

13. Public Square (Large open area)

14. Industrial Area (Area with small rectangles)

15. Residential Area (Area with small squares)

16. Commercial Area (Area with small rectangles)

17. Government Building (Large rectangle with flag)

18. Embassy (Large rectangle with flag)

19. Consulate (Large rectangle with flag)

20. Bank (Small rectangle with 'B')

21. Post Office (Small rectangle with 'P')

22. Police Station (Small rectangle with 'P')

23. Fire Station (Small rectangle with 'F')

24. Hospital (Small rectangle with 'H')

25. School (Small rectangle with 'S')

26. Church (Small rectangle with cross)

27. Public Square (Large open area)

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29. Residential Area (Area with small squares)

30. Commercial Area (Area with small rectangles)

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82. Church (Small rectangle with cross)

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84. Industrial Area (Area with small rectangles)

85. Residential Area (Area with small squares)

86. Commercial Area (Area with small rectangles)

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94. Hospital (Small rectangle with 'H')

95. School (Small rectangle with 'S')

96. Church (Small rectangle with cross)

97. Public Square (Large open area)

98. Industrial Area (Area with small rectangles)

99. Residential Area (Area with small squares)

100. Commercial Area (Area with small rectangles)



first to exhibit an excess of housing supply two years ago.

In the mid-northern zone there are some lots available. In addition, large houses are being torn down and replaced by apartment buildings. The City Planning authority has changed the density codes for this area, resulting in a population which is too large for existing street capacity. This zone is described in greater detail in the next chapter.

An alternative area for the same income level housing is the land in the mountains on the northeast. Even though very steep, this area has become a very popular sector because of the view over the city. Fortunately, the claims of the water supply company and ecologists have been heard, and the construction permits on this area have been restricted.

The northwest part of the city is a very actively developing sector. The biggest housing projects are located in this area and are designed mostly for the middle-income class. As the projects move further west, the income level of residents is lower. Several of the projects are of a thousand houses or more and are being built by the largest construction firms in the city.

In the downtown section, only a few major housing projects have been built in the past two years. Even though the downtown is a highly dense area, it contains primarily private and public office buildings.

Southwest Bogota is the most actively developing sector for middle-low and low income families. It is also the most dense industrial zone. Though it is easy to develop, it also has the traffic congestion problems characteristic of the most northern part of Bogota.

Families of lowest income live in southeast Bogota, an area with the greatest need for infrastructure facilities. Several of its neighborhoods have been developed without authorization of City Planning or of the public services companies.

## B. L.

B.L. is the family-owned construction company center of this study. This chapter explains how B.L. fits in the environment explained in the previous one.

**History of B.L.** B.L. & Co. was established in 1976 as a family partnership. The senior partners, the parents, were given all responsibility on decisions; the junior partners, the son and daughters, could participate in those decisions, but without the right to vote. (How the family affects or is affected by market segmentation, organization, capital, technology, and "value chain" is explained in the chapter **Family-Owned Companies' Culture.**)

B.L. has built an average of one project per year since 1976. Its growth is shown by the size of the projects. The first one included 12 apartment houses with a total area of 23,250 sq.ft.; in 1981, 28 units were built with an area of 42,200 sq.ft.; and by the end of 1988, B.L. was completing 51 apartments in a building of 78,000 sq.ft.

**Market Segmentation.** B.L. has focused on the upper-middle and high income housing markets in Bogota. Except for a group of two-story houses, all the buildings are located

within an area of 20 blocks. These urban area projects have all been developed by the same land developer.

The company offers this market a personalized service that is different from that of most other builders. After seeing the apartment, a client can do business directly with the owner of the company. In this manner, clients feel that their need to negotiate amounts and schedule of payments is being satisfied.

Buyers for this type of construction do not conform to a single prototype. Some may be price-sensitive while others are quality-sensitive; and what one might like another may find unpleasant. The designs of B.L.'s buildings are especially successful because they are adaptable to a wide range of individual needs, ranging from bachelor owners to large families. B.L. manages to meet these needs while maintaining the proper ratio of one-bedroom, two-bedroom, or three-bedroom apartments in each building.

**Organization.** The company has a flexible organization structure in which operations, purchasing, sales, and administrative divisions are under the direct authority of the President (see Figure 5). The President is also the head of the purchasing and sales departments where he receives help from members of the technical and administrative staff. Although the organization is meant to be functional, the small size of the company requires that

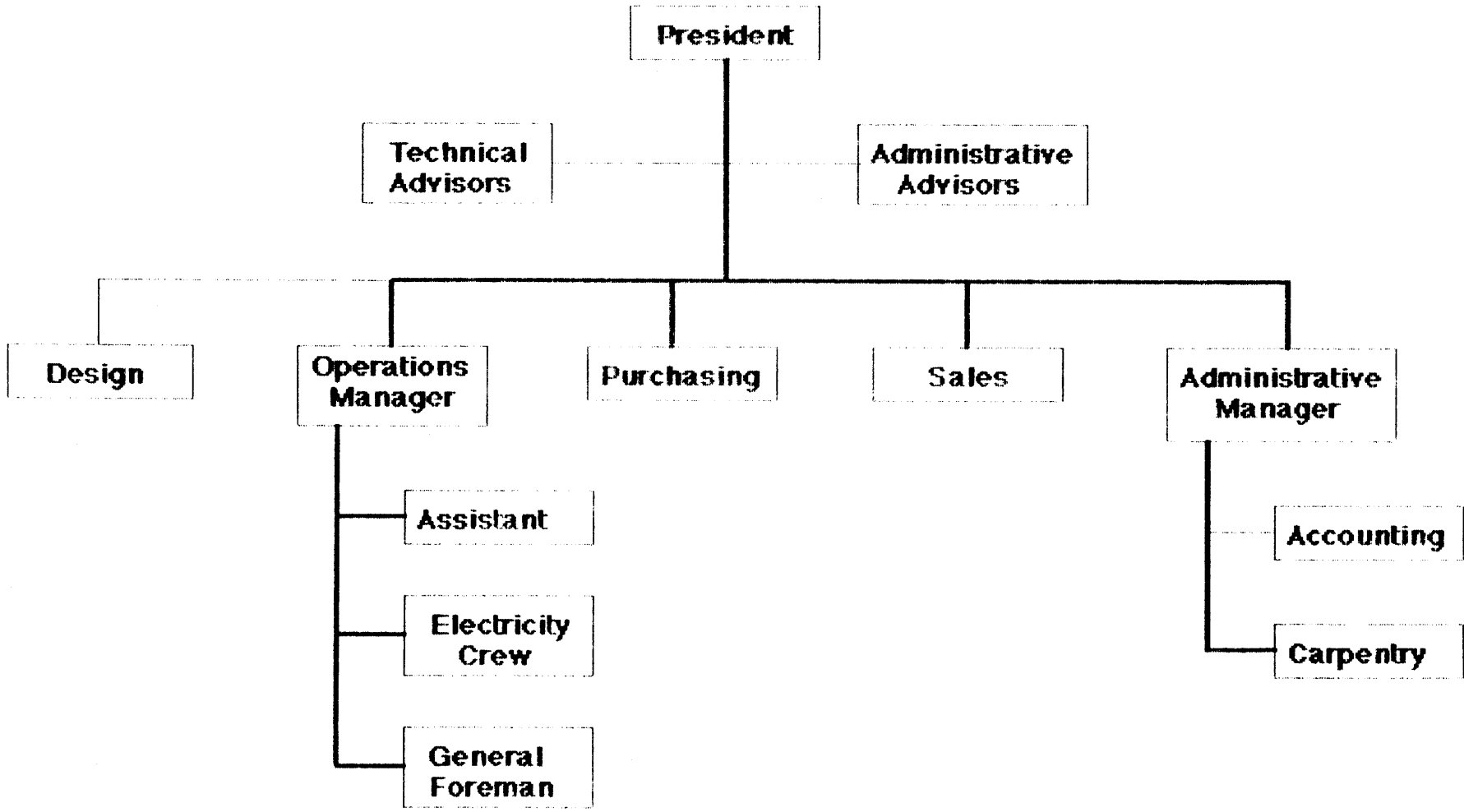


Figure 5: Organization of B.L.

everyone be willing to work in various areas as needed. Since projects are done one at a time, the whole organization is able to focus on the successful completion of the specific project currently undergoing.

The design function is linked to the organization according to the construction to be executed; sometimes the architect becomes a member of the company, while at other times the complete architectural design effort is done under contract. The need for better designed buildings has led to the hiring of higher quality architects.

The Operations Manager supervises a crew that varies widely, depending upon the job; the crew may consist of one assistant or a staff of 50, including foreman, journeymen, and apprentices. Also there is likely to be an electricity crew, since company experience is that when electrical work is subcontracted, it is very difficult to get personnel for overtime work or for short periods when just a few men are needed, such as at the very beginning and very end of a project.

All the construction site employees work under contracts defined as "until-the-end-of-the-job"; this means they are not on a permanent payroll. Even though they go to work on other construction sites when B.L.'s work is finished, many come back to the company when another project begins. On B.L. projects, employees receive incentives in the form of bonuses at the end of each project which are higher than

other builders' incentives.

The company usually contracts several Technical Advisors who deal with structural and electrical designers, foundations and piping. B.L. considers it critical to have the best professionals in these fields, since a technical failure can cost an amount larger than the whole capital of the company.

The Administrative Manager maintains an up-to-date cash flow of the whole company and is also in charge of all the processes and needs of the carpentry section, a subsidiary business that provides wood supplies and products to the projects. This function is managed as a separate company because carpenters are considered the most important potential cause of delay in the construction process.

**Capital.** Since its formation, the company has pursued several strategies that are considered by the President to be very important to the success of a small construction company. A low investment of capital is considered essential to handle the cyclical nature of the construction industry. All the heavy equipment required for the completion of projects is rented. Since the company builds only one project at a time, it would not be possible to keep owned equipment fully utilized. The largest capital investments for the company are the sites for future projects site and the percentage of the project in



construction for which they are financially responsible (see Figure 6).

The price structure for a typical B.L. building is as follows: 14% land; 17% foundations and structure; 15% wall partitions and wet finishes; 15% dry finishes; 24% finance and overhead; and 15% income before taxes. A high percentage of the profit is reinvested in the growth of the company through the purchase of a bigger or better sites for the next building.

The company is one of the most financially efficient in the industry, a reputation it has acquired by a record of fast repayment of loans. In order to maintain this reputation, the President keeps tight control on the actualized cash flow and the balance of levels of incomes and expenses of the company. Thus there is continuous pressure on Operations Manager to keep the construction site on schedule, and on the sales department to process and complete the paperwork (contracts and licenses) as rapidly as possible.

The company has diversified to some extent by selling carpentry products to other construction companies and small pieces of customized furniture to apartment buyers. This occurs when B.L.'s own project needs are smaller than the production capacity of the carpentry operation. In this way B.L. keeps this major capital investment at permanent full-time production and utilization.

B.L.

BALANCE SHEET AS OF DECEMBER 31, 1989  
Colombia \$ 435.00 = US \$ 1.00

	Pesos (000)	Dollars
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash	3,217	7,395
Accounts Receivable	192,944	443,550
Real Estate for Sale	392,489	902,274
Projects in Construction	51,896	119,300
Temporary Investments	3,288	7,559
	-----	-----
<b>TOTAL CURRENT ASSETS</b>	643,834	1,480,078
<b>INVESTMENTS AND OTHER ASSETS</b>		
Long-Term Investments	870	2,000
Fix Assets	79,591	182,968
(Depreciation)	(7,376)	(16,957)
Deferred Expenses	66,637	153,189
Value Adjustments to Real Estate	88,616	203,715
	-----	-----
<b>TOTAL OTHER ASSETS</b>	228,338	524,915
	=====	=====
<b>TOTAL ASSETS</b>	872,172	2,004,993
<b>LIABILITIES</b>		
<b>CURRENT LIABILITIES</b>		
Accounts Payable	23,096	53,094
Financial Payables	507,038	1,165,604
Tax Provisions	5,976	13,739
Down Payments Received	115,267	264,982
	-----	-----
<b>TOTAL CURRENT LIABILITIES</b>	651,377	1,497,419
<b>LONG-TERM LIABILITIES</b>		
Accounts Payable to Partners	19,010	43,701
	-----	-----
<b>TOTAL LIABILITIES</b>	670,387	1,541,121
<b>NET WORTH</b>		
Capital and Legal Reserve	17,974	41,320
Accumulated Profits	95,194	218,837
Capital Surplus	88,616	203,715
	-----	-----
<b>TOTAL NET WORTH</b>	201,785	463,873
	=====	=====
<b>TOTAL LIABILITIES AND NET WORTH</b>	872,172	2,004,993

Figure 6

**Technology.** B.L. has invested in three micro-computers that serve the needs of the Accounting Department, the Sales staff, and the Operations Manager. Computerization of the accounting and the payroll functions have helped greatly in the analysis of company flow. Since apartment sales contracts are very similar, and their writing takes a long time, they are now done on a word processor. The computers are also used in the development of construction schedules, but not for subsequent management control. The Operations Manager hopes that B.L. will eventually use computers for estimating the quantities of materials, a task which is now done by hand.

The company has not invested much in research and development; it usually waits for the suppliers to offer new products. On several occasions, however, B.L. has collaborated with suppliers, giving them the opportunity to make prototypes or to place samples in B.L.'s buildings. New methods of construction used by other builders are analyzed carefully by the company. If these methods require high investments or do not show clear evidence of faster construction schedules they are discarded. B.L. considers that it is much better to have high control over reliable old methods than to gamble with procedures that are not 100% proven. The only experiment done directly by the company did not give the expected results. A new material for

reusable formwork was tested by the Operations Manager; it ended in greater concrete wastes and it required more qualified man-hours than the old procedure of bamboo boxes.

**Value Chain.** B.L. has been both the owner and contractor for the housing projects it develops. It buys most of its materials and products from different suppliers, with the exception of carpentry products. Because of its owner, contractor, and supplier roles, B.L. can be located at several points of the construction industry value chain.

The only major difference between the Colombian construction value chain and the U.S. chain, is the presence in the U.S. of the engineer as a subcontractor of the architect. In Colombia, the engineer is usually selected directly by the developer or owner. This means that the developer or owner is required to serve as a coordinator between these two professional. This gives the developer/owner more control over the specifications prepared by the architect. In the Colombian industry it is also more common to find the developer and general contractor in a single company.

The typical value chain in the U.S. is depicted in Figure 7 below, though it can be slightly different for some companies that have integrated vertically.

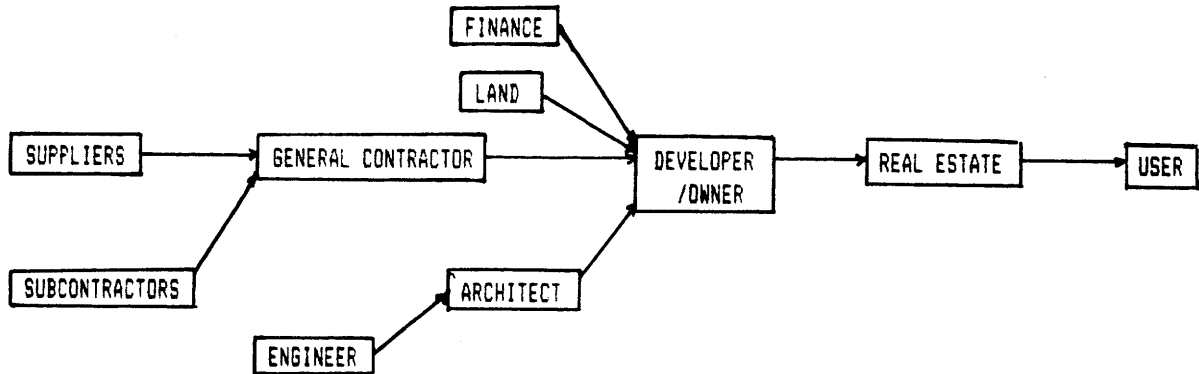


Figure 7. U.S. Construction industry value chain

In this chain, B.L. is a subcontractor (carpentry), a general contractor, an owner, and a realtor. As said before, sometimes it is also an architect; and, since all the partners live in buildings made by the company, it is also an user.

Financing is provided by one of the Savings and Housing Corporations described in the previous chapter. Although B.L. has used the same corporation for the past ten years, it continues to appraise the interest rates of the others. Since the government controls and limits these rates, their range is not wide. By maintaining an excellent relationship with the same institution, B.L. is treated as a special client.

The same can be said of B.L.'s relationship with the land developer and with some of its suppliers of raw materials. B.L., even though a small company, has taken maximum advantage of its solid business relations, its opportunities

to choose the best locations for its projects, and its ability to access raw materials at good prices.

**B.L. Near Future Projects.** In exchange for some apartments, the company acquired a property where a totally different market can be served. The project will involve lower cost buildings in a massive project consisting of 370 apartments. The company has been working on this project for several years. Some of the reasons why it has not been built yet are the company's lack of confidence in this segment of the market and the problems the company has encountered in dealing with the local regulations on new urbanization.

B.L. is also now ready to begin a project with the same characteristics as those it has built before. This project was to begin after the initiation of the lower cost buildings in the previous project. However, the delays in that project has forced the company to expedite the beginning of the higher cost housing project. This acceleration has presented no problem to the company since it involves the kind of work it is accustomed to.

## COMPETITIVE FORCES

This chapter analyzes the competitive forces that drive the construction industry in Colombia and how they affect B.L. The analysis is based on Porter's techniques for analyzing industries and competitors. The five forces to be studied are: 1) Threat of new entrants, 2) Threat of substitute products or services, 3) Bargaining power of suppliers, 4) Bargaining power of buyers, and 5) Rivalry among existing firms (see Figure 8 below).

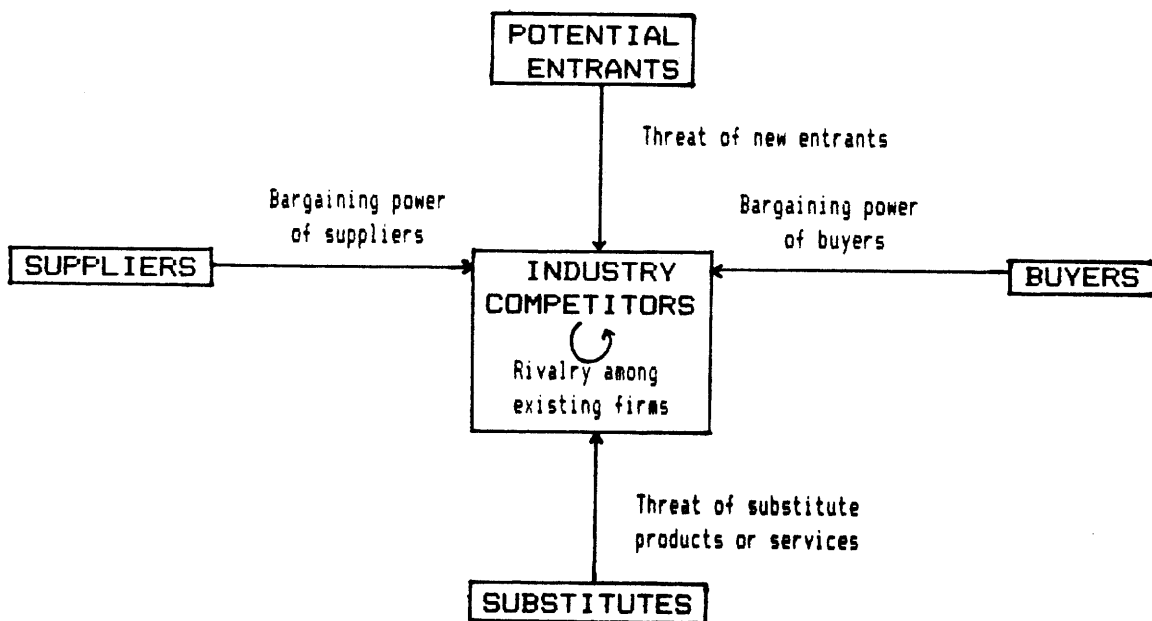


Figure 8. Porter's Forces Driving Industry Competition

**Threat of New Entrants.** As previously mentioned, the

entry barriers to construction for new investors are very low. This has been one of the reasons for the excessive supply in the market segment in which B.L. works. The possible barriers to entry applicable to other industries (e.g. high capital investments, switching costs, and lack of access to distribution channels) are not major barriers in construction, and only affect a few specific segments of the industry.

Economies of scale are few in construction. The control of a construction site requires the permanent presence of managers or superintendents. Construction activities are high in labor contents, unlike other industries where physical processing of products is done by machines or where the activities done by a worker are always the same. However, trends toward the industrialization of certain stages of the building process and the systematization of office activities are beginning to establish technological advantages for firms already in the market.

In Colombia one of the emerging new technologies is concrete sliding forms which can be economically only on repetitive projects. Therefore, this capital-intensive technology poses a barrier to entrants in a single segment of construction. B.L. must fully analyze the impact of this technology on its own ability to be successful as a new entrant in this market segment.

The Colombian construction industry is keeping up with



advancing information systems technology, particularly as it applies to the control of several projects at the same time and the efficient handling of the paperwork surrounding a project. Relative to the cost of construction projects, information technology is inexpensive and therefore not a major barrier to new entrants.

The possibility to buy construction supplies wholesale offers economies of scale for the larger established firms. However, the full advantage of this is diminished by the power of suppliers (see **Bargaining power of suppliers**).

The need for vertical integration is a more serious barrier to entrants, because it requires that an entrant must have to enter not one, but several industries at the same time, thus requiring a higher level need of capital. For example, several building firms in Colombia have vertically integrated by adding formwork rental services, carpentry services and products, concrete plants, and real estate services. Supplier firm expansion into, and integration of, construction is relatively uncommon, except when the firm is both the land developer and the builder at the same time. Some corporations and some brick-producers have added developer/construction subsidiaries to their organizations.

The nature of construction activities and a favorable learning curve preclude a barrier to entry in this aspect of the industry. Learning the basics of construction is very

easy. In addition construction activities are hard to mechanize because each project is different. Nevertheless, it is not unusual to find entrants that, after their first experience in construction, do not persist in staying in the business.

Product differentiation is difficult to find, except for very high-income projects. Even though some projects offer better workmanship or higher quality components, it is difficult for many buyers to notice the difference. Product differentiation is only found after a firm has enjoyed a long-time reputation for building quality homes. Thus the prestige of older firms in construction is a major entry barrier. However, there are cases where the entrants are former employees of the older firms who can claim they have gained the experience in these firms. Therefore reputation can act both as a barrier to, and as a support for entrants.

B.L., even though it is a small company, has taken full advantage of a privilege to choose the best locations for new projects and, its access to raw materials. As mentioned in the last chapter, these advantages have resulted from very good relationships with suppliers who offer the best sites or best prices to B.L. before doing so to other builders. B.L. also considered that up to date information about the industry provides an important edge. Thus B.L. partners are constantly participating in industry discussions, conferences, and congresses. These three

advantages, if possessed by all current builders in the market, would act as significant entry barriers. On the other hand, an entrant that can develop these advantages can become successful, just as B.L. did at the time it entered the market.

New entrants need not expect retaliation from other construction companies. Because the duration of preconstruction activities is so long, it is difficult for one builder to make a move once another builder's project has begun.

Price reductions to deter new entrants is only found on those markets that are near or at its saturation point; therefore the entrant shall look for markets free of this problem. For the builder that is already established in these markets - like B.L. - it becomes extremely important to have a strategy to cope with the market saturation problem, particularly if new entrants are appearing.

**Rivalry.** In order to understand the analysis of rivalry among existing firms in the Colombian construction industry, it is necessary to provide a definition of the kind of industry it is. Based on the generic industry environments described by Porter (1980), construction can be defined as a fragmented industry. This definition is most appropriate even though this industry is not mentioned on Porter's list of fragmented industries.

Aside from the fact that the total market share of the top 4 firms is less than 25%, construction can be considered a fragmented industry because of its low entry barriers, and the relative absence of economies of scale or experience curve. Some of the diseconomies of scale that benefit small companies are: 1) The lack of advantage for bigger firms in dealing with buyers; 2) The high inventory cost and capital requirements for large companies; 3) The ability of small companies to more readily provide a customized product; and 4) The ability of small firms to provide better and closer local control. B.L. considers these advantages as keys to its success. The fact of being a family-business enhances these advantages as will be seen in the next chapter.

Construction companies have made use of all the different competitive strategies available; but in a market so fragmented, it is extremely difficult to discern what these strategies are. The strategy of many builders is to acquire strengths that others already have. In other instances, the strategy of an entire segment of the construction industry has been to cope with fragmentation by increasing entry barriers through adoption of new technology that allows series production for the more price-sensitive markets.

Even though some of the conditions for the occurrence of strong rivalries exist in the Colombian industry - numerous and or equally qualified competitors and slow industry growth - rivalry inside the traditional building industry is

reasonable, ethical, and nondestructive. For example marketing materials and presentations only show the benefits of a project and never the weaknesses or shortcomings of a competitor's project. This "sane" competition may change however, with the new conditions of excessive supply.

The builders that provide housing can be divided into new entrants and those who have been in the business for longer time. Price levels for apartments are usually set by these new entrants. This often gives the traditional builders higher profit margins because of their ability to deliver higher quality products and their experience with cost and schedule control systems. Faced with the new condition of oversupply, the new entrants often reduce their costs or even sell without profits. The traditional builders, with their greater experience and better control systems, will most likely be the ones that survive.

**Threat of Substitutes.** The possible substitute for the products of the housing industry is existing housing. However, the sale of this product is difficult because of the lack of loans for existing housing. If the banks or the government design a method for increasing the sale of used houses, resale activities may become a strong competition to newly constructed housing. At the same time however, the owner of existing houses will then have the means for upgrading their housing through the purchase of a new house.

Rental of houses is not a very attractive business because of the higher profitability of the savings system and the limits placed by the local authorities on rental fees. If rental becomes attractive, it will not be a big competition to the housing construction industry; in fact it will impulse construction because investors will be willing to buy newly build apartments to use for rent.

**Bargaining Power of Buyers.** Supply and demand relationships are the primary determinants of the bargaining power to buyers. In Bogota buyers have become a stronger force as the availability of housing in the middle-high and high income market has increased. Buyers now have the opportunity to shop around for better prices and to ask the realtors for discounts or better payment terms. In such a buyers' market, only the all-time best quality producers will succeed.

Even though the market is showing signs of oversupply, B.L. has not yet felt them. Potential buyers, knowing of the market problem, see B.L.'s products and then shop around. Very often however, when they return, the apartment that was their choice has already been sold. B.L. partners assert that their continued success in selling apartments is because their products are reasonably priced and of good quality.

**Bargaining Power of Suppliers.** Suppliers, depending on their product, have high or low strength in the current market. A supplier's strength depends mostly, on the number of other suppliers in his product and material line and the degree of fragmentation of the supplier's industry. Some of the non-fragmented suppliers are the banks, land developers, foundation contractors, and most of the producers of raw materials, such as concrete, cement, bricks, piping, tile, sanitary equipment, bathroom and kitchen appliances, rugs, and paints.

Loans for the construction process depend on the government's policies, the amount of money in the savings system, and the number of construction companies. Some builders, like B.L., have developed long term relationships with the savings corporations. A history of good real estate development is very important to assure credit for future projects. This is even more important in the loan market in Colombia, where the construction lender is also the homebuyer lender.

Land developers are fragmented from the point of view of total construction activity. Every owner of a lot or of a house in a higher density zone is a possible supplier of land. However, in the market segment in which B.L. operates most land is provided by the descendants of a large farm owner. In order to reduce the strength of this supplier, the company is now looking for sites outside this zone that

have good perspectives for development.

Certain raw materials are produced by very few suppliers or by organized suppliers that set prices for the whole industry. B.L. has tried to overcome the high strength of some of these suppliers by being a "model" client, not by paying high prices, but by paying invoices on time. In another situation, B.L. reduced the power of traditional facade-brick producers by using acrylic-quartz paints as a substitute. With the concrete producers that have a set price, B.L. gets the best payment conditions.

Construction industry, being the most important buyer of most construction products and materials, should be in a position to demand lower prices. Builders in CAMACOL have tried to do so, but industry fragmentation and the suppliers that are members of CAMACOL have prevented any changes and the lowering of prices.



## THE CULTURE OF FAMILY-OWNED COMPANIES

Besides the fact of working in the housing construction segment, B.L. is also shaped by the owners' expectations about the company. Since it is owned by a family, the goals of B.L. are linked to those of the family. This chapter will analyze how the company objectives interrelate with those of the family.

**Definition of Family Business.** There is disagreement about the precise definition of a family-owned company. Some authors on this topic restricted the definition to those companies that have transferred power to a member of the second generation of a family. Other authors merely require the presence of several family members in the ownership and management of the firm. However, all authors constrain the definition to the ownership of a company by a single person or several members of a family.

Despite its importance in the world economy and history, family business is a very recent field of research. As Alcorn (1982), one of this subject researcher, says, this topic was first analyzed in the movies before being analyzed in the real business world. The study of family-owned companies by business professionals began with the problems

encountered by the post-World-War II entrepreneurs in the 1960's when many founders were leaving their companies. Each entrepreneur that created a company had added his own personality to it. Thus his way of life, attitudes, and environment made each company a different and unique entity, difficult to compare to others.

Today's studies are carried out by consulting companies and by people from academia. Some researchers have tried to define and group family organizations by size, primary purpose, percentage of ownership, or stage of development. The "stage of development" approach appears to be the best way to categorize firms because it tends to parallel size, generation, and culture of the family business. The stages of the family business are also different depending on the point of view of each author. Some authors take family generations as a basis for grouping, while others only consider the first generation and how it manages the changes that occur. The following are the different stages of a family company, taking into consideration most of the conditions that authors have given to differentiate one stage from another: 1) Creation, 2) Growth, 3) Maturity, 4) Transition of power to heirs, and 5) Business institutionalization.

The culture of the company may change from a paternalistic one in the first stages, to a professional management culture in the last one. These two extremes have

very different characteristics, but there are several other possible cultures between them. Dyer (1986) outlines several types of assumptions for these and for intermediate cultural patterns.

B.L. does not fit exactly into Dyer's pattern since from its creation, it was meant to be a family business. However, B.L.'s culture coincide with the paternalistic model. These include: the existence of a hierarchical organization; a belief that people are untrustworthy; the presence of some kind of nepotism (to be analyzed later in this chapter); and, although the management group may participate in decisions, the final authority resides in the founder or in his family. B.L. also fits into the more advanced participative culture because it has the pattern of the present- or future-oriented companies.

**Definition of Culture.** Unlike most other construction companies, B.L.'s objectives create a unique approach to the competitive forces mentioned in the previous chapter. The atmosphere in every B.L. activity is guided by a "pattern of basic assumptions - invented, discovered, or developed - to cope with its problems of external adaptation and internal integration" (Schein, 1985). This atmosphere is the culture of the company and, even though not specifically written or stated by its members, they all recognize its existence.

The fact that B.L. is a family-owned company has

determined most of its policies. From its conception, B.L.'s purpose was to provide for the well-being of the family members (education, housing, etc.), along with economic independence sought by the company founder - a motivation shared among most entrepreneurs. B.L. was set up as a family partnership. As mentioned in **History of B.L.**, the by-laws of the company gave each of the six family members one-sixth of the partnership. A point that distinguishes B.L. from other entrepreneurships is its implicit intent of succession and the participation of all family members.

The fact of having a different culture from publicly held organizations, is probably the only point in common among family businesses. The family business culture in itself, may have various shades, but there will always be the need to merge the family and business needs.

**Problems of Family Businesses.** The change from one stage of development to another is frequently traumatic for a family business. Over time, the needs and relationships of the company and the family have developed and changed according to the objectives of both.

The three major problems created by the merger of the needs of the family and the company are:

- "1) A lack of discipline being exerted over profits and performance in all parts of the organization.
- 2) A failure to rise quickly to meet new marketing challenges.

- 3) Situations where nepotism rules unchecked by objective standards of meritorious managerial performance." (Donnelley, 1964)

These problems arise out of the conflicts of interests occurring between the family and the company.

Some psychologists have specialized in the above problems, viewing them as consequences of the personality of the entrepreneur or of rivalries within the family. They suggest that the founder, because of preceding resentments, creates a company that is an extension of himself. When the moment arrives to transfer power, or to involve other family members in the organization, the rivalries among them also arrive.

The relationships of the family members with the company, and the industry environment, make the problems appear differently in each stage of development. The frequency of occurrence of these problems is summarized in Figure 9

below.

Problem	Lack of discipline over profits and performance	Failure to rise quickly to meet new markets	Situations where nepotism rules
Stage			
CREATION	LOW	HIGH	LOW
GROWTH	HIGH	LOW	HIGH
MATURITY	HIGH	HIGH	HIGH
TRANSITION OF POWER	DEPENDS	LOW	HIGH
PROFESSIONAL MANAGEMENT	LOW	LOW	LOW

**Figure 9. Frequency of Occurrence**

For the entrepreneur that is creating a new company, the initiation and start up problems (search for capital and location, improvement of product and operation, selection of marketing and distribution) are so large, there is no time to think of the family and succession. Nor are there excess profits to worry about. These same problems are the reason why a start up company has difficulties in meeting new markets, a problem which is not limited to a family enterprise. At this stage few entrepreneurs consider their company more than their personal achievement. However, B.L.'s case is quite different. The founder of B.L. never thought of selling the company, he always thought of passing it along to his heirs.

Studies have shown that just after the first success of the enterprise, which sometimes requires a long period of work, the entrepreneur begins to think of what will happen to his "masterpiece" after his retirement. Thus family-related problems begin to appear at the growth stage of the enterprise, or at the moment when succession and income distribution become issues. Awareness of these problems is the best way to avoid them, and to arrive at a point where professional management and family business can coexist.

**Lack of Discipline.** Lack of discipline over profits and performance is a problem of organizations that have to meet

needs beyond those of the company. It can occur even though a family business may have low producing costs and excellent cost control by the owner himself. The entrepreneur has greater appreciation of the values of his property, and therefore takes better care of his assets and works harder to produce better quality. But when he distributes profits, it is done without consistency from one year to another. Unfortunately, statistically, the level of profits of a family business cannot be compared with that of its public counterparts because of the lack of audit. The family business has the ability to disperse profits as salaries, thus making them appear as operating costs.

Lack of discipline in performance occurs when the owner places the family above the company on his scale of values. B.L. has felt this lack of discipline in profits and performance. The projects are built according to the workload and convenience of family members without regard to the perspectives of other employees or to the appearance of other market opportunities. Thus non-family members at the managerial level, sometime see unpredictable future that makes them think about opportunities outside the company.

However, lack of discipline is a plus when restrictions on expenses is required. The example of families making personal sacrifices while the company is growing is seen by several researchers as an advantage of closely-held corporations. As manager of the company and family head the

entrepreneur can cut expenses in both places. For public corporation owners it is sometimes difficult to understand that their organization cannot return the promised dividends and end up blaming the managers for mismanagement. Nevertheless, businesses that do not overcome lack of discipline, will not make it to the ultimate stage of institutionalization. When this stage is reached, growth of the company has been big enough as to make prior family sacrifices seem unimportant.

**Failure to Rise Quickly to Meet New Markets.** Failure to meet new markets is not an issue for a growing company that is looking for additional work; that is their objective. But once the company has arrived at a stage of maturity where production is high and controlled, the culture of the company may be "not to grow". Since the founders have made it through the first stages, they may consider that surviving is enough. And it has really been a great battle since only a small percentage make it to the transition of power stage (Ward, 1987).

The President of B.L. has stated that the company has no reason to grow since it controls its buildings and the parents of the family know where their money is going. If this philosophy persists beyond the transition of power stage, the company will continue failing to meet new markets. The next chapter, **Strategy**, describes an



alternative to new markets.

The transition of power stage is sometimes associated with ideas of growth and search for new markets by those who inherit the company. The psychologists have defined this heirs' need of expansion as a search for the success enjoyed by their parents. In several cases where the "children" try to produce rapid changes without considering the legacy of family culture built by the parents, the consequence has been outright failure. Unfortunately, when not prepared for succession, heirs may well lose the company and the principal benefits for perpetuation of family business in the first place - the opportunity for financial freedom and personal growth.

There are also cases where inheritors do not perceive the opportunities of new markets. This is common where the heirs have not had experience outside the family business, and where the company and its personnel are overly committed to, or identified with, a particular service or product.

**Situations Where Nepotism Rules.** Nepotism (favoritism towards relatives) is another problem of family business for which awareness is the only solution. Some families have established very rigid rules to cope with this problem, while others simply try to live with it. The former usually hold a philosophy of "business first". They create rules for the entrance of the next generations to the company such

as: higher education; mandatory work outside the family business; and success in these and other activities.

The families that try to survive with nepotism believe in a "family first" philosophy. This type of culture believes the qualifications of family members depends solely on the generation they come from. The former type family is generally more successful than the latter, since no productive company can exist with incompetent managers, and with the situation of business problems being turned into family problems and feuds.

There is also a "family enterprise first" philosophy, which believes in the integration of the need of employment of family members, as long as it does not damage the company or its objectives. The followers of this philosophy create jobs inside the enterprise in accordance with the capabilities of individual family members. The consequence is not always the best because of its effects on the performance of non-family employees. Since this type of nepotism creates the possibility that family members are more likely to get the primary jobs, outsiders feel precluded from the opportunities of far advancement in the future. As a result, highly qualified managers may not be motivated or able to produce the full measure of performance of which they are capable.

B.L. can be considered a "family enterprise first" type business because it has created specific jobs for the

children of the founder. Compensation is awarded according to the individual contribution to the company. However, all family members are assured an acceptable standard of living. Even though the founding parents believe that outside experience would be useful for the children, they do not make it a condition of employment in the company. One reason for this job creation approach is to give the children experience in the different fields they may pursue in college. It also creates enthusiasm for the perpetuation of the business.

An example of possible problems with non-family employees occurred when an operations manager resigned because of the threat that one of the heirs posed to his position. As the manager explained, his future in the company would be hindered by the presence of a family member who was serving as his assistant in order to acquire the knowledge required to take over the position.

**B.L., A Family Business, and The Competitive Forces.** It might be concluded from the foregoing discussion that family businesses only have problems to deal with. In this section the positive aspects are described. The family business has several competitive advantages unique to its nature and culture. In addition, family members attachment to the company creates a high exit barrier.

One of the major advantages of a company in a fragmented

industry, like construction, which is enhanced in the family business, is the ability to give a "personal service". As mentioned by the president of B.L., this is a clearly discernable advantage in the selling process. Yet, it can also be a restraint on growth, if it is based solely on the work load of the founder. This restriction can be overcome by adding more family members to the selling force.

Reputation and being an employee with the same last name as the company, are two factors which motivate and encourage family employees to work hard for the welfare of the firm. This a strong competitive advantage over the competitors in the industry. Many buyers recognize the need of a family business to maintain its reputation and therefore are more willing to do business with them.

Over a period of 14 years, B.L. has created a reputation for the construction and sale of quality buildings and apartments. This is reflected in the large number of new buyers that come to B.L. projects because of the recommendations given by former buyers. These good references, which are in a localized market, result from the personal sales approach of the company, as well as its timely response and resolution of the enquiries and claims of the inhabitants of its buildings. The mother-founder is also very involved in the design process to insure that the apartments are as efficient as possible. She is very concerned with the quality details that a woman is most

likely to notice and appreciate. Her abilities in this regard are well proven and a unique capability of this particular family business.

In the industry, B.L. also has an excellent reputation as a responsible and concerned builder. This concern is evidenced by its participation in the industry activities which gives the company valuable local contacts with suppliers as well as knowledge of current issues and challenges confronting the industry. All family members are encouraged to participate in these activities.

Another advantage of the family business is that relationships with certain suppliers and other resources are made easier. One example is the labor force. The affection of an employee towards a company is higher when the environment offers both a high degree of recognition and a feeling of belonging. It has also been observed that employees who recognize the high exit barrier aspect of a family company feel more secure with a family member managing the company rather than an outsider. Therefore they often actively encourage family control by the heirs. This is not true of course in the case of the outsider who has higher ambitions.

Employment of family members is also an advantage to the business because these employees are more reliable and create a lower turnover. In addition, the family can supply highly reliable employees to cover positions left by

absentees. This occurred in B.L. when its president was called for a public office: a son-in-law and the mother replaced him for a period of four years.

## STRATEGY TO BE PURSUED

The following are the conclusions and recommendations of what shall happen with B.L. They are based on the environment described in the first chapters and the family business theories stated in the latter one.

**B.L. and the Industry.** Several current market and industry conditions in Bogota forecast a different future for the Colombian construction industry. Now that the high-end housing market has been saturated for the first time, more sever cycles can be expected. The activity in this segment will go from very prosperous periods, to periods where just a minimum of housing will be sold. This situation has occurred in the construction industries of countries where the level of housing has reached a minimum point of satisfaction. Before this point is reached, the demand for housing was a more permanent and stable market.

With respect to the industry, there is increasing industrialization of several building processes. This situation, combined with a declining and cyclical market reduces the traditional industry's ability as a significant and reliable employment generator. When this happens the government may not be willing to continue its treatment of

the construction industry as a leader industry in future economic plans and programs.

In view of these prospects for the future, B.L. may have to fight for survival as never before. The competitive advantages previously identified will probably give the company good prospects for the near future, particularly in comparison with other builders. But will the strategies pursued in the past be useful forever? Should the company attempt to grow within the present market segment or should it diversify into other market segments.

The analysis done in prior chapters strongly indicate that the current culture of the company may not be able to handle the massive kind of projects currently being considered. On a construction site of 370 apartments, the company will not be able to continue the personalized service to all its future clients. Since it is focused for a lower income consumer it is expected that these clients will be less quality-sensitive and more price-sensitive. Another problem may be to produce at low cost when the company employs have always been committed to quality production. The constructors in this lower-cost market segment already have procedures that are useful on large construction projects which take maximum advantage of high-quantity production. There are other builders that have invested heavily in sliding formwork and other new technologies that give them higher rates of production and



the ability to sell at very low costs.

Growth of the company most likely will not be considered by the current president since the company lacks the procedures to control every cost and detail on such a great project. The ability to exercise this control has been a competitive advantage over the other construction companies. Although a higher volume of construction can be controlled through an enlarged computing system, this would force the president to rely more heavily on the work done by the functional departments of the company. This is difficult to occur in a company which is accustomed to seeing that everything is done in the way the founder has designed it.

However if the corporation still pursues family well-being as a major objective, and if the family has grown, it must look for higher levels of profits. Maintaining a larger lineage requires more resources and more control of the expenses.

An alternate investment of the company's profits may be to increase vertical integration (as it has done with carpentry) with respect to subproducts that are considered troublesome to the finishing and quality of the building, for example the window frames. Experience can be taken from the carpentry operation and its industrial-like controls which are able to produce closets, doors, and other furniture with high quality at low cost.

Another typical problem of the family business, is the

lack of capital supply that leads to a focused strategy and limits the mobility to new markets. As with most family businesses, B.L.'s desire to keep the company closely held, impede the entrance of non-family investors. Since this is one of the permanent objectives of B.L., a focused strategy is appropriate, especially in a market where people are willing to pay for a differentiated product. To continue serving only the high-end market segment may lead to high profits, but also to difficulties to expand.

If the family decides to pursue expansion, one way to cope with the lack of capital might be to build for others. In this approach, the company would work under a specific contract with an outside capital investor. B.L. would perform the design, build, and sell processes for those who do not know the construction business and are deterred by the problems encountered by other new entrants to the industry.

Another strategy is to have the company prepared to serve quality-sensitive markets other than high-end housing. These other markets would help counteract the cycles in the housing sector. The personalized service approach would be a sales strength when dealing with school owners, industrial clients, and other capital investors. The company has the necessary experience and capabilities to undertake turn-key contracts; it knows the regulations, the designers, the financiers, the subcontractors, and the suppliers. If

required, it also can perform the selling process.

**Prepare for Transfer of Power.** Companies that leave considerations of succession to the last minute (e.g. on the death or extreme sickness of the founder) usually suffer more traumatic changes during the transfer of power. Therefore, the company must prepare in advance for a transfer of power. The president, even though still young, has mentioned a desire to retire. But as it happened in several cases mentioned in the literature, the president might well return to the company for fear that the heirs were spoiling his legacy. The chance of this occurring can be lessened if the founder is aware of and accepts the necessary need for cultural change which is accomplished slowly and on a planned basis.

After an official transfer takes place, the former president can always be assigned activities to keep him involved. When the successors wish to make changes, they can consult with the founder. However, it must be clear that his position is that of a consultant and not that of a final decision-maker. These changes, if successful, will instill more confidence in the inheritors. The reason for success is not necessarily the brilliancy of the idea, but the commitment of the total organization to pursue a common goal. The support of the older generations can contribute greatly to this pursuit.

Another way of developing self-confidence in successors is insisting that they engage in outside employment at some point in their careers. Working in other organizations, for other bosses, or in other industries, can give family employees a broader understanding and appreciation of the business world. Then, as successors they may have a greater chance to successfully pursue changes of objectives in a company. It introduces an appreciation of the good side of professional management to the family business. However, there is always the risk that the heirs might find more satisfying career opportunities outside the family business.

It is important to establish acceptance for the possible alternative of an outsider as the next president of the family business. This has been done in companies where the second generation is still not prepared to assume the responsibilities of management. It also provides more motivation for the ambitious outsider who can see the presidency as his ultimate goal; and it can be the first step to institutionalization of the business.

To ensure success, any cultural change must be slow. Equally important, the company must continue the cultural values created by the founder that gave the family business its competitive advantage in the first place. In order to maintain the name and reputation of B.L. in particular, the inheritors must learn from the founders those activities and skills which are important, the "personalized service",

hallmark of the company.

**Professional Management.** The importance of business institutionalization arrives when the control and interests of the company are spread out among several persons, such as founders and heirs. Professional management helps distinguish the needs of the business from those of the proprietors. It also differentiates the links among family members as family relationships or as partnership relationships. As the number of inheritors increase, these two issues become more difficult to manage. The establishment of a set of rules for the family business is therefore important and essential to its continued success.

Normally these rules are not inherent in the original culture of the family business. Therefore, the company must make a conscious effort to develop them.

Nepotism is outruled in professional management, but it can still be useful for family members with undergraduate level academic experience. This helps create in the family members a sense of ownership and responsibility towards the business.

The rules of the next culture should dictate minimum capabilities and accomplishments from any family member that want to become a part of the business. Those family members that do not want to be employees of the business should appreciate that they are going to receive higher levels of

profits from their ownership shares if the managers are skillful.

If professional management is finally adopted as the appropriate culture, it will help the company adapt to meet the needs and requirements of bigger and more efficient organizations. Concepts such as a matrix management organization can enhance the efficient use of resources and increase the motivation of employees with ambitions. In a construction company this can be achieved by assigning project managers to each project and giving them technical support through the functional departments of the central office. The most valuable and competent employees can be used on several projects or in the stages of construction which are most to their liking. The company must also be willing to provide longer term contracts to the key personnel.

**Final Recommendation.** B.L. must define a plan on the following topics in the frame of the family business:

1. Search of new markets for high quality work to pursue of a focus strategy.
2. Cope with the problems of low cost work if expansion is still desired.
3. Use of vertical integration as a method to invest and expand.
4. Establish professional management as the method to

assure success and well-being of the family.

5. Assure succession to reliable managers, family or non-family members.
6. Foresee cultural changes required for expansion, for non-family employees motivation, and for more family members participation.

Prepared to confront these issues, the company will have the competitive advantage of having a prepared strategy. This is how management differentiates from business administration. Having thought about the above topics does not imply that a strictly planned development has to take place; it means that the company will be able to handle the decisions that are more suitable to itself and the family.

In the final analysis, the strategy to be pursued by the company must take into consideration the willingness of the family to design and adapt to a new and necessary set of rules. This awareness, and the ability to accept planned change must begin in the first generation and must be transferred to the generations to follow.

## APPENDIX A

### Corporations' Loans Distribution

Resolution Number 2 of 1989 (January 12) by which norms on the matter of Saving and Housing Corporations are being dictated.

The Monetary Board of the Republic of Colombia [...] resolves:

1st Article. The total of new loans given by the saving and housing corporations [...] will be distributed as follows:

a) Not less than twenty-five percent (25%) in loans referred to houses with prices equal or under 3,000 UPACs [US \$16,500 Nov./89]...

b) Not less than twenty-five percent (25%) in loans referred to houses with prices above 3,000 UPACs and equal or under 5,000 UPACs [US \$27,400]...

c) Not less than five percent (5%) in loans for used houses...

d) Not less than five percent (5%) in loans for houses [...] of developments of the Priority Urban Programs...

e) Until twenty percent (20%) in loans referred to houses with prices above 10,000 UPACs [US \$54,800] and equal or under 20,000 UPACs [US \$109,600]...

f) The remainder in loans referred to housing between 5,000 UPACs and 10,000 UPACs...

...3rd Article...When a corporation does not meet the [above] requirements by the end of each quarter, it will be obliged to make up for such a defect [...] buying Bonds of Urban Foment released by the Central Mortgage Bank or Titles of Constant Value released by the Fund of Saving and Housing.

Other articles in this law refer to the maximum a corporation can lend to an individual house (9,000 UPACs) and the different interest rates applicable for each of the ranges (a through f).



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