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THE USE OF CONSORTIA FOR THE INTERNATIONALIZATION OF FIRMS – MOTA-ENGIL CASE STUDY

Maria João Sousa

Universidade Católica Portuguesa (Porto)

Susana Costa e Silva

Universidade Católica Portuguesa (Porto)

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Faculdade de Economia e Gestão

Universidade Católica Portuguesa

Rua Diogo Botelho, 1327

4169-005 Porto - PORTUGAL

Abstract

Internationalization has been widely studied throughout the years. Broadly, it has been predicted as irrevocable and having increasing impact on firm-related strategy. Within entry modes, consortium, has not received as much attention as others. Hence, it seems important to understand how this specific entry mode allows the entrance of firms in the international markets.

This study intends to answer the question of "how" to internationalize, anticipating the consortium as the most feasible way for construction firms to enter certain markets. The reasons that determine its choice concern the specificness of the projects, markets and of the firm. In the first part of the study, we review the existent literature on consortia as an entry mode and as a tool of internationalization used by construction firms. Through this review we build a framework that reveals the motivations that lead to this choice. In the second part, we present the case study of Mota-Engil, as a potential source of valuable information which may contribute to the understanding of the phenomenon under study. This case study corroborates the motivations found to create consortia. The paper closes with its contributions, limitations and suggestions for future researches.

Keywords: consortia, internationalization, cooperation, construction.

Introduction

In order to expand its activity to other countries, a firm needs to settle in a clear and assertive way its strategy concerning entry modes. Among the several entry modes available to firms, none can be considered as being the best, *de per se*, and we should, instead, choose the one that better suits the case at hand (Chang, 1995; Folta, 1998; Hennart, 1991; Reddy *et al.*, 2002; Williamson, 1991).

In this article, we intend to study a specific entry mode: the consortium. This entry mode has been widely used in the construction industry, especially in international expansion. Therefore, the question examined here is: "In what way do consortia allow the internationalization of firms?" We will try to depict the determinants that lead to the choice of this entry mode by construction firms, in order to understand their international strategy.

In Anglo-Saxon literature consortia are considered non-equity joint ventures, different from the equity joint ventures because they don't imply the creation of a separate entity, with legal form, through the equitable contribution of capital from the partners (Erramili *et al.*, 2002). The specificity of this entry mode allows firms to collaborate during a certain period, to share resources, split risks and then easily dissolve the partnering at the end of the project. This issue seems to be poorly studied in the international business literature (Ireland *et al.*, 2002; Kumar and Nti, 1998; Narula and Dunning, 1998; Reuer and Ariño, 2002), which rouses a larger interest in its study. The frequent use of the consortium as well as the various situations in which it applies, justifies the need to further investigate this subject within internationalization literature.

Literature Review

The consortia as an entry mode

The existing literature provides several classification types of entry modes. Most types use criteria such as: risk and degree of control. Anderson and Gatignon (1986) argue that the best entry mode results from a trade-off between the degree of control that the firm intends to carry out and the level of risk involved.

In this paper we use a typology of entry modes consisting of three groups, according to the degree of control, risk and flexibility:

- Export modes: low control, low risk, high flexibility.
- Contractual modes: shared control and risk, shared property.
- Investment modes: high control, high risk, low flexibility.

According to this typology, the consortium is a contractual entry mode. This kind of contract happens when firms have some kind of competitive advantage which, separately, they are not able to take advantage of, due to various constraints. Hence, a firm will start cooperative activities with other organizations. A consortium or contractual joint venture is formed to execute a certain project with limited durability (Sillars and Kangari, 2004). The project, due to its specificity, usually high risk and investment, requires team work of two or more firms in a separate organization. These are formal cooperation agreements between firms which do not imply capital sharing, nor the creation of a legal entity. Both parts have legal and strategic autonomy, which asserts more freedom to the partners involved.

A consortium, as a legal entity, constitutes a **non-equity** and **non-corporate joint venture**, according to international business literature.

Consortia in the construction business

Literature on marketing in international construction activity is scarce (El-Higzi, 2001). Construction is a service rendered, and therefore, it is an activity of great complexity. Complexity is great because of all the individual characteristics, inherent to the non-conventional nature of its services.

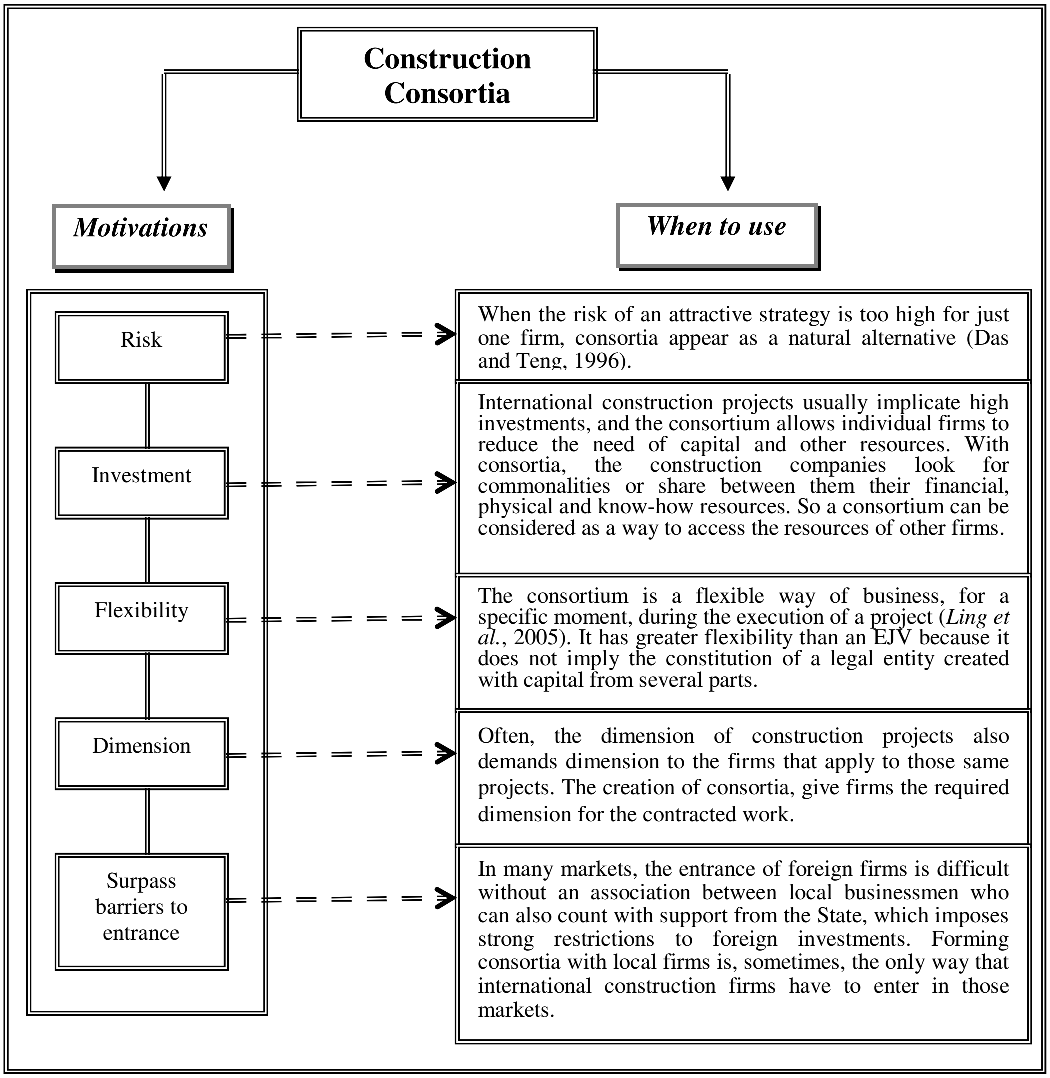
Construction is a capital intensive industry. In this industry financial availability is a key factor. Governmental assistance, the decrease of trade barriers, the existence of assistance programmes to export and of aid packages are factors that foster the international growth of firms of this industry (El-Higzi, 2001, Gunhan and Arditi, 2005). Moreover, an important part of the construction business is promoted by public investment (Tiong, 1990, Ye and Tiong, 2000). So, it is fundamental to the construction firm to find political support for the project they intend to carry out (Ling *el al.*, 2005).

Besides the typical risks inherent to a domestic construction project, at the international level, firms are exposed to a complex and subtle network of political, economic and cultural risks (Ashley and Bonner, 1987, Han and Diekmann, 2001). According to Terpstra and Sarathy (1991), increased levels of complexity and uncertainty are faced by firms that act in an international environment, considering that competition, the political, legal and governmental environments, the technological development of the country, culture, language, and even the weather are not well know and may affect firms' success.

International business literature emphasizes mostly equity JV, while the consortium is treated in a very superficial way (Beamish and Banks, 1987, Luo and Park, 2004, Wang and Nicholas, 2007). In the construction sector, existent studies are still very scarce, and entry modes in that industry are treated in a general way.

The consortium is often chosen by construction companies, because it meets several purposes and restrictions (Figure 1).

Figure 1 - Motivations for the choice of consortia in the construction sector



Due to the complex nature of the activities, process, environment and organization of the construction industry, firms are exposed to an extremely high level of **risk** (Bing *et al*., 1999). Thus, several researchers identified risk sharing as an important motivation to form interfirm alliances (Kogut, 1991; Oliver, 1990, Powell, 1987). Like consortia, these types of alliances transfer risk and control to other firms (Brouthers, 1995).

Investment is also a particularly conditionary factor to the performance of the construction firms. This sector is very capital intensive in which, in order to carry out projects, a great level of commitment of resources and, consequently, a large investment is necessary. So, construction firms unite themselves, often, in consortia to contribute with physical, capacity, experience or financial resources (Badger *et al.*, 1995; Chan *et al.*, 1997) in the required proportion in order to carry out the project.

By creating consortia, the **dimension** necessary to the adjudication of the large-scale projects can be achieved. Smaller firms, for instance, find in consortia a growth opportunity, by becoming partners of larger firms with more resources (Sillars and Kangari, 2004).

Since they don't imply common property nor the constitution of a separate legal entity, consortia offer greater **strategic flexibility**. Being a non-equity joint venture, consortia give more room to maneuver when a decision is taken (Das and Teng, 1996). This entry mode still works as a way to surpass the **entrance barriers** established in many markets, by local firms. They unite themselves in order to obstruct the entrance of external competition. By creating consortia with local partners, the foreign firms achieve a larger opening for their activities through the entities from the destination country (Shen and Wu, 2001).

Methodology

According to Yin (1994), as a rule, the case study represents the most suitable strategy to follow when the research questions include a "how" or a "why", when the degree of control that the researcher has over the events is restricted or null, and when the study is focused on an actual phenomenon in its natural context. A case study approach is adopted because of the need to gather detailed information from managers in order to respond our research question. The phenomena under analysis calls for a qualitative research methodology (Whitla *et al.*, 2006) and thus we chose a case study: Mota-Engil.

This group is currently the largest. This company uses consortia construction group in Portugal, for the case study, is justified by the frequent use of consortia as an internationalization tool. This case study contributes to understand and to explain the motivations which lead the firm to adopt this entry mode. It might also contribute to instruct possible management activities in similar areas.

The Mota-Engil Case

Construction is the sector that generates more jobs, at the European level. 26 million workers depend on it, directly and indirectly[1]. The enlargement of the European Union to many Eastern countries that belonged to the former Eastern Block created new business

[1] in Mota-Engil, 2007a.

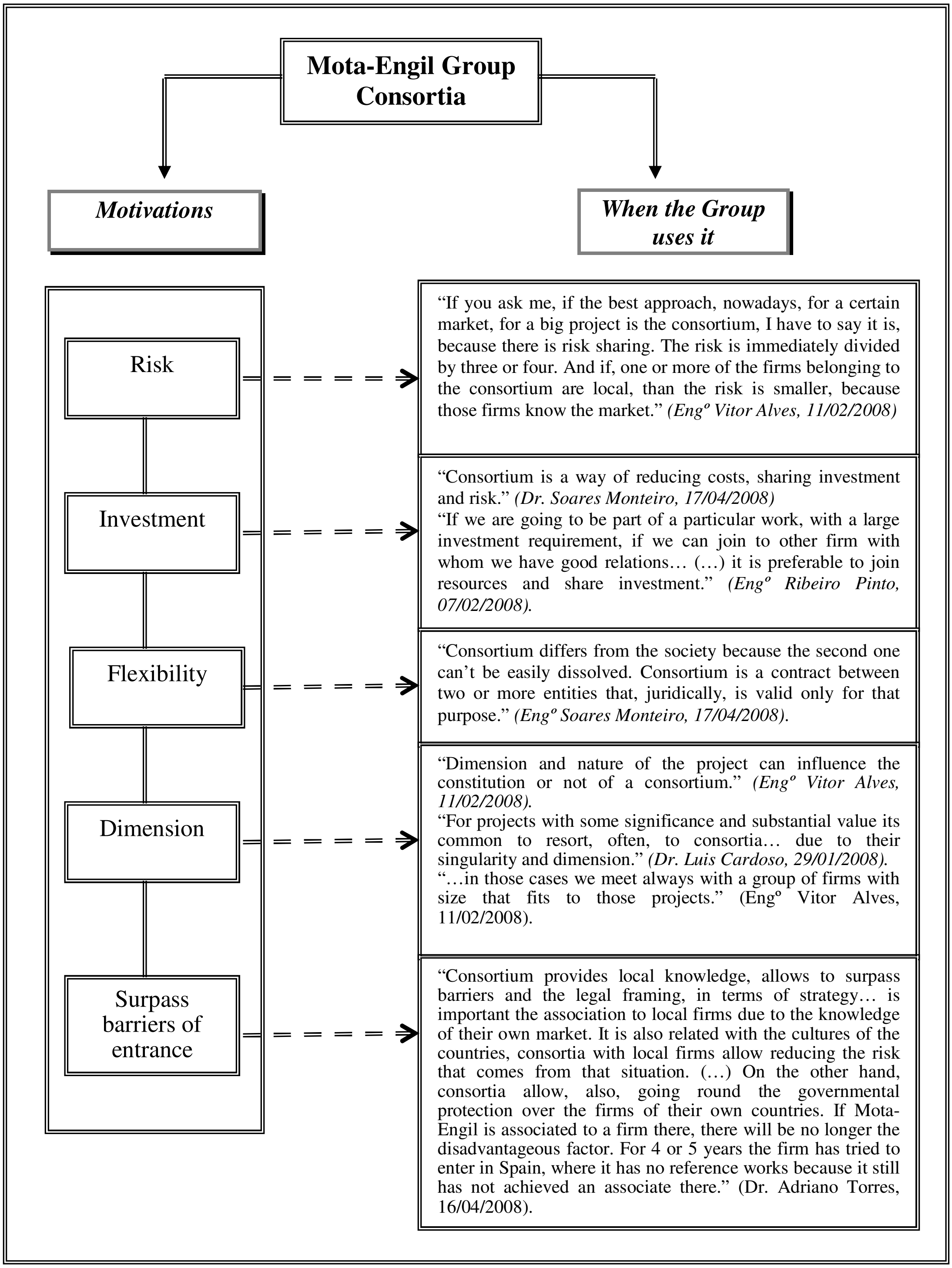
opportunities and, consequently, expansion of international operations to new markets. Large European construction firms cross each other in public competitions in countries such as Poland, the Check Republic, Slovakia, Hungary, Romania, Ukraine and Russia. Usually, they are associated to local firms with a certain dimension, due to the knowledge they have about the market, legislation, environmental aspects and safety. In addition, in Africa, the big construction boom is happening in Angola with 26% growth per year. This fact allows the entrance of many Portuguese construction firms in that market. It is also important to mention competition from Chinese firms, despite the quality of their work being inferior to the standard of many European firms in the same area. The lower quality work of these firms results, essentially, from the use of cheap, unqualified labour, the offer of services in exchange for commercial compensations with the support of the Chinese State and the practice of dumping in the market prices.

Mota-Engil, one of the main private economic groups in Portugal, explores and develops an integrated businesses portfolio focused in the construction chain of value with performance levels aligned with the best international practices. Leader in the national market, at the European level the company is the 67th largest firm in the construction area[2]. The international market represented, in 2007, 43% of the Group's construction activity[3]. The Group is currently present in 20 countries.

In the Mota-Engil strategy, consortia are precious means of market approach in certain circumstances due to a combination of motivations, as described before in Figure 1. Figure 2, below, points out consortia of the Mota-Engil Group using the same motivations. It shows that these motivations are present at the moment decisions about the entry mode are taken.

[2] in Deloitte, 2008.
[3] in Mota-Engil, 2007b.

Figure 2 - Mota-Engil Group motivations to choose consortia



When the Group tries to carry out a certain project, the consortium appears as the most suitable method for the dispersion of the risk. Because, in consortium, the inherent risk to the project no longer falls upon just one firm. It is shared by the associates (Ling *et al.*, 2005). The risk is, thus, smaller for each firm individually.

The so called "construction works"[4], which always present high technical complexity and high safety requirements, are largely executed in consortium. The purpose is to minimize the associated risk. In several African countries, in which entering implies considerable risk, especially in the cases of high political risk, consortium is the choice for Mota-Engil. The consortium guarantees some support between the cooperation partners.

- **The investment**

Projects of a large dimension require a substantial level of investment of resources, which only the firm is not always capable to achieve. The solution found by the Group is, together with other specialized firms, to create a strong consortium to combine financial, physical and know-how resources and share risks.This kind of cooperation is followed, for example, by Mota-Engil to carry out the project of the Atlantic Towers, in Angola. This is considered the biggest construction work in the city of Luanda, with an investment of 110 million euros. The same thing happens in Mozambique, where the consortium Mota-Engil/Soares da Costa is executing the bridge over the river Zambeze. This is considered the biggest infra-structure carried out in the country since its independence, estimated at 66 million euros.

- **The flexibility**

When the purpose of cooperation is perfectly defined within a short and previously established period, the Group tries to materialize it through a flexible contract. This contract allows the Group to dissolve it, with no restrictions, at the time the project ends (Wang and Nicholas, 2007). Consortium is the option chosen because it does not imply the formation of a legal entity resulting from the investment of capital between both parts (Wang, 2007). Each part cooperates as a separate legal entity and bears their responsibilities. The consortium is subject to the minimum of administrative barriers, taking less time and being less economic, in bureaucratic terms, than an equity joint venture.

Often, a consortium works for Mota-Engil as the entrance door to certain countries. The purpose is to engage local knowledge and try to establish a network of contacts in the host

[4] The term "construction works", in construction activity refers to bridges, viaducts and tunnels.

country (Starssmann, 1898). Afterwards, the Group might move to an autonomous activity which will allow to consolidate a position in the market and improve the level of flexibility of activities. The same is applied to works with a previously established and short term, like the bridge over the river Catumbela, in the Angolan province of Benguela. Having a limited time frame leads to the preference for contracts that are easy to terminate. For the Group, flexibility means the adaptability of consortia to the places where it is working and to the means it has at their disposal.

- **The dimension**

When in competition for a project of large dimension the most common is for the Group to try to compete in consortium for the work contract. It tries to join with other firms that have experience and the necessary technical capacities to accomplish the project. Complementarity of the firms in terms of equipment, human resources and know-how allows the consortium to achieve the dimension and organization necessary to execute the work.

On the other hand, in markets with strong growth, the Group feels the need to reply to competition in consortium with international players. Because, despite being a leader in the home market, the Group does not always have the necessary strength and dimension to rival the biggest firms in the area, at the international level. The Central and Eastern Europe Markets, for example, highly competitive and attractive, forecast a fierce struggle between the giants of the sector. That is why those are the markets where the entrance through consortia is crucial, since they provide the concentration of associated firms to a common purpose (Terpstra and Simonin, 1993). Thus, the competition is reduced, since the competitors become, often, partners in consortia.

- **The entry barriers**

In markets with a small degree of receptivity to foreign investment and with a high degree of protectionism, consortia with local firms are a way for the Group to enter and conquer awareness so that they might, afterwards, develop their activities (Kogut, 1988, Ling *et al.*, 2005). The partners, foreign and local, can complement themselves mutually. Domestic firms have better knowledge of the local work conditions, of the localization of the sources of human and material resources. Foreign firms bring to the consortium a high level of expertise in financial, technological and managing terms (Raftery *et al.*, 1998).

The Spanish market is pointed out as a good example of this situation. The strong protectionism and association which characterizes the Spanish construction sector makes it difficult for a foreign firm to operate in that market. That is why, until today, the Group considers that it still has not made works of reference, in the construction sector in Spain. It points out, as a possible cause, the fact of not being able to create a consortium with Spanish firms for work contracts.

The interference of the State in this sector is high. In previous studies various legal barriers imposed by some Governments to the entrance of international construction firms were identified. Very often, the Governments support the local firms in prejudice of international constructors. They stipulate that the project must be finished by a national contractor. The incompatibility of the technical standards in the different countries is another difficulty faced by construction firms operating at an international level (Whitla *et al.*, 2006). Thus, even if the Group has small aversion to risk and the necessary investment to start a certain project, so that it does not feel the need to start a cooperation process, the barriers to entrance raised by the Government and by local firms, often, make a consortium as the only method to enter in those markets.

Conclusion

Main assessments

At a scientific level, our study contributes to enlarge the knowledge of an entry mode which seems poorly explored in terms of international business literature. Our study contributes also to understand the motives and benefits which induce firms to choose the consortium. Thus, it makes possible a more complete characterization of this entry mode.

The analysis framework of the consortium, suggested in this study, may contribute to the assessment the performance of this internationalization tool. The confrontation between the motivations which lead to internationalization and the gaps that the consortium intends to compensate makes it possible to infer about the usefulness and suitability of this entry mode under certain circumstances. This fact makes the consortium the only way a firm has to carry out certain internationalization strategies. Factors such as investment, risk, flexibility, dimension and barriers to entrance work as a motivation to the creation of consortia. They are related to the characteristics of the project, market and firm, according to the diagram in Figure 3.

In a consortium, firms:

- are able to reduce the **risk** inherent to projects and international markets;
- get the necessary **investment** for internationalization;
- guarantee some **flexibility** for decision-making in a environment of great uncertainty and constant change, such as the international markets;
- can create **dimension** indispensable to win work contracts and execute of large projects;
- surpass the **barriers to entrance** created by the host country Government and by the association of local contractors which obstruct foreign activities.

Figure 3 – Framework for the analysis of consortia

WHAT?

PROJECT / WORK

* High **risk** associated
* Necessity of large **investment**
* Project of large **dimension**

WHO?

FIRM

* **Risk** management
* Immediate availability of resources
* Restrictions to **investment**
* Desirable level of control implies a type of cooperation with **flexibility**
* **Dimension** of the firm is not always enough to carry out the project/work
* Subjected to the **barriers to entrance** imposed to foreign investment in many countries

WHERE?

INTERNATIONAL MARKET

* High **risk**
* Strong **barriers to entrance** created by the host country Government and by the association of local contractors
* Fierce competition between international players.

HOW?

CONSORTIUM

Risk	* **Risk** sharing through **cooperation**
Investment	* Way to access **resources** of other firms * Complementing the **resources** between the members of consortium → attainment of the total **investment** necessary for a certain project.
Flexibility	* It does not require the investment of capital between the parts to create a separate entity → **more flexibility** in **decision-making**. * **Easy dissolution** of cooperation after the execution of the intended purpose
Dimension	* Reach the **needed conjoint dimension** to win work contract and carry out large construction projects
Barriers to entrance	* **Association with local firms**, in consortia, allows: privileged position and knowledge of markets, **surpass** the **barriers to entry**

As an entry mode, the consortium allows for internationalization as a tool to adjust the firm to the internal and external condition of its expansion to new markets. This fact may present an important implication of this study at the management level. According to this perspective, this entry mode may work as a solution for the problems that, many times, managers come across. It can be included in the strategic consideration carried out when is outlined the international activity of the firm. Often, firms put aside certain projects and markets because they do not think they have the strength needed to resolve their weaknesses and to surpass the characteristic threats of doing business internationally. Instead of that, firms must perceive the consortium as a way to access new opportunities which they encounter on a daily basis.

Limitations and suggestions for future research

One of the limitations of our study is related to the methodological option of the case study. The choice of a single case design, may jeopardize the potentialities of an analytical generalization, given the characteristics of the firm studied. However, we think the choice of Mota-Engil allowed us to develop a suitable case, because it answers the research question and it is understandable. The sample selected for interviews could have been larger, giving, therefore, more robustness in terms of quantitative representativeness. The purpose of this project focused on the attainment of interviews to the point of saturation. From that time on the data to assemble no longer added any value to the investigation. So, we think that the qualitative representativeness is accomplished, and the interviews carried out gave rich information. Interviews also allowed the perception of the agreement between interviewers in relation to the issues questioned.

The enlargement of this investigation to other representative cases studding the same problems constitutes a suggestion for future works. This may fulfill the gap in representativeness, as expressed before. We can compare the results obtained in this study and get a possible corroboration of the same with the inclusion of different firm-related realities. The enrichment of the conclusions taken from this study can also be obtained through confirmation in firms that perform in similar contexts, in terms of international activity. Another issue that might work as a starting point for future studies is the comparison of strategies adopted by national construction firms, in terms of entry mode, with the options at that level by foreign firms. It will be interesting to inquire how often the option for consortium is presented to international construction firms. It is also suggested to analyze the similarities of motivations and circumstances which lead these firms to the choice of consortium, as an international strategy, compared to the results of the analysis carried out in this study. To infer about the importance that each motivation, individually, has at the moment of choosing the entry mode, can be another point open to future research.

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