UNIVERSITI PUTRA MALAYSIA

A CASE STUDY ON KELANG PORT MANAGEMENT SDN. BHD SETTING UP ITS FIRST JOINT VENTURE SUBSIDIARY COMPANY IN CAMBODIA

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CAUTION

Information relevant to Kelang Port Management Sdn. Bhd. as contained in this case-study is solely for the purpose of this study and is not intended to be quoted, used or publised elsewhere in order to maintain confidentiality of contents.

KELANG PORT MANAGEMENT SDN. BHD.

SETTING UP ITS FIRST JOINT-VENTURE SUBSIDIARY COMPANY IN CAMBODIA

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PART 1 : CASE

1. INTRODUCTION

Halim Harun, the Chief Executive Officer of Kelang Port Management (KPM) was very happy when he left the Board Room one evening in late June 1997, noted his Personal Assistant. What pleased him was not the number of papers approved by the Board on that day but that the Directors did not reject his proposal paper to set-up a joint-venture subsidiary company in Cambodia. According to Halim, KPM's proposal was to manage and operate the Inland Port in Phnom Penh on a joint-venture basis with a local partner.

"We cannot allow this special project to fail and let our company down. The Board members, shareholders and employees of KPM are watching as this is our first joint-venture project abroad." Halim was quoted as saying at a luncheon gathering attended by Team members Osman Long, the Corporate Manager, Dennis Wong the Operations Manager and Gopal Krishnan the Finance Manager. *"Our company has performed above expectation in Port Klang since privatisation. It's time we venture abroad. The project in Cambodia is a new challenge to KPM and to all of us"* he added.

Ten days later, a bloody coup d'etat erupted in Phnom Penh. Prince Ranariddh the first Prime Minister was effectively ousted after the weekend clashes that took place on 5 and 6 July between his troops and those of Hun Sen, the second Prime Minister.

On Monday 7 July, Halim convened an emergency meeting and summoned all members of the project team to attend.

Halim : *"The political situation in Cambodia is critical. There is a mass exodus of foreign investors from Phnom Penh due to the civil war. We have to report back to the Board within three weeks our next course of action. Do we want to call off the project?...........or put it on hold?........or go elsewhere and invest?."*

Osman : *"I propose we buy time by putting the project on hold. We will go in when the situation returns to normal. This way it will not cost us a cent if the offer is not taken up eventually."*

Gopal : *" Why not we call off the project and go elsewhere to invest. Our shareholders will certainly not want us to commit our investments in a politically unstable environment."*

Wong : *"Please don't call off the project just like that. We spent three months of hard work on this project. Remember if this joint-*

venture works, it will be a springboard for KPM to negotiate and bid for the main dish........that is the privatisation of the Port of Sihanoukville. Our local partner Ly Khieng Say is very influential...........and the port-related opportunities are vast in Cambodia."

The disturbance in Cambodia caused at least US$ 76 million in damage to business in Phnom Penh alone. The Cambodian government gave some assurance that foreign investors who incurred losses as a result of looting and arson would be compensated. It was not clear however how the cash-strapped Cambodian Government which depended upon foreign aid for at least 60 per cent of its budget, would find the money. Some major donors such as the United States had temporary halted aid to Cambodian became of the coup.

President of the Malaysia Business Council in Cambodia Chris Ho Yee Kong said that the fighting and its costs would not impact Malaysia's investment plans in Cambodia. ***"We have 300 Malaysian Companies in Cambodia which have pledged about US$5 billion over the next five years."*** He said in an interview with the New Straits Times.

2. COMPANY BACKGROUND OF KELANG PORT MANAGEMENT SDN. BHD

Kelang Port Management (KPM) was a consortium comprising Kontena Nasional Bhd with 52.5% equity participation, Malaysian International Shipping Corporation 25%, Selangor State Government 12.5% and the Pilgrim Fund Board 10%. The company took over the port operation from the Klang Port Authority (KPA) on December 1 1992.

Under the privatisation agreement with KPA, the company was given a 21 years lease to operate two gateways namely North Port and South Port and a dockyard. North Port and South Port had 22 berths with a total quay length of nearly four kilometres for container, breakbulk, drybulk and liquid bulk operations.

Facilities at Klang Port Container Terminal (KPCT) comprised five berths, seven quay cranes, 13 rubber-tyred gantry cranes and 20 straddle carriers. Storage facilities included a 24 hectares container yard with an annual capacity of 700,000 teus and three Container Freight Stations with a total area of 20,000 sq. meters.

Non-container facilities in North Port comprised five breakbulk berths and two berths each for liquid bulk and dry bulk cargo. There were eight multipurpose berths in South Port.

The company's dockyard was the only facility in the Klang Valley with the capability to handle crafts with displacement of up to 450 tonnes. The dockyard had five slipways. *(Appendix 1)*

3. PRINCIPAL BUSINESS

The principal activity of the company was the management of port activities which comprised services rendered to ship, cargo and container handling, rental of port premises, dockyard operations and other ancillary services. KPM also provided a wide range of support services including stevedoring, warehousing, pilotage, fire prevention and water supply to ships.

4. PORT PRIVATISATION

KPM was the successful bidder for the second phase of port privatisation Port Klang in 1992 . Under the terms and conditions of privatisation, KPM was obliged to absorb some 4200 employees serving with the Port Authority while the remaining 85 staff remained behind to serve the regulatory body. After four years the workforce shrank to 3500 as a result of natural attrition arising to be privatised in 1986 as it enjoyed widespread public recognition and confidence and had a good track record of profits to attract private investors.

The other reason to privatise the port operations was that the KPA operating as a government enterprise, did not have the flexibility to manage and operate its facilities on a commercial basis. The administrative and bureaucratic procedures often led to delays in decision-making and project implementation. Such inhibitive procedures did not provide Port Klang the same competitive advantage of a business unit viz a viz the other successful international seaports like the ones in Hong Kong, Singapore, Taiwan, South Korea and Japan.

It was also reasoned out that port privatisation would bring about considerable improvement in efficiencies and performances resulting in lower operating costs, higher throughput and therefore also more tax receipts to the government.

5. MISSION STATEMENT

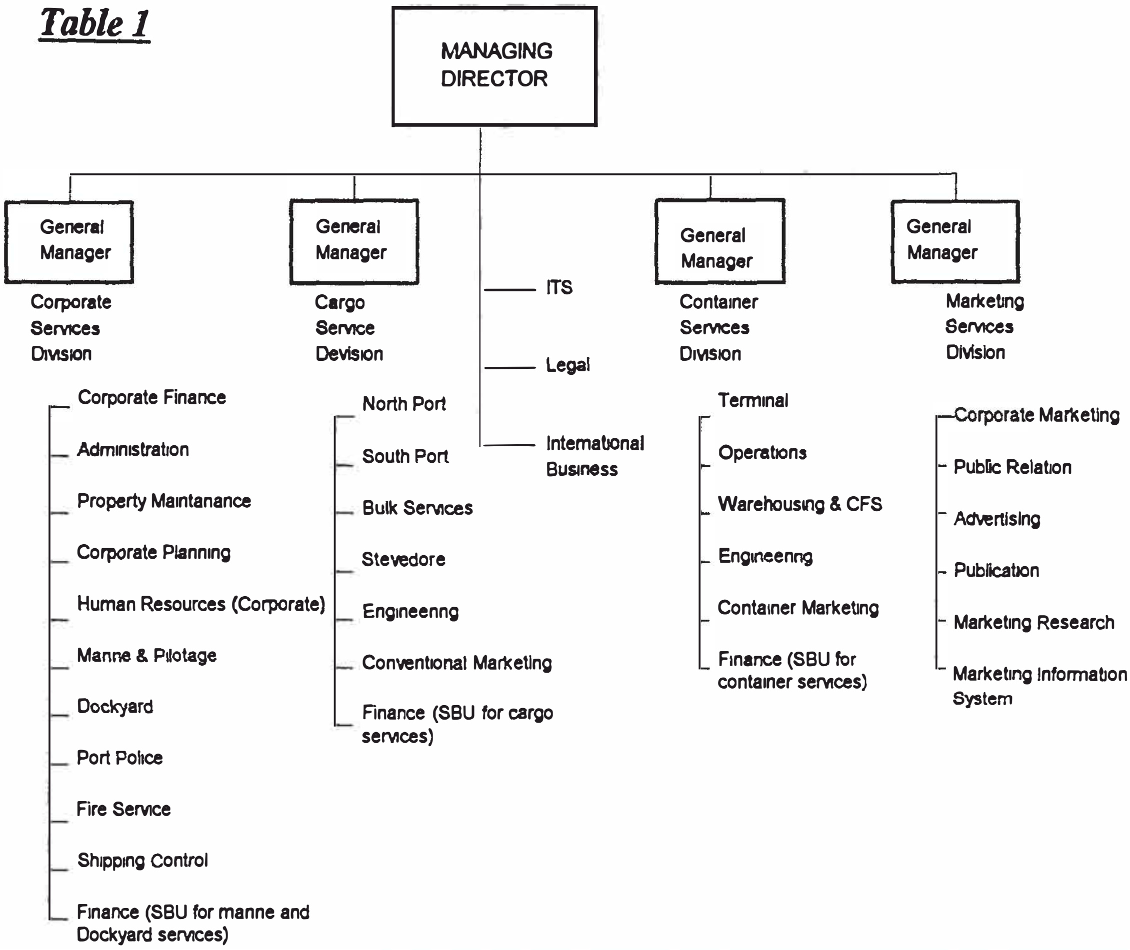
"The mission statement of KPM was to participate and contribute to the nation's growth by providing port users value for money services through dedicated and empowered people who constantly innovate and employ systems which are simple and measurable and in the process earn a reasonable return for its share holders."

Judging by the company's achievements over its four years of history, it was evident that the management and staff of KPM had succeeded in their mission and the results was more than hoped for.

6. ORGANISATIONAL STRUCTURE

KPM introduced the strategic business unit (SBU)* concept for its revenue generating Departments . Each SBU was required to develop and operate its own business plan as a profit centre in line with the company's objectives. The existing SBUs were the Cargo Services, Container Services, Marine Services and Dockyard Services Departments. ***Table 1*** showed the organisational structure and chain of command that ultimately linked each employee with the top organisational position as practised in KPM .

Table 1



* *Micheal E Porter-Most firm have divided their business into some types of strategic business units (SBUs), and instituted formal planning processes in which SBUs submit plans for review top management on annual or biannual basis.*

7. ACHIEVEMENTS SINCE PRIVATISATION

Since privatisation, there had been a new 'can-do' spirit in KPM. There was a change in attitude, a willingness to test one's capability and to dare challenge the fundamentals. The result was a stream of exciting happenings - from new records in cargo-handling performance to new ideas and innovations powered by the desire to excel. Some of the achievements by KPM since privatisation between 1992 - 1994 period included improvements in ship turnround time by 27%, total cargo throughput handled was up 23%, number of ships 40% and gang productivity 41%. Also the tonnage per employee increased by 46% and revenue per employee soared 49%. The stevedore attendance rate improved from 79% to 97% during the period under study. *(Appendix 2)*

Shippers' Weekly, a leading local transport periodical issued a special supplement to commensurate the third anniverssary of KPM in December 1995.

"The fact that KPM has been making progress year after year in terms of operational and financial performances bear testimony that the government privatisation of port services was indeed the right decision. As global trade becomes more sophisticated and demanding, it is only natural that the role of ports has also become increasingly challenging and complex.

However, I am confident that KPM working in tandem with all sectors of Port Klang community will continue to play a dynamic role in realising the government's vision of making Port Klang the load centre for the region."

This was the message from the Minister of transport Malaysia, Dato' Seri Dr. Ling Liong Sik. *(Appendix 3)*

8. OPERATIONAL PERFORMANCE

KPM recorded dramatic growth rates in terms of total cargo throughput since 1993. The company handled 20.7 million freightweight tonnes of cargo in 1996 compared to 13 million in 1993 as reflected in ***Table 2***. Total container throughput increased from 12,650 teus handled in 1993 to 443,700 teus on 1996. The projection for 1997 is 620,000 teus and 1,000,000 teus by the year 2000. The good performance achieved by KPM was fuelled by the buoyant economic growth of the country with GDP maintaining at over 8% per annum, a market-driven workforce and an increase in the international transhipment and redistribution activities at the port.

Table 2

CARGO THROUGHPUT 1993 TO 1996 (FWT)

YEAR	1993	1994	1995	1996
Import	9068278	10170081	11761743	13230717
Export	4007145	5207360	6675403	7543039
Total	13075423	15377441	18437146	20773756
Annual Growth Rate	-	17.6 %	19.9 %	+12.7 %

Source: KPM Annual Reports

9. FINANCIAL PERFORMANCE

For the financial year ended 31 December 1996, turnover increased by 10.1% from RM 258 million in 1995 to RM 285 million in 1996. Profit before tax improved from RM77 million in 1995 to RM83 million in 1996. This was attributed to increase volume of cargo handled and higher productivity . The tonnage handled per employee was 492 tonnes in 1996 compared with to 276 tonnes in 1993. The company's annual turnover and profit and loss before tax statements had recorded dramatic improvements since 1993 as reflected in ***Table 3.***

Table 3

PROFIT AND LOSS ACCOUNTS 1993 TO 1996

	1993	1994	1995	1996
1. Turnover	163,669,407	205,677,745	258,966,640	285,166,729
2. Profit/(Loss) before Taxation	(3,968,298)	14,879,739	77,380,127	83,334,974
3. Taxation	(5,496,000)	(10,038,000)	(28,920,000)	(30,880,000)
4. Profit/(Loss) after Taxation but before extra ordinary item.	(9,464,298)	4,841,739	48,460,127	52,454,974
5. Extra ordinary item	3,274,491	-	-	-
6. Sub-total	(6,189,807)	4,841,739	48,461,127	52,454,974
7. Dividend	-	-	-	(23,766,435)
8. Accumulated Profit(losses) brought forward	(1,162,651)	(7,352,458)	(25,107,19)	28,688,539 45,949,408
9. Accumulated Profit(Losses) carried forward	(7,352,458)	(2,510,719)	45,949,408	74,637,947

Source: KPM Annual Report

10. WHY GO GLOBAL

KPM's intention to set up its first joint-venture subsidiary company abroad was consistent with Government's policy to encourage more Malaysian-based companies to go international and to tap the vast opportunities in the overseas market. Since taking over the port operations from KPA in 1993, the company had performed remarkable well. KPM had the financial and human resources and expertise to explore the possibility of internationalising its business. Many of its executives with vast experience in the field of port operations and management were trained a broad at the various ports and shipping institutions and universities in the Netherlands, United Kingdom, France, Sweden, Japan and Singapore. In fact some of its executives also worked as Port experts on part-time basis for certain approved port projects for the World Bank, ESCAP, JICA and other agencies of the United Nations when they were attached to the Port Authority.

Another reason for KPM to go global was that competition within the three port operating companies in Port Klang was getting intense. Besides the company would enter into the maturity phase of its life-cycle over the next few years. It was therefore a perfect time now to venture abroad.

Global companies such as Motorola, Avon and Johnson & Johnson to name a few, generated more than 50 percent of their annual profits from sales of products in the foreign markets. KPM should emulate their performance as domestic markets were getting smaller and competitive. More and more international companies now looked beyond their national boundaries to exploit the vast business potentials and opportunities available in the global market place. The gradual dismantling of the tariff and non-tariff barriers as advocated by World Trade Organisation (WTO) also helped to create a freer and more transparent global trading environment.

The idea of globalisation had also caught up with many Malaysian companies in recent years with the government providing the encouragement, the incentives and the netwrok connections to promote off-shore investments and manufacturing abroad.

11. GLOBAL MARKET-ENTRY STRATEGIES

When KPM decided to go international, it had to decide the best way to enter a foreign market and the degree of involvement and commitment it was prepared to make. There were a variety of foreign market entry strategies from which the company could choose. Each had its own advantages and disadvantages depending on the company's strengths and weaknesses and the degree of commitment and risks it could take.

* **Exporting**

- common approach to foreign market development
- minimise financial risk by serving the global market

* **Licensing**

- a means of establishing a foothold in foreign markets without large capital market.
- overcome import restrictions licences granted for production, use of trade names, distribution channels.

* **Joint Ventures (JV)**

- collaborative relationships
- lessens political risks, economic risk
- use of local skills, distributors, channels (use JV for internal bids/contract job)

* **Manufacturing**

- lower labour cost
- avoid high import duties
- reduce transportation
- access to raw material
- way to gain market entry

* **Franchising**

- a form of licensing
- franchiser provides a standard products, systems and management services.
- franchisee provides market knowledge, capital and personal involvement in management.

In the case of KPM, the most appropriate global market -entry strategy would be joint-ventureship with reliable local partners in Cambodia. This was by virtue of the nature of business it was currently involved in. The type or the core business for KPM to participate in would be in port-related, transport, warehousing and shipping activities.

Joint ventures, one of the more important types of collaborate relationships, had accelerated sharply during the past 20 years. Besides serving as a means of lessening political and economic risks by the account of the partner's contributions to the venture, joint-ventures provided a less-risky way to enter markets that posed legal and cultural barriers than would be the case in an acquisition of an existing company in Cambodia.

12. COMPANY BACKGROUND OF MENG SENG PTE. LTD.

MSE was established in 1970 and resumed in operation in Phnom Penh operations after the political upheavals in 1986. Following the implementation of the Paris Peace Accord in 1992, MSE was appointed as the freight forwarder for the United Nations Peace-keeping Force in Cambodia to handle all its logistic functions. Equipped with modern telecommunications facilities, MSE maintained a headquarters in Phnom Penh and a branch office in Sihanoukville Port.

MSE currently managed operating the Inland Port as a monopoly. The company which had been granted the licence to operate Inland Port in Cambodia was officially opened in July 1996 by the Second Prime Minister Hun Sen. This was certainly a credential for its strong existence in the industry.

MSE had also been appointed by Regional Container line (RCL), Mitsui/Hapag Lloyd, Heung-A Line, American President Line (APL) and American Consolidation Services (ACS) as their shipping and forwarding agent. Such appointments had certainly improved on MSE networking capabilities to ensure the success of the Inland Port operations.

Besides the above, MSE was also given the concession to manage and operate the Phnom Penh By-pass road by the Cambodian Government. The By-pass road meant for heavy vehicles (including container trailers) to and from Phnom Penh passed in front of the Inland Port Complex making it more convenient for import and export cargo clearance This By-pass road project was a joint-venture business between MSE and DKLS, a Malaysian company listed on the Second Board of Kuala Lumpur Stock Exchange (KLSE).

(i) <u>Offer For Warehouse Rental at the Inland Port</u>

ACS, one of the main freight forwarder currently operating in the Port of Sihanoukville, had proposed to lease the warehouse at the Inland Port for value-adding activities. The proposal had since been left in abeyance, as MSE saw that such arrangement would not only siphon out its profit but would also negate the transfer of technology to the locals. MSE wanted the joint-venture company MSE/KPM to manage and operate the warehouse instead of leasing it out to third party

(ii) <u>Investment Incentives</u>

The Cambodian Government also offered attractive incentives to foreign investors which were beneficial to KPM and to its local partner MSE.

- 9% corporate income tax

- 8 years corporate tax holidays for certain industries
- 5 years tax losses may be carried forward
- 100% import duty exemption for export-oriented projects
- no restriction on repatriation of capital profits
- profits which are reinvested are fully exempted from tax.

Since June 1994, Cambodia had attracted over US$2 in foreign investment with Malaysian investors held in high esteem owing to the large number of strategic projects as shown in ***Appendix 4***.

13. KPM FIRST JOINT-VENTURE BUSINESS IN CAMBODIA

KPM was invited by Meng Seng Express Pte. Ltd. (MSE) to set up a joint-venture company to operate and manage an exisiting Inland Port in Cambodia. The role of KPM in the joint-venture Company (JVC) would be to provide a management contract to manage, operate and further develop the warehouse logistics and container yard operations at the Inland Port in Phnom Penh. KPM had the necessary expertise and resources to take up an equity share in this port-related business.

As a one-stop centre, the Inland Port offered its customers a package of services. This included inland trucking services, container storage, bonded warehousing, value-adding, container inspection and repairs, reefer operations,