CHAPTER 4
BUSINESS STRATEGY LEVEL

4.1 INTRODUCTION - THE HOME OWNERSHIP CAMPAIGN

The financial crisis in year 1997 - 1998 has resulted an overhang of RM 80 billion in property in the country. This is accordance to a report submitted by developers to National Economic Action Council (NEAC). (The Star, December 13 1998). This is a worry as the collapse of the property market would be a disaster for the economy. Therefore, the Government would have to first revive the share market, and stabilize the ringgit later and followed by stimulating the property sector next. With this the Government has proposed and organized a grand property fair in December 1998 and October 1999 as another move to revive the nation economy. In this fair, people would be given wide choices (models and plans) for viewing, comparison and advice to enable them to make a decision in purchasing a property. This campaign is a joint effort between the Government and private sector to revive the property section and the economy. It is called the 'Home Ownership Campaign'.

In this campaign, there are various incentives provided by various sector to encourage the transaction for properties. They are namely:-

i. Government incentives

a. Stamp duty waiver on SPA, transfer of property and loan documentation.

b. EPF withdrawal: Instant issuance of structured certificate on eligibility status of depositors.

c. Treasury Housing Loans (THL): Instant confirmation on eligibility of government officials to obtain THL; speedier approval and release of loans; government servants with minimum of one year service record are eligible to apply for THL; no minimum age and waiver of processing fee.

d. Purchase of properties by non-residents: For the first time there will be no restriction on properties costing more than RM 250,000 (discounted price). Restriction on properties below RM 250,00 still applies.

e. Up to 50% margin of financing from Malaysian banks for non-residents' abroad and blanket approval from FIC.

f. Automated release for bumiputra quotas for HOC1 and not applicable for HOC2.

ii. Housing Developers' incentives.

a. Properties costing RM 100,000 and below: Minimum 5% discount. An additional 5% discount for bumiputras.

b. Properties costing between RM 100,000 and RM 200,000: Minimum 10% discount. An additional 5% discount for bumiputras.

c. Properties costing more than RM 200,000: Minimum 10% discount. Another 10% discount for bumiputras.

iii. Financing institutions' incentives

a. Financing margin: RM 250,000 and below (up to 95%); RM 250,000 to RM 500,000 (up to 80%) and from RM 500,00 (up to 70%).

b. Lending interest rates: RM 100,000 and below (9%pa or BLR + 1.75% pa whichever is lower); RM 100,000 to RM 250,000 (BLR + 0% for the 1st two years and BLR + 1.5% thereafter (bumiputras) and BLR +0% in the first year and BLR + 1.5% thereafter (non-bumiputras).

c. Tenure up to 3- years.

iv. Fees and Charges

1. Processing fee is waived and legal fees on loan agreement shall be charged at the same rate as the SPA which range from RM 120 (flat) for properties costing RM 30,000 and below to RM 4,000 (flat) for those costing RM 1,000,000 or more.

v. Insurance

10% discount on MRTA insurance premiums, 25% discount on fire insurance and RM 10,000 PA coverage.

The results of the two Home Ownership Campaign were attached at the table enclosed.

In the HOC1, the results of this fair are as follows.

Table 6: Participants for HOC1

PARTICIPANTS IN THE HOME OWNERSHIP CAMPAIGN*

			Property Types**		
	No of participants	**No of projects**	**Terrace**	**Apartment/ Condominium**	**Shopoffice/ shophouse**
Selangor	75	100	40	42	27
Johor	58	66	41	20	29
Malacca	51	70	46	10	28
Penang	37	47	11	25	14
Kuala Lumpur	31	38	2	29	4
Negeri Sembilan	21	25	13	10	8
Kedah	13	23	8	-	16
Perak	8	8	2	2	2
Pahang	9	11	6	3	4
Terengganu	3	3	2	-	3
Kelantan	1	1	1	-	-
Sarawak	1	1	-	1	-

Table 7: Results of HOC1

DEAL CLOSED		
Total participating developers	492	
Total units offered	42,906	
Total estimated value	RM 12,150,867,280	
State	**No. of units**	**Total value (RM)**
Kedah/ Perlis	423	80,428,251
Penang	1,317	262,617,415
Perak	337	48,723,231
KL/ Selangor	5,832	2,070,110,035
Negeri Sembilan	429	51,631,453
Malacca	1,924	450,000,000
Johor	3,660	755,920,000
Pahang	474	65,879,497
Terengganu	23	6,242,128
Kelantan	23	885,445
TOTAL	**14452**	**3,791,807,455**

Source: The Star, 15 January 1999

SUPPLY AND SALES AS AT DEC 14,1999

Table 8: Results of HOC 2

		SUPPLY		*SALE*
STATE	*UNITS*	*VALUE (RM mil)*	*UNITS*	*VALUE (RM mil)*
Kedah	,461	496.7	970	102.2
Penang	,748	856.1	1,188	217.5
Perak	35	48.3	49	18.9
Selangor/ Kuala Lumpur	5,972	3,547.5	6,702	987.3
Negeri Sembilan	,980	648.8	924	100.0
Malacca	,108	565.6	1,328	145.7
Johor	,699	3,266.8	3,385	656.1
Pahang	,274	180.6	96	11.0
Terenganu/ Kelantan	12	5.0	36	0.4
Labuan	7	3.7	0	0.0
Sarawak	,688	69.6	330	1.9
Sabah	,201	566.7	1,328	160.7
TOTAL	0,135	10,253.4	16,336	2,401.7

4.2 STRATEGIES ADOPTED BY THE COMPANY

4.2.1 INTRODUCTION AND DEFINITION

The company has determined four criteria as the basis of its strategies to be deployed during the crisis, namely: -

i. Revenue
ii. Quality
iii. Delivery
iv. Flexibility

Further elaboration of the four criteria mentioned above are as follows: -

a. Revenue

Revenue is defined as selling price of the property developed for sale. The total amount of revenue will be the accumulated sales from all the property units. In the event of low revenue, it implies that the selling price is low but it would still be acceptable if the revenue is above the total cost required to complete the units. It is still profitable but the returns may be lower.

The construction cost of the units is governed by parameters such as location; the unit built up area and the finishes provided. Location costing would be based on the total land cost valued at current price – which is the sum of the initial purchase price and all the other holding costs such as interest, land use conversion premium, administrative cost and other miscellaneous costs OR the current professional valuation, whichever is lower. The total land cost divided by the number of units would be the land cost per unit.

b. Quality

The concept of quality used in this context can be viewed from two aspects: -

i. Process quality, and

ii. Product quality.

Process quality is defined as doing things right the first and every time so that the end product is free from any deficiency, possibly achieving the ultimate objective of zero defect. In ensuring process quality, the company is concerned about how to build the property units so that each and every individual purchaser can be really satisfied with the unit that is handed over to them upon completion. On the other hand, product quality is defined as the types of finishes provided to the unit under construction – for instance a house furnished with ceramic tiles or first grade slab marble obviously is perceived as of higher quality than one which is only cement rendered.

c. Delivery

Delivery relates to the completion time of a housing unit. The Housing Developer Act defines delivery as handing over of constructed units to the purchasers for vacant possession upon the issuance of Certificate of Practical Completion. In fact this provision is considered not good enough in protecting the interests of the house buyers as it still does not mean that the buyers who have taken delivery of the units will be able to stay or put up the units for rent. Delivery in this context of study will be the completion of the units with the issuance of at least a temporary Certificate of Fitness that enable the connection of utility infrastructure such as the supply of water and electricity to the units.

d. Flexibility

This criterion indicates how flexible a property developer is in assisting a purchaser to own his choice unit. The developer can exercise such flexibility in various ways, such as: -

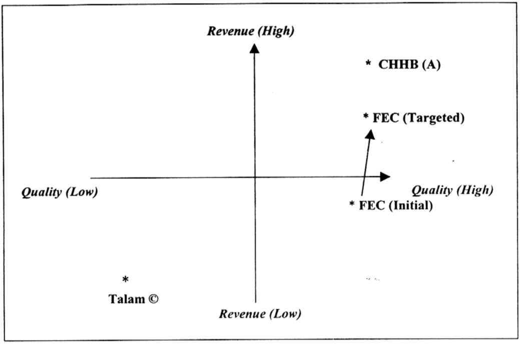
i. allowing easier term for down payment when prospective buyer make a booking;
ii. arranging one stop counters for the end financiers to meet house buyers;
iii. Assisting house buyers in their application for partial withdrawal from the Employees' Provident Fund as this is another source of financing the purchase of a property.

A property developer can also initiate other mode of flexibility such as allowing the buyers in upgrading their units during the course of construction. This indirectly helps the property buyers in expediting the completion of their units to their satisfactory. There are individual taste and preferences, which at times dictate the addition of electrical points, upgrading the finishes of the bathroom with beautiful ceramic tiles from 5 feet to full ceiling height.

4.2.2 REVENUE VS QUALITY

The 4 criteria mentioned above are the parameters that were studied by the company in positioning themselves against their competitors in the market. The first two criteria used are Revenue vs. Quality.

Figure 2: Revenue Vs Quality



A developer can position itself against its competitors based on the two parameters on the X-axis and Y - axis. A high end product developer like Country Heights Holdings Berhad (CHHB) chose to position itself at point A in Figure 2. This means that CHHB concentrates mostly on building high quality houses and sells them at high prices. This is very obvious as reflected by the properties developed in Country Heights and College Heights. The bungalow lots are now trading at a region of RM 50 to RM 90 per square feet. This range of prices for bungalow lots is rather high as compared to some bungalow lots that can be bought from some other areas that are much nearer to Kuala Lumpur. However, there are still people who are willing to purchase them because the standards of quality set by CHHB are rather high. The environment created by the soft landscape as well as tight security has attracted many high net worth purchasers whose presence in turn becomes another key selling point that motivates similar category of buyers who seek to be in the neighbourhood of this range of rich people.

On the other extreme end, one can take a look at point C. An example of such company would probably be the Talam Group (Talam). They have positioned themselves at the end of low quality with low selling price. The properties completed by Talam at Pandan Jaya area whereby the selling price was in the region of RM 110,000. Their development project at Bukit Beruntung near Serendah (60 km north of Kuala Lumpur) also portrays similar characteristic and image. This company targets at the segment of customers who would go for affordability rather than good quality at high selling price.

Far East Consortium Malaysia (FEC (M) Ltd.) can be classified as another category of property developer, which chose to emplace itself as builder of high quality property units with medium range of selling prices. This can be seen through its projects that were completed prior to 1996. For example, Puncak Prima is a luxurious condominium with full facilities situated at prime location in Sri Hartamas when it was first launch in the beginning of 1995, with selling price set at RM 240 per sq feet. At that time our competitors was Sunrise which sells their fully completed units at Mont Kiara in the region of RM 280 to RM 300 per square feet. If one were to factor in the element of capital cost into our project based on 10% at that time with anticipated completion period of 2 years, the ultimate selling price by the completion date would be RM 264 per square feet, which is still lower than the units sold at Mont Kiara then.

Despite adopting a slightly lower pricing strategy, FEC (M) Ltd. did not compromise on the quality and delivery date line of its products. Even during the height of financial crisis in 1997/98, when the general expectation was for a softer property market with perhaps low entry cost, the company persevered and switched to the strategy of selling properties under development at even much lower prices while still adheres to maintaining high quality product. In order to achieve this, the company has explored various ways of reducing the cost of running the business with the objective of achieving the targeted reduced selling price. Such strategy would involve reviewing on the following aspects of the business.

i. Tenders

We formed a strong Tender Committee, which consists of an Architect, Engineer, Accountant and Quantity Surveyor. This Committee is empowered to call for tenders from a group of pre-qualified contractors consisting of big contractors, medium size contractors and small size contractors. After evaluating the tender documents, we would be able to compare the costing of each individual contractor on each element in the Bills of Quantities Contract. From here we analyze how one cost would deviate from another.

Based on the costing, the Tender Committee would be able to know where is the major cost that is going to be incurred. With this insight we can concentrate on how to overcome the problem in a much-focused manner. For example, a condominium was designed on the basis that its units sit on top of two floors of car park. No doubt that this would be the best scenario in terms of selling but however it will be expensive as this will incur transfer to the slabs which would result in higher cost. It may be more prudent to put a separate car park block to avoid this transfer beam to reduce the cost as the selling price is more governed by the market perception more than the concept. This can be illustrated that residential units in a 10 storey-condominium in Cheras were sold for less than RM 150,000 each. On the contrary, incorporating car parking bays underneath the condominium building may not warrant a corresponding increase of the selling price to above RM 150,000.

Preliminary mark ups for the big time contractors are normally higher than the small time contractors. This is probably due to their higher overhead. However in terms of pricing on individual items such as formwork, reinforcement and concrete, there is a big possibility that the big time contractors would have a better pricing due to their credibility in obtaining good price and credit limit from their suppliers.

ii. Alternative design

The business environment is changing and becoming more competitive. House Purchasers are getting smarter each day, as they now know more about their rights and entitlement. However, construction cost is becoming more expensive as material and interest cost escalated due to Ringgit weakening against foreign exchange rate and the financial crisis. The negative effects on business during such turbulent times caused considerable erosion of sales revenue but increases in construction cost. In order to combat the erosion to the bottom line, the Tender Committee looks for alternative methods of construction that are available in the market that may reduce the cost of construction while simultaneously increase the speed of completion. One of the alternative methods adopted was the usage of half tunnel form.

iii. Management of debts.

During the last financial crisis, it was noted that there were many engineering consultants in the market, which was manned with minimum staff in their offices. Even though they have managed to secure much works to keep them occupied, but most of them faced the collection problem. It was rather ironical that some property developers despite having sufficient funds at their disposal instead abused the national financial crisis as an excuse in delaying payment to the consultants and contractors. This was self-defeating as it worsened the business environment unnecessarily.

Our company, the FEC (M) Ltd. adopts ethical management practices even in the height of the financial crisis. All consultation fees would be awarded on the basis of success. This means that all the consultants would have to produce plans, which were submitted to the various authorities for approval without billing us their cost. Upon approval and launching of products in the market, the first collection was used to pay the respective consultants. In other words, we succeeded in convincing the respective consultants to ride along with us in our property development venture. All the parties involved thus shared the carrying cost. This created a win-win situation because in the view of a consultant, any work available during the crisis would help them maintain a minimum staffing in their office. If they were choosy of their clients during the crisis, it would be highly probable that property developers will reject them when the economy recovers. Most consultants are fully aware of their positions and were readily accommodative to the developers' request as they have to service minimum overhead and its only logical for them to ride along with the developers. As for the developer, such arrangement enable them to reduce operating cost upfront until their housing development projects are successfully marketed. Hence this symbiotic relationship would reduce their risk.

iv. Management of cash flow

Part of our strategy during the crisis was to minimize risk by reducing cash outflow unless and until the project is successful launched. The down payment for a particular unit to be sold to a purchaser is rather rigid in our policy. This is because we do not wish to place the company under cash flow problem. By virtue of having high down payment would mean that the purchasers are genuine purchasers. They have to think twice before placing their money for booking a unit or risking it from being forfeited. There are certain purchasers that may have paid low down payment like RM 500 only. If he has second thought about the unit booked earlier, this purchaser may be willing to let the developer forfeit the RM 500 if he fails to find another buyer to replace him as a buyer. However to the developer the time wasted to get the purchaser to sign the agreement followed by time taken to terminate them would generally disturb the efficient management of sales and the cash flow as well. This is because upon selling, the developer will continue to build with the hope that when they complete to a certain stage of development, the company can claim for progressive payment from the purchasers and thus enhancing its cash flow.

Furthermore, construction work is carried out for those units sold with the expectation that that billing for payment can be made according to the schedule for payment as specified in the sales and purchase agreement. In the case of building double-storey link houses, upon the completion of structural works, the billing is 10% and the next stage would be for brickwork. We will not start on the brick works unless and until we have completed the structure for the whole block. This is in fact against the general construction sequence whereby when the contractor has completed the first floor slab and while doing the second floor column, they would continue with their brick-work for the ground floor. In this case it would mean that the developer would have to pay for the brickwork prior to billing the purchasers on the structure. This sequence helps a lot in completing the project as far as possible. During this crisis we concentrated more on flexibility than fast delivery in which it will ease the cash flow.

v. Management of quality

There are many trades involve in the construction of a building. They can be divided into two-section namely:-

a. the nominated subcontracts who are assigned for specialist work like electrical wiring, installation of firefighting equipment, cold water and sanitary plumbing, and lift;

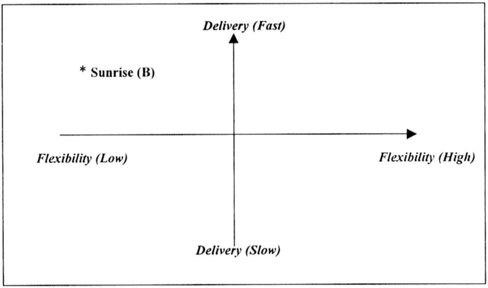
b. the nominated suppliers like tiles, ironmongery, tap fittings etc.

During this crisis, it was more prudent for the developers to buy the goods directly from the suppliers so that they are in control of the quality supplied as well as the supplier when they know that the project has a good sales reference, the possibility of them being paid would be much better as compared to dealing with the contractors.

4.2.3 DELIVERY VS FLEXIBILITY

The second two criteria are delivery Vs flexibility

Figure 3: Delivery Vs Flexibility



Developer such as Sunrise Bhd would probably be placed at point B where its focus is on fast delivery with very little flexibility. They normally deliver ahead of schedule but does allow slight variation by the purchasers such as adding power points or lighting points depending on the range of products. Products like the Sophia Tower allows purchasers to select the range of upgrading works to the unit provided always that the structure and the building plans does not deviate from those approved.

As for initial payment prior to signing sales and purchase agreement, Sunrise collects a minimum amount of RM 5,000. This is rather high because most developers in town allow a minimum booking fee of RM 500 to RM 2,000 only. But however they do have a department specifically assigned to assisting house buyers upon signing the sales and purchase agreement in applying for their housing loans.

Another developer is Talam or Larut Group, which under normal circumstances (before the crisis) tries to complete their product ahead of schedule but gives very low leeway for flexibility. They would concentrate to deliver their products as fast as possible to the customers so that the company can achieve higher turnover. No special effort is attempted to generate better customer's satisfaction such as providing additional services like upgrading their units. They believe that by virtue of completing earlier than the scheduled date, individual purchaser can save on interest payment to end financiers. However, this type of property developers exercise flexibility during acceptance of down payment for booking a unit - they are willing to accept as low as RM 1,000 per unit as booking fees. This flexibility is to facilitate purchasers to commit themselves into signing the Sales and Purchase Agreement.

FEC (M) Ltd. on the other hand would concentrate more in providing flexibility to the purchasers while at the same time still mindful of its obligation to deliver vacant possession according to schedule. The flexibility in this case would be to provide the services of upgrading the electrical packages. Besides this we would also provide free interior designs to those who needs them. We would not sacrifice services to the purchasers and quality of our product against speed. However in the case of flexibility in down payment to book a unit, we believe in at least collecting RM 10,000 or 5% of the sales price per unit whichever is lower.

There are certain reasons for adopting the abovementioned strategy, namely:-

i. Value Added Image

By providing the additional services to purchasers in upgrading their investment with us, we are aiming to create a ?e care' image for the company. Another advantage of upgrading the units during the course of construction is to expedite occupation of the new premises. Our previous experiences indicate that purchasers who are able to occupy their home sooner than expected save a substantial sum from servicing interest on loans - such savings are put to better use in enhancing the value of their respective investment through upgrading. Besides this, it is also good for the company as it is income generating, thus creating a win-win situation for all parties concerned.

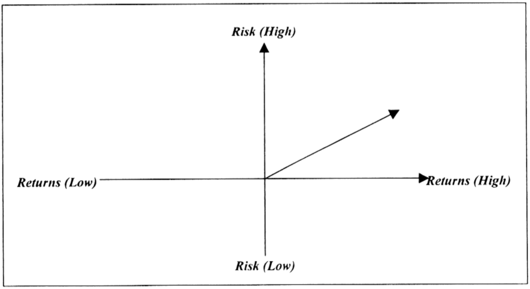
The rates for upgrading were the same as the original contract. Hence it is much cheaper compared to doing it at a later stage with a renovation contractor. Consider for example, addition of lighting points to the units. Under our tender the construction, the cost for a lighting point is approximately RM 38. There are 11 lighting points for each unit and for a condominium block consisting of 500 units, it would mean RM 209,000. In this scenario there is economy of scale but should one request a renovation contractor to add only 3 points per unit, then the charges would probably be RM 90 for each additional electrical point. Other than this cost there could be other charges like hacking and concealing the electrical conduit. Therefore, it is more economical for a purchaser to upgrade their units with us despite the fact we charge him RM 80 per additional electrical point. Any request for upgrading is good for the company as it generates additional cash flow, profits and project the image of a service orientated company; while at the same time the purchasers will save on the cost of renovation and avoiding the trouble of engaging other contractors.

4.2.4 RISK VS RETURNS

In property development or any other businesses, it should be noted that every CEO would like to have maximum returns. However the priority during the year prior to 1996 and the years 1997-1998 were totally different. When the economy was good, employment is high which pushed up labour cost but market demand for properties were high. People were more willing to pay for the properties they like as banks did not impose any restriction on the financing the purchase of houses. During good time like this, developers would go for maximum returns over their cost. However, this is not the situation during the crisis. FEC (M) Ltd. emphasized on taking only low risk.

Although there is a linear correlation between risk and returns but we would emphasize on maximum returns based on the risk factors that we are going into. For example, a housing project in Cheras, the neighbouring houses are two storey link houses and they are transacting at the region of RM 150,000, we would develop a product of two and a half storey with an attic which is a premium over the existing link houses but we would target to sell it at the same price, i.e. RM 150,000. We created a product of value for money. This target segment can only be implemented provided always it is viable. Should it not be viable, we will not pursue further. See Figure 4.

Figure 4: Risk Vs Return



In order to achieve the above objective of having low risk but reasonable returns, the entry cost for a project has to be low. Therefore, for the current land bank that we have, should the land cost is high and make the project not viable then we will not pursue further and will instead concentrate on projects on a joint venture basis. This is where the land cost is minimal. For example, during this crisis we sought out companies that have difficulty servicing bank loans. Loans owed by these companies are on the verge of being categorized as non-performing. In order for these companies to carry on further without increasing its holding cost further or to avoid foreclosure, they have to develop the land in order to service the bank loans. One of the ways is for this type of financially strapped companies to find another stronger organization for joint venture in developing the idle land and subsequently obtain sales proceeds for survival. This is where the joint venture party can come in to put in some working capital to initiate a housing development project. A typical case is a joint venture secured by FEC (M) Ltd.

4.2.5 BUILD-NOW-SELL-LATER

Before I proceed to propose this strategy, the understanding of certain fundamentals has to be reached. What does one mean by the 'built now sell later' concept?

Basically, there are two major interpretations on built now sell later. They are namely:-

i. A Developer cannot sell his property until they are completed and
ii. A Developer can sell his product before or during construction but he can only collect a small deposit from the purchaser. The Developer is not allowed to collect progress payment based on Certifications from Architect as is the present practice.

The merits of this concept are *what you see is what you get.* It is believed that this strategy will enable purchasers to physically inspect the final completed product and not be given houses of inferior quality, as is the alleged situation now. However, this concept has also the negatives . Banks will be reluctant to lend as the risk of failure, with much higher possibilities of buyers pulling out, or even no buyers, is now greater. Therefore this strategy has to be carefully evaluated prior to implementation.

In FEC (M) Ltd., this concept is being applied as part of our strategy during this financial crisis. This concept is implemented in one of projects in order to achieve a maximize profits. It is targeted to be implemented in our Plaza Damas project for the link houses. We intend to complete the 20 units of link house before we sell them. Of course as discussed earlier the interest cost will be high but we strongly feel that this concept will work as it gives purchasers confidence on the company. Besides, the cost of interest will ultimately be parked back to the purchasers in the selling price. This concept is only applied to situations whereby the property is situated at a prime location whereby the demand is more than the supply. With this practice not only does it enhance the image of the company but it also maximizes the profits as purchasers are willing to pay premium for completed products.

Besides this we have also indirectly implemented this strategy in our project in Desa Karunmas. Since we have launch the first phase of link houses of 301 units, there were a short grace period that we did not sell our second phase of 126 units of link houses due to the relevant authorities approval were not obtained yet. During this time, the construction progresses and reached to a stage of 50% completion where approximately 108 units of the link houses were completed before the infrastructure. It was at this time when we are ready to move the sales of the second phase. When this occur, many purchasers went to visit the site to have a look at these completed units and are fully satisfied with them. It is to the extend that the second phase of link houses were sold at an average of RM 182,500 per unit and were sold out within a week. This proved that purchasers will have more confidence and is willing to pay a premium for what they think they would received at the end of the Sales and agreement contract.

4.2.6 MANAGING INTEREST

The current financial crisis affects many conglomerates organization cashflow situation. This is mainly due to corporate dirty letter called the 'I'. It stands for the word Interest. Interests are often analogue by many Chinese businessmen as the blunt part of a knife where it is the least dangerous but can be a killer at times. The initial parts of the crisis have seen interest rates go as high as 15%. This would mean that a company would have to make a clean profit of at least 20% before they can obtain some cash in their business (assuming that all their clientele pays). This is because 15% will be used to pay interest effectively and another 4% for inflation rates. People that initially paid 10% interest rate for a business to run efficiently without cashflow problem are suddenly entangled into financial problems. Therefore, it is important that managing interest is still part and parcel of our strategy during this crisis.

FEC (M) Ltd.'s majority shareholder, Dato' David Chiu, has an indirect control over a two public listed companies namely:

1. Mori Denki and
2. Tokai Kanko

Japan as until to date has one of the lowest interest rates for loan. The current rate is only approximately 0.75%. FEC (M) Ltd. structures a sale of a land to be developed to Tokai Kanko with a guaranteed by back at 5% above the selling price on the conditions that the managing of this development to be hold by FEC (M) Ltd.. Tokai Kanko would then borrow money from the Japanese bank for such purchase at the rate of 0.75%. This money is then paid to the Malaysian Company for development and within the agreed stipulated time FEC (M) Ltd. pays back to Tokai Kanko with an additional of 4.25%. This effectively means that the Japanese company earns an income of 4.25% while the local Malaysian company would have an effectively loan of only 5%. Of course this structure is more complicated that it sound in here as it involves the local Central Bank as well as the counter part, but the idea is along this line.

4.3 A CASE STUDY

4.3.1 DESA KARUNMAS

This is a project typically undertaken by Karunmas Ehsan Sdn. Bhd. a wholly owned subsidiary of FEC (M) Ltd.. The land area for this development is 49.906 acres situated on the third layer of Jalan Balakong. There are basically three main access roads to the site. The first main road can be via the North South Highway from Kuala Lumpur driving towards south entering to Jalan Balakong via the Kuala Lumpur racecourse. It is approximately 6 kilometer after passing through the Mines Shopping Complex where you will reach to a traffic junction turning to the right for Taman Impian Ehsan. The project site is approximately 2 kilometer from this junction. The next accessible road can be from Jalan Cheras main road leading to a turning left for Jalan Balakong at 11 mile Jalan Cheras. After turning right to Balakong New Village one can drive straight for another seven kilometer before reaching the above said Taman Impian Ehsan traffic junction. The third access road comes from Kajang town center driving towards Putra Jaya. This site is located approximately 2 kilometer from Kajang town center or 7 kilometers away from Putra Jaya. Please refer to the location map attached. The address for this site is Lot 6504 of Mukim Kajang.

The original approved plans are prior to the crisis. It is approved on March 1997 and is anticipated at that to development the land based the below criteria.

Table 9: Concept of Development prior to financial crisis.

TYPE	UNITS	SIZE	SELLING PRICE
1. 2 ½ storey link houses - 1,650 sq ft	301	20 ft. by 70 ft.	RM 180,000
2. 2 ½ storey shops offices - 4,250 sq ft	23	22 ft. by 65 ft.	RM 450,000
3. 1 storey shops (controlled price)	22	20 ft. by 65 ft.	RM 60,000
4. 3 blocks of 10 storey condominiums	360	969 sq ft. built up (av)	RM 140,000
5. 5 storey of medium cost apartments	80	860 sq ft. built up (av)	RM 100,000
6. 1 ½ storey of bungalow factories	9	9,000 sq ft	RM 720,000
7. 5 storey low cost flats	120	550 sq ft. built up	RM 25,000

a. Managing profits and loss

With the government policies in encouraging properties to be sold below RM 150,000 as well as after receiving feedback from several leading real estate agents. The management decided not to gamble in going against the market. They decide to launch the product at an average price of RM 155,000 for the 301 units of 2 ½ storey link houses. To do this, one had to manage the product accordingly. The cost to construct per unit has to be much lower as compared to the original design whereby the targeted selling prices were RM 180,000. Failing to do the above would mean disaster as selling the product is one issue but ultimately the Developer may end up in developing for free. Therefore proper management in the sense of managing profit and loss is required.

The original tender price to construct one unit of the 2-½ storey link house based on the selling price of RM 180,000 is RM 78,000. However, now the selling price is RM 155,000 therefore the construction cost should correlate accordingly and the targeted construction cost should be RM 53,000 per unit. In order to achieve this, the management team looks into simplifying the design to reduce the cost. The management has simplified the internal layout by virtue of taking out all cantilevers to support the balcony. The shape of the building is now more square to facilitate easier construction in order to reduce cost. This results in reducing the unit area from 1,650 sq ft. to 1,512 sq ft. This can be seen from the attached drawings. In terms of finishes, the developer reduced further to make it affordable. Such changes would include the following:-

i. Floor finishes of local marble slab to 1 ft by 1 ft ceramic tiles. The cost difference is RM 2 per sq ft. because marble slab costs RM 3.45 per sq ft as compared to ceramic tiles of RM 1.45 per sq ft.. Besides this usage of ceramic tiles instead of marble slab would mean less weight on the floor slab and therefore results in lower floor loading.
ii. All windows, which originally are casement aluminum powder coated, would be changed to aluminum natural anodized sliding windows. The price could deviate as much as 25% of the original price.
iii. All bedrooms which conventionally uses parquet is changed to 1 ft by 1 ft ceramic tiles which reduces the amount of defects work at handing over stage and at the same time have a lower cost of approximately RM 0.15 per sq ft.
iv. All wall tiles will be of only five feet high instead of the original wall tiles of full height.
v. Usage of sanitary fittings would be more cleverly selected. Instead of having all the three bathrooms to have similar design maybe the Master bedroom and the second bedroom will have a better designed water closet compared to the third bathroom which is more meant for the maid.
vi. Roof pitch is being changed to 22.5% instead of 33% for the upper roof to reduce the amount of roof quantity required to complete one unit.

Upon obtaining the relevant approval and achieving an optimum design with that targeted cost, the developer launched it to the market on November 1997. The response was good and they managed to sell the 301 units within three days.

Subsequent to fully selling out the link houses the management decided to launch the condominiums. Of course once again the management had a brain storm on the selling price for the condominiums. In this case the management had finally decided to sell the condominiums cheap but high quality at a range of RM 100 to RM 120 per sq ft. The main purpose again is to achieve what they have done for the link house. But however, it is not true and they only managed to sell approximately 20 units per day of official launch. After trying for about a month, the sales figure is only 140 units. It is believed that buyers' response to new condominiums/ apartments launches has cooled. This is probably due to the present market, which is still adopting a ' wait and see attitude' for purchase of new condominiums. As reported by Colliers, the residential market especially condominium/ apartments sub sector has slowed down despite the fact that there is no official report.

b. Management of Cashflow.

In view of the above, the company have immediately decided to change the plans because they believe that should they continue further, there is a big possibility that the cashflow generated from the 301 units of link house would be jammed up by the condominiums. The changes for the plans are as follows:-

i. 3 blocks of 10 storey condominiums amounting to 360 units, to 2 blocks of condominiums amounting to 24 units and numbers of link houses.
ii. 5 storey of low cost apartments amounting to 120 units to 66 numbers of 2 ½ storey link houses.
iii. 9 units of bungalow factories to 66 units of 20 ft by 65 ft 2 ½ storey link houses.
iv. 5 storey of medium cost apartments amounting to 80 units to 170 units low cost flats.

The final changes to the plan have resulted in the layout plan having the following component :-

Table 10: Concept of Development after the financial crisis

TYPE	UNITS	SIZE	SELLING PRICE
1. 2 ½ storey link houses	301	20 ft by 70 ft - 1,512 sq ft built up	RM 155,000
2. 2 ½ storey shop offices	23	22 ft by 65 ft - 3,450 sq ft built up	RM 300,000
3. 1 storey shops	22	20 ft by 65 ft - 1000 sq ft built up	RM 60,000
4. 2 blocks of condominiums	240	1,000 sq ft average built up /unit	RM 118,000
5. 2 ½ storey link houses	39	20 ft by 70 ft - 1,512 sq ft built up	RM 185,000
6. 2 ½ storey link houses	61	20 ft by 65 ft - 1,512 sq ft built up	RM 180,000
7. 2 ½ storey link houses	26	20 ft by 70 ft - 1,512 sq ft built up	RM 185,000
8. Low cost apartments	170	650 sq ft built up	RM 42,000

With the above amendments, the management could resolve the problems of the 140 units of condominiums sold leaving behind another 80 units for value added. In terms of cashflow it may not be affecting as the sales value of the 140 units can cover the cost of construction of the total 240 units.

It is also believed that during this time residential link houses have higher demand than industrial. Therefore, an overall changes has been made. But this time, the management strongly believe that residential link house in this location has more demand than supply. The developer maximizes this opportunity by selling the 2 ½ storey link house at a much higher price with the same product. (See above for the selling price)

Based on the above amended layout the overall cashflow position is improved further. Please see below for a comparison in terms of cashflow, profits returns and also risk.

c. **Managing quality**

In this particular project, emphasize has been placed on the product and process quality. The tiles that were purchased were all from first grade tiles and never on any second grade tiles. The only difference is that the tiles would be laid up to 5 feet high instead of to the ceiling height. All material used are no inferior product and strong emphasize been placed to the Clerk-of-Works to ensure all material delivered to the site are duly inspected together with the relevant Consultants. In terms of process quality, before laying of any tiles the contractors were requested to square the building in order to avoid tiles being cut irregularly along the walls. The above are only one of the many examples.

d. **Managing flexibility**

The company offers upgrading packages to all purchasers which includes the following:-

Table 11: Upgrading Package for Desa Karunmas

TYPES	EXISTING	RATES/sqft	UPGRADING	RATES CHARGEABLE/sqft
Wall tiles	Bathroom 1 (5' high)	RM 2.28	Ceiling height	RM 5.00
	Bathroom 2 (5' high)	RM 2.28	Ceiling Height	RM 5.00
	Bathroom 3 (5' high)	RM 2.08	Ceiling Height	RM 4.50
Electrical				
Lighting Points	11 nos	RM 38.00	Add. 4 nos	RM 76.00
Heater Points	Nil	RM 80.00	Add. 3 nos	RM 160.00
Power Points	8 nos	RM 65.00	Add. 6 nos	RM 130.00
Fan Points + hook	1 no	RM 48.00	Add. 5 nos	RM 96.00

The above upgrading packages would be on the basis either one would take all or not to take at all. This is to avoid confusion during the course of construction. The company's in house Interior Designer carefully designs the above upgrading packages. All these points are deemed relevant to an end users.

In terms of booking fees to purchase of a unit, it is RM 5,000. It is rather high because it is a good way to obtain genuine purchasers. However, we provide end financing packages up to 95%. Bankers secured for end financing in this project includes Standard Chartered Bank, Citi Bank, Southern Bank, Multi Purpose Bank, Hong Leong Bank, Arab Malaysian Bank, Maybank, OCBC Bank and RHB Bank.

e. Managing Delivery

The first phase of the project consisting of 301 units, which were sold in November 1998, are targeted to complete and hand over by April 2000. The second project being launch is the condominium in which it is targeted to be completed by June 2001 while the balance link houses which completed and sold in July 1999 are targeted to be hand over by March 2001.

f. Cashflow

In the original development plans approved in the above, the anticipated duration of the project is about 4 years with an anticipated profits of RM 39,179,179,088.This gives a return of 39.9% over gross development cost. The cashflow indicates negative for the first 3 years starting effectively from the forth quarter of 1997. It peaks at the second quarter of 1998 with an anticipated cash outflow of RM 12,789,000. This is due to the initial cost expected to be incurred are as follows

i. survey fees on demarcation of boundary line, topography survey, and precomputation plans for the approved units and others.

ii. Site clearing and earthworks required to be completed prior to commencement of works.
iii. Professional fees amounting to approximately as per the schedule of professional payments scheme.
iv. Other minor cost such as office overheads being apportioned to this project as well as anticipated contingency sum for item2.

The amendment of plans changed the overall feasibility of the project from the original position of having RM 39, 179,088 to RM34,167,235 where this changes gives a return of 42.9% over gross development cost. The cashflow is much desirable as it is only negative from the forth quarter 1997 to the third quarter of 1998 which only peaks at RM 1,489,000 the third quarter of 1998. From here one can see that the although the amount of profits are lower but the return is higher. Therefore the risk factor is lower.

The difference in the above figures are based on the fact that the original plan is to build a little first in order to gain confidence from purchasers in buying our houses at a more premium price. However, when the crisis sets in, the organization decides that the 'name of the game' in this situation would be concentrated on affordability as emphasize in the 'Home Ownership Campaign' as well as the financial institution. Therefore for the purpose of gaining the confidence from the potential buyers, the company launch the product at their own hotel namely Dorsett Regency Hotel, explaining to the customers on the capability of the Developer. Besides this the price of the units were much lower to capitalize on a wider market segment on affordability as well as easy end financing.

The cashflow improves further as managing of debts step in. During this crisis where monetary contraction happens, many people are unable to pay for work done. This results in debt where many people term it as bad or difficult debts.

When this occur, people will calling for payment and rumours will start spreading on the company's performance. To avoid this in managing of debts, the management informs all respective contractors as well as consultants that the job given to them will be on success basis. Success is based on the fact that upon launching and the sales and collection is good then payment would be made to them immediately. This is shown in our cashflow accordingly. This method does work because as they find that many creditors do not really mind on payment being delayed but most important is that they would know when they will have their money for the work done and not leaving them in the dark as to when are they able to obtain their money.

4.3.2 SUMMARY

Based on the above study, it can be concluded that the changes made to the plans have resulted in the followings:-

1. **Returns**

Table 12: Anticipated profits for Desa Karunmas

	Before financial crisis	***After financial crisis***
Returns over GDC	***39.9%***	***41.4%***
Returns over GDV	***28.5%***	***29.3%***
GDC	***RM 98,285,912***	***RM 80,441,541***
GDV	***RM 137,465,000***	***RM 113,723,444***
Profits	***RM 39,179,088***	***RM 33,281,903***

2. Net Present Value

Table 13: Net Present Value for Desa Karunmas

Year	Before Crisis	During Crisis	NPV@1997	NPV@1997
1997	*(3,083)*	*(255)*	*(3,083)*	*(255)*
1998	*(4,200)*	*662*	*(3,780)*	*596*
1999	*4,384*	*16,221*	*3,551*	*13,139*
2000	*24,162*	*15,288*	*17,614*	*11,145*
2001	*25,005*	*9,079*	*16,406*	*5,957*
2002	*764*	*(228)*	*451*	*(135)*
2003	*817*	*298*	*434*	*158*
Total	*47,849*	*41,605*	*31,593*	*30,605*

The assumptions for the above calculations are:-

i. The cost of capital is 10%

ii. Net present value is calculated from the accumulated cashflow at the end of every year and not average out within that year

iii. The initially capital of RM 4 million is not taken into consideration because this calculation is done on the basis that is for only comparison. Therefore the initial fund is deemed to wipe each other off in the calculations.

iv. Cashflow for financing is deemed to be small in comparison to the overall studies and shall not be included in this calculations.

From the above results, it is clearly shown that the project would be viable based on the fact that the Net Present Value (NPV) is positive. Based on the results for NPV, it seems that the plans prior to the financial crisis have a higher value than the current situation by RM 998,000. However should the factor on interest is being factored in then the difference would be smaller by RM 340,000 which brings the difference in NPV to RM 658,000. As for the returns against either the gross development cost (GDC) or the gross development value (GDV), the current situation provides a higher return. Therefore it can be concluded that the decision made by the company of having lower risk despite of having a slightly lower return is justifiable.

4.4 RECOMMENDATIONS

The financial crisis for the year 1997 to 1998 has resulted in many companies in Malaysia having to change their original long-term plan. These changes have indirectly affected their original mission and vision. They are now concentrating more on survival rather than keeping their original plan in tact. High interest rates have eaten up their profits and greatly affect their cashflow. The original plan of buying into expensive and big land banks for future earnings were ended with problems in servicing the loans with high interest rates and some to even the extend that the banks are stopping and terminating their financing packages to them. For projects that were under evaluation for bridging finance came to an abrupt stop as the government policies of property development have change. The confidence level of property investors have gone down and placing of money into properties for capital appreciation and yield were no more attractive as financing cost for properties were high while placing money for fixed deposit rates were high. At one time the foreign banks are providing fixed deposit for Ringgit at an interest rate of 22% hoping to make money on depreciation of the Ringgit. With this, it indirectly reduce the level of confidence of people in investing into property as placing money into banks are giving yield much better than investing.

To overcome the situation above, the company, FEC (M) Ltd. has embarked into immediate strategies such as managing profits and loss, managing debts, managing qualities, managing interest as well as managing in concept of selling. These strategies immediately adopted were purely viewed at an angle that was experienced at that time. In fact, the company is the 'first mover' in changing the concept of development in Cheras, Desa Karunmas which goes in align with the government policies of having affordable homes. The company is able to do that as the holding cost financed by the equity from the shareholders were low at RM 4,000,000 and the change of priority of the Chief Executive Officer of the company were placed more on actual cash more than 'paper money'. This means that the CEO believes in cash that can be generated immediately rather than the company can make more money in the money if they were to hold on first. The company's product was first launched just three weeks prior to the first 'Home Ownership Campaign'.

There were no doubts that this company has successfully launch their products and strategies adopted by them were right but however, it could be better if the company were to analyze their strategies into more in-depth in relation the basic marketing principle of the SWOT analysis and Porter's five forces. In SWOT analysis namely analysis into the strength, weaknesses, opportunity and threat and Porter's five forces of threat to new entrants, bargaining power of the building materials suppliers, bargaining power of the buyers, threat of substitute products and rivalry among competing firms in the same industry would somehow improve its current strategy and building them more in depth. Situation like in the SWOT analysis for Desa Karunmas, it should be noted that at that time, there were almost no competitors for the same kind of product. The product is at the fringe of Kuala Lumpur with no other developers on the neighbouring doing the same kind of product and if even so other companies may not be attractive as their entry cost are high. The only weaknesses were at that time the access road to the project site were bad as it is situated 700 meters away from the nearest housing scheme. With this analysis, if done, may results in the company able to maximize their profits accordingly. Analysis into the Porter's five forces gives the company an idea where are their positions in relation to the market. This can assist them in achieving lower cost. Bargaining power for suppliers were low as they have a lot of stock with no purchasers or even have purchasers they may not be feeling comfortable to sell to them as collection may be a problem. As for this company, they have high bargaining power as the developer has fully sold their product and is able to arrange with bankers on payment on back to back basis. Like it or not the fact that the units of houses were fully sold and the developer would be in strong financial situation for this project would enhance the value of bargaining power from the developer.

The company should look into building beyond a shell to house people. Gone were the days that people believe a house is just a shell to house people. The environment is changing and the needs of people are more than a shell but rather a conceptual house which are decent and different in many means. The company should look into some value-added development that can enhance the value of houses. One of the value added features could be linking property development of a housing scheme with environment and also information technology. Housing scheme of today needs to be different from those days whereby the house offers the standard package of lounge, dining hall, 3 bedrooms and a kitchen with all other necessary bathrooms. The company should move on upon setting the initial pace of selling the initial product of less than RM 150,000. They should be value-added development in order to maintain its competitiveness. One of the typical example would a development completed by the Tan and Tan Development Bhd. on the zero lot concept for its bungalows in Sieramas. It also rekindled the old terrace house of having airwell to come out with attractive 'Courtyard Homes' which were snapped up quite quickly.

Other than the above, the company should note when the government starts announce that emphasize are being placed on affordable homes of less than RM 150,000 and bankers will support end financing for products as such, many developers rush in to resubmit their plans changing their development accordingly. This is especially true for developers that has high holding cost and prefers to cash out or at least is able to service their existing loan. This has resulted in more of this housing product and competition becomes more stiff. As such, there shall be many of this range of products and customers have more variety to choose. Therefore, the company, in view that they do not have financial problems, should view into certain projects that can create a product of range RM 150,000 to RM 180,000 to avoid this stiff competition. There is a strong believe that this category of housing will do well in view that many house buyers who are end users and has a little bit of money do not want to be associated to the range of people who purchase the houses for less than RM

150,000. They would prefer to be associated to a higher range living environment. Therefore, housing of this category may stand good changes of survival. However, this strategy should only be adopted at a later stage when products of below RM 150,000 become a glut.

FEC (M) Ltd. as at that time only look at building strategies that were effective from the external side. They seem to forget on human management factor on the internal side. Human management is important as whatever strategy the company has they must have it implemented by their employees. Like the saying goes 'knowing what to do is only the starting point but it is even more important to knowing what to do and doing it'. The company must look at the case of human management in motivating their staff at the same time careful at their overhead cost. Many times employers may feel that the best way in motivating their staff are through monetary value but during this crisis, it may not be best solution. There were cases that employers take the advantage of this crisis to reduce employees salary to even cut cost on overheads and during the good times they will give excuse that they need to save for the rainy days. The company should look into other means ways in human management such as managing employees or staff based on the individual core competencies. This indirectly motivates the employees as they can do things they excel in. They are able to show their strength on what they can do. Besides this, creating a family environment among staff would enhance their performance. Staff would be empowered to handle situations that at the end of the day it is beneficial to the company. They should be given an environment as though that they are the owners of the company. Other than the above, effective training program should be provided to respective staff in improving their core competencies and hence building them to more efficient and effective.

4.5 CONCLUSION

From the above discussion and recommendation, one can see that the overall strategies adopted by FEC (M) Ltd. is in align with the basic principle of business strategy. The concept of the strategies adopted by this medium sized property developer lean towards to Cost Leadership Business Level Strategy where the company has the following features:-

1. Relatively standardized products.
2. Features acceptable to many customers
3. Lowest competitive price.

In order to achieve the above, the company made a constant effort to reduce cost through mass production of similar products in building efficient scale facilities. Houses to be constructed would have similar design. Besides this, tight control of production cost such and overheads such as managing quality of the product using minimum staff by virtue of training the employee and having structured organizational learning procedure. Organizational learning process should includes monitoring costs of activities provided by outsiders such as material cost, workmanship cost in relation to process of construction whereby construction of a house in a boxy manner compared to houses that have kinks and cantilevers.

From the strategies adopted by the company as discussed in the earlier chapter and the recommendation, one can see the value creating activities adopted by the medium sized developer in achieving its strategy in overcoming the 1997 to 1998 financial crisis. The combination of the above shows the value chain that is summarized below.

a. *Firm Infrastructure*

Simplified planning practices to reduce planning costs. Plans of having similar type of product that can be produce in a mass manner. Relatively few management layers in order to reduce overhead.

b. Human Resources Management.

Effective training programs to improve worker efficiency and effectiveness. This includes in motivation process and managing human resources based on the individual's competencies.

c. Technological Department

Easy to use construction technologies such as simply and accepted design to facilitate easy cost and quality control.

d. Procurement

Systems and procedures such as tender called with suppliers of building material for material to be supplied for construction and frequent evaluation to monitor the supplier's performance. To increase this efficiency includes the idea in showing or explaining to the suppliers on the overall feasibility of the project and commitments on terms of payment. (Managing of debts)

e. Sales and marketing

Small and highly trained sales force which assist in portraying the image of the company as well as generate the sales volume for the company effectively.

f. Service.

Effective construction to reduce the frequency and severity of recalls. This context relates to our earlier discussion on managing quality and flexibility.

The company has brave themselves up effectively through this financial crisis. Not only they were not caught with the crisis, there have created a situation whereby the products sold would be able to keep them through for the next three years effectively. Proper strategies adopted by them were effective as at until todate but as to whether it could make them competitive in the future would still be a question mark. Therefore, in this study the recommendation make were more towards making the company to be more effective and competitive in the near future. There were no deep illustrations on the recommendations as it is beyond the scope of this study. The scope of this study concentrates more on strategies adopted by a medium size property developer in response to the Asian economic crisis 1997 - 1998.