



Building on success

Enabling and incentivising inclusive growth

September 2018

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Foreword



The Government is rightly investing in infrastructure which stimulates economic growth. But to ensure that the taxpayer is getting the best value for money for that investment, the growth it creates must be sustainable - and it must be inclusive.

Balfour Beatty supports the inclusive growth agenda and welcomes the Government's plans to extend the scope of the Social Value Act¹ and to strengthen its commitment to awarding contracts based on the full social value, rather than purely focusing on the cash cost. However, we believe the planned amendments should go further by extending the requirement to explicitly evaluate social value in procurement to the entire public sector and not just large, central government contracts. Furthermore, given that it is small and medium sized enterprises (SMEs) which create most of the jobs in our sector, we believe that they should be supported and incentivised to deliver even greater social, environmental and economic impact than they do at the moment – a concept we call “enabling and incentivising inclusive growth”. This would result in an even more positive impact for UK society in terms of skills, employment, business, community and environmental outcomes.

While on paper the quality weighting for decision making during procurement is often similar to the commercial score, the reality is that many commissioning authorities continue to concentrate on the lowest price as the deciding factor in the tender process. But at what cost? A focus on saving money on the initial bid price rather than considering the longer term savings and positive social, economic and environmental outcomes that could be achieved is surely a false economy. It is an approach which also risks damaging the British construction and infrastructure industry.

Commissioning authorities should take courage from the Government's re-emphasis of its commitment to social value and more consistently take into account the long-term benefits that could be gained beyond the infrastructure they are paying for. Doing so will help deliver the overarching strategic aims of the commissioning authorities and reduce costs over the long-term, leaving more money to be invested in key priorities.

There is still a long way to go to deliver on the ambition of the Social Value Act, but we believe that the construction and infrastructure sector has the potential to make a much greater contribution if we and our supply chain – particularly SMEs – were better enabled to help tackle inequality and generate more inclusive growth. We are primed to do it, with the jobs, training opportunities and local supply chain spend that flow from investment in infrastructure. This is an opportunity that must not be missed.

A handwritten signature in black ink, appearing to read 'Leo Quinn'. The signature is fluid and cursive, written over a light grey horizontal line.

Leo Quinn

Group Chief Executive

¹ Minister for the Cabinet Office David Liddington speech to Reform, 25 June 2018

Executive summary

It is widely acknowledged that investment in infrastructure not only improves the lives of those directly benefitting from it, but also underpins economic growth via the multiplier effect first highlighted by John Maynard Keynes in 1936².

For many years, the construction and infrastructure industry has also delivered “social value” – a legacy of positive benefits to communities beyond the simply financial. For example, by employing locally and creating sustainable apprenticeships in the area around schemes; boosting local small, medium and micro businesses, and social enterprises by ensuring they form a core part of the supply chain; maximising green space, and ensuring the value of materials is optimised through a circular economy. The ground-breaking Social Value Act 2012, which came into force in 2013, formalised this value add and set a requirement for all public procurement over a given threshold to have regard for social, economic and environmental wellbeing.

It is increasingly acknowledged that the construction and infrastructure industry has significant potential to benefit society more broadly and can help to fulfil the Government’s vision of “an economy that works for everyone³”; arguably more so than any other sector.

The Government’s Index of Multiple Deprivation⁴ sets out the seven key indicators used to define relative deprivation for neighbourhoods in England. The construction and infrastructure industry has a key role to play in improving several of these indicators including income, employment, education, skills and training, and living environment. Addressing these indicators by ensuring that towns and cities are diverse, with housing, jobs and infrastructure that is accessible to those from all socio-economic backgrounds is the best way of reducing the gap between the wealthiest and the poorest in society.

Companies such as Balfour Beatty have strong, established relationships with education providers and play a key role in training and skills development. We invest in the areas we operate in and aim to leave a positive social, economic and environmental legacy once works have been completed. We have thousands of SMEs working with us as our trusted supply chain partners around the schemes we work on. We believe that a forward-leaning approach which would make existing funding available for SMEs to use to amplify the social value they currently deliver, could turbo-boost existing efforts. We call this concept “enabling and incentivising inclusive growth”. This would result in significantly better outcomes and have greater impact for individuals previously excluded from social mobility, for the communities they live in and for the economy. The impact of this would be to address local needs and help plug the £5.8 billion funding gap that local authorities face by 2019/2020 from the reduction in revenue support grants. In addition, it would help reduce costs for central and local Government by improving the take-up and conversion of training and employment programmes, which would then lead to increased employment, increase tax income (regional) GVA and ultimately GDP.

On the other side of the equation, in spite of the good intentions by public sector procurement to take a more holistic view of value, awarding contract to the lowest cash bid remains the norm. In many cases, this is due to the pressure local authorities and other commissioners are under on costs given the tight fiscal climate. In our discussions with those in public procurement, a consistent theme is that, whilst in an ideal world they would take a more holistic view, and spend more to get better longer term outcomes, they feel they have to respond to immediate needs on limited budgets. As a consequence contractors are incentivised to bid as low as possible on contracts in order to secure them, even though pricing this low is damaging to the industry over the long-term, as is being increasingly acknowledged⁵. In order to minimise costs, many of the options to deliver true social value – ranging from creation of local employment opportunities and training through to using materials which will be cheaper to maintain in the long term are too often sacrificed.

² The General Theory of Employment, Interest and Money, John Maynard Keynes, 1936

³ Theresa May, 11 July 2016

⁴ The Indices of Deprivation 2015, HMG, September 2015

⁵ House of Commons, Public Administration and Constitutional Affairs Committee, July 2018

Key points and recommendations

Whilst responsible companies will refuse to compromise on quality and will attempt to leave a positive legacy, this is not sustainable over the long-term if procurers primary objective is to save short term cash. The emphasis must therefore move towards a balance of value and price, both in order to deliver value for money for the taxpayer and local communities, and to ensure the construction industry remains healthy, and is able to continue to deliver infrastructure and social value in the future.

Balfour Beatty believes that both those undertaking procurement on behalf of the public sector, and the construction sector, have a shared responsibility to find procurement approaches to deliver social value and value for money for the public pound.

This paper builds on Balfour Beatty's recent paper Shared Value: Helping local authorities unlock social value, which considers ways in which the social value being delivered through public projects commissioned by local authorities can be maximised.

1. Social value is not yet given the prominence it deserves in tenders. Changing this will require improved guidance for commissioners as well as courage from the commissioners themselves and a genuine culture change in public sector procurement.
2. The construction industry has the framework to act as an enabler for inclusive growth, with the skills, networks and employment and training opportunities required.
3. Further improvements are needed to the Treasury's benefits cost ratios to ensure that social value impacts which will effect inclusive growth are taken into account. At the moment, projects which could deliver jobs and inclusive growth in a deprived region are not being commissioned because the benefits cost ratio is higher for other projects in London or the southeast.
4. The staccato way in which social value objectives are set, linked to specific schemes, prevents the delivery of large scale social value strategies.
5. SMEs should be supported and incentivised to drive more social value. There are a million of them operating in the construction industry: we could generate significant value to society if we harnessed their combined power more effectively.
6. The current model should be evolved to bring the private and voluntary sectors closer together and facilitate the pooling of some of the funding which currently exists in order to create a single approach to applying for funds with a clear, pre-defined set of required social value deliverables, rather than the current fragmented approach.
7. The persistent focus amongst some commissioners on lowest-price over an approach which considers longer-term outcomes is damaging the UK construction industry and leading to missed opportunities.
8. Collaborative frameworks such as those operated by Scape Group and the North West Construction Hub (NWCH), could feasibly be used to enable shared employees in a model similar to shared apprenticeships.

Delivering inclusive growth

Balfour Beatty believes that social value should be used as a driver for economic growth that benefits all parts of society. The construction and infrastructure industry has a key role to play in delivering this inclusive growth. For example, a key challenge to inclusive growth is that of creating high wage, high value-add jobs across the country. Education, skills and employment opportunities offer the best chance of improving prosperity and ensuring that this prosperity is spread more evenly across society. A key element of inclusive growth therefore, is inclusive job growth, which the OECD defines as:

“Sustainable job creation that leads to a more equitable distribution of good job opportunities, both socially and geographically.”

The challenge is how to overcome the existing barriers to inclusive job growth and to facilitate employment opportunities for those who have been unable to access them. This might include, for example, those with health problems, carers, young unemployed people or ex-offenders. Inclusive job growth also means providing access to better jobs for those who are underemployed or working in roles that do not help them fulfill their potential: upskilling people and improving their employment opportunities or directly providing them with work is key to driving improvements in living standards and productivity and helping to tackle inequalities where they exist across the country.

The construction industry has the framework to act as an enabler, with the skills, networks and employment and training opportunities required. It is also a dynamic sector; fast evolving with an increased focus on automation, digital and artificial intelligence. It is vital that the focus of the programmes we develop cater for our future needs to provide maximum benefit and help tackle some of skills shortages we have.

However, there is also potential for some of the industry’s models to be evolved to deliver even greater benefit. For example collaborative frameworks such as those operated by Scape Group, Constructing West Midland (CWM), and the North West Construction Hub (NWCH), could feasibly be used to enable shared employees in a model similar to shared apprenticeships. This would mean even more people would be able to access work over a longer period rather than, as with most social value commitments, for the length of a specific contract. There are over 7,000 construction-related frameworks being used by local authorities, government departments and other public bodies across the UK. Facilitating such changes could have a significant impact.



Balfour Beatty has been working on these issues for many years. In our experience, there are a number of steps that should be followed to increase the social value being delivered via investment in infrastructure, which could in turn have a significant impact on delivering inclusive growth:

- Inclusive growth must become a core consideration in the commissioning process, considered from the outset and at every stage beyond.
- More importantly, to deliver inclusive growth, it must form part of an overarching strategy, shaped by the local community and in partnership with all of the relevant stakeholders. Inequalities will never be truly addressed if the desired outcomes are considered one commissioning process at a time. The strategy must come first and every procurement decision thereafter must deliver against that strategy.
- Social value can be seen as being subjective by some procurers, while suppliers can be unclear which social value elements will be prioritised by different procurers. Commissioning authorities must provide clarity about the social value outcomes they aim to achieve to enable contractors to work out how they can best deliver against them and reflect these ideas in their bids. Engaging and communicating with contractors in this open and transparent way helps in the delivery of benefits which deliver against the inclusive growth strategy.
- Commissioners must also be clear regarding the weighting social value will be given in the tender process. The best way to reflect the importance of achieving genuine social benefits and inclusive growth is to increase the weighting these priorities are given in the award criteria.
- Tenders which are overly prescriptive in what they expect to see delivered for the investment, for example a certain number of apprenticeships, achieve less than those which invite proposals for solutions to the persistent problems that an area faces, tied into the inclusive growth strategy.
- Close collaboration with all of the stakeholders, including the construction contractors, will also help to facilitate innovation and develop new ways of providing services, maximising the value of the investment and improving the outcomes.
- The social value being delivered must of course take account of local circumstances and the different barriers which stand in the way of inclusive growth in each area. However ensuring both the deliverability of what is being committed to and then making sure that the commitments are being delivered, as well as assessing at a holistic level what impact they will have on the overarching strategy for inclusive growth, is important. Measuring the impact of social value can be challenging. It must be set against consistent criteria and benchmarked over multiple projects, and the metrics must be robust in order to enable contracting bodies to effectively compare bids.
- Incorporating social value into procurement processes must be followed up with effective contract management to ensure the outcomes are being delivered.
- For construction contractors, playing their part in the delivery of inclusive growth requires the building of strong links with organisations which provide employment support, with education providers and local businesses.
- Contractors must ensure they act responsibly in relation to their local supply chains, leaving a legacy by strengthening local businesses.

In addition to these points, in terms of central Government's procurement, whilst we welcome the advances that have been made in capturing potential social value of large schemes, further improvements are needed to the Treasury's benefits cost ratios (BCR). For example, while the Treasury Green Book does highlight that wider benefits must be considered in commissioning decisions, and while a number of other tools exist to calculate some of the most important social value impacts in terms of inclusive growth such as the benefits of upskilling the local workforce, positive impacts on the health and environment of the local community, biodiversity, reducing antisocial behavior and reinvestment into the local supply chain, it remains the case that projects which could deliver jobs and inclusive growth in a deprived region are not commissioned because the BCR is higher for another project in London.

Enabling SMEs to deliver more social value

It has long been acknowledged that SMEs underpin the UK's economic growth. In 2017, they accounted for 60% of all private sector employment in the UK and 51% of all private sector turnover⁶. However SMEs have a great deal to offer specifically in promoting inclusive growth and delivering social value outcomes:

- They have a direct impact on the communities they operate in and are often rooted in them. This means that they have the established relationships and first-hand knowledge that enables them to address the area's needs and social issues. Of course, they also employ local people and have their own onward supply chains.
- As employers, SMEs are also direct providers of the jobs and training that help drive inclusive growth.
- SMEs are also innovative and agile. As SMEs are usually closer to the frontline, they can recognise the need to change earlier than bigger companies, and often have fewer and less rigid processes in place to slow innovation down. This enables them to be creative and nimble in how they apply priorities such as the delivery of social value outcomes.

However, we believe that the staccato way in which social value objectives are set, linked to specific schemes, prevents the delivery of large scale social value strategies, particularly limiting the ability to make the most of the advantages associated with SMEs. For example, a significant amount of funding sits with service providers, with whom SMEs have no incentive to build long-term relationships. Furthermore there are a myriad of different schemes with different funding criteria and deliverables creating additional red tape to anyone looking to apply for funding.

This fragmented approach must be addressed – we must think bigger, and more creatively, in order to deliver more. There are currently multiple sources of funding some of which may come from private sources and NGOs. However, the Government has a clear opportunity to streamline its own funding, especially in the light of Brexit. Ideally, therefore, there should be a single approach to apply for funds at a local level, with a clear, pre-defined set of required social value deliverables. These deliverables would vary depending on the local needs, but the definitions and evidence requirements of any deliverables would be pre-set. This would prevent overlap and duplication of existing schemes and ensure that the intervention types are tried and tested.

This local approach would also facilitate a more coordinated way of working with local SMEs and third sector organisations, such as schools, colleges and universities. It would furthermore provide mutual benefit; as well as making a difference in the local community through the deliverables, SMEs would have comfort of knowing, that there would be a continuation of service in accessing ex-offenders, school leavers, trainees, apprentices, graduates for example, to meet their needs, regardless of which provider was successful in applying for funds.

For these programmes to be sustainable there would need to be a clear understanding of what skills would be required in a given area and how these would be best resourced locally. This could be achieved by bringing together principal contractors, SMEs, commissioning bodies and service providers to align appropriate programmes, ensuring that supply meets demand. Principal contractors would work with the service providers to run supplier events, advertising the services and support that SMEs could access.

Furthermore, much like the model of shared apprenticeships, service providers should be tasked with specifically taking people who have been through a programme with a designated SME on their books for redeployment locally where projects or contracts come to an end. Apart from apprenticeships, this could be widened to cover other skills and training schemes and built into the funding criteria.

⁶Federation of Small Businesses, UK Small Business Statistics, 2017

The SMEs would be supported and incentivised to participate in these local programmes by having access to these local talent pools free of charge. Furthermore their social value performance would be scrutinised by the primary contractor.

The commissioning bodies would need to work with principal contractors by placing contractual requirements on delivering social value outcomes that address local needs. Without a clear commercial focus there is no principal driver to ensure that the local needs would be met. While this already happens in London and other big cities, increased collaboration within regions and across multiple schemes and principal contractors is needed outside of these areas. This would allow principal contractors to collaborate with SMEs at an early to stage and put forward solutions that deliver best value, rather than tendering based on lowest cost, which would drive principal contractors to focus on short-term cost savings.

An approach such as this, based on value, would unlock the potential to deliver a more ambitious social value agenda, which generates the outcomes local communities need while simultaneously tackling skills gaps across the economy and driving up tax receipts.

Given the huge number of SMEs operating in the construction sector, over a million according to the latest figures⁷, any initiative making it easier for them to increase the social value they deliver could have a huge impact on the delivery of inclusive growth.



⁷HMG, Business population estimates 2017, November 2017

Moving away from lower price tendering

Delivering inclusive growth and improved social value benefits via infrastructure investment relies not just on a refocusing of objectives onto longer-term, more strategic outcomes, but also on a strong, sustainable construction industry. Both of these in turn depend on a move away from lowest price tendering.

Although the Social Value Act encourages commissioners and procurers to consider value for money in the broadest sense, selection on the basis of price and award to the lowest priced bid remains the norm in many cases. Social value is not yet given the prominence it deserves in tenders.

It is important to remember that the tender price on a construction project is not the same as what the scheme actually ends up costing. If the tender price is too low to cover the actual cost of the scheme, the result is either corner-cutting and poor quality work, not paying local subcontractors a fair price in order to deliver at the tender price, or legal claims to recover additional costs incurred during construction, which can result in delays. In many cases, it is also leading to the Government or other public sector commissioners repeatedly having to renegotiate contracts with the private sector⁸, which is time consuming and costly in itself. In either case, the outcome is not a saving, but rather increased costs. Furthermore, the opportunity to deliver the social value outcomes that could have been achieved has been missed. Indeed, lowest price tendering can reward companies which do not invest in training, skills, innovation and leaving a positive legacy and which pay lip service to social value where it is included in tender documents, with either unambitious commitments, or without the intention of delivering them.

Balfour Beatty believes that changing this will require improved guidance for commissioners as well as courage from the commissioners themselves and a genuine culture change in public sector procurement.



⁸ House of Commons, Public Administration and Constitutional Affairs Committee, July 2018

Conclusion

With major infrastructure contracts increasing in size and complexity, the UK needs a strong domestic construction sector to deliver them. This is a long-term but circular relationship: contracts must balance efficient delivery of the infrastructure and social value outcomes necessary to underpin inclusive economic growth, with a margin that allows contracting companies to invest in skills, plant, technology and innovation to drive national productivity. The public sector is in a position which allows it to support innovation in a way which is good for commissioning authorities, good for the industry and good for UK Plc.

We believe that commissioning authorities must take a bold, joined-up approach to social value. Only by doing so will we truly maximise the potential of public money being invested in infrastructure across the country to deliver inclusive growth.

About Balfour Beatty

The UK's largest construction contractor, Balfour Beatty, was founded in 1909 and is listed on the London Stock Exchange. With 15,000 employees and over 40 offices in the UK, Balfour Beatty finances, develops, builds and maintains the increasingly complex infrastructure that underpins the UK's daily life.

With a legacy of projects across transportation, power and utility systems, social and commercial buildings: from Crossrail and Heathrow T2b to the M25 and M4/M5; and Sellafield; to the Olympics Aquatic Centre, we are proud to be a British company delivering iconic structures, bold engineering feats, behind-the-scenes innovation and joined-up thinking, financing and partnerships. Wherever we operate we aim to be integrated within the neighbourhood, supporting the local community, local businesses and local workforce. We use locally sourced materials wherever possible, and invest in future talent through apprenticeship schemes and work placement opportunities to leave a positive legacy alongside the schemes we deliver.

Balfour Beatty has a supply chain of around 10,000 trusted companies across the country, many of which we have worked in partnership with for over a decade, and some of which we have worked with for over thirty years. A large proportion, 74%, of these are SMEs. We take the Government's target of 33% of procurement spend going to SMEs very seriously, and are pleased that we have exceeded it by over 10% in 2017⁹. Furthermore, over the period of 2013 to 2017, 64% (£4.7bn) of our SME spend was with Small and Micro Business.

98% of our spend goes to UK based suppliers and has done every year since 2013. However, for Balfour Beatty, it is not just about spending with SMEs. We take a thoughtful, targeted, diverse approach, operating with the awareness that their location and ownership has a disproportionate social impact on driving inclusive growth.

⁹Balfour Beatty's spend data is independently verified by Dun and Bradstreet



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