#FutureOfConsultancy

Future of Consultancy

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Value based business models

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Foreword

Since November 2018, ACE has been planning, framing the ideas, and securing support for its Future of Consultancy campaign.

We've built a consortium of stakeholders, including SMEs, large consultancies, clients, professional bodies, government and others, laying the foundations of this work on behalf of our members.

It is now recognised by government as part of the Industrial Strategy, through the Construction Sector Deal and Transforming Construction Programme.

Digital transformation is creating opportunities for engineering and consultancy businesses to provide greater support to clients through the whole lifecycle of assets and networks, closing the gaps between policy, delivery and operation.

Technology is making it easier for consultancies to develop long term commercial relationships based on a deep understanding of what is of value to their clients and how their businesses operate.

It is this combination of financial reward for added value and greater repeat business that will underpin a sector that needs to be profitable to ensure it can make the required investments in innovation and skills.

As with any transition this will take time. Clients and consultancies will move at different speeds and existing practices will not become obsolete overnight.

Similarly, a single value-based business model will not emerge as there is no end point to which all consultancies should aspire as they become more mature.

Instead, separate models will be used dependent on what the client is seeking to achieve, the nature of the services offered, the risk and complexity involved.

This report sets out a range of possible value-based business models that will need to evolve to support our industry's transition.

Hannah Vickers, Chief Executive ACE

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Understanding and defining value

The ability to reward value is predicated on a clear definition of the value the client is seeking from the investment. Consultancy will need to become more adept at working with clients to tease out this definition. To support this conversation ACE has developed a “five capitals” models which sets a framework within which a client can define what value means to them for any specific investment.

Under each of the five capitals the client can determine metrics and relative priority of those metrics. For example, do they value initial capital cost over and above whole life operation cost or their Net Zero ambitions?

This definition of value then unlocks the ability to develop a commercial model and supply chain structure around value rather than volume. This is similar to the approach previously taken by the automotive industry where the evolution of their supply chain dynamics to streamline low value processes into a production line, whilst maintaining appropriate high-value interactions such as the focus on the design process.

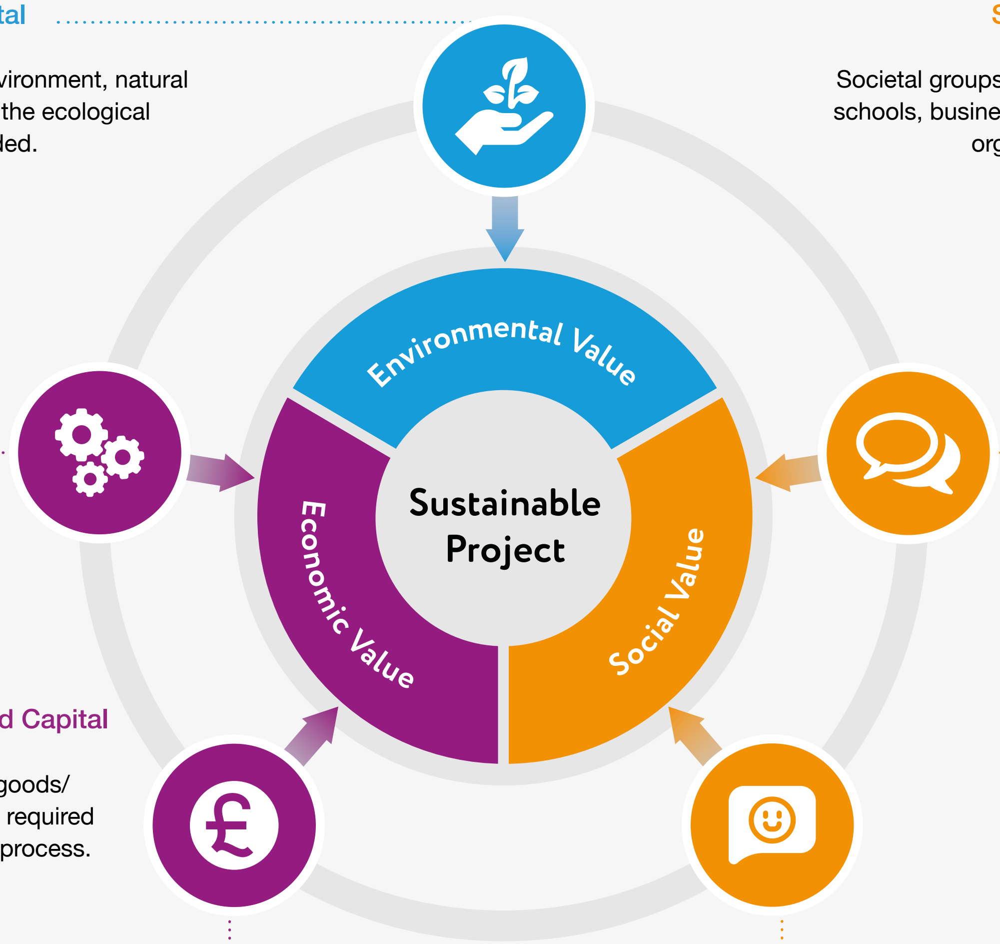
If the construction and built environment industries follow a similar path, the increased attention to the value of design and strategic advice will radically adjust the position of many engineering and consultancy firms in the supply chain.

Natural Capital

The natural environment, natural resources and the ecological services provided.

Social Capital

Societal groups, communities, schools, businesses, voluntary organisations etc.



Manufactured Capital

Materials and goods/ assets that are required to input to the process.

Financial Capital

Traditional economic measure of value which is intrinsically linked to natural, social and manufactured capital.

Human Capital

The individual: health, skills and motivation required for a productive economy.

Fig. 1 Five Capitals model

What are value based business models and why are they important?

In this context, value based business models incentivise consultancy to create value for the client rather than just rewarding inputs. The nature and diversity of clients and businesses within construction does not however lend itself to a single value-based business model. This means that a range of business models, fitted together like a jigsaw, will need to be deployed to realise the opportunities presented by different types of clients, asset owners and regulatory systems.

Figure 2 describes the results of ACE research into the possible range of value-based business models that will be deployed over the short to medium term. These models and examples of their use are described further in the table below.

The nature of opportunities for consultancy businesses will vary across the business models. Input and output business models are suitable for delivery by the consultancy businesses on their own, or via joint ventures with similar types of firms. The outcome section of figure 2 is likely to involve some form of alliance model that brings together consultants with organisations such as contractors and facility management companies.

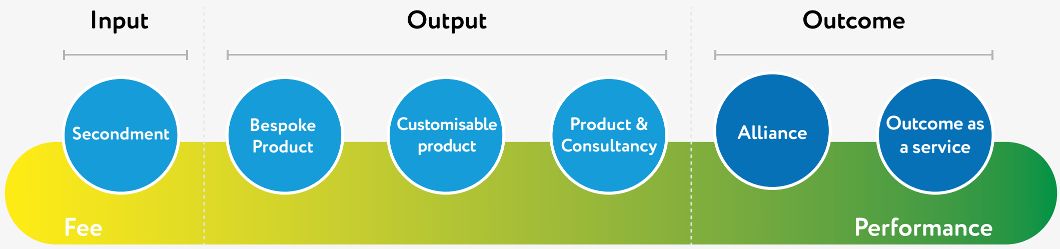


Fig. 2 The framework of potential business models for consultancy businesses in future

Definitions
Input - where reward is measured through the delivery of time.
Output - where reward is measured through achieving milestones or delivery of products.
Outcome - where reward is linked explicitly to the achievement of the clients success criteria with no reference to the methods or processes involved.

Model	Description	Characteristics	Likely deployment
Secondment	Provision of an individual on a time based contract.	Clearly defined tactical roles such as clerk of works, reservoir panels engineer.	Roles required by legislation or on secondment to replace an individual in the client's organisation with a particular domain expertise.
Bespoke Product	Delivery of a bespoke product on a fee plus performance based incentive (either financial or repeat business).	Clearly defined package of non-repeatable work.	Bespoke first principles design for a high-value project. Development of a report/business case.
Customisable product based on a standard kit of parts	Delivery of a product on a fee based return with a performance incentive for repeat business either with the same client or a across a range of clients.	Repeatable work which requires a change/reconfiguration ahead of deployment. Can be used on a framework across multiple clients.	Design in a design for manufacture and assembly scenario. Master planning utilising layout software. Design for private house builders with projects using a standard house layout.
Product and Consultancy	Delivery of a product with value adding ongoing consultancy service.	Clearly defined output where there is additional value added through the provision of an ongoing advisory service.	Compliance/safety assessment and follow up services across a network of assets. Provision of a live service in place of a static report e.g. air quality monitoring or a live environmental assessment. Digital twin creation and provision of a service providing ongoing advice.
Alliance	Consultants are part of a wider alliance with multiple parties including the client/ asset owner to deliver on outcomes through provision of products or services. Including Project 13 and Integrated Project Insurance type arrangements.	Large scale programme with a complex risk profile and lots of interdependencies and an established long term asset owner. Only useful to engage with one client/ asset owner rather than across a portfolio.	Large, complex infrastructure projects.
Outcomes as a service	Consultants are part of a wider joint venture with other businesses to deliver directly to end users. For managing performance of existing assets consultancy firms could provide this on their own.	This would typically be delivered in a joint venture with another organisation, however where a consultancy firm has the opportunity to deliver benefits by shaping the 'demand' profile it could be delivered solely by consultancy firms.	Accommodation as a service. Facilities management outcomes as a service. Apps aimed at end users/consumers.

Developing a value based commercial model

The client's role in creating the right enabling environment is critical to deploying value based business models. If this does not support the business models they will be constrained into buying inputs.

Some of the key considerations for clients in understanding their enabling environment are as follows:

- Their definition and level of understanding of both risks and value
- The situation
    - Governance structure
    - Funding duration and ability to mix capex/opex
    - Whether they have an operational interest
    - Maturity of any current performance data to set an appropriate baseline
    - Scale of investment
    - Potential for repeating of the type of work
- Market situation
    - Capability,
    - Risk appetite
    - Understanding of the value chain, i.e. where does value get added, and bringing this as close to the client as possible.

A market sounding exercise and open discussion with the consultancy industry, facilitated by ACE before a procurement process or route to market has been determined, will develop an understanding of both risk and value.

The purpose of the project commercial model should be to cascade the definition of value and incentivisation of performance throughout the project's supply chain.

Using the business models to create a commercial model

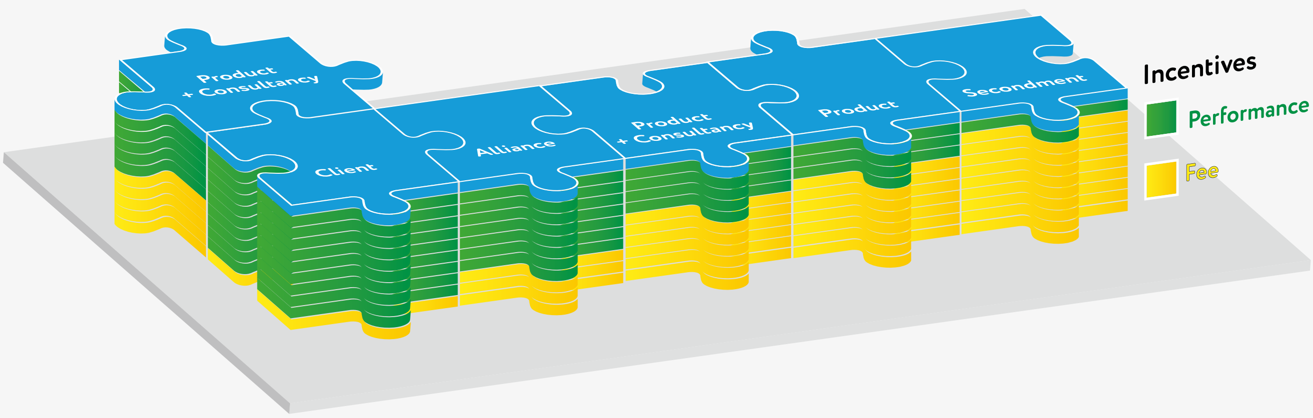


Fig. 3 A project commercial model showing how the different business models fit together an incentives are aligned.

Incentives in a commercial model

When developing the commercial model, it is important to consider how incentives will support the flow of value down the supply chain. These performance incentives can take two forms:

- Repeat business, where performance is rewarded with a future pipeline of work.
- Financial, where performance is rewarded with a monetary incentive.

Repeat business
The opportunity for repeat business is a very powerful incentive for rewarding performance without the need for complex financial calculations. This can be achieved formally through a framework with incentives on how future work is allocated. In the near future, an open supplier performance measurement system would allow clients to transparently view a suppliers' past performance across each other's portfolios to better inform procurement decisions.

Repeat business is a simple and effective performance incentive used by the private sector. Whilst the Public Contract Regulations do require a transparent procurement process, it is utilised less often in the public sector. There is scope through the design of frameworks and quality criteria it could be included more routinely.

Financial
Introducing a financial performance incentive is not a new concept, but to drive the right behaviours and ensure transparent performance measurement, it is more complex.

A simple performance incentive can take the form of a pain share/gains hare where profit it adjusted on the delivery of performance criteria identified by the client.

A much more powerful mechanism – such as in a *Project 13* style alliance – incentivises fees and profits on longer term project outcomes. This is not always appropriate, and would need to be used with care, as it could have a profound impact on the working capital of firms with any delay in payment waiting for proof of performance adding further pressure on tight cashflows.

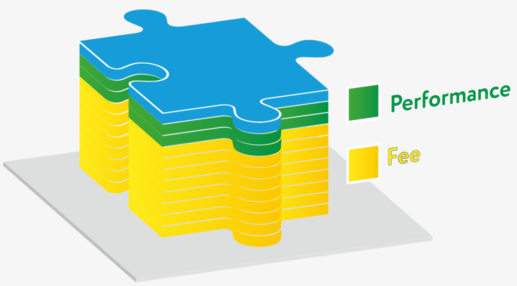
The scale of opportunity for financial incentives is illustrated when current industry profit margins are considered:

- Contractors must undertake £1,000,000 worth of work to make £30,000 profit.
- Consultants they must undertake £100,000 worth of work to make £6,000 profit, although the revenue streams of work available to them are much smaller.

In either of the above scenarios the sheer volume of work and levels of risk business take gives rise to a significant opportunity to leverage their reward mechanisms and dramatically incentivise performance, thus giving a significant push towards more productive methods and higher value work.

There is a risk in introducing financial incentives which rely on proof of performance, for example asset use data following construction which leads to a time lag in releasing the full financial settlement.

There is a spectrum with two extremes for how this could work



Example 1:
Simple financial performance incentive

Where a business is asked to put just their profit at risk with the opportunity to increase or decrease depending on their performance.

Example 2:
Advanced financial performance incentive

Where a business is asked to put part of their fee and profit at risk with the opportunity to increase or decrease depending on the performance of the overall programme, as can be seen in a *Project 13* style alliance.

Fig. 4 **Commercial model example**

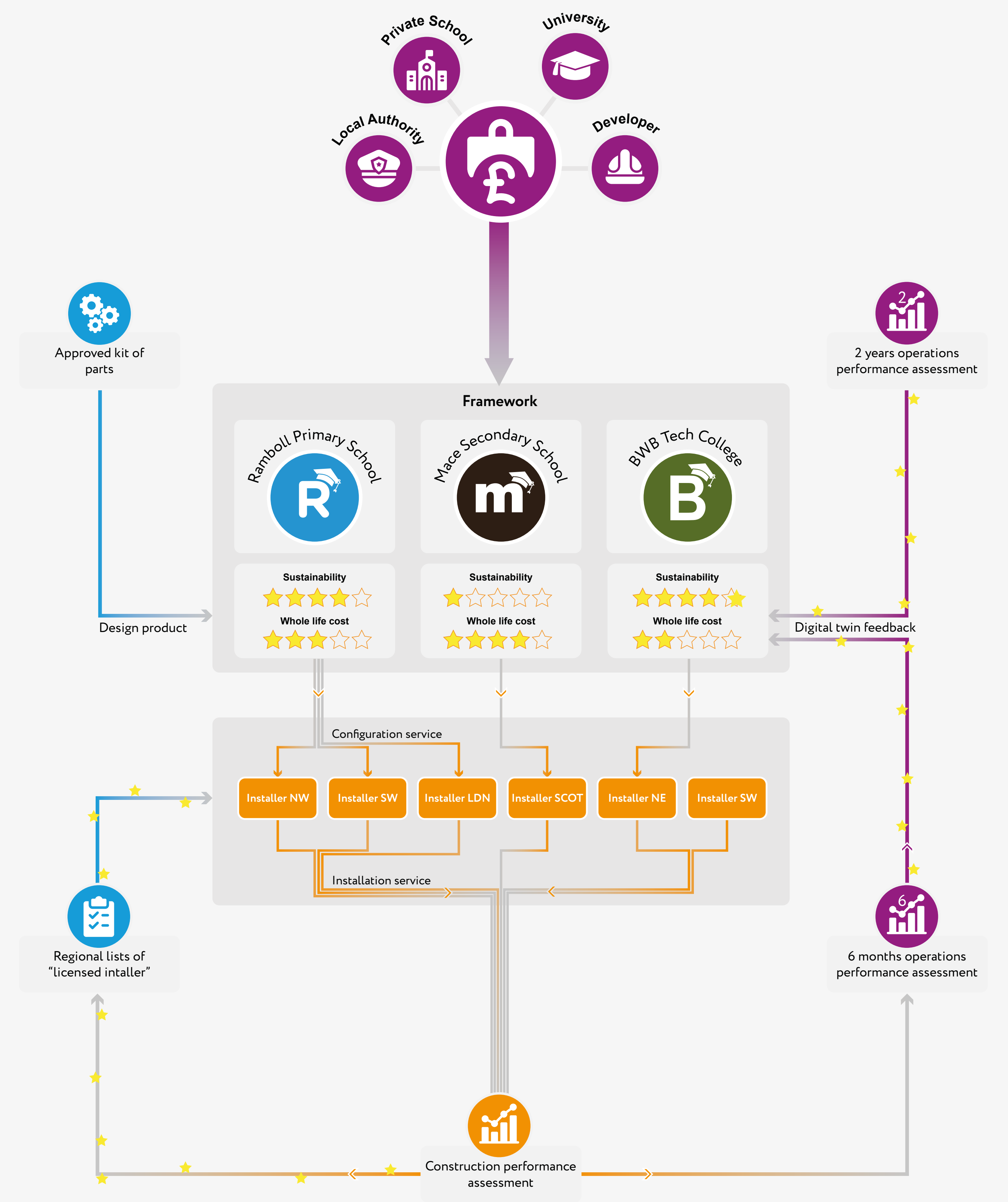


Fig. 5 Manufactured schools design programme

Pricing for investment - an opportunity for consultancy firms

The increased use of digital tools and manufactured solutions will challenge traditional consultancy business models which have, over time, evolved to generate returns on people-hours rather than investments in technology. This same technology opens up huge opportunities to better understand performance across the whole investment lifecycle and to use this insight to provide greater value to clients.

Business models which sell a blended offering, rather than just expertise, and which are sold through a range of value based business models which reward performance not just inputs, will increasingly become the norm.

The impacts of this shift are substantial:

- Enables a return on investment for innovation of new products and technology solutions and the value derived from data.
- Creates sustainable businesses delivering repeatable work/products while improving their productivity.
- Work is increasingly exportable as it is less people dependent.
- Disrupts the current areas of competition for the industry. We will need to set new rules on what to collaborate and compete on.

Under this new blended offering a shift in pricing strategy will need to take place in firms, ensuring initial R&D investment is spread across all future deployments of the product.

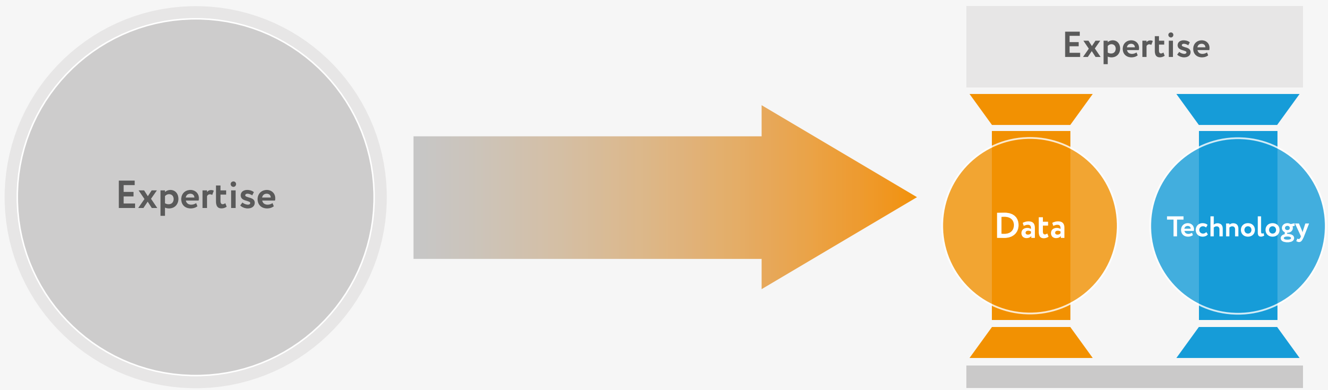


Fig. 6 Shifting the pricing strategy to create a return on data and technology

Recommendations and next steps

The value based business models framework identified by ACE provides a framework for the development of new commercial models for clients. We will take this forward by:

- Working with the Professional Indemnity Insurance Industry on the PI products to support the new business models.
- Working with the Construction Innovation Hub (CIH) and Infrastructure and Project Authority (IPA) to further explore:
  - The adaptation required to contracts to support these new models.
  - The development of a transparent supplier performance system where clients can access information and data on previous supplier performance for use in the procurement process.
- Seeking partners to develop an academic programme for business leaders focused on moving your business into new markets and deploying different business models.
- Working in collaboration with Civil Engineering Contractors Association (CECA) to support clients in designing their commercial models through advice and access to best practice, with the aim of delivering a balanced approach for both industry and clients.

ACE economic and policy papers

This paper forms part of a growing portfolio of research by ACE into the key issues involving financing and upgrading the UK's infrastructure and the effects on the wider economy, as Reports and Policy Briefings on a wide range of key issues.

To access go to: www.acenet.co.uk

How can we accelerate the delivery of a sustainable built environment?
A discussion paper that attempts to create conversations and options around sustainable built environment with examples and case studies.

Scrapping the Levy
A report which provides an analysis of council infrastructure spending with recommendations.

Unlocking housing
A report arguing for community design and invigorating local communities through placemaking.

Funding roads for the future
A paper recommending a more productive and sustainable road network in England.

Cities and Infrastructure
A joint paper with WSP that explores the infrastructure needs of our cites, how investment can improve growth and the importance in of political and fiscal devolution.

Review on EU Environmental Regulations
An in-depth review of all EU environmental regulations affecting the UK and how they will be affected by Brexit.

Triggering Article 50
This paper explores the complexities and realities facing the UK and the industry from Brexit.

The Housing Gap
This paper is the first in ACE's housing paper series and explores in detail the conditions within the UK housing market.

Performance of PFI
This paper is the third in ACE's infrastructure series and examines how to improve procurement in Public Private Finance Models (PPFM).

Public Private Finance Models
This is the second in ACE's infrastructure series and explores in more detail the rationale, performance and conditions that surround Public Private Finance Models (PPFM).

State Investment Bank
This paper is the final paper in ACE's infrastructure investment series and explores in more detail the rationale and practicalities of establishing a State Investment Bank.

Brexit and Employment Law
This paper looks at EU employment law and how our industry will be affected by Brexit.

Electricity Market Reform: Generating Results
This paper explores the role of the current energy companies in the retail and generation sectors and suggests reforms to EMR.

Funding Roads
This paper explores inefficiency within the road network and possible funding and financing solutions for the future.

Revolutionising Housing
This paper is the second in ACE's housing paper series and explores in detail a new model to rebalance the incentives for development.

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