The Bartlett School of Construction and Project Management

CASTLES IN THE AIR?

THE EVOLUTION OF BRITISH MAIN CONTRACTORS

REPORT SUMMARY

Professor Hedley Smyth

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INTRODUCTION

The recent demise of Carillion has again emphasised the vulnerability of main contractors and outsourcers. A great deal of attention has been given to the projects as the source of risk and financial problems. This report gives prime attention to the management of British-owned main contractors, arguing that many of the problems faced at the project level have their origins in the failure of management to sufficiently address the capabilities of the firm.

Management has evolved over successive decades, yet there has not been a fundamental change of approach in the management of main contractors since the Second World War. The report traces the main changes to the present day of low investment, a focus on short-term returns, dividends and aligned salary structures, and a transactional business model based on high returns on capital employed in a low interest rate environment that is unsustainable. Therefore, management has failed to invest in developing capabilities to serve emergent and current market needs. The result has been the loss of market share against European rivals over recent decades.

During the Second World War, government controlled the market and major projects were concentrated into the hands of a group of modernised leading contracting firms. They developed national coverage and technical capabilities for diverse workloads. New management structures and processes emerged with management control delegated to branches and subsidiaries, signalling more complex lines of management with strategic and operational decisions being separated. Strategy remained in the hands of autocratic leaders, family members or small groups of trusted senior colleagues.

During the postwar reconstruction period, organic growth consolidated the market position of the leading main contractors. A few major contractors were emerging from the larger group of leading firms with increasingly diverse workloads and strong national coverage. The structures became more complex as the types of work diversified and grew in peacetime. Technical capabilities diversified with more diverse and changing workload, building on the experience of diversification from wartime.

In the mid 1950s and 1960s, British-owned main contractors were among world leaders after the Second World War, second only to the US contractors. It was a period of sustained growth. Management was reactive and increasingly defensive, focusing upon building and engineering types, and on projects as the units of management thinking. In this period, family control was gradually ceded to leadership and management by other senior management; they became more corporate. The span of control of board level and senior management was insufficient and line management deepened. Many of the large firms had floated on the stock market. Short-term financial criteria to maximise ROCE was emphasised at the expense of investment.

The 1970s saw the end of the long boom. Major contactors took on smaller projects with the pressure on overhead resources and the need to maintain turnover, yet had commenced rationalising regional offices. Cutting capacity and costs were undertaken by delayering each management level and by seeing all activity that was not directly generating revenue as an overhead. Management failed to develop company functions to help grow businesses and integrate supply chains at the operational level. Investment in technology to yield a profitable return or the development of management capabilities to support the systems integrator role was largely lacking. Main contractors were cash generators. Firm management continued to react to market forces rather than proactively managing the position of the firm within the market.

The period between 1980 and the turn of the 21st century was one of decisive decline for the British-owned main contractor. Failure to develop growth strategies led to a shrinkage of market share. The management of downturns and recessions has seen management uncritically cut expenditure in a layered fashion until targets are reached without critically asking what capacity and capabilities will be needed to take advantage of the upturn. Contractors from other European countries selectively invested and acquired firms in the UK and other markets.

Between 1993 and 1996, the top British contractors lost over 18% market share against European counterparts. This was dramatic compared to the construction professional service firms who chose to increasingly internationalise, an opportunity open to British contractors with the City of London as a finance centre for projects worldwide. Management continued to be inward looking and focused at the micro-level of operations. They were becoming more operationally professional as a result, yet this was not being supported at the firm level to meet the emergent demands of clients and to grow the firm, despite undertaking complex and sophisticated projects, such as nuclear power stations and the Millennium Dome.

After 2000, there was a period of growth until the Financial Crisis. Main contractors failed to use the growth period to reform management practice in the firm to support the previous reforms in operational performance. British-owned contractors became minor players among European players and of reduced importance in the top tier by size in the UK market. The management of the main contractor, especially the large British-owned firms, appears misaligned with the demand in the marketplace.

The size of projects and the complexity of many means that organisational capabilities need to support construction project capabilities. The organisational capabilities include an outward focus to foster growth. While share markets and financial management have some responsibility, it is the task of management to address and balance the full range of management responsibilities. This need was given further impetus in the post-2008 economic climate of low interest rates, whereby ROCE can no longer be relied upon as a key component of the main contractor’s business model. Contractors have failed to respond.

CONCLUSION

The lessons of prior periods have not been learned and the two major British-owned contractors of recent times, Balfour Beatty and Carillion, have both suffered, fatally in the Carillion case.

Short-term transactional management prevails at a time when the economy needs transformation of its physical and social infrastructure for the health of the economy and society in general and for the post-Brexit environment.

The leading British-owned main contractors need to be transformational to take on and address the most complex and demanding projects and megaprojects to meet market and societal demands.

This is a summary of the full report *Castles in the air: the evolution of British main contractors*, available on The Bartlett School of Construction and Project Management website:
ucl.ac.uk/bartlett/construction/castles-in-the-air

Professor of Project Enterprises
UCL Bartlett School of Construction and Project Management
h.smyth@ucl.ac.uk

The Bartlett School of Construction and Project Management
1-19 Torrington Place, London, WC1E 7HB | +44 (0)20 7679 8263
ucl.ac.uk/**construction**