

Economic Appraisal of the North East Manufacturing and Productivity Service Post 2008

ONE North East

06 December 2007

Services for life

Document control sheet

Client	ONE North East
Document Title	Economic Appraisal of the North East Manufacturing and Productivity Service Post 2008
Version	03
Status	Final
Reference	Projects/ONE CPRG Appraisal
Author	Victoria Turner
Date	28 September 2007
Further copies from	email: documents@tribalgroup.co.uk quoting reference and author

Quality assurance by:	David Smith-Milne
-----------------------	-------------------

Document history			
Version	Date	Author	Comments
01	03 September 2007	Victoria Turner	
02	28 September 2007	Julie Longden	
03	06 December 2007	D Smith-Milne	Finalised

Contact details			
Main point of contact	Telephone number	Email address	Postal address
David Smith-Milne	0161 902 1150	David.smith-milne@tribalgroup.co.uk	Parkway House Palatine Road Manchester M22 4DB

Contents

1 Introduction and background 1

1.1 Introduction..... 1

1.2 Project Description 1

1.3 Service Offering..... 2

1.4 Project Objectives 10

2 Strategic and Policy Context..... 12

2.1 Introduction..... 12

2.2 National Overview 12

2.3 Regional Overview 15

2.4 Summary 16

3 Socio-Economic Context..... 18

3.1 Introduction..... 18

3.2 North East Regional Economy 18

4 Market Context..... 21

4.1 Introduction..... 21

4.2 The Global Market..... 21

4.3 The UK Market 22

4.4 The North East Market 23

4.5 Summary 24

5 Rationale 25

5.1 Introduction..... 25

5.2 Underlying rationale for the four programmes..... 25

5.3 Rationale for integrating the four programmes..... 25

6 Options Identification..... 27

6.1 Introduction..... 27

6.2 Long List..... 27

6.3 Forming the Short List 28

6.4 Short listed Option One – Do Minimum (baseline case) 31

6.5 Short listed Option Two – Integration of the 4 Projects..... 32

6.6 Short listed Option Three – Integration of the 4 Projects using an SPV 33

7 Benefits 34

7.1 Introduction..... 34

7.2 Key Benefits 34

7.3 NTF 1 jobs created and / or assisted 34

7.4 NTF 4 companies receiving assistance 34

7.5 NTF 6 skills..... 35

7.6 Gross Value Added (GVA)..... 35

7.7	Private sector contributions	35
7.8	Net Additional Jobs	36
7.9	Summary	39
8	Financial and Economic Appraisal	40
8.1	Introduction	40
8.2	Optimism Bias and Social Time Preference Discount	40
8.3	Benefits Profile	41
8.4	Summary	42
9	Financial analysis of the preferred option	43
9.1	Introduction	43
9.2	Revenue costs	43
9.3	Overheads costs	43
9.4	Direct delivery costs	44
9.5	Redistributing costs between fixed overhead and direct delivery	45
9.6	Improved output cost effectiveness	46
9.7	Summary	47
10	Risk and sensitivity analysis	48
10.1	Introduction	48
10.2	Sensitivity analysis	49
10.3	10% increase in all costs	50
10.4	15% decrease in net jobs created / safeguarded	50
10.5	50% reduction in overall efficiency gains	51
10.6	Combined impact of all scenarios	51
10.7	Criticality test	52
10.8	Other risks	52
10.9	Summary	52
11	Delivery	54
11.1	Introduction	54
11.2	The Procurement Process	54
11.3	Performance Requirements	54
11.4	Procurement Timeframe	55
12	State Aid	56
12.1	Introduction	56
13	Monitoring and Evaluation	57
13.1	Introduction	57
13.2	Management Structure	57
13.3	Monitoring and Evaluation	57

Executive summary

Introduction

1. This document is the economic appraisal for the North East Manufacturing and Productivity Services programme post 2008 (the programme). The document sets out, using standard and recognised techniques an appraisal of the options available for delivering the programme 2008. The analysis includes a detailed financial and economic appraisal. The document has been prepared for ONE North East (the Agency) to support the decision making of its Board and to secure the approval from the Central Projects Review Group for some £32, 190,105 to cover funding for the project between 2008 and 2013.

The programme

2. The Agency currently invests in a number of manufacturing and productivity support projects including; North East Productivity Alliance (NEPA) Best Practice, which is currently provided by Agency staff, Energy Resource Efficiency (NEPA Energy), Design in Manufacturing (NEPA Design) and the Manufacturing Advisory Service (MAS) which is currently provided by the Regional Technology Centre. Both the MAS and NEPA services are highly regarded by manufacturers in the region and have achieved excellent results to date. The NEPA brand has come to represent the highest quality standards and the service has developed a tried and tested and highly successful methodology. A full description of the individual projects that make up the programme is detailed in section 1.2.

Rationale

3. The main justification for the four programmes includes:
 - A systematic under-investment in skills: Human capital theory assumes that firms are perfect competitors for labour, whereas in practice firms often perceive it to be the case that they will not fully maximise the benefits of investments in the skills and capability of their workforce. Therefore, as papers by Margaret Stevens (Nuffield College, Oxford), Daron Acemoglu (LSE) and Ken Burdett and Eric Smith (University of Essex) and countless others show, employers are not always fully compensated for the costs of general training and will – at times therefore – acquire too little.
 - Information failure with respect to benefits/opportunities of investment in process change and innovation: There is asymmetry in the information available to innovators and experts in manufacturing process improvement and that which is available to those that could benefit from those innovations and processes. At a very simple level developers innovate without full understanding of the range of potential commercial applications and commercial organisations are not fully aware of the potential applications of new innovations. The market fails therefore to fully exploit innovations.
4. The programmes individually and on a consolidated basis are wholly compatible with current regional and national policy. In July 2004, the Government published a review of the 2002 Manufacturing Strategy and its achievements. It set out priorities for the future in an action plan, within which ‘high skilled, high performance workplaces’ and ‘promoting best practice’ are key priorities. The Cox review of Creativity in Business concludes that innovation is the only way for the UK manufacturing sector to survive and compete within the global market. Manufacturers need to embrace creativity, innovation and design to develop high-end, niche products for the future. The project makes a clear contribution to the Regional Economic Strategy, and is also in line with the Government’s Business Support Simplification agenda.
5. The rationale for integrating the four programmes into an single and consolidated programme includes:

- **Greater demonstrable economic impact** - One NorthEast recognises the importance of the NEPA and MAS brands in ensuring a service is available to all who need help manufacturing and productivity. However the Agency also recognises the importance of prioritising scarce resources and are, therefore, looking to put in place a high-quality service offering, which allows for resources to be targeted at areas of maximum impact.
- **Greater efficiency** - The new operation will be more efficient in terms of unit costs; back office costs; staffing ratios and customer resource.
- **Greater consistency** - In seeking greater consistency the aim is to ensure that any differential levels and types of service are based on market failure, impact rationale or the need for evidenced targeted support. The new service will result in a consistent framework of support across the region, including targeting at sector.
- **Contribute towards the Business Support Simplification Agenda** - The proliferation of business support initiatives in the North East and consequent confusion amongst business clients is well documented. Integrating the combined activities of MAS/NEPA builds upon the Government's Business Support Simplification Programme.

Options

6. Three options were short-listed from a long-list of seven. The three that are considered throughout the appraisal. These are:
 - Option 2: Continue to deliver projects as four individual projects (i.e. a "do minimum" option)¹;
 - Option 3: Deliver the four projects as part of an integrated programme, via a contract with a third party operator (or consortium of operators); and
 - Option 4: Deliver the four projects as part of an integrated programme under the management of a Special Purpose Vehicle.
7. These options were selected from a long list on the basis that they achieved maximum impact against the following criteria:
 - Greater economic impact
 - Greater efficiency
 - Greater Consistency
 - Protecting/developing integrity of brand
 - Contribution to RES
 - Attractiveness to bidders
 - Knowledge transfer between projects and customers
 - Providing a single gateway for manufacturing services

¹ Whilst strictly speaking this is not a do minimum or nothing option, the four projects would have proceeded without being integrated, and thus, for the purpose of the appraisal, this option is that which closely mirrors a no change scenario.

- Contribution to the simplification agenda
- Improving quality of service
- Minimising risk to the public sector

Quantifiable benefits and impacts

8. Table E1 sets out the overall quantifiable benefits that are achieved via the three short-listed options.

Table E.1 NTF Overall quantifiable outputs

Gross outputs	Option 1	Option 2	Option 3
NTF 1: Jobs Created and / or Safeguarded	7,778	8,245	7,707
NTF 4 Companies receiving assistance	4,067	4,311	4,030
NTF 4 skills	12,477	13,226	12,363
Gross Value Added (£)	99,062,635	105,011,173	98,159,673
Private sector Leverage:			
In Kind (£)	6,475,000	6,475,000	6,475,000
Cash Contribution (£)	3,316,670	3,316,670	3,316,670
Net Impacts			
Net Jobs Created / Safeguarded	4,954	5,251	4,908
NET MONETISED BENEFIT (GVA) (£000)	63,089,278	66,877,678	62,514,215
Present Value of Net Monetised Benefit (£000)	56,714,552	60,120,162	56,197,595
Present Value of GVA	56,714,552	60,120,162	56,197,595
Present Value of Public Sector costs	38,302,880	38,302,880	40,011,911
Net Present Value	18,411,672	21,817,282	16,185,684
Cost to benefit ratio	1:1.48	1:1.57	1:1.40

Financial analysis of preferred option

9. Option 2 is the preferred option. It produced the strongest NPV and benefit to cost ratio and scores strongly against the main “soft” criteria for the options appraisal, as outlined at 7 above. A summary financial analysis of the option is presented below.

Table E.2 Overall revenue costs, option 2 (preferred option)

	2008/9	2009/10	2010/11	2011/12	2012/13	Total
<i>Salaries & Staff Costs</i>	1,740,619	1,827,650	1,919,032	2,014,984	2,115,733	9,618,019
<i>Training</i>	100,000	100,000	100,000	100,000	100,000	500,000
<i>Travel & Subsistence</i>	146,460	149,389	152,377	155,425	158,533	762,184
<i>Recruitment</i>	29,669	30,263	30,868	31,485	32,115	154,400
<i>Equipment & Clothing</i>	156,269	159,394	162,582	165,834	169,150	813,228
<i>Marketing</i>	101,098	101,098	101,098	101,098	101,098	505,490
<i>Development Costs</i>	7,000	7,000	7,000	7,000	7,000	35,000
<i>Rent & Running costs</i>	327,318	327,318	327,318	327,318	327,318	1,636,590
<i>CRM System</i>	200,000	50,000	20,000	20,000	20,000	310,000
<i>Design Costs</i>	252,250	252,250	252,250	252,250	252,250	1,261,250
<i>Productivity Needs Diagnostics</i>	393,640	531,699	531,699	531,699	531,699	2,520,436
<i>Business Support & Training of Companies</i>	2,253,766	3,472,908	3,776,591	3,967,280	3,839,634	17,310,178
<i>Evaluation Costs</i>	10,000	10,000	20,000	20,000	20,000	80,000
	5,718,089	7,018,969	7,400,815	7,694,372	7,674,530	35,506,775

10. The analysis of the preferred option sets out specifically how and why there are clear commercial / financial benefits in consolidating the four programmes. One of the main benefits of this consolidation process is in the ability of the programme to redirect resources from fixed overheads (e.g. accommodation, travel etc) towards direct delivery costs (i.e. time and money spent with individual businesses). This redirection of resources allows an increase in the amount of direct delivery activity and therefore outputs and outcome. Because this increase is achieved via redirecting resources within the programme, the overall cost effectiveness of the programme also increases.

Risk analysis

11. The economic appraisal presents a risk and sensitivity analysis of a range of different financial scenarios in order to test the level of sensitivity the programme has to particular risks. Three main risks are identified here: a 10% increase in overall costs; a 15% reduction in outputs; and a 50% reduction in the efficiency savings achieved via consolidating the four projects. That risk analysis indicates that the model for the combined programme is most sensitive to a reduction in the net amount of jobs created / safeguarded. Just a 15% reduction results in a 27% increase in the cost effectiveness of the programme (as measured by the unit cost per net job created / safeguarded). If we combine this sensitivity with two others – a 10% increase in overall cost and a 50% reduction in efficiency gains achieved by combining the programmes, the overall effect is a 32% increase in cost effectiveness. Criticality testing also reveals that a 1.0% decrease in net additional jobs leads to a 2.1% decrease in the value of the economic NPV, which is a critical result. Criticality testing on the other two variables under this option demonstrates that they are both near critical.
12. Other risks include the project are: failure to secure ERDF funding, failure to gain CPRG or Treasury support for the project and risks to the current exemplary reputation of the MAS/NEPA brands and service.

- In the case of ERDF, the picture will become clearer after March 08. The Agency has taken a cautious but prudent approach to the level of ERDF to be requested and work is underway to try to ensure that the anticipated level of ERDF for MAS-NEPA is secured. However, draft plans are in place to scale back the project if necessary. This will lead to reduced outputs but will ensure that the project can still go ahead.
- With regard to CPRG/Treasury approval, an early meeting took place to seek their views from the start of the project development in July. A further meeting took place on 6th November to discuss ongoing development and feedback was extremely positive. At this stage, they are indicating support for the proposed approach.
- The question of a risk to the integrity of the brand and service is being taken very seriously and is a key consideration both in choosing the successful bidder through the OJEU process and in management arrangements of the new service once in place. Also a detailed transition plan is being developed. The Agency will be strongly represented on the Governance arrangements for the new service.

Delivery

13. The new service will be procured under OJEU and will be managed via a contractual arrangement. Stringent contractual controls will be agreed and applied where necessary.
14. The proposed bidders will be required to have the following attributes which are commensurate with those of One NorthEast, these include:
 - To have extensive knowledge of the manufacturing sector;
 - To possess credibility and expertise in delivering productivity, lean manufacturing, resource efficiency, design and other related services;
 - To be able to demonstrate an in-depth knowledge of the North East economy and manufacturing sector and understanding of the strategic context and importance of the sector to the region;
 - To possess track record of managing similar scale projects and demonstrate clear commercial acumen; and
 - To be able to demonstrate how they will boost the economy of the North East by supporting manufacturing businesses to become more productive, competitive and deliver increased GVA.
15. The whole support offering will be delivered by a management team suitably qualified in the relevant project disciplines. The overall governance will be by the following procedures:
 - Appointment of a 'Nolan' compliant board to oversee outputs and develop future possibilities for interventions;
 - Six monthly reviews by the delivery managers with an agency representative to review outputs and achievements. This will also be seen as an 'ideas forum';
 - Quarterly claims to the agency;
 - A monthly operations meeting of the delivery managers and other delivery partners such as Envirowise, NEPIC and the Skills Academies;
 - Activity/intervention based reporting via a simple A3 format with benefit costings;

- MAS will be required to report to MAS centre as determined by BERR; and
 - An agency representative will attend all meetings other than ongoing operational meetings.
16. It is expected that success stories will be published in journals and local press to promote the brand and support from One NorthEast

State aid

17. The Dissemination of Best Practice and Energy Resource Efficiency projects operate under Training Block Exemption rules, MAS operates under SME Block Exemption rules, and the Design in Manufacturing activities will be operated under Deminimus and Training Block exemption rulings in parallel. These are all in the process of being notified for the MASNEPA joint project which will run out to 2013

Monitoring and evaluation

Monitoring

18. The Agency proposer will be responsible for overseeing the project which will be managed via contractual arrangement. The proposer has considerable experience of this type of project management, and is also responsible for the BLNE contract.
19. The project will be monitored by Business & Industry Team in line with the Agency's business process. The Agency will put in place a monitoring group which will receive and verify all claims. The key monitoring system will consist of:
- Every 6 months a full monitoring audit will take place on each project. This can be increased to quarterly depending on performance (risk).
 - Every 6 months visits will take place to recipient companies picked at random to audit trail documents and outcomes. This will take place for each project.
 - Engagement with organisations such as ONS, NERIP and universities will allow for ongoing economic impact monitoring of the projects. This should be measured in terms of individual beneficiaries as well as company beneficiaries

Evaluation

20. ONE North East is currently working up a formal evaluation strategy for NEPA–MAS. This will focus on the extent to which interventions help raise productivity, turnover and employment in supported firms. In addition, work will attempt to quantify the impact on the wider regional economy. Establishing an appropriate counterfactual will be particularly tricky with this type of support. And the impact of our support for individual firms is likely to build up over a period of time. No single research method will deliver a thorough evaluation of MAS-NEPA. So we expect to adopt a range of methods to improve our understanding the effects of our investment. This will include: case studies of individual interventions and the impact on working practices; detailed monitoring of company performance from first point of contact onwards; and quantitative analysis to benchmark company performance against other firms and over time.

1 Introduction and background

1.1 Introduction

1.1.1 This is the Draft Interim Economic Appraisal of the proposed Manufacturing and Productivity Services Post 2008 project. Specifically it sets out – using standard and recognised techniques an appraisal of the options available for delivering this “programme” post 2008. The analysis includes a detailed financial and economic appraisal. In this section we set out a definition of the proposed project, a description of its proposed service offering as well as its objectives and anticipated quantifiable outputs.

1.2 Project Description

1.2.1 In April 2007, One NorthEast made a decision to move towards providing a more integrated regional manufacturing and productivity service post 2008. This new service will incorporate the national enhanced Manufacturing Advisory Service (MAS). It will also incorporate a range of other related manufacturing support activities which are currently delivered as separate initiatives. These include the current North East Productivity Alliance Best Practice Dissemination Project (NEPA BP), NEPA Energy, and NEPA Design. These elements will be delivered as a single, integrated service to the manufacturing sector across the region under the name of the MAS-NEPA service. Other related services may also be delivered via this route in the future.

1.2.2 The main objectives for integrating these services is to present a single integrated offering to manufacturing companies in the region, achieve greater economies of scale, improve sharing and learning, and improve the customer experience. The Department for Business, Enterprise and Regulatory Reform (BERR) has been advised of this project and has expressed strong support for the approach.

1.2.3 It has been agreed that the new integrated Manufacturing and Productivity Service Post 2008 will be delivered externally from One NorthEast and procured by undertaking an OJEU procurement process.

1.2.4 Following on from discussions with BERR, One NorthEast would like to recommend that the new integrated manufacturing service is known as “MAS-NEPA” and is branded as such. This will enable both the MAS and NEPA brand to continue to feature prominently as the key brands which are recognised by North East manufacturing companies. One NorthEast is keen to ensure that the integrity of the NEPA brand and the quality of the services are protected in the new integrated offering.

1.2.5 The Manufacturing and Productivity Services Post 2008 will be funded through a mixture of Single Programme investment and European Regional Development Funds as well as national funding for the MAS service and private sector cash and in-kind contributions².

1.2.6 In undertaking this project, 4 core objectives will be fulfilled:

- Protect the integrity of the MAS and NEPA brands and maintain continued association of the NEPA brand with One NorthEast;

² NEPA Best Practice and MAS in their current form have been supported by Single Programme, since April 2002 and April 2005 respectively. However, these elements will be incorporated into a single, enhanced offering within this project which will be delivered in a wholly integrated way. The project is therefore presented as new activity and not a continuation. Confirmation of this approach has been obtained)

- Safeguard the quality of the MAS and NEPA service and ensure that the programme continues to develop and improve;
- Maintain a significant degree of influence by One NorthEast to ensure the ongoing quality of the service; and
- Examine the current NEPA funding methodology and test the market for companies' ability to pay towards the service going forward.

1.3 Service Offering

National Policy

- 1.3.1 BERR (formerly DTI) led a review of the Manufacturing Advisory Service (MAS) as part of the current Comprehensive Spending Review (CSR). Its purpose was to inform policy-making; give a view on the overarching Government approach to business support delivery models; and consider associated public spending decisions. The review was published in January 2007 and informed BERRs current position.
- 1.3.2 BERR has stated that MAS has a fundamental role to play in manufacturing business support and believes that the MAS brand and image should also be used for other publicly funded services which support manufacturing business in relation to lean manufacturing, best practice, product innovation, resource efficiency and related business support services.

Regional Position

- 1.3.3 In April 2007, One NorthEast made a decision to move towards providing a more integrated regional manufacturing and productivity service post 2008. This new service will incorporate the national enhanced Manufacturing Advisory Service (MAS). It will also incorporate a range of other related manufacturing support activities which are currently delivered as separate initiatives. These include the current North East Productivity Alliance Best Practice Dissemination Project (NEPA BP), Energy Resource Efficiency (ERE) and aspects of the Design in Manufacturing project. These elements will be delivered as a single, integrated service to the manufacturing sector across the region under the name of the MAS/NEPA service. Other related services may also be delivered via this route in the future.
- 1.3.4 The main objectives for integrating these services is to present a single integrated offering to manufacturing companies in the region, achieve greater economies of scale, improve sharing and learning and improve the customer experience. BERR has been advised of this project and has expressed support for the approach.
- 1.3.5 It has been agreed that the new integrated manufacturing and productivity service post 2008 will be delivered externally from One NorthEast and procured by undertaking an OJEU procurement process.
- 1.3.6 Both the MAS and NEPA brand will continue to feature prominently as the key brands which are recognised by North East manufacturing companies. One NorthEast is keen to ensure that the integrity of the NEPA brand and the quality of the services are protected in the new integrated offering.
- 1.3.7 The Manufacturing and Productivity Services Post 2008 will be funded through a mixture of Single Programme investment and European Regional Development Funds as well as national funding for the MAS service. (NEPA Best Practice and MAS in their current form have been supported by Single Programme, since April 2002 and April 2005 respectively. However, these elements will be incorporated into a single, enhanced offering within this

project which will be delivered in a wholly integrated way. The project is therefore presented as new activity and not a continuation. Confirmation of this approach has been obtained)

1.3.8 In undertaking this project, 4 core objectives must be fulfilled.

- Protect the integrity of the MAS and NEPA brands and maintain continued association with the NEPA brand with One NorthEast
- Safeguard the quality of the MAS and NEPA service
- Maintain significant degree of influence by One NorthEast to ensure the ongoing quality of the service
- Examine the current NEPA funding methodology and test the market for companies' ability to pay towards the service going forward

1.3.9 The new service will contain the following key elements:

Manufacturing Advisory Service (MAS)

1.3.10 MAS is the national brand and service for manufacturing, supported by the Department of Business, Enterprise and Regulatory Reform (BERR). Currently the MAS offering to small and medium sized businesses is based on a rapid response service for urgent and short-term problems. MAS activities include:

- Enquiry Handling – A free service to provide information, solve an urgent problem or identify specialist help.
- Diagnostic Visit – A free half day visit to the company by a MAS specialist who will provide an immediate solution or an agreed action plan.
- Extended Diagnostic –Further consultancy where substantial progress can be made in a two day time scale.
- Full Consultancy – MAS will fund longer term assistance at 50% funding for a consultancy project for up to ten days.

1.3.11 The principal focus of this new phase of MAS remains in place and approximately 80% of overall programme resource is to be directed at the traditional MAS audience, by delivering existing services, using existing tools and methodologies. However this new phase introduces a number of additions to the range of MAS services and in particular, aims to offer longer term and more strategic support to clients. Clients will also be able to access consultancy support for up to 20 days in the new arrangements. These additions are not expected to account for more than 20% of overall programme resource.

1.3.12 From 2008 the enhanced MAS (based upon a nationally agreed specification to be signed off by September 2007) will offer the following additional services;

- A programme of visits to best practice exemplars
- Assistance in finding supplies, services or equipment
- Assistance to companies who want to improve their resource efficiency
- Assistance to companies developing and/or introducing new products

- Help for companies to work within a Supply Base or work with Supply Chains
- Help for companies to develop a medium to long term manufacturing strategy
- Help for companies to apply lean techniques across the whole enterprise.

Design Helpline Support for SMEs

- 1.3.13 To supplement the MAS offer, this project includes additional investment for helpline support for small and medium sized enterprises. This will be a light touch intervention which guides and signposts SMEs around the provision currently available within the region. This will be a responsive and informative service operated by experienced professionals who understand product innovation and design within the manufacturing sector and have detailed understanding of the regional business support provision within this area.
- 1.3.14 Advice and guidance will be given under the following main headings:
- Developing, embedding and resourcing, a product innovation strategy and process.
 - Idea generation and business case development for new products, particularly focusing on linking the technical aspects of product development with the commercial and branding aspects of the business.
 - Detailed design and analysis tools and techniques for new products.
 - Prototyping and testing, tools and techniques for new products.
- 1.3.15 The range of advice and guidance currently available within the MAS offer covers other aspects of the product development process e.g. design for manufacture and validation and therefore this will supplement what is available rather than duplicate services.

North East Productivity Alliance (NEPA)

- 1.3.16 In order to complement the MAS offer, which focuses on SMEs, and to ensure that the manufacturing sector as a whole can access quality support to increase productivity and competitiveness, a range of other activities will be supported within the project and marketed under the NEPA brand. These services are targeted primarily at mid-corporates and large companies and include the following:

NEPA Best Practice

- 1.3.17 NEPA Best Practice was originally set up in 2001 as a direct response to the heavy loss of manufacturing companies in the region. Emerging out of a consultation group comprised of Universities, Colleges and Nissan, its objective is to ensure that the North East is not only the most productive manufacturing region in the UK but an exemplar region from which other regions can learn and benefit. NEPA Best Practice is currently delivered by Agency staff and has three elements, engineering secondments, 'Narrow and Deep' programme, and bespoke productivity improvement. Since 2003, the NEPA Best Practice programme has created an average of 38 jobs, safeguarded 1028 jobs, assisted 75 businesses and generated 1,259 learning opportunities annually and helped firms make savings worth £19 million.
- 1.3.18 Going forward, we will build upon this success but the new service will be offered as an integrated package of support and delivered outside of the Agency. This element of the new service is designed to deliver training in manufacturing best practice as a result of technology transfer, utilising global best practice, linked to a productivity needs diagnostic.

Through specific activities tailored to meet the diagnosed needs of each company, the workforce is engaged to solve problems which will lead directly to productivity improvement. The objective of any productivity improvement is to assist a company to improve its competitive position in the market place.

- 1.3.19 Through analysis, companies are made aware of the potential effects of adopting new technology, both to their production lines and to their staff. All clients are encouraged to network in technology clusters based on knowledge requirements and ability levels. Supply chains within the region are investigated for all participating companies.
- 1.3.20 Key to the Best Practice methodology is the concept of bringing all staff within companies to the concept of learning, via the NVQ route or through more specific training such as senior management workshops, change management, leadership, and workshop management programmes. This training addresses both the climate and systems within an organisation and complements the core activity of the project.
- 1.3.21 This is delivered using two resource streams:
- Selected engineers from local industry who are seconded to the project as NEPA Engineers. These engineers are trained to a national standard in manufacturing best practice by a recognised third party and then disseminate this knowledge within local manufacturing companies.
 - A panel of approved suppliers who have been selected using an OJEU process.
- 1.3.22 Productivity interventions are delivered within companies to provide specific training in the tools of Lean Manufacturing, using 2 principal routes:
- A 15 day masterclass model led by NEPA engineers, which enables employees to understand the tools of lean manufacturing and utilise them in a specific way to make productivity improvements. This method is also used to train nominated Change Agents within companies to NVQ Level 3 in Business Improvement Techniques (BIT) over an extended period.
 - Productivity interventions in the form of workshops designed to suit the specific needs of predominantly smaller companies, more flexible in method and duration, led by a nominated supplier to the project chosen from the approved panel. These will be delivered as a joint MAS/NEPA offering.
- 1.3.23 The current funding methodology for NEPA Best Practice is based upon 100% subsidy for the first intervention, although the company invests significantly in terms of support in kind and downtime etc. The funding model needs to clearly express the real value of the company contribution.
- 1.3.24 As part of the new arrangements, this model will be examined to investigate the companies' ability to pay in order to generate income which will be invested to further develop the service. There will also be a charge for any subsequent interventions.

NEPA Energy

- 1.3.25 The Energy Resource Efficiency Project (ERE) was established in 2006-7 to help businesses tackle rising energy costs. It is currently delivered by NE Life. A team of specialist engineers has been seconded under the guidance of industry experts. The team works closely with firms to develop energy action plans, analyse current usage and highlight innovative ways of cutting bills. Thirty six organisations are currently working with the ERE programme with a further 22 about to join. An early success for the project is where ERE experts worked with a regional manufacturing company and identified that by

installing a heat recovery system on an ink drying machine this would potentially yield 60% less energy use. The company hopes to save in excess of £100,000 per annum from its current electricity bill which equates to over 10% of its total electricity costs.

- 1.3.26 ERE will now be incorporated into this project as NEPA Energy and be delivered as an integral part of the MAS/NEPA service. The element of the project will provide additional support for manufacturing industries in the region to manage their energy needs effectively. Energy intensive industries have, in many cases drawn on existing support services in this area, but now require a more innovative and sustainable way of managing their energy needs. Many industries have not as yet developed or are able to develop a strategy to address energy price increases.
- 1.3.27 NEPA Energy will draw on and enhance the services currently provided by the Carbon Trust, Envirowise and Midas etc. It will be fully integrated into the wider business support network to ensure that this specialised offer is utilised and capable of engaging companies in wider support to meet identified needs.
- 1.3.28 The current funding methodology for ERE is based upon 100% subsidy for the first intervention, although the company invests significantly in terms of support in kind and downtime etc. The funding model needs to clearly express the real value of the company contribution.
- 1.3.29 As part of the new arrangements, this model will be examined to investigate the companies' ability to pay in order to generate income which will be invested to further develop the service. There will also be a charge for any subsequent interventions.

NEPA Design

- 1.3.30 This element of the project aims to support the region's manufacturing sector to develop and improve their product innovation capacity. The main thrust of the service is in-depth and hands on support to help larger manufacturers adopt more structured and formal approaches to product innovation. The project aims to support around 30 companies each year and impact will be measured by speed of product introduction as well as number of new products introduced to the market.
- 1.3.31 NEPA Design has been developed to support the region's manufacturing sector to support their product innovation capacity. It has been developed following significant consultation and desk research with a number of the regions key manufacturers, business support professionals, educationalists and research.
- 1.3.32 The following key strands of support were identified as the areas which could provide the greatest return on investment:
- Helpline support for SMEs – a light touch, signposting service for those undertaking product innovations, highlighting areas of support and expertise within the region. (See above)
 - Product innovation capacity – an in-depth hands on service supporting manufacturers to adopt a formal approach to product innovation. Training and support will be given to the business over approximately 18 months. Subjects will include idea generation techniques, technology tracking and trend data, 3D design and analysis, prototyping techniques, commercial assessment techniques, brand and marketing and project management.

Product Innovation Capacity

1.3.33 This strand will provide specialist skills support to businesses to increase the Product Innovation capacity amongst employees. (Note: **The Product** is that element of the business process which is being re-designed as a result of the diagnostic process.)

1.3.34 This will take the form of an in-depth long term intervention that works alongside the business to identify strategic training activities to enable and improve product development and innovation capacity. Key to the success of this will be the quality and experience of the team responsible for the development and management of the individual interventions with businesses.

Step one – Introduction and diagnostic/benchmarking

1.3.35 Relationship building and undertaking an independent diagnostic of the product innovation capacity within the business.

1.3.36 Introduction and ongoing account management will be provided by one of the experienced NEPA product innovation engineers.

1.3.37 The diagnostic will provide an opportunity to look at the business as a whole, provide a benchmark for future development and to focus on key aspects of the product innovation process. These include:

- Idea generation
- Concept development (including drafting technical and design briefs)
- Detailed design, scoping and commercial strategy development
- Prototyping and testing
- Design for manufacture
- Hand over to manufacture

1.3.38 As a result of the company diagnostic training, the business will have a demonstrable new methodology to reduce lead times. As a direct result a company may reduce the lead time of a new product to market, or an existing product enhancement campaign, by up to 30%.

Step Two – Action Plan

1.3.39 The product innovation engineer will discuss the findings of the diagnostic with the business and agree the design action plan for that business. The action plan will identify:

- The key actions to be undertaken
- The target beneficiaries within the business for each action
- The proposed delivery mechanism e.g. 1-2-1, 1:many, training provider etc.
- The resources required, from both the business and the project
- The planned programme and timescales
- The agreed management, monitoring and communication plan

Step Three – Delivery

- 1.3.40 The Action Plan is likely to include a number of interventions taking place over a 12 month period, after which a review of progress and continuing requirements will take place. It is likely that most action plans will be complete after 18 months, in exceptional circumstances this can be extended to 24 months.
- 1.3.41 Level of support available to each business will vary, subject to assessment as part of the diagnostic, based on need and potential return on investment and ability to contribute to costs. The business model is based on up to £15,000 worth of training support available to each business over this period along with support and management provided by the engineers. However this will vary significantly based upon the assessment criteria. Any contribution/charging policy that may be introduced at a later date will be done in line with other elements of this project and with similar publicly supported programmes.
- 1.3.42 Training suppliers will be sought via an OJEU tendering process to enable a supplier database to be set up which covers each of the main areas of the Product Innovation Process. Each will be tailored specifically to the needs of the individuals, their role and the sectors they operate within. It will be the Senior Engineer's responsibility to manage the panel of providers and account manage each of the businesses throughout the delivery phase.
- 1.3.43 Figure 1.1 (over-page) provides a pictorial representation of the overall programme, including how the various components of it relate to one another and importantly to the broader context of programmes that surrounds MAS-NAPA (e.g. Business Link). Figure 1.2 outlines the intensity of service available through the various strands of the programme and how these vary with company type (i.e. SME and larger company).

Figure 1.1: Overall programme structure

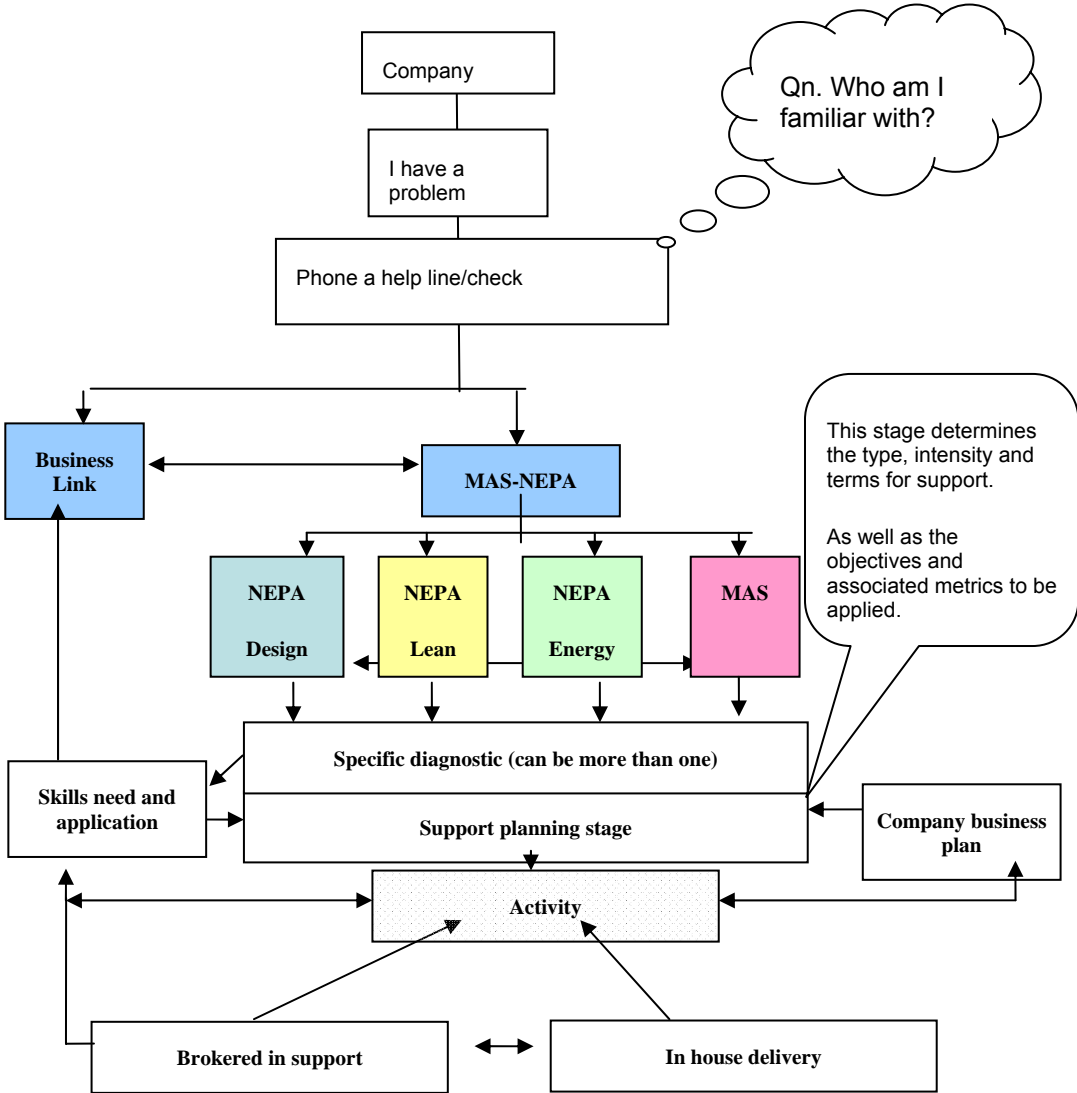
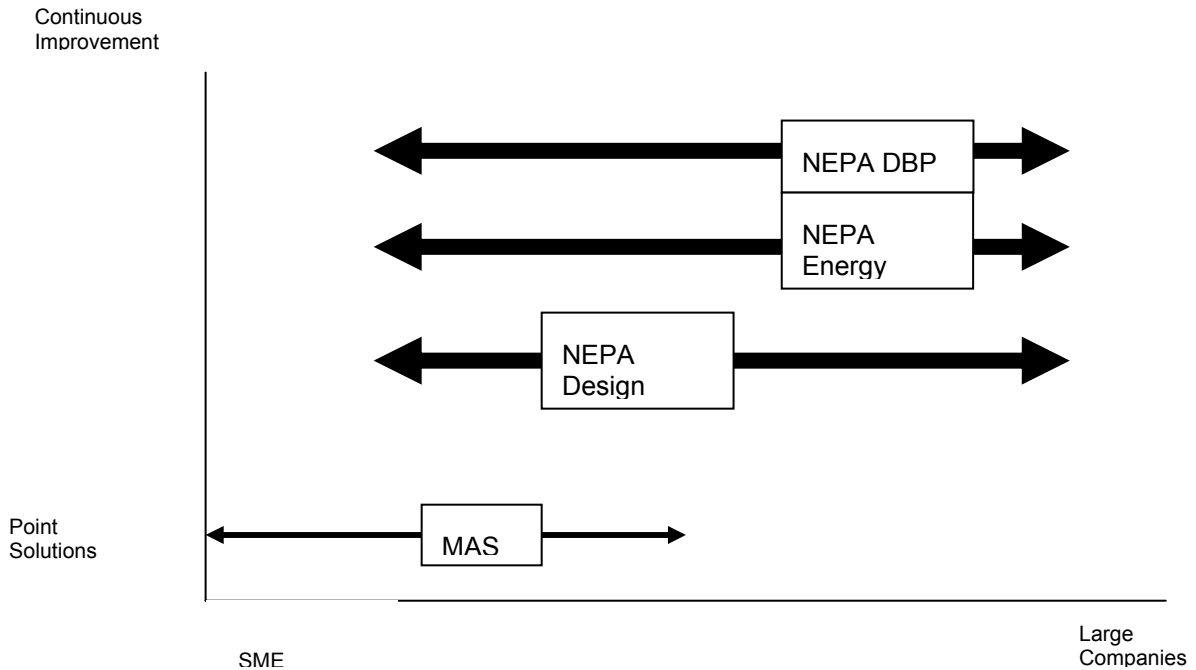


Figure 1.2: Intensity of Service



Key: Thickness of line = intensity of service

Customer Relationship Management

1.3.44 As part of the contractual arrangements with suppliers a customer relationship management process will be in place to ensure the Senior Engineer can monitor progress against the action plan and ensure that the aims and objectives of each intervention is achieved. This will ensure all short term/immediate outcomes and outputs can be reported.

1.4 Project Objectives

1.4.1 The new integrated manufacturing and productivity service will incorporate the national MAS, NEPA BP, ERE and aspects of the Design in Manufacturing project. Other related services may also be delivered via this route in the future therefore a flexible model which has the capacity to encompass additional services as deemed appropriate will be developed.

1.4.2 The main objectives of integrating these services are to:

- Greater economic impact
- Greater efficiency
- Greater Consistency
- Protecting/developing integrity of brand
- Contribution to RES
- Attractiveness to bidders
- Knowledge transfer between projects and customers

- Providing a single gateway for manufacturing services
- Contribution to the simplification agenda
- Improving quality of service
- Minimising risk to the public sector

1.4.3 There are clear opportunities to combine activities to gain considerable regional benefits in respect of efficiencies of expertise and synergies. BERR have also indicated that they would like to see these activities integrated.

2 Strategic and Policy Context

2.1 Introduction

2.1.1 In this section of the appraisal we consider the national and regional policies, programmes and initiatives that relate to this project. These sit principally within the Department for Business, Enterprise and Regulatory Reform (BERR), ONE North East and the Government Office for the North East. A summary of the main policies and strategies that have helped shape the Manufacturing and Services project post 2008 are presented hereon.

2.2 National Overview

Overview

2.2.1 Nationally the UK's poor manufacturing productivity relative to the US, Germany and France is well documented. The key challenges for the manufacturing sector nationally and in the region relates to competition from lower cost economies. Companies need to differentiate themselves, through their products, processes, human capital and service offerings so they compete on more than cost alone. This becomes increasingly important as the cost gap between the UK and elsewhere grows, as a result of local factors including the unstable cost of energy.

The National Manufacturing Strategy (2002) and Review (2004)

2.2.2 In May 2002 the Government published its Manufacturing Strategy. The importance of manufacturing to the North East and to the UK economy is reflected in this. It sets out a series of actions needed to create a high value, high skill manufacturing sector capable of introducing new products and processes into our economy, creating new markets, and delivering a huge boost to our prosperity.

2.2.3 The Strategy identifies 7 pillars and specific actions for each to help build a '*successful, knowledge intensive, highly-skilled manufacturing sector*'. One of the pillars is '*Best Practice – raising productivity and competitiveness by continuous improvement*'.

2.2.4 In July 2004, the Government published a review of the Strategy. This reviews the achievements to date and sets out a new action plan based on the 7 priorities including improving the skills base, promoting best practice, encouraging high value investment, investing in modern infrastructure, and promoting innovation.

2.2.5 This project will assist the Government in achieving these priorities and specific actions. The project will improve the skills and expertise of the current workforce using the NEPA best practice programme as the tool and benchmark to set the standard of the manufacturing sector in the region. It provides educational and learning opportunities for individuals and manufacturing companies, and promotes internationally renowned best practice techniques in this sector.

2.2.6 Similarly, MAS will assist manufacturing businesses in the region and enable them to better understand the modern manufacturing sector, encourage them to use alternative techniques and tools, and consider their own efficiency and capability through investing in high value products and processes, and new capital, and understanding all the potential innovation opportunities, that the region processes. This project will have a central role to play in the continuing changes to the manufacturing sector in the region, and the impacts this will have on the UK economy.

Catching up with the Continent – Final Report on EU and UK Manufacturing (2004) Productivity

- 2.2.7 This is the fourth report undertaken to assess UK's productivity performance against its EU competitors. It uses a sample of 600 companies in the UK, France and Germany to establish what drives and what constrains the performance of manufacturers focussing on the issues of skills, innovation and investment.
- 2.2.8 Currently, there are good signs for UK manufacturing with performance and productivity improving, and raising investment. There are however a number of important issues to address if sustained manufacturing is to be achieved. Some key statistics that came from the survey include:
- The UK has more small firms 84% compared to 68% in France and 65% in Germany;
 - 34% of UK firms are foreign owned compared with 20% in Germany and 12% in France;
 - There are lower rates in productivity growth in the UK compared to Germany;
 - Investment in UK firms is picking up but lagging behind the other two countries;
 - UK manufacturing has a poor image which has a negative impact on a firm's ability to attract the right people; and
 - The UK compares well on the proportion of companies undertaking all types of innovation activities e.g. products, processes.
- 2.2.9 Throughout this and the previous studies was a reoccurring theme, namely a series of factors contribute to productivity growth, these being – investment in skills, innovation and equipment. Failure to invest on one front could undermine another.
- 2.2.10 This project will contribute to ensuring these factors are enhanced across the manufacturing sector in the North East. NEPA best practice is aimed at not only improving the skills of the individuals but also at introducing new and innovative approaches to manufacturing and the processes involved. The conclusion of which is improving productivity and a company's ability to compete in the market place. MAS will assist in this by improving companies with the support, information and assistance they require. MAS will encourage business to generate new ideas and products, and understand product innovation and design.

The National Manufacturing Skills Academy (NMSA)

- 2.2.11 The NMSA initiative was launched in November 2005 by DfES. It is a central part of the government's skills strategy. The Academy will focus on meeting the skills needs of both large and small employers from the manufacturing sector, including Aerospace, Automotive, Electronics and Marine.
- 2.2.12 The role of the Academy is to increase the number of people training in engineering, leadership and management skills within the sector. The vision is *'to create training and education programmes which will set national standards for delivery and help employers to meet the demands of global competition in terms of improved productivity, competitiveness and profitability.'*
- 2.2.13 The Academy led employers and focused on consolidating the currently fragmented market of manufacturing skills training and on providing new industry-specific

development programmes for trainers and assessors validating them against new national standards. This will ensure that providers have the latest expertise, industry techniques and knowledge. As the NMSA develops, the skills and training packages developed as part of this project will be aligned with the Academy and delivered within it wherever possible.

- 2.2.14 This project ties in well with the aims and objectives of NMAS. NEPA best practice is an employer led initiative aimed at improving the skills and expertise of the current workforce. Collectively, these programmes can complement each other and provide individuals with the training needed to improve efficiency and productivity across a range of sub-sectors within manufacturing in the North East.

The importance of Design and Energy

- 2.2.15 The Cox review for Creativity in Business concluded that innovation is the only way for the UK manufacturing sector to survive and compete within the global market. Reducing costs and using lean manufacturing techniques will help but will not generate the new products and enterprise which businesses need to compete. Manufacturers need to embrace creativity, innovation and design to develop high-end, niche products for the future.

- 2.2.16 NEPA Design was created in response to the need to increase regional GVA by producing higher value products. A second need specific to this region is the fact that a major OEM (Nissan) is asking suppliers to diversify and reduce dependence on one customer. Many companies in the region are satellites of corporations and as such do not have a design capability. If companies are to compete against low cost economies they need to become agile and unique to offer new ideas with a rapid turnaround as cost effectively as possible.

- 2.2.17 NEPA Energy was created in response to two main demands/needs

- The cost of energy
- Global warming

- 2.2.18 The energy project was developed in response to a severe hike in energy prices in 2005/06 which forced the closure of Vald Birn (foundry) and a paper mill. In all 700 jobs were lost in a very short time frame.

- 2.2.19 The project trains manufacturing businesses in the skills necessary to utilise energy effectively and manage an unstable energy supply market, while remaining competitive and productive

- 2.2.20 Rises in energy costs affect manufacturing companies by increasing running costs, costs of transport and raw materials. Increases in domestic energy costs also cause the cost of living and therefore labour costs to increase over time. The inability of manufacturing companies in the North East to absorb these increasing costs was demonstrated by the loss of over 750 jobs during 2006 as a result of rising energy prices.

- 2.2.21 The Energy White Paper published on 23 May 2007 presents the government's energy strategy for tackling the long term challenges of climate change and secure, clean and affordable energy supply. The NEPA Energy project is aligned with 3 these goals::

- Cutting CO₂ emissions
- Maintaining the reliability of energy supplies

- Promoting competitive markets in the UK and beyond.

2.2.22 The technology Strategy Board (TSB), in its most recent call for £23m of funding states that “UK manufacturing is an important sector of the economy, which continues to evolve towards high-value, high-productivity, specialised solutions. ‘High value engineering’ In the UK has a bright future and is growing, but only by being competitive in the world’s open and unregulated markets.”

2.3 Regional Overview

Regional Economic Strategy (2006-2016), Leading the Way

2.3.1 In September 2006, the new Regional Economic Strategy (RES) was launched – ‘leading the Way’. The RES is about achieving sustainable, inclusive economic growth. It is based on 3 key themes – business, people and places.

2.3.2 The RES is focussed on improving productivity, and sets out specifically tailored support to specialist sectors including strategically important manufacturing sectors. The strategy aims to raise productivity, equip businesses in the North East with the products and processes needed to compete, improve skills for businesses, continue the commitment to R&D in the region, and investment in process industries, design and innovation. The RES wants to accelerate the recent success of businesses in the North East and focus investment on enhancing productivity, innovation and creativity that will encourage more competitive, sustainable businesses.

2.3.3 This project will contribute to the RES and the 3 key themes by building on the regional MAS and NEPA best practice, and the subsequent focus on spreading best practice in manufacturing, which combined with an effective and qualified skills base, will improve productivity in the region. Manufacturing companies will be encouraged to think outside the box, and understand the ease and attractiveness of the new products and processes of modern manufacturing. This project will assist the RES in achieving this, and improving the overall productivity of manufacturing businesses in the North East.

Manufacturing in the Regions – North East Report

2.3.4 The manufacturing sector in the North East employs over 175,000 people, representing one fifth of the region’s workforce, accounting for a larger proportion of employment and economic output than is the case for the UK. This is forecast to remain the same to 2010 and beyond. The RES recognises the need to support effectively businesses as they change and redefine their priorities, and central to this is the commitment and support needed in driving this sector. The RDA states that it will support the changes needed in the region’s manufacturing base to:

- Build on the manufacturing strengths;
- Help manufacturers to move up the value chain;
- Assist manufacturers to create new technology solutions which capitalise on developing the region’s science and research base;
- Promote best practice amongst the region’s manufacturers and encourage clusters and networking in the region, nationally and globally; and
- Promote the region as a place to manufacture, now and in the future.

2.3.5 These goals are embedded within the RES objectives aimed at supporting the National Manufacturing Strategy. Improving productivity and encouraging technological and

process innovation and investment in R&D are crucial to the future success of manufacturing companies in the region. This project will provide specialist skills support to businesses to increase their product innovation capacity, it will assist companies to understand the opportunities that innovation and best practice present, and will improve the regional skills base.

The North East Evaluation of Manufacturing and Productivity Activities

2.3.6 In 2006, an evaluation of the North East manufacturing and productivity activities was undertaken. Its core aim was to assess how the Agency could best utilise public resources in the areas of manufacturing and productivity. The main conclusions from this evaluation included that:

- the NEPA governance arrangement should be refined to better align it with its remit;
- the Best Practice Programme will need to investigate the issue of charging, introduced in a phased manner so as to continue the level of engagement currently enjoyed;
- the linkage between Best Practice and Workforce Development should be retained;
- MAS and NEPA products are systematically engaged in collaborative delivery, but there is little evidence of others operating at the same level; and
- there is scope to standardise and centralise diagnostic visits to companies. The PNA approach developed by NEPA represents good practice that could be built upon.

2.3.7 This evaluation illustrates the potential synergies this project offers the manufacturing sector in the North East, and in taking this project forward provides the platform for moving this sector into the next phase of developing a modern manufacturing sector in the region.

2.4 Summary

2.4.1 The Manufacturing and Productivity Post 2008 will incorporate the MAS, NEPA BP, ERE and aspects of the Design in Manufacturing project. These are central parts of the National Manufacturing Strategy and will contribute directly to its objectives by improving the productivity, performance and skills within the North East manufacturing sector.

2.4.2 BERR has stated that MAS has a fundamental role to play in manufacturing business support, and this project therefore will ensure that MAS and NEPA will continue to feature prominently in the development and growth of North East manufacturing companies.

2.4.3 At a regional level, the Manufacturing and Productivity Post fits in with the key objectives of the RES, and the key themes – business, people and places. Specifically, this project will:

- continue to accelerate the recent success of businesses in the North East and sustain our evolution to a high value added, internationally competitive economy.
- focus investment on enhancing productivity, innovation and creativity
- continue to enable more competitive, sustainable businesses to develop new products, processes and services; and

- improve the skills base of the regional workforce.

2.4.4 The Manufacturing and Productivity Post has the potential to link all the national and regional policies and strategies on the manufacturing sector, and play a central role in developing a framework capable of supporting companies in the manufacturing sector.

3 Socio-Economic Context

3.1 Introduction

3.1.1 In this section of the Appraisal we consider the socio-economic context for the Manufacturing and Services Project post 2008. Specifically, this section provides a summary of the main social and economic conditions that prevail in the region.

3.2 North East Regional Economy

Overview

3.2.1 The North East is home to 2.55 million residents³. Between 1995 and 2005 the North East population decrease by -1%, compared to growth of 4% nationally. However, from 2000-2005 the North East has attracted an additional 14,900 residents, equivalent to a 1% growth in resident population.

3.2.2 The long-term trend shows that Economic Activity rate within the region has increased over the past couple of years – reaching 76% in 2006 and is closing the gap on the national average, which is 2.4 percentage points higher than the North East rate. The highest level of economic activity is in Tynedale (83.1%) and the lowest rate is in Teesdale (68.5%)⁴. The long-term national trend shows economic activity rates have remained steady at around 79% over the last 5 years, although they have decreased marginally overall.

3.2.3 Some 7% of the working age population are unemployed in the North East⁵. This is higher than the national average by 1.5 percentage points in 2006. Unemployment rates have been decreasing both nationally and regionally since 2000; however both have seen an increase in unemployment rates since 2005.

3.2.4 The region has 1.06 million employees. In 2006 the employment rate in the region reached 70.7% - 3.4 percentage points lower than the national average⁶. The 2006 employment rate has remained relatively static since 2005 but the long-term trend shows an increase and the North East is closing the gap with the rest of England and Wales. Employment growth occurred between 2000-2005 at a rate of 10% compared to the England average of 4%⁷. Nationally the employment rate has seen little change – remaining just under 75% over the last 5 years.

3.2.5 The highest proportions of those in employment in the North East work in Public administration, education & health related industries at 32.5%⁸. This is mirrored in the rest of England, but at a slightly lower proportion of 26.2% The North East has higher proportions of employed people working in Manufacturing, construction, and energy &

³ ONS mid Year Population Estimates, 2005.

⁴ ONS annual population survey, 2005

⁵ ONS annual population survey, 2005

⁶ ONS annual business inquiry employee analysis, 2005

⁷ ONS annual business inquiry employee analysis, 2005

⁸ ONS annual business inquiry employee analysis, 2005

water, than the average national proportions, and a lower proportion working in banking, finance and insurance.

- 3.2.6 The number of people employed in the manufacturing sector in 2005 has decreased by 29% since 2000 (although this is in line with the national change at 29%). Despite this, manufacturing remains a critical employment sector in the North East. It is the 3rd largest sector, employing 131,253 people (12.3% of all employed) – this is above the rate in England at 11.1%. The majority of the region's workers are in full time employment, at 66.4% compared to 33.6% in part time employment.
- 3.2.7 Some 70,065 businesses operate in the region. The North East has experienced growth in terms of the number of businesses operating in the Region from 2000 to 2005, with a 6% increase – only slightly behind the average for England at 7%. 7.4% (5,170) of businesses within the North East are in the manufacturing sector⁹. This compares to 7.3% nationally. The number of businesses in the manufacturing sector in the North East is relatively stable, with only a -0.8% change from 2000 to 2005 (compared with -1.3% in England).
- 3.2.8 Of the 5,170 manufacturing businesses in the North East, 94% (equivalent to 4,879 businesses) employ between 1-99 employees¹⁰. There are 4 manufacturing businesses in the North East that employ between 1000-5000 employees.

Economic Composition and Performance

- 3.2.9 The overall level of GVA generated by the North East region was £35.9 billion in 2005 – equivalent to 3.4% of the UK economy¹¹. This is the second lowest of all UK countries or regions, ahead of Northern Ireland only, largely reflecting the North East's relatively small population. However, growth in the total level of GVA was higher than the national average in 2005 – 4.4% compared to 3.9%. The North East's growth rate in 2005 was the highest of all the UK countries and regions, jointly with London and the East Midlands.
- 3.2.10 In 2004, Manufacturing was the largest contributor to North East GVA accounting for 19% (£6.5 billion). The contribution of Manufacturing to the North East economy has declined from 1994 – 2004 by 3%. 2003 saw the lowest contribution of manufacturing to the North East economy since 1995, although there was a 3% growth in 2004 from 2003 levels (£6.52m compared to £6.32 in 2003). Between 1994 and 2004 manufacturing share of GVA fell by 9% whilst real estate, renting & business activities rose by 4%.
- 3.2.11 The level of GVA per head of population was £14,000 in 2005. This is the third lowest nationally after the East Midlands and Wales. However, there was a 3.5% growth on 2004 levels – of the English regions only the East Midlands had a higher growth level at 4%. This could suggest on this measure that the North East is starting to close the gap on other regions.

⁹ ONS annual business inquiry workplace analysis, 2005

¹⁰ ONS annual business inquiry workplace analysis, 2005

¹¹ ONS Gross Value Added figures, 2005 and local and sectoral figures, 2004

Income

- 3.2.12 Gross Weekly pay data for the North East in 2006 was £394 compared to the national average of £454¹². Annual wage rates for the North East are 16% below the average for England (£20,587 compared to £23,982) and are the lowest out of all the English regions.

Social Exclusion

- 3.2.13 12 out of the North East's 23 Local Authorities are ranked within the most deprived 20% in England¹³. Easington, Middlesbrough, Hartlepool, and Newcastle-upon-Tyne are ranked in the top 20 most deprived local authorities for multiple deprivation (out of 354 in England). The proportion of the working age resident population claiming benefits is 3.1% (equivalent to 48,366 residents) compared to 2.3% in England¹⁴.

Education

- 3.2.14 In 2006, 57.4% of pupils taking GCSEs in the North East gained 5 or more A*-C grades, compared to 59.2% in England.
- 3.2.15 The North East has a higher proportion of its economically active working age population with NVQ3, NVQ2, NVQ1, and Trade qualifications than England¹⁵. However, a lower percentage of the North East's economically active working age population have NVQ4 skills – 25.3% compared to 29.9% in England. This potentially reinforces the historic reliance on manufacturing and trade industries in the region. Amongst the economically active working age population, 9.6% have no qualifications – this is fractionally below the national average of 9.8%¹⁶.

¹² Annual survey of hours and earnings - resident analysis, 2006

¹³ DCLG Indices of Deprivation, 2004

¹⁴ ONS Claimant Count – resident working age population, July 2007

¹⁵ ONS annual population survey, 2005

¹⁶ ONS annual population survey, 2005

4 Market Context

4.1 Introduction

4.1.1 In this section of the appraisal we describe the market context for the proposed Manufacturing and Services project. This includes an exploration of the global and national manufacturing market.

4.2 The Global Market

4.2.1 Global manufacturing is characterised by increasing global supply chains and fast-growing markets¹⁷. Increased competition in the world market place has encouraged an economic shift with rapid growth and development across China, India and Eastern Europe. A number of factors have aided the development of new manufacturing markets, including the reduction of tariff barriers and transport costs, easier communications and increased capital flows which have all allowed low wage countries to compete more effectively, shifting production away from advanced industrialized nations such as the UK, the USA and mainland Europe.

4.2.2 China is at the forefront of the global manufacturing market as it has increased its share of world exports and Foreign Direct Investment (FDI), posing a continued threat to UK manufacturers:

- In the past two decades, Chinese growth has averaged almost 10% per year;
- China's share of world exports has risen from just over 1% in 1983 to 6.7% in 2004;
- In 2005, China was the third largest recipient of foreign direct investment (FDI) – attracting some £72bn in inward investment; and
- The UK imports from China have grown from £5bn in 2000 to almost £13bn in 2005.

4.2.3 Other key factors driving global manufacturing performance include enhanced automation and work processes through new technologies, increasingly effective use of ICT and investment in human capital. Effectively employed, these drivers have significantly reduced the contribution of labour as an input to production. This has particularly been the case in Europe, the USA and Japan where increases in productivity have driven down the number employed in manufacturing industries – conversely, it has also affected the growth of manufacturing capacity in the wider global market.¹⁸

4.2.4 Labour costs remain an important factor in determining the location of manufacturing production, especially low value added activities which tend to be labour intensive. This has helped to raise the profile of emerging manufacturing markets in South Asia – such as Thailand, Vietnam Indonesia and Malaysia - which benefit from lower labour costs, relative economic and political stability and a young, skilled workforce.

¹⁷ EEF and BDO, “Global Challenges – Opportunities and threats for UK Manufacturers”, June 2007

¹⁸ OECD, “The Changing Nature of Manufacturing in OECD Economies,” February 2006.

4.3 The UK Market

- 4.3.1 The manufacturing industry is an integral part of the UK economy and fundamental to national prosperity. It is responsible for a sixth of UK output, accounts for over half of all exports and undertakes 75% of all business research and development¹⁹.
- 4.3.2 Manufacturing has however recently experienced a turbulent period. Since 2001, the UK manufacturing sector has experienced difficulties related to the downturn in the global economy, although since 2004, the sector has shown signs of recovery. The forces of increased low-cost competition from China, India and Eastern Europe means that manufacturing firms will increasingly need to move up the value-added supply chain into knowledge intensive, high-skilled manufacturing to compete more on quality and less on price.
- 4.3.3 Manufacturing output in the UK fell from the end of 2000 to the beginning of 2003 by around 5%²⁰. The strongest output in manufacturing was recorded in 2004, and this growth has continued into 2006, increasing by 1.4% on 2005 levels. Latest data on manufacturing output shows an increase again by 0.8% in the three months to July 2007 compared with the three months to April 2007. Ten out of the 13 manufacturing sub-sectors showed increases in output, two sub-sectors showed decreases and one remained unchanged.
- 4.3.4 World trade has expanded rapidly in recent years, and UK firms appear to have enjoyed the benefits of increased exports. Manufacturing accounted for 55% of total UK exports in 2005 (£190bn worth of goods) – up 10% on the previous year.
- 4.3.5 The total amount of people employed in the manufacturing sector has declined since 2000 by -28%²¹ (equivalent to 837,750 employees). This reduction in employment has been driven by a shift away from more labour-intensive production and a renewed effort to increase productivity levels. Research from the Institute for Employment Research has shown that between 1984 and 2004 overall employment in manufacturing declined by 35% but that this was concentrated in manual, unskilled and clerical occupations. 38% of employees in manufacturing are in managerial or professional jobs with a further 58% in skilled trades²².
- 4.3.6 Over the last 15 years, the manufacturing sector has consistently achieved productivity gains in excess of the whole economy, therefore acting as a driver for aggregate productivity growth – productivity growth in manufacturing has outpaced the economy as a whole for almost the past five years²³. Figures for 2000-2005 show that the UK has experienced higher productivity growth than Germany, France, Italy and Japan²⁴. Only the United States experiences higher productivity levels. R&D spending on manufacturing is expanding, and in 2005 represented £10.3bn of the UK economy.

¹⁹ Review of the Government's Manufacturing Strategy, DTI

²⁰ ONS Index of Production, 2007

²¹ ONS annual business inquiry employee analysis, 2005

²² Institute for Employment Research, 2004

²³ ONS, % annual change in output per hour worked, 2006

²⁴ US Bureau of Statistics

- 4.3.7 The UK has a strong base from which to compete in terms of innovation and value-added manufacturing, with a strong University base, world-class science resources, skilled and flexible workforce, and strong transport links. Rapid advances are expected in areas such as information and communications technologies, materials biotechnology, fuels and nanotechnology in the UK, which will help the manufacturing sector create real competitive advantage and drive up productivity.
- 4.3.8 The key growth markets for manufacturers include²⁵:
- The aerospace market – forecast to grow by at least 25% in relative terms over the next 20 years, to £250 billion a year;
 - The pharmaceuticals sector – worth around £250 billion a year with a growth rate of 4-5% per year; and
 - The medical equipment sector – estimated to be worth around £107 billion and set to expand at an annual rate of around 8 to 10% in the next few years.

4.4 The North East Market

- 4.4.1 The North East like all regions has been facing the challenges of globalisation. In recent years, the North East has seen some of the negative consequences, not just in manufacturing plants such as Goodyear, Atmel, Circatex, Val Bird and Stag Furniture.
- 4.4.2 Manufacturing accounts for 20% of all output in the North East.²⁶ The manufacturing sector in the region accounts for a greater proportion of employment and output than in the UK as a whole. Cambridge Econometrics has forecast that manufacturing in the North East will contribute to 25.5% of GVA in 2010, compared to 18.7% in the UK.
- 4.4.3 In the North East there are around 6,000 manufacturing sites and the manufacturers are from a range of diverse industries, including strengths in chemicals and engineering. The region has a successful tradition as an exporting region. International trade represents around one third of GDP, more than any other region in the UK and there are 2,000 companies actively exporting.²⁷ Exports amounted to £8bn in 2005, 4% of all UK exports. Machinery and transport exports account for 41% and chemical goods account for 37%. Currently, 64% of all exports went to Europe, 13% North America and 10% to Asia.
- 4.4.4 Low value manufacturing still represents a high proportion of manufacturing in the North East, and the region cannot compete on price alone. Low skills are major cause of low productivity in the region. In 2005, the region had the lowest proportion of people with degrees or equivalent in the UK at just 12%, compared to 18% nationally, and also a greater number of people with no qualifications. The North East in 2001 also received less training than other regions.
- 4.4.5 Investment in R&D has traditionally been low; this has however significantly changed in recent years with the five Centres of Excellence and the Regional Centre for Manufacturing Excellence.

²⁵ Review of the Government's Manufacturing Strategy, DTI

²⁶ Regional Report North East, Alliance Trust Research Centre, 2006

²⁷ Manufacturing in the Regions: North East, ONE

4.4.6 The North East, through its revised RES, is specifically targeting low productivity. The region faces challenges – manufacturing employment has fallen faster in the region than other regions; there is need to stimulate investment in innovation to lift the companies further up the industrial value chain; and the low skills and falling productivity levels.

4.4.7 Much of the industry in the region in terms of output is owned and controlled by interests based outside the North East, and therefore success in manufacturing can only come from building competitiveness, raising productivity, incentivising innovation, enhancing skills, spreading best practice and ensuring a strong and stable economy. This is the approach set out in our manufacturing strategy agreed with manufacturers and their trade unions.

4.5 Summary

4.5.1 Whilst there has been a massive amount of jobs that have been lost in British manufacturing in the last thirty years, over the same period, manufacturing output has gone up, due to huge advances in productivity. In some sectors, like pharmaceuticals, output has trebled; whilst, in aerospace, it has doubled.

4.5.2 The manufacturing sector is still facing difficult times, particularly with spiralling costs of energy and commodities, however the UK Government is committed (as detailed in the National Manufacturing Strategy) to strong manufacturing in Britain.

4.5.3 Modern British manufacturing is now leaner; more competitive, less vulnerable; and far better placed to succeed. It accounts for one sixth of GDP; two thirds of exports and three million jobs. This type of core manufacturing is where the North East needs to be - high value, high skill, and high wage.

5 Rationale

5.1 Introduction

5.1.1 In Section 4 the evidence base for ONE's involvement in this project is provided. Detailed in this section is the rationale as to why these four projects should be integrated and the potential benefits this will bring to the sector in the North East.

5.2 Underlying rationale for the four programmes

5.2.1 The main justification for the four programmes have already been established. It is not the focus of this appraisal then to repeat or restate all of the detail in respect of these – rather the primary purpose is to argue a rationale for their integration. Nonetheless, it is relevant to highlight the main underlying reasons that justify public intervention into the four individual programmes. These include:

- A systematic under-investment in skills: Human capital theory assumes that firms are perfect competitors for labour, whereas in practice firms often perceive it to be the case that they will not fully maximise the benefits of investments in the skills and capability of their workforce. Therefore, as papers by Margaret Stevens (Nuffield College, Oxford), Daron Acemoglu (LSE) and Ken Burdett and Eric Smith (University of Essex) and countless others show, employers are not always fully compensated for the costs of general training and will – at times therefore – acquire too little.
- Information failure with respect to benefits/opportunities of investment in process change and innovation: There is asymmetry in the information available to innovators and experts in manufacturing process improvement and that which is available to those that could benefit from those innovations and processes. At a very simple level developers innovate without full understanding of the range of potential commercial applications and commercial organisations are not fully aware of the potential applications of new innovations. The market fails therefore to fully exploit innovations.

5.2.2 The programme is wholly compatible with current regional and national policy. In July 2004, the Government published a review of the 2002 Manufacturing Strategy and its achievements. It set out priorities for the future in an action plan, within which 'high skilled, high performance workplaces' and 'promoting best practice' are key priorities.

5.2.3 The Cox review of Creativity in Business concludes that innovation is the only way for the UK manufacturing sector to survive and compete within the global market. Manufacturers need to embrace creativity, innovation and design to develop high-end, niche products for the future.

5.2.4 The project makes a clear contribution to the Regional Economic Strategy, and is also in line with the Government's Business Support Simplification agenda.

5.3 Rationale for integrating the four programmes

5.3.1 In April 2007, One NorthEast made a decision that it wished to move towards providing an integrated regional manufacturing and productivity service post 2008. In order to begin to put this in place, it was agreed that the new service would incorporate the national MAS, the current NEPA BP and NEPA Energy and NEPA Design. Other related services may also be delivered via this route in the future.

5.3.2 The main objectives in integrating these services is to achieve greater economies of scale, more outputs will be able to be delivered for the same levels of investment. It will

also improve sharing and learning between the elements of the project and improve the customer experience. BERR has indicated that they would wholeheartedly endorse this as an approach.

- 5.3.3 It has been agreed that the new integrated manufacturing and productivity service post 2008 will be delivered externally from One NorthEast and procured by undertaking an OJEU procurement process.
- 5.3.4 Both the MAS and NEPA brands which are recognised and valued by North East manufacturing companies, will continue to feature prominently and the new service will be known as MAS/NEPA. One NorthEast is keen to ensure that the integrity of the MAS/NEPA brands and the quality of the services are protected in the new integrated offering.
- 5.3.5 One NorthEast believe through an enhanced manufacturing and productivity support service the following outcomes will be achievable:
- **Greater demonstrable economic impact** - One NorthEast recognises the importance of the NEPA and MAS brands in ensuring a service is available to all who need help manufacturing and productivity. However the Agency also recognises the importance of prioritising scarce resources and are, therefore, looking to put in place a high-quality service offering, which allows for resources to be targeted at areas of maximum impact.
 - **Greater efficiency** - The new operation will be more efficient in terms of unit costs; back office costs; staffing ratios and customer resource.
 - **Greater consistency** - In seeking greater consistency the aim is to ensure that any differential levels and types of service are based on market failure, impact rationale or the need for evidenced targeted support. The new service will result in a consistent framework of support across the region, including targeting at sector.
 - **Contribute towards the Business Support Simplification Agenda** - The proliferation of business support initiatives in the North East and consequent confusion amongst business clients is well documented. Integrating the combined activities of MAS/NEPA builds upon the Government's Business Support Simplification Programme.

6 Options Identification

6.1 Introduction

6.1.1 In this section we assess the various options that the public sector might consider in relation to the Manufacturing and Productivity Project. We begin with a long list of options and conclude with a short list.

6.2 Long List

6.2.1 The following options present potential vehicles that were considered when assessing the most appropriate conduit through which the objectives of the project could be met.

1. Do Nothing

6.2.2 This would involve the withdrawal of all funding for the 4 projects and the wind down of all related project activity. It would require no investment on the part of ONE North East or any other public sector organisation. All benefits, impacts and outcomes would cease.

2. Deliver 4 projects separately

6.2.3 Under this option, the current arrangement of delivering the 4 separate projects would be continued. Given that individual funding approval is already in place for the 4 projects and the necessary Board approvals made, the projects could continue in their current form from April 2008. This can be considered a “counterfactual” option as it most accurately reflects what would happen should the 4 projects not become integrated.

3. Full integration of 4 projects

6.2.4 Under this option, the 4 separate projects would be integrated to form the Manufacturing and Productivity Post 2008 project. This would involve ONE going to OJEU to tender for an external delivery partner, who would run the project. ONE would monitor and evaluate the preferred delivery partner.

4. Full integration of 4 projects under an SPV

6.2.5 Under this option, the 4 separate projects would be integrated and a Special Purchase Vehicle would be set up to deliver the project. The Special Purchase Vehicle would be a public private partnership between ONE and a preferred private sector partner.

5. Integrate NEPA BP and ERE as a single project and MAS and Design in Manufacturing as a further single project

6.2.6 Under this option, NEPA BP and ERE will be integrated. These are both intensive services and require similar support therefore merging them together is an option. Under this option, MAS and Design in Manufacturing would be integrated into another organisation for example Business Link. MAS would continue in its current form and Business Link would provide a helpdesk function for this programme. Design in Manufacturing would be incorporated within this.

6. NEPA BP, MAS and ERE to be integrated into one project and Design in Manufacturing to be included as a project at a later date

6.2.7 Under this option, NEPA BP, MAS and ERE would continue, albeit in a fully integrated sense. Design for Manufacturing would come on stream at a later date. This option reflects the fact that individual funding approval is already in place for the 3 projects, the

projects could continue in an integrated form from April 2008, and Design in Manufacturing would be included as a separate project at an appropriate stage.

7. Continue with a sole focus on MAS

6.2.8 Currently the **MAS** offering to small and medium sized businesses is based on a rapid response service for urgent and short-term problems. It is operated regionally, albeit within a national framework. The key activities include: Enquiry Handling, Diagnostic, Extended Diagnostic and Full Consultancy. The project will remain focussed on the traditional MAS audience, by delivering existing services, using existing tools and methodologies. Under this option MAS would continue to be delivered, whereas the other projects would cease. Here the region would continue to honour its national delivery obligations of the MAS service.

6.3 Forming the Short List

6.3.1 The matrix below provides a summary of the appraisal process (and outcome) that was used to form a short-list of options. Options were scored against a set of weighted criteria. These criteria were developed following:

- Extensive consultation within ONE to establish the main outcomes that staff across the Agency wanted the future programme to achieve;
- Evaluative evidence from current / previous iterations of the four programmes; and
- Consultation with stakeholders and partners to the four programmes;

6.3.2 The criteria were then each assigned a weight to reflect the relative order of importance attached to it. The weighting reflects an overall mark out of 80. Finally, against each weighted criteria a score of 1-3 was allocated. Thus the maximum score available to any given option was 240. The approach adopted is one that is similar in principle to the "Minimum Quality Threshold" criteria used in assessing options for European funded projects.

Figure 6.1: Long list option appraisal

	Maximise economic impact (10)	Greater efficiency (10)	Greater consistency (5)	Protecting / developing integrity of brand (5)	Contribution to RES (10)	Attractiveness to bidders (5)	Knowledge transfer between projects (5)	Knowledge transfer between customers (5)	Provision of "single gateway" to manufacturing services (5)	Contribution to Simplification Agenda (10)	Improve service quality via concurrent provision (5)	Minimise risk to public sector (5)	Overall Score
1. Do nothing	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	80
2. Deliver 4 projects separately	✓✓ ✓	✓	✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓	✓	✓	✓	✓	✓✓ ✓	155
3. Integrate 4 projects	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	240
4. Integrate 4 projects under SPV	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓✓ ✓	✓	230

	Maximize economic impact (10)	Greater efficiency (10)	Greater consistency (5)	Protecting / developing integrity of brand (5)	Contribution to RES (10)	Attractiveness to bidders (5)	Knowledge transfer between projects (5)	Knowledge transfer between customers (5)	Provision of "single gateway" to manufacturing services (5)	Contribution to Simplification Agenda (10)	Improve service quality via concurrent provision (5)	Minimize risk to public sector (5)	Overall Score
5. Integrate NEPA BP and ERE and MAS and Design in Manufacturing	✓	✓	✓	✓✓ ✓	✓✓	✓	✓✓	✓✓	✓	✓	✓	✓	110
6. Integrate NEPA BP, ERE and MAS and deliver Design in Manufacturing to be delivered at a later stage	✓	✓	✓✓	✓✓	✓	✓✓	✓✓	✓✓	✓✓	✓✓	✓✓	✓✓	130
7. Deliver MAS only	✓	✓	✓	✓	✓	✓✓	✓	✓	✓	✓	✓	✓	85

6.3.3 It was agreed that only those options that scored more than 150 of the overall maximum score would be short-listed for a more detailed appraisal. Using that process the following options were rejected:

- Option 1 – Do Nothing
- Option 5 Integration of NEPA BP and ERE and MAS and Design in Manufacturing as two separate projects;
- Option 6 – Integrate NEPA BP, ERE and MAS and Deliver Design in Manufacturing at a later stage; and
- Option 7 – Deliver MAS only.

6.3.4 Those that were short-listed were so specifically on the basis that they demonstrated the maximum contribution or potential contribution to the following factors:

- Greater economic impact
- Greater efficiency
- Greater Consistency
- Protecting/developing integrity of brand
- Contribution to RES
- Attractiveness to bidders
- Knowledge transfer between projects and customers
- Providing a single gateway for manufacturing services
- Contribution to the simplification agenda
- Improving quality of service
- Minimising risk to the public sector

6.3.5 The rejection of as “Do Nothing” option in this instance is relevant, particularly as the focus of the appraisal is on integrating four individual projects that are a) already operating and b) have already received funding approval for the ONE North East Board. Because of this a more realistic “counterfactual” option is then continuing to operate the projects individually as this is, after all, what will happen if the four projects do not become integrated.

6.4 Short listed Option One – Do Minimum (baseline case)

6.4.1 The current arrangement of delivering 4 separate projects would be maintained and approval for projects would be in place for a start date of 01/04/08.

6.4.2 All projects would continue to be delivered through ONE, and have the same objectives and roles. A brief summary of each is described below:

- **NEPA Best Practice** was originally set up in 2001 as a direct response to the heavy loss of manufacturing companies in the region. Emerging out of a consultation group comprised of Universities, Colleges and Nissan, its objective is to ensure that the North East is not only the most productive manufacturing region in the UK but an exemplar region from which other regions can learn and benefit. The project helps manufacturing companies of all sizes (SMEs & non-SMEs) to increase their productivity in a focused way by significantly improving the organisation's knowledge & application skills of *lean manufacturing principles* at all levels (from senior management to the workforce). NEPA Best Practice is currently delivered by Agency staff and has three elements, engineering secondments, 'Narrow and Deep' programme, and bespoke productivity improvement. Since 2003, the NEPA Best Practice programme has created an average of 38 jobs, safeguarded 1028 jobs, assisted 75 businesses and generated 1,259 learning opportunities annually and helped firms make savings worth £19 million.
- Currently the **MAS** offering to small and medium sized businesses is based on a rapid response service for urgent and short-term problems. The key activities include: Enquiry Handling, Diagnostic, Extended Diagnostic and Full Consultancy. The project will remain focussed on the traditional MAS audience, by delivering existing services, using existing tools and methodologies. Under this option MAS would be delivered independently from all other aspects of the programme.
- The **ERE** was established in 2006-7 to help businesses tackle rising energy costs. It is currently delivered by NE Life. A team of specialist engineers has been seconded under the guidance of industry experts. The team works closely with firms to develop energy action plans, analyse current usage and highlight innovative ways of cutting bills. Thirty six organisations are currently working with the ERE programme with a further 22 about to join. Again, under this option the project would be delivered independently.
- **Design in Manufacturing**. This project is yet to commence. When the project begins it will support the regions manufacturing sector to support the development of their product innovation capacity. The project has been developed following significant consultation and desk research with a number of the regions key manufacturers, business support professionals, educationalists and research. Again, under this option the project would be delivered independently.

6.5 Short listed Option Two – Integration of the 4 Projects

6.5.1 This option would involve the integration of the 4 projects described into a single and overarching "programme". For clarity, the programme would include NEPA Best Practice, MAS, NEPA Design in Manufacturing and ERE. The integration of the four projects is driven by the following principles and objectives:

- Scale and efficiency: both in terms of focusing direct delivery resource and sharing operational and back office overhead;
- Leveraging the strength of the brands: based on the established brands of NEPA and MAS;
- Providing greater clarity to customers: through a singularly accessible and branded programme;
- Improved cross project referral: improved lines of communication and client relationship management;
- The achievement of national policy: principally that relating to the business support simplification process;

- Securing a private sector operator to manage the process of delivery: the integrated programme provides an opportunity of considerable scale for established private sector operators.

6.5.2 It is the intention that this option would be delivered via a contract with a third party operator who will be procured through due process.

6.6 Short listed Option Three – Integration of the 4 Projects using an SPV

6.6.1 Option three is precisely as per option 2 albeit with the additional aspect being the programme is delivered via a Special Purpose Vehicle established specifically to deliver the programme. The SPV would have transferred to it all assets and liabilities associated with the delivery of the activities of the programme.

7 Benefits

7.1 Introduction

7.1.1 This section sets out an overview and analysis of the outputs (gross and net) that occur across the short-listed options.

7.2 Key Benefits

Strategic Added Value

7.2.1 The project will provide a range of strategic added value, including increased national and international reputation via the enhanced and integrated MAS-NEPA services and the very nature of the project will lead to much enhanced co-ordination and partnership.

Benefits

7.2.2 The main quantifiable benefits that will be delivered by the programme are:

- NTF1 Jobs Created and / or safeguarded;
- NTF 4 Companies receiving assistance; and
- NTF 6 Skills.

7.2.3 The forecast outputs are based on formula approach that uses actual recorded output and spend data for NEPA and MAS between 2002 and 2007. The formula works on the basis of a ratio of output per £1 million of programme spend. The benchmarks used are:

- NTF 1 Jobs created / safeguarded 197 per £1 million of programme spend;
- NTF 4 Companies receiving assistance 103 per £1 million of programme spend; and
- NTF 6 Skills 316 per £1 million of programme spend.

7.3 NTF 1 jobs created and / or assisted

7.3.1 Table 7.1 profiles the gross created and / or safeguarded by the programme, across each of the three short listed options.

Table 7.1 NTF 1 jobs created / safeguarded (options 1-3)

Output	Option 1	Option 2	Option 3
NTF 1: Jobs Created and / or Safeguarded	7,778	8,245	7,707

7.4 NTF 4 companies receiving assistance

7.4.1 Table 7.2 profiles the numbers of companies receiving assistance across each of the three short listed options.

Table 7.2 NTF 4 companies receiving assistance (options 1-3)

Output	Option 1	Option 2	Option 3
NTF 4 Companies receiving assistance	4,067	4,311	4,030

7.5 NTF 6 skills

7.5.1 Table 7.2 profiles the numbers of skills produced across each of the short listed options.

Table 7.3 NTF 6 skills (options 1-3)

Output	Option 1	Option 2	Option 3
NTF 4 skills	12,477	13,226	12,363

7.6 Gross Value Added (GVA)

7.6.1 Using an average GVA per employee figure of £12,736 for the North East region we have prepared a *conservative* estimate of Gross Value Added for the overall programme. This is presented in table 7.4 below. We emphasise the conservative nature of the estimate as many of the manufacturing businesses that will become beneficiaries of the programme in the future will have a higher than regional average GVA per employee.

Table 7.4: Gross Value Added

Option	Gross value added £000
Option 1	99,062,635
Option 2	105,011,173
Option 3	98,159,673

7.7 Private sector contributions

7.7.1 The design and development of the programme post 2008 has begun from a standpoint that recognises that the programme must include private sector contribution over the next 5 years. These private sector contributions are benefits to the programme and include both in-kind contributions and actual cash contributions.

7.7.2 Calculations for private sector in-kind contributions can be defined as costs of staff time or down-time that has been a direct result of being involved in the programme and also where companies have purchased a new product or service as a direct result of a NEPA intervention.

7.7.3 Cash are instances where a beneficiary business makes a direct contribution to a service they will benefit from which brings down the total cost of the service. For example, if a service costs £10K and a private sector contribution of £2K is made, the public subsidy has now been brought down to £8K for this intervention. In the case of this particular programme, it is a feature of its design that private sector contributions must not be used to reduce the total public subsidy, which will remain at roughly £32m but will be used to increase the number of interventions that are made in the market place. The main element of the project that will be able to generate private sector cash contributions is the Bespoke Productivity Improvements element.

7.7.4 Table 7.5 outlines the estimate of private sector in-kind contributions made over the next five years. This assessment is based on a sample of actual company contributions with an increase of £100,000.

Table 7.5 Private sector in-kind contributions

Leverage	2008/09	2009/10	2010/11	2011/12	2012/13	Total
Private sector Contribution in Kind (including down time) - NEPA Best Practice	695,000	795,000	895,000	995,000	1,095,000	4,475,000
Private sector Contribution in Kind (including down time) - NEPA Energy	200,000	300,000	400,000	500,000	600,000	2,000,000
Total In-Kind Contributions	895,000	1,095,000	1,295,000	1,495,000	1,695,000	6,475,000

7.7.5 Table 7.6 outlines the estimated cash contributions from companies over the next 5 years of the programme. These figures are based on assumed levels of private sector contributions, which have been calculated as a percentage of the “Business Support and Training” aspects of the programme (see table 9.1 for a breakdown of the programme costs).

Table 7.6 Private sector cash contributions

	2008/9	2009/10	2010/11	2011/12	2012/13	Total
<i>Private sector cash contributions</i>	259,435	383,901	704,432	994,372	974,530	3,316,670

7.7.6 Note that as the main differences between the options are attributable to their internal structure, the levels of private sector contributions are the same across all three options.

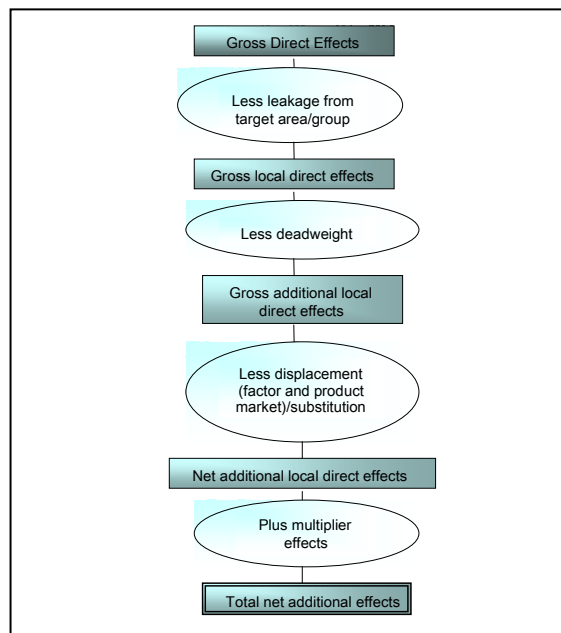
7.8 Net Additional Jobs

7.8.1 The approach taken by Tribal for assessing the economic additional impact of the development follows the guidance laid out by Guidance used by HM Treasury in the most recent ‘Green Book’. This essentially sets out the established principles for undertaking appraisal and evaluation in central government.

7.8.2 The additionality guidance used in the Green Book stipulates that when appraising projects the leakage, deadweight weight and displacement/ substitution must be taken away from the gross impacts of the project. A multiplier effect must then be added to give the net additional impact. This is seen as a more meaningful estimate of project benefits than the gross figure.

7.8.3 The specific inputs and outputs in the study that are required by central government are summarised in the diagram below.

Figure 7.1: Net additionality analysis



Leakage

7.8.4 Leakage is the benefits that would accrue to residents from outside the study area. In this case the North East. Leakage in terms of this project would be the number of jobs created being taken by those outside the region.

7.8.5 Projects that are focused at a narrowly defined group of beneficiaries located within a particular area (and assuming the eligibility criteria for determining who can receive support are strictly applied), are likely to have a very small amount of leakage associated with their outputs and outcomes. However, that provide general business advice to an unspecified audience are likely to have a greater degree of leakage.

7.8.6 In our analysis we have not included those that move into the region to take jobs as leakage as they would become part of the region. We have only included those that would be employed by manufacturing companies in the region but reside outside of the region. We have assumed this figure would be low at around 15%. We have assumed this measure as we understand that the overwhelming majority of beneficiaries to the current programmes and employees that are based in the North East. The types of employment benefits that the programme will create in the future are likely to be broad – from managerial through to operative positions. However, based on feedback received from companies who have participated in the programmes and on the basis of

discussions with the programme operators / managers we can confirm that historically, most of the employment impacts benefit people who live in the region.

Deadweight

- 7.8.7 Deadweight is the amount of the benefit that would have occurred regardless of the project and should not be included in the net additional figure. In the case of the creation of this particular programme the deadweight is the amount of jobs created in the region without the existence of any support.
- 7.8.8 This is somewhat difficult to estimate – although we can use recent trends in manufacturing employment growth / decline in the North East as a proxy measure – in order to gauge the general employment dynamism in the sector in the region. Between 2000 and 2005 manufacturing employment in the region actually fell – from a figure of 169,357 to 131,253. Forecasts are that manufacturing employment will continue to fall – driven partly by technological change and the continued competition from the “tiger” economies of the East.
- 7.8.9 It would be reasonable to assert then that manufacturing employment in the region is unlikely to grow significantly. Although this does not mean that any of the jobs created and / or safeguarded within beneficiary companies would not be created and / or safeguarded in the absence of support. Thus deadweight is an important factor in the appraisal and needs to be included within the additionality calculation.
- 7.8.10 The English Partnership’s guide to Additionality (2004) provides a range of deadweight estimates by project type. It also outlines a possible range of deadweight measures that reflect programme and project manager surveys on the one hand and beneficiary surveys on the other. Using these ranges, the deadweight measures for business support projects (of which this is obviously one) contained within the report are 15% and 36% respectively and an average of 26%. As no specific primary research has been carried out in relation to deadweight factors within this particular programme, the appraisers have elected to use 26% as the deadweight measure.

Displacement

- 7.8.11 Some of the gross benefits may include jobs that have replaced or displaced other jobs. These also need to be deducted from the gross jobs to calculate the net additional jobs. In the case of this programme it is possible that the benefits that occur within one company could have displaced impacts elsewhere – although owing to the careful selection of companies by the programme team, companies it is unlikely that one of two or more competing companies will be favoured. As a cautionary measure we have included a displacement of 25% which aligns with the Amion guidance of low displacement.

Multiplier

- 7.8.12 The activity that occurs as a result of the investments made via the programme are likely to demand intermediate goods and services from local firms. These firms are likely to increase their own demand for locally supplied intermediate goods and services. This increase in regional economic activity as a result of the supply change linkages needs to be added. We do this by adding a supply chain multiplier.
- 7.8.13 A proportion of the wages earned by employees in the centre will be spent in the region and benefit local firms. A proportion of the additional income received by these firms will

be spent in wages and spent in the regional economy. This increase in income needs to be added to the gross benefits and is done so by the application of the income multiplier.

7.8.14 The composite multiplier of the supply chain multiplier and income multiplier has been estimated at 1.35.

Net additionality results

7.8.15 Using the assumptions for Leakage, Deadweight, Displacement and Multiplier outlined above we derive results for the net additional jobs for each in option in the table below.

Table 7.7: Net Additional Jobs

OPTION	GROSS JOBS	LESS LEAKAGE	LESS DEADWEIGHT	LESS DISPLACEMENT	PLUS MULTIPLIER = TOTAL NET ADDITIONAL JOBS
Option 1	7,778	6,611	4,982	3,669	4,954
Option 2	8,245	7,008	5,186	3,890	5,251
Option 3	7,707	6,551	4,848	3,636	4,908

7.9 Summary

7.9.1 This section has provided an overview of the core benefits that post 2008 programme has the capacity to generate. These are considerable, even when based on the conservative sensitivities applied throughout this analysis. The appraisal has applied relatively conservative assumptions and forecasts that some £105 million of Gross Value Added will be generated regionally, some 8,245 gross jobs will be created or safeguarded and 5,251 net jobs will be created or safeguarded in the North East. Some 4,067 companies will be supported through the scheme.

8 Financial and Economic Appraisal

8.1 Introduction

8.1.1 In this section of the report we present a financial and economic appraisal for the three short-listed options. The appraisal has been conducted using a methodology which is consistent with HM Treasury's Green Book. The analysis considers all grant related expenditure being made, the anticipated outcomes (financial and non financial) as well as discounted monetised costs and benefits to generate a net present value (NPV) for each option under consideration.

8.2 Optimism Bias and Social Time Preference Discount

8.2.1 The following sub-section details the public sector costs associated with each option under consideration. Specifically, we present the gross costs, the costs following the application of appropriate *optimism bias* sensitivities, *discounted* at the **3.5% social time preference discount rate**.

8.2.2 There are only revenue costs incurred by the programme as for these we have assumed an optimism sensitivity on these of –20%, with a commensurate impact upon private sector contributions of –20%.

Table 8.1: Gross Costs, Optimism and Discounted (all options)

£	Gross Costs	Optimism	Discounted
Option 1	35,506,775	42,608,130	38,302,880
Option 2	35,506,775	42,608,130	38,302,880
Option 3	45,608,130	45,608,130	41,011,911

8.2.3 The application of an optimism bias sensitivity to the project obviously has the effect of increasing costs and using the now universally applied discount rate of 3.5% to arrive at current prices, the discounted costs for each of the three options are £38,303,880 for options 1 and 2 and £40,011,011 for option 3. As discussed earlier, the costs for option 1 and 2 are precisely the same. The main variance between them relates to the level of output generated – as the integration of the 4 underlying projects into a single programme allows for back office costs to be reduced and vired to front line delivery costs – thereby enabling more output.

8.3 Benefits Profile

Gross benefits

8.3.1 Table 8.2 illustrates the benefits profile across the options, discounted at the 3.5% discount rate.

Table 8.2: Gross Benefits

	<i>Option 1</i>	<i>Option 2</i>	<i>Option 3</i>
Gross jobs created	7,778	8,245	7,707
Gross Monetised Benefit (GVA) (£)	99,062,635	105,011,173	98,159,673
Present Value of Gross Monetised Benefit (£)	89,053,057	94,400,537	88,241,332

Net Benefits

8.3.2 Table 8.3 profiles the net benefits of the project, across all options, again discounting at 3.5%.

Table 8.3: Net Benefits

	<i>Option 1</i>	<i>Option 2</i>	<i>Option 3</i>
Net jobs created	4,954	5,251	4,908
Net Monetised Benefit (GVA) (£000)	63,089,278	66,877,678	62,514,215
Present Value of Net Monetised Benefit (£000)	56,714,552	60,120,162	56,197,595

Net Present Value

8.3.3 Table 8.4 profiles the net present value of benefits across all options and presents a benefit to cost ratio. In effect, this sets out – at current prices – the net benefit that the North East economy gains for the levels of cost incurred by the programme.

Table 8.4: Net Present Value of Benefits

	<i>Option 1</i>	<i>Option 2</i>	<i>Option 3</i>
Present Value of GVA	56,714,552	60,120,162	56,197,595
Present Value of Public Sector costs	38,302,880	38,302,880	40,011,911
Net Present Value	18,411,672	21,817,282	16,185,684
Cost to benefit ratio	1:1.48	1:1.57	1:1.40

8.3.4 From table 8.4 it can be seen that all options are economically worthwhile. They all produce a positive Net Present Value (NPV) which means that the economic returns – for all options – are greater than the public sector cost. The table also shows that Option 2 is the most economically beneficial / cost effective option – producing a benefit to cost ratio of 1:1.57 – that is for every £1 of public sector cost incurred by the project the North East regional economy benefits by £1.57.

8.4 Summary

8.4.1 The analysis provides a clear statement of the benefits of pursuing the projects – indeed both individually and as part of an integrated programme. In all options a positive NPV is generated. However, the most economically advantageous option is option 2 – the fully integrated option delivered via a contract with an operator. This produces a positive benefit to cost ratio and a significant economic return based on the level of public sector investment.

9 Financial analysis of the preferred option

9.1 Introduction

9.1.1 This section of the appraisal sets out a financial appraisal of Option 2 – the preferred option as identified in earlier sections. The projections have been developed through a detailed modelling exercise that illustrates:

- Revenue cost profile
- Efficiencies achieved via programme integration / consolidation
- Funding requirement

9.1.2 All costs and forecasts have been prepared with reference to historical financial data help by project staff.

9.2 Revenue costs

9.2.1 All costs for the programme are revenue costs. There is currently no capital expenditure projected during the lifetime of the programme. Table 9.1 illustrates the breakdown of revenue costs across the programme. This includes costs that are overheads and attributable to direct delivery activity.

Table 9.1 Overall revenue costs

	2008/9	2009/10	2010/11	2011/12	2012/13	Total
<i>Salaries & Staff Costs</i>	1,740,619	1,827,650	1,919,032	2,014,984	2,115,733	9,618,019
<i>Training</i>	100,000	100,000	100,000	100,000	100,000	500,000
<i>Travel & Subsistence</i>	146,460	149,389	152,377	155,425	158,533	762,184
<i>Recruitment</i>	29,669	30,263	30,868	31,485	32,115	154,400
<i>Equipment & Clothing</i>	156,269	159,394	162,582	165,834	169,150	813,228
<i>Marketing</i>	101,098	101,098	101,098	101,098	101,098	505,490
<i>Development Costs</i>	7,000	7,000	7,000	7,000	7,000	35,000
<i>Rent & Running costs</i>	327,318	327,318	327,318	327,318	327,318	1,636,590
<i>CRM System</i>	200,000	50,000	20,000	20,000	20,000	310,000
<i>Design Costs</i>	252,250	252,250	252,250	252,250	252,250	1,261,250
<i>Productivity Needs Diagnostics</i>	393,640	531,699	531,699	531,699	531,699	2,520,436
<i>Business Support & Training of Companies</i>	2,253,766	3,472,908	3,776,591	3,967,280	3,839,634	17,310,178
<i>Evaluation Costs</i>	10,000	10,000	20,000	20,000	20,000	80,000
	5,718,089	7,018,969	7,400,815	7,694,372	7,674,530	35,506,775

9.3 Overheads costs

9.3.1 Table 9.2 illustrates those revenue costs that relate to programme overheads. Overhead costs support the operation of the programme. They do not however make a direct contribution to the outputs and outcomes achieved by it.

Table 9.2 Overhead costs

	2008/9	2009/10	2010/11	2011/12	2012/13	Total
<i>Salaries & Staff Costs</i>	268,063	281,466	295,539	310,316	325,832	1,481,217
<i>Training</i>	80,000	80,000	80,000	80,000	80,000	400,000
<i>Travel & Subsistence</i>	35,428	36,136	36,859	37,596	38,348	184,366
<i>Recruitment</i>	23,735	24,210	24,694	25,188	25,692	123,520
<i>Equipment & Clothing</i>	113,591	115,863	118,180	120,544	122,954	591,132
<i>Marketing</i>	66,778	66,778	66,778	66,778	66,778	333,892
<i>Development Costs</i>	5,600	5,600	5,600	5,600	5,600	28,000
<i>Rent & Running costs</i>	261,854	261,854	261,854	261,854	261,854	1,309,272
<i>CRM System</i>	80,000	20,000	8,000	8,000	8,000	124,000
<i>Design Costs</i>	0	0	0	0	0	0
<i>Productivity Needs Diagnostics</i>	0	0	0	0	0	0
<i>Business Support & Training of Companies</i>	0	0	0	0	0	0
<i>Evaluation Costs</i>	8,000	8,000	16,000	16,000	16,000	64,000
	943,050	899,908	913,505	931,877	951,059	4,639,399

9.4 Direct delivery costs

9.4.1 The overriding majority of cost incurred by the programme is direct delivery. Direct delivery costs are those that are directly attributable to the achievement of the programmes outputs and outcomes. Table 9.3 profiles these.

Table 9.3 Direct delivery costs

	2008/9	2009/10	2010/11	2011/12	2012/13	Total
<i>Salaries & Staff Costs</i>	1,472,556	1,546,184	1,623,493	1,704,668	1,789,901	8,136,802
<i>Training</i>	20,000	20,000	20,000	20,000	20,000	100,000
<i>Travel & Subsistence</i>	111,032	113,253	115,518	117,829	120,185	577,817
<i>Recruitment</i>	5,934	6,053	6,174	6,297	6,423	30,880
<i>Equipment & Clothing</i>	42,678	43,531	44,402	45,290	46,196	222,097
<i>Marketing</i>	34,320	34,320	34,320	34,320	34,320	171,598
<i>Development Costs</i>	1,400	1,400	1,400	1,400	1,400	7,000
<i>Rent & Running costs</i>	65,464	65,464	65,464	65,464	65,464	327,318
<i>CRM System</i>	120,000	30,000	12,000	12,000	12,000	186,000
<i>Design Costs</i>	252,250	252,250	252,250	252,250	252,250	1,261,250
<i>Productivity Needs Diagnostics</i>	393,640	531,699	531,699	531,699	531,699	2,520,436
<i>Business Support & Training of Companies</i>	2,253,766	3,472,908	3,776,591	3,967,280	3,839,634	17,310,178
<i>Evaluation Costs</i>	2,000	2,000	4,000	4,000	4,000	16,000
	4,775,039	6,119,061	6,487,310	6,762,495	6,723,471	30,867,376

9.5 Redistributing costs between fixed overhead and direct delivery

9.5.1 The distribution of programme costs between overhead and direct delivery costs is important as it is via this distribution (or moreover changes to it) that the benefits of consolidating the programme are evidenced. Specifically, the preferred option outlines how – via the consolidation process – efficiency savings can be made within the programme, principally via a reduction in overhead costs. The savings that are made via this process have enabled the resources that were allocated to fixed overheads to be reallocated to direct delivery costs, thereby enabling a greater amount of outputs and outcomes to be achieved.

9.5.2 Table 9.4 presents a baseline analysis of the costs of the *current* (i.e. year 2007/08) programmes when operated independently. Specifically it sets out how costs are allocated between direct delivery and fixed overhead – prior to the programmes being integrated.

Table 9.4 Distribution of direct delivery and fixed overhead costs, un-integrated model

	Baseline Position – 2007/8 Breakdown of Spend				
	Direct Delivery	Fixed / Overhead	Total	% DD	% FO
Salaries & Staff Costs	1,388,039	330,906	1,718,945	81%	19%
Training	0	77,780	77,780	0%	100%
Travel & Subsistence	110,218	47,770	157,988	70%	30%
Recruitment	0	29,088	29,088	0%	100%
Equipment & Clothing	14,000	139,205	153,205	9%	91%
Marketing	17,625	83,473	101,098	17%	83%
Development Costs	0	7,001	7,001	0%	100%
Rent & Running costs	0	289,503	289,503	0%	100%
CRM System	0	0	0	0%	0%
Design Costs	0	0	0	0%	0%
Productivity Needs Diagnostics	0	0	0	0%	0%
Business Support & Training of Companies	2,425,825	0	2,425,825	100%	0%
	3,955,707	1,004,725	4,960,432		

9.5.3 Table 9.5 illustrates the amount of fixed overhead savings that are made within the overall programme as a result of integrating the four individual programmes. The amount of cost saving achieved has allowed for the level of resources dedicated to direct delivery to be increased, which has a commensurate increase on the levels of outputs and outcomes produced via the programme.

Table 9.5 Annual fixed overhead savings achieved via integrating the 4 programmes

	2008/9	2009/10	2010/11	2011/12	2012/13	5 Yr Total
Salaries & Staff Costs	67,016	70,367	73,885	77,579	81,458	370,304
Training	20,000	20,000	20,000	20,000	20,000	100,000
Travel & Subsistence	8,857	9,034	9,215	9,399	9,587	46,092
Recruitment	5,934	6,053	6,174	6,297	6,423	30,880

	2008/9	2009/10	2010/11	2011/12	2012/13	5 Yr Total
Equipment & Clothing	28,398	28,966	29,545	30,136	30,739	147,783
Marketing	16,695	16,695	16,695	16,695	16,695	83,473
Development Costs	1,400	1,400	1,400	1,400	1,400	7,000
Rent & Running costs	65,464	65,464	65,464	65,464	65,464	327,318
CRM System	20,000	5,000	2,000	2,000	2,000	31,000
Design Costs	0	0	0	0	0	0
Productivity Needs Diagnostics	0	0	0	0	0	0
Business Support & Training of Companies	0	0	0	0	0	0
Evaluation Costs	2,000	2,000	4,000	4,000	4,000	16,000
	235,762	224,977	228,376	232,969	237,765	1,159,850

9.5.4 Integrating the 4 programmes allows for an estimated £1.16 million of programme efficiencies to be achieved over the next 5 years if the programme. Redistributing these efficiencies to front-line delivery activity allows for an increase in direct delivery activity and therefore outputs and outcomes. Table 9.6 illustrates the overall effects of this redistribution.

Table 9.6 Increase in direct delivery costs as a result of programme integration

	Integrated Position – All Years Breakdown of Spend				
	Direct Delivery	Fixed / Overhead	Total	% DD	% FO
Salaries & Staff Costs	8,136,802	1,481,217	9,618,019	85%	15%
Training	100,000	400,000	500,000	20%	80%
Travel & Subsistence	577,817	184,366	762,184	76%	24%
Recruitment	30,880	123,520	154,400	20%	80%
Equipment & Clothing	222,097	591,132	813,228	27%	73%
Marketing	171,598	333,892	505,490	34%	66%
Development Costs	7,000	28,000	35,000	20%	80%
Rent & Running costs	327,318	1,309,272	1,636,590	20%	80%
CRM System	186,000	124,000	310,000	60%	40%
Design Costs	1,261,250	0	1,261,250	100%	0%
Productivity Needs Diagnostics	2,520,436	0	2,520,436	100%	0%
Business Support & Training of Companies	17,310,178	0	17,310,178	100%	0%
Evaluation	16,000	64,000	80,000	20%	80%
	3,955,707	1,004,725	35,506,775	87%	13%

9.6 Improved output cost effectiveness

9.6.1 The overall effect of increasing the level of resources available to direct delivery is an increase in the cost effectiveness of achieving outputs and outcomes. Under the current approach (i.e. un-integrated model):

- For every £1million of public investment some 219.1 jobs are created and / or safeguarded;
- For every £1million of public investment some 114.5 businesses are assisted; and
- For every £1million of public investment some 351.4 skills outputs are delivered.

9.6.2 These figures contrast with the integrated option, which achieves a 6% overall efficiency gain, and provides an output profile as follows:

- For every £1million of public investment some 232.1 jobs are created and / or safeguarded;
- For every £1million of public investment some 121.4 businesses are assisted; and
- For every £1million of public investment some 372.5 skills outputs are delivered.

9.7 Summary

9.7.1 The analysis of the preferred option sets out specifically how and why there are clear commercial / financial benefits in consolidating the four programmes. One of the main benefits of this consolidation process is in the ability of the programme to redirect resources from fixed overheads (e.g. accommodation, travel etc) towards direct delivery costs (i.e. time and money spent with individual businesses). This redirection of resources allows an increase in the amount of direct delivery activity and therefore outputs and outcome. Because this increase is achieved via redirecting resources within the programme, the overall cost effectiveness of the programme also increases.

10 Risk and sensitivity analysis

10.1 Introduction

10.1.1 This section of the appraisal builds on the sensitivity analysis at section 10 and provides an analysis and assessment of risks that may affect the programme and its ability to achieve its stated outputs and outcomes.

Table 10.1 Main quantifiable risks

Source of project risk	Effect of risk on project	Risk likelihood	Mitigation measure
Scenario 1: Increase in revenue costs	10% cost increase	Low 15% Probability	<p>It is perceived that this will be a generally low area of risk, with limited scope for significant increases in revenue cost, over and above those already modelled. The modelling already conducted has, in line with Green Book guidance, an optimism bias weighting already been built into revenue costs at 20%(max) and revenues reduced by 20%. In these terms, the current configuration of the options already presents a pessimistic scenario. However, this risk assessment tests further these issues through further exploring and testing the pessimistic scenarios already presented for revenue cost increases.</p> <p>There are two main mitigation measures for this risk. The first is the transfer of the delivery of the programme to the private sector. The contracting procedure for this has been initiated and a requirement of the successful bidder will be the achievement of specified outputs for a fixed level of resource. Secondly, through negotiations with the preferred supplier, ONE expects to operate an “open book” contract relationship which will allow the agency full visibility to costs.</p>
Scenario 2: Failure to attract interest amongst regional companies – i.e. limited programme	15% reduction in the overall levels of outputs forecast	High 80% Probability	<p>Again, the risk here has – in effect – already been modelled via the application of a -20% optimism bias weight being applied to all forecast outputs. In these terms, the appraisal already presents an already pessimistic scenario. Nonetheless, under-achievement of outputs is can be a regular occurrence within publicly funded business support</p>

Source of project risk	Effect of risk on project	Risk likelihood	Mitigation measure
take up			<p>programmes and accordingly, we have modelled the effects of this risk to programmes overall cost effectiveness.</p> <p>Part of the rationale for the integration of the 4 programmes is to avoid this. Integration will enable the installation of a single and overarching customer relationship management system which will enable cross referrals between programmes to be managed much more effectively than would be the case under a dispersed structure. Similarly, the creation of a clearer market facing brand and a single overarching marketing strategy will also help improve customer awareness of the programmes, thereby maximising interest and take up.</p>
<p>Scenario 3: Full extent of efficiency gains achieved by consolidating the programme not realised</p>	<p>Only 50% of total efficiency gains actually achieved</p>	<p>High – 40%</p>	<p>Whilst the rationale for integrating the programmes into a single overall programme is strong, the benefits (financially at least) will only be fully realised through careful planning and financial management. Likewise additional quantifiable economic benefits rest in the combined programmes ability to reduce overhead and increase direct delivery resource, thereby enabling more output. As such, this is an important risk.</p> <p>The risk will be managed and mitigated via the production and regular monitoring of a set of financial statements and accounts that will include a detailed and regular review of savings achieved in operational overhead. In part, the risk for achieving the reduced overhead will be transferred to the private sector operator, who will be under a contractual obligation to fulfil specified output targets with a fixed and finite level of resource.</p>

10.2 Sensitivity analysis

10.2.1 Building on the above issues and analysis, this section of the appraisal includes a sensitivity analysis in order to gauge the impact on the programme of:

- A further 10% increase in all costs;
- A 15% decrease in the numbers of jobs created and / or safeguarded; and
- A 50% reduction in the levels of efficiency achieved via integrating the 4 programmes; and
- A combination of all of these events.

10.2.2 In the analysis that follows we used the unit cost per net job created / safeguarded under the preferred option as a measure against which to compare the impact of the sensitivity – i.e. the sensitivity analysis compares the extent to which the unit cost per net job created / safeguarded increases or decreases as a result of the different scenarios.

10.3 10% increase in all costs

10.3.1 A 10% increase in overall costs results in an increase in the unit cost per net job created and / or safeguarded. Table 10.2 illustrates that under this scenario gross costs increase to just over £39million, against a baseline position of £35.5million and that the cost per net job created / safeguarded increases from £6,762 to £7,438. Thus 10% increase in all costs results in a 9% increase in the cost per net job created / safeguarded.

Table 10.2 Effects of a 10% increase in all costs.

Total Expenditure (£)	<i>Total</i>
Gross Costs (after 10% increase)	39,057,453
Optimism (after 10% increase)	44,916,070
Discounted (after 10% increase)	40,377,619
<i>Baseline (Preferred Option, no increase)</i>	35,506,775
Cost per (Net) Job Created (£)	<i>Average</i>
Gross Costs	7,438
Optimism	10,063
Discounted	9,046
<i>Baseline</i>	6,762

10.4 15% decrease in net jobs created / safeguarded

10.4.1 A 15% reduction in the numbers of net jobs created and / or safeguarded results in a significant increase in the unit cost per net job created / safeguarded. Specifically, a 15% reduction results in a 27% increase in the unit cost per net job created / safeguarded. Under this scenario, gross costs would remain as per the baseline position in the preferred option, whereas the cost per net job created / safeguarded would increase from £6,762 to £8,544 (gross).

Table 10.3 Effects of a 15% reduction in net jobs created / safeguarded

Cost per (Net) Job Created (£)	<i>Net Jobs</i>	<i>Cost per Net Job</i>

Cost per (Net) Job Created (£)	Net Jobs	Cost per Net Job
Gross (after 15% reduction in output)	4,566	8,554
Optimism (after 15% reduction in output)	3,881	11,573
Discounted (after 15% reduction in output)	3,881	10,403
<i>Baseline (Preferred Option, no reduction)</i>	5,251	6,762

10.5 50% reduction in overall efficiency gains

10.5.1 The model that underpins the appraisal assumes that roughly 20% of all fixed overhead costs will be saved by integrating the four programmes into a single one (this varies by cost item – 20% is a reasonable approximation of the average however). This scenario explores the effects of this efficiency gain reducing by 50% - i.e. to an average of 10%. The effect of this would obviously be a reduction in the amount of money that can be reallocated to direct delivery. This in turn would have an impact on the amount of outputs generated by the overall programme. Table 10.3 illustrates that a 50% reduction in efficiency savings has only a small impact on the unit cost of the net job created / safeguarded – 1.9%.

Table 10.4 Effects of a 50% reduction in efficiency gains

Cost per (Net) Job Created (£)	Net Jobs	Cost per Net Job
Gross (after 50% reduction in efficient gain)	5,153	6,891
Optimism (after 50% reduction in efficient gain)	6,062	6,735
Discounted (after 50% reduction in efficient gain)	6,062	6,055
<i>Baseline (Preferred Option, no reduction)</i>	5,251	6,762

10.6 Combined impact of all scenarios

10.6.1 The final sensitivity analysis involves analysing the impact of all of the above scenarios occurring together – i.e. a 10% increase in all costs, a 15% reduction the numbers of jobs created / safeguarded and a 50% reduction in efficiency gains. Unsurprisingly this has the most pronounced effect on the unit cost per net job created / safeguarded, with an overall increase of 32%.

Table 10.4 Combined impact of all scenarios

Cost per (Net) Job Created (£)	Net Jobs	Cost per Net Job
Gross (after all 3 scenarios)	4,380	8,917
Optimism (after all 3 scenarios)	3,723	12,064
Discounted (after all 3 scenarios)	3,723	10,845
<i>Baseline (Preferred Option, no reduction)</i>	5,251	6,762

10.7 Criticality test

10.7.1 Table 10.5 shows that under the preferred option, a 1.0% decrease in net additional jobs leads to a 2.1% decrease in the value of the economic NPV, which is a critical result. Criticality testing on the other two variables under this option demonstrates that they are both near critical.

Table 10.5 Criticality test: Preferred option

Variable	Effect on Economic NPV of a 1% Change in Value	Criticality Result
Increase in revenue	-0.9	Near Critical
Reduced Net Job Outputs	-2.1	Critical
Reduced Efficiency Gains	-0.9	Near Critical

10.8 Other risks

10.8.1 Other risks include the project are: failure to secure ERDF funding, failure to gain CPRG or Treasury support for the project and risks to the current exemplary reputation of the MAS/NEPA brands and service.

- In the case of ERDF, the picture will become clearer after March 08. The Agency has taken a cautious but prudent approach to the level of ERDF to be requested and work is underway to try to ensure that the anticipated level of ERDF for MAS-NEPA is secured. However, draft plans are in place to scale back the project if necessary. This will lead to reduced outputs but will ensure that the project can still go ahead.
- With regard to CPRG/Treasury approval, an early meeting took place to seek their views from the start of the project development in July. A further meeting took place on 6th November to discuss ongoing development and feedback was extremely positive. At this stage, they are indicating strong support for the proposed approach.
- The question of a risk to the integrity of the brand and service is being taken very seriously and is a key consideration both in choosing the successful bidder through the OJEU process and in management arrangements of the new service once in place. Also a detailed transition plan is being developed. The Agency will be strongly represented on the Governance arrangements for the new service.

10.9 Summary

10.9.1 The analysis indicates that the model for the combined programme is most sensitive to a reduction in the net amount of jobs created / safeguarded. Just a 15% reduction results in a 27% increase in the cost effectiveness of the programme (as measured by the unit cost per net job created / safeguarded). If we combine this sensitivity with two others – a 10% increase in overall cost and a 50% reduction in efficiency gains achieved by combining

the programmes, the overall effect is a 32% increase in cost effectiveness. Criticality testing also reveals that a 1.0% decrease in net additional jobs leads to a 2.1% decrease in the value of the economic NPV, which is a critical result. Criticality testing on the other two variables under this option demonstrates that they are both near critical.

11 Delivery

11.1 Introduction

11.1.1 This section provides an overview of the procurement process for this project, the criteria ONE have developed for evaluating individual bids, and the contractual and performance measures that will be put in place throughout the delivery process.

11.1.2 The procurement process is currently underway. Therefore, no detailed information can be provided on the final delivery framework for this project in this appraisal.

11.2 The Procurement Process

11.2.1 The new service will be procured under OJEU and will be managed via a contractual arrangement. Stringent contractual controls will be agreed and applied where necessary.

11.2.2 The proposed bidders will be required to have the following attributes which are commensurate with those of One NorthEast, these include:

- To have extensive knowledge of the manufacturing sector;
- To possess credibility and expertise in delivering productivity, lean manufacturing, resource efficiency, design and other related services;
- To be able to demonstrate an in-depth knowledge of the North East economy and manufacturing sector and understanding of the strategic context and importance of the sector to the region;
- To possess track record of managing similar scale projects and demonstrate clear commercial acumen; and
- To be able to demonstrate how they will boost the economy of the North East by supporting manufacturing businesses to become more productive, competitive and deliver increased GVA.

11.2.3 The procurement process will be structured according to the Competitive Dialogue process as defined by the European Procurement Guidelines. This process includes an initial short listing step followed by a stage where the delivery solution is discussed with Bidders prior to a final structure being defined. Once a definitive structure is agreed, Bidders will then be requested to provide fully priced tenders on the outlined structure.

11.2.4 All relevant methodologies and materials will be protected by copyright for use by the successful bidder. Work is now underway to apply for trademark status for the NEPA brand and to establish a range of branding guidelines. The brand will be offered under license to the successful bidder and this will ensure the integrity of the brand and One NorthEast's association with it going forward. In addition, work is underway to establish relevant domain names which will be used by the successful bidder.

11.3 Performance Requirements

11.3.1 Table 1 shows the Output tables presented to prospective bidders in the PQQ. This table shows the NEPA/MAS outputs.

Table 11.1 - Outputs

	2008/09	2009/10	2010/11	2011/12	2012/13	Total
Jobs created and safeguarded	1,146	1,542	1,717	1,879	1,961	8,245
Businesses supported	599	806	898	982	1,026	4,311
Skills	1,838	2,474	2,754	3,014	3,146	13,226

11.4 Procurement Timeframe

11.4.1 As part of the procurement process ONE has a detailed timeframe for the bidding process. The key dates are set out in the table below.

Table 11.2 procurement timeframe

Milestone	Target Date
OJEU notice posted	September 2007
Return of PQQ'S	October 2007
Notification of selected parties at Competitive Dialogue stage	December 2007
Issue Dialogue stage documents to facilitate discussion between ONE and Bidders	December 2007
Close of Competitive Dialogue Stage	February 2008
Issue tender documents to bidders requiring a fully priced tender	March 2008
Return of tender documents	April 2008
Clarification and evaluation	May 2008
Selection of preferred bidder	May 2008
Enter into contract with selected partner	May 2008
New service is due to start	July 1 st 2008

12 State Aid

12.1 Introduction

- 12.1.1 The Dissemination of Best Practice and Energy Resource Efficiency projects operate under Training Block Exemption rules, MAS operates under SME Block Exemption rules, and the Design in Manufacturing activities will be operated under Deminimus and Training Block exemption rulings in parallel. These are all in the process of being notified for the MAS-NEPA joint project which will run out to 2013.

13 Monitoring and Evaluation

13.1 Introduction

13.1.1 This section provides details on the monitoring and management structures for the project, the arrangements to be put in place to verify the project and how the project will be evaluated.

13.2 Management Structure

13.2.1 The whole support offering will be delivered by a management team suitably qualified in the relevant project disciplines. The overall governance will be by the following procedures:

- Appointment of a 'Nolan' compliant board to oversee outputs and develop future possibilities for interventions;
- Six monthly reviews by the delivery managers with an agency representative to review outputs and achievements. This will also be seen as an 'ideas forum';
- Quarterly claims to the agency;
- A monthly operations meeting of the delivery managers and other delivery partners such as Envirowise, NEPIC and the Skills Academies;
- Activity/intervention based reporting via a simple A3 format with benefit costings;
- MAS will be required to report to MAS centre as determined by BERR; and
- An agency representative will attend all meetings other than ongoing operational meetings.

13.2.2 It is expected that success stories will be published in journals and local press to promote the brand and support from One NorthEast

13.3 Monitoring and Evaluation

Monitoring

13.3.1 The proposer will be responsible for overseeing the project which will be managed via contractual arrangement. The proposer has considerable experience of this type of project management, and is also responsible for the BLNE contract.

13.3.2 The project will be monitored by Business & Industry Team in line with the Agency's business process. The Agency will put in place a monitoring group which will receive and verify all claims. The key monitoring system will consist of:

- Every 6 months a full monitoring audit will take place on each project. This can be increased to quarterly depending on performance (risk).
- Every 6 months visits will take place to recipient companies picked at random to audit trail documents and outcomes. This will take place for each project.
- Engagement with organisations such as ONS, NERIP and universities will allow for ongoing economic impact monitoring of the projects. This should be measured in terms of individual beneficiaries as well as company beneficiaries.

Evaluation

- 13.3.3 ONE North East is currently working up a formal evaluation strategy for NEPA–MAS. This will focus on the extent to which interventions help raise productivity, turnover and employment in supported firms. In addition, work will attempt to quantify the impact on the wider regional economy. Establishing an appropriate counterfactual will be particularly tricky with this type of support. And the impact of our support for individual firms is likely to build up over a period of time. No single research method will deliver a thorough evaluation of MAS-NEPA. So we expect to adopt a range of methods to improve our understanding the effects of our investment. This will include: case studies of individual interventions and the impact on working practices; detailed monitoring of company performance from first point of contact onwards; and quantitative analysis to benchmark company performance against other firms and over time.

Appendix A – Willingness to Pay

Introduction

1. The design and development of the MAS-NEPA programme post 2008 has begun from a standpoint that recognises that the programme must continue to include private sector contributions, measure these more consistently and explore ways in which these contributions can be increased over the next 5 years. These private sector contributions are benefits to the programme and include both in-kind contributions and actual cash contributions. This paper considers the *cash* contributions that ONE intends for companies to make to the programme over its next 5 years. The paper is based on the findings of a consultation exercise with a small selection of companies based in the North East that involved testing their willingness to pay for components of the MAS-NEPA programme.

The consultation exercise

Overview

2. Five companies were contacted in November 2007 who had received the 'Narrow and Deep' NEPA programme of support since 2003. In addition to this, 2 companies that have not been involved in any of the programmes were also consulted.
3. The total cost incurred by the NEPA programme in offering the support to the 5 companies totalled £403,601 equivalent to on average £80,720 per company. The total value of the In Kind contributions made by the participating companies was £249,890, or an average of £49,978 per company.
4. Other key outputs from the NEPA support are shown in table 1.

Table 1 – Cost of support and key outputs of the companies contacted	
Total cost of support	£403,601
Value of Company In Kind Contributions	£249,890
Learning Opportunities	352
Jobs Created	94
Jobs Safeguarded	531

Source: ONE North East / NEPA

Experience of the NEPA programme

5. There was a general consensus amongst the companies consulted that the overall experience of the NEPA programme had been extremely beneficial. The main benefits that the companies experienced were:
 - Increase in productivity;
 - Better trained staff;
 - Increase in turnover; and
 - Improvements to planning and implementation systems.

6. All companies had experienced sustained benefits from the NEPA programme, and were positive in their willingness to use the service again – if required – for further productivity gains.
7. The in-kind contributions are defined as costs of staff time. These costs are considered accurate and were specifically calculated by individual companies, using strict definitions adopted by NEPA Engineers.

In Kind contributions

8. Companies already make contributions “in-kind” to the NEPA programme. These are different to outright cash contributions, but are nonetheless, considered very important by all parties. Indeed, of the 5 companies interviewed, all felt that they had made a significant ‘in-kind’ contribution during the course of the ‘Narrow and Deep’ programme through the provision of staff to become Change Agents – a key component of the NEPA programme. In most cases, staff members were taken from their original jobs, and became dedicated to the NEPA programme.
9. Whilst this clearly had a significant benefit for the companies concerned (in ensuring the long term success of the programme) the time investment made on behalf of the companies is considered by all of them to be very significant. In-Kind contributions are at the heart of what the programme is about: it is one of the key ways in which both ONE North East can perceive the commitment to transformational change within the company and likewise one of the key commitments made by the company to the transformational process itself.
10. In some ways In-Kind contributions are more important than cash contributions to the programme precisely for this reason. A forecast of the level of in-kind contributions likely to be made by the overall programme post 2008 is set out in Table 2.

Table 2: Forecast In-Kind contributions

Leverage	2008/09	2009/10	2010/11	2011/12	2012/13	Total
Private sector Contribution in Kind (including down time) - NEPA Best Practice	695,000	795,000	895,000	995,000	1,095,000	4,475,000
Private sector Contribution in Kind (including down time) - NEPA Energy	200,000	300,000	400,000	500,000	600,000	2,000,000
Total In-Kind Contributions	895,000	1,095,000	1,295,000	1,495,000	1,695,000	6,475,000

11. The case study below helps to bring to life a real example of where and how contributions in kind are made through the programme. This is based on a genuine example of a company that has previously participated in NEPA.

CASE Study

CORUS Tubes Energy Business

Following the successful continuous improvement programme run by the company with NEPA over the last 3 years, the Energy Resource Efficiency Project is now focussing on the 84" Pipe Mill. The company aims to reduce energy usage and therefore costs, boost efficiency and reduce its carbon footprint by producing less carbon dioxide. This will assist in their continuing drive to improve competitiveness, win more orders, secure more jobs and increase profitability. The

continuous improvement programme has already resulted in a significant improvement in productivity over a 3 year period. The 42" mill has moved from a 10-shift operation to 15, 350 employees have successfully completed NVQ Level 2 qualifications in Business Improvement Techniques, while 44 people are now studying for Level 3 or 4 certificates.

The company has provided the following estimates on downtime and cash in kind contributions to date:

- ERE project (over the last year) – Downtime = £31,500. Cash in kind = £25,000. Future commitments: Further Downtime & cash in kind in 42" Mill.
- DBP project (over the last 3 years) – Downtime = £94,000. Cash in kind = £80,000. Future commitments: Cash in kind = £15,000.

Attitudes towards payment

12. A common theme running through the companies we contacted was that they had used the NEPA service when the financial and operating performance of the business was poor. Most suggested that they had already been approached by private sector consultancy firms to help deal with the issues at that time, but had found them to be too expensive and beyond their financial reach at that point in time.
13. For most companies, the fact that the NEPA service was free was the reason that they chose the NEPA programme – most felt that some of the benefits cited by NEPA could have been achieved by other consultancy organisations, but at a higher cost to the company itself. One company felt that it would have been difficult to persuade the Board to make a speculative investment into the NEPA programme if payment for services had been required, and would have been unlikely to use the service in this scenario. This was simply due to a lack of funds at that time to pay for services.
14. It was also felt that such an 'in-kind' contribution would not have been as feasible if a cash contribution was also required. This was in many cases seen as the trade-off between paid consultancy services and the NEPA programme.

Willingness to pay

15. A component of the interviews with companies involved testing their willingness to pay for the programme in the future. The intention was to establish a view as to:
 - General attitudes towards paying for the programme in the future;
 - Specific attitudes towards particular payment amounts; and
 - Specific expectations of the programme under a "cash payment" scenario.

General attitudes towards payment

16. Generally speaking there was a positive reaction from companies when asked if they would be willing to pay for the programme in the future. All of those interviewed spoke highly of the programme and its benefits, and likewise all companies considered those benefits to be of a scale and type that would – in the future – justify a cash payment.
17. This initial conclusion would appear to be consistent with intelligence gained from other regional business support programmes, where companies have already proven themselves willing to make cash contributions to their costs. One such programme is the regional Business Link

programme. Through this a total of 3,849 subsidies were given out to 3,148 businesses in 2006/07. In financial terms, this means that Over £12 million was made available to the region’s SMEs, with a regional average of £3,242 per company. SMEs were expected to contribute over £14 million for the grant aided projects, with an average of £3,770 being contributed. Of these companies:

- 513 manufacturers received 706 subsidies
- Total grants awarded to manufacturers was £2,153,033
- Total cash contribution by these manufacturers was £2,232,586
- Average subsidy per manufacturing SME was £3,050
- Average contribution made by the manufacturing SMEs was £3,162

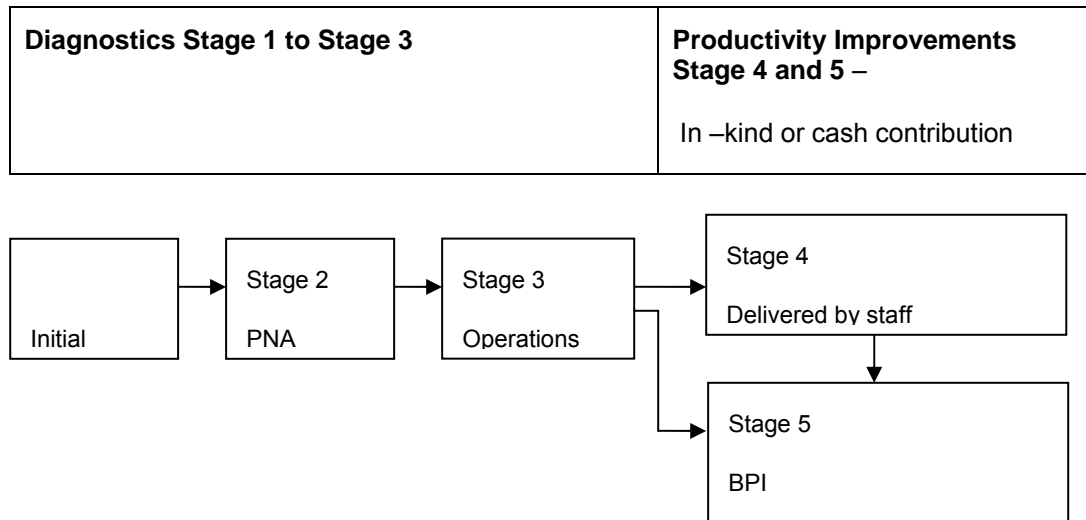
Specific attitudes towards payment amounts

18. In order to focus company discussions upon specific payment amounts a financial analysis of the NEPA programme in previous years was carried out. Specifically, an analysis of the average rate of intervention was computed. The 2008/09 forecasts for the overall MAS-NEPA programme is that costs incurred will be £5,718k and some 599 interventions will be made using this. This generates an average intervention rate of £9,543.
19. The consultant team were asked to test the appetite of companies towards making different levels of cash contribution, up to a point at which the overall intervention rate equally shared between the programme and the individual company beneficiary. Specific thresholds leading up to this point were also considered. These are illustrated in Table 2 and a phasing structure (year on year) is considered as part of this.

Table 3 –Intervention Rate Scenarios					
Businesses assisted	1	2	3	4	5
	2008/9	2009/10	2010/11	2011/12	2012/13
<i>Average intervention rate</i>	£9,543	£8,705	£8,246	£7,832	£7,483
<i>Programme Subsidy</i>	£9,543	£6,964	£5,497	£4,476	£3,742
<i>Company contribution</i>	£0	£1,741	£2,749	£3,357	£3,742
	£9,543	£8,705	£8,246	£7,832	£7,483

20. The table assumes that the cost effectiveness of the programme increases year on year – i.e. the average intervention rate decreases year on year as a result of the programme efficiencies achieved via integration and the movement of resources from fixed overhead towards direct delivery.
21. Companies were asked to indicate, based on their experience of benefits and impacts, which of the above pricing structures they would regard as acceptable and which, if any, they would not.

Figure 1: programme overview



22. In addition to specific payment amounts, Companies were asked to identify which particular components of the programme they would be willing to pay for. All companies were presented an overview of the key stages of the programme, as per Figure 1, above.
23. All companies agreed that the first 3 stages of the programme, much of which is exploratory and diagnostic in its orientation, were beneficial, but unlikely in their own right to produce tangible productivity improvements. The companies indicated that based on this, they would only be willing to contribute to the final aspects of the programme, Bespoke Productivity Improvements
24. The initial conclusions from this exercise are that:
 - There is evidence of companies showing willingness to pay for aspects of the MAS-NEPA programme;
 - That willingness to pay is however confined to those aspects of the programme that companies perceive to be most valuable to them – the non-diagnostic aspects;
 - Specific attitudes towards payment amounts varied company by company. There are no specific conclusions that can be reached from the exercise, other than the fact that companies are prepared to make a proportionate level of payment.
 - Some of the companies also considered a “payment by results” approach to be more feasible. However were this approach to be adopted it would skew the focus of the NEPA programme towards companies that had the most potential to generate profits to the programme and this would not always be compatible with the overall programme objectives. This is a key differentiator between the client group of the NEPA programme and that of other Consultancy services.
25. Based on these conclusions, the programme has been structured in such a way as to allow for a gradual increase in the levels of company cash contribution to the BPI component of the programme as follows:
 - 2008/9 – 10% increase
 - 2009/10 -10% increase

- 2010/11 -20% increase
- 2011/12 -30% increase
- 2012/13 -30% increase

26. This generates a cash contribution funding profile as per table 3.

Table 4 Company cash contributions						
	2008/9	2009/10	2010/11	2011/12	2012/13	Total
<i>Private sector cash contributions</i>	259,435	383,901	704,432	994,372	974,530	3,316,670