National Audit Office

REPORT BY THE
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The Regional Growth Fund

Summary

1 The Government wants to see strong, sustainable and balanced growth that is more evenly shared across the country and between industries. It also wants to rely less on the public sector for employment. Meeting these objectives in the current economic climate will be challenging. Places that rely on the public sector may suffer more from spending cuts and also lack the strong private sector needed to generate new employment and growth.

2 In its emergency budget of June 2010, the Government established a Regional Growth Fund (the Fund) with two objectives:

- to encourage private sector enterprise by providing support for projects with significant potential for economic growth and create additional sustainable private sector employment; and
- to support in particular those areas and communities that are currently dependent on the public sector to make the transition to sustainable private sector-led growth and prosperity.

The Fund is part of the Government's wider strategy for local economic growth, which is set out in the 2010 *Local Growth* White Paper and the 2011 *Plan for Growth*.

3 Private sector firms or public–private partnerships were invited to bid for a share of the £1.4 billion Fund for projects that supported its objectives, and which would not otherwise have gone ahead. Applicants had to bid for at least £1 million.

4 The Government initially allocated the Fund £1 billion to be spent between April 2011 and March 2014, increasing this to £1.4 billion in the October 2010 Spending Review. The Government set out in the 2010 *Local Growth* White Paper an expectation that the £1.4 billion would be allocated in at least three bidding rounds. In the event only two rounds were held. In the first round, which closed in January 2011, 464 applicants bid for a total of £2.8 billion funding and £450 million was allocated to 50 projects. In the second round, which closed in July 2011, 492 applicants bid for £3.3 billion funding and £950 million was allocated to 169 projects. A third bidding round offering an additional £1 billion has been opened, with applications to be received by mid-June 2012.

5 Ministers identified which bids should be shortlisted and, following detailed appraisal of the shortlisted bids, decided which projects should be conditionally allocated funding. Ministers were advised by an independent advisory panel, chaired by Lord Heseltine, with further information, analysis and support provided by a small cross-departmental secretariat of officials (the Secretariat). A single Accounting Officer (the Permanent Secretary for the Department for Communities and Local Government) is responsible for delivering value for money.

6 After the appraisal phase, the Secretariat entered into detailed discussions with bidders on the precise terms and conditions attached to payments from the Fund. Each project was then subject to due diligence, in which the company delivering the project must demonstrate its fitness to be a recipient to an independent reviewer.

7 The Chancellor of the Exchequer allocated a further £1 billion to the Fund in November 2011, to be spent between April 2012 and March 2015.

8 This report covers the £1.4 billion allocated to projects in 2011, in the Fund's first two bidding rounds. Our objective was to assess whether it will be spent cost-effectively, meeting the Fund's objectives. In assessing value for money we considered whether the projects selected offer the best achievable outcome and whether the supporting administrative arrangements were robust. We did not assess the individual projects. More information on the bids is available from the Department for Business, Innovation and Skills website. Appendix One summarises our methodology and further details are available on our website.

Key findings

How well the projects selected meet the Fund's objectives

9 **The bids selected offer substantially better returns than those that were not selected.** We found that the projects and programmes selected should be more cost-effective, overall, than those not selected, producing substantially more employment for the same resource invested. The Secretariat's economic appraisal of shortlisted bids followed established good practice guidance and generated a significant volume of useful, standardised information. The information included relevant measures, such as project location, expected gross and net additional jobs, the grant requested, and the ratio of public-to-private investment.

10 **Projects selected support private sector jobs in places that rely more on the public sector, in line with the Fund's objectives.** A key measure of the Fund's success is how well it was targeted at areas in greatest need. The Secretariat developed appropriate statistical methods to assess whether potential projects were located in areas of relatively high need. Based on this assessment, projects selected for support are generally located in places that are relatively more vulnerable to public sector job losses. We cannot say yet what the Fund's overall contribution will be to the broader aim of rebalancing the economy in any particular area in the longer term. Evaluations of similar programmes indicate that the sustainability of a boost to private sector employment locally will depend on other factors such as business productivity, the cost and availability of housing and other amenities, and local skills levels.

The number of jobs supported by the Fund

11 **The Secretariat's review of bids indicated that the projects the Fund is supporting could create or safeguard 328,000 jobs.** This was an estimate of the maximum number of jobs over projects' lifetimes. Each job was counted equally, regardless of how long it was expected to last. Around 20 per cent of these jobs would be created directly by supported projects. The remainder would be created indirectly, through programmes, or where bidders identified potential for knock-on employment effects in their supply chains. It will be difficult to monitor these wider indirect impacts, which will make evaluating the Fund's total impact harder.

12 **The Government expects to receive firm commitments from successful bidders to deliver 117,000 full-time-equivalent jobs.** The Secretariat's final offers to successful bidders are conditional on the average number of jobs maintained over the full course of each project. The average duration of projects is expected to be at least seven years.

13 **Not all the jobs delivered will be 'additional'.** Some of the jobs might have been created or safeguarded anyway, and assisting one firm over another might affect markets and competition. The Secretariat made reasonable assumptions about these factors and also the risk that projects might not deliver as intended.

14 **Taking account of these factors there could be 41,000 more full-time-equivalent jobs in the economy than without the Fund.** Estimates of bids' net additional effects were presented to Ministers to help them choose which projects to support.

The public sector cost of jobs created or safeguarded

15 **If the Fund delivers in line with expectations, the average cost to the Fund of each net additional job would be £33,000.** It is difficult to benchmark this cost against the cost per net additional job of similar previous programmes because evaluations do not contain strictly comparable information. However, based on the information available, a cost of £33,000 per net additional job is similar to the cost per net additional job achieved by programmes with comparable objectives.

16 **Over 90 per cent of the net additional jobs could have been delivered for 75 per cent of the cost, with the cost of each job then being £26,000. The cost per net additional job supported by the Fund varies from under £4,000 to over £200,000.** The National Audit Office defines value for money as the optimal use of resources to achieve the intended outcomes. Optimising value for money from the Fund would have meant creating as many jobs as reasonably possible in vulnerable areas. However, a significant portion of the £1.4 billion was allocated to projects that create or safeguard relatively few jobs for the money invested. For example, the 27 least cost-effective awards – totalling some £160 million – will cost the Fund £106,000 per net additional job.

17 **Holding three or more rounds to generate more cost-effective bids was an option but in the event only two rounds were held.** The Fund's Accounting Officer reported that Ministers judged that there were sufficient good-quality bids in the first two rounds to avoid the need for a third. In reaching this conclusion Ministers considered a wide range of factors including whether there were vulnerable areas that were not covered by more cost-effective bids. The Secretariat told us that in cases where the appraisal suggested lower value for money, they considered the potential to improve value for money through the detailed negotiation of projects' terms and conditions and due diligence. However, our analysis indicates that a significant number of projects in the first two rounds performed relatively poorly on criteria such as the amount of additional employment supported and the ratio of economic benefits to public costs, and the way in which the broader criteria described above were defined and applied is not clear enough to allow us to determine, on review, whether they should have outweighed objective considerations or not.

18 **The Fund's Accounting Officer advised Ministers that the Fund should only support projects where the projected economic benefits outweighed the public cost. This filter provided limited challenge to bids' cost-effectiveness.** Projects where the total economic benefits exceed the cost of public funding can still have a very high public cost per job, on which no upper limit was placed.

Getting the projects up and running

19 Around a third of successful projects had received final offers of funding at March 2012. Despite the scale of the task involved in assessing hundreds of bids and turning conditional offers into formal final offers, no administration budget was identified for the Fund at the outset. Officials collaborated effectively across departments and worked hard to manage competing pressures during the appraisal phase. However, agreeing terms and conditions of grants with successful bidders has taken the Secretariat significantly longer than expected. Finalising grant terms has been particularly time-consuming for projects where the initial value-for-money case was weaker. Delays at this stage have knock-on effects because due diligence cannot begin until significant progress has been made in agreeing grant terms and conditions. The pace at which the projects have been made final offers has, however, accelerated since December 2011.

20 The Secretariat could have retained greater control over the due diligence process. Beneficiaries bear the costs of due diligence and officials consider this encourages applicants to put in commercially sound bids. The risk of inconsistency in the level of assurance provided through due diligence could have been reduced had the Secretariat been more directly involved, for example by appointing specialists to review relevant bids.

Conclusion on value for money

21 If the Regional Growth Fund delivers as expected there will be 41,000 additional full-time-equivalent private sector jobs in the economy for seven years, supporting particularly those areas that currently rely more on the public sector. Bids were subject to standardised appraisal within competitive bidding rounds. Overall the projects selected should deliver jobs more cost-effectively for the taxpayer than the projects not selected. However, value for money was not optimised because a significant proportion of the Fund was allocated to projects that offered relatively few jobs for the public money invested. Applying tighter controls over the value for money offered by individual bids would improve the Fund's overall cost-effectiveness. Officials' time freed up from post-appraisal checks on projects where public money is providing fewer jobs could be spent on getting other projects up and running more quickly. Such an approach provides the prospect of better value for money and faster delivery from the further £1 billion allocated to the Fund in the Chancellor's November 2011 *Autumn Statement*.

Recommendations

22 We make the following recommendations to improve value for money from subsequent rounds of the Fund and identify broader lessons for programme management practice across government.

a **The Secretariat used standardised appraisal techniques to generate useful information to help Ministers choose between competing bids.** Departments, particularly the Department for Communities and Local Government and the Department for Business, Innovation and Skills, should embed good practices from the Fund's project appraisal methods more widely.

b **Applying tighter controls over value for money could improve the Fund's cost-effectiveness and allow officials to get projects up and running more quickly.** The Fund's management board, led by the nominated Accounting Officer, should:

- apply tighter controls over the value for money offered by individual bids, for example by comparing costs per job to evidence-based benchmarks, such as results achieved by similar projects and programmes;
- use funding flexibly, across smaller bidding rounds if necessary, to maximise the value obtained from public investment; and
- if value for money cannot be achieved through the Fund's competitive bidding process, consider whether alternative options could achieve the same objectives more cost-effectively.

c **Due diligence requires bidders to demonstrate their fitness as recipients of the Fund to an independent reviewer.** In future rounds of the Fund – and future programmes where appropriate – officials should explore ways to retain greater control of the due diligence process, where this could deliver sufficient assurance more efficiently.

d **The Fund did not have sufficient administrative resources to carry out all the necessary tasks quickly.** The Fund's Accounting Officer should make sure sufficient staff and resources are available to carry out all the necessary tasks in future bidding rounds. This is especially important if tasks like negotiating final offer letters and appraisal are expected to run in parallel.

e **Robust monitoring and evaluation will be required to validate the number of jobs created by the Fund.**

- The Secretariat should progress its draft evaluation strategy. Evaluation should begin while projects are being developed, to maximise the learning from experience.
- The Department for Business, Innovation and Skills and the Department for Communities and Local Government should develop and apply an evaluation framework and standard measures to improve the scope for drawing like-for-like comparisons between similar programmes.