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How Brexit puts the UK at risk of more collapses like Carillion

January 19, 2018 3.50pm GMT



Why does it always rain on me? Yui Mok/PA Wire/PA Images

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The construction industry has always been characterised by uncertainty. Managing large construction projects involves enormous challenges, coming from the political, economic, social and technological environments involved. The bigger the project, the bigger the challenge. For big infrastructure projects such as railways and hospitals, we're talking multi-million pound contracts and thousands of employees, over a number of years.

So, in many ways, the collapse of the UK's second-largest construction company, Carillion, is not surprising. The National Audit Office, which scrutinises the UK government's public spending, predicted that more than one-third of mega projects – the kind that the government outsources to Carillion – will fail in the years ahead.

And yet the shape and speed of Carillion's demise was still shocking – even to the many industry observers who were watching its poor performance over the past year. Not least because its rapid descent into liquidation, without first going into administration, put 40,000 jobs at risk overnight.

Carillion's demise shows the risks that are encountered in an industry that contributes £90 billion (6.9% of GDP) to the UK economy. Although it is still too early to know all the details of how and why it collapsed, it is an important reminder that the construction industry is characterised by risk, uncertainty and complexity on all levels. And something we should be mindful of is how Brexit will compound this.

Uncertainty abounds

A quick glance at the performance of Carillion shows that it amassed risky contracts without being able to fulfil its commitments. This put it under mounting debts – its liabilities were in excess over its total value of assets – and precipitated its demise. Winning lucrative contracts is great, but contractors need to have a positive cash flow to pay the various instalments of implementing its contracts.

The basics of planning and scheduling construction projects is that contractors need to keep schedules of their projects in balance with their available cash. In other words, contractors can win as many projects as they can, but they must be able to fulfil their outward payments at any given point of project implementation. When every contract comes with uncertainty, this is magnified when more projects are run at the same time.

Managing projects in general means managing uncertainty that is divided into known uncertainty and unknown uncertainty. For example, companies know that when they are building over the winter, they should allow time for bad weather slowing projects down. But an example of unknown uncertainty that Carillion ran into when working on the Royal Liverpool University Hospital was the “extensive” asbestos that was found on the brownfield site where it was being built.

The ongoing Brexit talks add a new layer to these uncertainties. The UK is engaged in negotiations with the EU on its single market access, which will affect the free passage of people and goods with its biggest trade partner. EU imports equal 6% of production costs in the UK's construction industry and 8% of the industry's existing workforce is at risk if the UK does not retain access to the single market.



Much-needed construction industry workers could soon be stopped at the UK border. Joe Giddens/PA Wire/PA Images

So there is a big worry over whether companies can implement projects in the UK smoothly. Construction projects are usually labour-intensive and the right skills are needed. **Government figures** show that the skills gap is widening and there is not sufficient labour to fill vacancies on big construction projects. Added to this is the UK's ageing workforce. Even without Brexit, the construction industry predicts a 20-25% decline in its workforce over the next decade. So, if the UK cannot reach a good deal for the construction industry, more big infrastructure projects will be at stake.

Brexit will also have an impact on the way that most big infrastructure projects are funded – through private finance initiatives or PFI. The government pays the private sector to build its big projects, awarding the contract to the best bidder. Some projects have also **benefited from the European Investment Bank**, which the UK will no longer be party to when it leaves the EU. This could make it more reliant on PFI, which is **highly controversial**.

The construction industry has barely recovered from the 2007-08 financial crisis. The latest figures show a slight growth in output, but this was merely thanks to residential construction. Commercial and public projects have been slowing down. With Brexit providing so much uncertainty in the months ahead, we should not be surprised if we see more construction companies struggling.



UK Construction Brexit PFI Carillion