



Government  
Commercial  
Function

# MARKET MANAGEMENT

Guidance Note



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# 1. Introduction

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## 1.1. Issue

Market management is about understanding the markets that we source from, recognising our influence on these markets, and designing commercial strategies and contracts that promote healthy markets over the short, medium and long term.

Better market management should lead to more competitive markets, fewer situations where we are over reliant on one or two suppliers, and improved value for money.

This Guidance Note introduces new rules and guidance for in scope procurements:

- Conduct a market health assessment and consider how the commercial strategy and contract design can be adapted to address market weaknesses.
- Strategic Outline Business Cases must demonstrate that appropriate market assessment and appropriate consideration of options to promote market health has taken place.

Further, the Guidance Note:

- provides an overview of market management policy;
- provides guidance on how to monitor market health; and
- provides guidance on how commercial strategies and contracts can be adapted to respond to market weaknesses and promote healthy markets.

## 1.2. Dissemination

The contents of this Guidance Note apply to all Central Government Departments, their Executive Agencies and Non-Departmental Public bodies. Contracting Authorities within the wider public sector are also encouraged to apply this advice.

## 1.3. Timing and scope

This Guidance Note applies to all new procurements that constitute outsourcing and have an expected contract value exceeding the relevant public contract regulation threshold.

## 1.4. Contact

Enquiries about this Guidance Note should be directed to the Outsourcing Programme team at [project.santiago@cabinetoffice.gov.uk](mailto:project.santiago@cabinetoffice.gov.uk).

## 2. Overview of market management policy

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### 2.1. Background

Healthy, competitive markets matter because they support our ability to achieve value for money for taxpayers.

Market management is about understanding the markets that we source from and then designing commercial strategies and contracts that promote healthy markets over the short, medium and long term.

Government already undertakes various activity that is related to market management. For example:

- ahead of new procurements, commercial staff use market engagement exercises to understand the interests and constraints of potential suppliers;
- the Crown Commercial Service (CCS) produces market intelligence reports and shares these with interested departments;
- commercial staff may set tender participation and evaluation criteria in a way that encourages new entrants; and
- commercial staff may disaggregate contracts, to encourage a wider supplier base over time.

However, government has not always succeeded in maintaining a deep understanding of the markets that it relies on, nor has it always succeeded in promoting entry and building a strong, competitive supplier base. For example, the NAO has reported on failed attempts within government to open up markets to third sector bidders due to resource intensive bidding processes and fixed time tables<sup>1</sup>; and the Committee of Public Accounts has questioned whether some suppliers have become too big and too important to government to be allowed to fail<sup>2</sup>.

In order to help address these issues and build healthy, competitive markets, a new market management policy has been developed.

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<sup>1</sup> See section 3 of [NAO Commercial Contract Management: Insights and Emerging Best Practice](#).

<sup>2</sup> See the [PAC report on Strategic Suppliers](#).

## 2.2. What is the policy?

As set out in the [Outsourcing Playbook](#), the key principle of our market management policy is to:

***“assess the health of the market you will be dealing with and consider how your commercial strategy and contract design can be adapted to address potential limitations”.***

This principle applies to all new procurements that constitute outsourcing and have an expected contract value exceeding the relevant public contract regulation threshold.

There is not a set form or template that market management activity must follow. Instead, a flexible, risk-based approach should be used. A detailed market assessment that comprehensively covers the questions and indicators in Section 3 ‘How to monitor market health’ will be appropriate where criteria (1) and one or more of criteria (2) to (6) apply<sup>3</sup>.

Criteria	Example
1. Government is a market-maker and/or accounts for a large part of the market	<ul style="list-style-type: none"> <li>Revenues from UK government account for around 25%+ of total market revenues</li> </ul>
2. Contract(s) are long-term	<ul style="list-style-type: none"> <li>Contracts with 5+years duration</li> </ul>
3. Contract(s) are for novel or contentious services	<ul style="list-style-type: none"> <li>Critical public service that is important to the public and to the department’s reputation</li> </ul>
4. Contract(s) are high-value to government	<ul style="list-style-type: none"> <li>Combined cost of £50m+ per annum to a department or £200m+ per annum to government as a whole</li> </ul>
5. Past experience or initial intelligence gathering suggests a risk of poor market health	<ul style="list-style-type: none"> <li>Statements by potential suppliers suggests a risk of 3 or fewer credible bids per contract</li> <li>Previous or initial market analysis suggests one or more of these issues: market concentrated in favour of a small number of firms, substantial barriers to entry, substantial barriers to switching between suppliers, misaligned incentives between buyers and suppliers, risk of poor value-for-money outcomes.</li> </ul>
6. First generation outsourcing	<ul style="list-style-type: none"> <li>Government is outsourcing a public service that was previously delivered in house</li> </ul>

Table 1. Criteria for undertaking Market Assessments

<sup>3</sup> For the avoidance of doubt, a detailed market assessment will be appropriate for all procurements that meet the definition of complex outsourcing in the Outsourcing Playbook.

Strategic Outline Cases must demonstrate that appropriate market assessment and consideration of options to promote market health has taken place.

To reduce the likelihood that Strategic Outline Cases are rejected or delayed, departments are encouraged to approach the Cabinet Office Markets & Suppliers team at an early stage and seek their sign-off of market assessments.

The Markets & Suppliers team may also proactively approach departments on a case-by-case basis to confirm that appropriate market management is taking place.

The sections on ‘How to monitor market health’ and ‘How to promote healthy markets’ below provide guidance to assist those that are undertaking market management activities.

### 2.3. When does this apply?

Market management activity should take place in the ‘Preparation and Planning’ phase of the commercial lifecycle and also during contract implementation as shown in Figure 1 below.

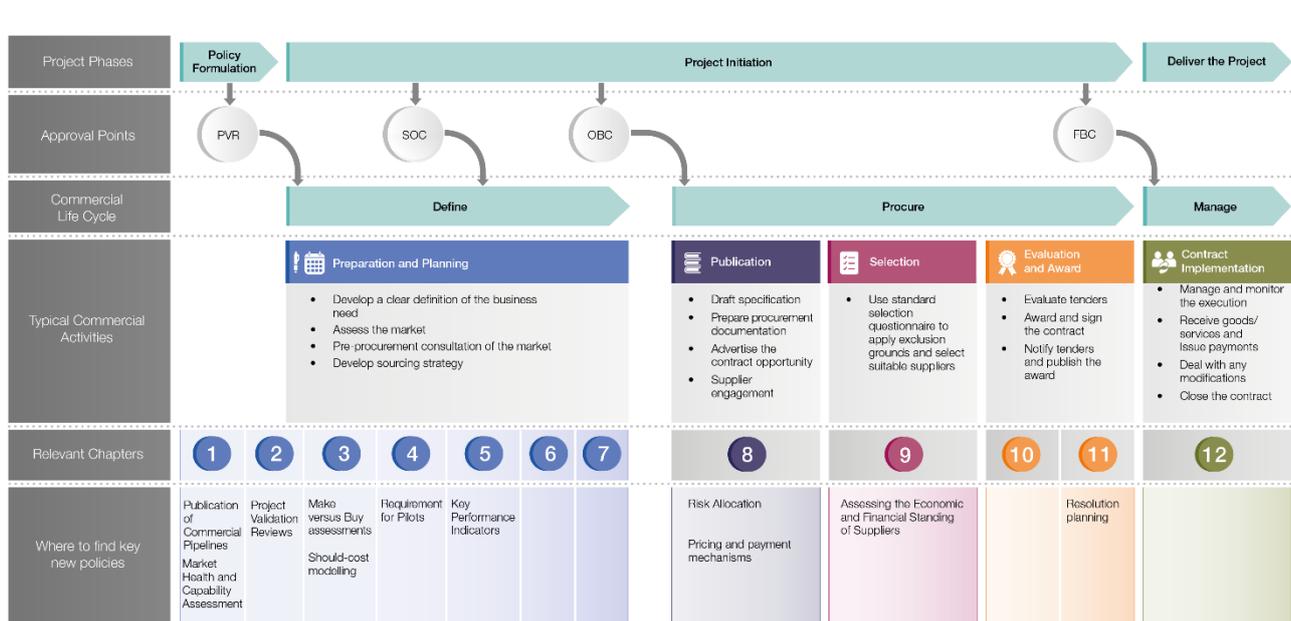


Figure 1. Commercial Lifecycle

In a repeat contracting scenario, a new market assessment will naturally be undertaken as one contracting cycle nears its end, as part of the process of developing the commercial strategy for the next contracting round.

Commercial staff should also monitor markets and update market assessments where important developments have taken place, as part of their ongoing contract management and monitoring activity.

Mid-contract updates to market assessments are more likely to be appropriate where several of the criteria in the previous paragraph apply. In addition, mid-contract updates are likely to be useful where government has levers available to respond to potential weaknesses that may be identified. An example would be if a contract break-clause was approaching.

## 2.4. Which organisations have a role?

The allocation of roles and responsibilities across organisations can be summarised as follows:

- **Accountability for market management:** each department will be accountable for ensuring that market management policy is complied with for the outsourcing markets that it buys from. The exception is that CCS will have accountability for all common markets for which CCS has a framework agreement.
- **Responsibility for market monitoring:** the department with the greatest interest in a market (the 'lead department') will generally be responsible for monitoring it and producing market assessments. CCS will have this responsibility for common markets where it has a framework agreement.
- **Responsibility for promoting market health:** each department will be responsible for acting to promote market health in the outsourcing markets that it buys from. CCS will have this responsibility for common markets where it has a framework agreement.
- **Advice and data to support market management:** The Cabinet Office's Markets and Suppliers team ([marketsandsuppliers@cabinetoffice.gov.uk](mailto:marketsandsuppliers@cabinetoffice.gov.uk)) will be the primary source of expert advice and data to assist departments that are undertaking market monitoring and are seeking to promote market health. Departments can also seek expert advice from the Competition and Markets Authority ([advocacy@cma.gov.uk](mailto:advocacy@cma.gov.uk)), in relation to larger markets and more complex or substantial competition issues. Finally, departments may seek external support, for example from economic consultancies.

The sections on 'How to monitor market health' and 'How to promote healthy markets' below set out roles and responsibilities in more detail and 'Appendix I – Roles and responsibilities' provides a summary table.

## 3. How to monitor market health

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### 3.1. Background

Market health is about both the buyer side and the supplier side of a market. In simple terms, markets are healthy when buyers are clear about their requirements, and can select and switch to best value for money suppliers, and when there is an adequate number of suppliers that are actively competing to offer what buyers want.

When these conditions are present, suppliers must make attractive bids in order to win contracts, and those that win contracts must work hard to deliver value for money, or risk buyers taking their business elsewhere.

### 3.2. Principles

Subject to the criteria in Table 1, under the market management policy, monitoring market health means:

- as a minimum, departments must ensure that a market assessment is in place early in the process of developing a commercial strategy; and
- departments must monitor the market (and if appropriate update the market assessment) during the life of a contract.

Ideally government should have a single, joined-up perspective on the markets that it buys from. The department with the greatest interest in a market (the 'lead department') will generally be responsible for monitoring it and producing market assessments. Other departments with an interest in the market should contribute to, and make use of, the market assessments produced by the lead department. Departments' commercial directors should agree upon a lead department for each cross-government market.

CCS will have market monitoring responsibility for common markets where it has a framework agreement.

Within departments, commercial staff will play a lead role in producing market assessments and in considering how commercial strategy and contract design can be adapted to address potential market weaknesses. They will ensure that this analysis and thinking is reflected in the development of commercial strategies and in the contract design process.

Commercial staff should draw on the expertise of other professions. Economists with competition expertise working in the same department are likely to be well-placed to assist with market assessments.

The Cabinet Office's Markets and Suppliers team will be a source of advice and data to support departmental commercial staff that are leading on market management.

### 3.3. Guidance on market assessments

In order to produce a market assessment, commercial staff should first identify a sensible market definition that can serve as a 'lens' or frame of reference for the subsequent analysis.

In economic terms, a market can be defined as a collection of products or services that are provided in a particular geographic area (or to particular customers) and that are connected by competition.

This means that, where two services are highly similar, to the point where buyers and/or suppliers could easily substitute between them, then they are likely to be part of the same market. It then makes sense to include both of these services within the scope of a market assessment. If a third service has some similar characteristics, but buyers would not consider it to be an adequate substitute, even if available at a lower price, then it is unlikely to be part of the same market. That service should not generally be included within the scope of the market assessment.

In the context of government outsourcing, government will often be the main buyer in a market. Therefore, in this context, **the market can generally be thought of as the services that government wants to buy and the geographic area in which suppliers/buyers are based**<sup>4</sup>.

The idea of the market assessment is to use a range of evidence to reach an overall view of market health and to identify any areas of potential weakness, so that appropriate action can be taken to respond to these (see Section 4 below on 'How to promote healthy markets').

The table below sets out the key questions that should generally be addressed within market assessments, as well as some sub-questions and types of evidence that can assist with this exercise<sup>5</sup>.

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<sup>4</sup> For more information on formal market definition, see the [OFT's Market Definition framework](#).

<sup>5</sup> The NAO has also produced guidance on market management; see area 11 of its [Good Practice Contract Management Framework](#) and Section 3 of its [Commercial Contract Management: Insights and Emerging Best Practice](#) document. The OECD and EU have also produced guidance on Market Analysis and how to engage with suppliers, through their joint initiative SIGMA; see [SIGMA: Market Analysis, Preliminary Market Consultations, and Prior Involvement of Candidates/Tenderers](#).

### 3.4. Contents of a market assessment

Topic and key questions	Sub-questions	Useful evidence/tools
<i>Market overview</i>		
<ul style="list-style-type: none"> <li>What are government's needs and what will it be buying?</li> </ul>	<ul style="list-style-type: none"> <li>Is this the first time the service is being outsourced?</li> <li>What is the value and complexity of these goods or services?</li> <li>Which departments will be buying these?</li> <li>What is government's current/intended commercial strategy?</li> </ul>	<ul style="list-style-type: none"> <li>Liaise with other departments procuring the goods/services to identify costs/revenue figures for past/current/planned procurements</li> <li>Commercial strategy documents</li> </ul>
<ul style="list-style-type: none"> <li>What are the key market drivers/trends with a bearing on market health?</li> </ul>	<ul style="list-style-type: none"> <li>How mature is the market?</li> <li>Is government a market-maker? Does it / will it account for a large part of the demand for these goods/services?</li> <li>What impact is technology, regulation, policy, politics etc. having on market health?</li> <li>How is this expected to evolve?</li> </ul>	<ul style="list-style-type: none"> <li>Off-the-shelf industry reports</li> <li>CCS Commercial Intelligence Market Reports</li> <li>Revenue and contract award data from past/existing contracts</li> <li>PESTLE analysis</li> </ul>
<i>Market features</i>		
<ul style="list-style-type: none"> <li>Supply-side assessment: who are the suppliers and how do they compete?</li> </ul>	<ul style="list-style-type: none"> <li>Which suppliers are/will be active in this market? (including public, private and others)</li> <li>What capacity and capabilities do they have relative to government's requirements?</li> <li>What market shares do they currently have?</li> <li>How concentrated is the market? (<i>see market share and HHI indicators in table below</i>)</li> <li>How closely do/will these suppliers compete?</li> <li>What has the trend been over time?</li> <li>Which suppliers could enter/exit the market?</li> <li>Is there any sign (or risk) of anti-competitive behaviour, such as bid rigging between suppliers?</li> </ul>	<ul style="list-style-type: none"> <li>Supplier identities from government databases</li> <li>Supplier assessments produced by Cabinet Office Markets and Suppliers team</li> <li>SWOT analysis</li> <li>Evaluations of past procurements</li> <li>Revenue and contract award data from existing contracts</li> <li>Market engagement exercises</li> <li>Case studies of past entry/exit in this market or similar markets</li> <li>For bid-rigging, consider CMA tools and guidance<sup>6</sup></li> </ul>

<sup>6</sup> See for example: [screening for cartels: tool for procurers](#); [60-second bid-rigging summary and e-learning module for procurers](#).

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<ul style="list-style-type: none"> <li>• Buyer-side assessment: how easy is it to identify and switch to best value for money suppliers?</li> </ul>	<ul style="list-style-type: none"> <li>• Does government have clear objectives?</li> <li>• Does government have good information on suppliers? And the ability to select best value for money offers?</li> <li>• Are incentives appropriate and well-aligned between buyers, suppliers and service users?</li> <li>• What are the barriers/costs to government switching between suppliers? (<i>see switching cost indicator in the table below</i>)</li> </ul>	<ul style="list-style-type: none"> <li>• Evaluations of past procurements</li> <li>• Capability assessments produced internally by departments, or by the NAO, parliamentary committees etc</li> </ul>
<ul style="list-style-type: none"> <li>• Contestability: how easy is entry, expansion and exit in this market? how strong are incumbency advantages?</li> </ul>	<ul style="list-style-type: none"> <li>• What are the barriers to suppliers entering and expanding? What about barriers to exit?</li> <li>• How strong is incumbency advantage in this market?</li> <li>• If an incumbent raised prices, reduced quality or left the market, what bargaining power would government have? Could alternative public or private suppliers step-in in a timely fashion?</li> <li>• What entry trends have we observed over time?</li> </ul>	<ul style="list-style-type: none"> <li>• Evaluations of past procurements</li> <li>• Market engagement exercises</li> <li>• Case studies of past entry/exit in this market or similar markets</li> <li>• Porter's five forces analysis</li> </ul>
<p><i>Market outcomes</i></p>		
<ul style="list-style-type: none"> <li>• Is the market delivering value-for-money?</li> </ul>	<ul style="list-style-type: none"> <li>• What are the levels and trends in price, quality, innovation and choice? (<i>see market outcome indicators in table below</i>)</li> <li>• What are the drivers contributing to these trends? For example, changes in government requirements, changes in the competitive environment, changes in input costs</li> <li>• Are buyers setting the right incentives for suppliers?</li> </ul>	<ul style="list-style-type: none"> <li>• Contract-level KPI data</li> <li>• Employee feedback on providers within the market</li> <li>• Any Value for Money assessments produced by departments, the NAO, parliamentary committees etc</li> <li>• Evaluations of past procurements</li> </ul>
<p><i>Conclusions and action plan</i></p>		
<ul style="list-style-type: none"> <li>• How healthy is the market overall?</li> </ul>	<ul style="list-style-type: none"> <li>• Is there effective competition between suppliers?</li> <li>• Are entry, expansion and exit barriers low and are markets contestable?</li> <li>• Are switching costs low?</li> <li>• How strong is any incumbency advantage?</li> <li>• Are there any other areas of market weakness?</li> <li>• Is the market supporting good value-for-money overall?</li> <li>• Overall, what are the key areas of market weakness?</li> <li>• Does trend analysis suggest that market health is improving or deteriorating?</li> </ul>	<ul style="list-style-type: none"> <li>• Results of the assessments above</li> </ul>
<ul style="list-style-type: none"> <li>• How should government respond?</li> </ul>	<ul style="list-style-type: none"> <li>• What actions should government consider taking to address market weaknesses?</li> <li>• What further work will government do to explore these options?</li> </ul>	<ul style="list-style-type: none"> <li>• <i>See section 4 of this document</i></li> </ul>

		<ul style="list-style-type: none"> <li>• Government Commercial Operating Standards<sup>7</sup></li> <li>• Office of Fair Trading guidance on the links between procurement/commissioning and competition<sup>8</sup></li> </ul>
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### 3.5. Indicators to use in a market assessment

The table below describes some indicators that can be used within a market assessment. The headline indicators are easier to generate and should generally be used. The additional indicators may be appropriate for more in-depth assessments (see the criteria in Section 2.2 above). Further guidance on calculating and using indicators is provided in ‘Appendix II – Further guidance on market indicators’<sup>9</sup>.

Indicator	Guidance	Potential cause for concern if...
<i>Market features: headline indicators</i>		
Failed bidding rounds	<ul style="list-style-type: none"> <li>• Identify the number of recent bidding rounds for the services where no acceptable bids were received</li> <li>• Tip: include bidding rounds undertaken by other departments</li> </ul>	<ul style="list-style-type: none"> <li>• One or more failed rounds identified</li> </ul>
Bids received	<ul style="list-style-type: none"> <li>• Plot the trend in the number of bids received</li> <li>• Tip: indicator is more informative if multiple similar bidding rounds have taken place</li> </ul>	<ul style="list-style-type: none"> <li>• Very few bids received</li> <li>• Declining trend in number of bids</li> </ul>

<sup>7</sup> See the [Government Commercial Operating Standards](#).

<sup>8</sup> See for example the [OFT’s government in market framework](#) and the [OFT’s report into public sector commissioning](#).

<sup>9</sup> See also the [Competition Commission’s Market Investigation Guidelines \(CC3\)](#) for more information on these sorts of indicators.

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Indicator	Guidance	Potential cause for concern if...
Market shares	<ul style="list-style-type: none"> <li>Plot the trend in the market shares of the main suppliers (typically the revenue earned by a supplier per annum, divided by the total revenues earned by suppliers in that market per annum)</li> <li>Consider also plotting the trend in the C3 ratio (the sum of the market shares of the three largest suppliers)</li> <li>Tip: these indicators are more informative in markets where government buys through multiple contracts at once</li> <li>Tip: if total market size is unknown (data on revenues earned from non-government buyers may not be available), then shares of supply to government should be calculated</li> </ul>	<ul style="list-style-type: none"> <li>Market shares of largest suppliers are high and stable or increasing</li> <li><math>90 \leq C3 \leq 100\%</math></li> </ul>
Win ratios	<ul style="list-style-type: none"> <li>Plot the win ratios of the main suppliers over time (the number or value of contracts won by a supplier over a period of time, divided by the number or value of contracts that government has awarded for those services)</li> <li>Tip: this indicator is useful in bidding markets, where government re-tenders one or several contracts on a regular basis</li> <li>Tip: it may also be useful to calculate switching rates to see how often a particular contract (or type of contract) changes hands</li> </ul>	<ul style="list-style-type: none"> <li>Win ratios of largest suppliers are high and stable or increasing</li> <li>The vast majority of contract awards go to three or fewer suppliers</li> </ul>
Switching costs	<ul style="list-style-type: none"> <li>Attempt to quantify the costs that government would incur as a result of switching suppliers (either now or in future)</li> </ul>	<ul style="list-style-type: none"> <li>Switching costs are substantial relative to contract value</li> </ul>
<i>Market features: additional indicators</i>		
Herfindahl-Hirschman Index (HHI)	<ul style="list-style-type: none"> <li>Calculate the sum of the squared market shares of suppliers in the market (market shares will generally be based on revenues)</li> <li>Tip: this indicator requires all market shares to be known</li> </ul>	<ul style="list-style-type: none"> <li>HHI score from 1000-10,000</li> </ul>

It is not possible to reach a conclusion on market health based on any one indicator alone. For example, high and increasing market shares (or win ratios) would generally indicate that competition may be weak and should be a prompt to look closely at the market and consider the reasons for these results. However, if cost and quality indicators suggest that the market is delivering good outcomes, and if the market has low barriers to entry, then (despite high market shares) there may in fact be intense competition between a small number of firms.

## 4. How to promote healthy markets

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### 4.1. Background

Those designing commercial strategies and contracts are typically subject to multiple objectives and constraints.

Considerations such as short-term affordability and limitations to departments' contract management capacity may point towards an approach of offering fewer, larger contracts in an attempt to reduce upfront costs and departmental overheads.

However, these approaches can lead to false economies and lower value for money over time. For example, these strategies may result in fewer bids, weaker competition and stronger incumbency positions for a handful of suppliers – either in the initial bidding process or in future contracting rounds.

Therefore, it is important to consider how commercial strategies and contracts can be adapted so that they have a positive impact on market health and value for money.

### 4.2. Principles

Under the market management policy, **promoting healthy markets** means:

- early in the commercial strategy development process, departments should consider the different steps that can be taken to promote healthy, competitive markets and should document this exercise;
- this exercise should build on the results of the market assessment and should seek to rectify any weaknesses.

The department with the greatest interest in a market (the lead department) will generally have overall accountability for promoting market health.

However, each department will be responsible for acting to promote market health in the outsourcing markets that they buy from.

CCS will have this responsibility for common markets where it has a framework agreement.

Within departments, commercial staff will play a lead role in considering how commercial strategy and contract design can be adapted to address potential market weaknesses. They

will ensure that this analysis and thinking is reflected in the development of commercial strategies and in the contract design process.

Commercial staff should draw on the expertise of other professions. Economists with competition expertise that work in the same department are likely to be well-placed to assist.

The Cabinet Office's Markets and Suppliers team can provide support. Advice can also be sought from the CMA in relation to larger markets and more complex or substantial competition issues.

### 4.3. Guidance on promoting market health

Government buyers can promote competition and make a positive contribution towards market health where they:

- are clear about their requirements and switch between suppliers in a timely and effective manner;
- design bidding processes and procedures that keep entry barriers low and maintain a level playing field between suppliers;
- look out for, and minimise the risk of, anti-competitive behaviour, for example bid-rigging;
- design contracts that do not create excessive barriers to step-in during a contract, or create an unassailable advantage for incumbents in future contracting rounds; and
- plan for medium and long-term market health and do not excessively focus on the short term.

The table below provides further detail on the steps that should be considered. These are organised by theme, however many of these steps also have wider applicability outside of the specified theme.

## 4.4. Steps to promote market health

Theme	Questions to consider	If the answer is 'no', consider taking the following steps...
Addressing Barriers to Entry	Do bid processes and procedures ensure a level playing field between suppliers?	<ul style="list-style-type: none"> <li>• Streamline complex and burdensome procurement policies and processes.</li> <li>• Consider the ability of smaller suppliers to take part in large procurement exercises, for example those carried out under joint purchasing by multiple government departments.</li> <li>• Consider encouraging Joint Ventures between SMEs. If this is used, brokerage support could also be offered.</li> <li>• Use Market Engagement to understand and tackle barriers to entry. Further guidance on Market Engagement can be found in Chapters 1 and 8 of the Outsourcing Playbook. This could include:               <ul style="list-style-type: none"> <li>○ Providing training or guidance to SMEs on how to submit compliant bids.</li> <li>○ Talking to existing and potential suppliers to understand their capacity and capability.</li> </ul> </li> <li>• In the absence of significant economies of scale and scope, consider disaggregating contracts for different services and limiting the duration of contracts, to encourage greater supplier participation and reduce switching costs.</li> <li>• When designing, specifying or encouraging new delivery models, ensure that suppliers are still incentivised to innovate and that sub-contractors can negotiate contractual terms with prime contractors on an equal footing.</li> <li>• Ensure outcome-based contracts do not place excessive risk with suppliers or dissuade new/smaller suppliers from entering the market.</li> <li>• Where demand is unpredictable and can lead to a greater risk transfer, consider rewarding providers for actual volume of work they do rather than a fixed fee payment, using pay caps and minimum income guarantees.</li> <li>• Design framework contracts to allow additional firms to be added during the life of the framework, if suppliers can demonstrate they meet the same objective criteria as existing suppliers.</li> <li>• Scrutinise bids and compare them against Should Cost models (further guidance on 'should cost' models can be found in Playbook One, Chapter 5: 'Preparing to go to market'). Accepting unsustainably low bids can lead to worse Value for Money.</li> <li>• Consider keeping certain assets and expertise in-house and only contracting out those aspects of service provision where there is scope for effective competition.</li> </ul>
	Does joint purchasing ensure a level playing field between suppliers?	
	Do sufficient economies of scale/scope exist to justify aggregated contracts and long contract durations?	
	Does the risk allocation between public and private sector ensure that a range of suppliers are able to compete?	
	Does the use of framework contracts allow for the entry of new suppliers if they meet the same objective criteria as existing suppliers?	
	Do we understand the true cost of supply?	
	Are the capital requirements involved in supplying the market reasonable?	
Addressing Barriers to Switching	Do buyers switch effectively and swiftly between rival suppliers and within appropriate timescales?	<ul style="list-style-type: none"> <li>• Take steps to promote quick and effective switching to more efficient suppliers, whilst not dissuading innovation or efficient investment by incumbent suppliers. For example:               <ul style="list-style-type: none"> <li>○ Consider contractually requiring incumbents to facilitate switching at the point of contract expiry.</li> <li>○ Where services involve bespoke systems or technology, ensure that the allocation of intellectual property rights maintain our ability to switch to other suppliers in future.</li> </ul> </li> </ul>

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	<p>Do requirements to ensure continuity of supplier ensure proportionate costs across existing and potential suppliers?</p>	<ul style="list-style-type: none"> <li>• Any requirements on potential suppliers to ensure a continuity of supply should take account of market conditions and their ability to make contingency arrangements in the event of failure or market exit. See the Guidance Note on <a href="#">Resolution Planning</a> for more information.</li> <li>• When comparing public sector in-house options with other suppliers, the cost of failure by public and private sector suppliers should be accounted for.</li> </ul>
<p>Creating appropriate and aligned incentives</p>	<p>Do multiple suppliers impose competitive constraints on one another? Are buyers encouraging the right level of risk, and focus on the medium/long term as well as the short term?</p>	<ul style="list-style-type: none"> <li>• Design commercial strategies and contracts in a way that incentivises suppliers to deliver value for money post contract award. For example, dividing up contracts can help maintain competitive tension during the term of contracts. Also consider using ongoing rating systems, outcome-based contracts, contracts where high performers are allocated increasing volumes over time, or greater benchmarking transparency.</li> <li>• Clearly articulate strategic guiding objectives and ensure these are understood by commissioners, procurers and suppliers. Check that incentives can be appropriately aligned to achieve these objectives.</li> <li>• Develop better performance monitoring information.</li> <li>• In markets where KPIs take a long time to crystallise, consider using interim milestones.</li> </ul>

# Appendix I – Roles and responsibilities

Scenario	Examples	Market management				
		Accountable	Market monitoring		Promoting market health	
			Responsible	Supports	Responsible	Supports
<b>(1) Markets with CCS framework:</b> departments buy the same goods and services; there is a CCS framework contract.	Facilities management, communications services	CCS <ul style="list-style-type: none"> <li>ensures that government monitors the market and acts to promote market health</li> </ul>	CCS <ul style="list-style-type: none"> <li>produces market assessments</li> <li>disseminates to departments</li> </ul>	Departments <ul style="list-style-type: none"> <li>share contract data and market intelligence with CCS</li> </ul> CO <ul style="list-style-type: none"> <li>provides advice/support/data to CCS</li> </ul>	CCS <ul style="list-style-type: none"> <li>ensures that framework promotes market health</li> </ul>	Departments <ul style="list-style-type: none"> <li>use commercial strategies to promote market health</li> </ul> CO <ul style="list-style-type: none"> <li>provides advice and support to CCS</li> </ul>
<b>(2) Other common markets:</b> several departments buy the same goods and services; there is no CCS framework contract.	Electronic tagging services	Departments <ul style="list-style-type: none"> <li>ensure that government monitors the market and acts to promote market health</li> </ul>	Departments <ul style="list-style-type: none"> <li>may produce market assessments (or sub-contract to CO or a lead department)</li> <li>disseminate to other departments</li> </ul> CO <ul style="list-style-type: none"> <li>may produce market assessments</li> </ul>	Departments <ul style="list-style-type: none"> <li>share contract data and market intelligence with each other / CO</li> </ul> CO <ul style="list-style-type: none"> <li>may aggregate and process departmental data</li> <li>provides advice/support/data to lead department</li> </ul>	Departments <ul style="list-style-type: none"> <li>use commercial strategies to promote market health</li> </ul>	CO <ul style="list-style-type: none"> <li>provides advice and support to departments</li> </ul>

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Scenario	Examples	Market management				
		Accountable	Market monitoring		Promoting market health	
			Responsible	Supports	Responsible	Supports
<b>(3) Non-common markets:</b> one department accounts for all or the vast majority of government purchases; there is no CCS framework	Prison services, clinical waste processing	Department <ul style="list-style-type: none"> <li>ensures that government monitors the market and acts to promote market health</li> </ul>	Department <ul style="list-style-type: none"> <li>produces market assessments</li> </ul>	CO <ul style="list-style-type: none"> <li>provides advice, support and data to department</li> </ul>	Department <ul style="list-style-type: none"> <li>uses commercial strategies to promote market health</li> </ul>	CO <ul style="list-style-type: none"> <li>provides advice and support to department</li> </ul>

Note: Departments can also seek expert advice from the Competition and Markets Authority ([advocacy@cma.gov.uk](mailto:advocacy@cma.gov.uk)), in relation to larger markets and more complex or substantial competition issues.

## Appendix II – Further guidance on market indicators

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This appendix presents a hypothetical example scenario in which the market indicators are calculated as part of a market assessment.

It demonstrates how to calculate the indicators and how these can feed into a wider assessment of market health. It is important to remember that market indicators only form part of a market assessment; a wider range of evidence will be needed in order to reach overall conclusions about market health. The wider questions and evidence that market assessments may cover are contained in the 'Contents of a market assessment' table in the Market Management guidance.

### Background

The Department for Medicine has outsourced secure delivery services for several years. A key contract is due to expire in 12 months and so the department reviewing its outsourcing strategy for these services and carrying out a market assessment.

- The Department for Defence also procures secure delivery services, so the tendering rounds run by this department are relevant for the Department for Medicine's market assessment.
- The Department for Medicine currently uses Supplier 1.
- The Department for Defence currently uses a mix of Supplier 2 and Supplier 3.
- Both departments retender for secure delivery services on a yearly basis.
- All three suppliers offer some wider services besides secure delivery services. These wider services are not purchased by the departments and therefore data relating to these are not relevant to the market assessment.

### Calculation of market indicators for use in a market assessment

The departments agree that the Department for Defence should lead on the calculation of market indicators for use in a market assessment.

The departments both have three years of comparable bidding data. The outsourced service has not been significantly affected by technological trends in the last three years. Therefore, a time period of three years is used to generate the market indicators.

## Market structure and contestability

The department starts by considering the **failed bidding rounds indicator**. Neither department have experienced any **failed bidding rounds** (i.e. tendering rounds with no bidders) so this indicator does not indicate any market health issues.

The department next considers the **bids received indicator**. Both departments have run three bidding rounds in the past three years. The number of **bids received** in each bidding round is set out in the table below.

Number of bids received:

	Department for Medicine	Department for Defence
Year 1	6	7
Year 2	6	7
Year 3	6	7

The number of bids received by each department has remained relatively stable at 6-7 bids per tender over the previous three years. Therefore the bids received indicator suggests the amount of supplier interest in the market is neither growing nor shrinking overall.

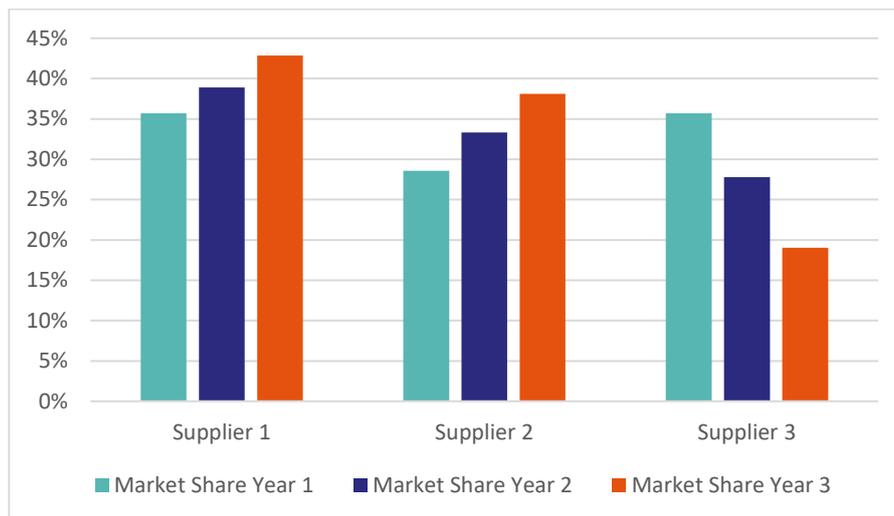
The department next considers **market share** indicators. As noted previously, government uses three suppliers in total. This is relatively low, but in itself is inconclusive. The table below shows the total spend by each department with each of the three suppliers for secure delivery services. To calculate these, the Department for Medicine had to obtain information from the Department for Defence’s previous tendering exercises.

**Market shares** were calculated by dividing the total spend on secure delivery services with a supplier by the total spend by government on those services for each year. Importantly, the spend below only relates to relevant services that are in-scope of the market assessment.

Suppliers’ revenues:

	Revenue Y1	Revenue Y2	Revenue Y3	Market Share Year 1	Market Share Year 2	Market Share Year 3
Supplier 1	£5m	£7m	£9m	36%	39%	43%
Supplier 2	£4m	£6m	£8m	29%	33%	38%
Supplier 3	£5m	£5m	£4m	36%	28%	19%
Total gov spend	£14m	£18m	£21m	100%	100%	100%

### Market shares:



This analysis showed that the market shares of the largest suppliers (Supplier 1 and Supplier 2) are high and increasing. Supplier 3's market share has decreased.

The market shares were also used to calculate a **C3** ratio and the **HHI**.

The C3 is calculated by summing the market shares of the three largest suppliers. As there are only three suppliers in this market, the C3 was 100%.

**Tip:** The C3 indicator does not indicate the relative size of the three largest suppliers. A market where the three largest suppliers have market shares of 80%, 10% and 10% would have the same C3 as a market where the three largest suppliers all have a market share of 30%. The first case is likely to be more concerning.

HHI is calculated by squaring the market shares of all suppliers in the market and summing these together.

$$48^2 + 35^2 + 17^2 = 3,818$$

This is above the threshold of 1,000 which generally means that there is a level of concentration in the market which could be a cause for concern. However, the department decides to gather further evidence, including on market outcomes, before drawing any conclusions.

**Tip:** Even where concentration indicators (such as HHI) show that a market is concentrated, the market may not be subject to weak competition. Suppliers in a highly concentrated market could still face intense competition if barriers to entry and exit are very low, so that contracts can easily change hands.

Win ratios are also calculated for each of the suppliers across the two departments tendering exercises. These can be found in the table below.

Win ratios:

	Bid	Won	Win Ratio
Supplier 1	6	3	50%
Supplier 2	6	3	50%
Supplier 3	6	3	50%

Win ratios are relatively high for each of the three suppliers.

**Tip:** Win ratios are helpful in shedding light on the strength of suppliers over time. This can be useful in bidding markets with one or more of the following characteristics:

- tenders take place infrequently,
- the value of individual contracts is significant from the perspective of the supplier, or
- there tends to be a single successful bidder (ie winner takes all),

In these situations, a snap shot of market shares based on revenue will not always provide a good indication of the strength of a supplier.

For example, if a supplier had recently won a very large contract and had a revenue-based market share of over 90%, but had a low win ratio based on the past five tenders, this would indicate that it does not have as much strength in the market as

## Market outcomes

The contracts used by the departments each contain a 95% success rate target for on-time deliveries. The department decides that this KPI can be used as a **market performance** indicator.

The suppliers' success rates for on-time delivery are set out the below. These indicate that Suppliers 1 and 2 performed well in Years 1 and 2, however their performance declined in

Year 3 and they are no longer reaching their target. Supplier 3 has consistently failed to meet the 95% target.

The department observes that:

- Work is flowing from the poorest performing provider (Supplier 3) to suppliers that are performing better.
- However overall market performance is declining.

KPI performance:

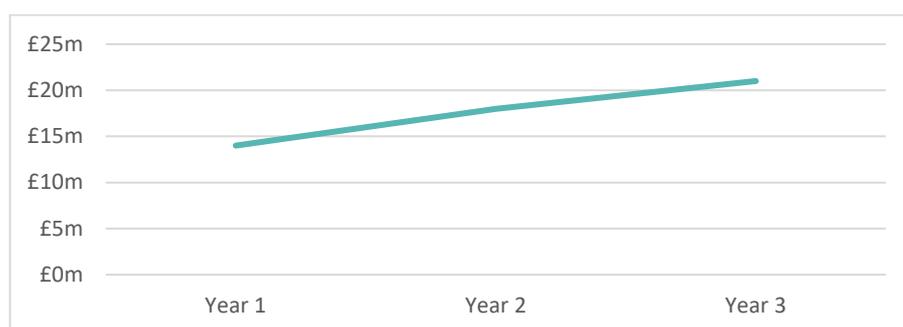
	Year 1	Year 2	Year 3
Supplier 1	96%	95%	84%
Supplier 2	95%	95%	73%
Supplier 3	94%	83%	60%

As part of its market assessment, the department plans to repeat this exercise for other KPIs set out in its contracts, and also bring in other more qualitative evidence on other aspects of performance such as levels of innovation.

Next the department assesses the overall cost of these contracts.

The total spend of both departments is displayed on the graph below, representing the cost to taxpayers.

Total contract cost:



Total contract cost has increased across the three years. The department observes that:

- Based on available indicators, market performance has fallen overall, so the rising costs do not appear to be explained by higher quality.
- For both departments, demand has stayed constant, so the rising costs do not appear to be explained by increases in demand.

Profit indicators are not calculated, as the suppliers do not report profits in a way that allows these to be segmented by services.

## Recap of market indicators and next steps

The indicators on market structure and contestability suggest:

- Departments appear to be receiving a reasonable number of bids on a yearly basis.
- However, only three suppliers actually hold contracts and the market has become concentrated in favour of two of those.

The indicators on market performance show:

- The quality of service delivered by the market appears to be declining.
- Yet at the same time, costs to government are rising.

The indicators calculated so far suggest that there may be weak competition in the market.

To identify a fuller picture of competition and market health, the Department for Medicine decides to undertake some wider market assessment work, including a buyer-side analysis and some supplier-side market engagement work. Amongst other things, this will consider:

- Why other bidders have been unsuccessful.
- Whether the departments face significant barriers to switching providers.
- Whether incumbent suppliers have a strong incumbency advantage.