

Turning the tide Opportunities for public-sector organisations in an economic downturn



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About this research

In preparation for this report, Deloitte LLP consulted a number of its clients in government departments and local authorities. The work also draws on insight provided by senior public sector partners from across the firm.

Foreword

The crisis across financial markets, a downturn in the property sector, and energy and commodities price volatility made 2008 a challenging year. Across the United Kingdom's economy, citizens and businesses are now preparing for a difficult and uncertain period.

This may lead to fresh discussions about the role of 'big' government, as the State reviews its responsibilities as a commissioner and a direct service provider. With a likely squeeze on public expenditure, however, government will not be able to 'do' everything. Public-sector leaders will need to find ways to manage these challenges effectively.

The Government's decision to invest in British banks and bring forward a £3 billion package of measures to improve consumer and business confidence have been analysed extensively. The purpose of this report is not to add to that commentary, but to signpost the likely impact of an economic downturn on the 'business of government' and how government organisations must respond to the changing climate. Macroeconomic intervention from the top of government is important, but equally significant will be the ability of the wider public sector to assess the financial health of its capital programmes, its critical suppliers and itself.

Beyond these immediate requirements, however, the downturn also crystallises two broader challenges. First, public-sector organisations need to consider how to manage their businesses in an environment that introduces new tensions between the layers of government as well as between the public sector and its private partners.

Second, changing policy requirements and citizen behaviour may drive demand for new capabilities, and shape the need for innovation and restructuring in order to meet new priorities.

This report, produced by Deloitte in consultation with its public-sector clients, sets out a series of measures public organisations could take to drive these tactical and strategic changes. While economic change represents a threat, it also provides renewed motivation and opportunities for public-sector leaders to transform their businesses in fundamental ways. Public-sector leaders need to consider the downturn in this way and seize the opportunities it presents.



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Executive summary



The economic downturn will affect the finances, operations and policymaking of public-sector organisations in a number of ways. To respond effectively, public-sector leaders must take action on two fronts.

First, they need to take a series of tactical steps to manage risks and threats that arise as an immediate consequence of the crisis across financial services. Second, public-sector organisations need to consider a group of more fundamental or strategic reforms to improve the efficiency and effectiveness of their businesses, and to adapt to the changing requirements of citizens.

The next five years will represent a crossroads as the downturn either drives radical transformation across the business of government or, unchecked, the tension between expenditure reduction and increased citizen expectations results in critical shortfalls in public-service quality. While government leaders need to consider the strategic action required to meet this challenge, they also need to anticipate and prepare for further shocks. This can be achieved by embracing new approaches to risk management, and by taking preventative action where appropriate to minimise the impact on critical business areas.

As part of their tactical responses, government organisations should make an immediate financial assessment of their own businesses and their partners, the suitability of existing risk-management processes, and likely changes to revenue streams as customer behaviour changes. This work could be supported by a series of measures to improve cash management and collection processes. It could also be aided by a near-term programme to explore cost reduction opportunities within existing operational structures and processes.

In a period of crisis, however, the previously unthinkable can often become the 'least bad' option. Many organisations are now considering risks, not in terms of the overall likelihood of disaster, but in terms of the level of impact should one occur. This fundamentally different environment requires government organisations to take radical steps to emerge as leaner, more commercially savvy entities that respond to changing circumstances and citizen requirements, and deliver the business of government in more cost effective ways. Public-sector organisations can achieve this transformation if they:

Embrace innovation and rethink delivery models

In light of cost pressures and renewed levels of dependency among specific customer groups, government organisations need to encourage greater innovation across their businesses. They also need to review traditional service delivery models and achieve better quality and more cost effective public services by diversifying their delivery channels, utilising customer data more effectively and actively managing social enterprise markets.

Exploit the best from the private and third sectors

Government organisations now have an emerging role as a 'customer of least risk' with an 'AAA' credit rating. Public-sector managers need to exploit this status in ways that drive efficiency and maximise the benefit to their businesses. Opportunities to negotiate better deals with suppliers and to redesign contract models by making greater use of 'reward for delivery' will be important. However, government organisations also have a role to play in effectively managing public-sector markets in ways that encourage supplier activity and guard against market failure. Fostering an understanding of commercial drivers among private partners will be fundamental to success in this area.

Build new capabilities

Collectively, government organisations are more likely to navigate the downturn successfully if they are able to co-ordinate their responses, and consider 'whole market' approaches to social and economic problems. The downturn will also place renewed pressure on finance functions to manage large cost-optimisation programmes and forward planning. In addition, it will increase the need for improved commercial and procurement capabilities as change across public-sector markets takes effect. High-quality leadership and a core understanding of shifting customer requirements will continue to be vital capabilities for public-sector organisations going forward.

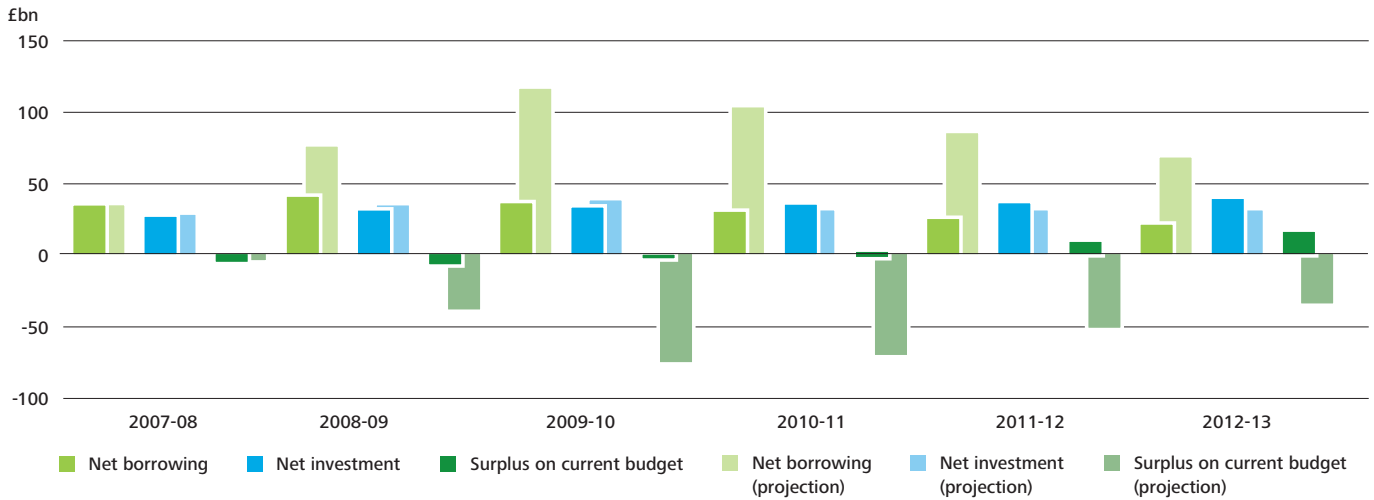
Embed permanent cost savings

Beyond the immediate effort to reduce operational costs within existing structures, there is an underlying requirement for government organisations to reduce their long-term cost base. To address this challenge, public-sector leaders may need to consider shared service transformation. They may also need to increase their use of collaboration and joint strategic partnerships across policy areas and regional boundaries, and make radical changes to traditional human capital management as organisations seek to lower notionally 'fixed' costs.

The economic downturn offers a chance for public-sector organisations to drive through changes they could not necessarily make in more prosperous times. But public-sector leaders cannot stand still and wait for change to envelop them. Using the downturn as a lever to invoke strategic reforms across a series of management areas is an opportunity leaders need to take now if they are to emerge from the downturn as first-class public-service delivery organisations.

Context: How public services are affected

Figure 1: Adjusted projections following the 2008 Pre-Budget Report



Source: HM Treasury, November 2008.

The disruption across financial markets during 2008 confirmed the importance of government as a safeguard to economic security.

Just as ten years of growth showcased the semi-autonomous power of global markets to drive economic prosperity, the period ahead may demonstrate the limits to that influence as the Government confronts economic and social problems that markets alone cannot meet.

Since the crisis, analysis has focused on recognisable economic indicators including consumer spending, the property market and unemployment. Yet the consequences for the public sector may also be significant. Despite the Government's decision to invest up to £50 billion in UK banks and bring forward £3 billion-worth of capital investment, acute challenges, such as changing customer behaviour and financial pressures, are likely to pervade the public sector over the next five years.

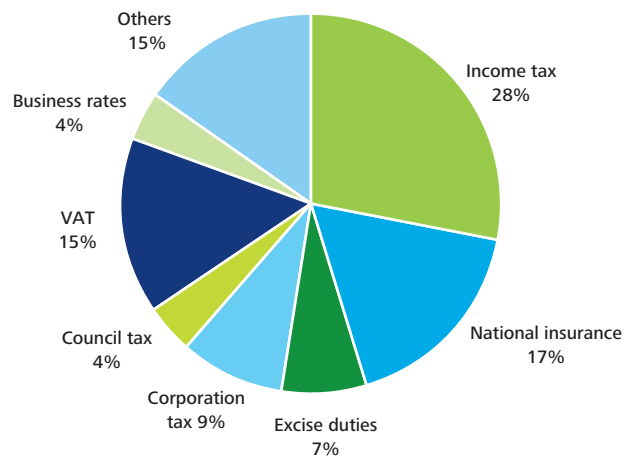
The clearest link between economic performance and public finances is tax receipts, which are projected to be around £575 billion over 2008-09. These represent the life blood of public-service revenue with around £265 billion coming from income tax and national insurance.² As employment and growth fall, receipts across each revenue stream, as shown in Figure 2, are affected. Net taxes and national insurance contributions are projected to fall by 3.3 per cent in the period 2009-10.³

The Exchequer has benefited from recent growth across both the financial services and property sectors, which accounted for half the increase in total receipts between 2002-03 and 2007-08.⁴ As part of an overall fall in receipts, stamp duty revenue is expected to fall by over 40 per cent in 2008-09, and business rates receipts are expected to be around £300 million below the Budget 2008 forecast.⁵

At local level, councils accrued £10.8 billion per annum (2006-07) from chargeable services, and 30 per cent of local authorities in England generate more revenue from charges than they do from council tax.⁶

Although central departments may limit their use of user charging models to products such as passport and driving licence applications, future policies on road pricing, social care or drug prescription charges may indicate a growth in central departments charging users for services. Greater use of co-funding models that involve the private sector in areas such as education and training, and regeneration may also emerge as a result of increasing cost pressure on government organisations. Further, the risk of market failure also increases as greater numbers of private-sector operators exit key markets such as healthcare, defence and specific projects such as the London 2012 Olympics.

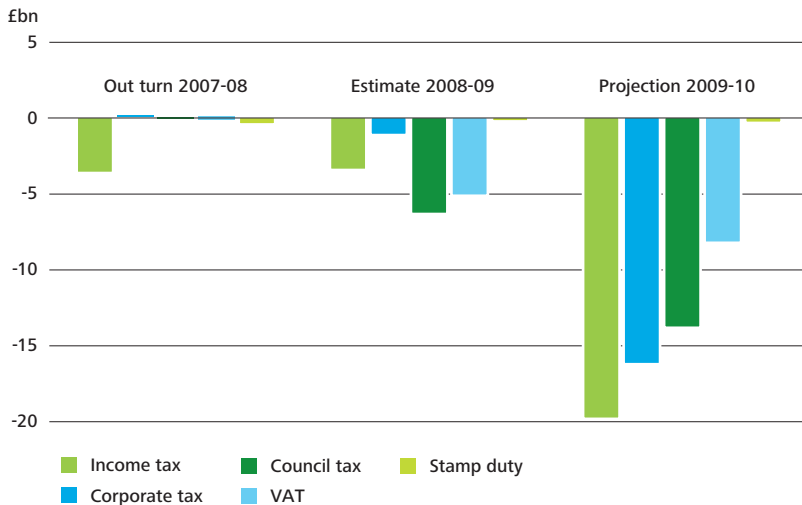
Figure 2: Government receipts by function 2008-09 (projections)



*Other receipts include capital taxes, stamp duties, vehicle excise duties, and some other tax and non-tax receipts including interest and dividends.

Source: HM Treasury, November 2008.

Figure 3: Reduced contributions against Budget 2008 expectations



Source: HM Treasury, November 2008.

Figure 3 illustrates how the downturn has led to write-downs in revenue expectations, with 2009-10 expected to witness the sharpest differentiation between earlier projections and current reality. As trading entities with balance sheets and large wage bills, government organisations are also vulnerable to macroeconomic change. Through inflationary increases, for example, the value of government funding to councils in England and Wales over the next three years is currently worth almost £500 million a year less than originally intended.⁷

Interest rate volatility can also affect government capacity to borrow, invest, manage arrears or engage in competitively-priced partnerships. In addition, it can cancel out any cost savings made through efficiency programmes. Although it is expected that inflation and interest rates are likely to be managed downwards over the next three years, the corrosive impact of recent volatility may continue to be felt across the next spending round.

As the Icelandic banking collapse illustrates, local authorities now face unprecedented risks across their treasury or cash management functions. In October 2008, the Financial Services Authority (FSA) reminded public organisations that institutional credit ratings only offer “an opinion of credit risk” and urged local authorities to look beyond credit ratings by “asking their own questions that relate to their own risk management and their own business”.⁸

Volatility in equity and commodities can affect public-sector liabilities such as pensions, as well as core social inclusion objectives like tackling fuel poverty. Increases in fuel and energy prices led to a £374 million rise in aggregated local authority energy bills over the last two years which, together with inflation, mean that central settlements for the next three years are now worth around £1.5 billion less than originally agreed.⁹

While not immediately catastrophic, a downward spiral of diminishing resources and increasing demand for services over the next five years could force public-sector organisations into a position of permanent fire-fighting. Alternatively, public-sector managers could use the new economic climate as a catalyst to bring forward strategic transformation by blending near-term tactical interventions with a wider programme of management and delivery reforms to break out of the cycle of remedial policymaking.

What's next? Anticipating future large shocks

The experience of the financial services crisis showed how private- and public-sector organisations were underprepared for system-wide shocks. Across the financial services, retail and construction sectors, markets are braced for the next big insolvency. Equivalent changes across the public sector might include the following:

Systemic failure across key public markets

As the economic downturn takes hold, private social-care providers could withdraw from the market, diverting demand for long-term and adult social care to the NHS and local authorities. In recent years, profitability in the social care sector has been hit by rising costs. This has led to increases in cross subsidisation, tightening eligibility criteria and a rise in unmet need among poorer socio-economic groups. Part of today's market vulnerability arose through a series of highly leveraged home care deals which saw larger cross-regional operators and smaller local providers borrow heavily against high multiples of future earnings. The impact of a series of market exits across a sector already under pressure could lead to systemic failure, as a critical number of providers exits the market.

Regeneration programme failure

Property values and investment activity are currently falling faster in regeneration areas than across established commercial and residential zones, increasing the likelihood of developer withdrawal and reducing the business case for public investment.¹⁰ Atrophy in the residential mortgages market is constraining demand for housing and reducing land values, and the outlook for businesses is making yield valuations problematic for commercial and retail development. Of the £3 billion brought forward under the 2008 Pre-Budget Report, £775 million has been earmarked for housing and regeneration investment. However, if councils are unable to secure developer or construction partners, government organisations may be forced to subsidise deals to implement them as planned.

Managing legacy debt

Over the next five years, government organisations may make greater use of means-testing to improve fairness across public services and provide targeted support to those who need it most. More widely, the Government may need to introduce greater flexibility in its collection and charging models to facilitate tax or arrears 'holidays'.

New approaches in response to changing customer circumstances may be ineffective, however, unless action is taken to factor in and manage individual legacy debt. Calculating a contribution based on salary alone, for example on parental student loan contributions, could drive further inequity if levels of personal debt and other commitments are not taken into account. Similarly, eligibility criteria for rent or council tax 'holidays' will need to consider each person's specific financial circumstances; the application of standardised criteria may be insufficient. In this way, the value of customer information and an understanding of customer requirements to inform effective and equitable policymaking will become increasingly important in the new climate.

Public-sector pensions

Public-sector pensions sustainability is a perennial challenge that may be amplified by the economic downturn. Local government expenditure on pensions in 2007-08 was £5.2 billion compared with £4.8 billion in 2006-07, an increase of 10 per cent.¹¹ The United Kingdom's largest public-sector scheme, the Strathclyde Pension Fund, fell from a £1.6 billion surplus in June 2007 to a £1.4 billion deficit in June 2008, largely as a result of falling equity prices, inflation volatility, and actuarial adjustments related to the ageing population.¹² Individuals most likely to be affected are defined contribution scheme holders who are close to retirement.

Public-sector employees, many of whom are in defined benefit or final salary schemes, are unlikely to suffer as a result of falling equities. The public-sector pensions deficit combined with changes to inflation and interest rates could increase the net public-sector pensions liability to an unsustainable proportion of Gross Domestic Product (GDP). At both the central policy and local government levels, reform options that have been deferred in recent years may need to be revisited as a result of the downturn.

The tactical agenda: What's needed now

In addition to the underlying requirement for strategic reform, there is a series of tactical measures government organisations need to take to manage immediate risks and vulnerabilities. These measures can be grouped into three broad areas: financial diagnosis, cash management and cost optimisation.

1. Financial diagnosis

Like central banks and financial services institutions worldwide, government organisations did not anticipate the speed and depth of the financial services crisis. In shaping their responses, managers could carry out an immediate assessment of their:

- Overall financial position and investment commitments, including the financial health of their delivery partners and key suppliers – particularly those that have critical service delivery responsibilities.
- Risk management processes, which are not seen as a negative measure of failure, but as a positive management tool to underpin successful delivery.
- Revenue streams to identify and manage income uncertainty. For councils, there could be a need to review each aspect of their Local Area Agreement to ensure it still meets changing local priorities.
- Contingency plans for the funding and delivery of key public services in the event of further economic shocks.



2. Better cash management

Government organisations do not normally experience liquidity concerns as income from tax (and central grants in the case of local authorities) is usually steady. As economic activity declines, however, local authorities in particular may experience greater volatility in their cash flow, which could increase pressure on their operating capital. Streamlining and simplifying cash management processes can help identify opportunities to reduce operational costs around telecommunications, IT and support costs, fuel requirements, accommodation and wage bills.

Working capital can be reduced through small improvements implemented in phases. These include reducing early payments to suppliers, reviewing investment appraisal processes and, where appropriate, liquidating mothballed or surplus asset inventories. To oversee this work, government organisations could establish an operational spending control authority to provide tighter control of discretionary cash expenditure, and manage reforms to cash management processes and policy. This could be followed by a series of operational improvements to collection processes across areas such as council tax and licensing.

3. Cost optimisation

Figures from 2007-08 show that local authorities exceeded their 2004 Spending Review target with savings of £3.45 billion in England alone.¹³ At central level, the Government claims to have made £26.5 billion of savings over the same period.¹⁴ A new target adjusted in the 2008 Pre-Budget Report seeks to save £35 billion by 2011, including a £4.9 billion target for local authorities.¹⁵ The Government has stated that so called 'savings' that come from price increases to chargeable services, by reclassifying "back office" staff as "frontline" personnel, or from the closure of one service used to cover cost increases in another, will be invalid.¹⁶

Public-sector leaders are under considerable pressure, therefore, to extract costs from within corporate and public services. The economic climate will intensify this. In response, government organisations could take a series of tactical cost-optimisation steps:

- centralise procurement of common commodities across their domains
- manage sickness and poor performance levels more effectively
- review and remove extraneous management levels
- terminate individual projects that provide no benefit to frontline service delivery or corporate capability building
- review operational requirements for temporary and contractor staff
- develop a programme to seek short-term revenue generating opportunities across non-statutory services
- explore alternative payment and billing options for contractors and engage in closer dialogue with suppliers to find ways to reduce costs over the near term.

Strategic transformation: Using the downturn as a catalyst

The steps described in the previous section are needed to manage threats to the operational continuity of government. However, they do not represent a calculated programme of improvement.

As the initial panic caused by the crisis across financial markets subsides, the downturn may provide public-sector leaders with renewed focus on a smaller group of core responsibilities, and a clearer sense of essential customer requirements. In this environment, getting basic public services delivered will be important. Given the likelihood of increased financial constraints and possible further economic shocks, however, public-sector leaders will need to develop new approaches to key aspects of their businesses.

1. Embrace innovation and rethink delivery models

Innovation has been vital to improving efficiency and service quality in public-sector organisations over successive spending review cycles. Shared services, e-Government, direct payments, strategic partnerships and the Private Finance Initiative (PFI) are all examples of how government has successfully innovated to drive efficiency. In the new climate, public-sector leaders need to be prepared to implement successful ideas quickly, adapt to new technologies and service delivery models, and accept that, as part of the process, some ideas will not prove successful. Other steps could include:

- leadership commitment to cultivate innovation at all levels
- high-quality customer analysis to understand the requirements of different citizen groups
- identification and removal of vested interests, outmoded policy and process dogma that constrain innovation

- mechanisms to test quickly, scale up and institutionalise ideas that have been shown to be successful
- portfolio management that involves regularly prioritising projects, and cancelling those that are no longer delivering value
- appropriate networks and communication channels to share new ideas across departmental and policy boundaries
- creation of specific roles in the organisation with responsibility for challenging and reforming process, policy and operating methods.

Reconsidering traditional service delivery models provides particular opportunity for innovation. For example, the Child Maintenance and Enforcement Commission (CMEC) will use a different business model as a result of changes in policy, processes, technology and organisation, and will operate at arm's length from government. CMEC also intends to make greater use of technology to deploy increased powers to chase outstanding debt. Further, it will work with outsourced providers to achieve its primary goal of maximising the number of effective child maintenance arrangements for children who live apart from one or both their parents.

The use of social enterprise is another area that could further diversify public-sector service delivery models. The Government estimates that there are over 55,000 social enterprises in the United Kingdom that contribute £8.4 billion to GDP.¹⁷ The benefits social enterprises can bring are widely understood, but public-sector leaders could do more to increase opportunities for them to assist across a greater range of services by:

- Identifying local social enterprises and ensuring any 'approved suppliers' regime is conducive to their offerings.
- Building a social enterprise network by sending clear messages that the public-sector supply side is opening up and offering support to organisations that have no experience of competing for public-sector tenders.
- Reviewing financial policy and rules (such as supplier eligibility based on number of years trading) to allow social enterprises to bid for contracts.
- Modifying contract models to encourage social enterprise. Social enterprises often find it difficult to operate in environments where only amalgamated or multidisciplinary contracts are issued. Conversely, they tend to thrive in environments where there is systemic sub-contracting, or where social enterprises are encouraged to interface with larger private-sector partners as part of consortia.

2. Exploit the best from the private and third sectors

Government at all levels relies on private- and third-sector partners to meet its service delivery responsibilities. The United Kingdom's Public Service Industry (PSI) is one of the largest and most mature in the world, accounting for 5.7 per cent of GDP and £79 billion in total revenue in 2007-08.¹⁸

Within the PSI, the PFI market, after ten years of growth stimulated by policy and the availability of cheap credit, is likely to be more subdued over the next three years. Despite the acceleration of capital programmes at central and local level, public-sector organisations could face reluctance from suppliers to commit to a deal if credit is not readily available.

Tighter profit margins and the rising costs of bidding (estimated to be around £11 million for a typical hospital contract) may lead to market exits as PFI deals become less attractive to investors.¹⁹

The changes in the PFI climate and the wider PSI present a series of strategic opportunities for public-sector organisations. Chief among these is a chance to exploit their position as a 'low risk' partner to obtain better value for money and negotiate cheaper contracts with suppliers. New private suppliers may be attracted to public-service markets by government organisations' access to credit. Because of their own fragile positions, some suppliers may seek to pass a greater share of risks and liabilities for delivery on to public-sector partners. But government organisations are in a strong position to challenge this. Suppliers may find themselves competing in an increasingly smaller pool of competitors. This offers commercial advantages for public-sector commissioners, as those suppliers that remain may be prepared to offer more for less to stay competitive.

Public-sector organisations could also develop new contract models that make greater use of 'reward for delivery' mechanisms such as supplier performance bonds, or linking fees on consultancy services to actual delivery. By properly understanding the commercial drivers of private-sector partners, government commercial and procurement professionals may be able to recast contract models in ways that improve delivery and financial assurance.

For their part, social enterprises that depend on government grants are generally less vulnerable than those that rely on donations from philanthropic or corporate channels (the sector as a whole receives 35.7 per cent from government contracts, with 50 per cent of that figure from local government).²⁰ If some third-sector organisations disappear as result of the downturn, those that are left are likely to have strong financial management, accurate pricing models, high quality leadership, and a capacity for delivering services at scale.

The downturn may accelerate the process of making the third sector more professional by instituting key market disciplines among organisations that remain. To maximise opportunities for these organisations to support government, departments and local authorities might seek to change bid eligibility rules and open up markets to a larger range of providers across more service areas.

3. Build new capabilities

Many public-sector finance directors (along with their private-sector counterparts) are facing their first recession in that capacity. Across government organisations, finance functions may need to acquire new capabilities in order to oversee a strategic cost optimisation programme, assess supplier capabilities and risks, and develop new approaches to planning within the context of an uncertain environment. More widely, however, the immediate actions taken following the recent crisis across financial markets illustrate how effectively government leaders can react in a crisis. Applying this capability within a more benign, 'business as usual' environment could help public-sector leaders to anticipate problems before they emerge.

Government organisations will also need to build capability across procurement and commissioning functions to gain maximum benefit from the opportunities described in point 2 (see page 11). In addition, departments and local authorities could consider ways to increase the professionalism of their treasury management and investment functions, improve their asset-management capabilities, and build corporate finance and commercial skills.

In the private sector, professional asset managers often occupy senior positions within an organisation. They also possess the influence and skills to manage physical assets, allocate people and IT optimally, and invest on the basis of a proper understanding of opportunity cost and depreciation. At present, imperfect knowledge (information dispersed throughout the sector) and resource immobility can constrain government organisations from doing so.

More than ever, government organisations need to develop leadership that combines effective governance of individual organisations with strategic thinking about whole-market solutions to social and policy problems. Social care, for example, is a policy area that at present is being addressed in a fragmented, parochial way, which has led to regional inequality and unmet need. Local Area Agreements and the Public Service Agreements represent the framework for a more co-ordinated approach, but high-quality leadership will be required to drive the collaboration and regional partnerships needed to prevent market failure.

The economic downturn will increase the need for accurate forecasting models to predict medium-term demand for key services. This could include assessing possible behavioural changes amongst customer groups and the likely burden of increased fraud levels, council tax arrears, homelessness and personal bankruptcy. Government organisations need to develop these capabilities to support their long-term policies and expenditure decision-making.

4. Implement permanent cost savings

Public-sector managers could consider ways to simplify, consolidate and streamline corporate functions to improve efficiency over the long term. The Cabinet Office estimates that central and local government spends around £7 billion per annum on human resources and finance functions, and that around 20 per cent of this cost could be saved through greater use of shared services.²¹ But by March 2007, departments reported that only about £315 million worth of savings had been achieved through efficiencies in the human resources and finance functions. Over the next five years, further opportunities to achieve cost savings will come through shared services, together with knowledge management regimes to circulate operational information more efficiently around government organisations.

In addition to shared services, there will also be opportunities for local authorities to make savings through strategic agreements with neighbouring or other authorities, the police, primary care trusts and others. In 2008, the Government allocated £185 million to fund Regional Improvement and Efficiency Partnerships.²² Such funding provides opportunities for local authorities to pool common functions such as legal advice and information services on waste management, agree common approaches to procuring and managing construction work, and develop joint agreements with single suppliers across different regions and services.

Measuring the impact of a downturn on customer behaviour will provide public-sector organisations with a clearer sense of their changing human capital requirements. Managers could consider the value in redeploying staff into business areas where resource demand is likely to increase. If local authorities expect a fall in planning applications, but a rise in council tax arrears for example, then an alternative to employing new case officers in Arrears departments could involve retraining and redeploying excess staff from Planning.

Success in cost optimisation is dependent on the credibility and value of 'efficiency' programmes across the workforce. Efficiency must be seen to be important to public-sector leaders, and responsibility for executing cost optimisation programmes should be given to individuals who have played an active role in their formulation. A 2006 YouGov poll showed that only 30 per cent of public-sector employees believe they can make a positive impact on how resources are used compared with 43 per cent in private-sector organisations.²³

Institutional antipathy and the perception of gimmickry around 'top-down' efficiency programmes have led to underachievement in the past. Developing a culture that, from top to bottom, believes in continuous improvement, understands customer requirements and where value lies at all levels is key. Celebrating innovative ideas and rewarding individuals and teams with a cash share of the efficiency gains might be two ways to improve co-operation.

A 2006 YouGov poll showed that only 30 per cent of public-sector employees believe they can make a positive impact on how resources are used compared with 43 per cent in private-sector organisations.

Conclusion: Seizing opportunities for strategic transformation

Over the last ten years, government at all levels has come under increasing pressure to deliver public services in cost effective ways and improve quality in response to rising citizen expectations.

This challenge has now been heightened by an economic downturn that may increase financial pressure and delivery expectations, and regroup priorities across a more simplified, focused cluster of essential services. Liabilities on the State may increase as public services become more important to a larger number of people. In addition, there may be further economic shocks around the corner, which could concentrate these challenges still further.

Yet amid this change and uncertainty, there are opportunities that public-sector managers must seize to transform their organisational stance from one that reacts to events and new problems as they arise, to a new, more strategic approach. By adopting a more long-term view, managers would be able to anticipate and prevent social and economic challenges before they emerge, and do so in a cost effective and sustainable way.

A series of whole-market shocks in 2008 will require a new style of management across the public sector, where roles that were previously functionally driven and narrowly defined now need to be more holistic in order to anticipate and prepare for future shocks. In its developing role as a regulator, government may also have a role to play in strengthening the leadership across key private-sector organisations that fulfil responsibilities across public-sector markets.

Implementing the proposals set out in this report depends on the ability of public-sector leaders to recognise the need, not only for a series of near-term tactical adaptations, but also for a broader programme of strategic transformation across several key areas.

These include developing new corporate capabilities in response to a changing financial environment, a strategic approach to drive down fixed as well as discretionary costs, and a willingness to embrace innovation and new service delivery models to improve delivery.

The final and most important aspect involves managing the changing relationship between government organisations and their suppliers and partners. Despite the risks, an ingrained reliance on the private and third sectors means that it is to public-sector organisations' benefit to maintain relationships with these partners. The new environment creates opportunities for public organisations to work more closely with partners, but to strike more favourable deals on their terms.

The downturn provides a chance for public-sector organisations to drive through reforms they could not necessarily achieve in more prosperous times. To think tactically at this time will only defer the damage caused by an underlying tension between public expenditure decline and rising costs and citizen expectations. Public-sector leaders need to confront this tension and transform their organisations into leaner, fit-for-purpose entities by implementing strategic reforms. The time to respond to these opportunities is now.

Notes

- 1 This report uses the terms 'government organisations' or 'public-sector organisations' to describe central departments, local authorities, devolved administrations, executive agencies and Non-Departmental Public Bodies.
- 2 2008-09 Near Cash Projections, HM Treasury, November 2008.
- 3 2008 Pre-Budget Report, HM Treasury, November 2008.
- 4 Ibid.
- 5 Ibid.
- 6 Positively Charged, Audit Commission, January 2008.
- 7 Local Government Association See: <http://www.lga.gov.uk/lga/core/page.do?pageId=1066431>
- 8 Statement by David Bailey, Capital Markets Sector Manager, FSA to the CIPFA Local Government Treasury Management Conference, 22 October 2008.
- 9 BBC News. See: <http://news.bbc.co.uk/1/hi/uk/7650192.stm>
- 10 Investment Property Database Regeneration Index. See: http://www.building.co.uk/regen_story.asp?storycode=3120292
- 11 Statistical release, Department for Communities and Local Government, 15 October 2008.
- 12 See: <http://www.efinancialnews.com/homepage/content/2451799962>
- 13 2007-08 Annual Efficiency Statements, Department for Communities and Local Government, September 2008.
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- 15 2007 Comprehensive Spending Review; 2008 Pre-Budget Report, both HM Treasury.
- 16 Measuring and Reporting Value for Money Gains: A Guide to Compiling the Data for National Indicator 179, Department for Communities and Local Government, October 2008.
- 17 Small Business Survey, Department for Trade and Industry, 2005.
- 18 Public Services Industry Review, Department for Business, Enterprise & Regulatory Reform, July 2008.
- 19 See: <http://www.independent.co.uk/news/uk/home-news/the-big-question-what-is-the-pfi-and-why-is-it-in-such-trouble-on-the-london-underground-457586.html>
- 20 See: <http://www.ncvo-vol.org.uk/sfp/?id=9876>
- 21 Improving Corporate Functions Using Shared Services, National Audit Office, November 2007.
- 22 Statement by John Healey, Minister for Local Government, April 2008: See: <http://www.communities.gov.uk/news/corporate/649334>
- 23 YouGov poll commissioned by the Office of Government Commerce, May 2006.

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