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**A Dose of Austerity
*Can Public-Sector
Institutions Swallow
This Bitter Pill?***



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A DOSE OF AUSTERITY

*Can Public-Sector
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As the global financial system continues to tumble, a prolonged period of enforced austerity looms for all aspects of the British economy. Austerity raises difficult and painful choices for the private sector, but microeconomic necessity will drive swift structural solutions. Unfortunately, the public-sector half of the economy will likely take longer to adjust.

We advise leading public servants to heed three important aspects of today's situation. First, the severity of the situation for public finances cannot be overestimated. This is not simply because of the Treasury's current indebtedness, but because of the fundamental importance of the government's real-world obligations to society. Senior leaders must create financial headroom if they are to deliver against these obligations.

Second, few of the current departmental efforts to respond to the 2007 Comprehensive Spending Review (CSR07) are anything more than incremental. Meeting this challenge will require a significant and deep-rooted shift in priorities.

Finally, delivering effective results requires fundamental behaviour changes at all levels of public service. Fundamental change is a bitter pill to swallow, but it can be made more palatable when it takes into account the inherent features of the civil service, including the size and complexity of its institutions and the breadth and depth of its staff experience. Leaders who adopt the appropriate response of fundamental change will regain

the initiative over the many unwelcome external forces that assail their service delivery ambitions.

This diagnosis will not surprise experienced civil servants, but the difficulty of successful delivery may well resonate strongly. Now is the time for senior civil servants to demonstrate their leadership of the public sector as vigorously as they have addressed the issues of the private sector. These leaders will need to impose their own agenda of fundamental change and act decisively to deliver their desired outcomes.

Financial Pressures and Severe Challenges

Most assessments of the situation in which central government finds itself have focussed on its heavy financial burden. In essence, public-sector net debt has risen rapidly from a low of 32 percent in 2001 towards the Treasury's self-imposed sustainable investment ceiling of 40 percent. Many economists estimate the figure will reach close to 50 percent following the recently announced rescue package, and a long debate will no doubt ensue about how to classify 'temporary public ownership' of financial institutions in light of this and other estimates. Whatever the final figures and whatever the hopes for downstream profits from investments in financial institutions, the government will be reluctant to raise taxes or cut benefits, and will first make major cuts within departmental expenditures. Although intense financial pressure may be unavoidable, it will be most unwelcome to the many teams of civil servants who have been preparing responses to other pressing challenges, including:

- Tackling serious crime and public disorder
- Protecting all citizens from terrorism
- Adapting energy usage to avert calamitous climate change
- Providing an ageing population with adequate pensions and healthcare
- Responding to reasonable expectations of customer service
- Maintaining a viable military in response to multiple threats overseas
- Supporting measures to eradicate poverty in the developing world
- Providing high-quality education, opportunities, and jobs
- Preparing to deliver a successful Olympic Games.

Any normal person valiantly striving for success on these critical objectives would balk at interference in his or her day-to-day work. However, it is more important than ever for civil servants not to flinch from the difficult task of fundamental change that will allow them to deliver lower-cost public services. Structural improvements in the public sector would benefit any of the political parties and offer the best medium-term prospect for successful delivery of the ambitious agenda listed above.

Stepping Beyond Incremental Plans

According to the Treasury, CSR07 sought to increase public spending by 2 percent per year in real terms, while reducing cash

expenditure by 3 percent per year in central and local government. These measures would reduce departmental administrative costs by 5 percent year on year.

Alas, the 2 percent increase of £2 billion pales in comparison to current financial bailouts and makes the CSR07 changes appear merely incremental. But pointing this out does not go over well with the cohorts of planners and project managers who have devised complex ways to achieve 5 percent year-on-year reductions in administrative costs. In fact, many of the required CSR07 changes are only now approaching fruition, and many people are wedded to the plans that underpin them.

Today's situation asks public servants responsible for large budgets to strike a difficult balance between showing rapid benefits and implementing initiatives that will be sustainable for the long term. Many public-sector transformation efforts to quickly create lasting fundamental change have tripped over themselves, as the next section shows—but it is worse to fail to leave the starting blocks. We may find ourselves within Year One of a three-year spending round, but that must not prevent us from aggressively rewriting 2009–10 and 2010–11 plans. Nimble footwork at this early stage can give leaders vital room to manoeuvre. Without such freedom, they will become firmly boxed into a corner at a time when the public most needs government support.

The necessary changes are radical shifts in the portfolio of capabilities that a department deploys. This change will include difficult decisions in closing down some capabilities and courageous decisions in transforming others.

These changes will amount to nothing, however, if they are not seen through to completion.

Strong Medicine Required

Despite the dedication and talent of senior civil servants, central government does not have an impressive track record of responding to strong medicine. One example of these difficulties can be seen in the frustration of government at its inability to drive substantial performance improvements when centrally imposed performance targets were implemented at the turn of the millennium. Another, more specific example was the well-publicised failures of the Child Support Agency, which was launched in 1992 with substantial ministerial pressure to replicate an analogous agency in Florida. Blighted by poor leadership and unclear objectives, the agency failed in 2003 because of an unrealistic and poorly executed turnaround programme, and still required £320 million in 2006 to tackle a backlog of 250,000 cases and 500 information technology defects.

Several features inherent to the public sector tend to thwart successful fundamental change:

- The policy objectives upon which every transformation depends for its long-term direction are judged most critically for their short-term political benefits. In this instance, the short-term incentives of politicians—particularly as any closely fought election approaches—are radically at odds with taxpayers’ desire to see a long-term return on investment.
- The government is obliged to treat all citizens fairly, but interpretation of this

requirement as a need for a universal approach has made some operational options unavailable. For instance, prioritising certain activities or segmenting customers for improved service delivery can be inexpensive changes that cause little disruption to operations and yet are extremely effective. (Fortunately, it is becoming clear that treating everyone fairly does not necessarily mean treating them all the same. A good example comes from Her Majesty’s Revenue & Customs [HMRC], which has radically improved processing times for both staff and one segment of customers with its short-form tax returns. Such distinctions between HMRC customers would have been unacceptable several years ago, and this change indicates an important avenue for radical productivity improvements within other areas of government.)

- The larger and more complex the institution, the harder it tends to be to manage intelligently. Yet political fears compel leaders to keep thorny issues under close control, thus driving centralisation and its associated bureaucracy. Examples of such centralisation occur as fearful governments pull resources towards Whitehall, or as anxious senior civil servants aggregate IT improvements into vast change programmes.
- Two fundamental elements of the civil service’s offering to its staff are career stability and breadth of experience. Transformation is often the antithesis of the career stability that has enshrined complex human resources procedures and constraints in all people-related changes and that has

led the civil service to retain too many inward-looking, low-quality middle managers. Perversely, the opposite is true within the upper echelons of the civil service, where the broad generalist model and short-term political pressure to announce another successful initiative dramatically shorten leaders’ time in any particular role. For example, how can one lead a major, multiyear transformation if one’s incentives are entirely focussed on the mere two years that one may hold the role—and thus not contingent on seeing any change through from policy conception to delivery?

- In the 1990s, aggressive outsourcing of IT capabilities stripped the government of its own IT experts. In addition, the requirement to foster competition between IT suppliers, although essentially a good idea, had the unforeseen consequence of locking departments into multiple contract ‘silos’ run by different providers. Fundamental change will likely require departments to revisit embedded contractual arrangements. We do not advocate a wholesale reintegration of IT supply, but rather a significant increase in government oversight of such suppliers.

To face up to its own responsibility for fundamental change, the public sector will need to consciously address each of the above points throughout the life of every transformation effort. Each individual point has its own solution and best practices, but the collective responsibility to deliver successful outcomes in the face of massive external demands will require, first and foremost, exceptional leadership.

Conclusion

Exceptional leadership is required to give the civil service the will and the ability to take this medicine proactively, and to apply it in support of the broader economic downturn and ambitious public service goals to which government aspires. Strong leadership will reveal itself through timely and appropriate interventions that create fundamental change in a way that is flexible and that goes well beyond the incremental change in existing CSR07 plans. The opposite approach, that of diligent adherence to existing plans, would act as a brake on progress at a time that requires farsighted and nimble delivery of outcomes.

Civil servants must not look solely to politicians for their inspiration, and the knowledge that an election looms within 18 months can be no excuse. From the outside, the inherent features of the public sector are difficult to understand and navigate, whereas changes led from within stand a fighting chance of answering its challenges. We challenge senior civil servants to counter each of the inherent features of the public sector listed in the section above, instead seeking:

- Timelines from policy creation to delivery horizons that stretch far beyond a two-week media cycle
- Appropriate use of customer insight to streamline business processes
- Smart division of labour as a counter to excessive centralisation
- Redefined people management approaches for both senior and junior civil servants
- Active management of IT infrastructure and suppliers.

Only the best and the strongest public servants can drive through a medium-term transformation agenda in the face of political pressure for continued short-term victories in the media. Successful application of this prescription requires investment in strong leaders, supported by relevant expertise, who both understand and challenge those barriers to change that permeate the public sector. Although there may be some temptation to recruit from the large pool of suddenly unemployed bankers, based on assumptions about their insight and acumen, this would be the wrong answer.

Senior public servants should act decisively and nimbly during this difficult time. They have a long history of responding to politically imposed change, but at a time of tight cost management, this raises the spectre of a scattergun approach to managing a department's portfolio. Leadership today will manifest itself in those who are able to impose change on their own terms.

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