New approaches for how the public sector improves productivity
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Improving public sector productivity through prioritisation, measurement and alignment

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> *Productivity isn't everything, but in the long run it is almost everything*
> Paul Krugman

Overview

As a term, productivity is a perennial topic of debate within the public sector and industry that most would describe as improved efficiency and effectiveness of an activity.

The reality however, is far more complex. Productivity has such a variety of interpretations across sectors of the Australian economy that the principles underlying a discussion about improving productivity in the public sector bear little relation to the way market focused sectors would think about the issue.

While every industry has a different view of productivity, the greatest point of difference lies between the public and private sectors. Simply put, the public sector is not able to adopt the shareholder return metrics that the private sector has embraced and, in of themselves, enable a whole industry of analysts, advisors and commentators.

This is not to say that public bureaucracies have not sought to understand productivity. Indeed, the term is common parlance and frequently finds itself used alongside the phrases efficiency, effectiveness, outcomes, evaluation and so on. The complicating factor though is that there is no commonly agreed way to measure public sector productivity. Such is the extent of the problem that there is an argument for treating productivity in the public sector as an unsolvable issue, or only relevant to publicly owned organisations able to exhibit commercial attributes such as state owned corporations. Anyone reviewing the literature on public sector productivity will not find it hard to appreciate this position.

This paper explores the drivers and experience of public sector productivity initiatives to date and argues that, despite the challenges of the past, productivity is relevant in the public sector context if focused around three key questions:

- Can a collective approach for strategically prioritising government programs and activities accommodate the diversity of responsibilities held by departments across the public sector?
- What can actually be measured as a means of determining productivity in the public sector, or is this an area for future research?
- How can plans and strategies to reform, and therefore improve productivity, be translated into an implementation plan that actually delivers on desired outcomes?

Each of these questions provides a way into addressing public sector productivity, whether it be about the supply and demand of services, from the standpoint of maximising focus on value adding activities, or simply executing on plans.

Background to the current productivity debate

Government productivity often gets overlooked in the national productivity debate. Productivity discussions and analyses have traditionally focussed on the 'market sectors' where goods and services are traded and more easily valued in monetary terms. In contrast, output in government services is by nature difficult to define and value.[1] The difficulty in measuring 'outcomes' in government services means it is impractical to estimate productivity in this sector.[2]

Despite these challenges, the importance of productivity in government services should not be overlooked, as the sector contributes significantly to the Australian economy and society. Indeed, according to the Australian Bureau of Statistics (ABS) there are over 1.8 million public sector employees making up over 16 per cent of total employed persons. Total wages for public sector employees totalled over $128 billion in 2011-12.[3]

Productivity in the public sector usually equates to three inter-related drivers.

- Reduction in the cost base – Pursuit of cost reductions in response to a constrained financial environment.
- Public sector modernisation – Attempts to restructure the public service as a result of machinery of government changes.
- Service delivery improvement – Improvement in outcomes for citizens by increasing efficiency and effectiveness of service delivery.

These initiatives often fail to achieve their desired outcomes because:

- Prioritisation – At a strategic level insufficient attention is paid to critically examining what the public sector should be in the business of doing, thereby embedding a range of activities that are no longer relevant to service delivery
- Measurement – Unlike in market sectors (i.e. where goods and services are sold for a price), productivity measures are not well developed, leading to the application of high level outcomes rather than a specific understanding of what an activity, function or program will do.
- Alignment – Regardless of the fiscal environment, capacity to connect strategy to execution has been limited and has created an environment of risk aversion, reluctance to drive wide-ranging reforms, and unmet expectations at the political level and amongst the community.

1. Sectors not included as 'market sectors' include the government activities of 'Public administration and safety', 'Education and training' and 'Health care and social assistance'
2. For example, in a policy department, just focusing on the number of policies developed ignores the quality of the policies, and so without a tradeable value there is no way to have a consistent measure of effective output.
3. ABS, 6248.0.55.002 – Employment and Earnings, Public Sector, Australia, 2011-12 (The vast majority of public sector employees work in the non-market sectors which includes, the Public administration and safety, Education and training and Health care and social assistance sectors.)

Budgetary influences for improving public sector productivity

Government expenditure is the traditional starting point for understanding public sector productivity.

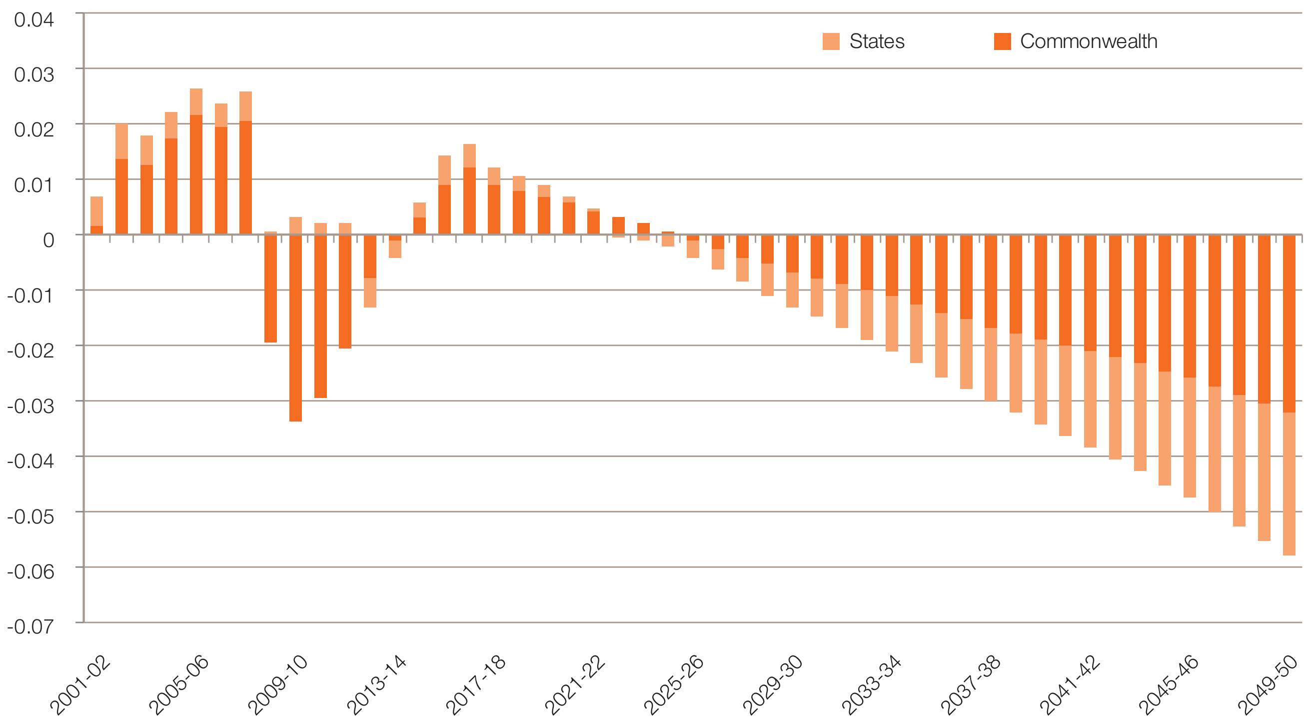
While a focus on 'cost' is important, particularly during periods of fiscal challenge, 'productivity' is about understanding how to optimise the inputs into service delivery outcomes.

Australia's productivity challenge is well acknowledged, with productivity falling across all sectors since the 2000s.[4] Although the issue of productivity in the public sector is not a new one, the understanding of public sector 'productivity' is often combined with national issues that may contribute to GDP productivity, for example taxation reform, workforce participation rates and debates regarding the size and distribution of welfare payments.

In a pure government context, budgetary challenges necessitate the need for a greater focus on expenditure.

During the 1990s and into the 2000s, Australia's government fiscal balances were rebuilt to a strong position due to asset sales and strong tax revenues. In the years prior to the global financial crisis (GFC), rapidly rising commodity prices provided a major boost to company profits and wages

Figure 1: Primary balance: Commonwealth and state/territory governments, % of GDP



Source: PwC analysis

Note: The primary balance is defined as the difference between revenues and expenditures, excluding interest transactions. This chart uses official budget forward estimates where they are available. To this extent it relies on budget estimates of future revenue growth and expenditure paths. It is based on an assumption of a steady 1.5% improvement in productivity each year.

4. Refer, for example to: 'Australia's Productivity Performance and Real Incomes', RBA: June 2012

growth in resources, and resources-related industries. This, combined with strong asset price growth, a maturing capital gains tax system, and strong household consumption growth, supported robust growth in tax receipts. Governments also felt confident enough to provide reductions in income tax rates, despite structural balances not being as strong as underlying cash balances.[5]

It was this strong public sector balance sheet that provided the Commonwealth Government with the flexibility to respond to the GFC, through discretionary stimulus, without exposing Australia to undue credit risk. Even today, Commonwealth finances are strong and the extent of confidence in Australia's public finances continues to be reflected in Australia's AAA credit rating.[6]

Drivers to a greater focus on productivity

The Australian Government has the budgetary position to choose a medium pace of consolidation; in government's own words 'making drastic cuts in the near term would come at significant cost to jobs and growth'.[7] This is sensible given that Australia's financial position remains the envy of other advanced economies and deficits are comparatively low when compared to other Organisation for Economic Co-operation and Development (OECD)countries.[8]

However, since the GFC, governments at all levels are facing a challenging situation and while deficits are comparatively low when compared to other OECD countries, a return to surplus has been more difficult than anticipated due to:

- a drop in revenues across all Australian Governments
- a need to respond to unresolved growth in expenses (often 6-8% year on year).[9]

The GFC and the overall tightening fiscal environment has brought productivity into focus, with the discussion mainly characterised by constraining expense growth. Any budget surplus in the near term will need to be achieved through strict fiscal discipline. For instance, a return to the spending growth in the pre-FY08 period would create up to $67 billion of additional pressure on expenses.[10] In this sense, any plans to implement unfunded programs will need to be based on improving productivity across the sector.

5. Parliamentary Budget Office. 2013.Estimates of the structural budget balance of the Australian Government: 2001-02 to 2016-17. Parliament of Australia, Canberra.
6. Parkinson, M. 2012. 'Challenges and opportunities for the Australian Economy'. Speech to the John Curtin Institute of Public Policy, Breakfast forum. Perth, 5 October 2012.
7. Australian Government, Budget 2013-14 http://www.budget.gov.au/2013-14/content/bp1/html/bp1_bst1.htm
8. http://www.budget.gov.au/2013-14/content/economic_statement/download/2013_EconomicStatement.pdf
9. The challenging fiscal future for Australian Governments is described and forecast in PwC, 2013, Protecting prosperity: Why we need to talk about tax, available at http://www.pwc.com.au/tax/assets Protecting-prosperity-22Jul13.pdf
10. Based on compound annual growth rate (CAGR) of 6.8% over five years – FY04 to FY08. Source: www.budget.gov.au

Ongoing structural challenges

Concerns around budgets deficits are also amplified when considered though the lens of 'structural' budget balances. Structural budget balances adjust for major cyclical and temporary factors and can provide an indication of the health of a government's balance sheet and debt sustainability. Recent reports have suggested that it is structural, rather than cyclical, factors driving Australia's high debt levels, reflecting actions by current and former governments to reduce taxes (personal income taxes, fuel excises) and an increased spending level. According to estimates by the Parliamentary Budget Office, Australia moved into a structural deficit of around 3.25% to 4.25% in 2011-12.[11]

Government's structural savings measures include limiting real spending growth and allowing tax receipts to recover naturally. As mentioned previously, these have been aligned for a steady improvement in structural balance over time. Therefore, even with proposed savings, it is expected to remain around 0.25% to 1.5% of GDP in 2016-17. This supports concentrating on public sector productivity to find resources for funding programs.

Conclusions

Revenue and expenditure are useful entry points to a public sector productivity discussion. However, it quickly becomes apparent that the public sector diverges from the private sector in how productivity is approached. For instance:

- Revenue as an income based on taxation, royalties, fees and charges only has relevance in public sector productivity from a purely macroeconomic standpoint
- Expenses being the costs incurred to deliver services only takes on meaning when the inputs to an activity are disaggregated into their component parts, which is not something typically done in the public sector (though it should be).

Budgetary challenges therefore, though important, are not the sole driver to improving public sector productivity. Notwithstanding this, given the challenging fiscal environment any plans to implement unfunded programs will need to be based on making informed choices about what to fund, deliver, or discontinue. PwC has developed a productivity based approach to assessing expenditure which provides governments with the framework for making these choices.

11. Parliamentary Budget Office. 2013. *Estimates of the structural budget balance of the Australian Government: 2001-02 to 2016-17.* Parliament of Australia, Canberra.

Maturity of current productivity programs

Governments at all levels have taken ambitious and often painful steps to lower the cost base of providing government services.

The benefits of these approaches have not always been demonstrated.

The conclusion is that a more strategically driven approach is required to create sustainable change.

The experience of productivity improvement programs in Australia's public sector has seen a tendency to directly constrain financial cost instead of adopting a more strategically driven productivity program. This tendency has thwarted many attempts to improve productive output across the public sector and led to limited success in finding sustainable cost reduction opportunities.

The underlying rationale for adopting this approach has been the lack of performance data about service delivery that can be used to make informed choices about where governments should direct their efforts.

Notable exceptions to this approach have been the perennial shared service reform programs that rely on the collection of performance metrics to substantiate the business case and the significant reforms within health to establish an efficient price for the delivery of clinical services.

Efficacy of traditional 'productivity' initiatives

The arguments above are not intended to devalue the efforts made to date – they are merely intended to point out that cost reduction and 'value for money' initiatives have a quickly realised terminus and can often affect delivery outcomes.
The table on the next page describes the benefits and limitations of these initiatives:

Table 1: Impact of 'value for money' led initiatives

Measure	Benefit	Limitations
Policies of 'zero new hires' and not replacing staff who leave voluntarily	Stabilises the workforce cost base in the short term Send a message to the organisation to prioritise activity with available resources	Usually completely undirected, leading to capability gaps across the organisation regardless of whether activities performed by the role are 'on strategy' or not Ongoing application can result in a organisation structure evolving with little relationship to what was originally intended, eg spans and layers that are too narrow or wide, inappropriate oversight of key functions, or top-heavy management
Application of 'efficiency dividends' across departments	Seeks to ameliorate the expectation of increased funding for the same activity year on year and attempts to inject a continuous improvement mindset into how activities are performed	Removes budget flexibility from senior decision-makers and weakens the role of the chief financial officer as departmental expense control is transferred to treasury and finance department officials Diminished capacity to invest in improving internal operations, leading to 'death of a thousand cuts' and degradation in service quality
Setting up back-office shared service centres	Investment has the potential to achieve a step change in service costs for non-core services within the department	Often established without consideration to the scale required to adequately achieve an acceptable rate of return to departments Business cases often developed with erroneous assumptions about the outlay required to design and implement the new shared service Usually scoped out with little consideration of what the department actually does, leading to compromises in the service catalogue and duplication in service provision
Outsourcing a government run service to a single commercial market provider	Removes the cost of a function from the salaries and wages line of the operating statement to the cost of goods and services line leading to the appearance of a leaner business model; savings may also result Demonstrates that productivity can be achieved by engaging with market providers instead of internal cost cutting Engenders commercial thinking in how services are procured, which can increase innovation	Can turn an inherent market failure into a monopoly. Arguably, stifles opportunities to enliven the market with more participants as barriers to entry are raised through the incumbency of a single service provider Runs the risk of evolving into cost shifting rather than achieving internal transformation through true outsourcing
Heavy compliance requirements for suppliers of goods and services to government	Sets a level playing field for the market by clearly establishing what is expected through a procurement process	Drives away competitive tension in the market Removes innovation as all tenderers are reduced to bidding to supply a commodity service when there is opportunity to achieve benefits by doing things differently Creates a culture of risk aversion, which has the capacity to increase rather than reduce the risks in the procurement process

Conclusions

The experience of applying these types of approaches is that they are often neither undertaken strategically nor sustainably. While reducing financial cost is one aspect of improving productivity, these types of approaches can tend to work against achieving productivity. The consequences to these types of approaches are amplified when they are used together:

1. They attack corporate memory through not filling capability gaps at the right time, which leads to 'grade inflation' in the hope of trying to replace experience with the employment of contractors who inherently bring a short-term outlook to policy challenges that may need to be addressed over the medium to longer term.
2. They 'salami slice' an enterprise rather than focusing on removing discretionary non-value adding activities, which leads to middle and senior management picking up responsibilities usually dealt with at lower grades within the organisation.
3. They introduce a survivalist mentality to the budget process in order to endure successive rounds of cost reductions. These 'fight or flight' characteristics lead to either combative relationships emerging between central agencies and line departments, or staff turnover as high value resources seek out more fulfilling and stable work opportunities.

Certainly, traditional approaches to cost cutting will not be sufficient to address the scale of the current fiscal challenge of government. An alternative approach to thinking about government service delivery is required in order to deliver sustainable productivity improvements.

Opportunities for action

Resolving the public sector productivity challenge relies on three focus areas:

- Prioritisation – Developing a collective approach for improving productivity to accommodate the diversity of responsibilities, functions and activities within the public sector
- Measurement – Creating public sector measures for determining productivity that can be adopted as a proxy to the 'shareholder return' indicator that is prevalent in the private sector
- Alignment – Translating plans and strategies for reform, and therefore improving productivity, through an implementation plan that actually delivers on desired outcomes

Each of these needs to be an area of focus for a modern public service. The places to start are through prioritising service delivery and driving a performance alignment mentality through public institutions.

Prioritisation

Taking a strategic approach to public sector productivity requires a standardised and repeatable approach that can be utilised across the varying operations that exist within a public sector environment.

Productivity is a relevant term in the public sector. What needs to change, however, is how the sector approaches the topic. Productivity is more than cost reduction; it is the improved efficiency and effectiveness of an activity; it is ceasing some activities and diverting the resources to more socially valuable uses.

The framework below provides a new and broader approach for thinking about public sector productivity. It is intended to act as a strategic overlay that can be applied to the business of government, centred on the fundamental questions of:

1. Why do I commission these services?
2. Who should deliver these services?
3. How do I better deliver these services?

Figure 1: Framework for assessing government programs, services and priorities

	What does answering this question achieve?	What supporting questions should be explored?
1 'Why do I commission these services?'	**Strategic alignment** Demonstrates the intersection between the government's political mandate and service delivery	• What are the government's electoral and policy commitments? • What is the currency of enabling legislation? • What future policy directions can be foreshadowed? • What Commonwealth / State priorities exist? • How does the service rely on the trust and legitimacy of citizens?
2 'Who should deliver these services?'	**Economic alignment** Provides an economic viewpoint on what type of competitive market exists	• What kind of market exists? (eg. nascent, established, monopolistic or failed) • What functions could or should be delivered outside of government? • Does capacity and capability reside in NGO /private sector? • What is the funding model for the service? (eg. funded through taxation or cost recovered fees and charges)
3 'How do I better deliver these services?'	**Productive alignment** Determines the strategies government must follow to achieve lowest unit cost whilst maintaining alignment to objectives	• What inputs can be measured to deliver outcomes? • What level of effort is required to deliver outcomes and outputs? • What is the cost of delivery of low value adding activities?

Program based budgeting and reporting

There is a discernible trend amongst large general budget sector agencies to achieve further efficiencies across their front, middle and back offices; A strategic view of the outputs of the agency is required. This is a challenge for many agencies, as traditionally executives have managed the expenditure of their organisations from an input perspective only (eg salaries, temporary labour, occupancy, goods and services). Budget processes are cumbersome too, as too often the development of next year's budget is a reductive process involving adding an increment to last year's actual expenditure. Very little expenditure analysis is conducted on the 'core' business of government.

We have worked with a number of agencies in the UK and Australia to define the actual services, programs and outputs that are delivered, and the associated expenditure. Once an initial 'inventory' of outputs is developed, and a hierarchy of programs defined, the agency can begin to strategically assess each program. Typical questions that arise include:

- Is the program/service/output currently aligned to government policy?
- Are there duplicate programs that are intent on achieving similar outcomes?
- Is there evidence programs are achieving intended outcomes?
- What productivity improvements have been made? (particularly for long-run programs)

Ultimately this information gives executives, Ministers, and indeed, the general public a more transparent view of what taxpayer's funds are used for, and data to be able to benchmark against any claim that the private sector could better deliver the service.

This also enables central agencies (Treasury, Finance, Prime Minister/Premier and Cabinet) to perform longer term budgeting along 'outcome' lines, and hence fulfil two desires; target government expenditure where it is needed, and, cut government expenditure where there is no longer a need.

Identifying the nature, scale and scope of the rationale for government intervention (or non-intervention) has been made considerably more transparent with the emergence of greater analytic capability.

Through answering these questions, government can determine what services need to be prioritised and how to prioritise their delivery using the best placed private or public sector provider for the task. Inherently, government is a multi-sector industry. To respond to that challenge the framework is deliberately agnostic and can therefore be applied in a range of scenarios including policymaking, regulatory and service delivery functions.

Overall, it is designed to create entry points for understanding the options decision-makers have for improving productivity. Many activities flow from the framework, under each of these questions:

1. 'Why do I commission these services?'

The intent of this question is to establish strategic alignment by seeking the justification for why certain services are delivered by government.

In effect, this question is intended to parallel the shareholder value question that would need to be answered in a private sector context. In this sense, it draws on the three dimensions of 'scope for government action' articulated in public value theory:[12]

- Legitimacy – Does government have the authority to act?
- Public value – Why should government act, and on whose behalf?
- Capability – Does government have the capability to act?

Once the rationale for delivering programs and services is understood, a view can emerge of what to prioritise, maintain, or de-emphasise based on a set of agreed facts.

12. Mark H. Moore, Creating Public Value Strategic Management in Government, Harvard University Press (1995)

Working with the private sector to create new business models to improve service delivery

PwC worked with the UK Cabinet Office to improve services and reduce costs associated with the administration of Civil Service Pensions. This fundamentally questioned who should be providing Civil Service Pensions. The function was dispersed across 10 separate business units working with 250 employees. A combination of fiscal pressures and new government meant that less funding was available for IT procurement. A more innovative approach was required.

The answer was to create a pathfinder mutual joint venture, called MyCSP Ltd, to administer public sector pensions. This is a new entity with ownership shared between government, a private sector partner and an employee benefit trust.

The new entity was launched in 2012, following an 18 month development programme during which time PwC led the design of the commercial model (including the negotiation of the supply contract back to government) and the procurement process that selected the private sector partner.

The management of the process enabled entrepreneurial growth through joining with the private sector. Importantly, the process built on private sector capabilities and allowed for private sector delivery but retained ownership by government. Instilled in the Joint Venture were on-going incentives to ensure the productivity of the sector.

2. 'Who should deliver these services?'

The public sector has a long track record of engaging with the private sector to deliver services. The purpose of this question is to establish economic alignment on whether a program or service is a candidate for market testing and whether a market exists. Government should be making a strategic assessment on the basis for retaining the responsibility (rather than the accountability) for the delivery of a program or service within the public sector when opportunities may exist to improve productivity by engaging with private sector and non-profit providers.

This question seeks to step away from the ideological and financial drivers that resulted in compulsory competitive tendering, best value and outsourcing and that were largely focused around low-value adding tasks (eg payroll) or aspects of service delivery that are easily commoditised and low risk (eg hospital linen).

Increasingly, four themes are pushing the public sector to consider increased engagement of the private sector:

1. Lower unit costs can be achieved through converting fixed costs to variable costs through contracting services – Partnering with an external party provides the opportunity to convert a fixed cost in terms of people and assets into a variable cost by virtue of contracting a service rather than owning the resources that supply it. Further, where competitive markets can be established the opportunity for lower unit cost as a result of scale presents a compelling case to outsourcing.
2. Natural advantages can be exploited by delivering the service through the best placed provider – with increasing demand for services, the public sector may not be the best placed entity for the delivery of services that are becoming increasingly complex in an environment where talent is constrained. Where the private sector is able to demonstrate delivery excellence in complex and high risk environments it has a natural advantage in delivering these services that to date has not been properly exploited.
3. Control of service delivery can be facilitated through engagement of a counterparty – For those 'commissioners' of services in the public sector there will be the perception that it may be easier to control service delivery outcomes by engaging a 'counterparty' to deliver the program or service with the right risk and control environment.
4. Outcome-based incentives have been encouraged through relationships between private and public sector – The maturity of the private sector in its engagement with the public sector is increasing, as is the contracting competency of officials, with the emergence of commissioning and payment by results both serving as good examples of this change.

There are also valid reasons for retaining functions within government; the approach is as important for valuing the importance of government service delivery as contracting services to the private sector.

Combined, these factors are driving the 'contestability' approach to service delivery, whereby classic public and private delivery models are blurring as private for-profit and not-for-profit organisations are seen as integral in delivering public services. An example of such blurring of traditional lines is shown on next page.

3. 'How do I better deliver these services?'

It should be expected that those activities that are retained and performed by the public sector are managed as efficiently and effectively as possible.

By seeking to establish productive alignment the opportunity emerges to resolve the ongoing data and information gap about the effort and cost required to achieve policy outcomes.

Concerted and well structured performance improvement programs that draw on proven methodologies such as LEAN and Six Sigma provide a means of codifying and then deconstructing core business processes that underpin government administration. Each of these processes can then be analysed at the activity level to increase the contribution that each of the inputs makes to service delivery.

It is these methods that have enabled organisations in other industries to maintain much tighter control over their cost base and to create standardised and repeatable activities. In a public sector environment, a process improvement mindset is becoming increasingly common, particularly in sectors such as health and transport where it is easier to measure both inputs and outputs. A wider opportunity exists however to expose common activities such as grant administration, regulation and compliance and reporting to a similar process.

While driving efficiency is a worthy outcome, two further benefits emerge from driving productive alignment:

- By functionally decomposing and transforming an activity or process it allows for it to be taken back for market testing once its value is more apparent
- By reaching a point where it is no longer economically viable to continue to improve a process it allows the public sector to explore options to introduce innovative alternatives to create further step changes in productivity.

Leveraging open innovation to respond to a government challenge

The push to digital delivery of services is providing considerable scope to reimagine delivery. In direct response to customer demand, Transport for NSW worked with our Digital Change team to identify the best developers and bring a range of real time bus apps to life. In order to make best use of the available data and facilitate rapid development of these apps, TfNSW hosted an App Hot House facilitated by our Digital Change team. The competition drew some of Australia's finest digital minds to battle it out and gave five winning applicants the opportunity to have their apps developed and used by TfNSW customers.

Over the two day App Hot House teams worked with a GTFS and API feed that delivered real time bus information. The challenge posed to the teams was to create prototypes of consumer-products for mobile phones, which they had to pitch to a panel of judges including TfNSW, industry experts and PwC's Digital Change team.

Crucial to the challenge was each team's ability to illustrate how its business model would enhance customer's travel experience and demonstration of their ability to execute the proposed idea. The winning teams were competing to receive:

- First access to the real time information
- The opportunity to collaborate with TfNSW stakeholders
- Promotional support from TfNSW for their apps.

This process saw TfNSW embrace a new style of working, namely 'open innovation' to accelerate and solve an immediate customer pain point. The open innovation approach requires management to appreciate that good ideas do not just generate from top-down within an organisation, but can also come from the bottom-up and even from outside the organisation (from its customers and other stakeholders).

PwC took steps to ensure that the structure of the competition, the process and the communication would develop a culture of collaboration between all participants. The design of open and clear communication channels was critical and we actively facilitated both days of the event. Through this journey, it was clear that the attitude of all stakeholders is critical for collaboration. An upfront approach between TfNSW and developers meant that each party could work 'hand-in-hand' to get the most out of the relationship.

Five winners were selected by a judging panel, of which three winners (TripView, TripGo and Arrivo Sydney) now have their products in the market. The apps contain real-time data spanning some 8,200 stops, more than 1,900 buses and almost 1,200 routes across the Sydney Bus Network. "Having real time information is a game-changer when it comes to public transport," commented Minister for Transport Gladys Berejiklian. In a press release she said, 'customers wanted real time public transport information and the three apps being released were just the beginning of the NSW Government's plans to provide it'.

4. Bringing the three questions together

The suggested framework is intended to act as a strategic overlay that can be applied to the business of government, centred on the fundamental questions of:

1. Why do I commission these services?
2. Who should deliver these services?
3. How do I better deliver these services?

Each of these questions is explored in the figure below.

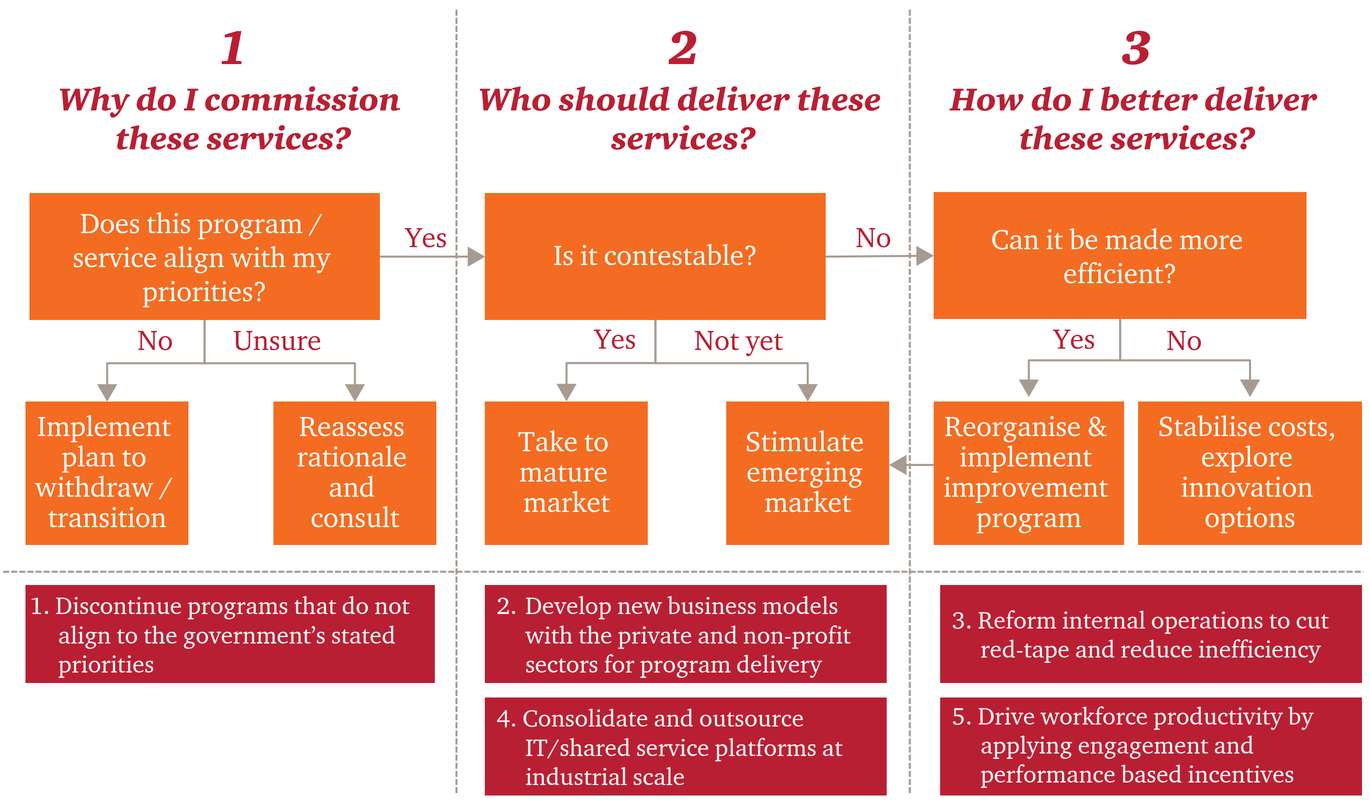
These questions provide a way into addressing public sector productivity, whether it be about the supply and demand of services, or from the standpoint of maximising focus on value adding activities. The outworking of this approach is a standardised way of achieving greater efficiency and effectiveness in the delivery of public services.

Applying this productivity framework identifies a set of opportunities to improve value and reduce cost. We have identified five target areas for improving public sector productivity derived from our experience working with Australian governments both federal and state level, as well as internationally.

1. Discontinue programs that are not economically justified and which do not align to the government's stated priorities.
2. Develop new business models with the private and non-profit sectors for program delivery.
3. Reform internal operations to cut red-tape and reduce inefficiency.
4. Consolidate and outsource IT/shared service platforms at industrial scale.
5. Drive workforce productivity by applying engagement and performance based incentives.

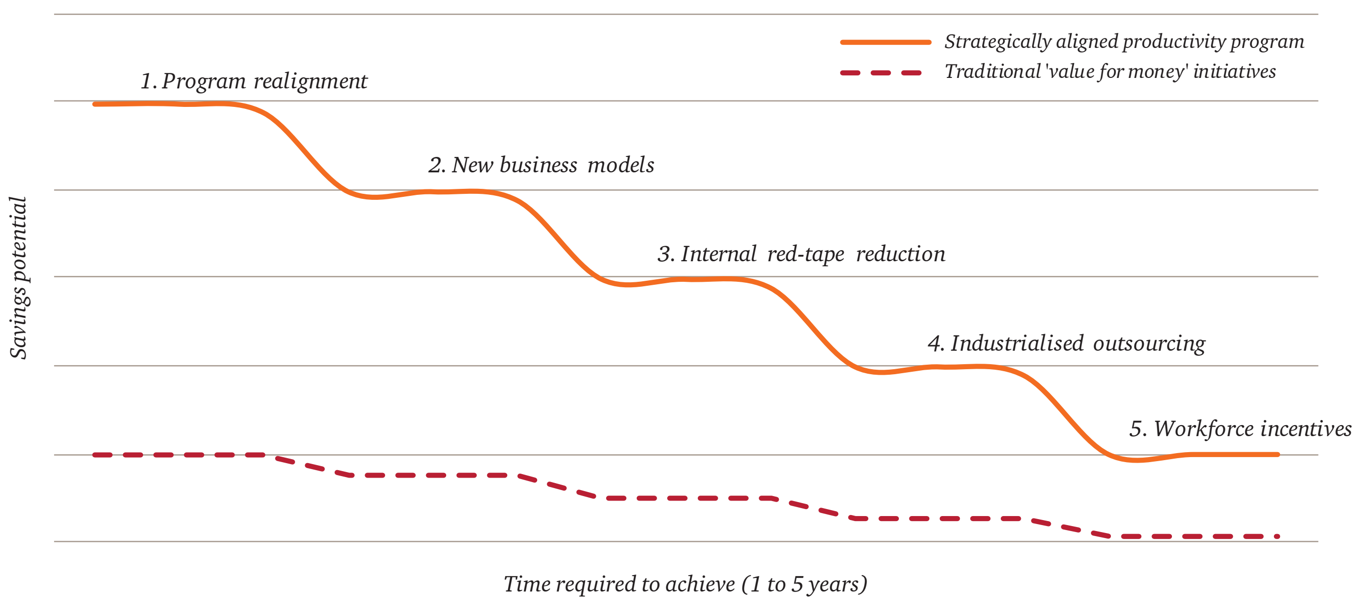
Each of these opportunities is mapped to the framework in the diagram below.

Figure 2: Framework for assessing and prioritising government programs and services



Each of these opportunities has its own savings profile. The illustrative chart below indicates the optimal model for prioritising these opportunities based on overall savings potential and time to realise benefits. The chart also contrasts the quantum of benefits with those that can be typically achieved through the 'value for money' initiatives that the public sector has adopted to date. Realigning programs and adopting new business models will drive the greatest cost reductions. However, reducing internal red-tape, back office outsourcing and incentivising the workforce will provide ongoing benefits to those programs and services that government decides to retain.

Figure 3: Savings potential realised from adopting a structured approach to productivity improvement



Measurement

Productivity measurement is a persistent challenge in the public sector as there are no common agreed definitions or measures that make the outputs produced by government tangible.

While these are legitimate concerns, other approaches can be adopted while the development of measurement frameworks "catches-up".

A measurement framework for productivity in a public sector setting is the greatest barrier to advancing the overall productivity debate. The challenges of measurement are such that in some respects it has perhaps become an obstacle to progressing action on productivity, and consequently has evolved to become an industry-wide barrier. In order to address productivity, focus has to move from government structure in delivering the service to the process, activity and functional level.

The benefits of the public sector better understanding productivity measurement are two-fold:

1. Developing frameworks to quantify productivity inform strategic approaches and reinforce iteration in strategic execution.
2. Making the investment in creating usable measurement frameworks is an objective that will yield long-term benefits as part of a continuous improvement program.

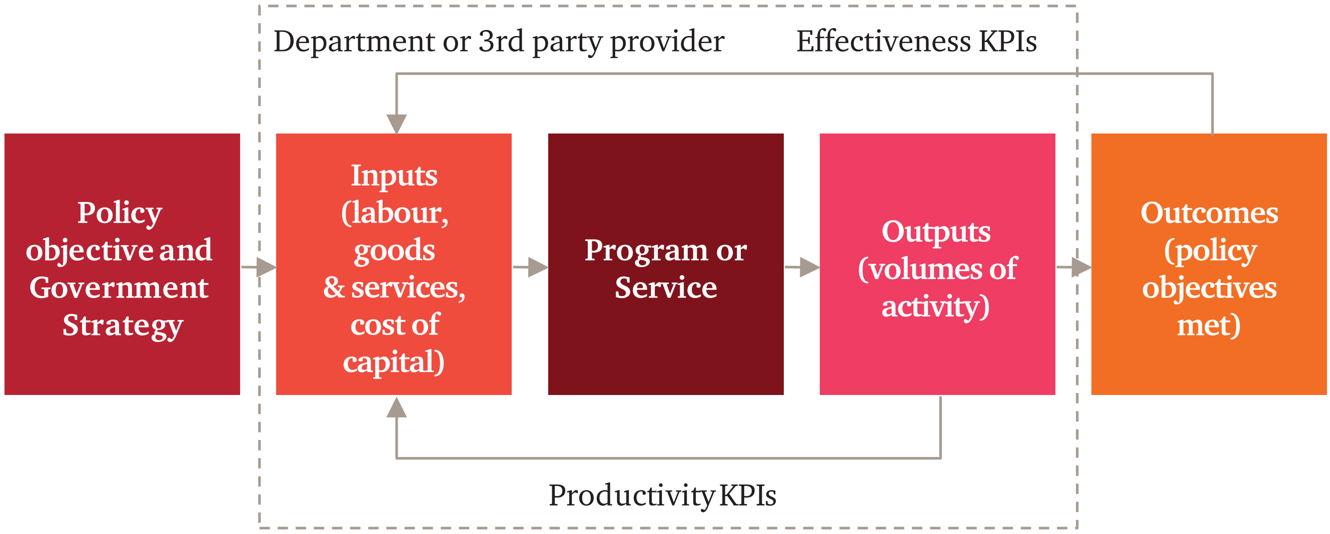
In this sense, productivity measurement is crucial to the successful delivery of a program.

Pitfalls of measuring productivity

Across the public sector there is no agreed basis for defining productivity, what it means and how it should be measured. Ongoing debates are apparent in relation to methodologies, data quality, and evidence regarding what reforms work in which circumstances. Beyond this, public sector understanding of productivity is limited because of the complexities involved in benchmarking and comparing the relative performance of aspects of service delivery between different jurisdictions and also the private sector. These are debates that escalate to the level of the OECD.

For example, difficulties arise when measuring productivity in the public sector because the output of public services is often un-priced, consumed collectively or has outcomes that span normal reporting periods thereby avoiding a matching principle between inputs and outcomes. In this way, development of a nexus between labour inputs, un-priced outputs and unquantifiable outcomes is extremely challenging. A further problem is measuring the full range of outputs and quality improvements delivered by public sector organisations that are valued by society. Hence, without comprehensive measures of output and outcomes within a comparable and controllable time frame, productivity statistics may be misleading.

Figure 4: Understanding the relationship between productivity and effectiveness measures and public sector outputs and outcomes



In Australia, early in-roads have been made in developing productivity measures. For example, the Auditor-General of Tasmania concluded in 2010 that services provided, based on activity levels, exceeded growth in public sector employee numbers over a ten year period (though not costs), suggesting an improvement in productivity over this period on a value-per-unit basis. The national health reforms of recent years including the setting of efficient prices for services is progress in terms of measuring productivity in clinical settings. To reinforce the challenges however, a recent report by the NSW Public Service Commissioner, stated: "despite [productivity's] importance, comprehensive measures and rigorous analysis of the public sector's productivity are rare".

Given these challenges there is a need for further research to be undertaken specifically in relation to the following areas:

- defining and measuring productivity, particularly in relation to measuring public sector outputs and determining direct productivity improvements
- identifying the internal and external drivers of productivity across the public sector
- understanding the balance between improving existing data sources and creating new data sets to realise practical data to inform productivity measures
- identifying the economic, organisational, management or other requirements that are needed for effective implementation.

Ultimately, the debate about measures is really an examination, and perhaps a challenge, on what government is, in the sense that measuring inputs and outputs cuts across the structure of the public sector. In fact, it quickly reveals that the public sector is not a single entity at all and that if any progress is going to occur in this area it will occur through dissecting the business of government at a process, activity and functional level rather than in structural terms.

Alignment

Successful execution of policy and strategy in the public sector is based on defining and agreeing priorities and risks, and then aligning them to performance drivers, leadership and behaviours.

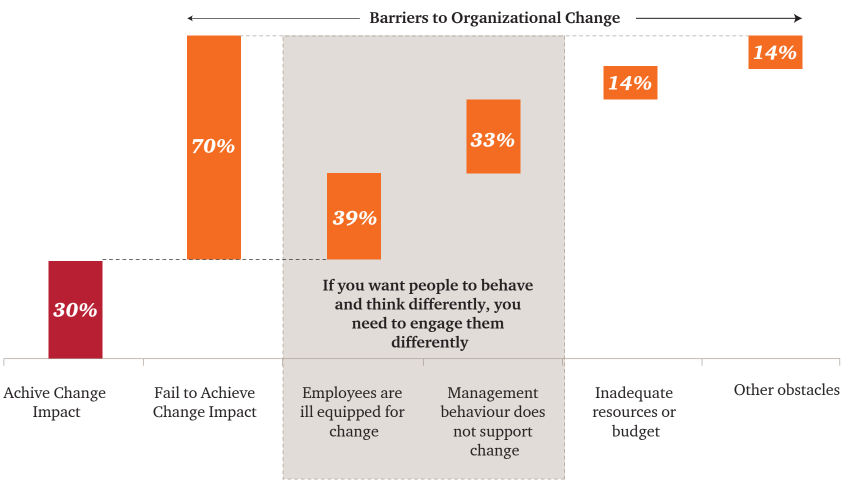
Performance alignment creates the opportunity to achieve productivity benefits by aligning execution execution with the strategic intent of government.

Many organisations find execution challenging. This is often due to rushing the transition from policy and strategy development to implementation; focusing too quickly on the process, system and structural aspects of implementation, before considering what is really going to make a difference between what exists now and the future. In this respect, a 'linear' approach to execution tends to ignore the intangible aspects of change management.

Moving from a 'linear' to an 'iterative' approach to executing on strategy

In a public sector productivity context, the theme of having strong strategy, but achieving poor implementation outcomes in terms of implementation, is highly relevant. There are many examples, both in Australia and overseas, that demonstrate the limitations of a 'linear' approach to execution – These include the ongoing attempts to implement shared service functions across different jurisdictions, machinery of government changes, and departmental restructures that take place with the aspiration of achieving (but often falling short of) improved service delivery outcomes. Without resorting to specific examples, there are many instances of change programs that have been high profile failures.

Figure 5: 70% of organisations fail to achieve the change impact they expected from a new strategy[13]



Given this experience, an iterative approach to policy and strategy development and implementation, that considers both the intangible and tangible levers of change, is a more relevant approach to improving public sector productivity. Although there are many facets to optimal strategy execution, execution failure is most commonly rooted in a failure of the leadership model.

Using the leadership model to bridge the 'white space' in execution

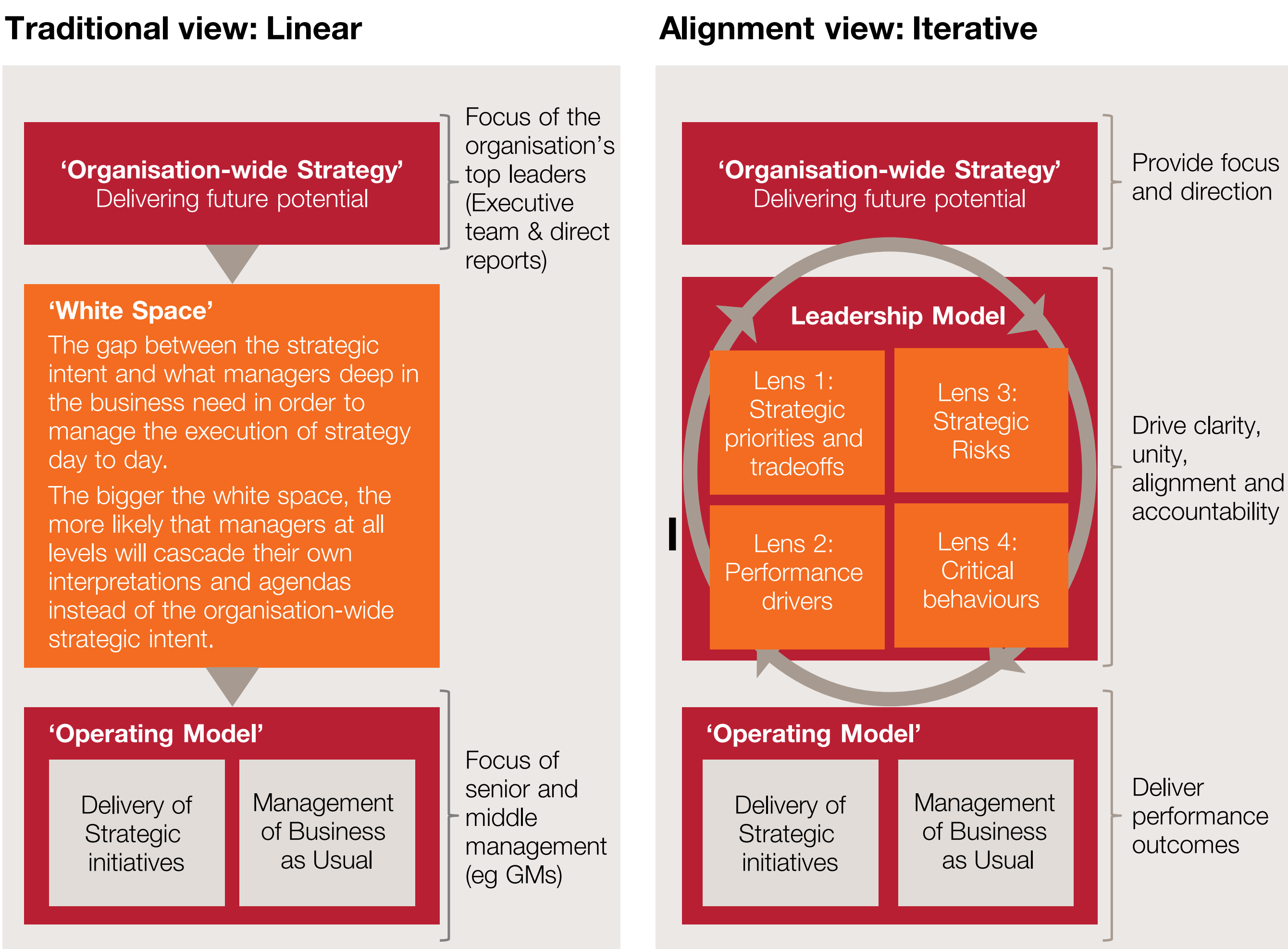
The leadership model is a critical part of execution as it explicitly addresses the transition aspect of change. It acts as the bridge between strategy and the operating model, and provides a feedback loop that helps an organisation respond quickly to change. The leadership model comprises four lenses that consider how an organisation's strategy is unpacked into specific executable actions:

1. How the key strategic risks to successful execution are identified, monitored, and managed.
2. The critical changes in behaviour required to deliver the strategy.
3. How these elements are integrated in a way that drives performance through the organisation.

The model is iterative and dynamic, with each lens reinforcing the other. This approach provides a simple yet powerful way of articulating the areas that organisations must focus on when considering alignment. Ultimately, focusing on the leadership model drives better alignment to executing strategy and reaching the organisation's strategic potential.

13. Meta-analysis: Beer and Nohria (2000), Cameron & Quinn (1999), Caldwell (1994), Goss, Pascale & Athos (1993), Kotter and Heskett (1992)

Figure 6: Using performance alignment to embed the leadership model in an iterative change approach



Performance alignment creates the opportunity to achieve productivity benefits by aligning execution execution with the strategic intent of government

Adopting the four lenses of the leadership model

Successful strategy execution is based on defining and agreeing strategic priorities and strategic risks, and then aligning performance drivers, leadership and behaviours. The leadership model is iterative and dynamic, with each lens reinforcing the other. This approach provides a simple yet powerful way of articulating the areas that organisations must focus on when considering alignment – In both business as usual and through strategic change initiatives.

- Strategic priorities and trade-offs – For a new strategy to be embedded into the organisation, employees need to understand how the strategy applies to their role, their day-to-day decisions and actions. Strategic priorities break down the complexity of the overall strategy into sub-components that more readily inform the decisions, behaviours and responsibilities at all levels in the organisation. Not all strategic priorities are equal – Some are prioritised over others due to their influence over long term value, their complexity or their criticality in addressing other performance aspirations. A well articulated strategic priority will acknowledge the specific choices or trade-offs that are inherent in the overall strategy. It is equally important to communicate what has been excluded as well as included. If middle management cannot see and feel a clear picture of the future world then it is unlikely they will be able to drive change effectively into the organisation.

- Assessing the strategic risks associated with each strategic priority – Strategic risks represent both upside and downside potential associated with the defined strategy and its execution/delivery. This is different to the other risks (eg business, operational risks) that most organisations consider. This lens helps to identify the strategic risks and opportunities, understand the uncertainty around a strategic priority and its potential contribution to performance. In doing so, the lens articulates what actions and levers are available to mitigate or manage these risks.

- Understand, define and enable critical behaviours – To execute strategy effectively, organisations require an understanding of the specific subset of critical behaviours at all levels of the organisation that drive disproportionate value (in this case improved productivity). These behaviours are also used as the lead indicators of whether an organisation is on track with respect to delivery of strategy and priorities.

- Align performance drivers – Performance metrics should reflect the strategic priorities, extending beyond the purely financial and short term. Budgets and aspirational targets need to be set in the context of the organisation's strategic risk appetite, and reporting frameworks need to provide information on emergent strategic risk to guide mitigating action and, where necessary, a change of direction. At a team and individual level, reward and performance management should reflect the strategic priorities and critical behaviours. In this context, reward encompasses not just pay and incentives, but extends to recognition, progression, working environment and opportunities for development.

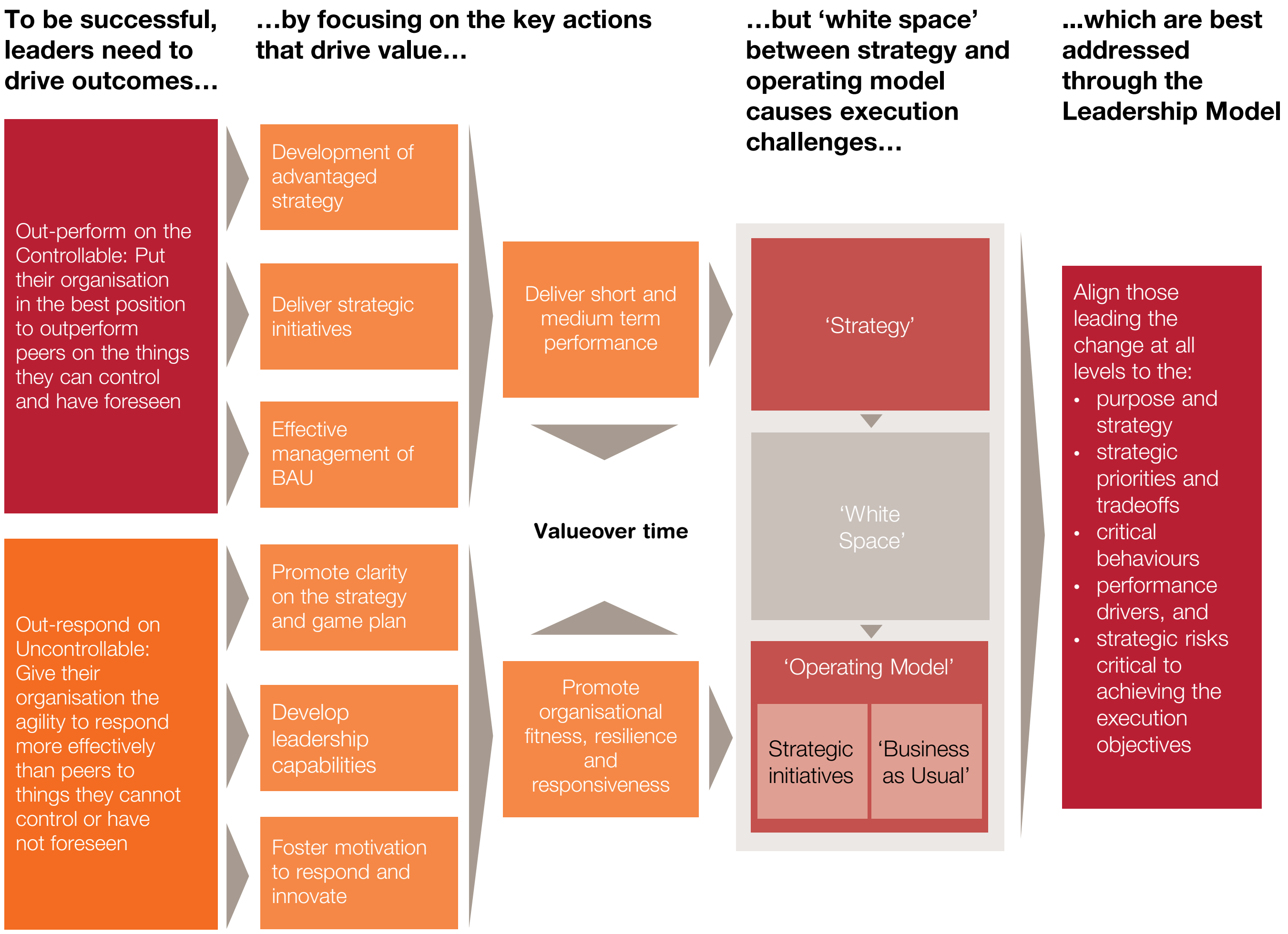
Adopting performance alignment thinking to drive productivity improvements

To be successful in a public sector operating environment, organisations need to out-perform on what they can control and out-respond to things they cannot. All organisations are drawn to doing the best that they can, through focusing on their strengths. Often this can occur at the cost of ignoring those areas where there is a need to improve. For example, where a department has the best and brightest talent in developing policy, can the same be said in terms of seeing this policy through to implementation? Inherently, a department needs the confidence of being able to succeed within the remit it can control, but also needs to be able to anticipate and respond to those aspects of organisation performance that are uncontrollable.

To complement this, a performance alignment way of thinking creates the platform for ensuring that policy formulation is successfully reflected in an organisation's operating model – This applies equally to the implementation of new strategic initiatives as well as managing business as usual. The process for achieving this is applying a focus on the lenses within the leadership model as a means to cutting out the "white space" in traditionally based implementation processes.

Adopting this way of delivering outcomes within an organisation will require senior leaders to adopt new ways of thinking and working. Performance alignment is a positive step away from the model of seeking to insure against failure by adopting disproportionate governance structures that are a facet of the public sector at present. Instead, it allows for senior managers to engage with the people within their organisations and ask what is required to make something work. In a productivity context, performance alignment is the vehicle for successfully achieving greater efficiency and effectiveness and sustaining it over the long term.

Figure 7: Improving productivity means public sector bodies need to out-perform on what they can control and out-respond to things they cannot



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