Government and the 15th Annual Global CEO Survey

Taking responsibility: Government and the Global CEO

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Contents

Foreword

Welcome to 'Taking responsibility: Government and the Global CEO' in which we assess the changing relationship between government and business

As in past years, we have extended and deepened the research for PwC's 15th Annual Global CEO Survey[1] by including a selection of interviews with senior decision-makers in governmental organisations across the world.

Our aim in doing this – and in publishing the findings here – is to understand better the implications for government policy of the views of CEOs and so contribute to mutual understanding and productive relationships between the public and private sectors.

Dealing with deficits – enabling good growth

Global recovery appears not only fragile but also unbalanced, with developing economies still growing but more mature economies, particularly in Europe, flat-lining or facing double-dip recession. Economic uncertainty and volatility continue to impact on business confidence to invest and grow.

Governments face different futures. For those in debt (mainly in the advanced G20 economies) there are years of pain ahead, with fiscal austerity the order of the day, and a priority to reduce their deficits and debts. Other governments, particularly in the developing economies, are in a more robust position and can look to the future with more confidence and optimism. Nevertheless, they are not immune from the risks of contagion from other indebted countries and the need to cope domestically with the consequences of crises in other regions, particularly in the Eurozone.

This report sets out how businesses are adapting their approaches in these uncertain times, including their priorities for government, and discusses in turn how governments:

- deal with (or avoid) deficits;
- support businesses to deliver 'good growth'; and
- help CEOs to address their biggest business challenge – the talent crunch – whilst also acting to attract and retain the people needed for the core functions of government.

Our aim throughout is to understand better the policy and public sector delivery responses needed to the challenging conditions facing business today and tomorrow. And one thing is clear: business and government as usual, with increasingly disruptive futures, is not an option.

We would like to thank not only the 1,258 company leaders across the world who shared their views with us for the CEO Survey, but also the 23 government officials who took the time to share their thoughts in depth with us[2]. We are grateful to them for their cooperation and frank insights.

We look forward to a continuing and fruitful dialogue on how to create the society and government of the future for the citizens of tomorrow – today – in a trusted, sustainable and more collaborative society.

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Global Leader Government and Public Services

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1 *'Delivering results: Growth and value in a volatile world'*, PwC January, 2012.
2 See Annex for details.

Summary

Economic uncertainty and volatility is dominating attention, both in business and in policy-making circles. Business is worried: 80% of CEOs are 'somewhat' or 'extremely' concerned about **uncertain or volatile economic growth** – the top concern across all regions, by some margin, and for all sizes of company. And nearly two thirds of CEOs (64%) are concerned about **lack of stability in capital markets**, particularly in Western Europe (76%), with the Eurozone crisis weighing heavily on CEOs' minds.

Globally, **short-term confidence has also taken a tumble**. The proportion of CEOs 'very confident' in the prospects for their revenue growth in the next year has fallen from 48% in 2010 to 40% in 2011. And within their organisations, a key business threat for CEOs is a lack of availability of key skills.

Governments need to provide political leadership to help turn this around and lay the foundations for a stable and lasting global recovery. **The priorities for governments** nationally and internationally are challenging and far-reaching. Governments need to act to:

- **Deal with fiscal deficits**, where they are currently in debt, and the consequences of contagion (where debt is less of an issue); and avoid future unsustainable debts.
- **Enable growth**, which is financially, economically and environmentally sustainable i.e. 'good growth'.
- **Tackle the talent crunch**, both in the private and the public sectors.

Of course, governments have different starting points. In the advanced G20 countries, governments need to act urgently to reduce public sector deficits and debt by reducing public spending and focusing on the growth agenda (and so increasing not only jobs but also tax revenues) as well as re-building trust and confidence in public institutions. Governments in many developing economies are more confident, optimistic and in a better position to shape their futures.

However, these countries still need to maintain fiscal discipline whilst also coping with the impact of rapid growth on inflation and also on talent availability. And all governments have a duty to focus on returns on investment and **maximise value for money** for taxpayers, whether or not spend is being reduced, whilst improving the quality of services delivered to the public.

We also recognise that national (and regional/state/local) governments are facing issues which need both global and local ('glocal') solutions, and who are also simultaneously competing (for growth) and collaborating (to solve the financial crisis). There are, however, many **common agenda items** across all levels of government in delivering outcomes.

Agenda for government
Dealing with deficits

Nearly two thirds of CEOs (65%) were concerned about governments' responses to fiscal deficits and the debt burden, with a majority concerned across all regions but particularly in Western Europe (76%).

For many governments (particularly in developed economies) the first priority is to deal with current (and avoid future) deficits and debts. Prioritisation, making tough choices and doing more (or increasingly the same or less) for less is the key to success. There is a range of ways in which governments can do things differently as well as doing different things to meet the needs of citizens and businesses alike. We believe there are five priorities for government:

Developing and **executing plans** to achieve better balanced public finances with a twin focus on:

- Reducing costs, particularly through standardising, streamlining and sharing services to increase the efficiency and effectiveness of enterprises, including deciding whether to make or buy goods, services and infrastructure.
- Developing new sources of funding to cover current spending as well as seeking to bring forward funds from the private sector in return for payments in future, increasingly linked to the successful delivery of outcomes (payment by results).
- Given the significance of labour costs, developing new approaches to **workforce reform**, with a priority to be more active in planning workforce strategies and managing and retaining 'pivotal' talent in order to achieve sustainable cost reduction.

- **Innovating service delivery** in particular by:
  - Opening up public services to any willing provider, requiring public sector organisations to partner and collaborate more effectively with the private and voluntary sectors.
  - Accelerating the take up of **new interactive digital technologies**, particularly social media and other tools which create a new interface between customers and providers e.g. crowdsourcing approaches to public service design and delivery.
- Improving **accountability and transparency**: critical to the transformation of public services is how best to make public services accountable and easy to access by the public as well as financially more transparent and robust.

  This requires reporting on a consistent basis, through reforms such as the adoption of International Public Sector Accounting Standards (IPSAS), and more comprehensive consolidation of liabilities (particularly debts at all levels of government). This will also assist stability in the capital markets by increasing the quality and reliability of governments' financial statements and so help restore trust and confidence in the ability of governments to manage their fiscal balances.
- Seeking **transitional assistance**, and future stability, through mechanisms such as Sovereign Wealth Funds.

If embraced wholeheartedly, these measures could lead to a radical reshaping of how the public sector manages itself and its assets, as well as developing new ways of working with the private and voluntary sectors.

Enabling growth

48% of CEOs believe the global economy will decline further in the next 12 months: indeed, only about 1 in 7 (15%) CEOs believe the global economy will improve in the next year.

There is no doubt that governments have a second key role: to create the **right conditions for growth**. There are many aspects to this but we emphasise three dimensions:

- Spatially, where **cities are a key engine** of sustainable growth. 'Smart cities' are also heralding a new level of cross-sector collaboration, driven by a focus on clean technologies, energy efficiency and sustainability.
- Sectorally, where **clusters of economic activity** are key to competitiveness as is the need for innovation systems and new ways of prototyping and financing growth, prioritised and focused through national innovation strategies.
- Across sectors, creating the enabling **infrastructure** needed for any modern economy to function effectively and competitively through a balanced and integrated infrastructure programme.

The financial crisis has also shown the risk of economic imbalances and going for growth at any costs. Delivering '**good growth**' requires attention to be focused away from narrow definitions of Gross Domestic Product (GDP) to a wider scorecard of factors and on a joint agenda for action particularly for jobs, income, health, work-life balance and infrastructure.

This in turn requires **more effective collaboration**, with governments working more closely with each other, with businesses and private benefactors and with citizens.

Finally, in those economies with greater state ownership of business, there is a need for a **revitalised, more radical approach to the role of state owned entities** (SOEs). Where governments decide to maintain state ownership, the primary task of SOEs is not just to generate a financial return on investment (ROI) to the government in the short and long term – it is value creation through the right investments creating a long term sustainable and competitive advantage for the nation. SOEs need to be actively owned, governed, directed and evaluated in a holistic way. A focus on costs and revenues is not enough: cost-benefits, outcomes and societal impacts are all vital parts of the future scorecard of SOEs.

Tackling the talent crunch

The number one investment focus for CEOs globally is on creating and fostering a skilled workforce: 71% of CEOs expect to make 'a significant' or 'some' increase in investment over the next three years. And 54% are extremely or somewhat concerned about the availability of key skills as a business threat to growth (similar in importance as a threat to an increasing tax burden).

Government has a dual role with respect to the talent crunch. Firstly, there are a number of areas where businesses, governments and educational establishments can work together to co-create solutions to meet **business needs**:

- Develop course curricula and training programmes which equip people with a range of **'employability' skills** as well as their particular subject matter skills and expertise, particularly to help young people where they need to access 'entry level' (often unskilled) jobs. A commitment to hard work, presentation and punctuality are every bit as important as basic numeracy and literacy.[3] In addition, communications, teamworking, analytical skills and innovative thinking are highly valued by business[4] as well as the relevant professional or technical skills for a given occupation. Training programmes should have these employability skills embedded within them so that individuals emerge with the full package of skills they need in the world of work.

3 *'Creating Opportunity, Rewarding Ambition,'* Centre for Social Justice, 2011.
4 *'Arab Human Capital Challenge',* Mohammed Bin Rashid Al Maktoum Foundation in cooperation with PwC 2007.

- **Developing new career entry paths**, which provide (particularly for young people) recognised, credible routes to high-skill careers. This involves reducing the barriers to entry and increasing access of candidates to opportunities e.g. by lowering the cost of vocational degrees and technical education programmes, which enables employers to tap into a broader, more diverse talent pool. Employers also need to step up and take a lead on this where they are lagging by playing a more active, direct role in the development of the employability and business skills that they need.
- Creating a **single market for training**, irrespective of the funding source (public or private). There needs to be an integrated approach to encourage investment and maximise the returns.
- **Tackling untapped and under-utilised talent** pools which could boost productive potential e.g. reducing the barriers to labour force participation faced by women in many countries, especially developing economies, as well as enabling ageing workforces to be kept healthy enough to work later into life and reskilling them.

Secondly, there are some key actions which government and public sector organisations need to take as **employers** to retain and engage core staff (beyond reward) including:

- Increasing the **attraction of public service** as a career choice for talented individuals by focusing on actions to make public sector organisations 'employers of choice'.
- Developing a durable **strategic workforce plan** without which organisations cannot realise their ambitions.
- **Defining talent needs** and aligning with the business by defining the type of skills that will be required for public services, identifying the people within the organisation who are best suited to particular roles and, where necessary, targeting external recruitment.
- A key feature of a strategic workforce plan is the consistent organisation-wide approach to mapping the motivations, capabilities, experience and potential of individual employees. **Systematic talent mapping** can be used to ensure the right people are assigned to the right roles. This is critical if the pivotal talent needed to deliver government's core functions is to be retained, engaged and motivated.
- **Nurturing local talent** where possible. The recruitment and development of local talent can provide a sustainable long term approach whilst skills transfer to local staff can reduce costs and enhance return on investment. However, for some countries and provinces, which lack local skills, the challenge is quite different – to find a sustainable pipeline of talent and skills to bring in from other areas, and overcoming regulatory and policy barriers.
- **Managing performance** effectively to develop the potential of staff and result in rewarding jobs and careers.
- Making greater **use of technology** to digitise processes, enhance work flexibility and engage staff through greater work-life balance.

Conclusion

Fiscal balance, good growth and employable talent: these are key outcomes needed by any society. Governments face different priorities and will need different approaches according to unique national and local circumstances. But there is no doubt that the future of the global economy depends on governments and businesses, individually and collectively, making the right decisions and taking responsibility to deliver on this monumental agenda.

Dealing with deficits

Fiscal deficits, large government debts in some countries and contagion across countries have created a headache for policy makers and businesses alike. So how can governments in debt deal with their deficits and execute their strategies to reduce spending when tax revenues are also under pressure as growth underperforms? And what can other less indebted governments learn to avoid getting into this situation themselves in future?

Maria Ramos,
Group Chief Executive,
ASBA Group, South Africa

"We need greater stability in financial markets. On the back of that, we need to create jobs, and that, taken together, will generate greater confidence…. It's the lack of confidence that I see as one of the greatest risks at the moment."

Uncertainty in the global economy is influencing business confidence and investment in many countries. This is being particularly affected by sovereign debt crises, driven by unsustainable public sector deficits and debts in some (particularly Eurozone) economies.

Indeed, the potential political and economic outcomes emerging from the Eurozone crisis in 2012 are disparate, although all share a similar theme. A harsh adjustment to a new fiscal reality will be unavoidable, regardless of the path politicians decide to follow.[5] And this may take some time to unwind, as Frederik Rosengren, CFO of the Swedish Prosecution Authority notes: "We had budget deficits and debt in the beginning of the 90s, we thought it was a huge amount, we were close to 70% of the national gross product in debt…and it took Sweden 20 years to come where we are today and for some countries it will take at least 10 to 15 years to make a recovery."

And although the biggest fiscal challenges are in the advanced G20 economies, the risks are not limited to them. As the IMF has stated: "Among developing economies, where the needed medium term fiscal adjustment is generally lower, the fiscal stance is nevertheless insufficiently tight in some cases in view of inflationary pressures and rapid growth, fuelled in part by strong capital inflows."[6]

One of our government interviewees – Erik Camarano, CEO of Movimento Brasil Competitivo (MBC) in Brazil – also points out the inter-dependency of developed and developing countries: "We are following the effects of the crisis in both the US and the Euro Zone and we have great concern because, if you look at our trade balance, our partners are mainly the US and Europe – the countries in Europe are major import and export markets for us."

In addition, all governments have a duty to focus on return on investment and maximise value for money for taxpayers, whether or not spend is being reduced. As Martin Tlapa, Deputy Minister for Industry and Trade in the Czech Republic said to us: "In the public sector I think that first important measure is to open up public policy. I mean, every taxpayer should see how the money is spent on the nation on the government level, so an open budget I think is an inspiration from the UK."

This sentiment accords with Idris Jala, Minister in the Prime Minister's Department of Malaysia: "Ensuring we get the maximum value for every dollar of taxpayer's money should be a key tenet of every government."

5 *'What's next for the Eurozone? Possible scenarios for 2012'*, PwC December 2011.
6 IMF Fiscal Monitor, September 2011. The emerging economies as defined by the IMF had a combined debt:GDP ratio of 41% in 2010 which compares with 98% in advanced economies.

What's top of mind for CEOs?

The CEOs in our Survey are clearly worried by the fiscal position of their domestic and overseas governments: over half of the CEOs we interviewed (56%) believe that their companies have been directly financially affected by the ongoing sovereign debt crisis in Europe, and 45% have changed their strategy, risk management or operational planning as a result. The highest responses came from in Western Europe (73%) and amongst very large companies with revenues over $10bn (70%).

These concerns are also in the top three **economic and policy threats** to business growth prospects, and in some cases even higher than our last Survey, as shown in *Figure 1*.

In 2011, nearly two thirds of CEOs were concerned about **governments' responses to fiscal deficits and the debt burden**, including CEOs in countries not undertaking major austerity measures. In 2012 the result is little different at 65%% of CEOs, with a majority concerned across all regions but particularly in the US (75%) and Western Europe (76%) as well as in Japan (84%), Australia (80%), India and Argentina (the latter two both at 79%).

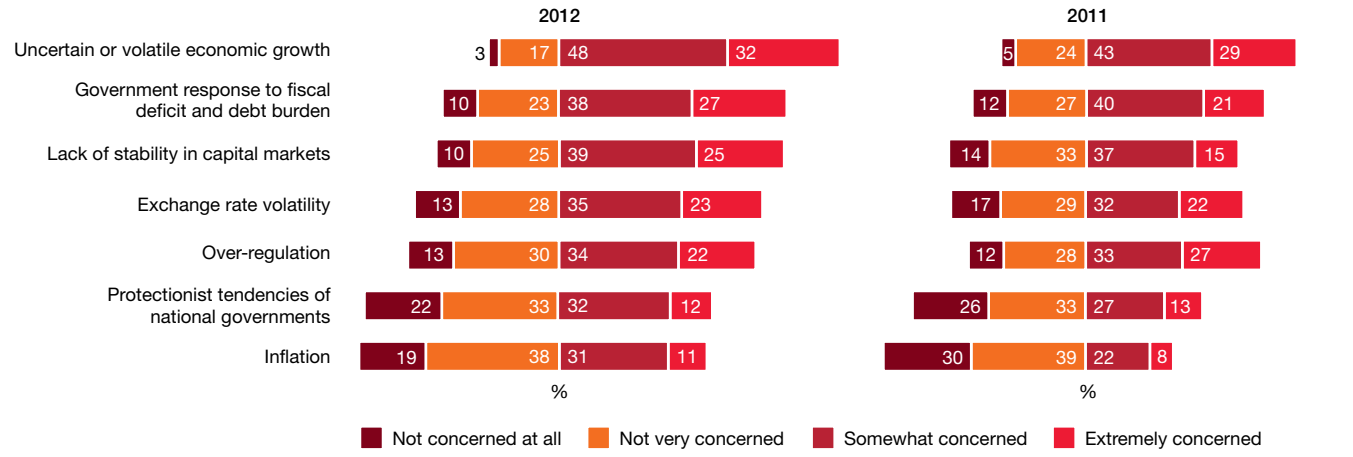
Similarly, two thirds of CEOs (64%) are concerned about **lack of stability in capital markets** – a considerable increase from last time – and particularly in Western Europe (76%, and Germany at 86%), with the Eurozone crisis weighing heavily on CEOs' minds. Of note, 88% of Australian CEOs are also somewhat or extremely concerned.

Krzysztof Gulda,
Director of the Department of Strategy at Poland's Ministry of Science and Higher Education

"Crises generally make it impossible to carry out some reforms, but on the other hand, a crisis is a good time to verify the validity of all types of expenditure. There are some difficult areas, which require open public debates."

Figure 1: Economic and policy threats to business growth

Q: How concerned are you about the following potential economic and policy threats to your business growth prospects?



Base: All respondents (2012= 1,258; 2011=1,201)

"In 2012, 80% of CEOs are somewhat or extremely concerned about uncertain or volatile economic growth."

Both of these threats feed the highest ranked concern – economic uncertainty. In 2011, 72% of CEOs were concerned about economic uncertainty; in 2012, 80% of CEOs are somewhat or extremely concerned about **uncertain or volatile economic growth**. And this is the top concern across all regions, by some margin, and for all sizes of company. Along with customer demand, this is the key driver of changes in their strategies for two thirds of CEOs (66%). In addition, 55% of CEOs in the UK, 53% in the Middle East and 48% in Scandanavia believe public spending cuts and/or tax increases will drive changes in strategy.

Very large companies appear more concerned about all of these threats, but in the same order ranking as other CEOs. State-backed companies have the same top two threats, but the third is exchange rate volatility. There are, however, differences across region with exchange rate volatility being a top three threat for CEOs in Central and Eastern Europe, Asia Pacific, Latin America, Africa and the Middle East.

But there is some **support for government action**: almost half (45%) of CEOs agree or agree strongly that the government in the country in which they are based has handled the implications of the global economic crisis effectively to date. However, this is mainly the feedback from CEOs in emerging economies (59% agree or strongly agree compared to 30% in developed markets) as well as some developed countries less impacted by the financial crisis such as Canada (86%) and Scandinavia (64%).

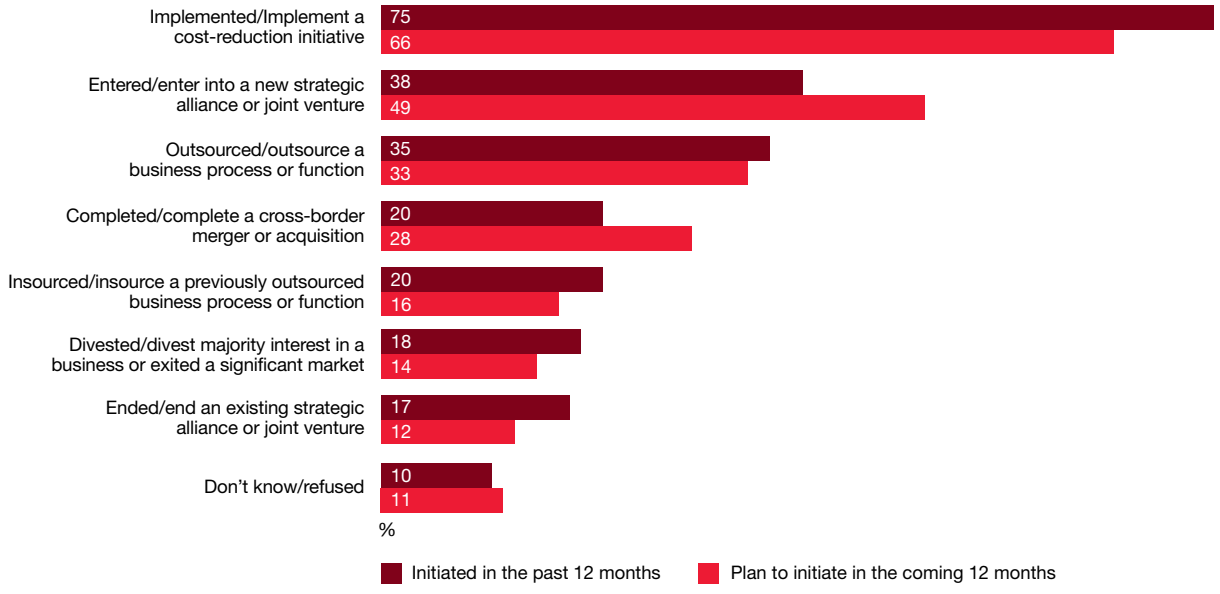
Implications for government

Views vary on what governments, individually and collectively (e.g. through the G20), should be doing in response to the impact of fiscal deficits and the contagion effects from other countries, although clearly solutions to capital market instability are urgently needed.

In the private sector, **cost reduction** has remained a key feature of business in 2011 in response to difficult economic conditions, and is set to continue (*Figure 2*):

Figure 2: Restructuring activities

Q: Which, if any, of the following restructuring activities have you initiated in the past 12 months, or plan to initiate in the coming 12 months?



Base: All respondents (1,258)

- 75% of CEOs implemented a cost reduction initiative in the last 12 months and two thirds (66%) plan to implement one in the next year.
- Two thirds (66%) of CEOs plan to increase the emphasis on their innovation portfolio in terms of cost reductions for existing processes (as well as developing new products and services, 68%).
- One third plan (33%) plan to outsource a business process or function in the next year, rising to 45% of very large companies.
- Strategic alliances and Joint Ventures (JVs) are also planned by about half (49%) of CEOs in the next twelve months.

Andreu Mas-Colell, Regional Minister of Economy and Knowledge of the Generalitat de Catalunya (Regional government of Catalonia) in Spain comments: "I'm in favour of a profound transformation of the public sector. We're making a huge effort trying to eliminate inefficiencies but it would be naïve to think that the fiscal adjustment needed in Catalonia and in Spain is going to be managed just by improving efficiency in the small; we're going to have to go much further."

Ultimately growth is needed in debt-laden economies to restore fiscal balances (see next section). However, for those battling with deficits now or seeking to avoid running up large deficits in future, the **actions needed by governments** to restore confidence mirror many of those undertaken, under way or planned in the private sector. These include cost reduction, innovation (including in public procurement), raising new revenue streams as well as improving governance and accountability and seeking transitional support.

Cost reduction – a strategic priority

When budgets come under pressure, the spotlight immediately turns to labour costs, usually the largest part of the cost base of most public sector organisations, as well as to greater sharing of services within and across organisations.

Where workforce reduction is necessary there is a need to manage it carefully to minimise the impact on unemployment, by reskilling and redeploying displaced public sector employees. There is a range of innovative workforce reforms which can be developed in response such as:

- Partnerships with private sector manpower providers to performance manage and retrain staff, to find new employment for them where possible, and to manage redundancies where it is not.
- Redesigning national public sector pay structures so that they relate to the skills and experience needed to deliver services at local and regional level rather than reflecting organisational hierarchies, which may offer a more sustainable approach to maintaining public sector employment in the places where it is most needed.
- Arrangements for voluntary reduced working hours and holding back increment-induced pay inflation.

The scope for potential savings from sharing services, particularly in the back office, is also well known but often little progress has been made because:

- The subject has rarely commanded the attention of senior managers in the public sector.

Richard O'Brien,
President and Chief Executive Officer,
Newmont Mining Corporation

"Nobody wants to talk about revenue increases or just decreasing expenses. We need to do both. As a CEO, that's what we struggle with every year, every day, and that's what governments need to do."

Marco Cuccagna,
General Manager of
Equitalia S.p.A., Italy

"Controlling operating costs and rationalisation through initiatives such as outsourcing are integrated in our immediate, short and medium-term programme and are a critical tool for the financial structural success of our group as well as the operating structure."

- No real attempt has been made to standardise and simplify many repeated processes (such as benefit payments) across the public sector – the essential precursor to making them more efficient.
- Most organisations have only looked at the issues within their own boundaries – whilst there are some shared service organisations in operation, they cover only a fraction of the whole territory.

There should be a clear expectation on all public sector organisations that they will drive down their back office costs through mandating more standardised and simplified processes across the public sector, creating a contestable market for support services (with a range of private and public sector suppliers) and separating existing public sector shared service operations from their customer organisations.

This thinking also applies across organisations within the public sector. There is a huge opportunity for public sector organisations to work collaboratively to determine how they can share their office functions to save money. For example, rather than several HR teams covering identical issues for several local governments, why not merge the function into one team looking after a set of councils? Or at a regional level, could the services of the local or state government, law and order (policing and law courts) and other regional bodies be shared?

As Lars Martin Klieve , Treasurer in the City of Essen, Germany notes: "It is also possible to optimise economically common tasks between the inter-communal corporations of the various cities or various social enterprises in order to carry out specific tasks in terms of shared services. In terms of optimising the process there are no limitations."

More also needs to be done to increase the inter-operability of standards, systems integration and enable single points of contact to be established within and across public services. Justin Riemer, Assistant Deputy Minister, Enterprise Division Finance and Enterprise in Alberta, Canada gives one example affecting business: "We're trying to provide a one-window approach to regulatory approvals in the oil and gas sector right now to look at things such as improved processing times and making it easier for the private sector to deal with government. It will be a challenge to get there and a change in culture is required, but from the outside looking in it will hopefully greatly enhance our ability to move things forward on a timely basis."

Finally, the strategic decision needs to be made as to whether to continue to provide services, shared or otherwise, in-house ('in-sourcing') or outsource them in areas like IT, HR and financial management and also in the front line.

Innovation – out in the open

There is an important challenge for government and public sector organisations – to be willing to do things differently (e.g. through shared services and outsourcing) as well as prioritising to do fewer (and different) things. As Justin Riemer in Alberta, Canada comments: "We're always looking at ways in which we can improve things and I think looking at more innovative service delivery is going to be a mantra for the future for not only our government but many others as well."

This requires a shift in mind-set for many, where risk aversion is too often the norm. Public sector leaders must challenge their existing service delivery models to ensure that they are really delivering value for money at all times. As John Bradley, Director General, Department of Premier and Cabinet in Queensland, Australia, comments: "In terms of public sector performance, we're considering opportunities to refocus service delivery through a structured innovation agenda, which seeks new user-focused ways of delivering services rather than purely a cost cutting exercise."

It is critical for public services to be designed around the needs of users, not based on traditional professional boundaries and ways of working. As John Bradley goes on to say: "We're seeing a lot of integration of our service delivery points. In the case of the Department of Communities, five agencies have recently been brought into one, and it has a policy called 'no wrong door'. The principle is that a community member who makes contact with one part of the agency, whether it's in relation to housing services or other social services, will be assisted to find their way quickly to services they need, rather than being turned away and being sent to another part of the agency."

Radical devolution of power and responsibility can produce better outcomes for much less money. New technology also opens up new avenues for innovation as more government services are provided online. Importantly, innovation can be assisted by unlocking the potential of commissioning models across government. In particular, by providing business with the right incentives and aligning profit with the needs of society, it is possible to achieve a wide range of policy goals.

Ian Watmore, Permanent Secretary of the Efficiency and Reform Group in the UK's Cabinet Office, provides an interesting example: "We have a piece of the Civil Service which administers people's pensions for them in a business called 'My CSP'. We want that to be run in the future in a three way partnership between government, the private sector pensions specialists and staff should get a stake as well. So it becomes a mutual because of the staff element, and it becomes a joint venture because the government retains and carries an interest in business when it's voted off. I think if we could do that on a bigger scale with more businesses, then what we will be doing is essentially using public sector operations to create new businesses in the economy which themselves can grow over time. So those are the kinds of innovations I think government can do, in addition to the traditional sorts of building more infrastructure."

Andreu Mas-Colell in Spain makes a similar point: "Public spending responsibilities don't necessarily have to be met through public bodies or agencies. It can be desirable sometimes that they be carried out by private institutions and in many cases in particular, by not-for-profit institutions."

As such, innovation also requires a change in buying behaviour and procurement practices, with the opening up of public service delivery and collaboration with a wider range of private and not-for-profit providers through joint ventures, alliances and public-private partnerships. Whether resources come from the public, private or voluntary sectors is a secondary issue; what matters is the service delivered to citizens and outcomes achieved. There is therefore a need to challenge the traditional boundaries between the public sector and other sectors of the economy in service provision.

Whilst, as discussed earlier, there has been much debate about this, it has in the main been limited to two specific areas: greater involvement of the private sector in providing back office services; and the potential involvement of the voluntary sector in providing services which touch individual citizens e.g. the unemployed, vulnerable or offenders. Governments can, however, go further and look to engineer more fundamental changes by making a clear commitment to diversify the range of providers in bidding for, and supplying, services traditionally delivered by the state. For instance, in the UK, the Government has stated that it wants to embed the idea of "diverse and innovative providers competing to raise standards" in the delivery of public services.[7]

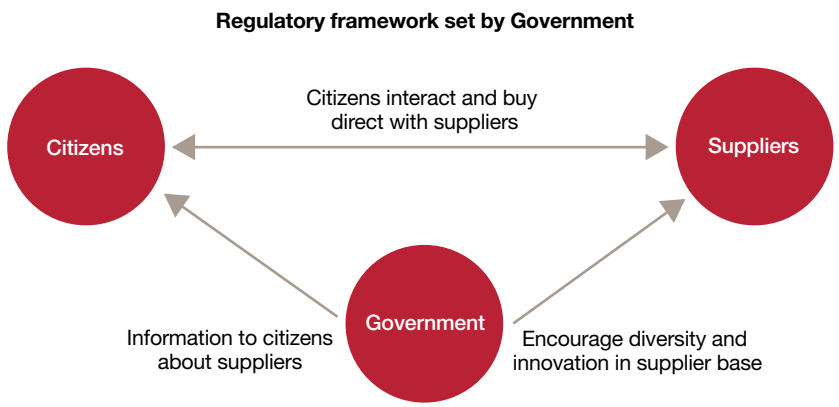
This raises, however, some important questions:

- How best will supply markets spring up in response?
- What are the incentives for private and voluntary sector providers to enter?
- What framework does government need to put in place to promote and sustain effective competition, focused on outcomes?
- And how can government ensure there is a level-playing field of competition between providers, large and small?

Shifting from old models of delivery, characterised by monopoly providers and top-down interaction between suppliers and citizens, to new models, characterised by diverse providers, greater citizen choice and more innovation would be substantial, as shown in *Figure 3*. In this system, citizens are in the driving seat, decision-making happens at the right level and the supply-chain is diverse and innovative, with multiple organisations competing to provide services.

In such an open system suppliers and citizens work in partnership within a regulatory framework set by government. This requires a substantial shift in structure, relationships, engagement and behaviours in the ecology of public service provision. It also creates a challenge of leadership for the government – how best should it encourage greater participation in the delivery of public services, resulting in greater innovation? Over time, how can it do less and encourage more of others? More immediately, it requires an investment of time in setting out the vision, building the skills required, and acting in a catalytic way to promote collaboration.

Figure 3: A new open model for public service delivery



"Whether resources come from the public, private or third sectors is a secondary issue; what matters is the service delivered to citizens and outcomes achieved."

7 *'Open Public Services'*, White Paper, HM Government, July 2011: paragraph 6.4.

Creating this new model involves three clear shifts in thinking and action, relating to: greater citizen empowerment; a more diverse public sector supply market; and a new approach to public sector commissioning. The transition set out in *Figure 4* requires change at three levels.[8] Firstly, citizens need to be empowered, by having access to meaningful information and having a say in the way services are run, for instance, through feedback as patients on their satisfaction with the outcomes of medical procedures. Secondly, suppliers need to have proper incentives, through mechanisms such as payment by results, coupled with a strong regulatory framework to ensure the fulfilment of outcomes is at the centre of engagement.

Finally, government needs to change its own approach to commissioning to encourage a more diverse set of providers based on fair competition, including promoting a stronger skill set among commissioning and procurement officials.

These changes require a much deeper, and more open form of, partnership between citizens, suppliers and government than before. As a result, government needs to re-assess its own role. As Debra Woodgate, Commissioner, Civil Service Commission in the Government of Manitoba, Canada, states: "We are all looking at what business we should be in. What is our business, what are we good at and what is the private sector good at? So I would say it is a good opportunity to really go back and say what is the business of government and what areas should we be in."

Both politicians and citizens also need to understand that such a dynamic system is not always predictable, with innovation and creativity coming from multiple sources – including citizens. In particular, accelerating the take up of new interactive digital technologies, particularly social media and other tools, can create a new interface between customers and providers e.g. enabling crowdsourcing approaches to public service design and delivery.

Critical to the management of this transformation is how best to make the new open system accountable and easy to access by the public, to which we now turn.

Figure 4: Transition to the new open model of public service delivery

	Traditional/'closed' model of delivery	New/'open' model of delivery
Citizens	Limited influence on decision-making Disconnected from service provider(s) Limited access to data	▶ Part of the decision-making process ▶ Engaged with the service provider(s) ▶ Full access to information and analysis
Suppliers	Little incentive to innovate Using size to provide multiple services Disconnected from service users	▶ Competition drives innovation ▶ Working alongside multiple providers ▶ Responsive to users and focused on outcomes
Governemnt	Monopolistic supplier or contractor Contracting based largely on price, not outcomes Disconnected from citizens	▶ Creating a framework for diverse suppliers ▶ Contracting based on outcomes and delivery ▶ Engaged with citizens

8 More details can be found on *'Out in the open: Delivering public service reform'*, PwC, 2011.

Accountability and transparency – good governance

There is a need to improve accountability and transparency both for operational reasons as well as the need to restore trust in the reputation of government for its financial management.

As public service value chains become more complex, with new players entering the market, governments must be more transparent in their reporting, to foster good governance and accountability. Our research[9] has found that true accountability is best achieved through devolving and aligning three powers: decision-making; delivery and performance; and budget setting and financial control. Any accountability regime should be responsive and open to feedback from the public.

"Governments need to step up and provide information which delivers real insight into public financial management and decision-making."

Decision-making, delivery and budget-setting need to be aligned so that the public can hold a single individual or institution responsible for decisions made, services delivered or money spent. Ultimately, the benefits of such a system are better, more responsive services that meet the expectations of the public and deliver outcomes. Crucial to this alignment is communicating the change to the public so that they are informed and empowered to challenge service providers directly, or through representatives, when expectations are not met.

Similarly, in the area of financial accountability, capital markets need to trust that governments are managing their finances effectively including the transparent reporting of debt. Most governments, however, still account on a cash basis and often do not maintain balance sheets, with little information provided about their assets and liabilities. And even where they do, off balance sheet items are an issue which can lead to under-statement: the liabilities reported do not necessarily consolidate the debts at all levels of government including at state and city level and for all state-owned enterprises. Furthermore, future liabilities like pensions often get excluded from commonly used government debt comparisons.

Governments need to step up and provide information which delivers real insight into public financial management and decision-making.[10] This requires more robust accounting systems in the public sector worldwide with reporting on a consistent basis e.g. through international financial reporting standards – IPSAS – and more comprehensive consolidation of liabilities. This will in turn assist long term stability in capital markets by increasing the quality, reliability and trust in governments' financial statements and so help restore confidence in the ability of governments to manage their fiscal balances.

Balancing the books – raising new sources of funding

There is a need for government to take a fresh look at how services are funded. There are several methods through which government at various levels can raise revenue and bring forward capital spending to finance front line services and future infrastructure projects, as set out below.

Charging

Public sector organisations in most countries already charge for some of the services they provide. Whilst there may well have been (and continue to be) good reasons of public policy for providing services free of charge, charging for public services can be seen as a way to 'share the pain' when cuts in spending need to be made, as well as 'nudging' new behaviours.

Public authorities need to ask whether there any services currently provided for free where charging would be appropriate, whether charging could be introduced e.g. to manage overall demand for a service, or differentiated e.g. charging for 'premium' elements of a service like fast turnaround. In all cases, there is a need to ensure that charges are set at the right level to cover fully absorbed, rather than simply incremental, costs.

9 'Who's accountable?', PSRC/ippr, October 2009.
10 *'Do the right thing'*, Steve Freer, Public Finance Opinion, November 2011.

Commercialisation of public assets

The public sector already raises funding for its services from many sources in addition to taxation and charges to the public and businesses. Examples include licences for use of assets and income from sponsorship and advertising. What needs to be challenged is the degree to which public authorities look to maximise value from assets and the comprehensiveness of the measures taken. Almost every public body has opportunities to generate significant additional revenue from its assets. There is a need to evaluate whether assets are 'working' as hard as they should be and identify potential revenue opportunities (see *Figure 5*).[11]

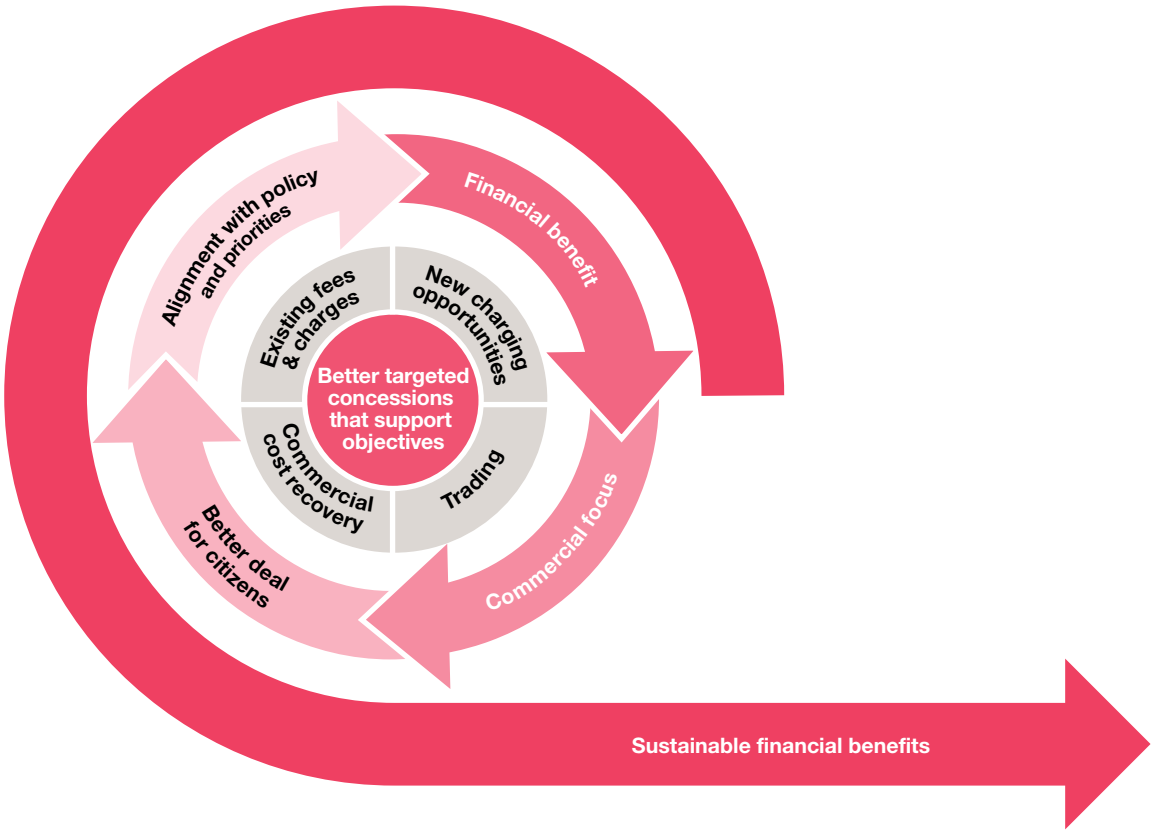
Tax Increment Financing (TIF)

TIF is a tool for financing infrastructure which is common in the USA allowing public bodies to borrow money for infrastructure projects against the anticipated increase in income expected as a result of the infrastructure project. TIF funding is merited by the extra tax revenue coming from a future development and pays for the very infrastructure that otherwise would prevent such an investment; for instance transport links or site assembly that underpin the decision of the private sector to invest.

Public Private Partnerships (PPPs)

Although definitions vary, PPPs are now a well known instrument of finance characterised by "cooperation between the public and private sectors for funding, construction, renovation, management or maintenance of an infrastructure or the provision of a service."[12] Private sector returns are linked to service outcomes and the performance of that asset over the contract life. There are risks, however, arising from poorly constructed PPP deals: as such, both government and business must work closely to fully establish the scope of projects, objectives and a method for managing the contract over its lifecycle. Strong procurement and commissioning frameworks are vital in delivering value for money infrastructure projects.

Figure 5: Revenue Income Optimisation Model



11 *'Revenue Income Optimisation: Raising more revenue'*, PwC factsheet, 2010.
12 *'Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions'*, COM, 2004, Paragraph 1, UK.

Bonds

Where national legislation allows, state and local government may consider raising finance direct from the capital markets from bond investors (such as pension funds). The ability to get an investment grade rating requires a high level of financial discipline and control in the public authority, demonstrated in the rating process. The bond issues could be linked either to a proven revenue base such as tax receipts, business rates, tolls and charges, or could be used to finance some form of regional asset base of infrastructure similar to the finance raised by the utilities, normally under some form of regulated asset base regime. There are strong arguments to consider ring fencing such assets and raising long term finance to maintain and invest in those assets to maintain the inter-generational bargain; the notion that we should leave our assets in at least as good a position to the next generation.

Another particular class of bond is also emerging – Social Impact Bonds (SIBs) – which offer the potential for private investors to provide working capital and other finance to providers to deliver new public services through outcomes-based contracts.

The assumption is that by using 'payment by results' commissioning arrangements government can use a proportion of the savings that result from improved social outcomes to reward investors that fund the intervention. Investors are subsequently rewarded if pre-agreed outcomes are achieved.

Social Impact Bonds are most likely to be applicable in situations where a new service, based on payments for outcomes, is likely to address complex social needs (such as drug addiction, homelessness or re-offending) and generate significant longer term (cashable) savings to the public sector (see *Figure 6*). Clear statements of (intervention) impacts and their relation to public spending effects, and robust commission and contract management over the lifecycle of the project are critical to attract private investor interest and generate cashable savings to support the delivery of value for money outcomes.

SIBs, along with TIFs and PPPs, are all mechanisms seeking in different ways to bring forward funds from the private sector in return for payments in future, increasingly linked to the successful delivery of outcomes.

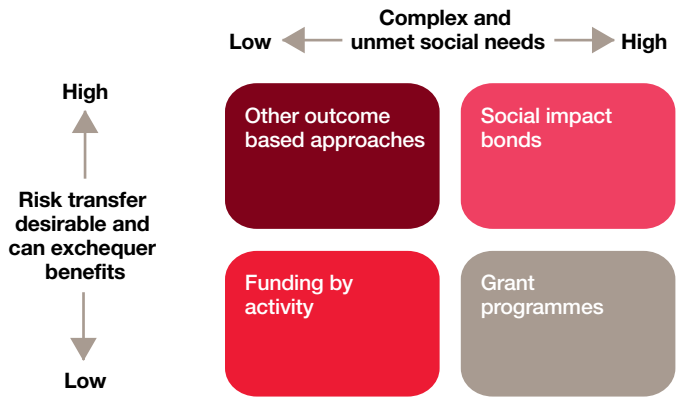
If embraced wholeheartedly, these measures could lead to a radical reshaping of how the public sector manages itself and its assets, as well as developing new ways of working with the private and voluntary sectors.

Transitional support

There is also a role for inter-government support in the transition to a more sustainable fiscal balance (before the need for crisis measures). It is not surprising to see governments in developing countries with cash reserves, particularly through their Sovereign Wealth Funds (SWFs), rising in prominence during the financial crisis. SWFs are major holders of government debt and are now being actively courted by European governments to aid in solving the Eurozone debt crisis. This prominent role is not an accident. High commodity prices and global current account imbalances mean that SWFs are growing rapidly and their ability to act as long term providers of capital has also made them attractive as investors.

Increasingly, the creation of SWFs is seen as a buffer for governments in tough times. For CEOs in developing countries, who have concerns about inflation, exchange rate volatility and bribery and corruption, SMFs also have obvious attractions (see *A key to economic success?* opposite).

Figure 6: When are social impact bonds applicable?



A key to economic success?

To understand whether SWFs have a material impact on the host economy, PwC's Macro team analysed the historic performance of 51 countries over 30 years.[13] Key findings included:

- **Setting up a Sovereign Wealth Fund may help to reduce inflation** – the presence of a Fund is linked to lower inflation, even when accounting for a number of other factors likely to affect inflation, such as monetary policy stance, the state of the labour market and the current account balance. This result is stronger for commodity rich countries than for those with a non-commodity based trade surplus.
- **Exchange rate appreciation may be lessened by a Sovereign Wealth Fund** – in countries with floating exchange rates there is a relationship between the presence of a Sovereign Wealth Fund and a weaker exchange rate. The effect was equally strong for countries with and without commodity wealth. This may occur because monies can be held in foreign currencies (often in US dollars), so not bidding up the value of the local currency.
- **Sovereign Wealth Funds may help improve transparency in an economy**[14] – the analysis found levels of transparency to be correlated with measures of economic development such as GDP per capita and the depth of financial markets. Even when these factors are taken into account, however, there are lower levels of perceived corruption in countries where a Fund is present. The effect appears slightly stronger in countries with non-commodity based trade surpluses.

PwC's View

There is a range of ways in which governments can do things differently as well as doing different things to meet the needs of citizens and businesses alike, as we set out in detail in last year's report.[15] Prioritisation, making tough choices and doing more (or increasingly the same or less) for less is the key to success where budgets need to be cut.

We believe there are five priorities for government:

- Developing and **executing plans** to achieve better balanced public finances with a twin focus on:
  - Cost reduction, particularly through standardising, streamlining and sharing services to increase the efficiency and effectiveness of enterprises, including deciding whether to make or buy goods, services and infrastructure.
  - Developing new sources of funding to cover current spending, as well as seeking to bring forward funds from the private sector in return for payments in future, increasingly linked to the successful delivery of outcomes (payment by results).
- Given the significance of labour costs in most public sector cost bases, developing new approaches to **workforce reform**, with a priority to be more active in planning workforce strategies and managing and retaining pivotal talent in order to achieve sustainable cost reduction.
- **Innovating service delivery** in particular by:
  - Opening up public services to any willing provider, which requires public sector organisations to partner and collaborate more effectively with the private and voluntary sectors.
  - Accelerating the take up of **new interactive digital technologies**, particularly social media and other tools which create a new interface between customers and providers e.g. crowdsourcing approaches to public service design and delivery.
- Improving **accountability and transparency:** critical to the transformation of public services is how best to make public services accountable and easy to access by the public as well as financially more transparent and robust. This requires reporting on a consistent basis, through reforms such as the adoption of International Public Sector Accounting Standards (IPSAS), and more comprehensive consolidation of liabilities (particularly debts at all levels of government). This will also assist stability in the capital markets by increasing the quality and reliability of governments' financial statements and so help restore trust and confidence in the ability of governments to manage their fiscal balances.
- Seeking **transitional assistance**, and future stability, through mechanisms such as Sovereign Wealth Funds.

13 *'Sovereign Wealth Funds – the key to economic success?'*, PwC 2011.
14 Based on a Transparency International measure of corruption perception.
15 *'Rethinking government: doing things differently'*, PSRC, 2011.

Enabling good growth

Confidence is key to global recovery: in business and across capital markets. So, how can governments best foster and support business to meet their growth ambitions? And what sort of growth is desired by their citizens?

Globally, **short term confidence has taken a tumble**. The proportion of CEOs 'very confident' in the prospects for their revenue growth in the next year has fallen from 48% in 2011 to 40% this year (*Figure 7*). The impact of uncertain or volatile economic growth (along with events including the sovereign debt crisis in Europe and the earthquake and tsunami in Japan) has driven this global trend downwards. In contrast, short term confidence has only held up so far in Latin America, the Middle East and Africa.

Very large company CEOs are the least likely to be 'very confident' in their short term growth prospects (29%), perhaps as they are the ones most exposed to global contagion due to the interconnectedness of their businesses. Western Europe has the smallest number of very confident CEOs at 27%.

Furthermore, 48% of CEOs believe the global economy will decline further in the next 12 months. Indeed, only about 1 in 7 (15%) CEOs believe the global economy will improve in the next year.

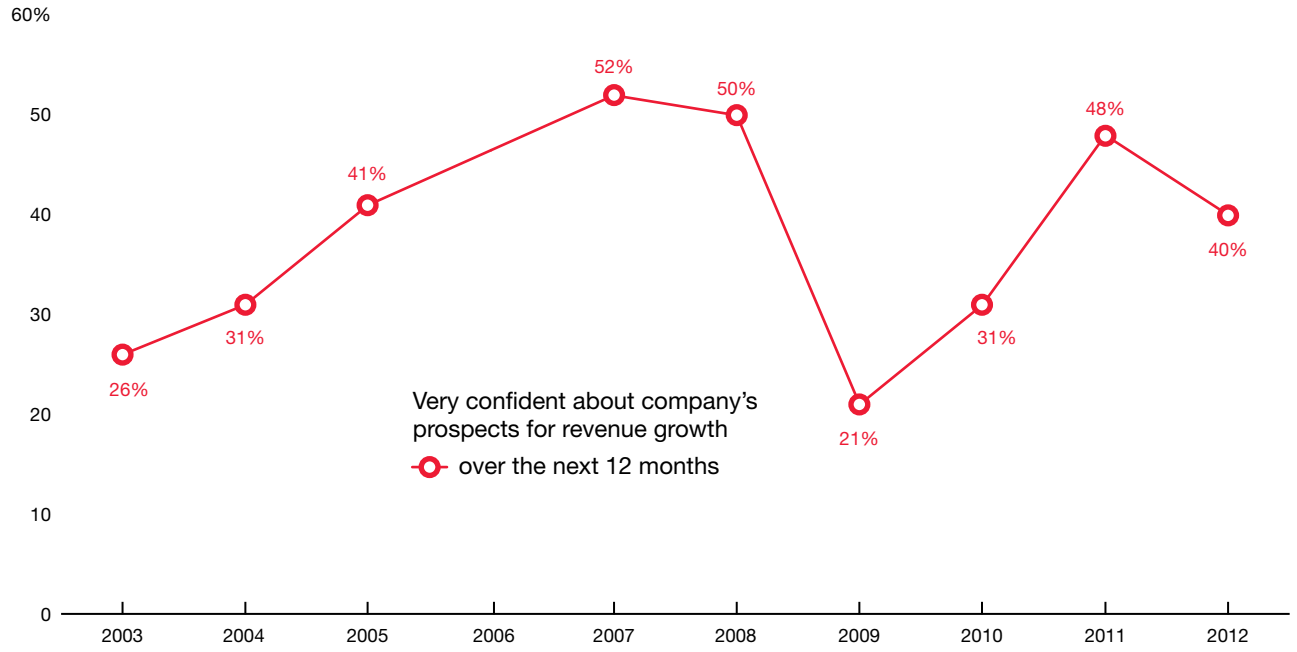
Longer term confidence is higher and slightly more stable:[16]

- 47% of CEOs are very confident in their longer term growth prospects (3 year horizon), down 4 percentage points on 2010 and similar to pre-recession levels (2006).
- 52% of very large company CEOs are 'somewhat confident'.

North American CEOs have the strongest longer tem confidence amongst developed economies, with 54% very confident. CEOs in Western Europe are least confident, expecting lower growth in their domestic markets, and are looking outside their traditional markets to developing countries for growth. Indeed, 59% of CEOs see emerging markets, particularly in Asia Pacific, Middle East, Africa and Latin America, as more important to their company's future than developed markets, especially for very large companies (73%). The BRIC economies plus the US and Germany are the top six for overall growth prospects.

Figure 7: Short term confidence dips

Q: How confident are you about your company's prospects for revenue growth over the next 12 months? Yearly comparison



Base: All respondents (2012=1,258; 2011=1,201; 2010=1,198; 2009=1,124; 2008=1,150; 2007=1,084; 2006 (not asked); 2005=1,324; 2004=1,386; 2003=989)
Note: Percentage of CEOs who are very confident about their companies' prospects for revenue growth

16 Interesting to note in an age of quantitative easing, inflation along with lack of stability in capital markets and exchange rate volatility appear to have the most corrosive impacts on longer term confidence.

Growth – where and how?

CEOs see two routes to growth: increasing market share in existing markets (30%) and new product/service development (28%) are their main opportunities to grow in the next year.

CEOs also envision a business environment defined by **growing integration** among countries and are **reconfiguring their operations to meet local market needs**. CEOs are simultaneously building local capabilities in important markets, extending operational footprints, building strategic alliances and creating new networks for new markets that include R&D, manufacturing, and services support. They are adapting how they go to market, reconfiguring processes and, at times, entire operating models.

CEOs are also **addressing the risks that greater integration creates**. During 2011, global businesses had to confront a portfolio of unrelated high-impact global risks – from political upheaval and a nuclear disaster to massive floods and a sovereign debt crisis. Through it all, CEOs have learned that prudent risk management should focus less on the probabilities of particular events, and more on understanding the potential consequences they have to prepare for from a range of risks. The challenge was the supply chain disruption from Fukushima and the Thai floods, not the events themselves.

But this growing integration does not mean that CEOs see similar convergence of government policies such as taxation and regulation – only about a third (36%) see this happening. It is also worth noting that for the first time in many years, **over-regulation** is not a top three economic and policy threat (see *Figure 1* earlier).

Nevertheless, it is still an issue for the majority of CEOs (56%, down from 60% in 2010), although it is the second biggest threat in Latin America and Africa. For instance, in Brazil, Erik Camarano comments: "As it is now we have a statistic from the OECD which says that in Brazil 31 new regulations are created at the federal level only every day and that doesn't include the states or the city level which also have a degree of autonomy let's say in terms of taxes."

Bribery and corruption is also a concern to over half of CEOs in the developing countries of Latin America and Africa (*Figure 8*) as well as Central and Eastern Europe (CEE).

Figure 8: Over-regulation, bribery and corruption, by region

Q: How concerned are you about the following potential economic and policy threats to your business growth prospects?

	North America (236)	Western Europe (291)	Asia Pacific (440)	Latin America (150)	CEE (88)	Middle East (23)	Africa (30)
Over-regulation	57	45	60	61	57	39	73
Bribery and corruption	10	19	43	56	52	48	63

Base: All respondents 1,258

The state-backed CEO

Even the most free market of economies have some enterprises in the state sector: for others, state owned or state-backed enterprises still form the backbone of the national economy. In this year's Survey, more than one in ten (12%) of our CEOs have some form of state backing. But do their views differ from those CEOs without state involvement?

In the main, the state-backed CEOs in our Survey appear to have similar levels of confidence and see similar challenges to their private sector counter-parts. There are, however, also some significant differences, as set out in *Table 1* (although these may be driven by the particular countries and sectors in our sample[17]).

In particular, the state-backed companies in our Survey are more likely to expect the global economy to improve, are less likely to be somewhat or extremely concerned about uncertain or volatile economic growth and fiscal deficits and believe their governments domestically have handled effectively the implications of the global economic crisis to date. Lack of finance appears to be the main business threat: state-backed CEOs are more likely to anticipate a major change in their capital structure and capital investment decisions over the next year and would also like personally to spend more time meeting lenders and providers of capital.

Table 1: Differences in views of state-backed CEOs

Topic	State-backed business views
Threats	• More likely than the overall sample to be somewhat or extremely concerned about protectionist tendencies of governments and bribery and corruption, although relatively more likely to expect openness to trade in goods and movement of people. • More likely to be somewhat or extremely concerned about energy costs and an inability to finance growth.
Growth	• These CEOs more likely to feel that their strategies will change in fundamental ways in the next 12 months, driven more than for private sector companies by changes in industry disruption, capital structure, risk tolerance, and shareholder expectations. • More likely to see their main growth opportunity through new product/service development rather than expanding market share. • State-backed CEOs more likely personally to want to spend more time on setting strategy and managing risks. • Less likely to have used Mergers & Acquisitions (M&A), outsourcing or insourcing and JVs/alliances in the last year but more likely to have implemented a cost reduction initiative. • Looking ahead more likely to be anticipating divestment or market exits.
Talent	• State-backed CEOs more likely to see it as difficult to hire in the industry as a whole, with greater challenges with regards to recruiting and retaining senior managers and skilled production workers. However, they are still more likely to be confident that they will have the talent they need to execute strategy in the next three years. • More likely to be looking to partner to overcome skill shortages and planning to invest over the next three years in creating a skilled workforce (as well as maintaining the health of their workforces) and believing that business in general has a role in workforce development (educating/training youths and adults who are not their employees), and more so by investing in adult/vocational training programmes. • More likely to see talent constraints as having had an impact on pursuing market opportunities, growth, innovation and service delivery as well as costs. • Also the majority of state-backed CEOs have seen headcount decrease or stay the same in the last year with most expecting this to continue next year. • More likely to believe they have comprehensive information on labour costs, staff productivity, assessments of internal advancement and employees' views and needs.

17 There are significantly more state-backed enterprises particularly from China as well as Italy and with a relatively greater proportion in the sample from banking, life insurance, industrial manufacturing, primary metals and transportation and logistics, computers, electronics and networking and telecoms; state-backed companies in our sample are also more likely to be smaller (less than $500m revenues) and established for 15 years or less.

Implications for government

Governments already know that they must respond to the top concerns of business and support growth. As noted previously, where in debt governments need to cut their deficits, and/or avoid building up future problems, whilst guarding against over-regulation and bribery and corruption particularly in developing countries.

So what are businesses' **priorities for governments**? CEOs see three clear priorities to improve the environment in which they operate beyond reducing the burden of tax and regulation (*Figure 9*):

- Ensuring **financial sector stability** (57%), particularly for CEOs in Europe and North America.
- Improving **the country's infrastructure** (53%), particularly in developing countries in Latin America, Central and Eastern Europe, the Middle East and Africa.
- Creating and fostering **a skilled workforce** (47%), which addresses CEOs' top business threat to their growth prospects (although less of a priority in Asia Pacific).

Of note, less priority is given by business to government:

- Reducing poverty and inequality (37%), except in Latin America and Africa where CEOs see this as the no.2 priority for government.
- Maintaining the health of the workforce and securing natural resources that are critical to business (both 21%).
- Addressing the risks of climate change and protecting biodiversity (17%).

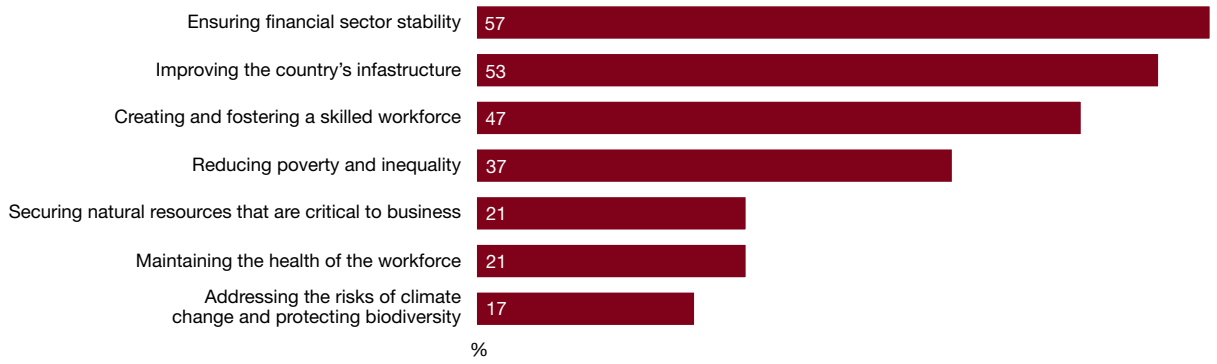
However, these issues are of importance to governments and their publics. In addition, state-backed companies place higher importance on their governments securing natural resources, addressing climate change risks and reducing poverty and inequality.

The case of health is also slightly different: CEOs believe they have a key role for the health of their own employees: two thirds (61%) of CEOs are committed to increasing their investment in maintaining the health of their workforce over the next three years. Only skills (at 71%) comes higher as a priority for investment in these areas.

There is no doubt that governments have a key role to create the **right conditions for growth**. There are, however, many dimensions to this from macroeconomic policy through to support to particular sectors and/or segments by company size. We focus below on three key areas: cites, clusters and infrastructure.

Figure 9: CEO priorities for government

Q: Which three areas should be the Government's priority today? (maximum of 3 responses were provided)



Base: All respondents 1,258

Cities of the future

Cities are a key engine of sustainable growth. But to achieve the future development of a sustainable and competitive city requires an integrated strategic approach.[18] This involves developing a clear vision, encapsulating a city's strategic ambition, and the internal management capabilities such as inspirational leadership which allow a city to prioritise, invest in and strategically manage the building blocks or 'capitals' needed by any city for long term prosperity. These include social, environmental, cultural, intellectual, infrastructural, ICT and political participation capital.

As stated in the 2011 edition of Cities of Opportunity, 'Holistic balance characterizes the top 10 cities in our rankings: all are well established centres of economic energy and intellectual vitality. Although dispersed among four continents, their common bond is depth: of economic infrastructure and networks; of law and jurisprudence; of commercial protection; of educational systems and cultural foundations; of civic organizations; and of social security.'[19]

And more than ever before the growth that cities can achieve is strongly linked to their power to address social, environmental and economic issues in a holistic manner, whilst making the most of future opportunities. This includes the development of 'smart cities', with a new level of cross-sector collaboration driven by a focus on clean technologies, energy efficiency and sustainability. But the most pressing challenge for many cities now is how to make this happen and turn city visions into reality (see *Leadership is not enough* below).

Leadership is not enough

There is one standout internal capability driving strategy implementation in cities and local governments: **leadership**[20] – top level sponsorship is an absolute requirement. But leadership on its own is also not a panacea. Public service outcomes are no longer dependent on the one, but the many, both within and across organisations. With a proliferation of public, private and voluntary sector organisations working together in partnership to deliver public services, all stakeholders – internally and externally – need to be aligned in order to maximise the chances of success. And in an era of fiscal austerity for many local governments, now is a time to prioritise and focus, both on outcomes and on the challenges of financing their delivery as well as increasing their agility and the ability to get things done quickly.

Figure 10: Capabilities to execute strategy

18 *'Cities of the future – global competition, local leadership'*, PwC, 2005; also summarised in *'Rethinking government: Doing things differently'*, PSRC, 2011.
19 *'Cities of Opportunity'* Partnership for New York City/PricewaterhouseCoopers, March 2011.
20 *'Making it happen: A roadmap for cities and local public services to achieve outcomes'*; PSRC, 2011.

The lessons from city management can equally be applied nationally particularly the need to:

- Engage businesses, and citizens, through inspirational leadership and clarity of vision.
- Invest in the multiple internal capabilities needed to succeed and deliver more efficient and effective public services.
- Develop and enhance the nation's 'capitals'.
- Execute strategy efficiently.
- Collaborate more effectively with others, be they governments, citizens, business, academia or NGOs.

Clusters of innovation

Clusters of economic activity are key to competitiveness. Hundreds of high tech jobs are created every day thanks to the ability of companies and workers to absorb new technologies and new consumer demands. This year's CEO Survey reinforces the importance of innovation: two thirds of CEOs plan to increase the emphasis on their innovation portfolio in terms of both cost reductions for existing processes and developing new products and services.

As observed by the TechAmerica Foundation following the recent economic crisis, those regions with strong world class clusters have recovered from the downturn much faster than regions without structured clusters.[21] Facing international competition, pressure on access to key resources, global warming, food security and safety issues, productivity gaps, new technological and scientific breakthroughs and new customer habits, governments need to design appropriate strategies to develop new, globally competitive advantages in emerging industries. This requires business framework adaptation, supportive innovation policies, new risk absorption capacity and excellence in cluster policies.

This is a huge and complex task which needs an effective national innovation strategy (see *Designing an Innovation Nation* below).

Designing an Innovation Nation

Companies will invest in emerging industries that are growing at a faster rate than the overall economy. Such industries usually emerge when: customers need a change; the customer base is not fully established; new technologies replace older ones; or new socio-economic conditions emerge. Such industries are also characterised by new supply chains with limited stocks, reduced number of intermediaries, real time data and product management flow and critical delivery time. Clear examples of this new wave of industries propelled by the rise of new technologies, new societal needs and changing economic models include mobility, eco-environment, creative industries, health and ageing, security, education and food for the future.

Emerging industries suffer from uncertainty over market acceptance of their new technologies and over their sustainability and return on investment. As such, specific framework conditions are often required to see them really take off: a favourable regulatory and tax environment, specific public procurement programmes, newly designed engineering education programmes, new prototyping and demonstration units, seed capital and financial risk absorption capacities.

Our extensive research and experience with governments, multinationals, start-ups and venture capitalists has identified some critical success factors for a successful 'Innovation Nation' including:

- The development of a 'Penta Helix' approach involving government, universities, the private sector, enthusiastic citizens and not-for-profit institutions in the definition of local, shared visions, a well proven local innovation chain and a strong commitment of the public and private sectors to execution of the agreed strategy.
- A review of the innovation financing chain to ensure the full availability of capital from research to commercialisation, with the provision of public and private capital.

Rob van Gijzel, Mayor of Eindhoven in The Netherlands comments: "The basis of our success is the open innovation strategy which enables companies to combine knowledge and investments in the pre-competitive stage which results in smaller risks, a faster process and standardisation. This in turn leads to a faster application of technologies in society without wasting energy on competition and double development processes. Very smart but also desperately needed, considering the challenges we are facing worldwide!"

21 *'Cybercities 2010 : The definitive analysis of the High-Technology Industry in the Nation's top 60 cities'*, TechAmerica Foundation, 2010.

Infrastructure

For any modern economy to function effectively and competitively, government needs to ensure that there is adequately developed and maintained infrastructure. Well targeted infrastructure spend facilitates economic growth (see *Infrastructure as a driver of economic growth* opposite).

In Brazil, Erik Camarano comments: "What's happening is that this is fostering growth in several key infrastructure areas which are old demands that we have in Brazil, like paving and building new roads, building turbo electrical plants and hydro electrical plants, and now also investing in increasing the lanes in the airports and infrastructure for the airports. We're running to reach the award of the football World Cup in 2014 and also the Olympic Games in Rio in 2016."

Clearly there are some limits: if a government spends its entire budget on infrastructure, funded by punitive taxes, then this will not facilitate economic growth. However, hard infrastructure, such as road and rail networks, is always an important factor influencing firms' decisions of where to locate. As noted by Lars Martin Klieve in Germany: "In the past, our strong infrastructure attracted investor confidence in Germany increasing our strength, but today it is apparent how our infrastructure is suffering adversely thus also affecting investor confidence in Germany."

Ian Watmore in the UK also comments: "Infrastructure has got a long term payback, but you've also got the short term effect of the jobs in construction and other industries, but also you make your country a better place in which to do business, so other people then follow and stay." In addition, reliable utilities such as electricity, water and sewage, together more recently with telecoms and internet provision, are essential for economies looking to attract new businesses.

It is also important to recognise the non-economic effects of infrastructure spending. In the case of non-transport infrastructure spending, more reliable electricity and clean water, sewage and good internet access improves standards of living vastly, particularly in developing countries. Transport infrastructure spending also improves people's quality of life either by making travel more comfortable and safe or by reducing travel time to allow people to spend more time on whatever they want to do. A balanced and integrated infrastructure programme is the key to facilitating economic growth.

But this growth must also meet not only the needs of business but also of the country's citizens as well as the global community.

Infrastructure as a driver of economic growth

The question of whether government infrastructure spending drives economic growth has a long history. Aschauer in his seminal paper[22] claimed that a lack of public investment in capital caused productivity growth to slow down in the 1960s-70s. Economic literature suggests, on balance, that well directed public infrastructure spending does drive economic growth both at a national and regional level.[23] It also appears that infrastructure is most important for developing countries, which mirrors the calls for CEOs in these countries who see it as a priority for government.

Why is this the case? Not just because of the multiplier effect of the spending – because all government spending will have a multiplier effect. Infrastructure spending has effects on top of the initial multiplier. For instance, in the case of transport infrastructure spending, improving transport links opens up new labour markets for firms and lowers their costs, thereby increasing employment and growth. Similarly, reducing the time it takes for someone to travel to a new area means they are more likely to want, and be able, to work there. In addition, improving transport links lowers the cost of transporting goods and materials from one place to another, making some unprofitable transactions profitable. This can also facilitate the creation of new businesses.

Furthermore, it is clear that other types of infrastructure investment integrated with transport infrastructure are also vital for growth. If a country has good transport links but poor telecommunications or regular power cuts, then businesses are unlikely to locate to these areas. Proximity to infrastructure facilities like airports and motorways are integral to business location decisions. In addition, proximity to good hospitals, schools and reliable utilities has a major impact on where workers want to live, and so firms are likely to want to locate nearby.

Good growth or any growth?

The financial crisis demonstrated the risk of economic imbalances and going for growth at any costs. In 2010, 72% of CEOs agreed or agreed strongly that they would actively support new government policies which promote 'good' growth i.e. growth that is economically, socially and environmentally sustainable.

Minister Idris Jala in Malaysia comments this year that: "The government must encourage and provide a viable environment for the private sector to become the growth engine of the nation's economy. Increasing government spending to spur economic growth is clearly not sustainable and recent events in Europe have clearly shown the need for 'good' growth." Ian Watmore in the UK also notes: "One of the crucial policy areas for governments is to get some sort of growth agenda but it's got to be based on sustainable and substantial wealth creation, and a sense of fairness amongst the populace for when they're stimulating the economy."

22 *'Is public expenditure productive?'* David Alan Aschauer, Journal of Monetary Economics 23 (1989) 177-200.
23 PwC working paper: *'Does Government Infrastructure Spending Drive Economic Growth?'*.

Good Growth

One of today's great policy challenges is achieving balanced growth that is financially, socially and environmentally sound. For those still emerging out of recession, understandably policy makers and commentators are focusing on quarterly gross domestic product (GDP) as the key barometer of economic health. But GDP as a meaningful measure of wellbeing and success is being challenged – by economists and leading thinkers in and outside of government in both the developed and developing countries.

Our contribution to the national and international debate on measures of wellbeing that look beyond GDP – the Demos-PwC 'Good Growth Index' – gives the UK public and business a key role in determining priorities for economic success . The findings of our research, undertaken in collaboration with the think tank Demos, shows that the UK public (and business) takes a wide view of economic success.[24] For the public, 'good growth' means jobs and income, although this only accounts for a third of what the public thinks is important to good growth. Similarly important are:

- **Good health:** people need to be healthy enough to work, and stay in work, particularly as retirement ages increase.
- **Work-life balance:** when forced to make trade-offs this assumes greater importance, with the UK public willing to sacrifice income to spend more time with family and friends.
- **Adequate infrastructure:** particularly transport and affordable housing.

But what is '**good growth**' and how can government act to foster it? Research we have undertaken in the UK shows that the public believes there is a scorecard of factors, particularly jobs, income, health, work-life balance and infrastructure (see *Good Growth* above). The challenge for policy makers is to factor these views into the formulation of national growth and local economic development strategies.

The role of government is increasingly as a facilitator, enabling the private sector to grow. This is neatly summed up again by Minister Idris Jala: "I absolutely believe that the private sector knows best how to conduct business. What the government must do is to act as the catalyst to encourage growth in 'good' sectors, and ensure via infrastructure and policy. Once growth has reached a self-sustaining 'tipping point', the government must adopt a hands-off approach, playing the role of the facilitator."

Frederik Rosengren in Sweden also notes: "I think most companies, Board members and so on are interested in helping to build a good society but then they have to know what kind of society do we have to build. I believe a key factor is that the politicians should define what kind of society we would like to have and then involve the companies, how could we best help you out to create a society which is good for all of us."

24 *'Good growth: a Demos and PwC report on economic wellbeing'*, Demos, 2011.

PwC view

There is no doubt that governments have a key role to create the **right conditions for growth**. There are many aspects to this but we emphasise three key dimensions:

- The role of **cities** as engines of sustainable growth, which require support to help build the capitals needed for long term prosperity: social, environmental, cultural, intellectual, infrastructural, ICT and political participation capital.
- Clusters of economic activity are key to competitiveness. Governments need to design **national innovation strategies** to develop new, globally competitive advantages in emerging industries through business framework adaptation, supportive innovation policies, new risk absorption capacity and excellence in cluster policies.
- For any modern economy to function effectively and competitively, government needs to ensure that there is a well maintained **infrastructure**. A balanced and integrated infrastructure programme is the key to facilitating economic growth.

The financial crisis has also shown the risk of economic imbalances and going for growth at any costs. Delivering 'good growth' requires attention to be focused away from narrow definitions of GDP to a **wider scorecard of factors** which in many cases overlap with business concerns and create a joint agenda for action particularly on jobs, income, health, work-life balance and infrastructure.

This in turn requires **more effective collaboration**, with governments working more closely with each other, with business and private benefactors and with citizens. For example:

- Public-business collaborations can make things happen on the ground e.g. the joint programme between the governments of the UK and Sweden on 'Innovation against Poverty' – to build the capacity to innovate, invest and create jobs through Small and Medium-sized Enterprises in Africa, Latin America and the Middle East. Effective collaboration requires the primary stakeholders to set joint outcome targets, whilst the public sector needs to build new partnering competencies and professionalise performance monitoring and management.
- Public-public: particularly national and city governments e.g. creating smart cities with business, and creating jobs as a result.
- Public-citizen collaboration: new technology and social media can be used more effectively to increase government/citizen interaction and co-design policy and delivery.

Finally, in those economies with greater state ownership of business, there is a need for a **revitalised, more radical approach to the role of state owned entities** (SOEs):

- SOEs should not be run as private stock exchange companies given the different business logic and task – state-owned firms have state aims to pursue, whilst those with minority state involvement e.g. some part-nationalised banks, can be guided in their corporate aims by government to foster the 'good growth' agenda. As Dr. Pailin Chuchottaworn, President & Chief Executive Officer of PTT plc in Thailand, commented: "Being a state enterprise – a national oil company – our first duty is to guarantee energy security for the Kingdom of Thailand. Our second duty is to contribute to the sovereign wealth of the nation. And our third duty is to ensure sustainability for the organisation. Sustainability, as I use the term, means that we must have the economic resources to ensure our continuity, and – being a state enterprise – we must maintain the support of the public, which grants us our 'license to operate.' Because of the nature of our business, which involves the use of public resources, public approval is vitally important to our company's success."
- SOE's primary task is therefore not just to generate a financial return on investment (ROI) to the government in the short and long term – it is value creation through the right investments creating a long term sustainable and competitive advantage for the nation.
- SOEs need to be actively owned, directed and evaluated in a holistic way including e.g. from human, social, environmental, intellectual and financial perspectives. A focus on costs and revenues is not enough: cost-benefits, outcomes and societal impacts are all vital parts of the future scorecard of SOEs.
- SOEs also need new principles for corporate governance covering the roles of owner, board of management and supervision, CEO and auditor regarding tasks, roles and internal collaboration to minimise the disruptive impacts of day-to-day state involvement/interference.

The talent crunch

Last year's CEO Survey revealed the need for businesses to focus on talent management. Workforces need new skills to keep up with new technologies and more creativity to bring new products to market. Employees are changing their expectations about what makes for a desirable employer. But why are organisations (in both the private and public sectors) still finding it so difficult to attract and best utilise talent? And to what extent are talent shortages costing organisations money (higher costs, lower productivity and lost revenue opportunities)?

Theoretically, finding a good candidate to fill a position should be a near-frictionless exercise today. There have never been as many educated people in the world, and social networking sites create instant access to this vast pool. Technological advances mean more functions can be done remotely – or can be outsourced to secure what was once very difficult to attain: highly-specialized or lower-cost resources.

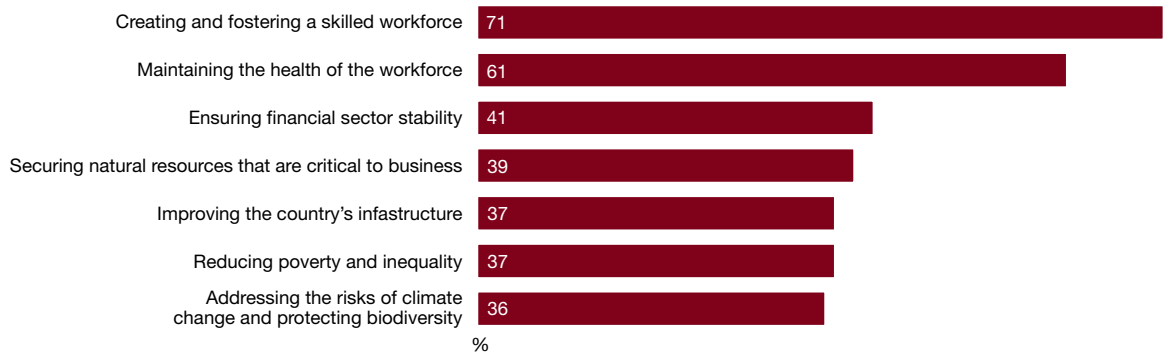
Nonetheless, the talent crunch persists. In a survey of more than 200 HR executives at global companies, recruitment group Alexander Mann found that 55% had experienced difficulties recruiting in the last six months and 70% per cent attributed this to a skills shortage in the talent pool.[25] Breaking this down to specific skills, a survey of the impact of talent shortages on the global labour market by Manpower shows that 22% of employers globally say their applicants lack the technical competencies or "hard" skills needed for the job, while candidates' lack of business knowledge or formal qualifications is the main reason identified by 15% of employers.[26]

The need for skills

It is a complex and frustrating challenge for business leaders, and **tops the CEO agenda**: the number one investment focus for CEOs globally is on creating and fostering a skilled workforce. 71% of CEOs expect to make 'a significant' or 'some' increase in investment (*Figure 11*), particularly CEOs in Latin America and Africa (87% and 90% respectively). And three quarters (78%) of CEOs plan to make changes to their strategies for managing talent.

Figure 11: CEO priorities for their investment

Q: How much does your company plan to increase its investment over the next three years to achieve the following outcomes in the country in which you are based?



Base: All respondents 1,258;

25 *'The self-imposed talent shortage'*. Griggs, Financial Times, 2011.
26 *'Talent Shortage 2011 Survey Results'*, Manpower Group.

CEOs are finding it **difficult to source the talent required** to deliver growth:

- 1 in 2 (54%) are extremely or somewhat concerned about the availability of key skills as a business threat to growth (equal in importance as a threat to an increasing tax burden), although less than half of CEOs in North America and Europe see this.
- 43% of CEOs believe that it has become more difficult to hire workers in their industry (although only 32% of Western European CEOs think this); small and medium sized companies are facing the greatest challenge in recruitment.
- Only 30% of CEOs are very confident that they will have access to the talent needed to execute their company's strategy over the next three years. The higher the CEO's confidence with regards to access to talent to execute strategy, the higher the confidence about the company's long term growth prospects.
- The number one people challenge for CEOs globally is recruiting/retaining high potential middle managers in both developing and developed economies: 1 in 2 CEOs (53%) see this as the greatest challenge.

Talent constraints are also having a real impact on growth and profitability: about a quarter of CEOs (29%) were unable to pursue market opportunities and 43% of CEOs have seen labour costs rise. Indeed, confidence in revenue growth over the next three years is higher than confidence in the talent needed to execute over the next three years.

But why? Clearly, talent is vital to global competitiveness and a key risk: innovation and talent are two sides of the same coin – you cannot innovate without the right people and one third of CEOs saw reduced innovation as a consequence of talent constraints.

Some **key actions** are being taken by business to address their talent needs. The main actions are within companies. In particular, two thirds (67%) of CEOs plan to develop and promote talent from within their workforce, and 70% plan to recruit local talent wherever there is a need to address skills shortages.

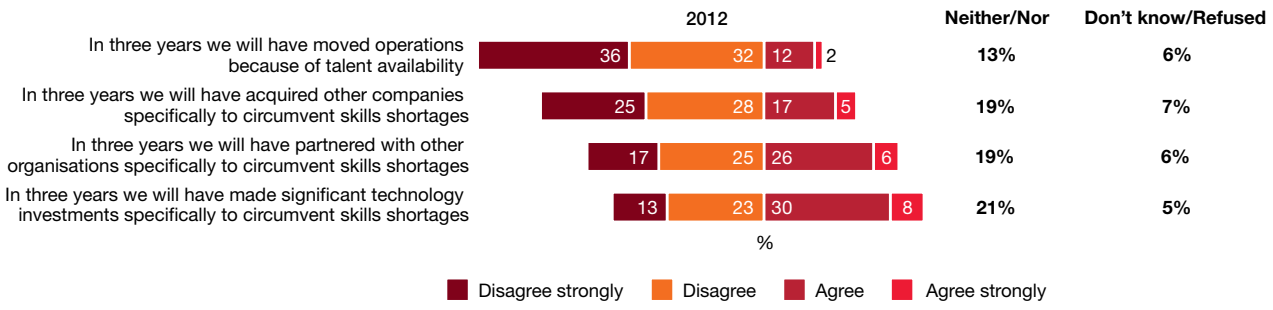
In addition, technology investments and partnerships are seen by a third (38% and 32% respectively) of CEOs as the type of changes needed to circumvent their skills shortages. Fewer CEOs see the need for acquisition or shifts in operational bases as a solution (*Figure 12*).

CEOs face a challenge, however, to monitor and evaluate their investments, with a desire to receive more information on all areas of their investments: only for labour costs is there comprehensive information (and then only for 48% of CEOs). In addition, two thirds of CEOs (68%) view developing their leadership and talent pipeline as their second most important priority on which they would personally like to spend more time (first was meeting customers, by one percentage point).

Of note, government immigration policy is only a significant factor in site decisions internationally for 17% of CEOs; in contrast tax policy is 'significant factor' for 44%.

Figure 12: Circumventing skills shortages

Q: To what extent do you agree or disagree with the following statements about the future of your global workforce?



Base: All respondents 1,258

Implications for government

There are two implications for government: one in terms of the role government has, jointly with business, in overcoming market skills and talent shortages; and another for the public sector itself in recruiting and retaining its own workforce to undertake its core functions.

Collaboration between business and government

Business takes a wide view: 4 out of 5 CEOs (84%) believe business has a wider role in workforce development i.e. education and training of youths or adults beyond their own employees, particularly in emerging countries (90%). Most CEOs (78%) are making direct investments to make this happen, particularly in Latin America (95%) and Africa (97%).

Businesses do therefore appear to see a win: win in collaborating more with governments and so improving the quality of their workforces and their talent pipeline. 69% of CEOs invest in workforce development primarily to ensure a future supply of potential employees, and 55% to improve the overall living and working conditions where they operate. As Alma Powell, chair of America's Promise Alliance, stated in The Wall Street Journal: "It is in their [employers] interest to ensure we have workers in the future who are educated and employable."[27]

This is part of a wider trend we have observed with businesses reaching back further into the talent pool and seeking to 'grow their own', with a growing proliferation of employer-led universities and colleges. Indeed, over a half of CEOs say that they are investing in adult/vocational training programmes (58%) and formal education systems (54%). Poland offers an interesting example of collaboration between government and business (see *Higher Education in Poland* below).

And this is not a case of government forcing collaboration. Percival Manglano, Regional Minister of Economy and Treasury of Comunidad de Madrid (Regional Government of Madrid) in Spain comments: "I don't think it's the role of government to force companies to cooperate with universities. If they find some added value and universities offer training that businesses need then they will do it because it's in their interest. But I don't think governments should try to enforce that type of cooperation. What government can and should do is ensure that universities, especially public ones, offer the best education and research services."

Higher Education in Poland

According to Krzysztof Gulda, Director of the Department of Strategy at Poland's Ministry of Science and Higher Education: "Less attention is paid now to the learning process and greater attention is paid to learning outcomes. It is important to note the kind of attitudes that will be shaped during that process of education. This change in my view should bring closer together the university's provision with what is expected by employers. Our research showed that students go to employers overloaded with knowledge, but lacking the ability to use this knowledge and draw conclusions. First of all, there is a lack of analytical skills, and the ability to form conclusions, views and process large amounts of data. Students are also deprived of soft skills such as: self-presentation, managing their own time and teamwork. All these features must now be included in the descriptions of these new studies and later executed as acquired skills.

Another change is the admission of people from outside the university, not belonging to a group of academic teachers, to lead classes. We try to involve specialists from various disciplines in the teaching functions, so they lead classes and workshops. Generally the rule is to allow a more business-based environment at the university through the creation of systems of teaching and through the possibility of participation in the teaching process.

For national vocational schools at bachelor's level are created even legal opportunities, so that local businesses can have their representatives on the governing boards of these schools. We are trying to bring closer in this way the business environment to universities, so that the final product as a graduate fits more with the expectations of the employer."

27 Wall Street Journal, 18 July 2011.

There are increasing examples of a new type of public-private partnership involving a more active, strategic role being played by business in education. For instance, Pearson – which owns exam board Edexcel in the UK – and is planning to start offering vocational degrees with a further education college.[28] In India, Walmart has established some free academies to train future store workers in a joint venture with a local conglomerate. And the opening of P-Tech, a six year high school, in large part created by the IBM International Foundation, where students can earn a diploma and an associate's degree in a computer science related field and have first crack at a job with IBM.

This year's interviews in the Far East demonstrate further this trend. In Malaysia, Minister Idris Jala comments: "There are many examples of industries that are working with education institutions to ensure the workforce is industry ready in Malaysia. Strand Aerospace Malaysia is working with local universities on their curriculum to ensure that the human capital is industry ready upon graduation. This is just one example of a PPP in Malaysia. Intel Malaysia, a leader in microelectronics has been working with local universities all over Malaysia through curriculum development, offering their engineers as teaching staff for industry relevant subjects in addition to grants and fellowship to students in local universities.

To achieve our ambition to be a high-income nation with industry ready human capital, we hope to see more PPPs between private companies and education institutions at various levels."

Mary Ann Lucille L. Sering, Commissioner/Vice Chairperson of the Climate Change Commission in the Philippines provides another example: "We're pushing for example the Philippines to be a green manufacturing hub. We have now entered into a partnership for one local big bus company here who wants to replace or introduce electric buses. Because they know that there's not a lot of these skills they're helping the Climate Change Commission together with the Department of Education to provide a curriculum in the private sector and also to provide some financial support in that sense because they know they need that skill. So that's the kind of partnership arrangement we're working with them on."

Many businesses that work in developing countries are keen to spend on training and development, compared to those mainly dealing with richer countries, because these markets are growing faster and fewer people come out of the education system "work-ready".[29] Mr Baba Kalyani, Chairman and Managing Director of Bharat Forge Ltd, India commented: "Two years ago, we started an Industrial Training Institute (ITI) in Khed in partnership with the Maharashtra government. Today, it is the number one ITI in the country and has benefitted Khed greatly: people are getting jobs that pay INR 15,000 a month."

Not all countries, however, are keen on this trend with some arguing that direct involvement of business in education results in short-termism as business is more focused on the 'here and now', rather than providing a broader education base to equip people better in the longer term. As Yvonne van Rooy, President of the Board of Directors, University of Utrecht in The Netherlands states: "We are responsible for the high quality of the course. It's not the private sector asking and we deliver, because then we have to risk that it's all getting too practical. We have the Universities of Professional Education and they are in much more closer contact with the private sector, because they really educate for a specific profession." Coen Teulings, General Director of the Dutch Central Planning Bureau in the Ministry of Economic Affairs, Agriculture and Innovation adds: "The concept of companies sponsoring research in universities doesn't work – research should be university, not industry, led."

28 BBC News (12 December, 2010) Publishing giant Pearson looks set to offer degrees.
29 *'Got Talent. Competing to hire the best and motivate the rest'*, Special Report, September 2011.

Another trend is the increasing interest in applying tried and tested mechanisms for collaboration across sectors. For instance, the use of apprenticeships outside more traditional craft skills e.g. in fast growing services markets like the professions (see Box on *Higher Apprenticeships*). Svein Kristensen, Director General of the Norwegian Tax Administration (Skatteetaten) comments: "It is definitely possible to develop further the relationship between government and municipalities and business to get better and more relevant education. Particularly for those who are not so academic or theoretical, as they also must get a good basis of education. For example the apprenticeship scheme is administered in close cooperation by the both the school and industry and commerce."

Justin Riemer in Alberta, Canada adds: "We have an industry apprenticeship training board that's made up of leaders within industry that regularly consult with the post-secondaries on the types and needs and requirements for industry for that particular area. We train more apprentices in Alberta than any other jurisdiction on a per capita basis. We have 10% of the population, but we turn out something like 20% of the apprentices in the country."

In addition, demographic changes are variously impacting on economies, alongside barriers to certain labour markets ranging from older workers to gender-based differences, with female labour market participation tending to be lower in most countries than for males. Frank van Massenhove, CEO of PMV – Finance, Vlaanderen in Belgium comments: "Of course, the biggest problem is to let people work longer in their career. There is a real problem in Belgium because a lot of people after fifty-five are not working and mostly women. Less than half of the active female population above fifty-five is working and this is a real problem." Yvonne van Rooy in The Netherlands notes: "What is not sufficiently developed yet is the lifelong learning process. There is a lot of post experience education but, for instance, to keep people over 60 years old vital in their work, that's I think a new area to be developed which is very important, given this prospect of our aging society and shortages on the labour market."

Clas Olsson, Chief Analyst at the Swedish Department of Employment adds : "There have been a number of reforms in recent years to stimulate people to work longer. Lower payroll taxes for people who are above sixty-five and so on, but the age at which you retire is not fixed anymore in the law. We have a pension system whereby you can have more per year if you work longer and you will have less per year if you go earlier. So it is flexible… and it is up to the individual to decide."

Higher Apprenticeships for UK professional services

Apprenticeships are work-based training programmes that offer a combination of on and off-the-job training leading to nationally recognised qualifications. PwC is leading work for the UK Government to create a new Higher Apprenticeships programme for the professional services.

The aim of the programme is to create a nationally recognised, accredited, work-based route to high-skill careers in the professions for young people and adults who want to earn whilst they learn. The programme will provide employers of all sizes with an important new channel for recruitment and development: it will enable them to tap into a broader, more diverse talent pool; and give them the opportunity to play a more active role, earlier in the careers of their current and future workforce. As such the programme represents an important opportunity for employers to improve diversity in the workforce, and to ensure that the workforce is equipped with the blend of business skills required in a modern professional services environment.

The new programme will include distinct occupational routes for the audit, taxation and management consultancy professions, closely aligned with the professional standards and qualification pathways maintained by the relevant professional bodies – enabling students to work towards chartered status as part of their Apprenticeship programme.

Another key strand of the programme is the development of a learning and development delivery model to support a blend of different learning styles and channels including face-to-face, peer and e-learning. Employers will be able to access the new programme from autumn 2012; it is expected that some 1,500 Apprentices will join the new programme over the period to March 2015.

However, countries do have different experiences. For instance, Svein Kristensen in Norway comments: "I see the need for interventions in the market, for example to ensure we use all the available talent. For example in Norway, we have a high participation of women in the workforce: we have come a long way, even though there are still some challenges with regards to gender. Examples are interventions to ensure 40% female board representation for all ASA companies. In Skatteetaten we have targeted more women in leadership positions and I will say we have come far. Furthermore, we have come far in ensuring broad ethnicity – more cultures in our workforce. We have not, however, succeeded so far as we hoped with regards to disabled workers."

PwC view – collaboration between business and government

There are a number of areas where businesses, governments and educational establishments need to work more actively together to co-create solutions to meet business needs:

- Develop course curricula and training programmes which equip people with a range of **'employability' skills** as well as their particular subject matter skills and expertise. Given the rise in youth unemployment in a number of developed countries, help is needed for young people particularly where they need to access 'entry level' (often unskilled) jobs – a commitment to hard work, presentation and punctuality are every bit as important as basic numeracy and literacy.[30] In addition, communications, teamworking, analytical skills and innovative thinking are highly valued by business.[31] as well as the relevant professional or technical skills for a given occupation. Training programmes should have these employability skills embedded within them so that individuals emerge with the full package of skills they need in the world of work.
- **Developing new career pathways** which provide (particularly for young people) recognised, credible routes to high-skill careers. This involves reducing the barriers to entry and increasing access of candidates to opportunities e.g. by lowering the cost of vocational degrees and technical education programmes, which enables employers to tap into a broader, more diverse talent pool. Employers also need to step up and take a lead on this where they are lagging by playing a more active, direct role in the development of the employability and business skills that they need. International experience shows variable engagement. Apprenticeship pathways are a good example: these are well established and supported in some countries but not in others. For instance, whilst the UK has 6% of young people taking the one-year apprenticeships this lags notably behind German-speaking countries, where at least 40% of school-leavers are taken on by employers in three-year apprenticeships leading to a recognised qualification. The so-called dual-system countries[32] show corresponding benefits for youth unemployment which stands at only half the level of the 19% reported for the UK in 2010.[33] Higher Apprenticeships are being developed in some countries like the UK as one solution to this issue. For governments, the development of such pathways has an important role to play not only in tackling youth unemployment but also increasing social mobility.
- Creating a **single market for training**, irrespective of the funding source (public or private), as is happening in the UK with the launch of an investment fund of £250m for employers. There needs to be an integrated approach to encourage investment and maximise the returns.
- **Tackling untapped and under-utilised talent pools** which could boost productive potential. In particular:
  - Reducing the barriers to labour force participation faced by women in many countries, especially Africa and the Middle East.
  - As populations age, and state pensions ages rise, a wider programme of change is needed if an ageing workforce is to be kept healthy enough to work later into life. This includes embracing new approaches to the delivery of health, social care and adult skills including addressing health inequalities and re-skilling and supporting greater flexible working for older workers.

30 *'Creating Opportunity, Rewarding Ambition,'* Centre for Social Justice, 2011.

31 *'Arab Human Capital Challenge'*, Mohammed Bin Rashid Al Maktoum Foundation in cooperation with PwC 2007.

32 A dual education system combines apprenticeships in a company and vocational education at a vocational school in one course. This system is practiced in several countries, notably Germany, Austria, Bosnia and Herzegovina, Croatia, Serbia, Slovenia, Macedonia, Montenegro and Switzerland, but also Denmark, The Netherlands and France, and for some years now in China and other countries in Asia.

33 OECD (2011) figures quoted in 'Rethinking apprenticeships', IPPR, 05/10/2011.

Martin Tlapa,
Czech Republic

"We have a lot of things to do on the government level because the institutions, and the quality of the institutions, is one reason why we are lacking in our competitiveness strategy. Some people have said we need to improve public sector services, including the talent and work force for government services and public institutions."

Government as an employer

Government and public sector organisations have similar challenges to acquire, develop, engage and retain their workforces. Having the right people and making the most of them is fundamental to success: this puts a spotlight on the selection and identification of the right people for particular roles as well as on the mechanisms for reward, recognition and development.

These challenges do vary, however, across types of occupations, from policy-makers to specialists like teachers, and by sub-sector. For instance, the latest Local Government Chronicle Confidence Survey in the UK notes a decline in confidence since the UK's general election that 'Your council can attract and retain the skills and talent needed to work through recession.'[34] Failure to compete in the 'war for talent' will inevitably mean scaling back services and projects and costs rising – to hire people and train existing employees to fill the gaps.

There is also an image problem potentially to overcome. The results of PwC's most recent survey of the millennials generation[35] shows that those born between 1980 and 2000 do not find public sector work very appealing, lagging behind all other sectors with the exception of oil and gas, defence, and insurance. This is re-inforced by a report last year from the World Economic Forum's Young Global Leaders network which shows the difficulties in attracting young people to a life in the public eye.[36] In addition, many indebted governments are looking to cut jobs and impose pay freezes or reductions, which not only squeezes the incomes of many public servants but also acts as a further blow to staff motivation, morale and retention. It also risks further diminishing the attraction of public services as a career choice.

Mr Van Massenhove in Belgium puts it succinctly: "When you don't hire new staff you are not very attractive in the labour market for a long time and you lose your branding, you lose your expertise on the ground because people are leaving and they can't be replaced by others". In Germany, Lars Martin Klieve comments: "Bringing the workplace and family care/ commitments together is becoming increasingly important when employers want to be seen in an attractive light and make both possible. This could involve more part-time work, teleworking, working from home and the creation of jobs compatible with family commitments, for instance, also allowing children in the workplace in exceptional circumstances."

Developing countries have further issues with the lure of overseas markets for their top talent. As Mary Ann Lucille L. Sering in the Philippines comments: "There's a job-skills mismatch. Our economy is growing in 2005-2010 an average of almost 5% every year and yet our unemployment barely improved during that period. This means that inclusive growth is not happening. If you are talking about just skilled labour there's a lot of us here in Manila. Skilled labour. But highly skilled I'm not familiar with because most of those that are highly skilled normally the first thing they want to do is leave the country." And this is not just an issue in developing countries. Percival Manglano in Spain comments: "As long as the Spanish economy doesn't grow, there will be shortages of qualified staff due to the simple fact that they will want the best for themselves and for their children and emigrate – if there are no jobs available in the country they'll emigrate."

In the face of these challenges, government and public sector organisations need to pursue a twin-track approach:

- maintaining the engagement of current staff, particularly the pivotal talent i.e. those employees whose performance can make or break the organisation's ability to deliver its services; whilst
- addressing the risks to the image and attractiveness of the government as a future career choice for talented individuals.

34 Although it should be noted the confidence rating fell from +18 before the election to c.-40 six months later but has since been on a rising trend, but still negative at -18.
35 'Millennials at work: Reshaping the workplace', December 2011.
36 'The war for talent goes public', produced by PwC in collaboration with the World Economic Forum's Young Global Leaders.

This requires a relentless focus by public sector leaders on making their organisations 'employers of choice'. Given that often pay is not as attractive as in the private sector, this means looking at the overall package being offered such as non-financial benefits like more flexible working and understanding individual motivations and using this knowledge to engage staff fully in their work. It also means more attentiveness to performance management both to ensure that public sector workers are able to fulfil their potential, as well as managing out poor performers (although in some countries this would require changes to employment laws). Finally, it means enabling individuals to fulfil their potential by opening up opportunities across organisations to enable them to increase their experience and accelerate development, particularly those destined for leadership positions.

Our government interviews had a range of views on this agenda. Svein Kristensen in Norway comments: "We must focus on being modern and exciting for young and highly educated employees. We must be attractive to keep them in their jobs."

Debra Woodgate in Canada appears to agree: "I think there has been a huge reduction in the importance and the value of public service…However, I am finding with our recent grads they are choosing to come, they recognise the importance and that they are stewards of our most important assets for future generations. We also have a retention issue, because of the pay levels… We have to keep people here for other reasons and we are working on focusing on learning plans and on development, giving people different opportunities. I often say that it is now a situation where people join the Manitoba government and you can have ten different jobs."

Similarly, Marco Cuccagna in Italy comments: "The motivational message we perceive from students today is that they would like to be able to work perhaps at a slightly lower salary than the equivalent in the private sector, but to work for the public in the belief of serving the welfare of the community. These values had been long forgotten. I would like to reflect on the fact that today young people value the possibility of a decent job perhaps well remunerated but principally in line with their skills and which allows them to leave a mark in terms of making a contribution to the community."

Martin Tlapa in the Czech Republic also raises the issue of more flexible employment arrangements: "We need to have a more flexible model for hiring and firing people". This appears to be an issue in a number of other countries, including developing economies.

PwC view – government as an employer

There are some key actions by government and public sector organisations as employers to retain and engage core staff (beyond reward) including:

- Increasing the **attraction of government and public service** as a career choice for talented individuals by focusing on actions to make public sector organisations 'employers of choice'.
- Developing a durable **strategic workforce plan** without which organisations cannot realise their ambitions.
- **Defining talent needs** and aligning with the business by defining the type of skills that will be required for public services, identifying the people within the organisation who are best suited to particular roles and, where necessary, targeting external recruitment.
- A key feature of a strategic workforce plan is the consistent organisation-wide approach to mapping the motivations, capabilities, experience and potential of individual employees. **Systematic talent mapping** can be used to ensure the right people are assigned to the right roles. This is critical if the pivotal talent needed to deliver governments' core functions is to be retained, engaged and motivated.
- **Nurturing local talent** where possible. The recruitment and development of local talent can provide a more sustainable long term approach whilst skills transfer to local staff can reduce costs and enhance return on investment. However, for some countries and provinces, which lack local skills, the challenge is quite different – to find a sustainable pipeline of talent and skills to bring in from other areas, and overcoming regulatory and policy barriers.
- **Managing performance** effectively to develop the potential of staff and result in rewarding jobs and careers.
- Making greater **use of technology** to digitise processes, enhance work flexibility and engage staff through greater work-life balance. The striking example from our interviews was given by Mr Van Massenhove in Belgium: "We design our organisation so that people can work when they want to work and where they want to work. So all the processes are digitised and sixty-nine per cent of our people are working at home."

An agenda for action

We understand that governments have different starting points:

- **Mature economies** in North America, Europe and parts of Asia Pacific, need to act urgently to reduce public sector debt by reducing public spending and focus on the growth agenda (and so increasing not only jobs but also tax revenues).
- **Developing countries** can be more optimistic: the BRIC and Middle Eastern economies are in a better position to shape their futures. However, these countries need to maintain fiscal discipline whilst also coping with the effects of rapid growth on inflation and also on talent availability.

There are, however, many common agenda items across national governments. We believe governments need to up their game and act to:

- **Engage businesses, and citizens, through inspirational leadership and clarity of vision** which captures the government's strategic ambition. This will help to channel public sector resources towards accomplishing the vision.
- **Invest in the multiple internal capabilities needed to succeed and deliver more efficient and effective public services.** Beyond inspirational leadership, this includes the resilience and attractiveness of a nation's 'brand', the ability to learn from others through social intelligence, the skills to manage finances effectively and the capability to prioritise and manage governments' key programmes and projects, its performance risks and its assets including the human capital employed in performing governments' core functions.
- **Develop and enhancing the 'capitals'** needed to succeed at national, regional, city and local levels in a holistic way: financial, social, environmental, intellectual, human, cultural, infrastructural and political.
- **Execute strategy efficiently:** Business as usual is not an option: governments across the world need a new approach to innovation if they are to make breakthroughs in doing things differently and doing different things. Rapid prototyping of new ideas is needed to speed up the cycle. This should be enhanced by facilitating rapid diffusion of new ideas using new communications technologies including social media.
- **Collaborate more effectively.** Governments must work together (through forums like G20) and with business (as well as citizens, the private sector, academia and NGOs) to foster more holistic, balanced 'good growth' and support businesses e.g. in their ambitions to foster the skills and health of their workforces. Business looks to government to ensure financial stability and the enabling infrastructure (transport, housing, energy) as well as skills through effective education and training interventions. More can be done to help businesses cluster, accelerate innovation and learn from each other, using enabling technologies. In particular, governments can do more to help private sector businesses with better access to markets, reducing barriers and opening up markets, including those for some public services.
- **Improve accountability and transparency.** As public service value chains become more complex, with new players, governments must also be more transparent in their reporting, to foster good governance and accountability. This includes more robust accounting in the public sector worldwide e.g. through IPSAS, which will assist long term stability in capital markets by increasing the quality of, and trust in, the information on fiscal balances.

Annex: Government interviewees

Name	Organisation	Country
John Bradley	Director General, Department of Premier and Cabinet, Queensland	Australia
Frank van Massenhove	CEO, PMV – Finance, Vlaanderen	Belgium
Erik Camarano	CEO, Movimento Brasil Competitivo	Brazil
Sergio Ruy	Secretary of State, State Government of Rio de Janeiro	Brazil
Gina Rallis	Assistant Deputy Minister, Human Resources and Skills Development	Canada
Justin Riemer	Assistant Deputy Minister, Enterprise Division Finance and Enterprise	Canada
Debra Woodgate	Commissioner, Civil Service Commission in the Government of Manitoba	Canada
Martin Tlapa	Deputy Minister, Ministry of Industry and Trade	Czech Republic
Lars Martin Klieve	City Treasurer, City of Essen	Germany
Marco Cuccagna	General Manager of Equitalia S.p.A.	Italy
Idris Jala	Minister in the Prime Minister's Department	Malaysia
Rob van Gijzel	Mayor of Eindhoven	The Netherlands
Yvonne van Rooy	President of the Board of Directors, University of Utrecht	The Netherlands
Coen Teulings	General Director of Planning Bureau	The Netherlands
Svein R. Kristensen	Director General Norwegian Tax Administration (Skatteetaten)	Norway
Mary Ann Lucille L. Sering	Commissioner/Vice Chairperson Climate Change Commission	The Philippines
Krzysztof Gulda	Director of the Department of Strategy, Ministry of Science and Higher Education	Poland
Ibrahim Al Moaiqel	Director General of the Human Resources Development Fund	Kingdom of Saudi Arabia
Percival Manglano	Regional Minister of Economy and Treasury of Comunidad de Madrid (Regional Government of Madrid)	Spain
Andreu Mas-Colell	Regional Minister of Economy and Knowledge of the Generalitat de Catalunya (Regional Government of Catalonia)	Spain
Clas Olsson	Chief Analayst, Swedish Public Employment Service	Sweden
Frederik Rosengren	CFO, Swedish Prosecution Authority	Sweden
Ian Watmore	Permanent Secretary, Efficiency and Reform Group, Cabinet Office	UK

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