

Opportunities in adversity

Government and public sector survey snapshot

Overview

The worst economic conditions since the Great Depression have forced global governments to unleash a barrage of fiscal stimulus programs designed to offer immediate support to consumers and businesses. These efforts have exacerbated short-term government debt levels and have increased the need to use scant resources more efficiently. At the same time, the downturn has created fresh opportunities to invest in longer term infrastructure projects needed to implement the sustainability/innovation agenda, and it has opened the door wider to calls for lasting government reform.

With the Economist Intelligence Unit, we interviewed senior executives and leaders from major firms and governments around the world in June 2009 to gain insight on how they are managing their businesses during this period of uncertainty. The following report highlights findings specifically from the government and public sector respondents. The respondents to the survey indicated they were largely surprised by both the speed and severity of the downturn, yet they felt strongly that governments are taking the right steps to mitigate the impacts upon societies at large. Looking ahead, the government and public sector leaders saw new opportunities for cost-reduction/efficiency, accountability, transparency and service-delivery efforts, particularly in rationalizing information technology (IT) resources.

With the awareness that governments are facing unique sets of nationally specific challenges, Ernst & Young highlights several areas for improvement or increased focus as public sector leaders continue to innovate on the policy front and work to put this difficult period behind them.

About this survey

For this study, the Economist Intelligence Unit surveyed 569 C-suite and board-level executives.

Respondents were drawn from across the world and across a wide variety of industry sectors, including the government and public sector. Government and public sector leaders surveyed were drawn from a variety of disciplines, including comptrollers, technology directors, and department heads.

The research was carried out in June 2009. Responses are rounded to the nearest percentage.



Current challenges: limiting the damage

The following survey results must be interpreted through an understanding of the unique market challenges facing the government and public sector. Governments face the worst budget/financial conditions since the Great Depression, as a combination of shortcomings in policy, regulation and capital markets has given rise to a deep global recession. In 2008, the ratios of government gross debt to gross domestic product were historically high in a majority of industrialized economies. Efforts to pull national economies out of recession have been stymied in part by a lack of available credit for working capital, trade finance and other investments. Consumer and investor confidence remains low, leading to lower output, employment and prices. Mutually dependent nations have seen their trade flows and remittances reduced as a result.

In response, governments across the globe have instituted stimulus or rescue packages to stabilize employment levels, bolster their own economies, and even attempt to jump-start the global economy through increased trade activity. With difficulties in the banking sector blunting the impact of monetary stimulus programs, fiscal policies have become important complementary tools to cushion the blow of the crisis. Fiscal rescue packages put forward by governments have included tax cuts for individuals and corporations as well as spending increases in key areas. Governments have expanded their focus beyond financial institutions to help strengthen the viability of other nonfinancial corporations, to invest in infrastructure projects, and to shore up social welfare and other public services.

As a consequence of large stimulus packages, public debt will continue to swell in the vast majority of OECD countries. This will put pressure on government leaders to control costs and to consider other reforms. This sentiment is expressed in the survey responses; government leaders indicate that they see opportunities to improve the effectiveness of cost-cutting initiatives. Survey respondents also show a willingness to explore new areas for outsourcing or shared service centers.

A survey of the government and public sector

Both the speed and severity of the economic downturn appear to have caught more government leaders off guard than their counterparts in the private sector. Only automotive sector respondents were more apt to say that they were surprised by its impact.

Q: Please indicate whether you agree with the following statement: We have been surprised at the speed of the downturn (% strongly agree or slightly agree) – top five sectors.



Shown: percentages of respondents.

While four out of five (81%) said their organizations have accelerated cost-reduction initiatives over the past year, many respondents questioned their efficacy, particularly in the case of IT rationalization and headcount changes.



As should be expected, government and public sector respondents also had a more favorable impression than in the broader survey (+14%) about the steps governments have taken to mitigate the effects of the economic downturn. No single industry group exceeded government respondents' own assessment on this issue.

Q: Please indicate whether you agree or disagree with the following statement: My government has followed the right policies toward the economy in the past six months (% strongly agree or slightly agree) – top five sectors.

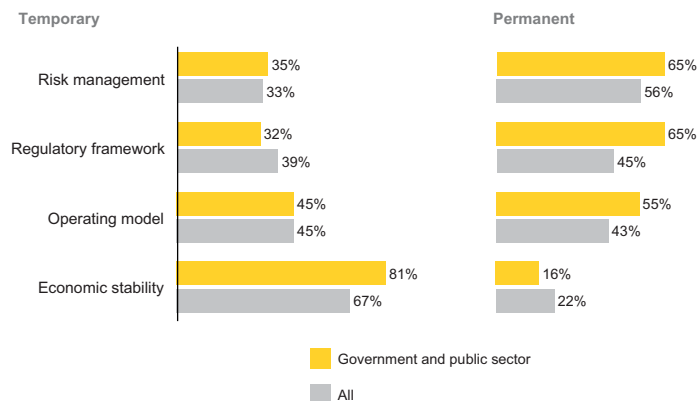


Shown: percentages respondents.

In considering the impact of the financial crisis on their organizations, four out of five government and public sector respondents saw a temporary change in their economic stability, which is being addressed in many jurisdictions by fiscal stimulus packages. Additionally, there are a number of areas in which a majority of sector respondents see permanent crisis-induced changes. For example, almost two-thirds of government leaders see permanent changes in their risk management practices and in regulatory frameworks. The increased significance of risk management is likely a response to the evidently weak risk-prevention frameworks in the private sector that have contributed to the current crisis. Along with growing demands to tighten risk management, government respondents also viewed regulatory frameworks as a key area of permanent change. The emphasis upon risk and regulation may be a result of longer tenures of government officials and civil servants than their peers in the private sector. The weight placed upon these two areas may also reflect a commitment on the part of sector respondents to enforce stability, transparency and accountability. This could be accomplished by means such as IPSAS (International Public Sector Accounting Standards) reporting, internal audit optimization, and risk preventions.

A majority of government sector respondents also believed that their operating models have undergone a permanent rather than a temporary change. The long-term efficiency and effectiveness of government and public administrations seem therefore to be paramount in the future framework of respondents' organizations.

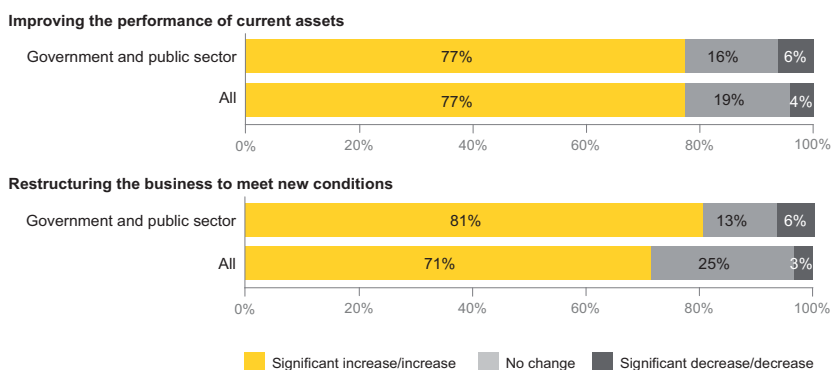
Q: In which of the following aspects of running your organization has the current crisis had either a temporary or permanent change?



Shown: percentages of respondents.

When asked about the significance that their organization attaches to restructuring their business, 81% of government and public sector respondents stated that there was either an increase or significant increase in importance to this activity. The strong response rate is likely reflective of the pressures for substantial administrative and regulatory reforms resulting from the financial crisis. When the question was posed about the change in importance their organization attaches to improving the performance of current assets, there was nearly an equally strong response from the sector. Given the unique nature of governments' primary assets (i.e., the ability to determine and collect taxes) and the current challenging environment, government leaders seem to recognize that they will be under increased scrutiny for how well they manage public assets.

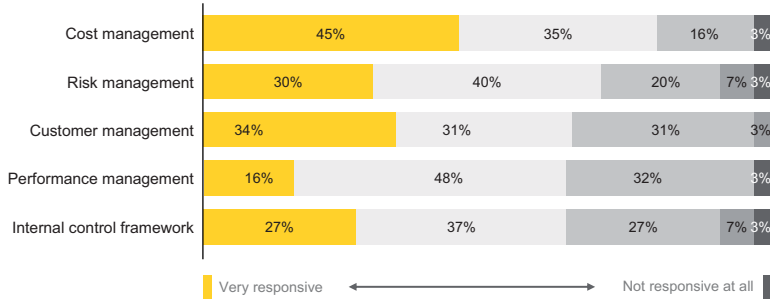
Q: Over the next 12 months, what change do you expect in the importance that your organization attaches to the following activities?



Shown: percentages of respondents.

Government leaders report that they have been responsive to the changes faced by their organizations. More than three-quarters of sector respondents reported that their organizations have been very responsive or responsive in the area of cost management. Government leaders also indicated that they have been responsive to changes relating to customer management and risk management. Also scoring highly were responsiveness related to performance reporting and related to internal control framework.

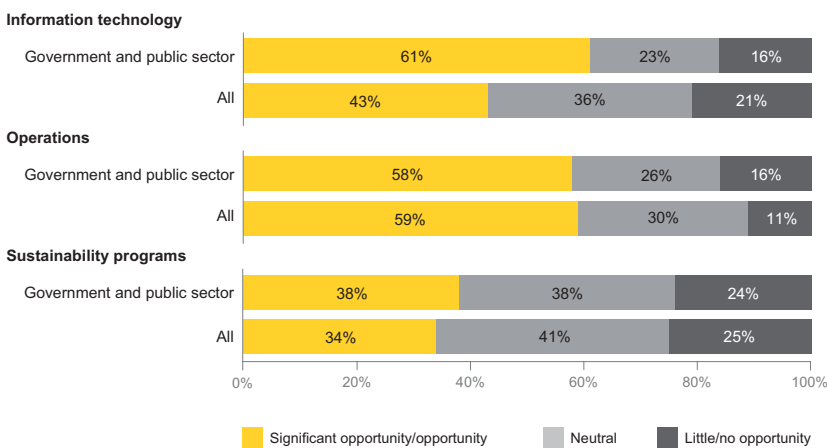
Q: Over the past 12 months, how responsive to rapid change have you found your organization to be across the following functional areas?



Shown: percentages of government and public sector respondents.

Although government and public sector respondents appear to have been responsive to changes in cost management over the past 12 months, they see opportunities for further cost reductions in the next 12 months. Over three-fifths of respondents (61%) indicated they saw either opportunities or significant opportunities for additional cost reductions relating to IT in the coming year (and sector respondents were more likely to consider outsourcing or shared service options for IT software or network management). There was nearly the same response rate (58%) when asked about opportunities for further reductions in their overall operations. Government and public sector leaders are clearly interested in finding ways to work in a leaner environment. E-government, shared services and strategic procurement are just a few examples of ways government leaders could rationalize costs while improving or maintaining service levels.

Q: How would you rate the additional opportunities for cost reduction over the next 12 months across the following functions in your organization?



Shown: percentages of respondents.

The use of public funds to bail out industries, support the labor market and invest in infrastructure projects will bring new scrutiny to capital programs, increasing the need for consistent accounting and reporting of stimulus spending.

Market responses

In response to the financial crisis and global economic downturn, governments are reassessing their strategic options and focusing their internal efforts on continued cost reduction. Ernst & Young's government and public sector team has evaluated the current landscape and has identified the following major actions that government leaders should consider in the months ahead:

- ▶ **Track the money.** Government leaders will need to justify taxation strategies to citizen'/ taxpayers through consistent accounting and reporting of stimulus spending. Reviewing expenditures with an eye toward allocating scarce resources and concentrating spending around key objectives will raise public confidence in their leaders' ability to address the recovery. Associated measures include short-term actions to support firms and families, complemented with steps to implement longer-term policies to support the sustainability/innovation agenda. Government leaders will face increasing public scrutiny for major capital programs, and will be tested in their ability to control costs, mitigate risks and effectively deliver timely measures to support the labor market, social housing, sustainability and innovation.
- ▶ **Creating effective tax policies.** Government leaders will be challenged to monitor and fine-tune stimulus packages through impact assessment of tax measures and global benchmarking. Additional revenue streams should also be evaluated as potential ways to decrease public debt.
- ▶ **Strengthen governance rules.** To enable adequate risk-mitigation measures, government bailouts and acquisitions of troubled assets demand consistency in governance rulemaking, planning and preparation of exit strategies.
- ▶ **Improve transparency.** Citizens are pushing for a more participatory approach to the management and monitoring of public budget and expenditure programs. A transparent and efficient use of public funds is the direction that national governments are asked to take in light of global financial turmoil, which is perceived as a result of lacking transparency and accountability measures. Hence, governments are not only required to design effective regulatory measures for the private sector but also to abide by the same principles they demand through such measures.

- ▶ **Employ new financing strategies.** As public debt levels soar, investors' appetite for public-private partnership/private finance initiative deals diminishes. Governments may need to undertake asset-efficiency programs and valorization of public real estate in order to release cash and pay down debt.
- ▶ **Restore fiscal discipline.** Government leaders will be challenged to continue the push for stricter fiscal discipline.

Survey responses show that government leaders are concerned with the effectiveness of cost-cutting initiatives and are looking for new ways to operate their organizations for greater efficiency. In addition, government leaders have shown that they are responsive to changes in internal controls and performance reporting, indicating a commitment to improve governance and increase transparency.

Conclusion

Governments around the world face a series of daunting challenges as they attempt to guide their nations through the global economic downturn. They are tapping into scarce resources, and are faced with increasingly difficult policy choices as they manage the crisis. Within this context, it is important that governments effectively manage their own costs, verify that proper controls are in place and maintain high standards of governance and transparency. In order to effectively lead the way through these difficult times, governments need to make sure that they have their own houses in order.

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