



Brexit and the business of government

UK Public Sector | #stateofstate

This year's *State of the State* finds the UK Government moving from an era of challenge around one primary objective – eliminating the budget deficit – into an era of parallel challenges as it moves towards Brexit.



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Welcome to *The State of the State 2016-17*

Now in its fifth year, Deloitte LLP and Reform have once again collaborated to analyse material from a wide range of public sources including the Government's accounts, public spending data and departmental reports. We augment that data with insight from original research to produce a snapshot of the public sector that is grounded in the realities of our public finances and constructive in its thinking.

This year's report finds the UK state disrupted by a new pressure: Brexit. While most sectors of the UK economy will be affected by the country's departure from the EU, just one – the public sector – is responsible for its planning and implementation. Our assessment suggests that leaving the EU, for all the complexities of that task, is an opportunity to rethink – rather than replicate – where the UK repatriates responsibilities currently undertaken by the EU.

As in our previous reports, we see the UK public sector responding to difficult public finances with commitment and innovation. Surveyed this year, both public sector leaders and citizens want services that are flexible, personalised, digitally enabled and appropriately funded. The strong public satisfaction with public services in the years of austerity is testament to those leaders' sense of public service, resilience and professionalism.

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Mike Turley,
Global Public Sector Leader,
Deloitte



Andrew Haldenby,
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Executive summary

Brexit and the business of government

This year's *State of the State* finds the UK Government moving from an era of challenge around one primary objective – eliminating the budget deficit – into an era of parallel challenges as it moves towards Brexit. The next five years will call upon the public sector to navigate the UK's complex route out of the European Union while continuing major reforms, managing uncertainty in the economy and maintaining business as usual.

Leaving the EU will be an era-defining task for the Government. Political stakes are high and media scrutiny will be intense. But if the Government shifts its fiscal policy from austerity to investment, it still needs to recognise the importance of continuing transformation programmes across the public sector to realise their benefits. Our interviews with 40 public sector leaders found that many are concerned about the level of distraction from reform that Brexit could cause in Whitehall and the devolved governments. And our survey of citizen expectations shows that the public wants the Government to focus on the NHS more than on leaving the EU over the year ahead.

The State of the State also observes that Brexit has significant implications for public sector productivity. In the shorter term, the renegotiation process will place substantial new burdens on departments in Whitehall, Belfast, Cardiff and Edinburgh that will need to be resourced. In the longer term, leaving the EU could require the UK public sector to establish new processes or even new agencies to take on activities that it repatriates from European institutions. However, that provides an opportunity for the Government to rethink – rather than recreate – every responsibility it repatriates from the EU to make sure they are as productive and effective as possible.

“Leaving the EU could require the UK public sector to establish new processes or even new agencies to take on activities that it repatriates from European institutions.”

Government through business lenses

Government is not a business. However, applying 'business lenses' to the public sector can allow for fresh analysis.

Viewed through a productivity lens, the Brexit process of departing the EU adds a major additional responsibility to government departments in Whitehall, Belfast, Cardiff and Edinburgh. Leaving the EU also means the UK public sector may need to take on responsibilities currently undertaken by EU institutions. *The State of the State* observes ten elements of the public sector that are particularly exposed to Brexit:

1. The public finances because spending levels rely on performance in the wider economy.
2. Whitehall's capacity, capability, in trade negotiations and engagement with business.
3. Tax systems and laws which could need to be recreated in the UK if negotiations lead to a remote relationship with the EU.
4. Regional and rural funding because the UK receives around £4.5 billion of funding per year, mostly targeted towards farming communities and disadvantaged places.
5. Regulations, both generic such as employment regulations and sector-specific such as for public sector procurement.
6. Transport, especially where it crosses national borders.
7. Immigration, including the status of EU citizens working in the UK, and their welfare entitlements.
8. Policing and border control, not least in how information is shared between EU member states.
9. Workforce arrangements, especially for the NHS and social care where EU nationals form a significant part of staff numbers and workforces are already under pressure.
10. Higher education because the UK's universities access substantial EU funding for research and host 125,000 EU students.

Viewing the public sector through a talent lens, *The State of the State* explores how robotic automation has significant potential to maximise the human endeavour of its workforce while delivering long-term cost savings. Cognitive and other technologies could substantially reduce the number of employees engaged in repetitive or predictable jobs, make better use of staff time for public sector workers who interact with the public and provide insight for people with more strategic or leadership roles.

Our analysis suggests that 861,000 public sector jobs could be lost to automation by 2030, saving some £17 billion annually in wages compared to 2015. Of course, such a shift would be gradual process.

The citizen view of the state

For this year's *State of the State*, Deloitte and Reform commissioned Ipsos MORI to undertake an exclusive survey into public attitudes and expectations on the state. The polling took place this summer through face-to-face interviews with more than 1,000 members of the public from across the UK. Key findings from the survey are:

1. Dealing with Brexit is a high priority, but not nearly as high as the NHS. When asked to name what the Government's top priorities should be, 33 per cent said Brexit, but 57 per cent said the NHS.
2. When asked to name what would improve public services in their area, the three top answers were better public transport, better hospitals and more investment.
3. Austerity's impact has been felt more in the past year. Our survey found that 27 per cent of the public feel they have been affected by austerity which is an increase from 23 per cent last year.
4. Support for tax rises to fund public spending has risen over the austerity years. When asked for views on tax and spending, some 60 per cent of the public believe that public services should be extended, even if doing so requires tax rises.
5. People expect public services to get worse because of Brexit. Overall, 41 per cent of the public think that Brexit will make UK public services worse. However, the most pessimistic groups were those most likely to have voted to remain in the EU.
6. Citizens want the public sector to listen more and collaborate better. When comparing the public sector to the private sector, the public believe that the public sector could be better at listening to preferences and offering personalised services. They also feel that different public services should work together to deliver services.
7. Our survey found a digital divide in which willingness to interact with the public sector online is split by age and social class. In other words, younger people and those in professional employment want to engage online far more than older people and those in more manual occupations.

In the words of public sector leaders

The UK's public sector leaders are uniquely placed to commentate on the state of the state. As in previous years, Deloitte and Reform have interviewed 40 leading public figures from across England, Northern Ireland, Scotland and Wales including ministers, permanent secretaries, senior civil servants, council chief executives, NHS chief executives, chief constables, police and crime commissioners, chief fire officers, directors of education bodies and non-executives. Six themes emerged from those discussions:

1. Brexit brings uncertainty, but leaders are sanguine.
2. The NHS needs continued transformation as well as funding.
3. Digital transformation is struggling to meet ambition.
4. Demand management is part of a wider issue in the citizen-state relationship.
5. The public sector's future will be more collaboration and a more flexible workforce.
6. Leadership needs to be effective, high-profile, diverse and continually renewed.

"Applying 'business lenses' to the public sector can allow for fresh analysis."

Recommendations

Our analysis for *The State of the State* leads to five recommendations:

- 1** Government should maintain focus on business as usual throughout Brexit – and that includes transformation programmes
- 2** Brexit is an opportunity to rethink rather than recreate
- 3** Digital transformation needs to focus on changing organisations one step at a time while maintaining momentum
- 4** Engaging the citizen in public sector reform will help reset expectations and manage demand
- 5** Public leadership needs to be celebrated, valued and supported to meet new challenges



Government in numbers

The UK state is a complex mosaic of organisations, democratically accountable to 44.7 million electors and supporting a population of 65.1 million people.^{1 2}

The Government's accounts identify more than 6,000 organisations across England, Northern Ireland, Scotland and Wales as the UK public sector. Together, they employ 5.3 million people which is 16.8 per cent of everyone in employment. That is the lowest percentage since current records began in 1999.³

As well as national Government in Whitehall, three distinctive administrations based in Belfast, Cardiff and Edinburgh run the UK state, each held to account by a unique elected assembly. Six political parties are currently parties of national and devolved government, plus an independent minister in the Northern Ireland Executive. Some 145 ministers serve as the UK's national political decision makers.

"As the Government is expected to trigger Article 50 and begin Brexit negotiations in 2017, it is unlikely that any UK representatives will take part in the 2019 elections to the European Parliament."

A total of 947 elected representatives currently legislate and scrutinise government in our elected assemblies, along with 799 members of the House of Lords acting as a second chamber of the UK Parliament.

In June, 33.6 million UK citizens voted in a referendum on membership of the EU, representing 72.2 per cent of the electorate. A majority of 51.9 per cent, equalling 17.4 million people, voted to leave.

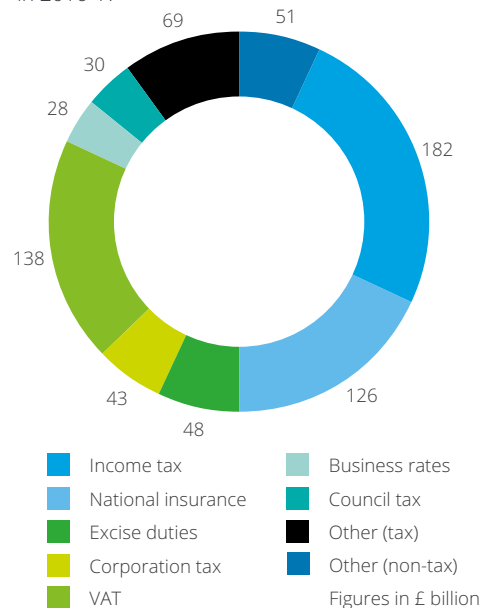
The 73 UK members of the European Parliament will continue to scrutinise EU legislation that affects the UK until Brexit is complete. As the Government is expected to trigger Article 50 and begin negotiations in 2017, it is unlikely that any UK representatives will take part in the 2019 elections to the European Parliament.

This financial year, the UK Government will raise £716 billion and spend £772 billion, as shown in figure 1. The difference between what the state earns and what it spends – the deficit – is funded by borrowing, and this financial year the Government is expected to borrow £56 billion. The cumulative effect of that borrowing over time means the Government's debts have risen threefold since the financial crisis to £1.6 trillion in 2016.⁴

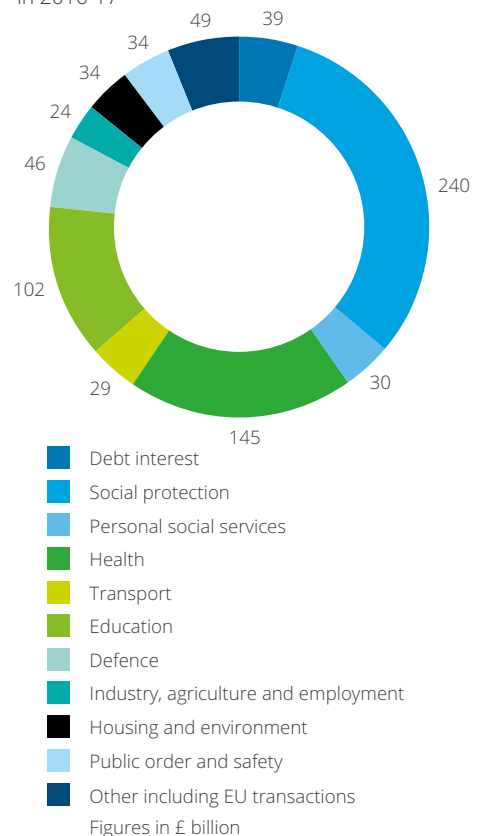
The UK Government's latest balance sheet shows £1.46 trillion of assets including land, the road network and military equipment, and liabilities of £3.56 trillion including public sector pension schemes and borrowing. The state's net liability – the difference between what the Government owns and what it owes at an accounting year end – rose by £263 billion to reach £2.1 trillion at last count for the 2014-15 financial year.

Figure 1.

Government income will be £716 billion in 2016-17



Government will spend £772 billion in 2016-17



Source: Budget 2016, HM Treasury

The state of the public finances

Since 2010, the UK Government has been striving to eliminate its budget deficit to deliver – as former Chancellor George Osborne described – a public sector “that lives within its means”. But this year’s vote to leave the EU will disrupt those plans, and economic uncertainty in the wake of the referendum looks set trigger a shift in the Government’s fiscal priorities away from austerity and towards investment to stimulate growth.

This section of *The State of the State* explores the state of the public finances – and what Brexit could mean for their outlook.

Economy, interrupted

After the 2008 global financial crisis, the UK entered its deepest recession since quarterly data was first published in 1955. The economy finally returned to its pre-crisis level in 2014, and the UK began to benefit from growth levels among the best of major advanced economies.

“Deloitte’s quarterly CFO survey – the recognised barometer for corporate sentiment amongst the UK’s big businesses sank to a three year low as the vote loomed.”

However, uncertainty began to drive a slowdown in hiring and investment after February 2016 when former Prime Minister David Cameron announced the June referendum date. Deloitte’s quarterly CFO survey – the recognised barometer for corporate sentiment – found confidence amongst the UK’s big businesses sank to a three year low as the vote loomed.⁵ The Office for Budget Responsibility (OBR) revised its growth forecasts down accordingly, by 0.3 percentage points to an average 2.1 per cent a year to 2020.⁶

In the immediate aftermath of the referendum, economic indicators were mixed. Within one month, the FTSE 250 – which tracks companies reliant on UK income and sterling – was down £27 billion and the pound had fallen 13.5 per cent against the dollar. But at the same time, the FTSE 100 of more international companies was up by £70 billion. Consumer confidence suffered its fastest monthly fall in 26 years according to the GfK index, yet figures from the Office for National Statistics (ONS) suggested that the UK’s economic growth improved in the three months leading up to June 2016 – so any uncertainty around the referendum period did not appear to affect growth at the time.⁷ However, a post-Brexit meeting of G20 finance ministers concluded with a clear statement that the referendum result had added to uncertainty in the global economy.

Recent months have also seen a collapse in global bond yields, with some £6.9 trillion of them now yielding below zero. July 2016 saw Germany issue bonds with a negative yield for the first time as investors preferred to hold on to Europe’s benchmark bonds, even at the risk of less money in return when the bonds mature. UK Government debt – issued in the form of bonds – is performing better than German debt, suggesting that the markets are less concerned about the UK’s solvency than they were after the global financial crisis.

The Bank of England was decisive in its monetary reaction after the referendum. Within six weeks of the vote, the Bank reduced interest rates to their lowest ever level to stimulate spending and announced plans to buy £60 billion of government bonds and £10 billion of corporate bonds from companies outside the financial sector that contribute to the UK economy. Quantitative easing of this kind is undertaken by central banks when interest rates are close to zero in order to increase the amount of money in the system, encouraging businesses and people to borrow and therefore create jobs and spend more money. Its effect will, as with all quantitative easing measures, be subject to interpretation and debate.

Economists continue to study individual indicators as they arise, but a more comprehensive picture of the referendum result’s immediate economic impact will not become clear until the Chancellor’s Autumn Statement and the full OBR data that informs it. In the meantime, Deloitte’s latest quarterly CFO survey shows that a heightened sense of uncertainty continues among UK corporates, with most expecting their investment spending and hiring to be weaker over the next three years as a result of Brexit. The consensus view among economists is that the UK economy will slow in 2017, but will probably avoid recession.

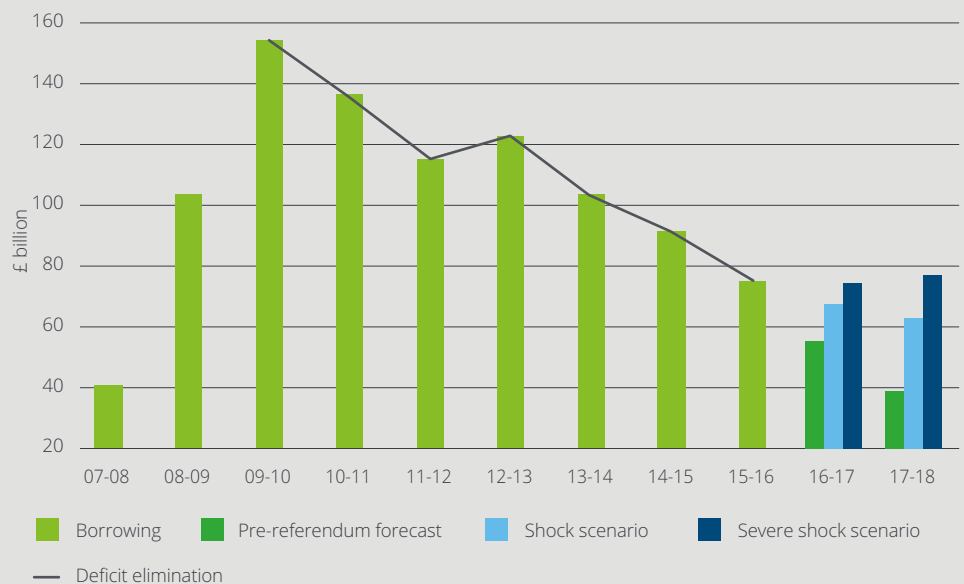
Public finances, disrupted

The global financial crisis hit the UK's public finances hard, triggering a recession that pushed tax income down and public spending up. The gap between what the Government was earning and what it was spending – the deficit – grew to a post-war record in 2010, when the state spent £154 billion more than it earned. Elected that same year, the UK Coalition Government unified behind a common purpose to eliminate that deficit and deliver an annual budget surplus so that the state's income exceeded its spending. Former Chancellor George Osborne described that fiscal objective as ensuring “a country that lives within its means”.

The UK Coalition ultimately reduced the deficit by half over its five-year term, achieving 80 per cent of that reduction though austerity measures that cut public spending. The remaining £74.5 billion was forecast to be eliminated by 2019-20, but new Chancellor Philip Hammond has confirmed that the timetable will not be met.⁸ He will set out details in November's Autumn Statement – which could be used to “reset fiscal policy if we deem it necessary”, according to the Chancellor.⁹

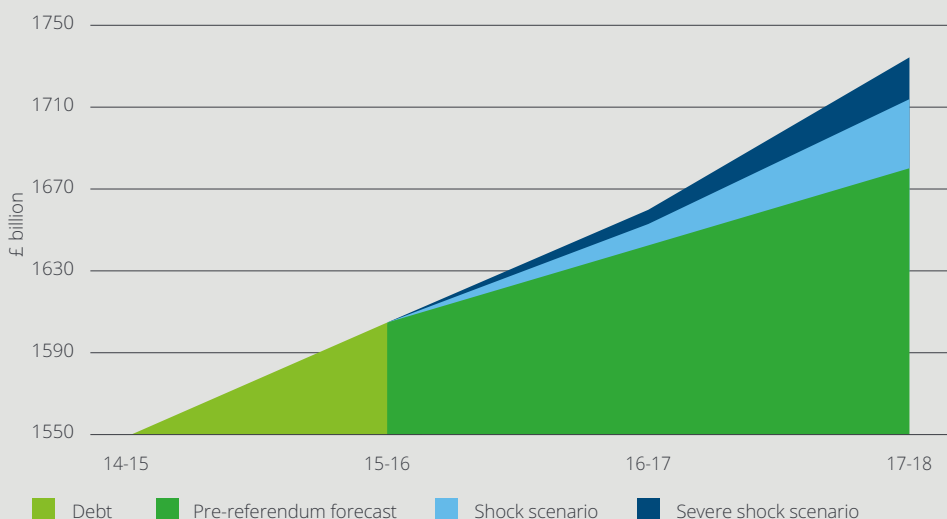
Figure 2 shows how the deficit has been reduced since its 2009-10 peak as well as the pre-referendum forecast for its continued reduction. The chart also shows HM Treasury modelling of how the referendum result could affect borrowing in the event of either a ‘shock’ or ‘severe shock’ in the economy as a result of the vote. According to the Treasury calculations, the deficit could be between £12.2 billion and £19 billion more in 2016-17 than if the UK had voted to remain in the EU. And by 2017-18, the Government could borrow between £24.2 billion and £38.5 billion more, taking the deficit higher than its 2015-16 level.

Figure 2. Eliminating the deficit



Source: HM Treasury and Office for Budget Responsibility, 2016

Figure 3. Public sector net debt



Source: HM Treasury and Office for Budget Responsibility, 2016

That higher deficit would of course increase the Government's debt. Figure 3 shows how public sector debt has gone up in the past two years, as well as the pre-referendum forecast. According to Treasury modelling, the Government's debt could be between £11.3 billion and £17.3 billion more in 2016-17 than if the referendum result had been ‘remain’. And by 2017-18, the Treasury calculates that the Government may need to increase its debt by £34.4 billion to £53.5 billion as a result of Brexit pressures.¹⁰

Resetting fiscal policy

Chancellor Philip Hammond has already indicated that the deficit elimination timetable – known as the fiscal mandate – will not be met. That raises four questions in relation to the public sector:

1. Will the mandate or the objective change?

In 2011, the UK Coalition established a Charter for Budget Responsibility that required it – and subsequent governments – to set out objectives for their fiscal policy as well as a ‘fiscal mandate’ against which progress could be assessed. The original mandate committed the Government to eliminating the budget deficit and beginning to see debt decline as a percentage of GDP. While the Chancellor adjusted the mandate’s parameters in the years that followed, it has remained the Government’s financial yardstick.

The fiscal mandate has been a constructive device that helped shore up confidence in the 2010-15 Government’s management of the public finances during a period of global financial instability. It also provided a transparent measure by which the Government could be held to account, while maintaining flexibility to change according to economic circumstances. But as the UK prepares to leave the EU, those circumstances could be changing so significantly that the Government will consider whether to extend its timetable for the existing objectives, introduce new fiscal policy goals, or both. The 2011 Budget Responsibility and National Audit Act requires the Government to set and maintain fiscal objectives and a mandate – and it also describes how the Treasury can change them, explaining why it needs to do so to the House of Commons.

2. Will infrastructure spending replace austerity as the dominant fiscal theme?

In early 2016, the Organisation for Economic Co-operation and Development (OECD) called on governments in advanced economies to shift away from austerity measures and invest more in infrastructure in order to boost sluggish economic growth. The International Monetary Fund (IMF) has recommended since 2013 that the UK should increase infrastructure spending, and this year called on all G20 nations to scale up their infrastructure spending in a bid to stimulate short-term demand and catalyse private investment.

While austerity measures were recognised as a legitimate policy choice in the wake of the financial crisis, an alternative response now appears to be under consideration as the UK gears up for Brexit. Although the Government announced increases in infrastructure spending last year, the Autumn Statement may go further still in shifting the Government’s emphasis from austerity to stimulus spending. The OECD and IMF views are backed up by OBR analysis that suggests spending on investment, public services and benefits are the interventions most likely to provide rapid economic boosts while providing a platform for medium and longer term growth.

Citizen polling for *The State of the State* shows that the public want to see greater infrastructure investment, especially in public transport and healthcare – and so a move towards investment at the Autumn Statement could be well received. Government will of course need to consider regional balances and the pressing need for housing as part of infrastructure plans. In 2015, the Government committed to releasing enough public sector land in England to build 160,000 homes by 2020. A year into those plans, the Government had only sold enough land to meet five per cent of that commitment. Multiple programmes across the public sector are identifying further surplus land and realising its potential is now key.

3. Will Brexit compromise or support public sector transformation?

Leaving the EU is an era-defining task for the Government. Political stakes are high and media scrutiny will be intense. But if the Government recalibrates spending plans as part of a fiscal reset, it needs to recognise the importance of continuing other change programmes across the system. Interviews with 40 public sector leaders for *The State of the State* found that many are concerned about the level of distraction Brexit will cause in Whitehall and the devolved governments, and whether it could jeopardise transformation programmes that are still needed to help public bodies make the most of their resources and cope with increased demand. Our survey of citizen expectations shows that the public sees the NHS as a greater policy priority than leaving the EU, suggesting an appetite for continued change and not a sole focus on Brexit to the detriment of public services.

4. For how long will the Government continue to run a deficit and increase its debt?

When governments run deficits, they make up the shortfall in their spending by borrowing. Even while the UK’s deficit is reducing, the Government has still borrowed £471 billion since 2010-11, bringing its total debt to £1.62 trillion. That equals 84 per cent of the UK’s GDP.

A secondary element of the fiscal mandate established in 2011 was that debt should decline as a share of GDP. In March 2016, the OBR assessed that the Government will miss this target in 2015-16 but is expected to achieve it in 2016-17. However, a fiscal reset and a shift to investment rather than austerity could change this outlook and the Government could decide to borrow while interest rates are low. A change in fiscal policy might of course see the deficit increased deliberately in order to fund investment.¹¹

Government through business lenses

Government is not a business. But applying 'business lenses' to its issues can provide useful perspectives. As in previous years, *The State of the State* considers the public sector through the lenses of productivity, talent and the balance sheet.

The productivity lens: Exposure to Brexit

Through a public sector productivity lens, Brexit has significant implications. In the short term, the renegotiation process will place substantial new burdens on a number of government departments in Whitehall and the devolved administrations that will need to be resourced. In the longer term, Brexit could require the UK public sector to establish new processes or even new agencies to take on activities that it repatriates from the EU.

Brexit provides an opportunity for the Government to rethink – rather than recreate – every responsibility it takes back from the EU to make sure they are as productive and effective as possible.

To explore these productivity implications further, *The State of the State* assesses ten of the most exposed aspects of the UK public sector to Brexit:



1. Public finances

The state of the UK's public finances rests on the state of its wider economy, and is therefore highly exposed to Brexit's impact. HM Treasury modelling suggests that the deficit – the difference between what the state earns and what it spends – could be up to £19 billion more this financial year and £38.5 billion more in the next financial year as a result of the referendum result.¹² Making up that shortfall could see the government's debt rise by up to £17.3 billion this financial year and £53.5 billion in the next. How any shift in the public finances affects public spending would of course depend on ministerial choices and appetites for adjusting fiscal policy.

Changes to exchange rates also come with implications for the public sector as a major purchaser of goods and services. The post-referendum fall in the pound could push up the cost of imports like pharmaceuticals and fuel, for example.

While the public finances are exposed to Brexit effects nationally, the local public sector's finances are also exposed in the event of economic decline. Reform to council finances has made local government highly dependent on the strength of their local economy, and recessionary pressures increase demand on local services including housing, children's services and the NHS. Recalibrated fiscal plans could also have particular implications for non-protected areas of day-to-day public spending, especially if the Government weights investment towards infrastructure.

2. Whitehall's capacity, capability in trade negotiations and engagement with business

While all sectors of the UK economy may be affected by Brexit, just one – the public sector – is also responsible for its

implementation. In the weeks following the referendum result, Whitehall moved swiftly to establish the Department for Exiting the European Union (DExEU) and take stock of its capability needs. However, there is little doubt that disentangling the UK state from the EU will present an era-defining challenge to the civil service. In fact, a memo to the Cabinet Secretary from the Hon Bernard Jenkin MP, chair of the Public Administration and Constitutional Affairs committee, described Brexit as Whitehall's biggest challenge since the Second World War. It went on to urge the civil service to build trade negotiation capacity quickly, fill gaps with external expertise as required and make sure that officials remain energised for the task ahead.¹³

That ability to negotiate trade deals will be particularly crucial if leaving the EU means leaving its single market and forging unilateral trade deals with the rest of the world. That appears likely unless the Government is prepared to maintain freedom of movement for EU and UK citizens alike, so the UK will need to seek its own Free Trade Agreement (FTA) with the EU rather than follow the Norway or Switzerland models where free movement is part of their arrangements. Such FTAs typically take between five and seven years to negotiate, with a further year for ratification. History suggests that caution will be required in negotiating trade agreements, as sudden loss of access to major markets has been known to cause dire economic impact. New Zealand's preferential market access to the UK ended abruptly in 1973 when the UK joined the European Economic Community (EEC), reducing New Zealand exports to the UK by half within one year. Finland's access to the Russian market similarly came to a halt in 1991 with the dissolution of the Soviet Union, accelerating a recession that saw unemployment rise from three to 18 per cent in four years.¹⁴

Brexit is also set to represent a step change in the level of government engagement with business. New trade arrangements and the UK's wider economic realignment will require reenergised support for exporters as well as new industrial strategies from Whitehall and the devolved administrations.





3. Tax systems and laws

If negotiations ultimately lead to a more remote relationship between the UK and EU, the implications for taxation could be far reaching. EU law covers customs duty, VAT and elements of excise duties, and so the UK could need its own customs duty and administration, even if it remains in customs union with the EU. If UK VAT law is decoupled from EU directives, transactions with EU states would become imports and exports rather than goods moved freely around a single market, with potential impacts on systems and cash flow. In both cases, the UK may ultimately gain greater freedom to make different choices but the short-term challenge will be one of systems and law. This will impose costs on businesses, which will need to adapt to such new systems. Direct taxes levied on income or profits are not expressly dealt with by EU treaties so are less likely to be affected – although some benefits from existing EU directives could be lost, depending on the future relationship.



4. Regional and rural funding

In 2015, the UK received around £4.5 billion of EU funding. Some 70 per cent of that was targeted support for rural communities and farm incomes, while most of the remainder came through the European Social Fund and the European Regional Development Fund. They help to finance projects intended to help disadvantaged places across the EU by boosting employment opportunities, building local infrastructure and forging links between regions.¹⁵ Whitehall will need to work through the implications of Brexit on this funding.



5. Regulation

EU regulations exist to create consistency across the EU over issues as wide-ranging as health and safety, consumer rights and product specifications. For the public sector, such regulations affect its organisations in both generic and sector-specific ways. Generically, as employer for almost a fifth of the UK's workers, EU regulations shape the public sector's employment offer, including maternity and paternity leave as well as rights for part-time and fixed-term employees. More specifically, most parts of the public sector are also subject to detailed EU directives. In healthcare for example, EU rules govern blood and tissue use, ensure that clinical qualifications are recognised across member states and set expectations for reciprocal access to state healthcare for EU citizens. Whitehall and the UK's regulatory bodies therefore face a complex challenge in assessing how the detailed regulatory landscape will need to change as the UK leaves the EU, and what the implications will be for public bodies subject to EU directives.

"If negotiations ultimately lead to a more remote relationship between the UK and EU, the implications for taxation could be far reaching."



6. Transport

European legislation covers substantial elements of transport and in particular where it crosses national borders. As with many other areas of Brexit negotiations, the UK Government will need to balance the benefits of policy freedom with the benefits of market access, and the extent of its impact will be defined by the extent of the UK's departure from existing EU arrangements. For example, continued membership of the European Common Aviation Area would offer unbroken access to the single aviation market, but membership requires obligations under EU law. For the rail sector, negotiations will need to resolve whether UK companies can continue to tender for franchises in other EU states, and vice versa, as well as the future of Europe-wide rail interoperability. The UK's Rail Safety and Standards Board considers harmonisation of rail standards to be necessary for the functioning of an EU-wide rail market, but critics argue that most trains running in the UK are built solely for use in this country and interoperability is therefore unnecessary.¹⁶

"Whitehall and the UK's regulatory bodies face a complex challenge in assessing how the detailed regulatory landscape will need to change as the UK leaves the EU, and what the implications will be for public bodies subject to EU directives."



7. Immigration

The UK has never been part of the EU's Schengen agreement that allows for passport-free movement across borders, and has maintained an opt-out on EU border control measures. However, polling shows that many people who voted to leave the EU did so because of immigration, so the Government may seek to address their concerns in its approach to Brexit.¹⁷

EEA nationals have a right of permanent residence after a specific period of continuous residence in a host EU country and some qualify for dual nationality. The UK is also part of the Common Travel Area, essentially having a borderless agreement with Ireland, Isle of Man, and the Channel Islands. And while the UK has opted out of EU measures on third-country legal migration, it nonetheless received £240 million from the EU to assist in various programmes around irregular migration and integration.

Some fundamental issues that need to be considered and answered include, most importantly, determined rights – especially whether there will be a cut-off date for EEA migrants exercising their right to freedom of movement and the privileges that come along with it. Further questions arise around the treatment of people who acquire permanent residency but arrived after withdrawal negotiations as well as people with an offending history or a 'right to reside'. Other issues include evidential requirements, changes in circumstance, health and welfare entitlements, and non-EEA family members' rights.

“Polling shows that many people who voted to leave the EU did so because of immigration, so the Government may seek to address their concerns in its approach to Brexit.”



8. Policing and border control

The UK's exposure to EU measures on policing is mixed. On one hand, the UK already has an opt-out on certain security and justice issues and cooperates within several international – rather than EU – frameworks. But on the other, the UK works across the EU extensively through measures including the European Arrest Warrant, reciprocal searching of national crime databases and cross-border initiatives. At the same time, UK police cite terrorism, organised immigration crime and cybercrime as growing threats that require extensive cross-border cooperation. The UK's Brexit negotiations will need to address serious concerns from the police. Before the referendum, Europol's director warned that Brexit would oblige the UK to leave the institution, making cooperation more costly and less effective.¹⁸ In addition, a group of former police chiefs including two former Metropolitan police commissioners warned that Brexit would leave the UK at a disadvantage in tackling terrorism and organised crime.

Substantial changes to border controls would raise numerous complex challenges for a variety of government agencies. For example, passport controls at airports have for some years been designed around automated gates for EEA nationals that may need to be rethought, a change to the visa regime could ramp up the processing burden and the complexity of transactions that could be required at UK borders might require an entirely new operational approach.



9. Workforce

Depending on the outcome of negotiations, Brexit could have significant implications for the health and social care workforces. About 55,000 EU nationals work for the NHS and a further 80,000 work in the adult social care sector, which have a combined workforce of 2.6 million. While the number of EU nationals may seem limited as a proportion of the total, employers are already struggling to recruit and retain over both sectors. Public sector employers have acted fast to reassure EU nationals in the wake of the referendum result, but many employees remain understandably concerned. Research by the Chartered Institute of Personnel and Development (CIPD) found that 33 per cent of public sector workers feel less secure in their jobs as a result of the referendum, compared to 22 per cent of employees generally.¹⁹



10. Higher education

The UK's universities are particularly exposed to Brexit issues. The EU's Erasmus+ programme allocates around €1 billion over seven years to the UK to encourage and support student mobility, and the Bologna process has created a harmonised higher education system. Around 125,000 EU students study at UK universities and EU funding accounts for some 11 per cent of research income for the UK's top higher education institutions – so the UK Government will need to work with universities to mitigate the impact of an exit from any of the EU's higher education programmes or negotiate their continued membership.

The talent lens: Automation in the public sector

If viewing government through a productivity lens allows a distinctive perspective on the implications of Brexit for the public sector, applying a talent lens offers a new angle on the future for people in the public sector.

Recent technological advances have created a new era of automation in which repetitive and predictable tasks are increasingly undertaken by robots, either in the form of software or devices. For the public sector, automation has significant potential for supporting cost reduction, meeting citizen expectation, boosting productivity and freeing up employee time.

To assess the scale of potential of automation for the UK public sector, its occupations can be divided into three types of role:

1. Administrative or operative roles in which activities are mostly repetitive and predictable. They can be desk-based such as administrative jobs or more physical, such as hospital porters.

2. Interactive or frontline roles which mostly require a high degree of personal interaction, such as teachers, social workers and police officers. These roles often have case management layers that could be supported by technology.

3. Cognitive roles that mostly require strategic thinking and complex reasoning, such as finance directors and chief executives.

Data from Oxford academics Carl Frey and Michael Osborne, working with Deloitte, suggests that in the public sector administrative and operative roles are at high probability of automation over the next two decades while other public sector jobs – those in the frontline or requiring substantial levels of complex thinking – are highly resistant to complete automation but could be enhanced by such technologies. Around a quarter of public sector workers are employed in administrative or operative jobs which have a high chance of automation, based on Frey and Osborne's estimates. Automation would not displace employees overnight – its impact is gradual – but it could see 861,000 public sector jobs lost by 2030. That would deliver a saving of £17 billion off the public sector paybill in 2030 compared to 2015.

Automation could also help the sector release surplus real estate. While space might need to be adapted for the technology, it is likely a substantial proportion of office space currently

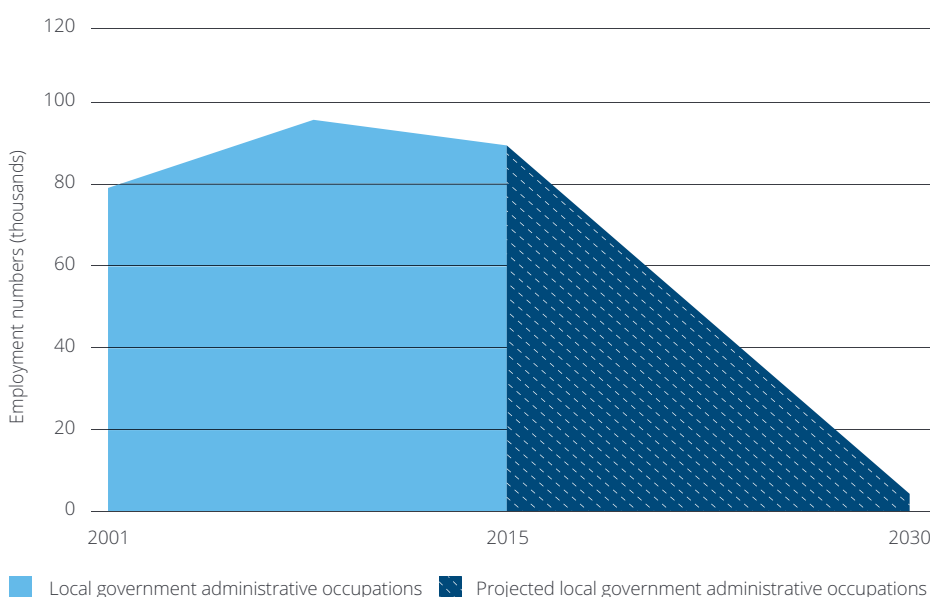
occupied by the administrative or operative public sector could be released for sale. Disposing those surplus assets could reduce revenue expenditure and generate capital receipts.

For administrative roles, a typical example of how automation could replace human labour is where data needs to be manually fed into several systems. That is a current burden in shared service arrangements such as those in local government, where legacy systems may not be interoperable, and Robotic Process Automation (RPA) now provides a software alternative.

For operative roles, a typical example of automation is through autonomous vehicle technology which is increasingly popular in metro train systems such as the driverless Docklands Light Railway.

Figure 4 shows actual and projected employment for local government administrative jobs to 2030.

Figure 4. Local government administrative occupations



Source: Osborne and Frey, ONS and Deloitte analysis 2016

About half of public sector jobs are interactive and have a relatively low probability of being automated over the next 10-20 years. However, automation offers potential in these occupations for complementing human capacity and minimising administrative elements of the roles.

In hospitals, sensor technology is starting to be used to monitor patients' vital signs, which frees up nurse time for interacting with patients more meaningfully.

"The increased ease of data collection, data accuracy and associated data analytics can help decision-makers form a deeper understanding of performance and future demand."

In other care settings, including people's homes, devices can now be used to alert health professionals to problems such as falls. Again, such technology has the potential to free up professional time and minimise operative tasks.

Figure 5 shows actual and projected employment for these two example occupations.

Approximately one-fifth of public sector workers are in occupations that require complex problem solving, judgement and cognitive reasoning that could not currently be automated. However, as with interactive roles, there are often tasks within the occupation that can be more easily completed or enriched with automation.

For example, senior figures in policing, fire and prisons could utilise technology such as data analytics to inform decision-making but the complex nature of their roles means that automation is likely to complement their roles rather than replace them. The increased ease of data collection, data accuracy and associated data analytics can help decision-makers form a deeper understanding of performance and future demand.

Some roles with complex elements such as healthcare practice managers could see a decline in numbers where better information flows have the potential to increase the quality of resource allocation.

Figure 6 shows actual and projected employment for these examples.

Realising the potential of automation will require data, the skills to exploit it and the software or devices to make it happen. *The State of the State* suggests that the Government should support the public sector in improving its collection and use of data, ensure that data can be shared across the sector with legislation if necessary and fund investment in automation projects. A sector-wide plan could provide a clear view of costs and potential savings over the next two decades.

Figure 5. Care workers, home carers and nurses

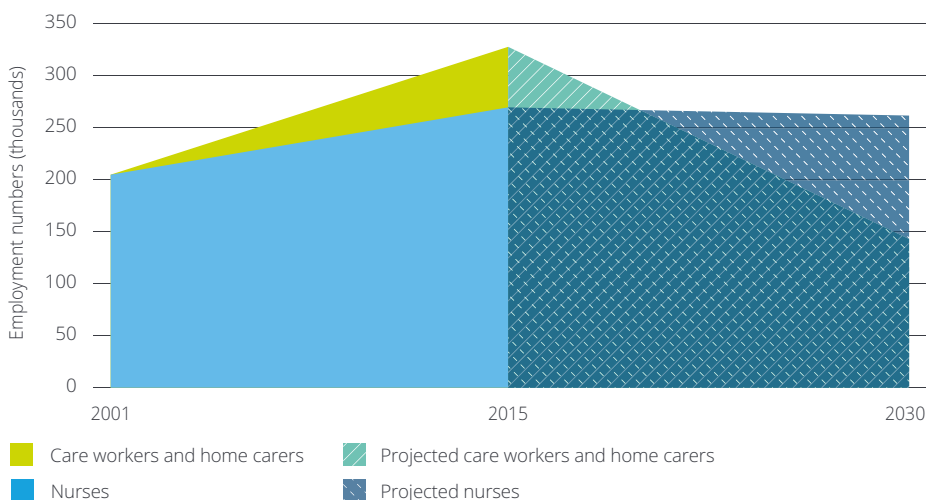
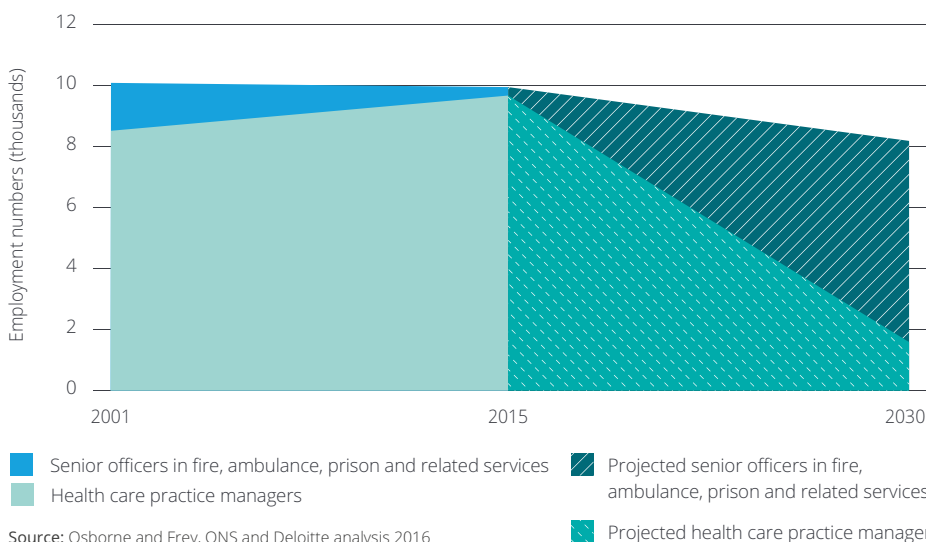


Figure 6. Senior officers in fire, ambulance, prison and related services and health care practice managers



Source: Osborne and Frey, ONS and Deloitte analysis 2016

The balance sheet lens: Reading the Government's accounts

The UK Government is a world leader in public sector financial reporting, and 2014-15 represents the sixth year HM Treasury has published the largest consolidated public sector accounts in the world: Whole of Government Accounts (WGA). They allow for a view of the state through a balance sheet and income statement lens that provides a perspective on the public sector's underlying financial health and sustainability.

An extract of the most recent WGA report is shown in **Figures 7 and 8**.

Figure 7. The state's income statement

	09-10	10-11	11-12	12-13	13-14 Restated	14-15	Notes
Revenue	£583.4bn	£614.0bn	£616.0bn	£620.7bn	£652.9bn	£659.3bn	The primary source of revenue for the state is taxation. Taxation accounted for £566.7 billion in revenue in 2014-15. In addition to taxation, the state earned non-tax revenues of £33.4 billion from the sale of goods and services.
Total expenditure	(£667.2bn)	(£701.7bn)	(£715.1bn)	(£717.3bn)	(£718.4bn)	(£733.9bn)	Government's total expenditure covers all of its costs, including £217.7 billion paid in social security benefits, £193.8 billion in staff costs and £191.7 billion to purchase goods and services.
Net financing cost	(£78.6bn)	(£83.2bn)	(£88.1bn)	(£79.4bn)	(£79.9bn)	(£83.6bn)	Net financing cost includes £56.6 billion in pension interest payments, as well as £27.6 billion in costs of servicing government borrowing.
Other	(£0.3bn)	(£0.3bn)	£1.3bn	(£2.7bn)	(£0.3bn)	£6.2bn	In 2014-15, the state had revaluation gains on its financial assets and liabilities, as well as a profit on the disposal of assets.
Net expenditure for the year	(£162.7bn)	(£94.4bn)	(£185.3bn)	(£178.7bn)	(£145.7bn)	(£152.0bn)	Net expenditure describes the shortfall between the Government's income and its expenditure in accounting terms.

Since WGA was introduced six years ago, there has been an overall reduction in net expenditure of £10.7 billion that illustrates austerity measures in accountancy terms. That reduction had been consistent year-on-year until 2014-15, when the accounts show an increase in net expenditure of £6.3 billion. However, that is largely driven by accounting adjustments rather than increases in spending levels. For example, a change to the discount rate used for public sector pension costs caused an increase of £5.3 billion in net expenditure.

As outlined in last year's *State of the State*, changes to the public sector boundary continue to bring new entities on to the Government balance sheet. The refreshed European System of Accounts 2010 resulted in the ONS reclassifying Network Rail to the public sector and the income statement and balance sheet have both been restated to include it, as well as the Pension Protection Fund. This continues to highlight the importance of early consideration by the Government on how ONS is likely to classify any new entity or arrangement, as well as existing entities which have ties to the public sector.

"Since WGA was introduced six years ago, there has been an overall reduction in net expenditure of £10.7 billion that illustrates austerity measures in accountancy terms."

The inclusion of Network Rail in the Government balance sheet drove an increase in infrastructure assets of £49.8 billion in the restated 2013-14 WGA. Infrastructure assets are expected to increase by billions of pounds in 2015-16's WGA, as Network Rail updates its valuation methodology to depreciated replacement cost, from an income based approach utilised previously.

"As outlined in last year's State of the State, changes to the public sector boundary continue to bring new entities on to the Government balance sheet."

Figure 8. The state's balance sheet

	09-10	10-11	11-12	12-13	13-14 Restated	14-15	Notes
Assets	£1,249.5bn	£1,234.3bn	£1,270.6bn	£1,297.5bn	£1,414.9bn	£1,455.3bn	Assets - what the state owns - include £395.5 billion in infrastructure assets, £374.4 billion in property and £51.2 billion in land assets.
Liabilities	(£2,477.4bn)	(£2,420.0bn)	(£2,617.4bn)	(£2,925.4bn)	(£3,255.5bn)	(£3,558.5bn)	Liabilities - what the state owes - include £1,493.3 billion in public service pension liabilities and £1,174.5 billion in government borrowings.
Net liability	(£1,227.9bn)	(£1,185.7bn)	(£1,346.8bn)	(£1,627.9bn)	(£1,840.6bn)	(£2,103.2bn)	Net liability - the difference between assets and liabilities - have increased since 2013-14 by £262.6 billion. The primary driver of this increase was a change in the discounting rate used to value the public sector pension liability.

Overall, the balance sheet net liability position has increased by £262.6 billion in the year. This increase has been driven largely by the change in the discount rate used for measuring the value of the public sector pension liability from 1.3 per cent to 1.8 per cent. The change of 0.5 per cent in the discount rate resulted in a significant £190.2 billion increase in public sector liabilities due to the long-term nature of this liability.

Previous years' WGAs have likewise seen significant increases in liabilities due to accounting provisions, for example, with increases due to nuclear decommissioning and NHS negligence claims. Alongside the pension discount rate change and the anticipated 2015-16 revaluation of the railway network, these adjustments illustrate how even small changes in accounting policies can have large scale ripple effects across how the public sector's assets and liabilities are measured. Accounting measures aim to recognise liabilities much sooner than measures of deficit and debt under the National Accounts.

The citizen and the state survey

Understanding public attitudes has always been important to government and the public sector. Political leaders strive to respond to the electorate's priorities and public service managers want to deliver on citizen expectations. But a clear view on what matters to the public is more important than ever in an age of spending restraint – it allows the public sector to make more informed choices about allocating resources and reforming services in ways that deliver the most citizen impact.

For this year's *State of the State*, Deloitte and Reform commissioned Ipsos MORI to undertake an exclusive survey into public attitudes and expectations on the state. The polling took place this summer with face-to-face interviews with more than 1,000 members of the public from across the UK. This chapter sets out seven headline findings:

1. Dealing with Brexit is a high priority, but not nearly as high as the NHS.

2. More people expect public services to get worse because of Brexit.

3. Satisfaction with most public services remains high.

4. Austerity's impact has been felt most within certain groups – and has risen in the past year.

5. Support for tax rises to fund public spending has risen since austerity began.

6. Citizens want the public sector to listen more and collaborate better.

7. The public sector needs to bridge the digital divide.

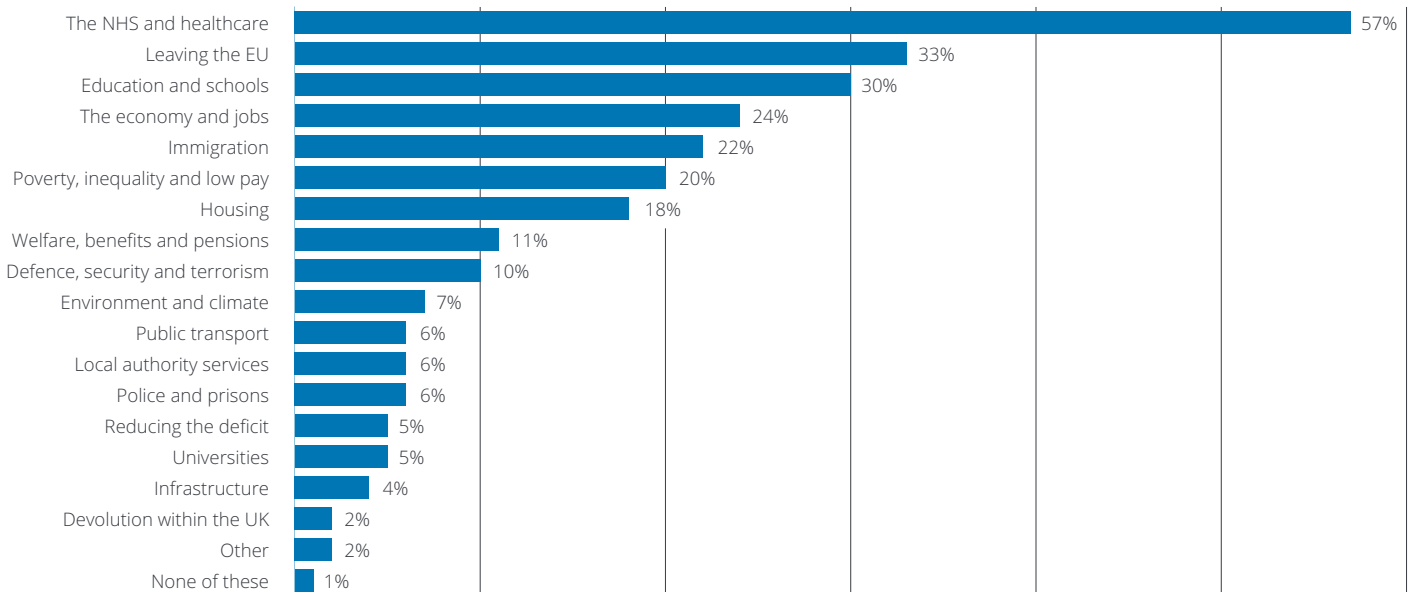
1. Dealing with Brexit is a high priority – but not nearly as high as the NHS

Headlines

- Public services, the economy and immigration are key public priorities
- Dealing with Brexit is a new priority and second only to the NHS
- Public transport and investment are more important local issues

Our survey asked people what two or three issues the Government should prioritise for the year ahead. As shown in figure 9, some 57 per cent said that the NHS is a priority, making healthcare the most common concern. The second biggest issue named by the public was Brexit, with one-third describing it as a top priority.

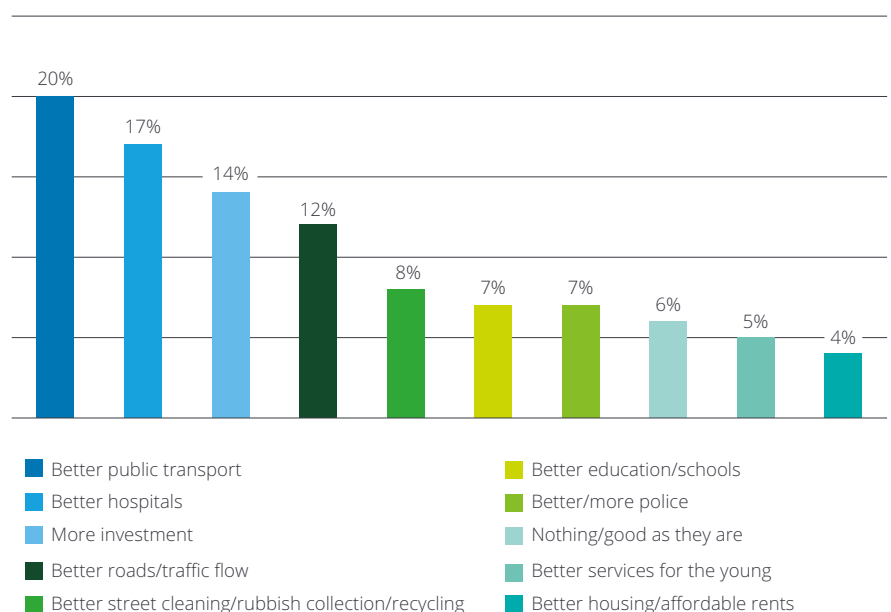
“A clear view on what matters to the public is more important than ever in an age of spending restraint – it allows the public sector to make more informed choices about allocating resources and reforming services in ways that deliver the most citizen impact.”

Figure 9.**Which two or three policy areas do you think should be the priority for the UK Government over the next 12 months?**

Base: 1,099 UK adults

The issues different groups want government to prioritise reflect the things they most care about. Women are more likely to say the NHS should be prioritised, and those with children place greater importance on education. Younger people aged 18-24 want a greater focus on higher education than other age groups, while older people and those from working class backgrounds are more worried about immigration. People on lower incomes, and Londoners, tend to see housing as a high priority.

Our survey also asked the public to tell us about their local priorities for improving public services. As figure 10 shows, public transport was the most mentioned issue, followed by local health services. The next priority was a more general one: a call for more funding, money or investment. This suggests that some among the public would like to see greater spending on local public services generally.

Figure 10.**What things would you say would most improve public services in your area?****The ten most mentioned factors**

Base: 1,099 UK adults

2. More people expect public services to get worse because of Brexit

Headlines

- Overall, 41 per cent believe Brexit will be worse for public services and 28 per cent believe it will be better
- People who voted to remain in the EU are most likely to have a strong, pessimistic view for the future of public services
- Three in five people think taxes will rise as a result of Brexit – but the public is split on whether leaving the EU will mean higher public spending

Our survey asked people if they think leaving the EU will be positive or negative for the UK's public services. Overall, 41 per cent think Brexit will make public services worse compared to 28 per cent who think it will make them better. Around a quarter believe Brexit will make no difference to public services, as shown in figure 11.

Figure 12.
What difference will Brexit make to tax and spending?

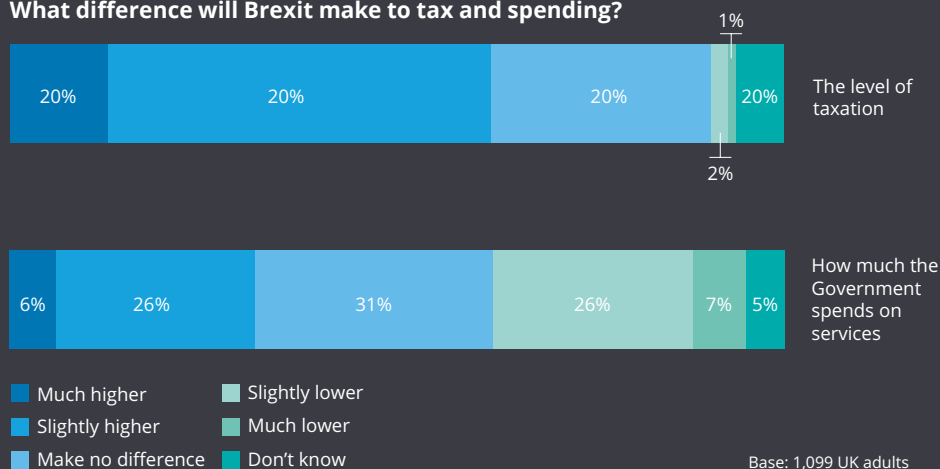
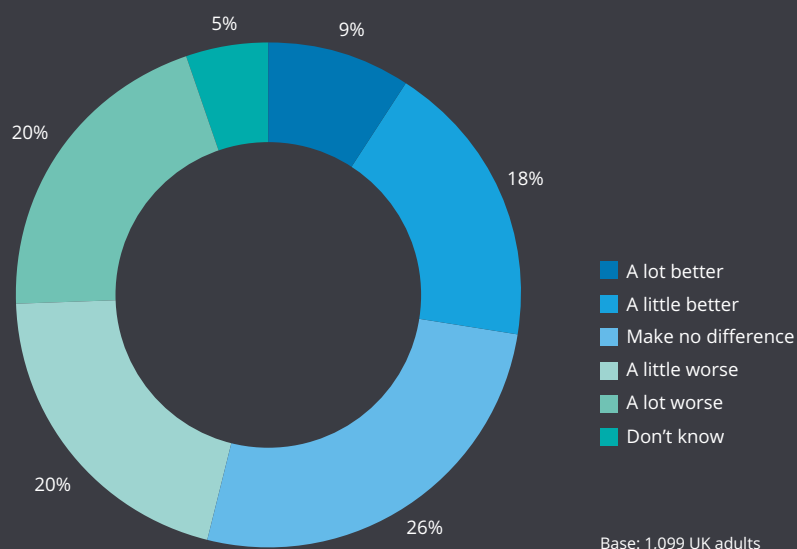


Figure 11.
To what extent will leaving the EU be better or worse for Britain's public services than if we had voted to remain?



As we might expect, groups of people who were more likely to vote to stay in the EU hold more negative views about the consequences for public services. Those groups more likely to vote to leave are more positive, although less strongly. It seems likely that the remain voters are still convinced that Brexit will damage the public services while leave voters are convinced it will not, albeit less firmly. This holds in terms of regional differences too. Voters in London, Scotland and Northern Ireland, for example, were more likely to have voted to remain in the EU and are now more likely to be pessimistic about the future of the public services as the UK exits.

We also asked people if they expect taxes to increase as a result of the EU referendum result. Three in five believe that they will – but the public is evenly split on whether those tax rises will deliver more public spending, as shown in figure 12.

3. Satisfaction with most public services remains high

Headlines

- Nationally, people believe the public services are getting worse – yet their own experience is positive
- The number of people saying the public services exceed their expectations has grown
- Public services are less likely to fall short of expectations than in 1998

Our survey explored whether people believe public services are getting better or worse, with trend data going back to 1998 that allows us to see how this has changed over the past 18 years. Overall, our survey found that nationally, more people believe public services are getting worse than in 1998. However, their own experience of individual services is largely positive and in some cases has improved over the last 18 years. That suggests public awareness about austerity has created a sense of worsening services, or reducing expectations – but actual experience of services remains good.

Figure 13.
How satisfied are you with each of these public services?

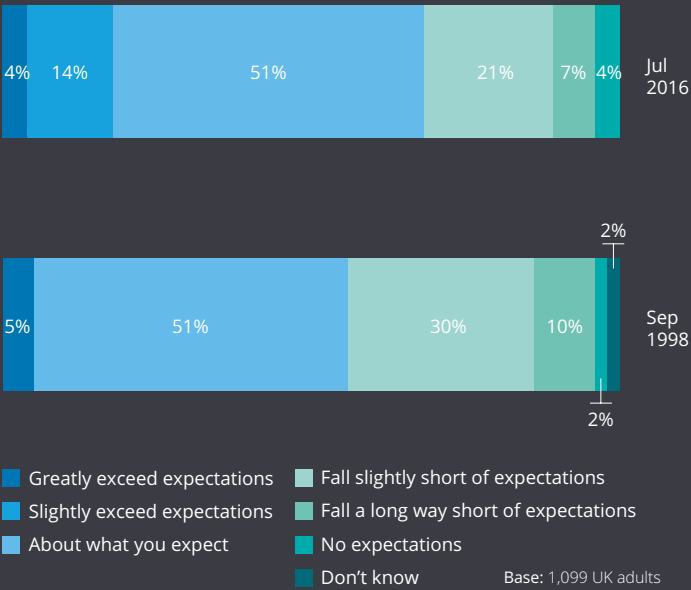
Satisfaction with...	1998	2000	2002	2016
Local sports or leisure centres	77%	76%	76%	86%
Parks and open spaces	79%	81%	81%	86%
Libraries	87%	88%	85%	85%
Recycling facilities	78%	80%	76%	82%
Universities and higher education	82%			78%
Schools				78%
NHS hospitals	80%	82%	76%	77%
GP surgeries				72%
Police				68%
Local bus services	62%	64%	66%	67%
Social services for adults/older people				60%

Base: 1,099 UK adults

“Overall, our survey found that nationally, more people believe public services are getting worse than in 1998. However, their own experience of individual services is largely positive.”

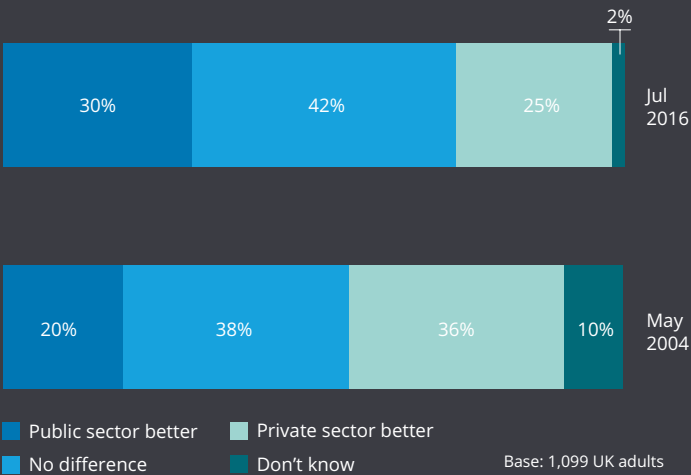
In fact, the proportion of people who say that public services exceed their expectations has jumped from five per cent in 1998 to 18 per cent. The number of people reporting that public services fall sort of their expectations has dropped as well – from 40 per cent in 1998 to 28 per cent. And the number of people saying that their experience of public services is about what they would expect has remained the same at 51 per cent, as shown in figure 14. While there is still some way to go, this suggests that public services are doing a better job of exceeding public expectations, even if more are still disappointed than delighted. What is harder to measure is whether expectations have become more or less demanding over that time.

Figure 14.
Thinking about what you expect of public services, do they...



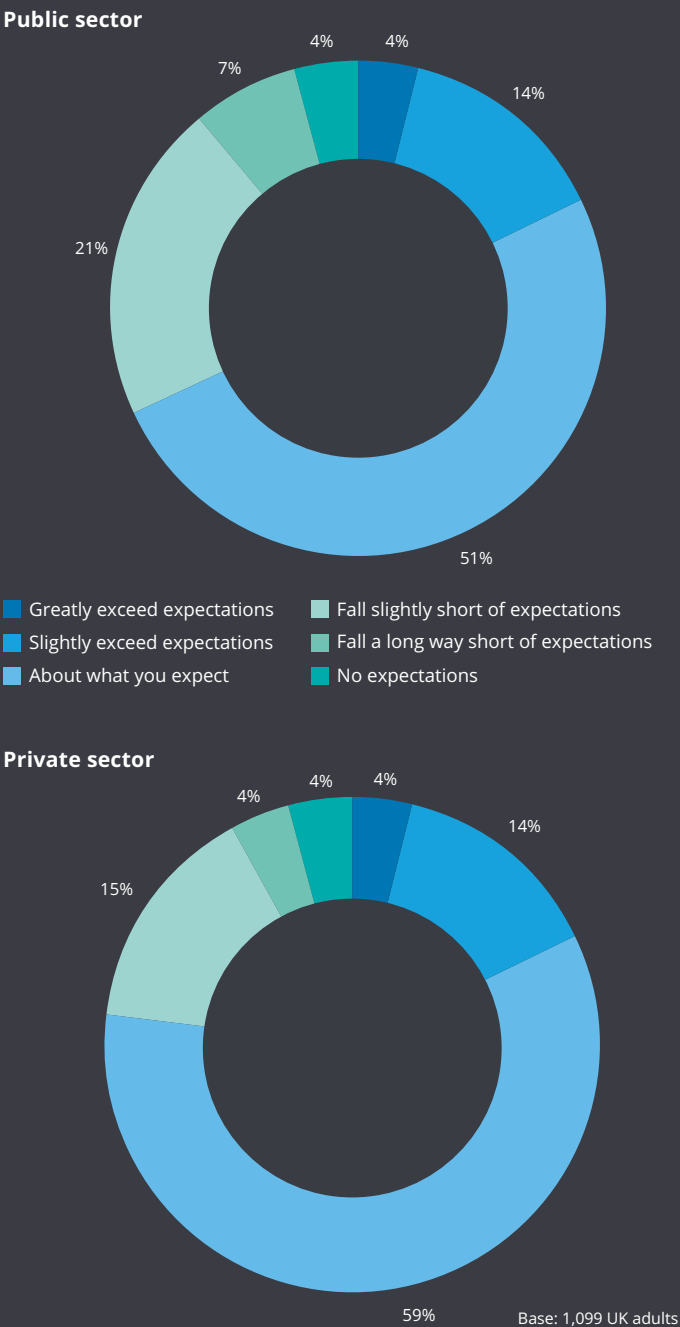
We asked people to compare their experience of public sector services with private sector services like shops and banks. Our results found that three in ten people think the public sector is better at providing services than the private sector, although the majority see no difference. Drilling down into the data, heavy users of public services are no more or less positive about them than those who are less reliant.

Figure 15.
Do you think the public or private sector is better at providing services?



While the survey shows that the public sector is more likely to fall short of meeting peoples' expectations than the private sector, it shows that it is just as likely to exceed them.

Figure 16.
Thinking about public services and private sector companies, would you say they...



4. Austerity's impact has been felt most within certain groups – and has risen in the past year

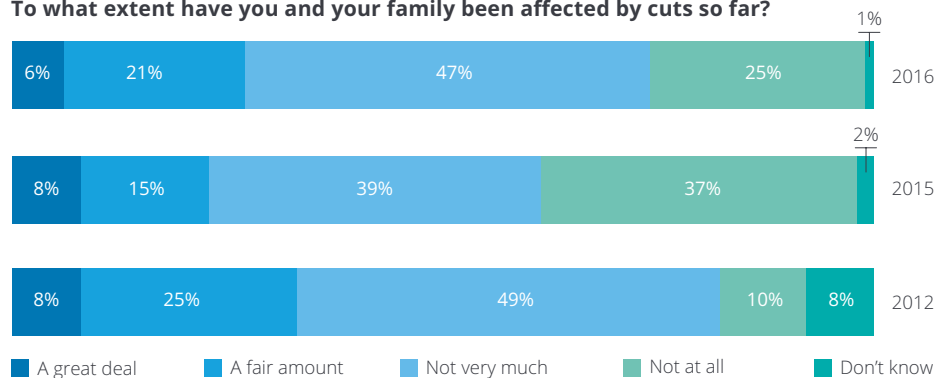
Headlines

- The number of people saying they have been affected by cuts has increased in the past year
- But most people say they have not been affected much or at all
- The impact of austerity is felt most by parents, renters and BAMEs

Most people in the UK do not feel they have been affected significantly by austerity measures. As **figure 18** shows, a quarter of the public told us that they had not been affected at all and almost half told us they had not been affected very much by spending cuts. However, over a quarter have felt the impact of cuts and this has increased since last year.

Those who feel most affected are found in certain groups in the population: parents, people from black and minority ethnic backgrounds, and people who rent their homes are more likely to have felt a personal impact from the cuts. At the other end of the spectrum, people over 65 are the least likely to have noticed cuts affecting them or their families.

Figure 18.
To what extent have you and your family been affected by cuts so far?



Base: 1,099 UK adults

5. Support for tax rises to fund public spending has risen since austerity began

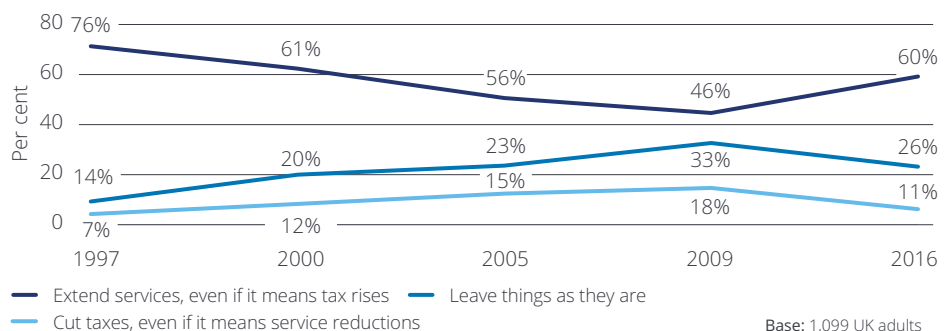
Headlines

- Support for tax rises to fund more public spending has gone up significantly since 2009
- People in Scotland, women and high earners are more likely to want spending rises
- People on low incomes, men and younger people are more likely to want tax cuts

Our survey asked people how they felt about the extent of government services in relation to levels of taxation. More people now want to see increased spending on public services, even if that means tax rises, than was the case in 2009. Support for tax rises to fund public spending has therefore risen since

austerity began, bringing public opinion in line with the early 2000s, as shown in **figure 19**. However, responses to further questions on expectation make clear that the public continues to expect the public sector to be cost effective and accountable.

Figure 19.
Which of these statements comes closest to your view?



Base: 1,099 UK adults

The types of people more likely to support extending government services are high users of public services, women, high earners and those aged 45-64. Scots also stand out as being more supportive of greater public spending. By contrast, those more likely to support tax cuts include men, those on lower incomes and people aged 15-34.

6. Citizens want the public sector to listen more and collaborate better

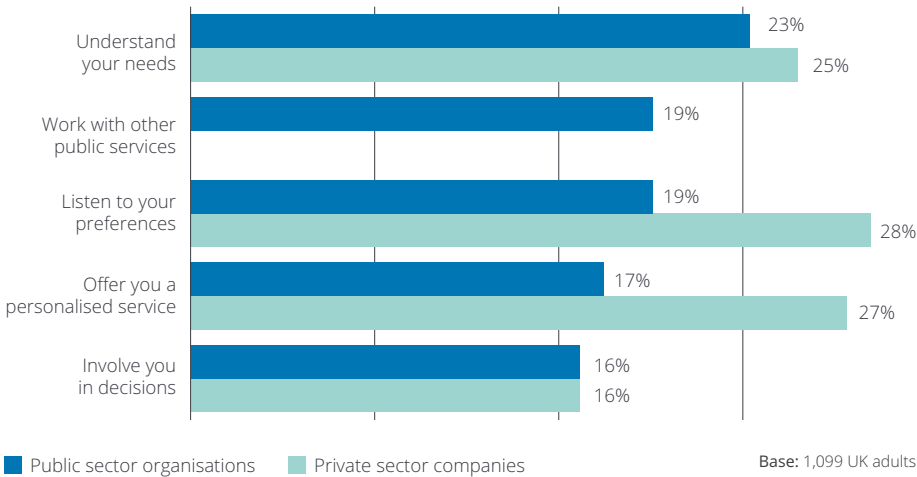
Headlines

- People feel the public sector is behind the private sector in listening to customer preferences and offering a personalised experience
- Those over 65 are less likely to feel the public sector is responsive to them
- Citizens believe public services should work better together and that partnerships with businesses and charities deliver the best quality, cost effectiveness and accountability

Our survey asked people about how they interact with the public sector in order to explore how customer experiences of services might be improved. This element of the research used the private sector as a reference point.

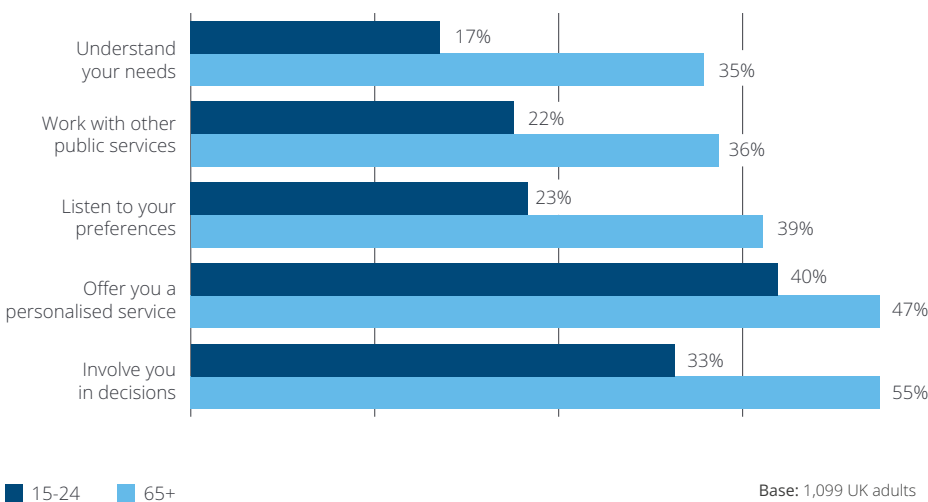
Overall, the results show that the public sector lags behind the private sector in two main aspects. First, 19 per cent of people believe that the public sector listens to their preferences, whereas 28 per cent think that the private sector does. Second, 17 per cent believe that the public sector offers a personalised experience whereas 27 per cent think that this is the case in the private sector.

Figure 20.
How often do organisations that deliver services...



As figure 21 shows, older people – who are more likely to use public services – are consistently less likely to feel that the public services are responsive to them. More than half of over 65 year-olds say that the public services do not involve them in decisions, compared to one third of younger people.

Figure 21.
How often do organisations that deliver public services...



We also asked the public about partnership working to deliver public services. The results suggest people see better joined-up working across the public sector as key to improving quality, maximising cost effectiveness and ensuring accountability to the public. As **figure 22** shows, most people also believe that the public sector should work with businesses and charities to deliver public services. But where businesses or charities alone deliver services, the public are less convinced that quality, cost effectiveness and accountability will be delivered to the same extent.

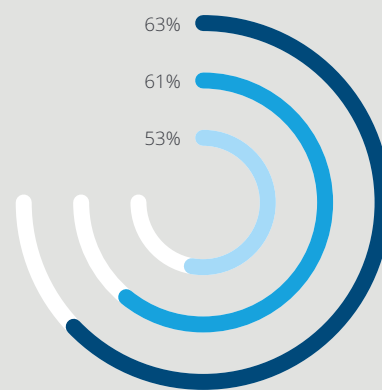
Of course, many public bodies already collaborate effectively and at scale. For example, the One Public Estate programme led by the Cabinet Office and Local Government Association brings together local public sector organisations to manage their land and property collectively – delivering savings, supporting better integrated services, creating more convenience for users and freeing land or property for housing or enterprise.

Figure 22.

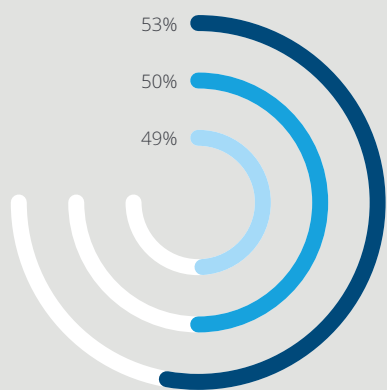
What impact do you think these different ways of organising public services would have on each of the following?

Per cent better

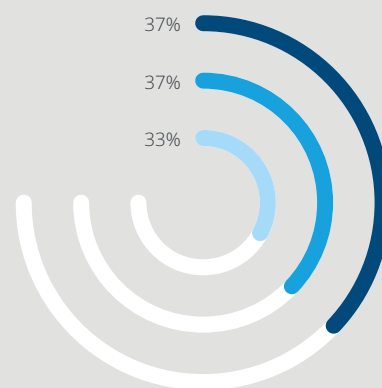
Different public services working together more often



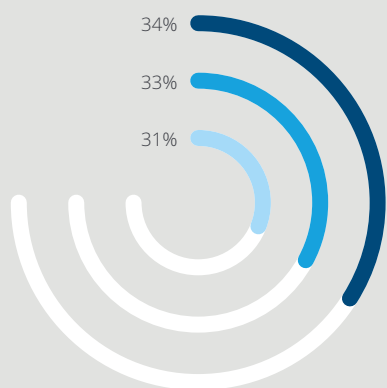
Public sector, businesses and charities all working together



Businesses delivering public services



Charities delivering public services



■ Quality
■ Cost-effectiveness
■ Accountability

Base: 1,099 UK adults

7. The public sector needs to bridge the digital divide

Headlines

- Overall, people prefer using the telephone for engagement with the public services beyond finding out information
- There is a clear digital divide, with a very high preference for digital interaction in the under 45s and among professionals
- The public don't see any difference in digital ability between the public and private sector

Our survey asked people to tell us which means of communication they prefer to use when contacting public services for a variety of different needs. It shows that people generally prefer telephone contact if they need to engage with a public body beyond just finding out information (something they are generally happy to do online).

However, deeper analysis of the data suggests a digital divide by age and social class. In other words, a preference for online contact with the public services is very high among people aged under 45 and more affluent people, but trails off with age and socio-economic status. Further detail is shown in figure 24.

“Deeper analysis of the data suggests a digital divide by age and social class.”

Figure 23.
What two or three ways would you prefer to contact public services for each reason?

Table shows per cent of people who mentioned each method in their two or three options

Preferred method of contact to...	Phone	Email	Meet	Online	Letter	Social Media	Text	Any Online
Find out information about a public service	46%	17%	14%	59%	5%	8%	2%	70%
Change personal details	54%	28%	23%	32%	16%	1%	2%	53%
Ask a public service to deal with a problem	76%	29%	24%	17%	10%	1%	2%	40%
Make a complaint about a public service	63%	38%	21%	17%	20%	4%	1%	49%
Suggest improvements in how a public service is run	40%	40%	15%	23%	18%	6%	1%	55%
Provide positive feedback about the service you received	40%	40%	17%	25%	18%	9%	4%	57%
Make an appointment with a public service	82%	20%	20%	18%	5%	1%	3%	34%

Most preferred method of contact

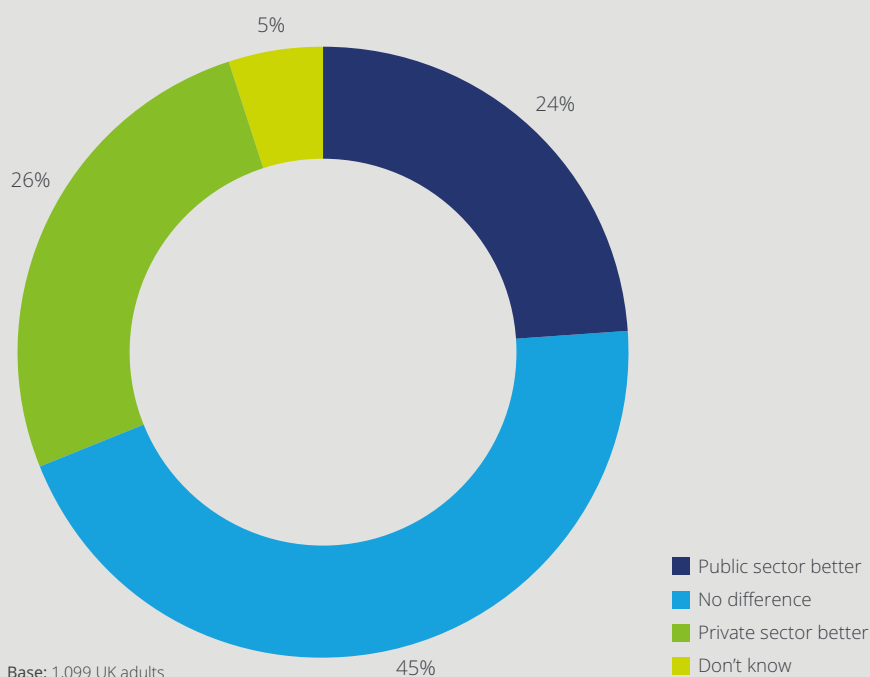
Base: 1,099 UK adults

Figure 24.
What two or three ways would you prefer to contact public services for each reason?

Per cent who prefer online to...	Age				Social class			
	15-44	45-64	65+		AB	C1	C2	DE
Find out information about a public service	82	68	44		81	73	72	51
Change personal details	61	53	28		72	58	49	29
Ask a public service to deal with a problem	47	41	25		56	47	35	21
Make a complaint about a public service	61	47	26		64	56	45	29
Suggest improvements in how a public service is run	67	55	28		71	61	53	32
Provide positive feedback about the service you received	70	59	28		70	66	56	35
Make an appointment with a public service	42	32	18		50	37	27	19

Base: 1,099 UK adults

Figure 25.
Which is better at offering services and information online – private companies or the public services?



For public bodies working on digital transformation in their customer engagement, these findings suggest that they need to encourage the use of digital channels by providing well-designed digital experiences that will become increasingly accepted by the public. The survey also shows the very strong appetite for digital interaction in the under 45s and among professionals. While that suggests a very strong future for digital channels as contact methods for the public sector, it also highlights the challenge of making sure that they do not exclude any user groups as interactions move online.

In the words of public sector leaders

The UK's public sector leaders are uniquely placed to commentate on the state of the state. As in previous years, Deloitte and Reform have interviewed 40 leading public figures from across England, Northern Ireland, Scotland and Wales including ministers, permanent secretaries, senior civil servants, council chief executives, NHS chief executives, chief constables, police and crime commissioners, chief fire officers, directors of education bodies and non-executives. Their perspectives provide real insight into the challenges facing the public sector and its outlook for the future.

Six consensus themes emerged from those interviews:

1. Brexit brings uncertainty, but public leaders are sanguine.
2. The NHS needs continued transformation as well as funding.
3. Digital transformation is struggling to meet ambition.
4. Demand management is part of a wider issue in the citizen-state relationship.
5. The public sector's future will be more collaboration and a more flexible workforce.
6. Leadership needs to be effective, high-profile, diverse and continually renewed.

These issues are, of course, overlapping. For example, digital transformation has far-reaching potential for NHS transformation as well as for sector-wide demand – but it requires leadership.

1. Brexit brings uncertainty, but public leaders are sanguine

The public sector is highly exposed to the EU and the UK's decision to leave could have significant consequences for it – and not least for the Whitehall departments that need to implement the UK's departure. Many public leaders interviewed for *The State of the State* told us about questions that Brexit raises, but most were sanguine about its implications.

While many of our interviewees were personally disappointed with the EU referendum result, they were pragmatic and ready to show leadership to meet the challenge. A police chief constable said that leaders across the UK “need to stand up, accept the situation and make the best of it”. Those in central government were more anxious. In the UK civil service, one senior figure said that “Brexit has thrown a huge spanner of uncertainty into Whitehall”.

Many commented on the uncertainty that Brexit creates. A council chief executive described the referendum results as starting “an undefined period of instability”. One chief constable noted that no-one yet knows what leaving the EU will do to the UK's public finances but a council chief executive warned that it could “mean another round of cuts and a further shock of austerity”. Other leaders wondered if the departure process would distract Whitehall and others from existing priorities.

The most-cited concern focused on workforce implications. Several noted that the number of EU workers in social care and in the NHS seems limited at around five to seven per cent, but that proportion can rise in some services and uncertainties over their status add to an already stretched situation. An NHS trust chief executive told us that “Brexit has injected enormous uncertainty.”

“While many of our interviewees were personally disappointed with the EU referendum result, they were pragmatic and ready to show leadership to meet the challenge.”

Leaders in the devolved administrations additionally recognised the uncertainty over EU funding for their rural and farming communities and the potential impact on foreign direct investment. A senior figure in Northern Ireland – which has seen exceptional levels of inward investment in recent years – recognised that being part of the EU and being part of the UK have both been factors in attracting foreign companies.

Interviewees in Scotland also noted that Brexit raises the prospect of a second referendum on Scottish independence. The director of a national public body said that meant her “view of the next five years is muddier” than she would want, with Brexit “adding layers of uncertainty and complexity.” A director in one of Scotland’s largest councils reflected that “the independence referendum saw stagnation” that could be repeated and “other stuff will get pushed down the priority list.”

Education leaders raised concerns about universities. One senior figure said that “higher education is where the Brexit frenzy is happening” and the director of a national education body told us that Brexit raises questions on the future of university research funding through the EU’s Horizon 2020 programme. She went on say that “the UK’s research-intensive universities do very well out of Horizon 2020. It may be that we can still join in with that. It may not.”

Interviewees from local government told us that they are concerned about Brexit’s impact on local economies, not only because of the shift towards business rates for council funding but because recessions increase demand for council services. A council chief executive in the South East said that “Brexit is a worry – for treasury management, for property prices and for workforces. What worries me most is the City of London’s status. If that goes, the rest of the UK economy is not strong enough.”

Some interviewees told us about opportunity for the public sector in Brexit. A local government chief executive said that “Brexit offers an opportunity for a constitutional review in the UK at what level decisions should be taken. If we are repatriating responsibilities, we need to make sure they are restated at the most appropriate level.”

Public sector leaders on Brexit

“Brexit has thrown a huge spanner of uncertainty into Whitehall.”

“Brexit won’t make that much difference. My concern is that younger people won’t want to live in this country and we’ll be losing doctors and nurses.”

“The UK’s research-intensive universities do very well out of Horizon 2020. It may be that we can still join in with that. It may not.”

“Brexit could be financially significant. I just don’t know what it will mean for the public finances. And interest in other things may wane if the civil service is tied up in that.”

“Brexit offers an opportunity for a constitutional review in the UK at what level decisions should be taken. If we are repatriating responsibilities, we need to make sure they are restated at the most appropriate level.”

“We are where we are. We need to stand up, accept the situation we are in and make the best of it.”

2. The NHS needs continued transformation as well as funding

NHS interviewees described an extremely challenged health service. Most were clear that additional funding might provide short-term fixes to current problems, but transformation is also required to put the NHS on a sustainable footing. Many felt the pace of change needs to quicken.

All of our NHS interviewees told us that nationally, health service finances are a pressing concern. NHS trusts ended the 2015-16 financial year with a combined deficit of £2.45 billion with 95 per cent of NHS acute trusts recording a deficit – and our conversations explored why. One trust chief executive told us that “hospitals are full to the gunnels with people who don’t need to be in expensive hospital beds and would be better cared for at home”. The director of a leading health body described current demand pressures as “a hospital sector under siege”. And while the Department of Health has tried to restrict spending on agency staff, one senior figure said that the national cap on costs “is not worth the paper it’s written on” because trusts will not take risks with understaffing and “agencies work around the rules”. Another said that the “the use of agencies is a symptom, not a cause of NHS workforce problems”. Several called for investment to address workforce shortages rather than demonising hospitals for using agency staff to meet immediate needs.

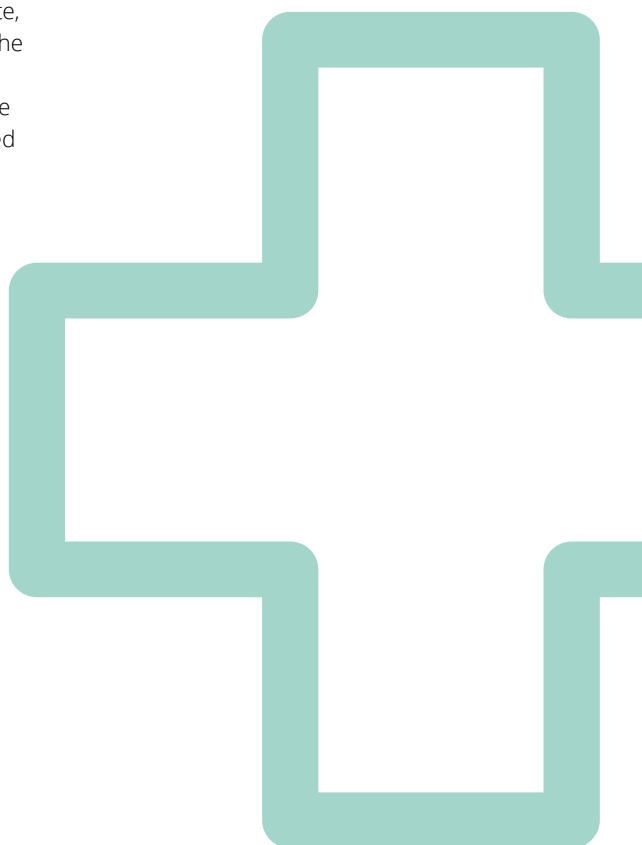
Most NHS interviewees raised concerns about spending cuts in social care and their impact on the NHS. A trust chief executive told us that such cuts “are a deep concern because they loop back to us.”

While the mid-term financial problem is a serious issue – and one NHS leader said that by 2018-19, the health service will be “at a precipice” – many interviewees saw them as symptomatic of more long-standing problems that need to be resolved to ensure the NHS is fit for the future. Some even thought that promises of additional funding, including those made during the referendum campaign, were counterproductive and an “excuse to avoid doing the big stuff” for some NHS trusts. An NHS non-executive told us that “ringfencing has helped but has also been a hindrance in that it’s made people believe they can trundle along”.

Instead, most told us that reform progress in the health service needs to accelerate. Several mentioned the potential of implementing the Carter review, which showed the wide variations in clinical and non-clinical practice across the NHS as well as the potential savings in creating greater consistency. It also sheds light on poor utilisation in the health estate, suggesting substantial potential for the NHS to reconfigure facilities, reduce maintenance costs and move to more modern facilities rather than outdated and inefficient buildings.

Public sector-wide, almost all of the leaders we interviewed told us that they were struggling with digital transformation, but NHS interviewees were particularly vexed by the lack of progress. A non-executive described the NHS as “one of the biggest unreconstructed services” in terms of digital, and went on to question why people are not able to speak to a GP via video calls or routinely make appointments online.

“NHS interviewees described an extremely challenged health service.”



Many interviewees saw greater collaboration between NHS bodies as a source of major savings, in which trusts share support services such as pathology labs within groups by default. Some hoped to see bolder change in which the NHS reviewed whether smaller hospitals were sustainable, restructured “sub-scale” GP practices, or explored how revenue could be raised with charges or premium services. The chairman of one NHS body accepted that such reform is “a national taboo politically – but if you’re writing *The State of the State*, it’s got to be flagged”.

Public sector leaders on the NHS

“Austerity continues to offer protection but with no recognition of demand.”

“Change is really hard because leaders are buried in the day to day.”

“The ringfencing has helped but it has also been a hindrance in that it’s made people believe they can trundle along.”

“Politicians keep... saying there may be more money and people will think ‘everything’s alright then, we’ll get more money’. But by 2018, by 2019, we’ll be at a precipice.”

“Hospitals are full to the gunnels with people who don’t need to be in expensive hospital beds and would be better cared for at home or in another setting.”

“The financial challenge facing the NHS is unprecedented in its history. The funding cuts to social services are a deep concern because that loops back to us.”

“We’re getting a mixed message from the department and national NHS bodies. The message is: you’re got to cut costs and get efficiency savings. On the other hand, would you please start collaborating and get into system transformation plans with very little framework around them. So huge risks, huge mixed messages, huge tension.”

“Actually I’m quite optimistic. The NHS enjoys massive support, very high levels of patient satisfaction, a huge number of committed staff and a tremendous amount of goodwill. So the model is not broke.”

3. Digital transformation is struggling to meet ambition

The potential of digital transformation for the public sector has been a recurring theme in *State of the State* interviews for the past three years. Exploiting digital has far-reaching potential for the public sector – not least in better managing demand and facilitating collaboration. However, the tone of our interviews has shifted from ambition to frustration at the barriers to progress and this year, most public sector leaders told us that they want to see digital change accelerated.

Many interviewees told us they felt their organisations should be more digitally advanced than they had been able to achieve. One council chief executive echoed others' views when he said "we're nowhere near where we need to be...digital is very much a work in progress". Another rated his own authority as "four out of ten". A permanent secretary in a devolved administration felt that his department was "always a year away from an outcome".

The same dissatisfaction at progress is evident across most of the UK. In Scotland, the head of a national body said "we're at Digital 1.0, but Digital 3.0 or 4.0 is where we need to be". The Welsh Government's national approach is seen as providing consistency across the country, but a director in one NHS trust told us that her organisation might have moved forward at a faster pace with different priorities. Northern Ireland has seen some of the most focused progress, with the civil service exceeding its 2016 digital targets and now setting its sights on digital transformation in the wider public sector.

Amid the frustration, many leaders have a clear view of the barriers to change. Several told us that their organisations had taken existing processes and made them digital before subsequently concluding that they had missed the opportunity to rethink their systems. A local government chief executive said "we digitised paper systems. We were the worst for that", and another said "we've wasted time digitising systems that weren't fit for purpose in the first place. It's rethinking these systems that will radically improve productivity". A senior civil servant admitted that his department was "seeing the world as digitally-enabled services rather than rethinking a digital world".

"Many interviewees told us they felt their organisations should be more digitally advanced than they had been able to achieve."

Skills were cited as the most significant barrier to change – not just in recruiting and retaining digital expertise, but in leading transformation. A local government chief executive said that many of his peers wrongly "pass anything digital to the head of IT", concluding that "there's a lack of competency to lead in a digital environment" across the public sector.

Risk aversion and fear of failure were raised by a number of interviewees as further barriers to progress. The leader of a national agency mused that "most people in the public sector would rather die in a ditch than roll out a large IT system. It will end their career". A minister told us that "we're scarred from big IT projects so there's a timidity to push the envelope" and a senior civil servant admitted "we've been burned".

As public leaders learn from experience and work through the barriers to change, they continue to see the potential for technology as an inherent part of their organisation's future. Some talked about the potential for connected technologies in helping elderly people stay in their own homes, thereby reducing demand on public services. Others see the most potential in citizen interaction, allowing the public to make appointments and flag concerns to public bodies online or speak to a health professional via a video call. But many want to see digital technology combined with data to provide management insight. A local government chief executive said "the big digital thing for me is management intel...to develop the culture of a management information brain in the council" and a permanent secretary said "we're basically a big data store and we need to manage that to find patterns" that could inform decision making.

A consensus view emerged on data sharing. A digital leader in healthcare argued that "you can't get away from the fact that healthcare is an information industry that requires the right information in the right place at the right time", but that regulations over data stymied progress. A police and crime commissioner compared data security challenges in the public sector to those in banking, concluding that banks "have secure information and have got away with it". He also laid bare the stakes in making sure information can be shared between public bodies, asking "how many times do we find when a child dies that every agency had a piece of the puzzle? IT is the way to make something happen".

Mobile technology was raised by most police interviewees. Forces have made substantial progress in rolling out mobile technology that reduces the administration burden and the need for police officers to return to stations. While that technological change was not easy, chief constables told us that cultural change has been the hardest part. One chief constable said that in spite of advanced mobile technology, many officers “like to come back... and plug into a wall” and another described a colleague so reticent to change their mobile device that they warned “you’ll have to prise this [phone] from my cold, dead hand”.

Several interviewees raised digital exclusion as a live issue. The director of a national body in Wales warned that society’s ongoing digitisation could widen inequality if people cannot access support to which they are entitled unless they are online. She added that technology can be prohibitively expensive for people on low incomes, including the significant number of older people in poverty.

Public sector leaders on digital

“We’re at digital 1.0 but digital 3.0 or 4.0 is where we need to be.”

“Most people in the public sector would rather die in a ditch than have to roll out a large IT system. It will end their career.”

“We’ve wasted time digitising systems that weren’t fit for purpose in the first place. It’s rethinking these systems that will radically improve productivity.”

“There’s a lack of competency to lead in a digital environment. That’s one of our huge training needs.”

“The progress is all good but we’re seeing the world as digitally-enabled services rather than rethinking a digital world.”

“The problem with digital redesign is: does the sector have the skills?”

“Anyone who has been involved with the public sector will have horror stories to tell about how poorly we’re doing with the digital piece.”

“Digital is very much a work in progress. If we’d carved it up into smaller pieces, we would’ve got more done”



4. Demand is part of a wider issue in the citizen-state relationship

The nature of the citizen-state relationship has been a recurring theme in *The State of the State* interviews over the past three years, and many public sector leaders have been adamant that the relationship needs to change in order to manage down demand on their services. Continued austerity and increased pressure have piqued that view, with leaders now crystallising their thinking about how the citizen-state relationship must evolve in the years ahead.

Demand from citizens is a particularly live issue for police forces. A police and crime commissioner told us that “at the weekend, the police become THE public sector. If a patient goes missing, [NHS staff] call the police. If a car is dumped or rubbish fly-tipped, people call the police. If there’s a noisy neighbour, people call the police”. Some forces have begun approaching their demand management by assessing the risks, solvability and harm levels associated with individual incidents.

At the same time, the nature of crime is changing substantially. Although crime is falling overall, police interviewees told us that child sexual exploitation, organised immigration crime, cybercrime and terrorist threats are continually growing threats – and they require different engagement with the public. A senior policing figure told us that law enforcement organisations need to clarify “what prevent and protect looks like” across the new threats facing UK communities. Just as the police used to encourage burglary prevention by promoting window locks, they now need to design and promote prevention tactics for child sexual exploitation, cybercrime and more.

For policing, visibility to the public represents a longstanding dilemma. A chief constable described in an interview how he was torn on the issue – on one hand, knowing that the public want to see a visible community police presence, but on the other hand, knowing that visibility is not the most efficient way to detect, prevent and solve crime. Another questioned whether a police officer should make physical visits to deal with online crimes, asking “why are we sending police to someone’s house to deal with a problem on Facebook? That’s a virtual problem. Can’t we deal with it in a virtual way?”. These trends raise important questions on police visibility – not just in communities but online as well.

Interviewees from the NHS also told us about increased demand, driven by an overlapping set of factors. A trust chief executive described how A&E attendance has risen along with the rate of admissions through A&E. As he put it, “that’s higher numbers, but increased acuity. We’re seeing frail older people coming to A&E and being admitted with more serious conditions and they are staying longer”. Others raised concerns about demand driven by unhealthy lifestyles, including one leader who said “I don’t think people realise there’s a health contract. They need to look after themselves”.

For local government, rising demand for social care continues to cause concern, and some council interviewees told us that central government was prioritising funding for the NHS while council finances struggled to cope with increased social care costs. More widely, the chief executive of a city council told us that “people’s expectations are increasing year-on-year” and went on to say that “people want the council to solve their problems”.

The need for public sector demand management through interventions such as restricting eligibility or preventative measures is well recognised. However, our interviews suggest that demand needs to be seen as one dimension of the wider citizen-state relationship – and that relationship needs to change. As the leader of a national agency in Wales told us, the public sector is “talking about demand growing for what we already produce, not what people want”. In other words, government and the public services need to understand citizen needs better and focus on outcomes for the public rather than restrict its existing services. Leaders from across the sector told us that they wanted to engage more effectively with the public and develop a more mature citizen-state relationship that would see personal responsibility grow and reliance on state intervention fall.



One chief constable said that the police should “push the boundaries around what we do” and another described an ongoing shift to “policing according to need”. They felt that the police should move away from “being all things to all people” and should signpost demand back to different parts of the public sector where possible.

The chief executive of an NHS trust said that “we need to be giving control back to people, rather than them being reliant on the big, shiny building with ambulances in front of it. That’s a very different culture” and a national NHS leader told us that “the population can be manoeuvred into a sensible place”.

While most leaders focused on their own organisation’s relationship with citizens, others took a wider view. As one minister pointed out, “if people have a good job, good housing and they make a contribution, they don’t get sick”.

Public sector leaders on the citizen-state relationship

“People say we should manage demand. But demand for what? We’re talking about demand for what we already produce, not what people want.”

“People’s expectations and expectations in terms of quality are increasing year on year. People don’t let you get away with anything but the best service and the best technology.”

“Citizen expectations are not being aligned with what’s delivered.”

“I don’t think people realise that there’s a health contract. They need to look after themselves.”

“Communities and the voluntary sector need to have their skin in the game.”

“At the weekend, the police become THE public sector. If a patient goes missing, [NHS staff] call the police. If a car is dumped or rubbish fly-tipped, people call the police. If there’s a noisy neighbour, people call the police.”

“We need to be giving control back to people, rather than them being reliant on the big, shiny building with ambulances in front of it. That’s a very different culture.”

“The language has changed massively, that policing is about protecting the vulnerable and reducing crime. It’s more explicitly about policing according to need – and that’s a fundamental shift. The police used to pride ourselves on being all things to all people.”

“What we’re getting towards is engaging people in the whole piece of what they want and more away from a paternalistic environment.”

“We need to think: what’s the role of the council versus the role of the citizen? We always used to put ourselves in the role of ‘doing the doing’ but we need to change that.”

5. The public sector's future will be more collaboration and a cultural shift

Public sector leaders take a pragmatic view of spending cuts. Many of those interviewed for *The State of the State* told us how they had used budgetary pressure to drive constructive organisational change, but that headcount reductions have taken a toll on morale.

When we asked the chief executive of one council about the impact of austerity, he told us that his authority has “stopped doing stuff and reduced the gold-plated service”. But he was clear that the far-reaching change already driven in the council would not have taken place without the pressure of austerity. That view was echoed by many interviewees.

Our interviews shed light on how the impact of austerity has varied across the UK's administrations. In Scotland, the public sector has not experienced the same pace and depth of spending cuts as England and the leader of one of the country's national public bodies told us “the counterside to that is we're seeing less innovation and less transformation as there has not been that drive”.

In Wales, the leader of a non-departmental body told us that if cuts continue at the same level as last year, she would need to change her organisation's business model fundamentally.

In Northern Ireland, the Civil Service (NICS) has reduced staff numbers by almost a fifth in just two years. A civil servant told us that his teams are “working harder and working longer”, and that morale and capacity to deliver had been affected.

When we asked our interviewees to describe how their organisation is likely to change over the next five years, many talked about two key areas.

First, a number of leaders told us that the next phase of reform for their organisation is a cultural shift. One senior civil servant said “the next big change is culture change. We need a larger risk appetite and to be more creative, more innovative and deliver services in a way citizens want”. A senior local government figure told us that by 2020, she hoped her staff “will be better able to operate outside their comfort zone”. Those same views were echoed by leaders from across the local public services. While they had already succeeded in cutting costs, reshaping their organisation and working more effectively with partners, most told us that changing the culture of their organisation was crucial in meeting their future challenges.

Second, interviewees from all parts of the public services talked about the need for greater collaboration. A chief constable told us that for the police, “by 2020, there will be deep collaboration”. NHS leaders told us that hospitals need to better join up to share common services. And civil servants told us that collaboration needs to be improved between government departments as well as with other sectors. One summed up by saying, “we need to disrespect existing boundaries”.

Some told us that parochialism is a significant barrier to collaboration between organisations. One council chief executive told us that “local politicians can be vain and parochial”, while another said that devolution deals have been causing “some very unpleasant fights and relationships are getting fractured”.

Others suggested that public sector organisations should do more to learn from each other. An NHS non-executive argued that “we've got a ‘not invented here’ culture, so people aren't taking advantage of learning and what works across the system”.

While the public sector leaders we interviewed had relatively clear views of where they want to lead their organisations, our research suggests that there is no single, shared vision for public sector reform – especially in England. One local government chief executive noted that austerity has been “designed without any end point in mind”, suggesting that a positive and ambitious vision would help the sector maintain a common direction of travel during the uncertainty of Brexit.

“The next big change is culture change. We need a larger risk appetite and to be more creative, more innovative and deliver services in a way citizens want.”

In contrast to England, an interviewee in Scotland felt that the Scottish Government has a clearer vision for its public services than the UK Government. And civil servants and politicians in Northern Ireland told us that the Executive had agreed a crisp and clear view of the future through its Programme for Government. These comments suggest that England's public services would benefit from a renewed and shared vision of what they should move towards over the next decade.

Public sector leaders on the future

"By 2021, there will be fewer folk in the civil service. We'll be more informal and more open plan. I hope it'll be a bit less risk averse but that remains to be seen."

"By 2020, if all goes well we will be working much more collaboratively across central government but also working with the local and voluntary sectors. We need to disrespect existing boundaries."

"By 2020, we'll have a much more integrated local state, more horizontally integrated. We'll need a workforce appointed to attributes and less to role."

"I suspect by 2020, there will be deep collaboration. Some forces can't survive and I imagine there will be mergers."

"By 2020, I'd like us to have built sufficient trust in the health and care system to be pooling resources and sovereignty, prioritising care close to home, encouraging prevention and reducing peoples' reliance on big expensive care facilities."

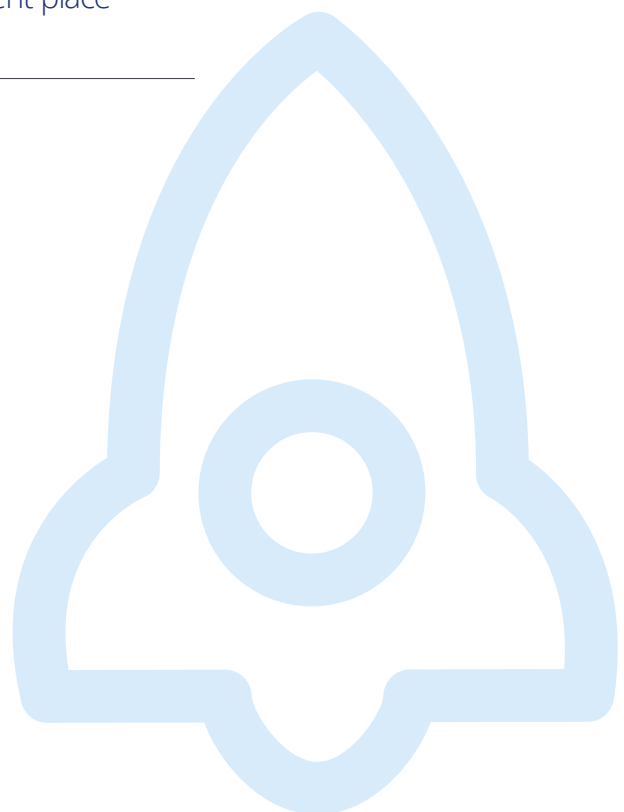
"I'm optimistic for the future, but we need a cultural shift."

"There is real efficiency to go for in the system, with too many component parts. We've got a 'not invented here' culture so people aren't taking advantage of learning and what works across the system."

"Most universities are thinking more strategically, thinking about what courses they offer and looking at their costs. Higher Education won't be in a massively different place by 2020."

"We're trying to change the mindset. Their mindset is 'I'll do this job for a few years and then move up to the next level'. But we've taken out layers of management because we couldn't afford them."

"Our workforce needs to be much more fluid. We need to develop a workforce that is able to respond and operates in a different model."



6. Leadership needs to be effective, high-profile, diverse and continually renewed

As leaders in their own organisations, our interviewees were able to share their experiences of leading and managing a top team. Our research found that pressures on public sector leaders are shifting in some subtle but critical ways, and that talent management needs to be energised across the sector.

Many interviewees told us that strong leadership will be particularly important for the public sector given the nature of its current challenges. For the civil service, effective leadership can often mean the ability to drive change and lead implementation. Hence, a senior civil servant told us that “we need to place a premium on effective leadership – that’s key to delivering”. For the local public services, their central challenges include driving cultural change within their organisations, reshaping the citizen-state relationship and improving collaboration. All of those challenges rest on effective leaders that can engage people – which is why one interviewee told us that the sector needs “strong, clear, high profile, public leadership”.

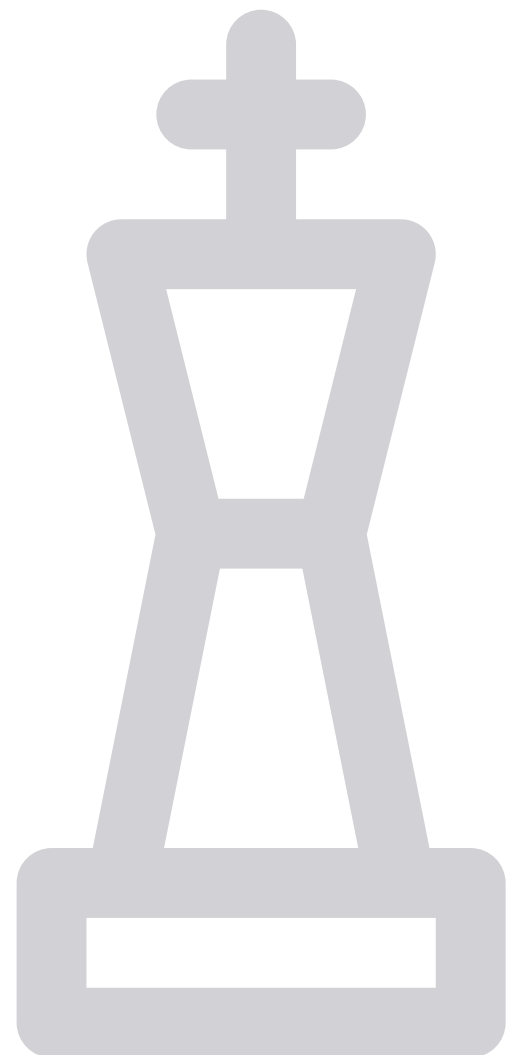
An ability to connect with the public, or lead wider organisational engagement with the public, is an increasingly important dimension of public sector leadership and a wider talent requirement. As one chief executive reflected, “we need to say to the public, ‘this is a proper partnership’ – and that’s where leadership comes in.” Leading in a networked and collaborative environment also requires new forms of leadership. As a civil servant told us, “leadership before was about leading your own people but now it’s going to be about corralling people over which you have no direct control”.

While most interviewees were clear on the importance of effective leadership, many told us that recruiting or developing top talent to leadership roles was more difficult than ever after six years of austerity. A chief fire officer said that “austerity means people are doing more, in smaller teams. And smaller teams mean we are drawing leaders from smaller teams”. A local government chief executive explained that traditional progression routes had been disrupted in his council because management had been delayed. Another told us “the problem is we recruit and promote professionals, not managers. And managers are what’s needed”.

Public bodies in rural areas face an additional, geographic challenge in securing top talent. A council chief executive explained “we need to grow our own talent, because we’re hours away from a city. We’re fishing in a pool of people who want to come here and make that lifestyle choice. The NHS is the same”. He went on to tell us that his council could not attract a single credible applicant for a post paying a £70,000 salary.

Diversity is a central consideration for many leaders in their search for talent, as well as in their wider workforce. One city council chief executive told us that a voluntary redundancy scheme had seen the departure of a high number of long-serving staff members and the council had “got a more diverse workforce as an accident of downsizing”. Another senior local government figure explained that a high proportion of her employees had worked at the council for decades, but recruiting to new posts to deal with new challenges was difficult. A chief constable was clear that “a diverse workforce performs better” and said that his force’s leadership programme “still has too many fat, white, middle-aged men”. For that reason, he was supportive of direct entry into senior police roles.

“Many interviewees told us that strong leadership will be particularly important for the public sector given the nature of its current challenges. For the civil service, effective leadership can often mean the ability to drive change and lead implementation.”



Pay is also an issue that needs to be considered if the public sector is to attract top talent. A council chief executive told us when she tries to offer an attractive reward package to recruit to key posts, her elected members “think it’s crazy money”. The leader of a national agency said that “our approach to pay and reward does not have enough flexibility for people who can be paid a lot more by the private sector”. And a Whitehall civil servant told us that pay rates do not necessarily harm recruitment – but they do affect retention.

Several interviewees explained that public sector salaries need to be considered in the context of career risk. An NHS chairman observed that a high number of interim chief executives run trusts in England because making mistakes is seen to cost people their jobs, explaining that “there are no chief executives now because if they slip up, they’ll be shot. We need to accept people make mistakes”.

“Pressures on public sector leaders are shifting in some subtle but critical ways, and talent management needs to be energised across the sector.”

Public sector leaders on leadership

“There are no chief executives now because if they slip up, they’ll be shot. We need new leadership and we need to accept people make mistakes.”

“Leadership is how you make people feel part of doing something different and special.”

“Leadership before was about leading your own people but now it’s going to be about corralling people over which you have no direct control.”

“There’s a scarcity of leadership across the health sector. You can see that in the number of vacancies in chief executive and finance director posts.”

“The public sector needs to be at the top of its game. We need strong, clear, high profile public leadership.”

“We need to say to the public, this is a proper partnership and that’s where the leadership comes in.”

“There’s got to be more opportunities for moving people between public services. Not a lot of that goes on but the leadership is the same, it’s just a different context.”

“We need to place a premium on effective leadership – that’s key to delivering.”

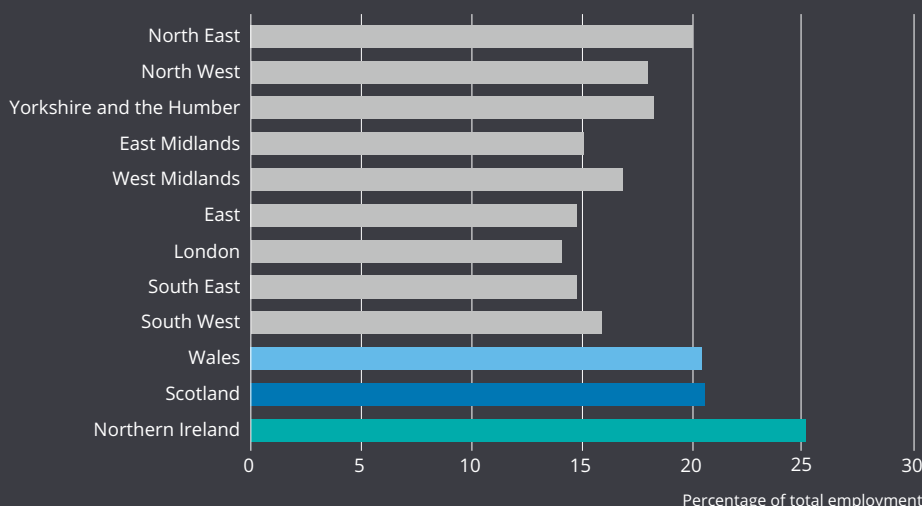
“Attracting talent is a challenge and paying salaries is a challenge.”

“When we need to recruit, I will think that we’re not paying enough of a salary but the councillors will think that it’s crazy money.”

Devolved governments of the UK

Since devolution began in the late 1990s, the UK's devolved administrations have continually diverged from Whitehall as each exercises its powers. Politically, successive elections have seen the distance grow between Westminster and Holyrood, Stormont and the Senedd and this year, the EU referendum result has seen the devolved administrations distance themselves even further from the UK Government. This chapter of *The State of the State* explores governments around the UK alongside quotes from our interviews with public sector leaders.

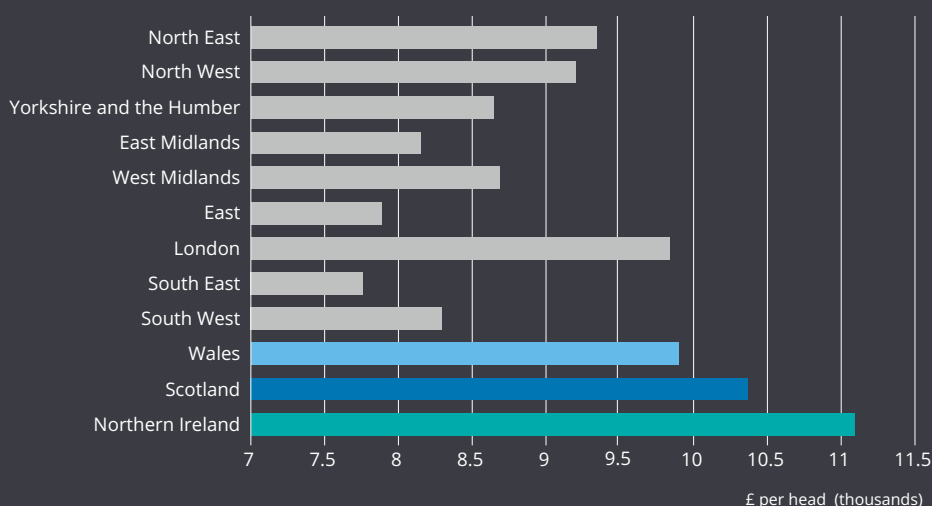
Figure 26. Public sector as a percentage of total employment



The public sectors in the UK's four countries differ significantly in their employment and spending profiles. Figure 26 shows how the proportion of public sector employees varies across the UK, with the highest proportion in Northern Ireland at 25 per cent of all employment compared to the UK average of 19.6. Figure 27 shows how the same pattern is reflected in spending.

Source: Office for National Statistics, June 2016

Figure 27. Total identifiable spending per head on services



Source: Public Expenditure Statistical Analyses 2016, HM Treasury figures for 2014-15

Northern Ireland:

The state of the state

More cohesive political leadership has created an opportunity for Northern Ireland to accelerate change already underway in its economy, communities and public sector. But at the same time, the effects of Brexit raise unique concerns for the region. That combination of opportunities and risks mean this assembly term could shape Northern Ireland's prosperity for generations.

Last year's *The State of the State* observed how the complex politics of a five-party coalition hampered decision making in the Executive. In contrast, negotiations after this year's election established a two-party government, plus an independent minister, that quickly created a sense of optimism, energy and confidence in Northern Ireland's future.

That was achieved in part through the publication of a Programme for Government framework which focuses on outcomes and against which the Executive will be held to account. Government-wide plans can fail to gain traction or credibility, but Northern Ireland's programme appears to be permeating the public sector – at least at this early stage. Crucially, ministers recognise that their ability to deliver against the programme will be judged at the 2021 elections.

The formation of a first official opposition is a further sign of maturing government in Northern Ireland that will help build confidence in its governance and stability. And effective oppositions do not just hold administrations to account for actions after they have been taken – they help instil a sense of diligence and forethought in ministers and officials keen to avoid criticism.

While political complexities stalled decisions in the last Executive, the Northern Ireland Civil Service was still able to reduce its headcount by 17 per cent within two years and reduce its number of departments by a quarter. Leaders recognise that the Voluntary Exit Scheme used to reduce staff numbers was a blunt instrument that has affected the administration's ability to deliver as well as morale. However, it has set Northern Ireland's public administration on a more sustainable footing and its leaders are now focused on people-centred and cultural change. As across the UK, Northern Ireland's public sector recognises that it needs more capability in managing transformation.

Economically, this decade has seen a renaissance for Northern Ireland that has exceeded expectations. In 2011, the Executive set targets for Invest Northern Ireland, the regional business development agency, to promote 25,000 new jobs, attract £1 billion in employment related investment and stimulate £300 million of investment in research and development over five years. By 2016, the agency had promoted 42,488 new jobs, attracted £3 billion in employment related investment and seen £589 million invested in research and development. Arguably the agency's biggest success has been in growing Northern Ireland's reputation to corporates globally.

The central economic challenge for Northern Ireland now is to continue on its positive path by playing to its strengths and focusing on industries – like cyber security – that are growing and can help maintain investment momentum.

Whilst Northern Ireland may be on a promising path, the region is uniquely exposed to Brexit. It will become home to the UK's only land border with an EU member state, and while the Prime Minister has assured leaders in both Northern Ireland and the Republic that it will not revert to a 'border of the past', some form of access and customs control seems inevitable. Northern Ireland is also a significant beneficiary of EU funding that aims to support places at economic or social disadvantage. That has included €1.3 billion since 1995 for the peace process that has funded the creation of shared spaces between communities, victim support and urban regeneration. Three waves of funding have been deemed so successful that the programme is shared as a peace-building exemplar in other regions of the world.

Northern Ireland's fishing, farming and food industries are also significantly exposed to Brexit. A letter from the First Minister and Deputy First Minister to the Prime Minister this summer stressed the vulnerability of the agri-food sector both to the loss of EU funding and to trade barriers with the single market.²⁰ Clearly, Northern Ireland's political, business and community leaders need to be fully engaged in Brexit negotiations as they unfold.

"More cohesive political leadership has created an opportunity for Northern Ireland to accelerate change already underway in its economy, communities and public sector."

Those negotiations will need to consider how they affect Northern Ireland's attractiveness for foreign investment. While inward investors will have been attracted because Northern Ireland is within the EU, they will also have been attracted because it is part of the UK – so there may be positive dimensions of Brexit to explore.

The formal process of leaving the EU may be underway when Northern Ireland is able to reduce its corporation tax in April 2018 to bring it in line with the Republic of Ireland's rate of 12.5 per cent. Analysis from Ireland's finance ministry suggests that if its corporation tax had been 15 per cent from 2004 to 2012, the number of foreign companies locating in the country would have been a fifth less. That suggests a cut could add to Northern Ireland's attractiveness – and it would also bolster the argument for further fiscal devolution to the Executive. The combination of mature government, high calibre ministers and continued economic opportunity suggests that Northern Ireland is ready for the next phase of devolved power.

Public sector leaders on Northern Ireland

"A big full stop has been put down on what has happened before. The previous five years was hallmarked by...if there was a desire to do anything, getting it done was almost impossible. Now there is a freshness: a rebooting of government."

"There's a lot of joined-up agreement between the parties. It's a better political environment. I hope we're seeing a maturing government."

"The programme for government is not just a framework, it will permeate government. And it will allow some difficult conversations like 'if you're not pursuing the programme for government, why are we doing this?'"

"We've produced a leaner and more productive civil service in the biggest changes since 1973, but it's largely gone under the radar."

"Attracting talent is a challenge and paying salaries is a challenge. It's very hard to attract people here unless they have a reason, like relatives here."

"Northern Ireland needs to accept the reality that we're a small, regional economy. But we have to ask what type of economy we want. What's our potential? What are we good at?"

"We need to become a more competitive economy. We are not what we were in industrial times. But we can be a big player again, but at different things."

"The level of reduction in Northern Ireland's public sector has not been as steep as in England. But spending has not grown at the rate it did, and that's had an impact."

"There are hard decisions ahead of us to live within our budget."

"We'd like to have more fiscal powers. Let us control the stuff."

Scotland:

The state of the state

In 2014, the independence referendum accelerated further devolution to Scotland. Two years later, the EU referendum has marked a second inflection point in Scotland's relationship with the UK. While the constitutional extent of any changes remains to be seen, Scottish Government policy certainly continues to diverge from the rest of the UK in its approach to public spending and public sector reform.

Scotland stood out in the EU referendum result as the UK's most europhile nation. While the overall result saw 48 per cent of the UK electorate wish to stay in the EU, some 62 per cent of Scotland's electorate voted to remain. Unsurprisingly, the Scottish National Party Government moved swiftly to distance Scotland from the result and moot a second Scottish independence referendum that would see the country leave the UK, but remain within the EU. However, two potential barriers quickly became apparent. First, the EU is only able to negotiate departure with a member state – which is the UK – and second, the UK Parliament may need to pass legislation to allow for a second independence referendum.

Nonetheless, the Scottish Government has made the bold move to publish an Independence Referendum Bill for consultation.

Doubts were cast over the financial prospects of an independent Scotland this summer, when Government Expenditure and Revenue Scotland (GERS) figures showed that Scotland's deficit – the difference between public spending and income – is double the UK's overall deficit when measured as a share of GDP. That has been caused by the global slump in oil prices, which mean Scotland's share of north sea oil revenues has plummeted from £9.6 billion in 2011-12 to just £60 million in 2015-16. Commentators suggested that, under these conditions, Scotland would struggle to operate as an independent country. However, GERS data is produced for Scotland as part of the UK – it does not model scenarios for an independent Scotland in which the Scottish Government would be enabled to make its own fiscal choices.

“Scotland stood out in the EU referendum result as the UK's most europhile nation. While the overall result saw 48 per cent of the UK electorate wish to stay in the EU, some 62 per cent of Scotland's electorate voted to remain.”

The Scottish National Party Government elected in May 2016 came to power with a commitment to investment in the public services and a resistance to Westminster-driven austerity. Within weeks, the First Minister established a set of policy priorities that include substantial health and social care investment, a review of local government to redefine its role and changes to social security including an end to the 'bedroom tax'.

That programme for government was followed in the summer by the announcement of a capital spending programme of £100 million, which is expected to be drawn from 2015-16 underspends. Projects will be assessed for the funding based on how quickly they can start, the number of jobs they will create and their wider effect on the supply chain. If the UK Government decides to recalibrate its fiscal policy towards investment, it may take a similar approach. Whether this investment is enough to stimulate Scotland's economy remains to be seen – while the UK economy grew by 0.4 per cent in the first three months of the year, Scotland's remained flat.

Public sector leaders on Scotland

"The big thing on our radar is the performance of the Scottish economy. The Holy Grail is to get that right and have a more vibrant and resilient economy."

"Public sector organisations in Scotland have not been subject to the same financial pressures as the rest of the UK. The counterside to that is that we're seeing less innovation and less transformation as there has not been that drive. That's not to say the Scottish Government is not as ambitious as UK Government, and it's got a clearer vision."

"In Scotland, we've got the vision to put people at the heart of public services but we're not thinking through what that looks like in practice. We want to get in tune with the zeitgeist. Citizens want to be more informed and more in control."

"Brexit will take up a lot of politician and officer time and the stuff we need to be doing could get lost. The independence referendum saw stagnation and we might be entering that period again. All the other stuff will get pushed down the priority list."

"It's unarguable that Brexit makes a second referendum more likely, adding layers of uncertainty and complexity."

"Scotland has a significant reliance on EU funding for our rural economy, so there's uncertainty about what Brexit will mean for that."

"Demographic pressures are huge in Scotland. Our population is not growing as much as the rest of the UK and it's ageing."

"As a rural council, we need to grow our own talent because we're hours away from any city. We're fishing in a pool of people who want to come here and make that lifestyle choice. The NHS is the same."

"There's something about the public sector in Scotland that engages a certain type and a good slice of the younger generation. They come in with a desire to do something worthwhile."

"For Scotland, the answer... it's digital. But broadband is a huge rural issue."

Wales:

The state of the state

This year's Welsh Assembly elections saw a minority Labour Government formed with support from Plaid Cymru for a term of office that looks set to take Welsh devolution forward. After a legislative holiday to allow for the new political arrangements, the Welsh Government has laid out focused plans to stretch its new fiscal powers as well as a distinctive public policy agenda through six Bills in its first year.

"The Welsh Government has laid out focused plans to stretch its new fiscal powers."

The first two Bills in the new legislative programme – the Land Transaction Tax and Anti-avoidance of Devolved Taxes (Wales) Bill – are symbolic: they are the first tax Bills introduced in Wales in 800 years and build upon the establishment of a new Welsh Revenue Authority, currently underway.

The third Bill plans to challenge the UK Government's trade union reforms. While the Trade Union Act will impose ballot thresholds for public sector unions, legislation in the Welsh Assembly will aim to repeal sections that apply to the public services in Wales.

The fourth Bill will set out public health improvements, reintroducing a Bill from the previous Assembly. While its measures on public toilets, piercing and tattooing will be carried over, restrictions on the use of electronic cigarettes in enclosed public spaces will be dropped.

Fifth, the Welsh Government will legislate to better support children and young people with additional learning needs and sixth, legislation will abolish the right to buy and right to acquire in a bid to safeguard social housing supplies.

That legislative programme – and in particular the Bills on trade union rights and housing – illustrate the diverging policy agenda between Westminster and the Senedd.

In the wake of the EU referendum, the vote's implications for Scotland and Northern Ireland attracted international attention, not least because citizens in those countries had voted to remain in the EU. In Wales, the referendum result of 52.5 per cent to leave the EU mirrored the UK result – even though 39 per cent of all Welsh exports go to the EU and the country is a major beneficiary of EU funding. Per head, every Welsh citizen received three times more EU funding in 2015 than every English citizen. And from 2014 to 2020, Wales received more than £2 billion of structural funding and Welsh farmers received £250 million a year in direct payments.²¹

Clearly, the central questions for the Welsh Government in Brexit negotiations are whether trade deals will support Welsh export industries and whether the UK Government will replace EU funding streams.

In contrast to Scotland, Welsh independence does not appear to attract significant support. According to an ICM poll, some six per cent of people in Wales would like to see the country become independent from the UK. However, a substantial 43 per cent believe the Welsh Assembly should have more powers, suggesting that the current direction of travel and continued devolution is meeting citizen demand.²²

"Clearly, the central questions for the Welsh Government in Brexit negotiations are whether trade deals will support Welsh export industries and whether the UK Government will replace EU funding streams."

Public sector leaders on Wales

"Wales is struggling with a whole range of issues that have come together. Financial issues, demographic issues, structural issues, navel gazing and demand. It's the sum of all those. You've got to question if that's too much to deal with at once."

"The Welsh Government got a shiny new toy with primary legislation, and boy has it played with it."

"The well-being act in Wales is potentially radical. It's about quality of life for people in this country."

"The financial situation is very, very pressurised for both revenue and capital. There are additional resources but they aren't keeping pace with demand and that's likely to continue for some time yet."

"Public services are...incapable of focusing on outcomes rather than outputs. We need to rethink the narrative to talk about what matters to people."

"There are some things the Welsh Government had expected EU funding to be available for, so that's creating some tension."

"The pace of change [on digital] has been driven by the all-Wales body. Locally we might have made different choices, but I see the benefit of the national standards."

Recommendations

Our analysis for *The State of the State* leads to five recommendations:

1. **Government should maintain its focus on business as usual throughout Brexit – and that includes transformation.**

While Brexit is an era-defining challenge for Whitehall and the devolved administrations, the public sector needs to maintain focus on business as usual. And even if a fiscal reset makes additional public spending available, the Government should continue to drive transformation – not least in the NHS, which is a clear public priority – and work with the sector to agree a constructive and positive vision to replace the cost-reduction narrative of austerity.

2. **Brexit is an opportunity to rethink rather than recreate.**

Leaving the EU may require the UK public sector to take on new responsibilities currently undertaken through EU membership. As the UK's departure is negotiated, Whitehall and the devolved administrations should be prepared to rethink processes rather than recreate them, making sure that technology is fully exploited.

3. **Energise digital transformation by changing organisations one step at a time while maintaining momentum.**

Public sector leaders are frustrated by the pace of digital transformation. Our experience suggests that public bodies shift to digital best when they hack away at their organisation one step at a time – within a wider digital vision, and with relentless momentum – while avoiding the trap of simply digitising existing processes.

4. **Public sector reform needs to focus on engaging the citizen.**

Our research finds that citizens believe the public sector does not listen or personalise services as well as the private sector, and that the relationship between the citizen and the state needs to mature in order for demand to be reset. Public bodies can address these issues by energising their engagement programmes and making sure their leadership is outward-facing and high profile.

5. **Celebrate, value and support public leadership.**

Recent events have piqued the need for effective public leadership. Brexit adds substantial and complex demands on government departments, new threats are altering the nature of policing, patient and staffing pressures continue to challenge the NHS, financing reforms place a new emphasis to support economic growth on local government and citizen expectations continue to change. At the same time, public sector salaries can struggle to attract and retain the right talent and scrutiny can be intense. Our research suggests that the Government needs to celebrate, value and support public sector leadership by ramping up its capability and leadership development activities as well as supporting leaders who take the sector forward.

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