Optimising Finance in the Public Sector

by Shane Mohan

Shane Mohan outlines how government financial managers can deliver the future of finance to their organisations.

Financial management in the public sector is complex. Multiple, sometimes conflicting, short- and long-term priorities must be addressed. Budgets, borrowings and taxation need to be balanced against support for economic growth, investment in infrastructure and increasing demands for public services.

Over the last decade, Government has had to manage these tensions in the face of great financial turmoil, globalisation, demographic change, technological disruption, and in more recent years an economic upturn accompanied by an uncertain policy environment (with Brexit currently the dominant issue).

In our recently published 'Future Finance' report, Deloitte examines how the public sector finance function is evolving against this background. We have identified key priorities for government financial managers and the key enablers we believe will help in driving a future-orientated finance function.

We've spoken to the people at the coalface in this regard – insights for this report were generated through interviews with senior government finance specialists in nine European countries (Ireland, Austria, Denmark, Finland, Germany, Luxembourg, Netherlands, Norway, and the UK), as well as through input from Deloitte experts.

The financial backdrop

The financial context for public sector managers has evolved significantly since the economic crisis.

A decade on, European economies are in a healthier position. The EU as a whole has experienced moderate GDP growth, averaging 1.8 per cent from 2012 to 2017.

Government budget deficits, which increased substantially to an average of 6.6 per cent of GDP in 2009 for the EU-28, have largely been brought back in check, and averaged 1 per cent of GDP in 2017. These changes reflect not only the recovery in GDP growth but also public spending restraint and prioritisation.

According to OECD data, social spending across Europe has risen over the last decade in response to growing health care and age-related expenditure demands. While significant cuts were made in an effort to balance the books – for example, in operating expenditure (notably public sector wages) and in capital investment - average public sector debt in the EU nonetheless rose substantially from 58 per cent of GDP in 2007 to 81.6 per cent in 2017.

Ireland is clearly an outlier in Europe in terms of our own growth trajectory, with average GDP growth of 11.5 per cent/modified GNI growth of 7.5 per cent in the five years to 2017. Our government debt and deficit, which spiked following the crisis, have shrunk significantly relative to both GDP and GNI.

Persistent and emerging challenges

The financial crisis might have receded, but European governments, including our own, continue to face a range of external and internal challenges, and persistent budget pressures.

A modest upward trend in interest rates (in the UK and US at least) may present new challenges to fiscal sustainability, given high levels of public sector debt. There are also threats to tax bases, for example from globalisation, an ageing workforce, new technology (e.g. sharing economy business models) and regulatory changes (e.g. international tax reforms). Meanwhile, governments are experiencing shifts in requirements for social and infrastructure expenditure, related to population changes (most notably, due to care for the elderly and migration flows).

At an organisational level, interviewees commented on challenges in:

- Connecting financial managers with the broader administration and with political leaders
- Obtaining an accurate view of the public sector cost base, returns on investment and forecasts
- Balancing the financial demands of short-term priorities against "big ticket" investments to deliver efficiency in the long-term
- Balancing requirements for central financial supervision and control with delegating more autonomy to line ministries, agencies and local government
- Recruiting and developing a workforce with the required skills for 21st century financial management. Tax and legal, data science and digital skills were listed as key gaps.

While the external pressures on public finances are being mitigated to some extent through fiscal policy – for example, through taxation or pension reform – there is pressure on financial managers to do more with less. They must also operate in a much more flexible and insightful manner to respond to their dynamic operating environment.

Priorities and trends for the 'Future Finance' function

Our research identified a number of priorities and trends for public sector financial managers:

- Generating further efficiencies – moving beyond rationalisation and consolidation, and leveraging technology to drive efficiencies. Suggested measures to support this agenda include ongoing efficiency reviews and exploring the use of technologies such as robotic process automation, cognitive and cloud computing.
- Balancing oversight with operational autonomy, including preserving reputation with creditors and providing operational flexibility to budget holders. Measures that can help with these include performance-based budgeting and blockchain for audit.
- Improving decision support – how to best evaluate proposed investments, accessing and using the best data for decision making and connecting with the rest of government. Measures that can support improved decision making include data analytics for modelling, planning and forecasting, and accrual accounting.

Delivering performance improvements

A range of initiatives are under way to improve decision support, balancing financial oversight with operational autonomy, and supporting efficiency in the finance function. Government finance teams are reforming accounting and budgeting practices and are moving towards using a wide range of emerging technologies to record, analyse, and transact government business.

At Deloitte, we have identified three key enablers that can support finance teams in their efforts and that will allow performance improvements in the finance function. These are as applicable in the Irish context as they are elsewhere in Europe.

Enabler 1 – People

One of the biggest gaps to fill to enable finance transformation is on the people side – replacing retirees and addressing years of under-recruitment, and at the same time acquiring a whole new set of skills and capabilities. Finance teams in the public sector need professionals with a range of strategic and technical abilities to support the effective implementation of ambitious programmes for change.

Connecting the finance function with the rest of government business is important, and developing the concept of business partnering is a means of doing this. Business partners are finance professionals who work with policy-makers and operational parts of government to support and inform management decision-making. Such structures will allow finance professionals to help policy-makers manage performance, plan the business, provide insights and support decisions.

Along with the appropriate structures to support business partnering, strategic skills and capabilities are required in areas across planning, budget forecasting, data analytics and financial reporting, combined with knowledge on topics as diverse as regulation, taxation and international business. In addition, finance business partners require strong interpersonal, negotiating and influencing skills, and a good understanding of the business area they support.

Professionals at the operational end of finance will need to understand how to optimise processes using digital technology and understand how finance operating models can evolve across policy areas, business support and shared services.

Unlocking this potential will of course require investment – the value of channelling resources into training and recruitment cannot be underestimated.

Finally, embedding a culture of adaptability and innovation is vital to supporting transformation within a rapidly evolving environment. Embracing practical, yet novel, approaches to service design and delivery, such as design-thinking, can help foster a more positive and creative view on change within organisations.

Enabler 2 – Digital

Digital tools such as RPA, cognitive computing and analytics, are allowing finance managers to move from routine manual processing tasks, and affording them more time to interpret, analyse and add value from a strategic perspective.

As digital technologies are evolving rapidly, finance managers need to make continuous efforts to identify and assess potential technologies, in order to boost internal capabilities within the function, as well as to respond to external challenges, such as tax fraud. Embedding routine digital foresight activities, such as horizon scanning, into finance function activities can help teams anticipate digital challenges and opportunities arising for new technologies.

In turn, responding to the pace of disruptive change requires investment in IT systems and solutions which afford flexibility. For example, core systems which can support cloud technologies and software as a service can provide for more responsive, low-risk, low-cost investments in the long run.

Enabler 3 – The Business Case

Government finance teams are becoming more analytical in their investment decisions. As with any change initiative, securing buy-in and sponsorship from the highest levels in government is crucial. Strong leadership is needed to promote a clear vision and culture of innovation, highlighting the benefits of change initiatives and instilling confidence in those undertaking change and those impacted by it.

Business cases to support change in the finance function need to reflect the level of external disruption and the pace of technological change. Budget holders expect swift proof of concepts and faster returns on investment. Short pilots and proofs of concepts which highlight tangible benefits upfront can help secure buy-in.

Over the course of our interviews for the Future Finance report, we noted that few interviewees were tracking benefits. However, where this was done, it was viewed as highly beneficial. Benefits tracking should be applied in the widest sense. For example, the return on investment for robotic processing does not need to be about cost-cutting. It should relate to the broader organisational agenda – for example, removing employees from tedious tasks, making task planning more flexible, and achieving performance and quality improvements. Identifying and quantifying such measures and tracking their outcome will help maintain the momentum required for any performance improvement initiative.

Yes, public financial management is complex. However, by implementing the measures and using the enablers identified, government finance teams can navigate this complexity to deliver a stronger, future-proof finance function for their organisations.

For more information, please see our report at deloitte.ie/futurefinance.

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