Strategic Management for Public Services Delivery

Jan-Erik Lane

Pacific Institute of Advanced Studies in Development and Governance, University of South Pacific, Fiji

Abstract

After the many years of public-sector reforms in advanced capitalist democracies, a concept of strategic management for the delivery of public services would be highly relevant for the conduct of operations by public organisations, or bureaux, as well as in schemes of outsourcing. However, it must take into account the specific features of the public sector (such as the occurrence of bounded rationality and the risk of garbage-can decision processes) as well as the implications of the rule of law. Outcome measures constitute the starting point in the derivation of public-sector strategic management. As the 'new public organisation' replaces bureaucracy, then the flat and boundary-less organisation will need more of a strategic management focus, especially when combined with outsourcing.

Key words

strategic management; new public management; public sector; organisation; public services

Introduction

The concept of management originated in the private sector with respect to large firms. It locates a sphere of discretion for top echelons of private firms, being situated between the shareholders, on the one hand, and the workers, on the other. This senior management decision-making is strategic in orientation, to the extent that it concentrates on goals and the selection of main action alternatives with a view towards the future (Brown *et al*, 2004). How relevant is this concept to the public sector?

Advocates of the New Public Management claim that strategic management fits well into public-sector governance, although there are still sceptics who argue that public administration is the proper framework for the study of the execution and implementation of government policies (Fredrickson & Smith, 2003). Public administration underlines the rule-oriented nature of public sector decisions, as well as the strong position of the politicians as the 'owners' of public resources in deciding on public-sector ends and means. In contrast, strategic management in private firms presupposes that senior managers are at arm's length from the shareholders, as the managers of private resources have enough autonomy to engage in decision-making about organisational ends and means in the future.

Reforms have pushed the public sector in the direction of strategic management (Ferlie *et al*, 1996; Pollitt & Bouckaert, 2004), especially in countries where the New Public Management philosophy has been endorsed officially (Pollitt *et al*, 2004). Agency autonomy has increased, as politicians often concentrate only on goals, leaving the implementation of policy to so-called executive agencies. Policy objectives tend sometimes to be ambiguous and complex, leaving considerable space for alternative ways of executing policies. Finally, technology has developed, increasing the degrees of freedom in choosing alternative means, for example, internet government. As politicians and agency chief executives sometimes work together in public-sector governance, the question arises of how they can steer the organisation towards desired outcomes, or improved performance. What are some of the typical choices that senior management would face in public organisations? I suggest that the concept of strategic management may elucidate the situation.

Strategic management has no established definition. One may wish to remain sceptical as it smacks of fads and fashions. The question is, however, whether it is so similar to concepts such as strategic planning, comprehensive rationality, and top-down management that it will be so critiqued that it falls apart (Mintzberg, 1993). Yet, strategic management should, rather, be linked with the theory of the new public organisation on the basis of the theory of contracting under asymmetric information – economic organisation theory that stresses incentives in contracting (Tirole, 1993; Ricketts, 2003).

Strategy against tactics

It holds true that even though the concept of strategy is vague it is still highly useful for the analysis of decision-making processes, for instance, in military affairs, private firm management and in game theory in general (Dutta, 2000). With respect to the public sector, where agencies vary greatly in size from the minuscule to the gigantic, the public choice literature analyses several organisational strategies, including bureaux expansion, bureaux reshaping, bureaux autonomy and bureaux turf. Their analytical focus is the implications of the bureaucrat's egoism, which, sometimes, drives bureaux towards inefficient levels of output and the capture of slack, which, sometimes, shapes their activities towards prestigious tasks (Dunleavy, 1991). In public administration, there can be found a strong emphasis on the collective, yet self-centred, interests of an almost immortal or impenetrable agency, inevitably generating resistance to change and reinforcing established procedures (Kaufmann, 1989).

The policy network approach, on the other hand, underlines the interdependency of agencies on private partners in order to get the job done (Kickert *et al*, 1997). The New Public Management suggested a strong remedy against both agency autonomy and agency inefficiency, namely outsourcing the provision of services, or the contracting out of public services provision. Osborne and Hutchinson's (2004) version of reinventing government entails undoing the classical institutions of bureaucracy, and putting the provision of almost all services on a system of short-term contracts. Today, there is a realisation of the limits of contracting out in the post-New Public Management era, as agencies attempt to focus on their core activities, underlining the importance of achievement of social objectives over productivity (Lane, 2005).

Strategic management in a post-New Public Management assessment of public service delivery would focus on the achievement of social objectives of provision, taking them as the guiding indicators in the design of public organisations and their conduct of continuous operations. What matters first and foremost is the effectiveness of the agency in meeting its social obligations. The constant public sector reforms have in many places led to a hollowing out of the state (Peters & Savoie, 2000). The provision of public services has strong distributional consequences, which implies that state contraction leads to increased inequality or, even, more poverty. The occurrence of garbage-can decision processes (Pollitt, 2008) does not, however, undo the relevance of a normative framework focusing on strategic management, as 'is' does not entail 'ought'.

At the same time, public sector reforms have increased the awareness of the importance of strategic choices about how best to provide public services. Markets may provide, or help provide, services designated as 'public' or 'essential' and there are several ways to contrive market provision through the employment of various tendering and bidding schemes.

The theory of strategic management should be seen as a normative approach to public service delivery with no claim to being able to describe ongoing practices. Whether, and to what extent, this occurs is an interesting question but strategic management is more about what is feasible in terms of public-sector reform. It asks: given the demand for efficiency, how is it best to design public organisations that are more prone to engage in strategic management, despite all the factors that lead to myopia, organisational slack and organisational autonomy?

The concept of strategic management when employed for the analysis of decision-making is complex and perhaps not a very precise one. It engulfs a variety of different kinds of decision-making: the lowest level of strategy is operational strategy, which deals with day-to-day operational activities, such as scheduling criteria. Business strategy is the aggregation of operational strategies of a single private firm or of strategic business units – a semi-autonomous unit within an organisation – that is responsible for its own budgeting, new product decisions, hiring decisions, and commodity pricing decisions. In a diversified private firm, business strategy refers to the way in which it competes in its chosen market segments. Corporate strategy is the overarching strategy of the diversified private firm, answering questions like: in which businesses should we compete? How does being in one business add to the competitive advantage of the corporation as a whole? The concept of dynamic strategy aims to portray firm strategy, both business and corporate, embracing ongoing strategic change and the seamless integration of strategy formulation and implementation. But these conceptions of strategy do not sit well in the public-sector context, except, perhaps, for the incorporated public enterprise. What is needed is a conception of strategic management that applies to the provision of core services by the public sector.

The specificity of public services and the limits of an algorithm for public services

A public service is not like a business area such as a multi-purposes private firm operating in the marketplace:

- it is an activity undertaken by a political body, governed often through democratic political processes
- its provision is regulated in public law, meaning that the public employees or bureaucrats providing these services have to act within the framework of rule of law (Lane, 1996)
- it is partly or wholly financed by taxes.

Strategic management has to accept these restrictions. What would strategic management signify? It belongs to the rational theory of organisation and it shares with other rationalistic approaches the weakness that it does not describe organisational reality accurately. It is easy to point out that in the public sector strategic management is political, which may raise much resistance and may end in organised chaos. But let us here focus on the potentiality of strategic management and what its promise would be in a period of public-sector reform.

Of course, strategic management would be constrained in the public sector. The politicians constitute the principal and the managers are merely their agents. The legal framework of the public sector would also narrow down choice options in order that rule of law may be accommodated. A most serious constraint is the lack of any viable or verifiable indicator of the value of public services that are not traded in the marketplace sector. While public services paid for wholly or partly by taxes do generate value, it is not easily measured. The problem is that strategic management seeks to maximise value, given choice constraints, but what if the measurement of value is not forthcoming automatically or unambiguously? The public manager must, thus, start the process of strategic management using a proxy measure of value, like, for instance, policy objectives and their corresponding outcome indicators.

There are also other more troublesome considerations to take into account when calculating a strategy for the provision of public services. These derive from the key insights into the way public administration works in reality and result from either self-interest seeking tactics (myopia) or confusion (ambiguity) on the part of participants, and they are very difficult to operationalise.

Objectives and the relevance of outcome indicators

Politics and politicians set more restrictions on public organisations than ownership boards set on private firms. In public organisations, goals tend to be ambiguous and complex, meaning that the government would be more hesitant to delegate much decision-making on objectives to agency managers. Since public-sector activities tend to be regulated by means of public law, the room for change is more confined. Yet, at the same time, agencies are not merely oriented towards the technical aspects in fulfilling goals, handed down by politicians. Agencies participate in the discussion on the selection of objectives, both by evaluating existing goals and suggesting new future goals. This stands in contrast to the private sector, where private owners, given that the goal of profitability is fulfilled, would not interfere in the conduct of a firm's strategies, although they would want to approve of major changes.

This is not to deny that much of strategic management at the agency level consists of how best to get things done. Strategic management is operational, meaning that it targets the structure of the main public service activities and determines how they are to be carried out. Whereas it used to be the case that there was one mode of production of public services – tax-financed bureaucracy – it is now the case that the choice among alternative forms of provision calls for deliberate strategic thinking.

Strategic managers in the public sector face the problem of maximising or satisfying a set of goals, some derived from within the agency while externally imposed. Failure to achieve those goals will elicit criticism, albeit at the risk of being fired. This is a fundamentally outcome-focused perspective on public management. It is only viable if outcomes can somehow be measured and compared, and their meaning verified, in a non-costly manner. The development of evaluation methodology in the social sciences now allows for the employment of a variety of outcome measures. Such outcome criteria may target:

- number of services produced
- quality of services
- satisfaction with services
- quantity and distribution of services
- unit costs.

Strategic managers would face specific objectives for each of these outcomes, which would state the direction of change that managers need to embark on in order to achieve these objectives and, therefore, improve service outcomes.

It is, thus, the stated outcome indicators and their interpretation that should guide strategic management in the public sector. Most core public services are provided without charge and are funded through taxation, which means that strategic managers need some kind of information about what value they produce for end users. This means that the designated outcome measures become a proxy for the utility derived by public-service end users and stakeholders. Outcome measures offer both benchmarks for the monitoring of activities and suggesting where improvements could be made. The agencies may wish to turn to professional policy analysts or evaluation specialists in order to have this outcome information. Without it strategic management would fumble in the dark, choosing alternative modes of organisation without key outcome reference points (Joyce, 1999; McLaughlin *et al*, 2001; Stacey, 2007).

Team production: the relevance of stability and employee satisfaction

To achieve public-service provision objectives, the strategic manager uses an allocation of resources, which used to be measured in terms of physical and labour resources but today are measured in terms of a financial allocation, allowing the managers more leeway as to the choice of production functions. From the strategic point of view, the strategic public managers would face a few critical choices:

- the size of the team
- the composition of the team
- the allocation of tasks between internal production and outsourcing.

All three of these choices would be resolved, one way or the other, when the contracts are handed down and signed. At the end of the day, strategic management is about contracting. Performance and remuneration constitute the essential elements of contracting in the public sector, just as it is in the private sector. They will reflect the bargaining power of managers, on the one hand, and of employees, on the other.

In the classical model of public-sector management the implementation of a master plan, calculating the optimal rates of performance given full knowledge of the effort levels of employees linked with alternative payment schemes, symmetric information and strategy-proof behaviour are assumed. Since all is, in principle, known or knowable, strategic management comes down to a question of computation, deriving a set of algorithms for performance – remuneration schemes that build on sincerely held preferences and automatic enforcement of agreements. In reality, however, contracting always involves uncertainties, unknown even unknowable risks, insincere preferences, tactical behaviour with guile, and asymmetric information (Hiller, 1997). Strategic management can only reduce these limitations on rationality with redundancy, slack and duplication.

Size of the team

If there was a true algorithm available for the size of the crew to bring on board when sending out the aeroplane to deliver public services at some location, then strategic management would calculate the exact number that need to be employed either in-house or outsourced. Theoretically, given perfect information and no transaction costs, the optimal size of the workforce is where the marginal product of labour is equal to the marginal cost of labour, with each unit of labour receiving remuneration corresponding to his or her marginal value product. However, in team production functions the exact values of these variables tend not to be known or to be unverifiable. The result is that teams tend to be larger than optimality and remuneration tends not to be set at the level of marginal productivities. Yet, the total value of the public services output must be greater than the total cost of its production, if the net value of that output is to remain positive, which means that the size of the team has to be cut back in order to achieve this outcome.

The New Public Management launched an attempt to disclose the basic parameters of team production by aggressive outsourcing and contracting in. However, there is a definitive limit to the usefulness of such forms of contracting, as they lead to staggering transactions costs in relation to the making and enforcement of all the contracts and tournaments. Yet, in team production the optimal team size is seldom fully known, due to asymmetric information (Rasmusen, 2007).

Structure of the team or organisational design

Providing public services is a labour-intense process. Only recently has the massive employment of information technologies started to change the structure of organisations by empowering lower echelons to do more advanced work at the expense of middle-level supervisors. New insights from organisation theory, based on the evolution of technology, suggest that the old model of bureaucratic organisation is no longer as relevant as it used to be (Kernaghan *et al*, 2000). The relevance of strategic management thus needs to be evaluated in the context of the 'new public organisation'.

Organisational design is the design of an organisation's structure: functional, divisional, and matrix. Functions or divisions belong to mechanistic organisations, which has been the traditional or classical design in many medium- and large-size organisations. It is rigid in form with often clearly delineated jobs, a well-defined hierarchy with a formal chain of command for decision-making and control. In contrast, an organic structure is more flexible, and more adaptable to participative forms of management. Organic organisations that have a flat structure with only one or two levels of management – offering a decentralised approach to management – would stimulate greater employee involvement.

A matrix organisation is one in which teams report to two or more managers. Matrix structures may include functional and divisional chains of command simultaneously in the same part of the organisation, commonly for one-of-a-kind projects. Boundary-less organisations are similar to flat organisations, with a strong emphasis on teams, where cross-functional teams dissolve horizontal barriers and enable the organisation to respond quickly to environmental changes and to spearhead innovation. The flat organisation calls for a learning organisation to facilitate team collaboration and the sharing of information; more able to adapt and respond to change than a hierarchical organisation. This design would empower employees to acquire and share knowledge and apply this information to decision-making.

The so-called 'new public organisation' has a flat organisational structure instead of the hierarchical one, which would, somehow, have to be governed. If subordination in terms of a formal structure is not to be used, then perhaps only strategic management can direct teams towards the achievement of their objectives, to be evaluated in terms of either productivity or effectiveness, or both. No doubt, employee satisfaction has played a major role in the transition from a hierarchical organisational structure to a flat structure. Also, technology has made it possible to empower lower-level echelons. Thus, strategic management offers a tool for co-ordinating the activities of an agency that is less mechanistic and more boundary-less in form as well as learning (Ashkenas *et al*, 1998).

Contracting and teams: monitoring versus transaction costs

Public service provision can be looked on as a contracting problem with a huge set of contractual situations involving a variety of people: politicians, higher-level managers, middle-level managers and the street-level bureaucrats (for in-house provision), and contractors (for outsourced provision). Making use of the insights of economic organisation theory (Ricketts, 2003), strategic management, when used to determine the size and structure of teams, addresses the problem of mixing in-house production with outsourcing. In reality, this is a contractual question, which occurs in all forms of team production and involves three different types of contracts and their surveillance:

- long-term employment with monitoring versus short-term outsourcing with constant tendering
- *ex ante* and *ex post* contract disparity
- contract monitoring costs (in-house provision) versus switching costs (outsourced provision).

When people are employed in teams, the contract tends to have a longer duration than used in conventional buy-and-sell situations – spot contracts (Milgrom & Roberts, 1992). Thus, there arises the question of the fulfilment of the contract *ex ante* as distinct from *ex post*. The two may not correspond. The disparity between them may be very large, raising all kinds of questions about verification and counter measures against contractual reneging. Monitoring used to constitute the classical tool for minimising this disparity, involving, at the end of the day, the taking of disciplinary measures before termination procedures are engaged. It comes though, with a considerable cost in terms of running surveillance and taking disciplinary actions.

In the philosophy behind the New Public Management, switching contracts is a better method for minimising this disparity between *ex ante* and *ex post* contracts. Thus, the crucial issue now is whether monitoring costs are greater or smaller than switching costs. Advocates of the New Public Management would be inclined to argue that switching costs are smaller than monitoring costs, given the likelihood of collusion among agents. There are simply too many tactics that can be used in monitoring, making it toothless. Advocates of public administration would definitely argue that monitoring costs are smaller than switching costs, magnifying the costs of switching from one team to another. Two other considerations strengthen this proposition: stability in service provision and employee satisfaction.

Conclusion

The concept of strategic management is essentially a normative one, which may be critiqued for its assumptions, being unrealistic for agencies in the public sector. It belongs to the rational approaches to public-sector decision-making coming into conflict with the proposition that instrumentally rational decision-making is problematic in the public sector where agencies are not entirely self-determining (Mintzberg *et al*, 1998).

Yet, strategic management is not entirely without merit when debating the direction of public-sector reform. As a normative concept, it complements the tradition focus of public administration on bureaucracy and the rule of law by emphasising the need to achieve service-provision objectives through organisational design as well as governance objectives through the handling of contracts with the team responsible for public service provision. It fits well with the theory of the new flatter public organisation using information technology – the boundary-less learning organisation (Kernaghan *et al*, 2000). Such an organisation would need to defend its rationale through goals evaluation, done by strategic management, giving due regard to, and respect for, the constraints on management that come from bounded rationality as well as the rule of law requirements of the state.

The concept of strategic management appears highly promising when interpreting what is happening in public service provision after the onslaught of the New Public Management. It underlines the relevance of designing public services delivery systems so that they can deliver outcomes by taking normal incentives in a team of people, insiders or outsiders, into proper consideration (Koch, 2008).

Address for correspondence

Jan-Erik Lane
Pacific Institute of Advanced Studies in Development and Governance
University of the South Pacific
Laucala Bay Campus
Private Mail Bag
Suva
Fiji Islands

Email: lane_j@usp.ac.fj

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