How to Survive Budget Cuts— and Thrive

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IN 1994–5, AS THREE OF ITS SEVEN-MEMBER COUNTRIES LEFT EFTA (EUROPEAN Free Trade Association), a small international organization located in Geneva and Brussels, management was asked to cut its budget by about 60%—without reducing essential services to the remaining four members. I was part of the management. We survived and subsequently—if not consequently—thrived and trebled our output. This experience is of limited immediate value today, of course. Let us say that it has been a trigger, though, for my ensuing interest in the matter. Should I be asked the question: 'How did you do it?', my spontaneous (hence subjective) answer would be: 'Simplification and motivation, and as outcome: on the whole empowerment.' These two themes underlie my remarks today.

Budget cuts are acts of a lesser God. Only adroit adjustment brings survival. We must take budget cuts as an opportunity to enhance organizational strengths by implementing reforms. But what reforms?

Clear goals and objectives as well as adequate means are essential for the good performance of an organization—this is what we strive for. The private sector is very successful in achieving this balance. Profit expectations are its unfailing guide, no matter how numerous the objectives and the means of production—relative prices are the measure of all things. In theory, it is a matter of economic engineering.

Alas, a thick fog of uncertainty covers the world of action. One is forced to fall back on trial and error, which is fine, provided, one is able to ruthlessly decide what is to be pursued and what is to be discontinued. Profitable products survive on the shelves for another day. The enduring success of the market system is not so much in 'picking winners'—for conditions change continuously—but in identifying and disposing of 'lemons'; and doing so very quickly.

Economic theory is silent on how the process of trial and error should work. The existing market system has created specific institutions to implement it. As the economist Schumpeter pointed out long ago, *limited liability* (which makes risk-taking possible) and *bankruptcy* (which weeds out undeserving activities) are the twin pillars upon which the success of the market economy rests. In the end, command economies were bankrupted wholesale by their inability to secure the bankruptcy of particular activities.

To sum up, this is the much simplified view of how the really existing market system works:

(a) as part of a fully interconnected system, relative prices provide a guide for establishing production *priorities*;
(b) relative prices are a rapid and unfailing *feedback* system;
(c) bankruptcy is the unassailable mechanism for *weeding out failures*.

This short introduction is needed because in the public sector, there is a desire to be as 'efficient' as the private sector. The public sector is perceived as bloated, ineffectual, and in need of reforms. What better way to achieve this than by introducing private-sector methods?

As a preliminary step, private-sector terminologies and titles are introduced to replace the old and venerable ones—the ambassador now is to be the CEO—in order to underscore the drive for efficiency. Is it going to work?

If only it were so simple… Only if we knew how the private sector works at its core would we be able to mimic it effectively in the public sector. All the mouthing about the 'private sector' approach is otherwise just another exercise in 'cargo-cult'—natives on Polynesian islands building mock airstrips in the expectation of airplanes full of goods landing consequently.

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The public sector evidences the greatest difficulties in achieving a balance between objectives. Why? After all, the market is good at establishing

relative prices for various cars—on the whole, consumers do judge them in terms of one another. Why can't we 'make up our minds' when public choices are involved? The trouble is, public choices are about incommensurables. We have no unambiguous way of expressing health goals in terms of education, or security in terms of equity. Voting is as close to a 'pricing system' as we can get, but since the votes are not interlinked through the common denominator of the market—money and costs—voting can yield contradictory results (as Kenneth Arrow demonstrated long ago) and in any case it is little more than a 'beauty contest', for the voter does not reveal his preference in knowledge of the (financial) consequences of his choice.

I do not propose that there is a way to resolve this valuation problem, though we may be able to attenuate it by clever modelling. I can, however, point out one implication of this state of affairs. The political game inevitably promises more than can be achieved with the allocated budgetary means, which are essentially pre-determined. Imbalances ensue.

The issue of dealing rationally with the imbalances between goals and means is urgent. Today governments and administrations are drowning in their own policies. Or to use a contemporary image—ministries have become both 'policy- and administratively obese'.

This obesity has two main (interconnected) origins. The first one has already been mentioned: too many objectives for the resources at hand. Nothing new here—being overstretched is the fate of most past empires. What is new is the formal deliberative character of policy formulations today, which makes the selection process the more complex if not downright cumbersome. Lord Castlereagh wrote his own three-page instructions for the participation in the Vienna Congress, and read them out to his colleagues in the British Cabinet before he set off. The rest he winged. This would no longer be possible today, as we go out of our way to identify obvious and hidden stakeholders, and hear and heed minority views.

The other and more subtle (and contemporary) source of 'administrative obesity' is 'documentability', or 'transparency'. Driven by a sometimes prurient press, the public scrutiny of public policies and administrative processes has become an obsession. Every step is carefully 'lawyered' and 'due process' reigns supreme. The problem is compounded by technical feasibility: what the computer renders feasible, politics renders compulsory. Nothing wrong per se with transparency, but it comes at a significant cost.

The outcome is predictable. Self-administration and 'due process' verification displaces substance. More resources are used to achieve fewer and fewer outcomes—the layman's definition of 'obesity'. The consequence of 'policy obesity' is a lessened responsiveness of the public sector to demands. If the public is dissatisfied, so are the civil servants. Motivation is declining rapidly, even in elite ministries like Foreign Affairs. A general call for reform—if not outright privatization—is heard, and this, in the short term at least tends to accentuate problems.

Is this the public sector's fate? Not necessarily. After all, the market too is not always good at 'picking winners'. But one thing the market is good at—weeding out poor products, thanks to bankruptcy. Here is a fundamental difference that needs addressing. How do we create an institutional mechanism for the public sector to achieve the same effect as bankruptcy in the private sector? How do we get rid of obsolete and ineffectual policies and processes?

The issue is one of good housekeeping, disposal of waste policies and processes. As we all know, housekeeping is a humdrum affair; it is not about picking winners, where glory and fame could be earned, or a place in history—or in the board room. It is about staying fit and lean—about terminating what is not essential, even if it is desirable.

This is also an ongoing task. If for no other reason, it has to be carried out internally. To this end *internal* or managerial accountability is needed—e.g. mechanisms equivalent to bankruptcy for less significant policies and activities. Today explicit mechanisms do not exist, even though necessity drives a haphazard process of 'muddling through'.

It is my intention today to explore administrative elements towards a 'bankruptcy' or 'redundancy' system for public administration. I propose:

(1) methods determining opportunity costs of activities in terms of time spent on them;

(2) in the event of new tasks, I propose mandating a simplification of tasks as well as binding offset in terms of existing tasks. There would be unassailable internal structures and processes to ensure that calls for simplification and offset are not just so much eyewash on the way to the next round of 'task creep'.

Time Management or Determining Opportunity Costs

It was the habit of one of my former bosses to congregate everyone every day for an hour for what we cynically called 'morning prayers'. Bored

with the proceedings, I once worked out that this autocratic display represented one whole man/year, or 6–7% of total available time for the chronically understaffed office. My boss did not like the finding.

Time budgeting is widespread in the private sector. The painter I'm about to employ will measure the square meters he is supposed to paint and multiply them by an empirical coefficient (usually supplied by the trade organization) reflecting the cost per square meter. Presto, he can make a fairly accurate offer of the cost.

We should adapt and adopt such a budgeting methodology. What if a meeting is called? The invitation would have to include a pro-forma estimate of the time and personnel involved. When you click 'send' on a long e-mail that you want to distribute to everybody and his brother, a window should pop up with this question: You are about to impose X hours of reading on the system. Do you really want to send it?

One would start by establishing the time cost of simple activities—such as a meeting. Progressively, using such simple building-blocks, more complex activities would be subject to budgeting. One could progress to 'collateral costs', once the direct costs have been better understood. How far one can go would be determined inductively on the basis of experience and needs.

It should be noted that such budgets are 'pro forma'. Their purpose is to provide the decision-maker with a *sense* of the effort involved in carrying out a decision. In this light, 'orders of magnitude' are sufficient. Orders of magnitude are more than sufficient in ranking the cost-effectiveness of planned activities. Once such a budget is established for, say a series of meetings, the task of choosing those worth attending becomes surprisingly simple. At least one government represented here today requires price tags for ministerial junket trips—with significant results. Why not generalize this?

When state enterprises in command economies were privatized, one major obstacle to increased efficiency was the lack of economic sense in the workforce. The concept of waste was foreign to them—they just did what they were told, and damn the cost. Does it sound vaguely familiar?

The mirror to time budgeting would be *time accounting*—recording how units and individuals have allocated their time between identified tasks and activities. In my concept, time accounting would not be used so much for individual control—it would be a record-keeping device aggregating rough quantitative data for assessment and planning purposes.

Why am I focusing on time? The largest single cost item in the MFA's

budget is personnel. Time management is the way best to use personnel. Far from me, the thought of gunning for full-scale centralized and inflexible time allocation: my ambition is far more modest. I'd simply settle for obtaining a fair idea of how time is actually spent or should be spent within the Ministry.

Once such basic elements are in place and validated by experience, we could move incrementally to more complex budgeting. What if the administration issues a new administrative rule? A prerequisite for approval would be an estimate of the time involved in its implementation. Too ambitious an objective? The software offered by the private sector, e.g. to manage expense accounts, comes with an estimate of the time involved in using it and thus the cost savings that can be obtained. Is it too much to ask from an administration that harbors ambitions to be 'as efficient as the private sector', by establishing for their in-house software, protocols and procedures of equivalent information?

As we move along further, we can establish the costs of certain policies. Pursuing 'human rights' issues does not simply involve the number of people in a Human Rights Division, but the work generated in other sections of the ministry and the diplomatic network. Once we have a rough idea of the cost involved, we can match this to outputs or even outcomes. Or we may use the values to obtain opportunity costs—what we forego in other areas: is it more effective and sensible to spend time on human rights, or on economic and commercial issues?

The next step would be to establish *indicative* time–budget benchmarks to be matched against time accounting data so as to spot blow-outs early on. The benchmarks would apply to individual policies, but also to the time allocation patterns of organizational units like an embassy, or the individual. An example: the benchmark could establish that an ambassador should not allocate more than 20% of his time to administrative tasks.

The benchmarks should function both as allocating devices as well as circuit-breakers aimed at avoiding work overloads from competing claims on available time of the individual or unit. To continue with the same example, as soon as the ambassador approaches his benchmark for time spent on administration, he should review his work and delegate or delete tasks, in order to stay within the benchmark. Armed with the quantitative data showing that the imbalance is structural, he may approach the center for remedy.

Benchmarks may be overridden—through a deliberate decision. The decision ought to be both justified and explicitly *compensated*, however.

Based on explicit findings, activities that no longer fit into the time allocation budget are declared 'bankrupt' or 'redundant' and struck from the list of tasks to be carried out.

More basically, what I propose is nothing more than making explicit and conscious what takes places anyway, in a hidden and muddled fashion. The alternative to the deliberate scuttling of redundant policies and activities is 'compensation creep'—units or individuals choosing on their own what to do first, what to do later, and what to abandon. We all have felt the effects.

Is my proposal not an additional burden on the harried civil servant? Yes and no. As work today is mostly mediated through the computer—even reading newspapers—the PC can be harnessed to gather data. The costs of certain patterns remain relatively stable. Once established, the data-gathering effort can be reduced to sampling. The key, in my view, lies in its impact on motivation. If it can be shown that such data-gathering and budgeting leads to work simplification, and a de-listing of obsolete activities—in other words, that this data-gathering effort makes a difference in the daily life of the bureaucrat—it will be quickly adopted. Moreover if it can become a tool of individual empowerment at the workplace, it will be a winner.

Towards a 'bankruptcy' process

I consider 'task overload' to be a major—if not the major—threat to the well-functioning of an organization; yet I see no structured, neutral, and effective way to deal with it.

'Task overload' occurs at the micro-level: the individual and the unit. It also occurs at the macro-level—the ministry as a whole. I propose to deal with both these issues in turn.

Within the framework of 'service contracts', e.g. between the embassies and the center or between the head and its staff—i.e. at the micro-level—annual tasks and activities are agreed upon. Once signed, these contracts (as their name purports) are binding for *both* parties. Changes in the 'service contract' would have to be negotiated, should new priorities emerge—as they will. For this eventuality, there should be explicit rights and obligations concerning a 'task overload'—an *obligation* to compensate for the new task by declaring an equivalent existing one redundant AND the *right* to refuse uncompensated new tasks.

This give-and-take approach should become a habit, and a sign of

mutual respect. In normal circumstances the process would be informal and flexible—most people are prepared to put in the extra effort, if it is properly acknowledged. This is obtained by the explicit provision of the 'circuit-breaker' ensuring that the bargaining can take place fairly and the outcome is not determined by authority or guile. Exercising the right of refusal—triggering the 'circuit-breaker'—is, like war, an admission of defeat for all concerned.

Such rights and obligations operate not only for individuals, but also for smaller and larger units. So I'd envisage both the ambassador and the embassy demanding (and receiving) compensation for an unexpected ministerial visit—lest they be turned into a glorified travel agency.

This, however, is not enough. There is no one to speak up for the integrity of the system as a whole and against overall 'task overload'. This is new. In the private sector, 'task overload' is not such an issue—why the public sector? For a good reason—if a firm wants to expand production, it is free to hire and obtain credit. As long as profits are confidently expected at the end of the year, the firm faces no insurmountable obstacle in adapting resources to goals. This is not the case in the public sector, where resources have been fixed in a general budgetary process. As a result, there is an inevitable conspiracy between political leadership and the CEO of the Ministry wanting to do too much with the given resources. When carried to an extreme, the system will buckle under the pressure— by making mistakes. The system needs an independent voice and advocate to defend it against excess tasking. This advocate is expected to be unassailably neutral between activities.

The diplomatic inspectorate (DI), in my view, is best placed to take on this role, for in its roaming surveys it is able to obtain a good, unbiased, and unvarnished view of the actual working of the system. Unfortunately, the DI is currently used mostly in a 'control' mode, to verify individual compliance, or to spot the occasional malfeasance, the breaking of PC rules in human relations, rather than as an instrument to verify the well-functioning of the system.

Next to the traditional inspection role then, I would envisage for the DI a planning role as well along the lines indicated above, aimed at ensuring the integrity of the system. In its new capacity, the DI would aggregate and evaluate the 'time management' information for the development of 'pro-forma budgets' and 'benchmarks'. The Head of the DI would furthermore be part of the top management structure. In his new role,

he would report on actual time allocation, establish forecasts of 'blow-outs', identify compensation needs and advice on all matters concerning the integrity of the system.

Proposals for new policies that are submitted to the management structure should include concrete proposals for 'task offsets'. The DI would assess such proposed compensation prior to the launch of a major new activity. The DI would be able to block, or at least delay implementation, should the offset measures appear inadequate. In this way, the DI would become the 'ombudsman' for the system. Finally, the DI would take the lead in making proposals for the simplification of procedures, or set corresponding simplification targets.

Is this not the task of Administration? In order to be effective, an advocate for the system must be unassailably neutral towards all claimants on the resources of the Ministry. Administration has itself become one of the major sources of tasks—it is thus not in a position to speak credibly about simplification. Nor is the integrity of the system a task for the trade unions, which report to the membership and not the political structure.

My proposal aims to force the discussion about scuttling tasks that are no longer a priority, out into the open and to make it one of the core management tasks. The proposed rules and structures would make an explicit addressing the issue compulsory. This is the equivalent of determining in a neutral way the 'bankruptcy' of tasks that are no longer deemed useful. The DI would facilitate the process and be its guarantor. The DI, therefore, should have sufficient powers to force management into compliance.

CONCLUDING REMARKS

If these suggestions sound terribly outlandish and far-fetched—they are not. Let us be quite clear on one point. The system does it anyway—often in a muddled or downright devious matter. Anyone who has viewed *Yes, Minister*, on television knows about the ways in which the civil service outwits unpleasant or unreasonable demands. What I propose is to make an existing process accountable. As the saying goes—what has to be done is worth doing well.

Some of my proposals—like time accounting and budgeting—have long been implemented in the private sector. Others—such as the *obligation* to compensate and a *right* to refuse uncompensated new tasks—arise

from the specific character of the public service. The inflexibility of the budget constraint should be matched by an equally inflexible system for preserving the system from overload.

The direct effects of the proposals have been highlighted. A word now about the collateral impact: in my view, my proposals would do wonders for motivation—for the individual and the units, they amount to empowerment. When the responsibility for the proper working of the system is widely shared, I would expect it to work more smoothly, and more effectively.

My proposal has an added advantage. It can be implemented incrementally—in a 'trial-and-error' fashion, adapting it to the culture of each ministry. One may wish to begin small—a unit or even an individual is used to test the concept, to enucleate difficulties, and test its limits. Success will make us confident that we can enlarge the scope of the reform to larger units. Failure spells a rapid and painless demise. Experimental success will facilitate adoption throughout the system, for the benefits will be there for all concerned to see. In other words, this approach would be quite different from a top-down approach which yields discontinuities in the running of the Ministry and has an implicit risk of catastrophic failure.

I am aware that my proposal flies in the face of current fashion for military–industrial structures in public service. Such proposals start from the point of view that a coherent set of objectives can be established at the top and that these objectives will percolate down the system for effective implementation—provided the 'principal-agent' problem can be resolved by appropriate incentives. The main justification for such proposals lies in their analogy to the private sector.

My contention is that such proposals are doomed to failure. They are but 'cargo cult'. They ignore the fact that the public and the private sector are inherently different. I have made my case here by pointing out that the public sector has no bankruptcy system for eliminating inferior policies. I have made proposals to remedy this situation.

Two other core problems remain—the problem of developing a coherent set of objectives as well as that of timely and precise feedback—reality checks, if you wish. I intend to take up these issues in another framework.