

# The Productivity Conundrum

## A conversation with Murray Sherwin

Productivity Commission Chair Murray Sherwin deals in big, meaty issues. Like why, despite appearing to have the right infrastructure in place, does New Zealand continue to drift down the OECD standard of living rankings, and how do we improve public sector productivity given its significant contribution to the country's economic well-being? He talks with *Public Sector* writer ROSE NORTHCOTT about the productivity conundrum.

### How do we measure NZ's public sector productivity?

It's a real challenge, in terms of methodology. We are putting a lot of effort into this along with our colleagues at Statistics New Zealand, trying to get a handle on what's going on in terms of trend movements and productivity in the public sector. We have some analytical work underway and hopefully will have material rolling out from the latter part of this year into next year.

### Why is it important?

The public sector, excluding benefits and straight transfers, accounts for something approaching 20 percent of GDP. Because it is so large, and its influence is so broad, it is critical that the public sector perform well and absorb the least resources necessary to do the best job.

### What has to change to improve public sector productivity?

There are two elements. One is how the public sector itself goes about doing its own work – how it picks up new technology, how it amends its processes to make use of available capacity of new technology, finds better ways of interacting with the public and delivering outcomes.

At least as important is the impact public sector decision-making has on the private sector. We did a major piece of work last year on regulatory institutions and systems and how well those regulatory regimes work. That has an enormous impact on the economy and private sector productivity.

### What can be done now to improve public sector productivity?

Most of our reports have a public sector element to them. Themes that come up repeatedly are skills and training, ensuring people are properly skilled for the role they have.

There are also cultural themes – the culture of an organisation, the leadership and engagement processes within agencies all matter to performance. The key thing is ensuring people are clear about what they are doing, why and how.

The quality of policy advice also matters enormously. The notion of free and frank advice has been under pressure in a number of places and it's important we don't take our eye off that ball.

We don't actually measure the effectiveness of a lot of what we do in the public sector. We therefore don't learn as much as we should about what works



and what doesn't and so we don't run the continual feedback loops necessary if we are to learn from our experience.

### Is there a need for structural change to improve public sector productivity?

I always shudder when I hear references to structural change. We seem to leap to structural changes too quickly and pay too little attention to cultural changes and the evolution process that most agencies need to go through to improve.

We face continual tensions around empowering rapid and decisive decision-making and action, versus more consolidation or collaborative actions. It's always a trade-off and there's not likely to be any grand solution out there. Cultural and capacity issues are really important. We need to be thoughtful and deliberate in understanding how complex systems interact and what part is shaped by architecture and what part by culture and behaviours.

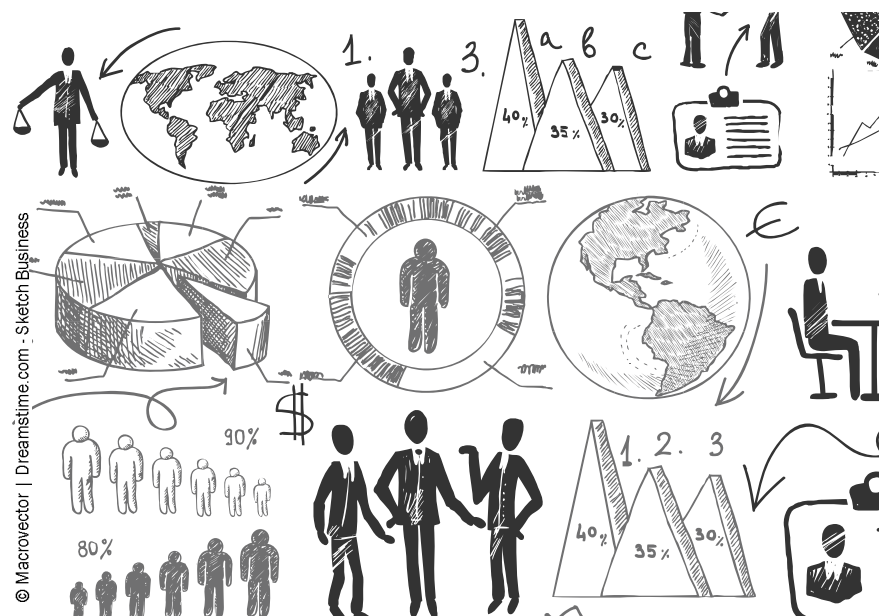
### Is intolerance of failure stifling public sector innovation?

Yes. You see a good deal of discussion of this in our draft social services report. A low tolerance for risk translates into highly prescriptive top-down directives. You see it in contracts with the social sector for NGOs. They are very prescriptive about what they must do and how they should do things. The outcome of that is to remove a lot of the capacity for decision-making at the front line close to the people in need. There is pressure on the people in the system to be compliant rather than respond to the needs they are trying to service.

Inevitably, politicians are highly averse to having a microphone stuck under their nose and being expected to be knowledgeable in detail about specific instances. It's time to push some of that further away from politicians. It is not at all helpful to society in the long term to drive that degree of risk aversion into the system from the top.

### Is New Zealand moving back up the OECD standard of living ladder?

The fact remains that over the last 40 to 50 years we've dropped well off the curve



from where we were. Climbing back up the international rankings is not straightforward. But it matters, because our productivity performance determines our living standards and the quality of choices that we have available to us, both individually and collectively.

We are in the process of working out a meta story or narrative in which we lay out our understanding of this whole period of relative decline and what policies and strategies will best assist us to regain lost ground. Why do we struggle to match productivity gains we've seen in the rest of the world? Why, in particular, do we struggle with that challenge when many of the basic bits of infrastructure for a high performance, high productivity society appear to be there?

By the usual indicators, our public sector is pretty damn good – it's free of corruption by and large, well led and highly competent. We have a regulatory system which, while we can always find things to improve, is good by international standards. We have good governance structures and transparency. All of that should contribute to higher performance economically. We've got all the basic infrastructure pieces in place. Identifying what's missing is the conundrum that economists have been wrestling with for years.

My own presumption is that distance matters, as does size – to a degree. But we've always been where we are geographically and have been a small economy, so something else has changed. The research we are doing points to a lack of connection with international value chains. Countries performing well are closer to international value chains. They draw inputs from other countries and add value to those. We have tended to be at the end of the value chain and less engaged in high frequency transactions, adding value at different stages of the value chain.

There is also an issue characterised as

**“We did a major piece of work last year on regulatory institutions and systems and how well those regulatory regimes work. That has an enormous impact on the economy and private sector productivity.”**

knowledge-based capital: to what extent we are making investments in high knowledge fields building intellectual property and innovation. We are off that curve.

### What qualified you for this job?

My career started at the Reserve Bank where I was working in public policy and economics. I did stints at the OECD and the World Bank on secondment from the Reserve Bank. I think New Zealanders need to spend time working offshore to get some perspective on life in New Zealand. Both my offshore jobs provided me with a lot of learnings and networks.

I was then part of the Muldoon advisory group in the early 80s, a particularly interesting time, and left that in time to return to the Reserve Bank and work through the 1984 foreign exchange crisis. That interesting juxtaposition of roles has given me broad experience. Nine years as MAF CEO gave me exposure to a broad raft of issues from biosecurity to trade policy. That was the apprenticeship, if you like.

### How's your job satisfaction?

This is really interesting work with the satisfaction of starting an organisation from scratch – building it from nothing over four years and working with a really great group of people. We are given big, meaty mandates to work on and our work is being taken seriously. I couldn't ask for more than that.

### Being a Productivity Commissioner is a part-time role; what else do you do?

I chair a body called the Innovation Partnership, a group of individuals from the public and private sector, including Google, Chorus, InternetNZ and MBIE, who have a shared interest in driving greater innovation through the internet and associated

technologies.

I also chair a Strategic Risk and Resilience Panel made up of individuals from government and the private sector pulled together by Andrew Kibblewhite (Department of Prime Minister and Cabinet Chief Executive). We're tasked with advising the government about big picture risks that Cabinet or the prime minister might be worried about, assessing how well we are dealing with those risks, how New Zealand could build resilience and response capability, and where the priorities should sit. We look at everything from natural hazards to cybercrime to financial risk to wider socio-economic risks, plague and pestilence.

### Is the Productivity Commission making a difference?

I think so. We're finding strong interest in our work. Ministers and officials are taking our work seriously and we've had strong commitments from the government to implement our recommendations. In many respects, the extent and quality of the conversations we are having with ordinary New Zealanders about productivity-related issues is just as important.

But an awkward issue for us is turning that positive response into harder, quantitative measures of performance. That is always going to be a challenge, as our longer-established counterparts in Australia will attest. So that is a work in progress for us. Ultimately it's the business community, workers and ordinary New Zealanders who need to find our work useful to them. We work hard to communicate and engage with the public and are trying to make our work very relevant to New Zealanders. It's about working smarter and lifting living standards and well-being. ■

