Big ambitions for small businesses
Amarendra Sinha on India’s manufacturing plan

Rising from the ashes
How Detroit fought back from bankruptcy

Government to the people
Australia’s digital revolution
Welcome back to Citizen Today, EY’s magazine for government and the public sector.

The prolonged aftermath of the global financial crisis, combined with the effects of demographic change and technological advance, has changed how governments deliver services. There is a renewed focus on value for money. How can public spending deliver the maximum possible benefit? And there is a new imperative to be more responsive to the needs and preferences of service users. How can governments provide services to citizens who are more connected than ever before and who expect convenience? As Kathryn Campbell, Secretary of Australia’s Department of Human Services, puts it: “People have very busy lives. They don’t want to be spending time queuing, they want to be spending time with their family and friends.”

The interview with Ms Campbell (see page 18) is one of the features in the latest edition of Citizen Today that deal with this new reality for government. She explains how the use of digital platforms is helping her department to become more responsive to citizens and free up capacity to meet ever growing service demands.

As governments decide how to allocate scarce resources, departments are under increasing pressure from treasury departments and citizens to spend taxpayers’ money prudently and, in return, create the most value possible. Our feature on defense (page 10) explores how better management of procurement, talent, technology and budgets can help build capabilities without large spending increases. While on page 22, we examine how schools in the UK can achieve better results not through higher spending but by creating an organizational structure that improves governance and drives economies of scale. Continuing the education theme, we find out why tuition fees are off the higher education agenda in the Czech Republic (page 25).

Elsewhere in this issue, we discover why the US must get better at administering public-private partnerships if it is to make much-needed infrastructure improvements (page 16). Staying in the US, we report on the city of Detroit and its emergence from bankruptcy (page 12). We show how the city was stabilized and set out the lessons that other municipal authorities, in the US and further afield, can draw. Indeed, many municipalities in Germany are in a precarious financial situation. On page 31, Hans-Peter Busson, EY’s Government & Public Sector leader in Germany, explores the extent of the problem and sets out what can be done to balance the books.

And finally, our cover story interview (page 6) is with Amarendra Sinha, Special Secretary and Development Commissioner at India’s Ministry of Micro, Small and Medium Enterprises. He tells us why the Government is putting small businesses at the forefront of its drive to make India a manufacturing powerhouse.

I hope you enjoy this issue and gain insight from our interviews and analysis. If you have feedback or ideas for future features, then please get in touch. I’d like to hear from you.
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March of the Makers
Small businesses already play a pivotal role in India’s economy. But if the country is to fulfill its ambition of becoming a global manufacturing hub, the sector must grow rapidly. Amarendra Sinha, Special Secretary and Development Commissioner at India’s Ministry of Micro, Small and Medium Enterprises, tells EY’s Amar Shankar how the sector can lead the manufacturing charge.

In our closely interconnected global economy, the activities of small businesses can sometimes be overshadowed by those of larger companies that operate across borders, time zones and cultures. But while their reach and scale may be less, small business owners chase the same goals of growth and profit.

Few can doubt the importance of India’s 40 million small business owners. The micro, small and medium enterprises (MSME) sector contributes nearly 8% of the country’s GDP, 45% of its manufacturing and 40% of its exports. It provides the largest share of employment after agriculture. These are impressive numbers. But they need to grow further. Amarendra Sinha, the Special Secretary and Development Commissioner at India’s Ministry of Micro, Small and Medium Enterprises, sets out the challenge: “The vision of Prime Minister Narendra Modi is to promote India as a global manufacturing hub,” he says. “The growth of our manufacturing sector is unimaginable without the evolution of the MSME sector.”

Growing pains and gains

Over the past two decades, India has enjoyed economic expansion, more investment and growing influence around the world. The country’s rapid economic rise was driven by its domestic market, an emerging middle class, cost competitiveness and a huge labor pool. So, when the global financial crisis hit, India was able to withstand the turbulence that left other economies deeply scarred. However, India’s economy has recently suffered something of a slowdown. Foreign investment has fallen and the rate of economic growth has slowed. This weakening has shown the importance of introducing reforms to improve infrastructure, governance and transparency – and tackle other challenges that are common to many developing countries.

The election of a new government in 2014 brought momentum to the reform agenda. The new prime minister, Narendra Modi, has a mandate to develop market-friendly policies, speed up decision-making and improve public administration.

One of Prime Minister Modi’s key priorities is the recently-launched “Make in India” campaign, which encourages businesses from around the world to invest and manufacture in India. “The objective of the program is to achieve a sustainable level of 10% manufacturing growth over the long run,” explains Sinha. “The Make in India campaign is focused on creating jobs and enhancing skills in 25 sectors, including automobiles, automobile components, defense manufacturing, aviation, electronics and leather.”

“The challenge is to encourage global companies to manufacture their goods in India”

So, what issues does the campaign seek to address? “First, the share of manufacturing in India’s GDP is around 16%, compared with more than 30%, and growing, in some other Asian countries,” says Sinha. “Second, MSMEs in India perform poorly when it comes to competitiveness, quality, innovation and growth. This is due to challenges in accessing finance, technology, skilled workers and markets. SMEs can be revitalized by providing competitive finance, relevant world class technology, the sustained supply of skilled workers and access to markets. There is a strong business case to enhance both supply side and demand side interventions to MSMEs to improve their competitiveness.”

What is the office of the Development Commissioner doing to support small business owners and promote growth in the sector? “Besides policy formulation for the development of MSMEs, we also help business owners to access finance, technology, skilled human resources and markets,” says Sinha. He outlines the Government’s two main policies for increasing competitiveness in the sector, both of which were established by the previous government. First is the Skill Development Policy, which aims to result in India having 500 million skilled people by 2022. Second is the National Manufacturing Policy, which has the objectives of increasing the share of manufacturing in India’s GDP from 16% to 25% within a decade and creating 100 million additional jobs.

“Against this backdrop, and after much deliberation and exchange of ideas, we developed the Technology Centre Systems Program (TCSP) to bring about...
transformation. This program seeks to improve the technological and skill base of MSMEs in selected manufacturing industries,” says Sinha. The program is inspired by leading practices from both the Western and Eastern hemispheres, which are then carefully tweaked so they work in the Indian context.

Sinha says that he has been studying similar interventions across the world, and exploring how public and private sector can work together to realize the potential of small businesses. He notes the results achieved by Germany’s innovation drive, and cites the example of Belgium’s IMEC (previously the Interuniversity Microelectronics Centre), which exposes MSMEs to new technologies.

The Office of Development Commissioner is responsible for running 18 MSME technology centers. These not-for-profit societies help local MSMEs in certain sectors. Over the years, these centers have taught skills to a range of people – from school dropouts to engineering students – and supported local MSMEs with prototyping and tooling. They provide production support and business advisory services. Success stories of these technology centers have given confidence to launch the next wave of institutional intervention. The Kannauj Technology Centre has helped India become the world’s biggest exporter of menthol, and the Bhubaneswar Technology Centre has played a significant role in India’s space program.

The TCSP sets out plans to upgrade existing centers – most of which were established between 1969 and 1992 – and create new centers that cater to industries that have growth potential.

So how does Sinha see the future of technology centers? “Currently, they have a three-pronged agenda: skilling, production support and consultancy. We will add another dimension: business incubation services that allow tomorrow’s entrepreneurs to turn their ideas and aspirations into enterprises.”

“These technology centers will be the catalysts that fire innovation and improve competitiveness among the MSMEs they serve. The ultimate objective is to establish a system of technology centers that harnesses large manufacturing units, applied research institutes, R&D organizations, educational institutions and skill development providers.”

All to play for

The stakes are high. The growing power of India’s domestic market has attracted international attention. But the challenge now is to encourage global companies to manufacture their goods in India. MSME technology centers have a big role to play. “Four decades ago, only one car ruled the roads in India, and that was Hindustan Motors’ ‘Ambassador’,” says Sinha. “Today, all the world’s leading auto manufacturers have positioned their products here. Considering that many organizations are evaluating the call to Make in India, it is important that we establish a national ecosystem to help MSMEs improve their competitiveness and enable them to serve such global value chains.”

The TCSP envisions technical consultants developing roadmaps to align MSMEs in the global value chain of large manufacturers. These roadmaps will be in cutting edge areas, such as 3D printing, rapid prototyping, lean manufacturing and mechatronics. Sinha explains: “This is a planned approach for future requirements rather than a reactive approach to play catch-up.”

In publicly funded programs, supply side interventions are usually the order of the day because they are easier to measure and manage. In the case of MSMEs, the demand side has received less support. For example, a small entrepreneur may be hesitant to engage with a large
original equipment manufacturer and vice versa. Hence there is a role for a facilitator.

“In this program,” says Sinha, “we call this facilitator a cluster network manager, who will work to provide demand side interventions, and support and market the services of MSMEs. The manager will help turn ideas into reality by linking academic and applied research institutions to entrepreneurs.

Platform for growth

These policies are integrated under a national IT platform. It will help MSMEs to build their market through a B2B platform, recruit through an online job portal, and offer guidance on publicly funded schemes and services. “The TCSP’s monitoring, evaluation and grievance redressal mechanism will also be built into the IT platform. In effect, this national portal will establish virtual clusters that enable MSMEs to extend their footprint by responding to opportunities beyond their geographic remit.” These online ecosystems will act as catalysts to speed up innovation and collaboration. Sinha is excited about the possibilities: “The sky is the limit,” he says.

Sinha believes that the TCSP can be replicated in other countries. “This program is focused on enhancing the competitiveness of MSMEs through easy access to world class technology, skills and market linkages. Most countries that are struggling to provide such support can adopt this approach,” he says. There has already been interest from other countries. Given that the program is partially funded by the World Bank, it can be replicated in other parts of the world by the Bank or Government of India through its bilateral initiatives.

But for now, Sinha is firmly focused on India. The stage is set, with India expecting reform to translate into growth. The country’s small business owners are set to play a major part.

“The Make in India campaign is focused on creating jobs and enhancing skills.”

Amarendra Sinha is Special Secretary and Development Commissioner at India’s Ministry of Micro, Small and Medium Enterprises

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Amar Shankar is an EY Advisory Services leader in India
NATO challenges its members to spend two percent of their national wealth on defense. With this target in mind, and with public finances in many governments around the world coming under increasing pressure, policymakers and citizens are seeking reassurance that the money allocated to armed forces is spent wisely. So, what can be done to ensure that spending has the biggest possible impact?

Better budget management

Budget holders in defense ministries need clear accountability. This will enable them to view the end-to-end picture of how money is being spent, what it contributes to capability and how it affects operations. When you are directly accountable for the money that you’re spending, you are more likely to look after it well. So, promoting accountability is a good way of taking waste out of the system.

The people making these decisions also need financial skills. Historically, defense ministries are well stocked with cost accountants, but lack management accounting skills. Developing the capability to analyze and assess how well money is used, rather than just how much is spent, is a priority.

The greater emphasis on financial management means that the defense environment is becoming more like a business. As well as exposing their people to commercial...
training, defense ministries may have to start looking at joint recruitment and talent development with commercial organizations, and bringing in people at senior levels who have got commercial management experience.

Defense ministries are competing with health and education services for scarce resources. Finance ministers are more likely to reward departments that not only spend wisely, but are seen to spend wisely. So transparency and communication are important considerations.

**Quicker, smarter procurement**

The nature of the threat facing governments and their armed forces is changing fast. As a result, there are new demands on military innovation. The US has signaled this change with the Third Offset Strategy, a new long-range research and development program that aims to shorten timescales and help defense procurement become faster and more agile.

For example, information-based systems and the exploitation of big data – which are now at the heart of defense capabilities – will be out of date before they are deployed if the procurement process takes too long. And with threats and technology changing fast, the deadlines for deployment are getting shorter.

A whole range of smaller businesses and specialized industries are developing the high-end technology that defense ministries need to harness. The challenge is to reach down through the supply chain to get access to the high-end innovation that is taking place in these smaller networks – and to encourage new entrants, with new ideas, to the market. This innovation can drive faster, more responsive procurement.

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**The war for talent**

As the defense environment expands, the demand for specialist skills grows ever wider. And in some countries, those pockets of skills are getting smaller. If a country has only got a small pool of trained engineers or technologists from which to draw, attracting and retaining them is difficult – especially given the rewards that can be on offer in the private sector. And in today’s globalized job market, skilled people can, and do, move across borders.

As economies strengthen, competition for the high-end specialist skills required in defense is going to increase. So the offer must be attractive. Defense ministries may not be able to compete with the private sector on pay, so they have to emphasize the other benefits, such as the experiences you gain, the sense of purpose and the skills you learn that will serve you for life.

However, we are reaching the point where defense ministries can no longer hold all capabilities and skills in-house. They should think more about what kind of skills they must retain, and what they should contract in, or co-develop.

For example, if you want to have high-end nuclear engineering skills, do you need all of those skills within government or within domestic industry, or can you manage it as a pool across the two? Can government and industry co-source and co-develop? This, of course, requires a very high level of trust, but it can address the challenge of how defense ministries train and retain talent.

The defense terrain in changing fast. Pressure on budgets, procurement and talent is intensifying. But, by taking an innovative and rigorous approach, these threats can be engaged and overcome.

"With threats and technology changing fast, the deadlines for deployment are getting shorter"
On the morning of 11 June 1805, a fire started in a Detroit bakery. The blaze spread quickly, destroying wooden buildings. Despite the best efforts of citizens who tackled the fire, most of the city burned down.

The Great Fire of 1805 is commemorated on the city’s flag, which carries the motto, in Latin: “It will rise from the ashes.” And rise it did. Grand boulevards were built, the city’s population expanded, its men fought bravely on the fields of Gettysburg, and it thrived in the 20th century, powered by industrialization, armament and, of course, the automotive industry.

But, 200 years after the Great Fire, the city faced another crisis. As manufacturing industries declined and the population fell, Detroit became a byword for urban decline. High rates of unemployment and crime, coupled with blighted neighborhoods and a widespread failure to collect taxes, put intolerable pressure on the city’s finances. On 18 July 2013, Detroit became the largest city in the US to file for bankruptcy. Five months later, it was declared bankrupt, with liabilities of US$18.5b.

Detroit rose from the ashes once more, emerging from bankruptcy in December 2014. Its liabilities have been restructured and the city is now on course for a second revival. So, could this happen in other cities, and what can be learned from the experience of Detroit?

Heightened risk

Detroit’s story reflects a broader situation of financial distress across many other cities and municipal entities, including school systems and utilities. More cities are finding it difficult to raise revenue, while their operating and legacy expenditures continue to escalate.

Other cities face insolvency as they grapple with difficult underlying economic conditions, high levels of debt, and large, underfunded liabilities, such as pensions and retiree healthcare. So, it seems a good time for municipal policymakers to rethink the possibility and implications of a comprehensive restructuring process.

Downward spiral

Most cities that plunge into financial crisis follow a similar path. A combination of broad demographic and economic trends, such as an ageing and declining population or...
rise in local unemployment, means that revenues tend to decline. The city still needs to provide core services to citizens. With more people getting old or losing their job, demand for these services grows. So the city finds it hard to control costs.

The city must also continue to serve its long-term obligations. There are fewer funds available to pay down debts, such as pension and health care benefits. In the effort to keep a minimum level of services running and pensions paid, the city is forced to spend less on maintaining its infrastructure, including public safety fleet and equipment, recreation facilities, transportation and public lighting. It becomes a less attractive place in which to live, and people with sufficient financial means tend to move to the suburbs in search of a better quality of life, taking their tax dollars with them.

The city then starts running annual budget deficits. Policymakers tackle the deficit by cutting labor costs, issuing short-term debt, reducing contributions to liabilities and privatizing assets. If the structural imbalances in the budget persist, even after applying these short-term solutions, then crisis takes hold. The city's access to credit markets becomes limited. Its cash position deteriorates. How much longer can it pay its workers? Policymakers come to realize that financial firefighting is putting off the inevitable need for restructuring.

So, what happens to a city that files for bankruptcy? EY assisted in devising and implementing Detroit's restructuring plan under the leadership of the City Mayor, CFO and Emergency Manager. Of course, each municipality will have its own set of circumstances and priorities. But our work with Detroit has enabled us to draw together the features of a successful approach to restructuring.

Control costs and revenue now and in the future

The first feature is controlling costs and revenue. As part of the restructuring plan, cities can look for efficiencies in their operating budgets, consider whether they should continue to provide non-core services, and explore partnerships with public and private sector entities.
When it comes to cutting costs, cities may be tempted to take a top-down approach, and decide to cut, say, 10% across the board. However, this is unlikely to produce the anticipated benefits. Cities must deliver public safety services, such as police and fire, and these services take up big chunks of their budgets. Blunt tools, such as a uniform cut, don't take into account the large number of exceptions that would have to be made in an effort to keep services going. So, despite the urgency associated with reducing costs, it is critical to undertake a department-by-department analysis.

Just as controlling costs is vital, so is protecting revenue. Although the composition of a city's revenue stream is generally consistent year after year, it is critical to monitor the underlying trends that will affect future revenue estimates.

In the effort to balance the budget, cities often rely on one-time revenues, such as asset sales or proceeds from issuing long-term debt. This can mask a systemic imbalance in annual budgets in the short term. Some cities suffer from the failure to replace eroding revenue sources. As a result, they need to review sources regularly and adapt their budgeting accordingly. Identifying new grant funding opportunities is an important ingredient, and maintaining sufficient budget reporting is critical to ensuring that this source of funds continues, particularly in the early days of restructuring.

The importance of financial controls cannot be overstated. It is good practice to have a long-term perspective on city finances, beyond periodic audits. This requires capital investment in systems, updated budgeting and audit processes, and regular strategic financial reviews.

Get a grip on liabilities

Focusing on costs and revenue may not be enough. Restructuring long-term liabilities may also be necessary to make a city's finances sustainable.

It can be a challenge to restructure pension liabilities, given contractual and state law protections. City officials should understand the state law provisions that may affect their ability to restructure these liabilities. It is also important to invest in actuarial analyses, financial forecasts and scenario planning.

Administrators can conduct a thorough review of existing medical plans and benefits for active employees and retirees, and benchmark them against other cities. In addition, municipalities need to be aware of the federal subsidies that are available to retirees for medical coverage, and take these benefits into account when developing a proposal. Armed with this analysis, officials can seek to cap the municipality's commitment to funding these obligations in the future.

Debt instruments need to be analyzed individually in order to assess the strength of the pledge or security. Certain general obligation bonds have a dedicated tax revenue stream to service them, while others are limited general obligation instruments. A city's ability to restructure debt obligations is likely to be dependent on the type of instrument and the structure of the security or pledge on dedicated revenue streams.

Negotiate smartly with creditors

City employees and retirees are key stakeholders in negotiations. They work, or have worked, for the good of the city, and reductions in their benefits are likely to
be sensitive and controversial. Against this backdrop, city officials need to negotiate with representatives of all creditors. Negotiations can take the form of informal meetings or formal processes such as collective bargaining, mediation and arbitration. The preparation of a clear blueprint of the restructuring plan, with proposals for all creditors, including unions, pension systems and debt holders, is critical to a productive negotiation process.

Comprehensive restructuring creates much-needed breathing space for the city to negotiate with each creditor group. The city of Detroit negotiated with financial creditors, bond insurers, swap counterparties, union leaders and retiree groups in informal talks and court-supervised discussions.

"On 18 July 2013, Detroit became the largest city in the US to file for bankruptcy"

These negotiations ultimately resulted in the city reducing about 70% of its unsecured obligations. It offered unsecured creditors (certain financial creditors, retirees and trade creditors) an estimated recovery of approximately US$2.9b on US$11.5b of long-term obligations, which included US$5.7b in retiree health benefits and US$3.5b in underfunded pension liabilities. Access to bankruptcy proceedings provided the city with greater capacity to prioritize its obligations, allowing significant, and unprecedented, negotiation with claim holders.

Through the negotiation process, Detroit de-risked its pension plans by negotiating a reduction in the pension plan liabilities for both the General Retirement System and the Police and Fire Retirement System, and reducing the assumed rates of return. Under the pension settlement, general retirees saw their pensions cut by 4.5% and the elimination of future cost of living adjustments. Uniformed retirees did not see any reductions to their pension checks, but gave up a portion of the future increases to their benefits. With benefit levels to retirees already low, city leaders were careful to minimize cuts to pension benefits.

The city also reduced its retiree medical liabilities by establishing two voluntary employee beneficiary associations to administer retiree health care benefits. In this way, the city was able to cap its exposure to this liability and reduce its outstanding obligation by approximately $5b.

In the case of benefits to active employees, Detroit participated in mediation sessions with its various police, fire and general employee unions to establish terms for new collective bargaining agreements. This process had to balance the goal of sustainable cash flows for the city against appropriate incentives for retaining and hiring employees. These negotiations took place in good faith, with employees continuing their daily duties, despite the threat of reduced benefits.

With respect to financial creditors, the city negotiated discounts to bondholders' claims, based on a variety of factors including their terms and level of security, with financial unsecured creditor recoveries ranging from 13 cents to 74 cents on the dollar.

**Invest today for a better tomorrow**

No city can look forward to sustainable growth without investing in its economy. This is necessary to strengthen communities, ensure public safety and improve citizen's quality of life - and to attract new investment and jobs.

So, a broad economic development plan is required. Once budget savings have been made, the challenge for administrators is to reinvest these savings smartly. This includes making clear, long-term plans for investment in core municipal services such as public safety, improving neighborhoods, updating infrastructure and providing incentives for businesses to move into the city.

Another priority is securing sustainable financing for capital expansion. Distressed municipalities, faced with less favorable debt markets, need to engage private investment for capital projects. Some examples include public-private partnerships, privatization of assets or utilities, and the exploration of other financing channels, such as a state infrastructure bank. The city may consider offering tax breaks or other concessions to attract private investment. Administrators can also look at winding down old infrastructure. They may consider commissioning an external review of assets and investment needs. A clear return on investment should be the main criterion when deciding the capital projects in which to invest.

**Facing the future**

Back in 1805, when their city was blazing, the people of Detroit formed a human chain from the river to the fire. They passed buckets of river water up the chain in a vain attempt to control and extinguish the fire. In the 21st century, when the city faced financial ruin, the tools at its disposal were more sophisticated.

Financial discipline, reducing liabilities, effective negotiation and planning for economic development enabled it to turn financial distress into a platform for growth. Detroit can once again face the future with confidence.

Gaurav Malhotra is Senior Managing Director at Ernst & Young Capital Advisors LLC
The US will require over US$1t of infrastructure investments over the next decade, with the current allocation of public funding unlikely to be able to meet this investment demand. This was the message from Secretary of Transportation Anthony Foxx at the Select USA Summit held in Washington DC on 23-24 March. Secretary Foxx stated that in order to address this significant investment need, the US public sector had to look seriously at new ways to engage with the private sector to deliver infrastructure.

Last year, EY published a report, entitled *Infrastructure 2014: Shaping the Competitive City*, that surveyed key cities in the US and other countries. One of its conclusions was that in order to create a competitive city, high quality infrastructure must be built.

At the Select USA Summit, Secretary Foxx chaired a discussion on infrastructure and the role of the private sector. I was on the panel, along with others including Colorado Governor John Hickenlooper, Cintra’s Nicolas Rubio and Christopher Leslie from Macquarie. The discussion showed that the private sector has a vital role to play in infrastructure development in the US.

This is not to say that public-private partnerships (P3s) and the role of the private sector is a completely new concept. A significant number of states already have enabling P3 legislation and have pushed forward with projects that have been funded through a combination of the Transportation Infrastructure Finance and Innovation Act (TIFIA) program, public funding and private investment.

Not all of these projects have been successful. But Colorado is a prime example of a state that has actively engaged with the private sector to deliver a number of successful P3 projects in the transport sector. Key reasons for success have been strong public sector leadership and a fully transparent process. The citizens of Colorado have been engaged in the process and fully understand the benefits they receive from private sector participation in the delivery of infrastructure.

With its continued economic strength dependent on renewed infrastructure, it’s time for the US to get better at public-private partnerships, finds Bill Banks.
Support goes beyond TIFIA. In 2014, US President Barack Obama announced the Build America Transportation Investment Center (BATIC) initiative. The center is intended to act as a one-stop shop for governments, developers and investors as they establish infrastructure projects across the US.

Engaging with the local community and contractors will help citizens to understand that the private sector is providing a long-term and sustainable partnership to deliver infrastructure. It is vital that the private sector shows the key benefits of its participation in P3 projects.

Project pipeline
In order to remain an attractive investment market for global infrastructure players, it is essential that the US can provide a fully transparent pipeline of infrastructure projects. The infrastructure market is global, and the US competes with the likes of Asia, Africa and the Middle East for infrastructure providers and investors.

A publicly available infrastructure projects pipeline will give the private sector the confidence to make the necessary investment decisions. Private sector players can position themselves to participate in these projects, form strategic relationships with local contractors and take a long-term view on market opportunities. Without a publicly available pipeline, some investors could turn their attention to other markets that can provide certainty.

Political champions
P3 is not a silver bullet for the infrastructure challenge. It will not make a bad project good. It is one option available to the public sector to deliver infrastructure projects. Not all projects will be suitable for private sector involvement and each should be considered carefully.

Historically, most P3 deals have been in the highways sector. However, other areas like airports are also ripe for private investment. For example, a procurement process began this year for Denver airport.

We now need to see more political champions who believe in the value that P3s can deliver. They need to explain the wider economic benefits that a properly constructed P3 project can deliver for citizens. It is also incumbent upon the private sector to demonstrate clearly that its investment in infrastructure can bring better outcomes for citizens than projects funded solely from the public purse.

The future
Clearly, the private sector does have a significant role to play in the delivery of infrastructure in the US. However, in order to do so, the private sector must be able to demonstrate to citizens the added value that it can bring. And the public sector needs to champion P3 and deliver a pipeline of projects so that private providers can plan with some certainty for the necessary investments.

Infrastructure development in the 19th century helped to lay the foundations for America’s economic success in the 20th century. If the world’s largest economy is to thrive well into the 21st century, it must rise to the infrastructure challenge once more.
Australia’s Department of Human Services is responsible for the development of the Government’s service delivery policy and provides the country’s people with access to social, health and other payments and services. The department is led by Kathryn Campbell, who took over as Secretary in 2011. Here, she talks to EY’s Lucille Halloran about how digital technology is improving the way citizens can access services.
Lucille Halloran (LH): How has the department changed since you joined?

Kathryn Campbell (KC): Back in 2011, we were preparing to combine the Department of Human Services with Medicare Australia, Commonwealth Rehabilitation Services and Centrelink. The objective was to build a mammoth 40,000-person department that delivers services to nearly every Australian.

These organizations had rich histories and were somewhat worried about coming together. My job was to lead these changes. Bringing the organizations together was like blending a family.

Of course, we streamlined our back-of-house services to find efficiencies and savings. But I had a particular focus on digital. Australian citizens had come to expect digital services from other providers, so why weren’t they getting them from government?

LH: How did the department become a leader in digital government?

KC: One of the things I realized was that we were running a public service ICT system for a retail operation. So, when the then CIO retired, I took the opportunity to hire a retail CIO. I wanted us to be like eBay.

We also needed a cultural change. We had to think differently about how we operated, and change the thinking of all staff, not just the ICT people and the executive. We had to turn our people into digital advocates.

There was a fear, particularly among our junior staff, that if they got customers to go online, their jobs would disappear. At the same time, we were downsizing from 40,000 to 35,000 staff. But we made it very clear that we were going to do it in a structured, orderly fashion. Those people who wanted to retire, or who weren’t comfortable with the new organization, left. But there were no involuntary redundancies. Staff started to realize that if they wanted to stay, there was work, even if it was different to what they were doing.

As we reduced staff numbers in some locations, our people realized that they had to get customers online, because that would free face-to-face resources for those citizens who needed them most. Very quickly, our staff became great advocates of this approach. If you go to one of our offices now, our staff will try to convert you to digital because they know that there could be someone waiting in the queue, not far behind you, who really needs support. The key to this culture change was treating people with respect.

LH: What lessons have you learned that helped you to lead transformation?

KC: You have to be out there constantly, talking to people, telling them what’s going on. No matter how often you say something, one part of the organization may not hear or may not understand. It is crucial to decode messages for staff and clients, and frame communication around their individual circumstances so that they can understand where it’s coming from.

Something that we relearn every time we do a project is the importance of communicating the significance of the transformation. We must address the questions: What does it mean for them? How is it going to work on the ground? How will it change their lives? If you’re going to perform an effective transformation, the change has to permeate through to all your people, customers and other stakeholders.

LH: What is your next major reform program?

KC: We are focusing on Welfare Payment Infrastructure Transformation (WPIT). WPIT will provide our customers with better digital services, give our staff a modern ICT platform and position the department to meet future policy needs. The WPIT program will see the replacement of the Centrelink ICT system, which has been in place for more than 30 years. We call it the “war horse” and it’s done a great deal of work. But it’s inefficient and it doesn’t allow us to be agile, flexible or fast.

WPIT will help us transform the way we do our business and put the customer at the center of what we do. At the moment, we have customers entering information digitally. This is great, but we can’t process it completely digitally. We have to have manual intervention. So what we’re trying to achieve is digital from end to end, which will be much quicker, much more accurate and much more efficient.

Another thing we are unable to do with our systems is tell people where they’re up to with their claim. We can’t say to the customer, right, you’ve gotten through this phase, this is how much longer the process will take.

Scott Morrison, the Minister for Social Services, calls it the Domino’s Pizza wheel. They tell you where your
pizza's being made, when it's in the oven, when it comes out of the oven, when it's in the box, and when it's in the car on the way to your house. We need to be able to give our customers that detail.

WPIT will also help to simplify payments. One of the reasons we get so many calls from citizens is the complexity of the payment structure. Legislation passed over the years has seen entitlements steadily build up, and it's now difficult for citizens to work out which ones apply to them. We want to get into a position where they tell us their circumstances and we can tell them what they might be entitled to.

This will also help when new budget measures are introduced or changes are made to payments. At the moment, when government wants to change people's payments, there can be a six-month time lag, sometimes longer. We need to build a system that gives us more agility.

We also want to develop a system that can be used in other agencies. We've worked very closely with the Australian Taxation Office (ATO), particularly on myGov, a single, secure account that links citizens to a range of government services. The ATO has led the way in this end-to-end processing, and we're hoping to learn from all their lessons and make sure that we stay aligned with them. Other organizations in government may not have the same customer experience as us and the ATO. Their priority could be delivering policy or applying regulations. So we need to provide a platform that these other entities can use, so that they don't have to reinvent the wheel.

In the future, we don't want to end up where we are at the moment with our system, where we've custom-made something 30 years ago that we have to keep maintaining. We'd like someone else to maintain it and to be able to get the latest update. So we think that a longer term relationship with industry is probably the better way to go.

Kathryn Campbell: “There has been a surge in demand for digital government services among the over-60s”
LH: People are used to face-to-face and telephone contact with government services. How are they reacting to the shift to digital?

KC: Australia is vast and our population is widely spread. There is no way we can have a Centrelink or Medicare office in every location that has 500 inhabitants. Maybe it's those imperatives that have driven us to provide digital applications. Our video conferencing service is a great example. Job capacity assessors use video conferencing to see people with disabilities demonstrating their capabilities. This helps the assessors determine what category of job assistance the claimants should get. These claimants are a long way from where these specialist services are located. So we need digital offerings to connect them.

To our surprise, we found that some of our vulnerable customers are more comfortable doing some things digitally than coming into an office. For example, we deal with a number of children who come to us and say that their family circumstances have broken down to the extent that they can't live with their parents or their family. We've discovered that they tell their stories in a much better way using digital communications. They are able to engage longer and they're not intimidated. We often end up doing follow-up work with them face-to-face, but that initial discussion is actually better on digital services, because that's how they communicate now.

Another surprising outcome is the willingness for retirees to engage with digital platforms. At first, some of our staff thought that they wouldn't be interested in digital offerings. But we've had a real surge in demand for digital services among the over-60s cohort. When retirees finish work, they have some time on their hands, and they generally have grandchildren who routinely use social media. And to keep up with what the grandchildren are up to, they have to engage with these platforms. So they engage with us this way too.

But we understand that there will be some people for whom digital services are not appropriate. We will ensure that they continue to receive excellent services.

LH: What do you think government will look like in the future?

KC: We need to provide digital services as effectively as banks and retailers. That has to become the norm. And we need to provide them in a seamless manner. We must focus on what the citizen needs, not how our organizations are structured.

I’d like to see us work more with our colleagues in state and local government. We do it now, but we do it differently in different places. When the citizen needs help, they’re not interested in what level of government is providing that help. So we need to get better at connecting.

If we have a person who needs support, they should tell their story just once and, with their agreement, we can share that story with the state government, which may be able to provide housing; the local government, which may provide some health support; and not-for-profit organizations, which may also provide help. It should be seamless for that individual. That's how it should work, and we're hoping that WPIT will allow us to get there.

People have very busy lives. They don't want to be spending time queuing, they want to be spending time with their family and friends. Digital platforms help us to provide government services that enable them to do just that.
Governments around the world need to do more with less. In many countries, fiscal pressures mean that spending rises on key services cannot match the levels seen prior to the financial crisis of 2007-08. But at the same time, demand for better services is rising. This is the case with education in England.

In the early 2000s, spending on English state schools rose significantly under the Labour government. This was accompanied by the beginnings of a reform program that saw power over schools start to shift away from local authorities. The Conservative-led coalition government continued the reform process. But it is far from complete. The population in England is rising and awareness is growing that the country must get better at equipping its young people with the skills they need to compete in the ever more globalized jobs market.

So, the English schools system must do more. But the challenge will be met not by more money, but by better governance and economies of scale. And the vehicles for achieving this are school groups.
Unfinished revolution

Currently, the governance and management of state-funded English schools is a mess. Previous, and ongoing, policies promoting academies and free schools — which are independent of local authority control — are well-intentioned. They liberate schools, reduce bureaucracy and increase autonomy. However, mechanisms of governance and accountability are now too dependent on “willing amateurs”, on school governing bodies, and on an over-stretched and compliance-oriented government watchdog.

The move toward more freedom and autonomy for schools in England has brought greater diversity to the school system. However, it has not achieved a generalized or sustained level of innovation, or spread best practice. This has left many schools trailing behind the best and many children unable to reach their full potential.

School groups offer a solution to this problem. School groups are organizations, such as not-for-profit trusts, that run a number of schools, usually in a local area. They offer a more coherent governance system that addresses the key issues currently damaging the system: unclear governance; inexpert governance; a lack of capabilities and professional development; and a lack of economies of scale and clear operating models.

Group therapy

With the declining role of local authorities, school governance is shared with a whole range of bodies, not all of whom have clear roles. This results in confusion and, in practice, means that a large number of schools are independent of any expert guidance or support. Performance management is often a reactionary, fault-finding conversation that only bites once a school is deemed to be “failing”.

School groups create an additional tier of governance automatically: the group governance structures sit over and above the governance of the constituent schools, each layer with clear articulated roles and decision-making powers. This central governance enables a constant performance dialogue with the individual schools, creating a proactive, supportive and developmental managerial conversation that encourages continual improvement.

The quality of school governing bodies is far too mixed. Governors often lack the core skills required to do the job of supporting school leaders and holding them to account. In addition, voluntary governors — many of whom have full-time occupations — lack the time needed to fulfill this role adequately.

School groups can offer expert governance across their network of schools via the group-level board and the corporate center. Only a small number of people are needed to fulfill these roles, making it easier to identify and recruit highly skilled individuals. The individual school-level governing bodies are then free to focus on local needs: to represent community and parent interests rather than try to drive up performance.

Many head teachers do not have the necessary financial and commercial acumen to navigate a schools landscape in which they have more autonomy. Increasing numbers work in silos, without the support and challenge to improve their school’s performance. Best practice teaching models are not shared and standardized across schools.

“Large school groups drive high performance across the system”

Schools within groups can benefit from the corporate center’s staff, who have considerable experience within their field. They might be ICT, human resources and financial professionals as well as educationalists, and are dedicated to their roles full-time. Excellent head teachers are also able to develop in their profession by undertaking group-level leadership roles, and promising school-level head teachers can learn from these leaders.

Individual, and small, groups of schools do not have the economies of scale necessary to invest in their development and improvement. Few schools have a comprehensive and holistic blueprint for running their school and, when they do, the scale of the group is too small to drive improvement across the school system.

Large school groups are able to make significant cost savings in procurement and shared staffing. The development of an effective operating model, which requires the sort of investment only large groups can make, provides a mechanism for reaching a much larger number of pupils with high quality education.

Policy action

In our view, a school system in which more schools belong to large groups, with strong corporate centers, will provide better education for many more pupils. They create the right structures to harness the best, and drive high performance across the system. However, this system will not develop on its own. Currently, only half of academies are part of a group, and the majority of these are in a group of 10 schools or fewer. Our view is that the following actions should be taken to encourage schools to join groups:

• The Government should expect most schools to join groups.
• The Government should strengthen the ability of school groups to develop strategic corporate centers. It should expect school groups to invest between 8 and 10% of the group’s revenue in its corporate center.
Individual schools that are part of high performing school groups should be exempt from inspection by the government watchdog. The school group should be inspected instead.

The Government should devolve school capital budgets to competent school groups.

Stronger structures, better performance

Through Parthenon-EY’s work in education around the world, we have seen what is required to create high quality governance, performance and support in schools. We strongly believe that our experience, and the evidence, shows this is best done in school groups that have clearly defined operating models. These operating models ensure a clear curriculum, pedagogy, management structure and labor model, aligning these elements around a coherent vision for all schools in a group.

We believe that school groups are the best way of achieving this in the UK and in many other school systems. They should be helped to grow as quickly as they are able, providing they can demonstrate that a consistent operating model is being implemented. Schools should be encouraged to join successful school groups with a range of incentives, including a lighter inspection burden and more flexible access to capital via the group.

There is an emerging sense in England that enough work has been done on structure and it is time to focus on the teaching practice. We do not accept this. School structure and governance – specifically larger, more centralized and more professional school groups – is vital to a successful school system. And this in itself will improve teaching and student performance.

Matthew Robb is Managing Director of Parthenon-EY
This article is based on the report Education in chains, written by Matthew Robb and Anna Grotberg. Read the full report at reform.uk/publication/education-in-chains
In mature democratic states, institutions have developed over generations, even centuries. But the Czech Republic, which was established in 1993 in the aftermath of the Cold War, has had to confront the challenges of modern society in a far shorter timeframe.

Over the last 22 years, tertiary education in the Czech Republic has changed beyond recognition. The number of institutions and students has increased rapidly; R&D activities have shifted to universities; university management has become more autonomous; institutions have forged links with international partners; and private institutions have opened.

However, around the world, societies are being transformed by knowledge and economies driven by innovation. Globalization means that competition is intense. So education systems are subject to pressure – from citizens who demand the right knowledge to succeed in tomorrow’s job market, from governments looking to boost the productivity of their economies and from businesses that have to hire people with the right skills. So, although the Czech Republic can look back with pride on the progress of its tertiary education sector, reform and expansion must continue.
Growing pains

Until June 2015, Petr Mlsna was Deputy Minister of Education in the Czech Government. In one of his last interviews before he left the education ministry to become Deputy Minister of Interior, he spoke to Citizen Today about the Czech Republic's tertiary education challenges.

“The challenges we face at present are, paradoxically, a side effect of successful policy,” says Mlsna. “The sector expanded very rapidly. It wouldn't be too much of an exaggeration to claim that the system — which in many respects had been designed to serve the educational needs of a small elite — is in a kind of post-traumatic shock brought on by its own expansion.”

Mlsna says that, in general, Czech tertiary institutions offer a high level of education to a relatively diverse group of students. However, the proportion of university-educated people in Czech society is still far lower than in many advanced countries, while the demand for highly qualified workers is rising all the time.

According to the deputy minister, ensuring that the tertiary system serves Czech society is a key principle. The recent expansion in student numbers has not eliminated the link between educational attainment and socio-economic background. “Despite efforts to reduce barriers to entry, achieving a university education in the Czech Republic still largely depends on family status,” he says. This must change.

Public expenditure is rising more slowly than student numbers. Money from European funding sources helps to reduce this spending gap, but there is still a shortfall. So, will students have to fund themselves? “Unlike its predecessors, the current Czech Government has made clear that it has no intention of introducing tuition fees,” says the deputy minister. “The main reason is to ensure that the already pronounced inequalities are not exacerbated.”

The deputy minister has studied the experience of countries that have introduced university fees over the last decade. He notes that Germany, with good reason, is moving away from the tuition fees approach.

However, he expects changes to the financing of public institutions. “Rather than a radical restructuring of the entire system, this is more likely to involve changes to the parameters of the current model of formula funding. European funds will also play an important role and will enable us to support our aims.”

Access and excellence

Mlsna says that the Government's aim is a “top quality public higher education system that is open to all social classes and offers everyone a chance to develop their educational potential to the maximum.” The Government's Education Policy Strategy to 2020 supports these goals, prioritizing a reduction in educational inequality, support for quality tuition and improved governance.

But serving society is only part of the challenge. The Government also wants the Czech tertiary sector to play a bigger role in the European and global production of knowledge. Balancing these interests is no simple matter. “The experience of many foreign education systems shows that the two initiatives can complement each other as long as the wide-ranging role of higher education is not lost,” says Mlsna. “For instance, theoretically I could imagine the Czech Republic making greater endeavors to push one or two of its universities into the top league of global research. However, under present circumstances, this would mean higher education not being made more accessible to a wider spectrum of Czech students.”

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Misna is not starting a revolution on Czech campuses. Policy in the sector is evolving. “Many years of discussion have revealed pretty clearly that there is no space for the radical redesign of tertiary education in the Czech Republic,” he says. The Government has decided to respect the principles of the 1998 Higher Education Act, the cornerstone of recent policy in the sector, and to modify only those parts of the Act that it deems outdated. “Despite the rapid developments of recent years, we have to ensure that there is continuity,” says the deputy minister. “In any case, it is clear from other parts of the education system that attempts at some kind of shock therapy rarely pay off in practice.”
Driving up standards

The main tool for improving standards is reform of quality assurance. Until now, this has been based on the accreditation of individual study programs by the state. “However, in a situation in which you have several thousand such programs, it seems only logical to transfer a greater share of the responsibility for their preparation, approval and implementation directly to the institutions themselves,” says Mlsna.

“This is not simply about reducing the administrative burden on the state. “The main aim is to create space for higher education institutions to improve the quality of their activities.” The new quality assurance system will also bring stakeholders such as employers into the accreditation process.

In many countries, employers are becoming more vocal about what they would like to see students learn at university. What measures are being taken in the Czech Republic to match graduates’ skills to employers’ demands?

“‘The Czech government has no intention of introducing tuition fees’”

“There is a certain disconnect between what students choose to study and the demand from employers,” says the deputy minister. “Nobody can reliably predict the long-term needs of the jobs market, which, to a considerable extent, is simply a natural phenomenon.”

Mlsna is not convinced that the problem is as serious in the Czech Republic as it is sometimes made out to be. Graduate unemployment is low, and graduates can expect to be paid much better than their less-educated peers.

“Data on the ability of graduates to find work has not revealed any alarming findings. It doesn’t even support the often-repeated cliché about unemployed humanities and social sciences graduates filling up the labor offices.”

The Government acknowledges that future employment prospects and earning potential are not students’ only considerations when selecting their courses. Mlsna is keen to encourage diversity. “Higher education has many different purposes and therefore many legitimate forms,” he says. The Government is taking account of this diversity by drawing a deeper distinction between the syllabuses of universities and colleges, and boosting the profile of vocational courses.

From the past to the future

“The link between research and education has been regarded as the definitive sign of the modern university since the 19th century,” says Mlsna. Many academics and policymakers in the Czech Republic still regard this alliance as a crucial guarantee of higher education quality.

However, recent studies indicate that pressure on universities to produce research brings a range of unintended consequences. “While research activities undoubtedly remain the primary source of academic prestige, teaching activities often fail to keep pace,” says the deputy minister. “Tuition becomes routine, and students are encouraged to regurgitate facts rather than develop innovative ideas of their own.”

“We cannot sit back complacently and assume that the existence of research and educational activities under one roof will lead naturally to innovative thinking on the part of students,” says Mlsna. A priority now is to create space for institutions to think through how they can best align teaching and research. “I believe that the newly introduced quality assurance system will create the right conditions.”

The Czech tertiary education system has come a long way in a short time. There is further to travel, but the Czech Government is keen to get there step by step.
European attractiveness survey 2015

Foreign direct investment (FDI) in Europe has hit a new high, according to EY’s 2015 European attractiveness survey.

The survey of more than 800 investment leaders from around the world shows that investors’ confidence has returned after the long Eurozone recession, and Europe has pulled further ahead of China as the world’s most attractive investment destination.

Here are some of the key findings:

- Europe attracted 4,341 projects (+10% on the 2014 survey) and 185,583 jobs (+12%), while global FDI flows slipped 8% to US$1.26t.
- Fifty percent of investors see Western Europe as the most attractive region in the world for FDI.
- Fewer respondents (38%, -6 percentage points) see China as Europe’s main competitor: the new closest challenger is North America (39%, +8 percentage points).
- Fifty-nine percent of investors (up five percentage points from 2014) believe that Europe’s attractiveness will keep improving in the next three years.
- Fifty-two percent of FDI projects and 30% of jobs created by FDI go to Europe’s top three destinations: the UK, Germany and France.
- The UK, with 887 projects and 31,198 jobs, retains a strong lead, but France (608 projects, +18%) has closed a little on Germany (763 projects, +9%).
- Central and Eastern Europe, Russia and Turkey attract 96,087 FDI jobs (52% of Europe’s total), outpacing Western Europe.
- Only 32% of investors have plans to establish or expand operations in Europe over the next year, while 64% do not.
- Foreign investors see bureaucracy (20%) and slow economic growth (17%) as Europe’s biggest flaws, ahead of the geopolitical unrest at Europe’s frontiers (11%) and big deficits (10%).

The full report sets out implications for businesses and policymakers, and explains how EY can help. Download the report, and reports for individual European countries and other areas, at ey.com/attractiveness

Megatrends 2015

Making sense of a world in motion

Megatrends are large, transformative global forces that impact everyone on the planet. EY has identified six megatrends that define our future by having a far-reaching impact on business, society, culture, economies and individuals.

While each of the megatrends stands on its own, there is clear interactivity. Digital, for example, is closely intertwined with expected transformations across the other five megatrends.

Big data, sensors and social applications will underpin the reimagining of health management. Digital technologies will drive the realization of tomorrow’s “intelligent cities.” Digital oil fields will lead to increased savings and output in the energy space, while “smart grids” will revolutionize the production, delivery and use of electricity worldwide. The ability to create digitally based business models has lowered the barrier to creating new and innovative ventures for entrepreneurs around the world.

In some cases, successful outcomes in one megatrend are related to developments in another. As the world urbanizes to the tune of 750 cities contributing 61% of global GDP by 2030, urban areas will require sustainable and resilient solutions to optimize resources, reduce risks and promote the wellbeing of all citizens. The economic promise of an increasingly global marketplace will be dependent on major investment in infrastructure and related financing in the world’s new and existing cities.

The megatrends illustrate a world in motion. Economic power continues to shift eastward. New markets and new trade linkages are emerging. The boundaries between industry sectors are blurring. New entrants that are digitally native are overturning existing business models. Existing players in one sector (technology) are entering other sectors (health) with exciting new propositions. As we hurtle toward 2030, developments within these six megatrends, as well as the interplay between them, will certainly bear close watching.

Find out more at ey.com/megatrends
Entrepreneurs are leading global job creation and young people are positive about their career ambitions, according to EY’s annual Global job creation and youth entrepreneurship survey of 2,300 entrepreneurs, and 2,800 young people aged 18–25, in 13 key markets.

According to our survey, 47% of entrepreneurs around the world expect to increase their total workforce in the next 12 months. These figures contrast strikingly with the hiring plans of CEOs at large corporates, with just 29% of them expecting to create jobs in the next year, as reported in EY’s Capital Confidence Barometer.

Hiring across borders
Entrepreneurs are increasingly looking abroad to expand their workforces. Emerging markets lead the way, with global hires most likely in the Middle East and North Africa (74%), China (68%) and India (63%). Young entrepreneurs are more likely to hire abroad than older ones, with 69% of under-35s expecting to hire globally in the next year. This is despite a lack of access to funding (43%) and negative economic factors (43%) – both reported as key barriers by our youth respondents.

Entrepreneurs focused on leaving a legacy
The survey finds that entrepreneurs are driven by more than financial gain. Thirty eight percent cite leaving a positive legacy behind as the top motivation for starting a business outside of goals relating to turnover and profitability. Other key motivations include making a positive contribution to the wider economy (36%) and inspiring others to follow their aspirations (32%).

Young entrepreneurs optimistic, but need support
The 2,800 young people surveyed are in education or involved in the jobs market. They present a positive picture, with 84% of them either quite (45%) or very (39%) optimistic about fulfilling their career aspirations. Sixty five percent are planning to run their own business at some point in their careers, and one in four have already started drawing up a business plan.

What young people with entrepreneurial ambitions most value is guidance and support from today’s entrepreneurs. A “hands on” internship and mentoring from a leading entrepreneur are seen as most likely to help them fulfill their goals (39%). It is striking, therefore, that only 36% say they feel they get enough support from local entrepreneurs, despite 75% of entrepreneurs feeling they do enough to support young people.

For more, visit ey.com/entrepreneurship
As Europe’s largest economy, Germany is a key member of the continent’s economic, political and defense organizations. And according to a June 2015 OECD economic forecast, Germany’s economic growth is projected to strengthen further, driven by both domestic and external demand. A robust labor market, low interest rates and low oil prices are expected to underpin household spending, while the depreciation of the euro will boost exports.

Germany’s unemployment is at a historical low and is likely to fall further. However, like its Western European neighbors, Germany must overcome significant demographic challenges if it is to achieve long-term economic growth. While the country’s innovation remains very strong, the declining population has already created pressure on German industry due to a decreasing number of engineers and other skilled workers.

Government spending will continue at high levels due to social net spending, but for the first time since 1969 the federal government’s budget contains no new net borrowing. However, in the near term, the structural budget surplus could be reduced to increase long-term growth-enhancing government spending. Investment has fallen short of depreciation over the past 10 years and government investment in transport infrastructure, in particular, needs to be raised.

**EY in Germany**

The public sector in Germany is decentralized, with three main levels: federal, states (16 Bundesländer) and local (around 11,000 municipalities). EY Germany has successfully built up a key advisory role at all levels of the German government, as well as at not-for-profit organizations. We offer a wide range of Assurance, Advisory, Transaction Advisory, Tax, Real Estate and Law services grouped under the following main clusters: Defense, Digital, Infrastructure and Public Finance Management.
**Defense**

Following the suspension of compulsory military service in 2011, German armed forces and the Federal German Ministry of Defense are facing the most far-reaching reform in their history. EY Germany’s Government & Public Sector team supports this process through various services such as IT Advisory, improved organizational structure, procurement and resource management.

**Digital government**

Digital government is a powerful tool to enable the provision of better public services to citizens and businesses. EY provides end-to-end services and consultation for the public sector in implementing digital government. We can help on every step from defining strategy to final implementation. Our services include: developing strategy; target group identification and expectation gathering; creating blueprints; re-engineering processes; and developing, auditing and implementing information technology.

EY Germany’s Government & Public Sector Advisory team has recently developed an “E-Government Potential Index”. The index helps our clients to identify which of their processes have the most digitization potential.

**Infrastructure**

Infrastructure investment and development is a top priority for governments around the world. Germany is no exception, and it faces challenges to meet its infrastructure obligations. Infrastructure projects are significant in size, scope, complexity and in financing arrangements. They also bring increased public scrutiny and more demand for stakeholder engagement.

EY Germany’s Government & Public Sector team provides support from the earliest stages such as project evaluation, through to procurement, financial close, construction and operations. We help our clients to devise and compare financial plans and delivery approaches for projects that involve public, federal or private financing, project revenues and/or grants – and help them to implement these plans.

**Public Finance Management**

EY Germany’s Government & Public Sector team is part of a globally connected network of experienced, multidisciplinary professionals who work with governments and public sector organizations around the world to address complex problems and achieve leading practice in Public Finance Management. Our services include: financial process improvement; public sector accounting reform (IPSAS/EPSAS); project feasibility services, including export credit guarantees; financial IT transformation; and cost reduction programs.

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**My view**

Hans-Peter Busson

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In this regular feature we catch up with senior EY government leaders about the issues they are seeing in their respective markets. Here, we talk to Hans-Peter Busson, Government & Public Sector Leader for Germany, Switzerland and Austria

You are the author of a regular EY survey of 300 German municipalities that sheds light on the financial situation of German cities and local governments. What do recent surveys show?

Our 2014 study shows that while the German municipal core budgets closed out the year with a small surplus, the gap between rich and poor municipalities is widening. According to our survey, every third municipality is no exception, and it faces challenges to meet its infrastructure obligations. Infrastructure projects are significant in size, scope, complexity and in financing arrangements. They also bring increased public scrutiny and more demand for stakeholder engagement.

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Germany’s federal government recently unveiled a program to bolster municipal investment power. What is the goal of this initiative?

First and foremost, it is meant to benefit financially weak cities and municipalities. The goal of the federal government’s initiative is to dismantle the considerable backlog in Germany with regard to infrastructure investment, such as for road construction, broadband networks and energy capacity. In addition, spending on future industries is intended to ensure Germany’s economic power.

How can EY Germany’s Government & Public Sector team help German municipalities in their reform of local finances?

Despite the support of some states and the federal government’s contribution to social spending, a sustainable and structural solution to the German municipal debt problem is not yet in sight. EY Germany’s Government & Public Sector team sees potential savings in areas such as the reorganization of local governments, inter- and intra-municipal cooperation, the sale of municipal possessions, economic optimization of municipal investments, and the merger of small municipalities.

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How can EY Germany’s Government & Public Sector team help German municipalities in their reform of local finances?

Despite the support of some states and the federal government’s contribution to social spending, a sustainable and structural solution to the German municipal debt problem is not yet in sight. EY Germany’s Government & Public Sector team sees potential savings in areas such as the reorganization of local governments, inter- and intra-municipal cooperation, the sale of municipal possessions, economic optimization of municipal investments, and the merger of small municipalities.

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You are the author of a regular EY survey of 300 German municipalities that sheds light on the financial situation of German cities and local governments. What do recent surveys show?

Our 2014 study shows that while the German municipal core budgets closed out the year with a small surplus, the gap between rich and poor municipalities is widening. According to our survey, every third municipality is no exception, and it faces challenges to meet its infrastructure obligations. Infrastructure projects are significant in size, scope, complexity and in financing arrangements. They also bring increased public scrutiny and more demand for stakeholder engagement.

EY Germany’s Government & Public Sector team supports this process through various services such as IT Advisory, improved organizational structure, procurement and resource management.

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