managementors

creating sustainable business advantage

White paper

The Productivity Challenge

This paper looks at why Productivity in the UK might not be rising as quickly as expected and some of the constraints on improving the headline numbers.

About Managementors

As a results-based consultancy, we help service industry organisations generate true performance improvements that translate into tangible margin growth.

We've proved this time and time again for many leading-edge blue chip organisations including Amey, Highways England and Computacenter.

Our expertise has helped many service and support organisations achieve lasting change. By introducing effective performance management into their operations, they've reaped the rewards of significant and sustained productivity improvements — over 30% in some cases.

This productivity improvement has always been measurable and delivered tangible benefits, so why is it that whilst the consultancy industry in the UK is estimated to be worth £7 billion a year, that the UK is perceived to be lagging behind other countries when it comes to productivity?

When overall productivity growth in the UK is largely flat, and output per hour is significantly below that seen in France and Germany, we consider what is causing this and whether it is an accurate representation of what is actually happening.

This white paper provides an insight into what we have experienced and how productivity may be only one of a number of elements on which organisations are currently focused.

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Foreword

Whilst discussions around 'productivity' have probably been taking place since the earliest humans debated who was the best hunter, it is really only since the industrial revolution that this has been a topic of scholarly discussion.

In 1775 Adam Smith wrote 'An Enquiry into the Nature and Causes of the Wealth of Nations' and discusses the reasons for varying levels of productivity, taking the examples of a pin factory and farmers across Europe. Smith concludes that "this great increase of the quantity of work which, in consequence of the division of labour, the same number of people are capable of performing, is owing to three different circumstances; first, to the increase of dexterity in every particular workman; secondly, to the saving of the time which is commonly lost in passing from one species of work to another; and lastly, to the invention of a great number of machines which facilitate and abridge labour, and enable one man to do the work of many."

As the industrial revolution gave way to further technological changes factory owners and, in times of crisis the government, were focused on delivering more output with lower inputs. From Hargreaves and Arkwright through to Henry Ford, there was a succession of technological changes combined with changes to working practices, which delivered almost continual increases in productivity, interrupted only by the great depression, before the command and control of the war economy saw productivity increase rapidly in key industries. Despite the industrial unrest of the post-war years, technological advances in the late 20th Century heralded further productivity improvements but recently, in the UK at least, these seem to have plateaued. We look at whether the published productivity figures represent what is really happening on the ground.

"From Hargreaves and Arkwright through to Henry Ford, there was a succession of technological changes combined with changes to working practices, which delivered almost continual increases in productivity"

Introduction

Compared with other OECD countries, the UK has had low productivity growth since the 1970's. The gap with other countries closed significantly during the 1990's and 2000's, with GDP per hour worked growing at an average rate of over 2% until the global financial crisis began in 2007.

Since then, however, productivity growth has been largely flat and the gap with other OECD countries has increased again, leading to the so-called productivity puzzle.

The Office of National Statistics publishes annual estimates of output per hour and it can be seen that in 2015 the UK lagged behind the US, France and Germany.

The conclusions of Adam Smith are still relevant today. We have delivered many projects where, whilst technology had been introduced, work was still required to address the skills of the workforce to ensure that companies saw benefits from their investment in this technology. Often the fundamental issues which caused significant lost time were still apparent and, whilst technology delivered some improvements in productivity, it often speeded up individual tasks without improving overall productivity. A significant effort was required to ensure that processes and behaviours were changed to ensure they were still relevant and that issues causing delays and frustration were resolved.

The MCA has recently carried out a productivity survey and 100% of managers said that productivity was important to their business and that probably matches our experience of companies who engage with us. But what about those growing sectors of the economy where productivity isn't such a driver? An engineer completing 3 jobs a day is generally more productive than an engineer completing 2 similar jobs and that is seen as a good thing, so is a teacher teaching 30 children seen as being more productive than a teacher teaching 20 children? Again, you could probably argue that they are, but is that really the outcome we want? Likewise, having one nurse looking after a ward is probably more productive than having 2 nurses but again is it giving the outcomes that a society wants?

So, maybe there are sectors of the economy where the driver isn't in actual productivity growth but is more focused on a measure of effectiveness. In these growth areas of the economy, it may be that it is outcomes which are more important than outputs. Potentially the growth we have seen recently in certain sectors of the economy is lowering the overall productivity measure of the economy and productivity, in some sectors, is actually growing more than it appears. This would go some way to explaining why consultancies, such as us, are delivering productivity improvements across the board but at a macro level productivity is stagnant.

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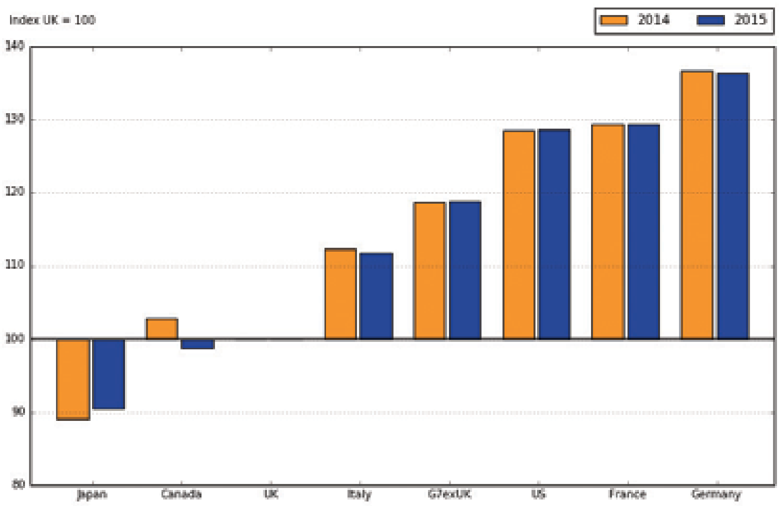

In recent years, whilst working in utilities companies, we have seen that a key measure of success is customer satisfaction and achievement of service levels and, as a consequence, recent projects have focused our activities on achieving those outcomes alongside cost reduction. In some regulated utilities environments, the non-achievement of customer satisfaction levels can lead to the loss of a contract, such is the focus on these areas. Consequently, companies have started to keep engineers 'spare' rather than run the risk of incurring penalties. Achievement of ever higher productivity is therefore often seen as too risky and a level of inefficiency is accepted. The challenge for these senior managers moving forward is to manage the tension between operations wanting to ensure they hit their targets, the finance department that wants to drive shareholder value and the regulator. Consultancies have had to work hard to find robust, innovative solutions which help achieve all of these objectives simultaneously.

Ofgem uses a RIIO model (Revenue = Incentives + Innovation + Outputs) and it has been seen that revenue caps with a move towards a focus on TOTEX, combined with outcome-based performance incentives, can drive innovation, stabilise or improve profitability and focus attention on the outcomes customers most want, rather than having a pure focus on short term cost reduction. Supporting businesses in achieving this has been a key driver of consultancy spend recently.

In addition, our experience of second or third generation outsourcing contracts has also been the increase in 'gain share' agreements, which has also driven a focus on service at an agreed cost rather than the earlier contracts, which often drove cost reduction at the expense of customer service.

Again, we have seen managers look to shore up their delivery and be less interested in investing in cost savings when they have to give a percentage of it back to the client. As a consequence, recent improvements in productivity have sometimes plateaued, or even reversed, as the focus moves towards outcomes. However, companies who have taken their eye off the cost and productivity side of the equation have come unstuck - look at Carillion and Interserve, where they have engaged in risky contracts without taking the measures required to ensure that they can be delivered, both productively and profitably.

There are, of course, other environments which operate in a purely transactional manner. Take, for example, a building maintenance environment, where the output is seen as resolving a fault or adds little perceived value in itself. In these environments there is much more of a focus on productivity – managers are rarely concerned with how a leaking tap is fixed, as long as it is fixed quickly, properly and at the lowest cost. Even here, however, there are starting to be discussions around outcome – where historically organisations were, for example, only focused on having all their lights working, they are now starting to consider the total cost of this and their energy usage meaning that, in the short term at least, maintenance engineers may be less productive than they have been historically, as they swap out perfectly functioning lamps for more energy efficient versions. The room is no lighter and has no more lights than before, but we have expended effort. How then do we measure productivity? Again, at a company level, this is possible if the correct metrics are put in place and robust control mechanisms ensure that the tasks are completed effectively.

"In recent years, whilst working in utilities companies, we have seen that a key measure of success is customer satisfaction."

Conclusion

So, maybe going forward there is a requirement to take a more nuanced view of productivity. Whilst most managers obviously need to keep an eye on productivity, this needs to be considered in parallel with other requirements. In some sectors of the economy, however, productivity figures might give a misleading impression about what is actually happening and being produced. As consultants, it is important to understand what the key drivers of success are and to ensure that performance improvement projects focus on delivering improvements to those elements which both suppliers and consumers derive value from. Productivity improvement is still key to driving this value but if consumers of a product or service are focused on outcomes, we also need to consider how an organisation delivers these sustainably.

Contact us to find out what Managementors can do for you

Call +44 (0)1256 883939

e enquiries@managementors.co.uk
w www.managementors.co.uk

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