# Making the most of our public services will demand a new way of thinking about support for innovation

Blog Admin

*With massive cuts to public spending looming, the public sector is facing the dilemma of how to do more with far less resources, and government appears to be keen to promote innovation primarily through market mechanisms.* **Charles Levy** *of the Work Foundation argues through case studies in higher education and the NHS, that a failure to understand innovation is damaging our public services and the wider economy and that more partnerships are required between the public and private sectors.*

Although our economy is finally showing signs of recovery, our public services face an almost unprecedented challenge. A productivity miracle is being demanded from the centre. Services are facing a triple lock:

- Public spending is under pressure – the Spending Review confirmed cuts of £81billion by 2014/15 and public sector employment is now predicted to fall by 310,000 over this period;
- Service demands are expanding due to demographic pressures and rising citizen expectations;
- Government is planning broad changes in the ways in which the public sector relates to the private – all services except the judiciary and security services are to be put out to competitive tender. Such large changes usually demand considerable investment to be successful, but it is unlikely that this will be available.

Despite this upheaval, three key challenges will remain for our public sector: it will still need to deliver world class public services; pressure will remain to do this in a way that places the minimum cost burden on private enterprise; and it will continue to play a major role in the wider UK economy, particularly in the knowledge economy through the position of the public sector within the wider innovation system.

Our analysis focuses on two areas which are frequently a centre of attention when we study private sector knowledge intensive industries, but which are very rarely considered in the public sector, namely how well intangible assets (R&D, software, design, brand equity and human or organisational capital) are being invested in or exploited and how well public services connect to and support a wider innovation system within their supply chains and partner organisations. This research gap is a worry since public sector activities are highly knowledge intensive – we know that annual public investment in intangible assets tops £50billion, and compared to the private sector, public sector workers are more likely to be a) employed in the most knowledge intensive industries and occupations, b) qualified to degree level and c) to describe their work as relying on knowledge intensive tasks. In other words, we should be thinking of and studying their operation as a knowledge economy industry.

We developed two case studies here focusing on how public organisations invest in innovation and support wider public-private innovation networks. The first looks at the public intangible assets bound up within the UK's higher education sector, exploring how these are managed and exploited through international education exports.

The UK Council for International Student Affairs suggests that universities earned £2.5 billion from international student fee income alone, representing between 10 and 30 per cent of the majority of universities' income in 2008/09. A further £2.5 billion is spent on goods and services in local communities while accounting for private sector colleges would increase these figures significantly. Hence, the direct impacts of international students on universities and the wider economy are sizeable and offer a significant incentive for the UK to guard and improve its market share.

Despite these large incomes, recent moves to cap migration may have a detrimental effect on the UK educational brand. Along with the US, the UK was previously perceived to be the most difficult country in which to obtain a visa to study. Changes here could result in the brightest students increasingly being drawn towards more welcoming countries such as Canada and Germany.

In higher education, there are significant limitations in terms of how well we are exploiting our strong public sector intangible asset base – future funding questions and recent visa changes risk reducing the

attractiveness of UK institutions, just at a time when international competition is improving in quality.

The second case study looks at how the NHS connects to the private sector and how well it supports public-private innovation ecosystems within its supply chains. It appears that NHS reform programmes are distracting attention from, and even retarding progress on how the NHS drives and supports innovation within its supply chain. If the NHS fails to demand and purchase innovative new products and services then this will represent a major block on the healthcare innovation system. There will be less incentive for suppliers to invest in better understanding the needs of the NHS. Suppliers may be less willing to fund research into meeting these needs, or perhaps would be more wary of forming risky joint ventures to develop products and services which exploit new insights into care approaches. Ultimately the procurement signals sent out from the NHS will impact on its ability to deliver better or more cost effective goods and services.

This represents a major issue. If the NHS is to achieve its ambitious efficiency targets without compromising its service offer, then it will need to draw on new ideas, products and services from its supply chain. Given its scale, this poor performance from the NHS will hold back innovation across the whole healthcare sector. Getting these conditions right would not only be positive for the NHS, but could represent a major boost to the private sector knowledge economy. The case illustrates the need to create or refocus bodies to build intermediary institutions capable of supporting a broad innovation ecosystem.

Success will depend on the public sector finding new and better ways to deliver services and to better leverage its support for the wider economy. Unfortunately the public sector has a particularly poor productivity record – our best measurements suggest that over the past decade public sector productivity actually fell. Worse still, our analysis shows that, just when it is most needed, other priorities appear to be overriding action to best exploit our public services.

The current public sector reform agenda appears to focus on driving innovation in the public sector through market mechanisms alone – putting more of the public sector out to tender. But this risks ignoring the issue – the private sector cannot be a substitute for public innovation. Instead we should also be making the most of our public services by exploiting public intangible assets and supporting the development of public-private innovation ecosystems which can drive performance within our public services and benefit the economy. Success here will depend on the public sector increasingly fostering new relationships with private sector partners. A shift from adversarial engagements towards more collaborative arrangements would better support the co-development of new products and services as well as the transfer of best practice.

*Read the full report:* Making The Most of Public Services: A systems approach to public innovation.