

Government and Public Sector

# Seizing the day

The impact of the global financial crisis  
on cities and local public services

a PwC Public Sector Research Centre publication



‘Our goals in publishing this report are to outline the challenges and the opportunities facing local government leaders following the onset of the global financial crisis and to set out our views on the future for cities and local governments and successful ways for local government leaders to act. The research builds on the insights from PwC’s Global Cities and Local Government Network’s publication ‘Cities of the Future’ and subsequent toolkit, drawing on our experiences in working with cities and local governments around the world.’

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# Foreword

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The ‘Great Recession’ has had a dramatic impact on the financial services sector and other areas of the private sector and highlighted the importance of the role of government at international and national levels in addressing global and systemic risks. But what has been the impact of the global financial crisis on the role, and brands, of cities and local governments? How have their budgets (both costs and revenues) been affected? And how confident are local government leaders in their ability to deal with future threats and most importantly, effectively and swiftly respond to these challenges?

This report addresses these issues, based on the findings of an international survey of the leaders of cities and local governments which sought to gauge their reactions, and understand their responses, to the global financial crisis. And it is clear from their reactions that local government leaders have already seen a significant impact on their organisations, brands and a collapse in revenues.

## Tough times, hard choices

Tough times are driving innovation, collaboration and service design and rationalisation. There are winners and losers – with local government leaders, particularly in Developed countries, facing the need to transform in the face of impending crisis whereas others, particularly in Developing countries, have the opportunity to learn the lessons and leap frog to new models of service delivery, particularly focusing on early intervention and prevention and making more use of commissioning.

Now is a time to get back to basics, focus on those functions where cities and local governments can add the most value and retain the talent critical to these core functions. It is also a time for greater and better collaboration, across public sector agencies, with private and voluntary/not-for-profit organisations and spatially, across geographies.

Our goals in publishing this report are to outline the challenges and the opportunities facing local government leaders following the onset of the global financial crisis and to set out our views on the future for cities and local governments and successful ways for local government leaders to act. The research builds on the insights from PwC’s Global Cities and Local Government Network’s publication ‘Cities of the Future’ and subsequent toolkit, drawing on our experiences in working with cities and local governments around the world.

We appreciate the time taken by the local government leaders who responded to our survey. In order to provide a geographically balanced spread this report focuses on the 58 responses we received for the global survey. The results are also split by Developed countries (33 responses) and Developing countries (25 responses), in cities comprising a total population of over 120 million people. We have also commissioned country specific reports for Brazil, The Netherlands and Sweden covering an additional 215 cities. The details of our sample and our methodology for this global report are set out in the Appendix.

This report would not have been possible without the active participation of all the contributing cities and local authorities. We would like to thank all respondents for their contributions and whose views form the basis for this report.



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# Summary

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Fears of a protracted global recession, over-regulation, lack of access to capital markets and a rising tide of protectionism dominate business concerns across the world.<sup>1</sup> In contrast, governments at all levels have seen the demand for their services rise inexorably which has led to a significant increase in public sector spending.

But all this is about to change. The insulated environment for cities and local government will not survive, with swingeing budget cuts on the horizon. Those local government leaders who believe that the growth days for public spending will continue risk complacency and failing to put in place the foundations for a very different future from the first decade of the 21st century.

Within 12-18 months the 'Great Recession' will have ended for the private sector but will only just be beginning for the public sector. There is recognition amongst many, but not all, of the local government leaders we surveyed that trouble is brewing with a revenue crisis top of their concerns:

- just over two thirds (67%) of the local government leaders in our survey believe that the global financial crisis has had a significant or very significant impact on their organisations, particularly in the Developed economies;<sup>2</sup>
- almost two thirds (63%) of respondents have already seen a revenue shortfall for 2008 or 2008/09 of up to 20%, with another 13% seeing revenues impacted by 20% to 40% and a remarkable one in twenty (5%) already seeing an impact of over 40%; and
- over half (55%) believe there has been a slight or highly adverse impact of the crisis on their city's/local government's brand/perceived image.

So where does this leave the leaders of cities and local government? The current model of local government faces major threats and is at risk of breaking. Public spending will have to be cut to turn the tide of debt in many (particularly Developed) economies and capital and talent is likely to move from the safe haven of the public sector to the higher returns to be found in private enterprise as the latter recovers. Many of the Developing countries, however, which had less exposure to the impact from the financial crisis also have an opportunity – to leap-frog to a new operating model with more focus on strategic commissioning, public-private partnering and pan-public sector working, from which Developed countries in turn can learn.

We believe, therefore, that there is a window of opportunity in the next year for local government leaders to prepare for transition and ensure that, as the private sector takes off again, cities and local governments have:

- positioned themselves to take advantage of a resurgence of global economic growth;
- protected their 'capitals' from the worst of the onset of public sector recession;
- innovated their service delivery models and roles in the supply chain;
- built resilience into their organisations by transforming their capabilities; and
- exploited this 'once in a generation' opportunity to transform the role they play in society.

We have already seen this cycle in the private sector. CEOs responded to the Great Recession by cutting costs and reducing staffing whilst focusing much more on managing risk. Yet, whilst CEOs battled to restore their relationship with consumers as well as regulators, trust in government's brand (at international, national, regional or city levels), appears to have survived. Indeed, the brand of local government is on the up – as a safe haven and trusted employer. So how can local government leaders build on this and sustain themselves and their organisations into the medium term?

City managers and local government organisations around the world are facing tough choices and need to innovate, collaborate with their neighbours and build effective and durable organisations. This is endorsed by the findings of our survey where we found that:

- frequent use is already being made of a variety of collaborative partnerships, such as public-private partnerships, public-voluntary partnerships, outsourcing and shared services with opportunities both to reduce costs but also increase revenues;

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<sup>1</sup> For more details of business views on their key business issues as they affect government, see 'Rethinking and reshaping the business environment: Government and the global CEO', PwC's Public Sector Research Centre (PSRC), January 2010.

<sup>2</sup> 'Developed' countries are defined as OECD members; 'Developing' as non-OECD members.

- almost all (96%) local government leaders believe that nurturing innovation is important or very important to their city/town's future growth and development, which in turn requires a supportive leadership and culture as well as talented staff; and
- about 80% believe that service re-design and service rationalisation are the most effective responses to financial crisis.

But it also appears that many local government leaders may be underestimating the size of the challenge they face and may not be considering the true extent of the range of strategic responses they will need to adapt to their new environment:

- seven in ten (72%) are confident or very confident that they will be able to achieve their socio-economic development targets in the next five years;
- over half of the local government leaders believe they have the tools to control spending, are empowered to make decisions and have control and flexibility over the management of local resources; and
- only one in five (21%) ranked commissioning in their top three important functions today, which falls to 12% in three year's time, despite this being one of a range of important strategic responses likely to be needed to address cut backs in public spending.

The responses to our survey therefore suggest a lack of urgency in the face of the storm to come. Now is not the time for incremental reductions of 5% or so year on year in budgets, rather it is a time to contemplate immediate deep cuts of up to 25%-30%.<sup>3</sup> Experience has shown that the private sector did not anticipate the severity and depth of the recession and acted too late but local government leaders can learn this lesson. Our challenge to local government leaders is – why wait before acting?

With clear thinking, and careful planning, these cuts need not decimate services. By reviewing discretionary services, working at early intervention and prevention, focusing on commissioning and being really serious about forming effective local partnerships, leading cities and local government teams are showing the way.

The window of opportunity is now, for making tough choices and building partnerships to sustain local government into the future. Cities and local governments need to take advantage of the current crisis and innovate their service delivery, re-shape and transform their roles and functions and put in place measures to retain the talent attracted over the last two years. For when the private sector returns to growth, it will be too late!

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<sup>3</sup> From an in-depth analysis of UK local government pressures – 'Perfect Storm' UK PwC, 2009.



# Impact of the crisis

There is no doubt that the global economy is coming through a huge crisis: indeed in many countries we have not seen the worst yet, with unemployment lagging the recovery. In this section, we set out the views of the local government leaders we surveyed on the immediate impact of the global financial crisis in terms of their revenues and spending priorities.

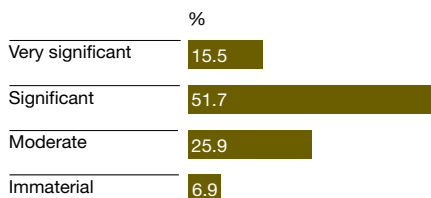
## A collapse of revenues

A little over two thirds (67%) of the local government leaders in our survey believe that the global financial crisis has had a significant or very significant impact on their organisations (Figure 1 and see respondents' verbatim quotes). This is more strongly felt by cities and local governments in Developed than in Developing countries (79% versus 52% respectively), which is not surprising since it is the Developed economies which have suffered the greatest impact from the Great Recession.

Furthermore, over half (54%) of all survey respondents believe that the financial pressures are already present in their organisations, with a further quarter (25%) expecting the pressures to peak in the next 2-3 years. Again, there are differences between type of country, with 94% of Developed countries believing financial pressures are already present or likely to peak in the next 2-3 years.

**Figure 1**

Overall assessment of the impact of the financial crisis and other financial pressures on your organisation



Base: 58 responses

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'Revenues of the budget are decreasing, grants from state have been cut, as a result the services may not be provided in a necessary amount.'

'In the near future the municipal organization will have to cut spending. However, the awareness of the urgency of cuts is only slowly growing. In addition, the municipality will need to be even more customer-friendly in order to facilitate the urban economy as good [sic] as possible (less rules, easier and smarter).'

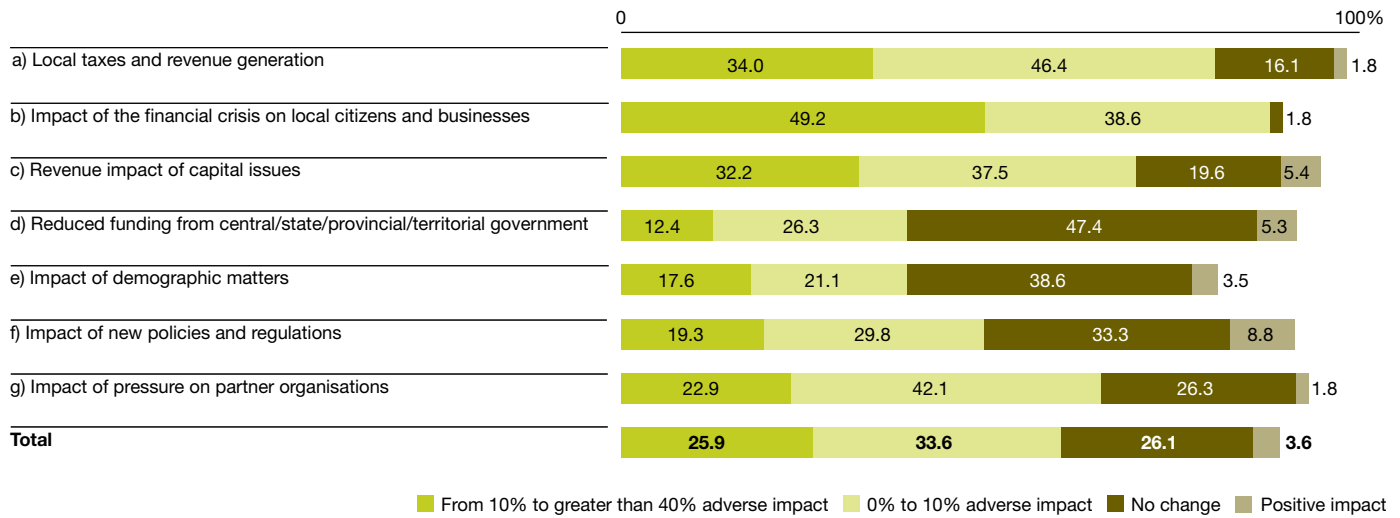
'The impact of the financial crisis has not yet reached the municipal sector. In 2007 and 2008 this sector experienced very positive developments in revenue. The development in revenue is also positive for 2009 and 2010. It will not be until 2011 and continuing to 2012 that these effects will reach the municipalities.'

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Overall, almost two thirds (60%) of the local government leaders in our survey believed that their most recent budgets had been adversely affected by a range of factors, with a quarter (26%) seeing an impact of between 10% and 40% or more (Figure 2).

**Figure 2**

As a % of your total budget for 2008 or 2008/09 (depending upon your reporting period) indicate the extent to which you believe the following factors have impacted upon revenues or costs.



Base: Responses for each statement varied from 56-57; responses may not total 100% as 'Don't Know' excluded; 'Other' responses not shown.

There has been a particularly dramatic impact on revenues (both from local taxes and other sources of revenue), with almost two thirds (63%) of respondents seeing a negative revenue impact for 2008 or 2008/09 of up to 20%, with another 13% seeing revenues impacted by 20% to 40% and a remarkable one in 20 (5%) seeing an impact of over 40%. Of note, there appears to be a difference between types of country with a quarter (25%) of local government leaders in Developing countries seeing a 20%-40% adverse impact compared to 3% of local government leaders in Developed countries.

‘The weak economic climate has negatively impacted the development of tax revenues. Tax financing is not increasing at pace with cost increases and population growth. The costs for welfare support and other social welfare operations is increasing. Certain municipally-owned companies’ operating revenues are decreasing.’

‘The financial crisis led to slow economic growth and most traders were unable to break-even in their businesses and this resulted in poor revenue collection from the traders. The financial crisis has harmed revenue collection and this impacts implementation of capital projects.’

‘Municipal governments have a strong influence on the life in cities, especially with regards to employment and income. The decision of the Municipality of Sao Paulo to reduce the minimum possible extent of the planned investments has contributed decisively to mitigate the impacts of the financial crisis in the city of São Paulo, even with the decline in municipal tax collection, recorded in 2009.’

This shortfall does not, however, currently appear to be driven by reduced funding from other tiers of government (be they central, state or provincial): indeed, almost half (47%) of respondents have seen no change yet of funds from these sources and one in twenty (5%) have seen a positive impact, where some national governments (such as in Sweden) have provided an infusion of funding to local government during the crisis.

The key adverse impacts on local budgets to date appear to be from:

- local citizens and businesses/other partner organisations, where 88% of the local government leaders surveyed see a negative impact and almost half (49%) believe that there had been an adverse impact of 10% or more – again, local government leaders in Developing countries perceive more of an issue, with 40% seeing a 20% to 40% adverse impact compared to 12% in Developed countries;
- the revenue impact of capital issues such as lower returns on investments, reduced interest rates on deposits and extended maintenance on surplus property assets, where 70% of local government leaders surveyed perceive an adverse impact; and
- new policies and regulations, where almost half (49%) of respondents believe there has been an adverse impact, although almost one in ten (9%) see a positive impact, perhaps due to either de-regulation or further devolution of power to the local level.

‘Existing pressures come from wage increases in collective agreements, ageing infrastructure, responsibility for funding of social programs (funded by senior levels of government elsewhere) and a lack of enough revenue sources/types that grow with the economy.’

### Local government – a ‘safe haven’?

Alongside the financial impacts of the global financial crisis, there are a range of less tangible impacts, most importantly on city brands. The local government leaders we surveyed have varying views on the impact of the crisis on the brand of cities and local government. Whilst 45% believe that there has been a slightly adverse impact on the brand or perceived image of the city/local government, with one in ten (10%) perceiving a highly adverse impact, a substantial minority of over a quarter (26%) saw no change and, indeed, close to one in five (17%) perceived an enhancement of their brand/image (Figure 3).

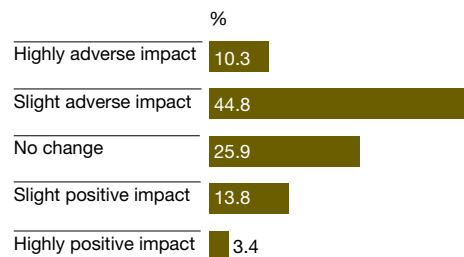
There appears to be a difference by type of country, with local government leaders in Developing countries perceiving a highly or slightly adverse impact (84% in Developing countries compared with 33% in Developed countries).

‘It is important to continue investments in promoting the city. One should try to avoid a dull and sad atmosphere.’

‘The current crisis must be understood as a short-term phenomenon and therefore its effects are also restricted to 2009. It did not affect the city brand or image, which are considered very valuable as have resulted from the actions performed by the current administration in recent years.’

**Figure 3**

What has been the overall impact of the financial crisis on your city/local government brand/perceived image?



Base: 58 respondents; respondents could only choose a single response; total may not equal 100% as ‘Don’t Know’ excluded.

Although at first sight this may suggest that the brand of cities and local government has been tarnished, the impact of the crisis is likely to be less than that experienced by the private sector. For example, an FT/Harris poll of adults in six Western countries last year showed the recession negatively influenced the public’s view of business leaders – on average, 67% people said they held a worse opinion of leaders as a result of the downturn.<sup>4</sup> This suggests to us that to a certain extent cities and local governments have been seen as a ‘safe haven’ in a time of crisis. With local citizens and business in distress and looking for help, local government can act as a safety net for their communities.

### Branding and collaborating across layers of government leads to success

On 2 October 2009, Rio de Janeiro was announced as the winner of the 2016 summer Olympics bid. Two main factors contributed to the city’s success. Firstly, successful branding neutralising negative concerns about security and poverty while emphasising Rio’s natural beauty, passion, diversity and creativity. Secondly, and most importantly, the alignment of the three levels of government – City, State and Federal – providing a good example of what can be done when all levels of government work together collaboratively towards a common goal and orchestrating a well integrated effort. With the bid won, the eyes of the world are watching how the three levels of government will continue to work together to deliver on the promise and to give the world an unforgettable experience that helps accelerate the city’s economic and social development.

4 FT/Harris Interactive Poll (April 2009).

Cities and local government must learn from the private sector's experience of the last two years (see below). Businesses ignored the warning signs and underestimated the severity of the crisis that faced them and there is a similar risk facing the public sector. There is no doubt in our experience that the impact will be greater than many of the respondents to our survey currently think. For instance, in the UK PwC has predicted cuts needed of 25%-30% of spend over the next three years.<sup>5</sup>

To address this sort of challenge, there will be a need to make tough decisions and act now as local government leaders can quickly lose the goodwill of their electorates and of their people: as soon as the private sector picks up, investment funds and talent will move back to a private sector focus.

## What can be learned from the private sector?

Private sector companies that are emerging from the downturn as winners are those who proactively undertook a strategic, financial and operational review, while positively maintaining 'business as usual' and managing varying stakeholders' agendas. The fundamental priorities for local government leaders to learn are:

### Strategy

- A clear and deliverable strategy which sets out: the focus for the organisation; what's driving it; what does it do best and why; and how this will be impacted by the downturn;
- The ability to respond to the constantly changing environment through sensitivity to market forces and having visibility of the future impact; and
- Having a clear mandate for change which is driven through the organisation.

### Finance

- In a downturn 'cash is king'. De-gearing balance sheets increases the flexibility of the organisation to deal with adverse events. Effective working capital management will also help to reduce cash requirements;
- Management should model a range of financial, operational and workforce scenarios that reflect the impact of the downturn on the organisation, allowing it to quickly explore their strategic options and speed up the decision making process; and
- Reliable management information is vital, with clearly defined performance indicators, giving clarity on which parts of the organisation are profitable and which are loss-making, is essential.

### Operations

- Focus should be on what really matters – organisations should evaluate which services, customers and channels create or destroy value including revisiting existing investment programmes and determining which initiatives could be stopped or deferred;
- Accelerating cost reduction programmes by building the infrastructure needed to deliver change without compromising the quality and timing of 'day to day' service delivery. This means cost reduction needs to be targeted rather than rolling out across the board cuts, and should be focused on extracting value and reducing complexity;
- Recognising the value of people. Regular and clear communication with employees is essential to ensuring their engagement; and
- Identifying key talent and developing appropriate incentives for them means that you can retain the people who are critical to your organisation's future.

### Stakeholder management

- Evaluating the likely impact of the downturn on your stakeholders and making sure you understand their agendas is crucial. Management will need to maintain a regular and open dialogue in order to manage stakeholder expectations and win their support for change.

We believe that these core principles are equally applicable in helping public sector organisations to work through their spending squeeze which is coming later, but may last for longer, than that in the private sector.

Source: 'Managing in a Downturn: Delivering public sector change in a volatile market', PwC Public Sector Research Centre 2009

<sup>5</sup> See 'Perfect Storm', PwC UK, 2009.

# Ability and readiness to respond

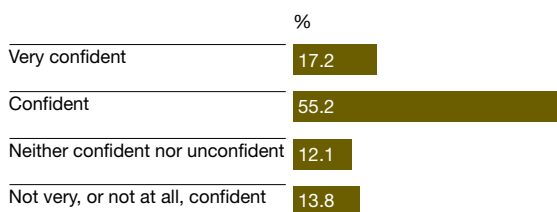
Cities and local governments face making decisions more rapidly and in a more complex environment than ever before. As a result, there is a need for agile management mechanisms to cope with the speed and complexity of decision-making in a modern global economy. We set out below the views of our respondents on their capability to respond.

## Signs of complacency?

In other sectors, such as financial services, there have been accusations by commentators of a complacent attitude to risks in the face of signs of distress. Is this the case in local government?

**Figure 4**

How confident are you that your local government will be able to achieve its socio-economic development targets within the coming five years?



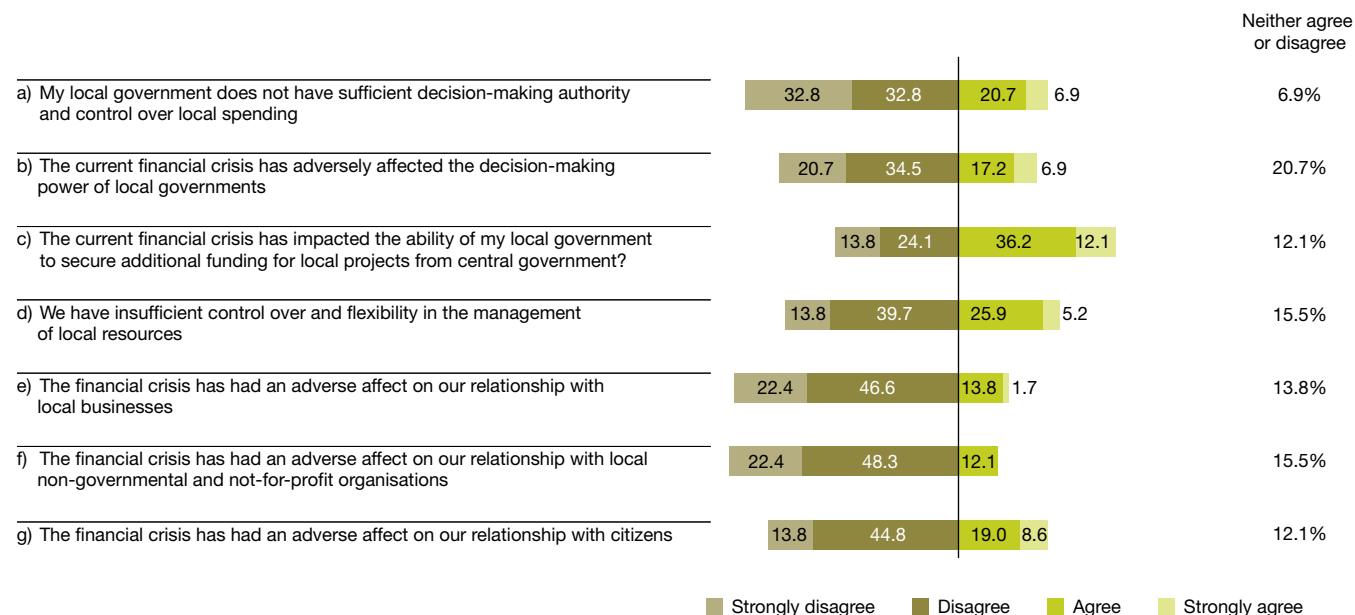
Base: 58 responses; respondents could only choose a single response; total may not equal 100% as 'Don't Know' excluded.

From our survey it appears that the majority of local government leaders (72%) are confident or very confident that they will be able to continue to deliver necessary socio-economic outcomes through a combination of careful financial management and appropriate investment (Figure 4). This is particularly the case in Developing countries where 88% of local government leaders are confident or very confident.

The leaders we surveyed also feel on balance that they have the tools to control spending, are empowered to make decisions and have control and flexibility over the management of local resources (Figure 5). They also perceive an enhanced role and reputation with local businesses, NGOs and citizens although this appears to be more the case in Developed countries. In Developing countries, a quarter (24%) of local government leaders believe that the financial crisis has had an adverse impact on their relationship with local NGOs and not-for-profit organisations, rising to a third (36%) with local businesses and over a half (58%) with citizens.

**Figure 5**

How strongly would you agree or disagree with the following statements?



Base: 58 respondents; responses may not total 100% as 'Don't Know' excluded.

There are more concerns over the availability of central funding for local projects, with almost half (48%) agreeing that the current financial crisis has impacted the ability of local government to secure additional funding for local projects from central government.

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‘The decline in the transfers of federal and state government’s funds in 2009 resulted in the stoppage of new municipal projects.’

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Importantly, local government leaders believe that the financial crisis has enabled them to attract and retain high calibre professionals: as part of our survey we asked local government leaders if ‘the financial crisis has allowed my local government to attract/retain higher calibre professionals’ – 43% agreed or strongly agreed. This is re-inforced by being seen as supportive by their own staff who have felt the impact of the crisis themselves: 40% agreed or strongly agreed ‘with the manner in which my local government is communicating with and supporting employees in personal distress due to the financial crisis’.

#### PwC’s view

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The talent that local government has attracted in the downturn and which it has nurtured through its caring approach to its staff is a strength which needs to be built upon in order to retain talent when the private sector upturn threatens to attract it away again.

We believe, however, that there is a huge risk that local government leaders become complacent and that the control that they feel they have over their own futures may be swept aside as central government hands down swingeing budget cuts, with local government leaders put under pressure to cut staff. This presents a ‘burning platform’ for local government leaders to identify, nurture and protect the talent in their organisations ahead of the private sector recovery.

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‘Retaining talent is key. The city-promotion is centred around this objective. The crisis is bringing about that we, as an employer, are able to attract more top talent.’

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#### Developing leadership and human capital

The Western Region Municipality (WRM) in the Emirate of Abu Dhabi is a newly created entity in 2007 which has the challenge of serving sparse populations located in a geographically dispersed region. Since its inception, WRM has defined two main priorities: to develop national leadership and human resources; and to invest in their training and development. As part of this focus on the human capital, the WRM has recently embarked on an integrated programme to attract and retain talent through defining a competency framework that is aligned with the WRM’s strategic objectives, conducting ‘Leadership Development and Assessment’, and defining individual and organisation wide capacity development plans. This clear commitment to leadership and human capital development is a key enabler in transforming the work environment at the WRM to an attractive one that competes on an equal footing in the war for talent.



# A changing role for local government?

The financial crisis has had a major impact on the private sector, leading CEOs to re-visit their purpose and strategies. Is the crisis having the same impact on the functions and spending priorities for local government leaders and city managers?

## A change of function?

Cities and local governments have a range of functions which vary by country and jurisdiction. Before the financial crisis, service provision was clearly seen as the most important function for cities and local government, with over four in five (86%) of respondents selecting this (Figure 6). The importance of service provision continues to remain important both now and in the future.

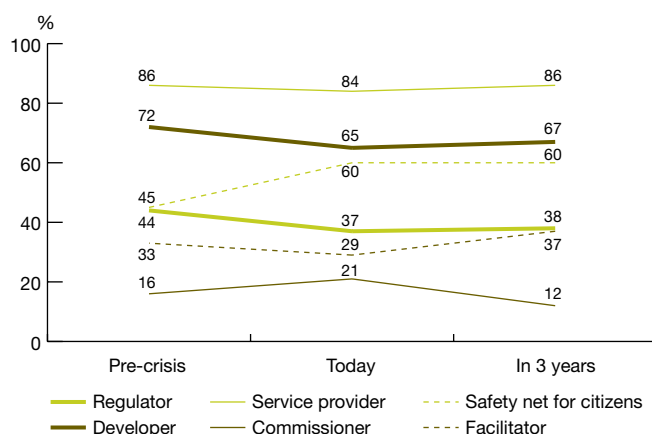
The other important functions are seen to be as a:

- developer (a provider of basic infrastructure services), although this role has taken a dip both today and looking forward, perhaps due to continuing problems in capital markets; and
- safety net for citizens, which has grown in importance with the onset of the crisis and then is perceived to remain high in importance not only today, as could be expected in the midst of recession, but also into the future.

To a lesser extent, the functions of being a regulator and a facilitator (creating an enabling environment for private/not-for-profit sector to implement initiatives) are important. There is, however, an apparently diminishing role for regulation. This appears to be primarily in Developed countries – 29% of local government leaders surveyed see this role as important in three years' time compared with a much higher 50% for local government leaders in Developing countries.

**Figure 6**

In your opinion, please rank, in order of importance, the following functions of Cities and Local Government before the financial crisis, today, and in three years time?



Base: Responses varied between 41 and 50 for individual functions; measured by aggregating the importance scores of 1, 2 and 3 (out of 7) for each function; 'Other' responses not shown.

Notwithstanding a slight rise today, this is also true for commissioning (even in Developed countries) with only 12% of all of the local government leaders surveyed seeing this to be an important function for cities and local government in the future. In responding to this question, it may be that for some countries commissioning has a negative image, but our view is that commissioning is a more sophisticated approach than, say, privatisation or outsourcing. It involves defining the type of need for public services, how this is best delivered (in the public sector or by private or voluntary sectors) and procuring from the source offering best value for money.<sup>6</sup> It is therefore a way of changing the role of government in the supply chain in an innovative way. As such, we see the role as of increasing importance: as public spending is restrained to restore fiscal imbalances, the public sector needs to look at radical ways to deliver more for less or the same for less.

<sup>6</sup> Commissioning in the UK health service is described as 'the process of deciding what services or products are needed, acquiring them and ensuring that they meet requirements. It is a complex process with responsibilities ranging from assessing population needs, prioritising health outcomes, procuring products and services, and managing service providers' (UK NHS).

## Bringing down the walls

In Ontario Canada, many citizens and businesses had difficulties in accessing basic services such as vehicle abstracts or business registrations due to inconvenient hours, limitations of service access channels or simply lack of clarity about where to go for service. The Ontario government's successful response was to create a new entity, Service Ontario, which was empowered to take ownership of the end-to-end processes, previously owned by other entities, to provide services through a number of integrated channels that allow each citizen or business to choose the delivery channel that is most convenient. Many services such as health cards, birth certificates, marriage certificates, driver's licences and business registrations are conveniently provided on-line, by phone, by mail, through kiosks or in person. In addition to increasing customer satisfaction by listening to its customers, Service Ontario also managed to reduce the cost of service delivery by promoting the use of more cost effective service delivery channels.

There is no doubt that whilst quite a few local government leaders see no major change in role, the verbatim responses we received demonstrate how some recognise that cities and local governments will face their own recession as the private sector climbs out of its own and that this will potentially have a dramatic impact on their future role. This inevitably entails reviewing the ways in which services are delivered and considering purchasing services based on a needs assessment rather than providing them in-house.

‘The fundamental role of the city has not been changed by the financial crises. The main role of the city is to provide people living and working here and also companies with maximised general conditions, good infrastructure, high life quality, social security and solidarity of the community. The financial crisis requires different additional challenges to the city.’

‘The financial crisis has not had an impact on the role of the municipality.’

‘There is no change in the role of cities, but the cities have to focus more on the role as buyer of services and products and have to take care of social welfare.’

‘In general we see that the role of the city is changing, with the facilitating role becoming increasingly important, as well as the role of a social safety net.... Also, the municipality (in the role of regulator) is asked by citizens and businesses to make rules simpler and easier to understand.’

‘The financial impact of the recession is only truly being experienced in the 09/10 financial year with reduced cash inflow. The impact on planning and service delivery will only really be felt during the 10/11 financial year as reduced sources of funding are made available.’

‘The fall in revenues (dividends and taxes on persons) will considerably reduce their potential to invest, which in turn threatens to have a negative impact on economic revival plans. The rise in unemployment and, more generally, exclusion from the labour markets, will cause municipalities to be confronted with even greater difficulties.’

## Spending priorities

The priorities highlighted in our survey for spending comprise a combination of meeting current needs whilst investing for the future. There has been a significant increase of spend since the crisis in areas of distress, particularly social care and health, as well as forward-looking investments, particularly economic development and investment promotion (Figure 7). Of note, over a quarter of local government leaders saw a major or significant increase of spend in social care and economic development, along with transportation (although 12% also saw a decrease for transportation).

‘Much more emphasis on safety net for citizens (social security), and on the role of local government as developer by accelerating investments in local infrastructure and sustainability. These investments will go on while the crisis continues.’

‘In future Cities and Local Government will concentrate more on economic development initiatives as a platform for economic opportunities for citizens.’

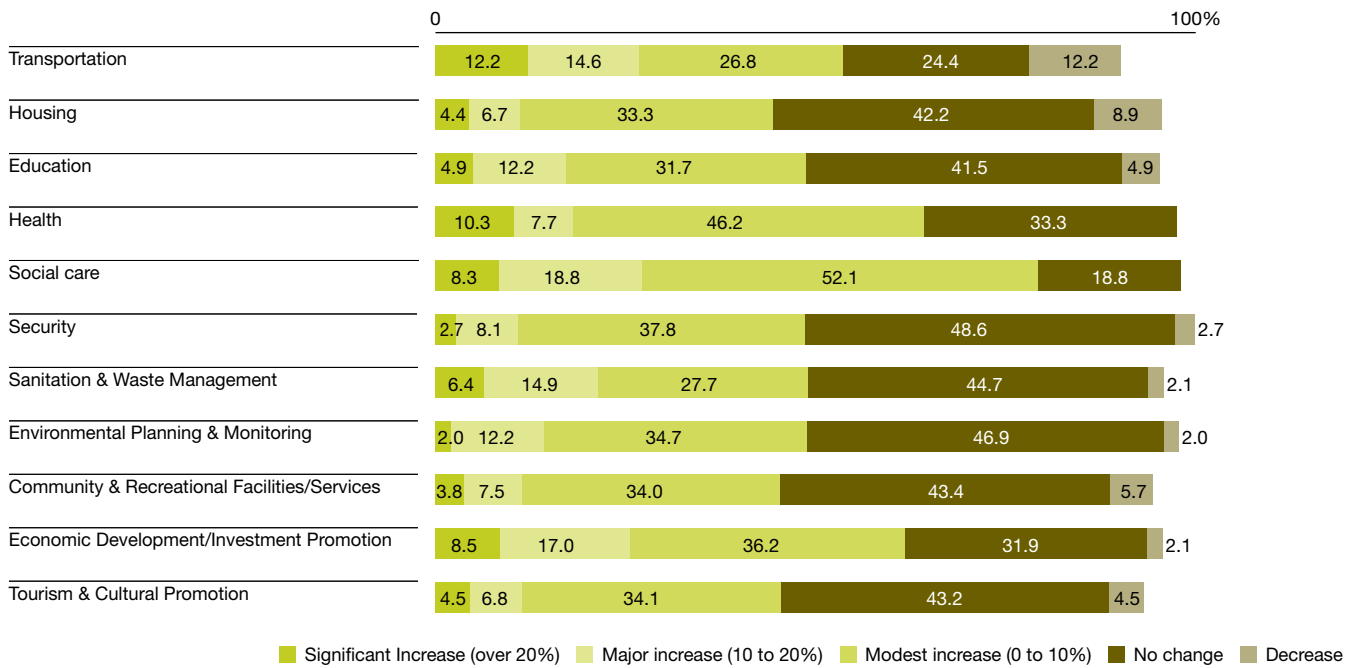
‘There was a reactivation of an agenda of economic development for the city through actions to improve the business environment (cutting bureaucracy, reducing taxes), working closer with the private sector and attracting new investments. On the management side, the strategic planning resulted in the definition of priority projects and performance indicators for each area (health, transport, employment and income).’

‘We are now investing in order to keep the impact of the crisis as low as possible, and to survive the recession. This puts heavy pressure on our reserves and financial position. If the economy starts to recover we will have to make cuts. How long this will take, and whether our actions will be effective, is very uncertain.’



**Figure 7**

Please identify the current main areas of spending for delivery of local government services in your city/town and indicate the change in level of spending (increase, no change, decrease) for each one of these services since the crisis took place.



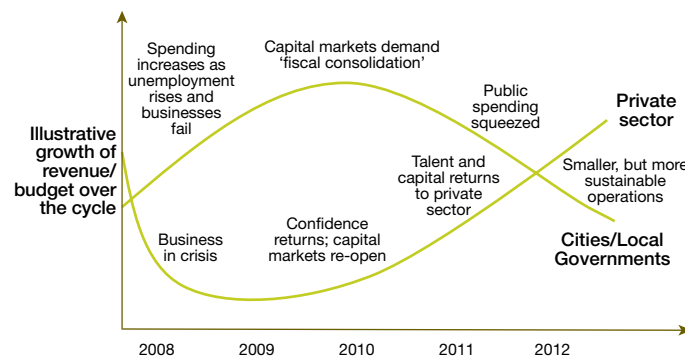
Notes: Base for responses for each area of spend varied between 37 to 53; responses may not total 100% as 'Don't Know' responses have been excluded.

**PwC's view**

The findings of our survey suggest that local government bodies themselves do not see a significant change in either the range of services or their role in delivery. But we believe that the size of the challenge will force them to consider moving to new delivery models such as commissioning, as was the case in the private sector.

The current focus on local government will also not last as long as local government leaders think. The window of opportunity is short and we believe there is an important change happening in the role of local government as it navigates the journey through the recession (Figure 8). During the private sector recession, its image was enhanced as it provided confidence and certainty during turbulent times. To survive their own public sector recession, cities and local governments must seek now to build on, and sustain, this brand into the future if they are to compete equally with a resurgent private sector.

**Figure 8**  
A difficult journey to navigate



# Critical success factors

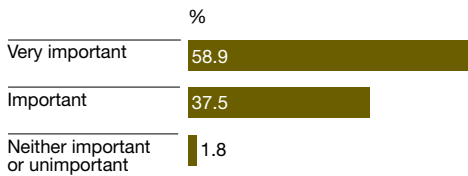
The response to the financial crisis needs to be strategic, seizing the opportunity, as well as addressing important underlying root causes and not just relying on cost cutting. We set out below the factors from our survey which appear critical to success for cities and local governments in riding out the storm to come.

## Innovation

Local government leaders recognise how critical it will be for their future to be innovative (Figure 9). It is important to observe that the financial crisis appears to have had a positive impact on local government: half (50%) of the local government leaders we surveyed believe that the crisis has had a positive impact on innovation, rising to 67% of local government leaders in Developed countries. This appears to support those who claim that being forced to make do with less forces organisations to do things very differently in response. For instance, some local governments have considered developing new functions to address the crisis such as municipal banking, although whether this proves to be an effective response remains to be seen.

**Figure 9**

How important do you think innovation in your city/town's local government is to its future growth and development?



Base: 58 respondents; respondents could only choose a single response; responses may not total 100% as 'Don't Know' and 'Not Answered' have been excluded.

A major barrier to change, however, appears to be cultural rather than regulatory issues: whereas 57% of our respondents believed that 'the financial crisis has made my local government more risk-averse', 50% do not believe that 'the current regulatory structure within my organisation inhibits innovation and change'.

In our view, this means there needs to be a call to action for leaders to show leadership and encourage innovative thinking and cultural shifts.

'Again, the creation of an innovative environment is what we have been implementing in the last 5 years and is not associated with events, characterized as a short term shock.'

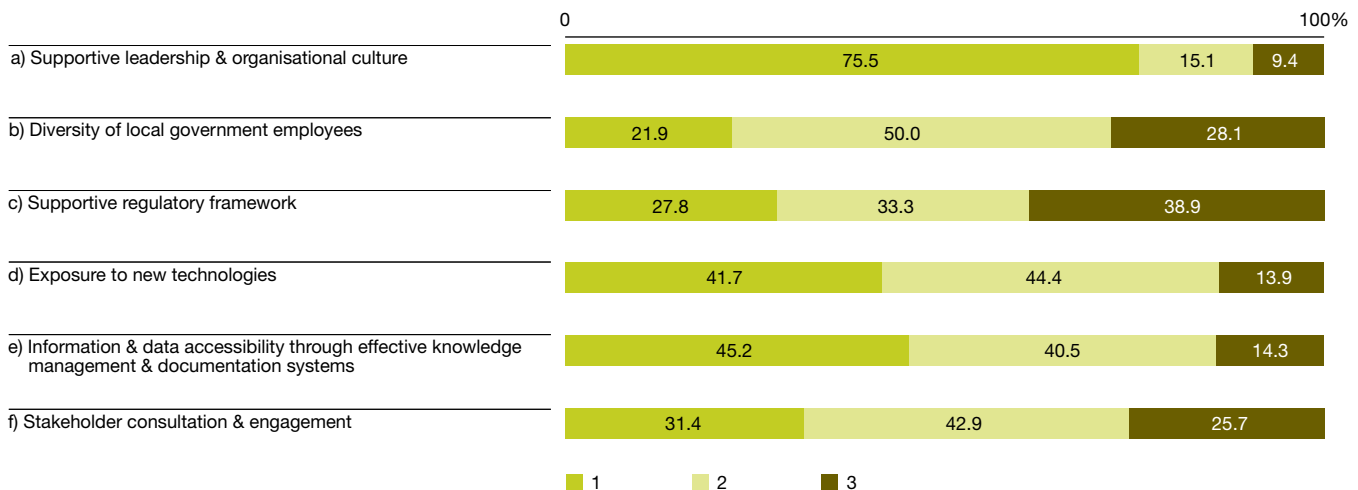
'Innovation has tended to relate to new service delivery in the past, now needs to focus on doing less and doing things more cost effectively.'

## Leadership

Many of those who responded to our survey are aware of the need for other, more positive influencers to be in place for innovation to flourish (Figure 10), particularly a supportive leadership and organisational culture which is clearly the top need across the board. For local government leaders in

**Figure 10**

Please rank the top 3 of the following factors (1 being the highest, then 2 and 3) according to their level of influence on innovation in local government.



Base: Responses for each factor varied from 32 to 53; 'Other' responses not shown.

Developed countries, better management of knowledge and information and stakeholder consultation and engagement were the next most selected factors, whereas for Developing countries a supportive regulatory framework and exposure to new technologies were next in importance.

The importance of strong leadership in transforming organisational performance, and giving the confidence to innovate, cannot be under-estimated in times of major change when both revenues and costs are under pressure. The example of privatised and de-regulated organisations demonstrates this vividly.

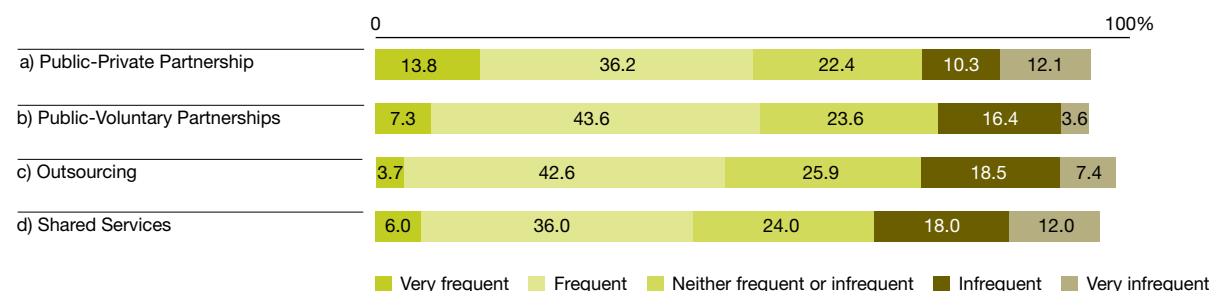
For instance, the telecommunications sector in many countries has been transformed from former state monopolies with often obsolete assets into a global industry with multiple products and markets, and converging with other sectors like media and computing. The winners in these new, de-regulated markets are those organisations which have balanced operational capability with leadership, strategic thinking and innovation.

## Collaboration

The financial crisis does not seem to have had a negative impact on collaboration: indeed, over 80% of respondents felt that there had been no change, or a positive/strongly positive impact of the crisis, on forming local partnerships with other parties and being open to forming/participating in regional and international networks. Frequent use is also being made of public-private partnerships, public-voluntary partnerships, outsourcing and shared services (Figure 11).

**Figure 11**

Please indicate which of the following collaborative partnerships are currently underway in your city/local government and their regularity.



Base for responses for type of partnership varied between 50 to 58; responses may not total 100% as 'Don't Know' and 'Not Applicable' have been excluded.

## Akkoord van Rotterdam: City and local partners hand in hand

Rotterdam businesses have been going through a difficult period, particularly harbour and construction activities, with unemployment high and consequent pressure on the social security budget. In the summer of 2009 the City, the Economic Development Board Rotterdam (EDBR), trade and industry and the education sectors developed the 'Agreement of Rotterdam' (Akkoord van Rotterdam). This is an action plan for both companies and local government to increase the employment of young people by means of training, stimulating entrepreneurship, investing in innovation and sustainability and by bringing forward infrastructure investments. The agreement also aims to stimulate young people to study longer whilst the Social Security Programme creates more jobs for disadvantaged and disabled people. So far the City has spent more than a third of the Euro 323 million reserved for supporting these actions during 2009/2010 .

'The more well-balanced a city is for both businesses and residents, the better it will fare'.<sup>7</sup>

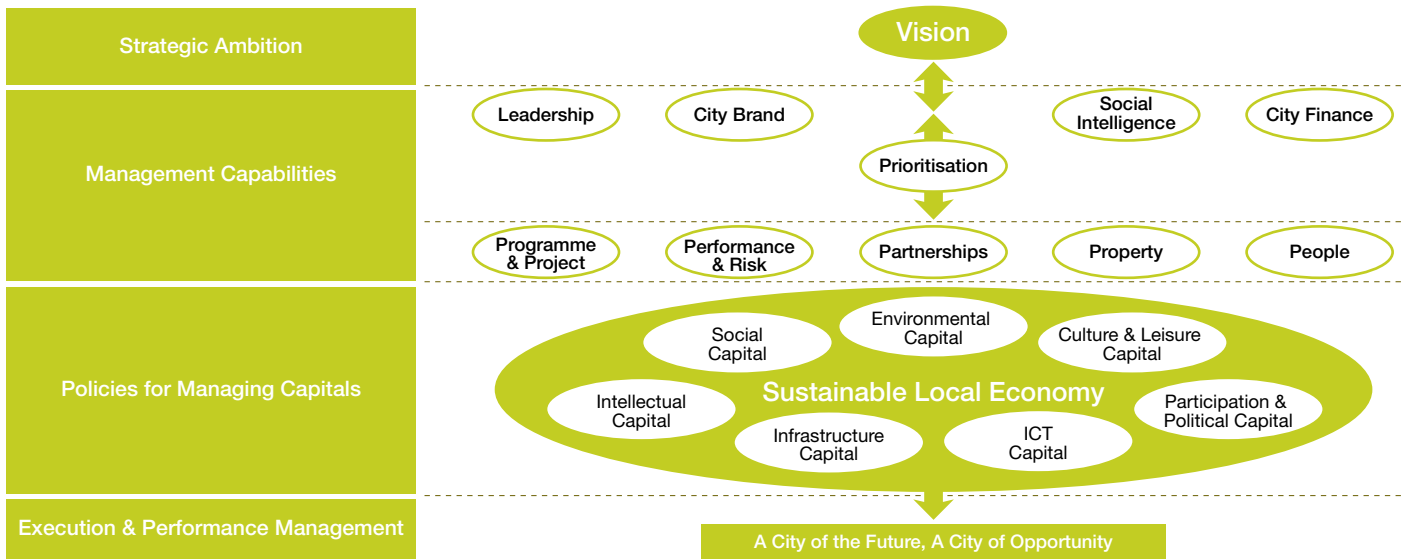
Cities and local governments facing multiple challenges, which were intensified by the financial crisis, have urgently to implement strategies that allow them to compete for business investment, retain talent and attract visitors.

As set out in Figure 12, the management of cities and local governments of the future is a complex affair. We recommend adopting a holistic approach that will take a city forward and allow local government leaders to navigate their economies through the current troubled waters.

The starting point for a city is formulating a clear vision which captures its strategic ambition. In order to channel all resources towards accomplishing the vision, the city's management has to develop multiple internal capabilities: an inspirational leadership, a resilient city brand and an ability to learn from other cities through social intelligence. Under the current circumstances, managing finances effectively is becoming an extremely essential enabler, together with managing the city's projects, performance risks, partnerships, assets and human capital.

Developing a clear vision and internal management capabilities allows a city to prioritise, invest in and strategically manage the building blocks or 'capitals' needed by any city for long-term prosperity – social, environmental, cultural, intellectual, infrastructural, ICT and political participation capitals. By putting in place and implementing the appropriate policies, a successful city will maximise its investment in those capitals which are most relevant to its strategic vision, while optimising its investment in those capitals which are less relevant.

**Figure 12**  
PwC's holistic approach



Of course, all of this must also be done in a way that is sustainable and through collaboration and partnering with citizens, the private sector, academia and NGOs. This approach is being adopted by visionary cities and local governments as a framework to think through the challenges of transformation and to help balance the competing priorities facing city and local government managers.

<sup>7</sup> 'Cities of Opportunity', Partnership for New York City/PricewaterhouseCoopers, March 2010

# A multi-tiered response

We set out to understand the actions being taken already by local government leaders and whether they are enough, in terms of their scope, speed and depth.

## Service transformation and rationalisation

Figure 13 shows views on the perceived effectiveness of a range of responses to the financial crisis. It is clear from the research that de-layering and selling assets are not the answers – all had relatively low responses – whereas service re-design and rationalisation are critical, along with collaborative procurement (mainly in Developed countries, 46%) and, in Developing countries, re-structuring (55% of local government leaders view this as extremely or quite effective).

‘Business transformation has taken on greater urgency as a result of financial crisis and need to deliver services with less resource and greater efficiency.’

## Acting at strategic, operational and tactical levels

Our findings on the effectiveness of different approaches is revealing and points to the need for a programmatic, multi-tiered response to the crisis. Such a coordinated programme requires a balance of actions which combine strategic, operational and tactical actions.

### Strategic

- Redesigning services and innovating delivery models (e.g. early intervention and prevention and transforming service delivery models): 78% of our respondents believed that understanding the root causes of issues and moving to prevention models was somewhat or extremely important

to delivering services within available budgets. Access to management information, perhaps to support this, is somewhat or extremely important for 84% of respondents.

- Citizen-centric innovation – as part of re-designing services, 86% of respondents agreed that engaging citizens in the decision making process was somewhat or extremely important.
- Economic development/attracting inward investment (86% of respondents) and addressing the environmental challenge (90%) are also important strategic actions.

### Operational

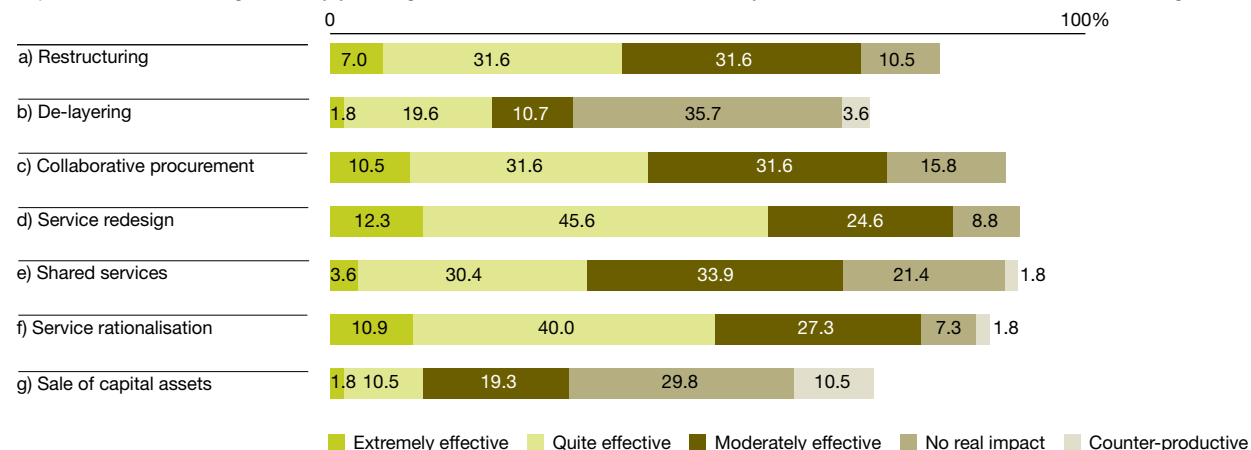
- Addressing cultural barriers to change: 70% felt this to be somewhat or extremely important.
- Co-ordinating effectively across the public, private and third sectors: 91% saw this as somewhat or extremely important (with over two thirds of local government leaders seeing collaborative procurement, shared services and restructuring the public sector as effective responses on this agenda).
- Service rationalisation (including reviewing the balance of the service portfolio and deciding upon which services to deliver): 78% of respondents see this as an effective operational response.

### Tactical

At a tactical level, cost cutting initiatives come to the fore largely as an output from the above strategic and operational responses.

**Figure 13**

How effective do you believe that these measures will be in addressing the challenge arising from the financial crisis. Please indicate the main responses that are being taken by your organisation to the financial crisis and your view on their effectiveness in addressing the challenge.



Base for responses to crisis varied between 55 to 57; responses may not total 100% as 'Don't Know' and 'Not Applicable' have been excluded; 'Other' responses not shown.

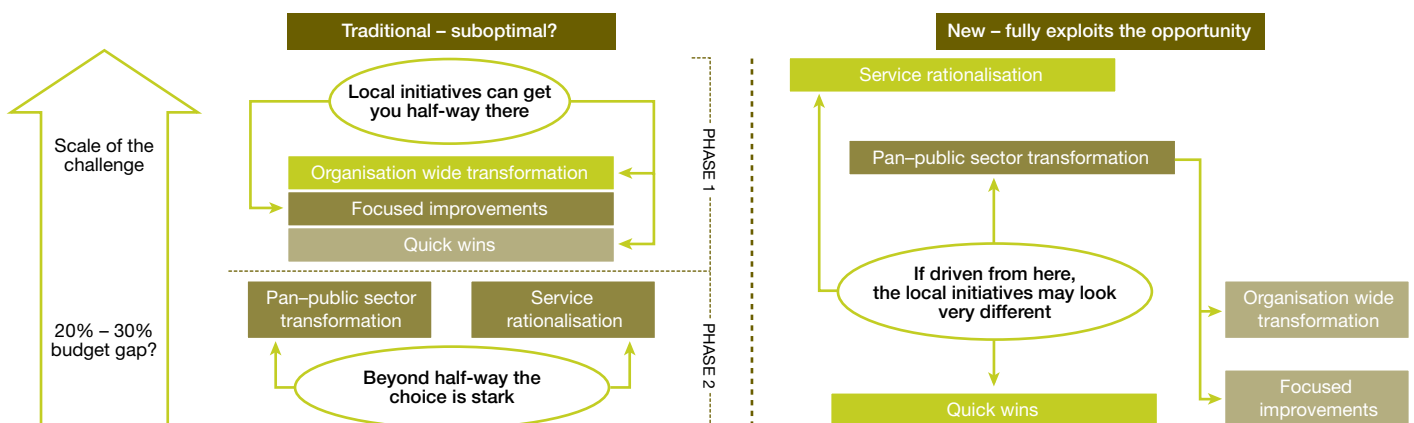
## PwC's view

The severity of the challenge facing local government leaders requires a new approach which includes:

- Resetting the vision and outcome expectations at the local level;
- Identifying the likely impact in each possible area of spend;
- Developing the right strategic approach against the scale of the challenge;
- Creating the cross-cutting programme that is right for recessionary times:
  - Looking harder for cost reduction and transformation initiatives that the organisation has not yet embedded;
  - Considering changing service levels;
  - Planning for key scenarios – avoidance of bad risks is always cheaper than management of the problem created; and
  - Transferring activity where possible and ethical.

Now is a golden opportunity to make a step change and grasp the challenge of service transformation and pan-public sector working first, rather than build up to it later (Figure 14). Indeed, Developing countries, with less fiscal worries, have a real opportunity to leap-frog Developed countries and lead the way.

**Figure 14**  
Making a step change



Given the size of the challenge, the traditional response would be to seek to identify local quick wins and improvements. In our experience, this will only provide part of the solution. However, even setting off on the journey in this manner may reduce the ability of city and local government leaders addressing the full magnitude of the challenge.

The better approach would be to start with the more strategic agendas around service rationalisation and driving collaboration across the wider public sector operating in the local community. This is the more challenging approach but this is time for leaders to show their leadership skills beyond the boundaries of their own organisations. The more traditional responses can then 'top up' any residual deficit.

## Total Place – towards a new service model for Londoners

Of £73.6 billion of public money spent in London in 2008/09, less than half was directed through bodies that are directly accountable to Londoners. This complex web of nationally run services produces a range of weaknesses in public service. Overcrowding of agencies can lead to confusion in delivery while different national goals often can conflict with each other. We found that this can undermine some of the key foundations for successful public services including early intervention, 'case management' support to individuals that cross many agencies and providing individuals with the ability to choose how and when they use public services. We identified that a more devolved and direct approach to funding could help improve services and save taxpayers' money: we identified potential savings of almost 15% i.e. as much as £11bn per annum.

# The future for cities and local governments

The results of our survey demonstrate that local government leaders face major challenges not just financially but in terms of building the brands of their localities, engaging and providing leadership for their communities and working collaboratively with an ever growing network of partners, across sectors and geographies, both nationally and internationally.

This requires nothing less than a transformation of local and city-wide management. Figure 15 sets out, at a high level, the key elements of the operating model for cities and local government, which in turn poses some important strategic issues for local government leaders.

## A focus on outcomes

For too long, local government leaders have responded to often centrally imposed targets and measured their performance against performance indicators which have not always connected to outcomes. In the new world, where the mantra is to do the same with less, a focus on outcomes is critical with the associated cycle of needs assessment, service policy and sourcing, service design and delivery and monitoring and evaluating performance against local outcomes.

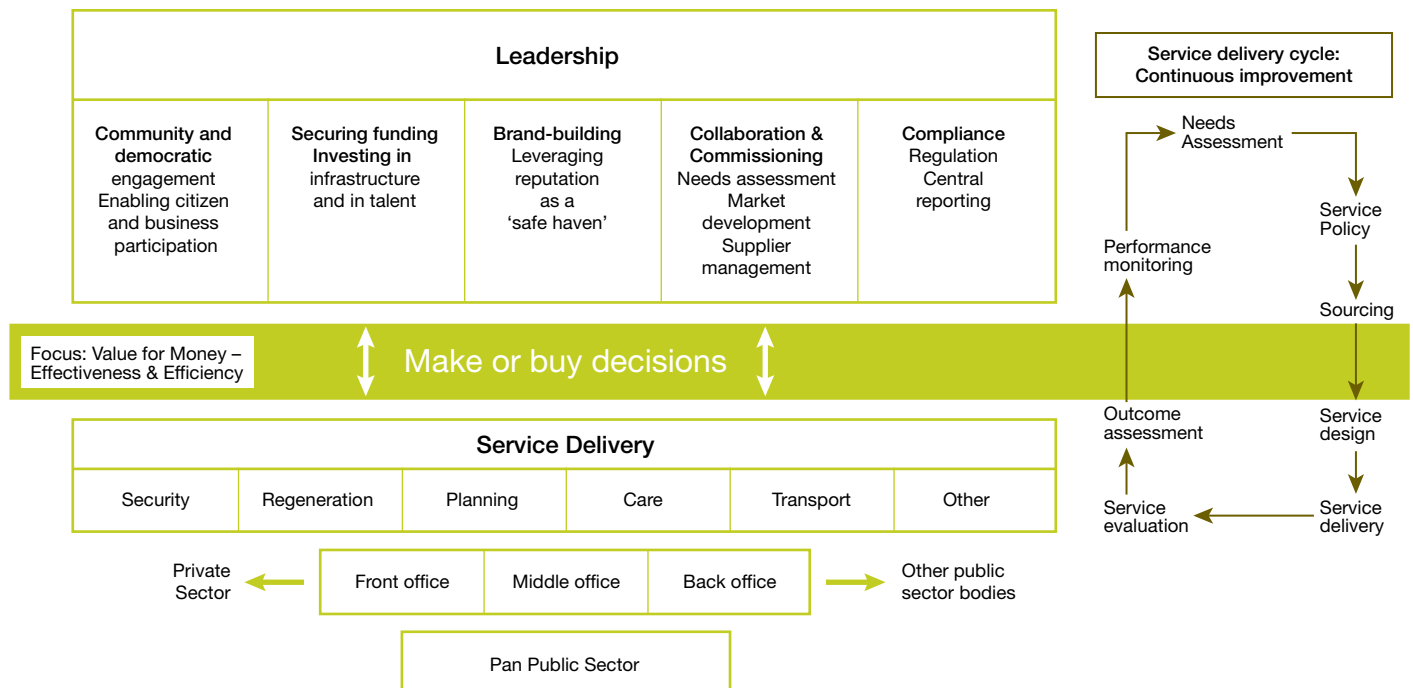
## Make or buy?

As part of this cycle, there is always a choice between providing services in-house or purchasing them from private or voluntary/not-for-profit enterprises. Local government leaders must decide which functions are so critical to their performance, and so risky if they go wrong, that they must be kept in-house. In reality, the number is small, but important such as providing social care, children's services and a safety net for the disadvantaged.

## Role of commissioning

There are many other services, such as cultural e.g. libraries, and leisure e.g. parks and community spaces, where the decision should be made on the grounds of value-for-money and where purchasing the services may represent better value than keeping them within local government.

**Figure 15**  
A new operating model





Where the decision is taken to buy, the role of local government as a strategic commissioner becomes of paramount concern. The skills and capability to procure are not the same as those to commission. The latter requires the ability not only to set up and monitor contracts but to:

- undertake a robust assessment of needs;
- shape and develop the market of providers to supply the services, particularly if this is under-developed in a locality; and
- manage relationships with suppliers to ensure quality is delivered and value for money achieved.

There are also some key implications for private and social enterprises seeking to provide the services needed by cities and local government, as set out below.

### Some messages for private and social enterprises

- **Context:** each city and local government will be at a different point in the cycle – many in the Developed economies will need help to address the crisis which faces them of budget cuts and a collapse of local revenues. In contrast others, particularly in Developing economies, may be looking to jump a generation and learn the lessons from cities and local governments in the Developed countries e.g. from Public Private Partnerships and outsourcing ventures, including the mistakes to avoid.
- **Strategic:** private and social enterprises need to understand the implications of the ‘make or buy’ decision and the scale of the potential markets that may be created by the onset of public sector recession at a local level. This will provide the business case for their investments in these markets.
- **Relationships with commissioners:** local government leaders will still need to deliver key outcomes and so will need the help of the private sector to do so – this will require private providers to get closer to the commissioners to understand better their needs now and in the future.

## Shared services

Sharing services across organisational boundaries to reduce costs is a concept whose time has very much arrived. However, local government leaders have the opportunity to go beyond their boundaries and work with others, such as in health, to bring about pan-public sector shared services which really leverage every pound spent and ensures the maximum is focused on front-line services.

Increasingly, these services are also not only in the back office e.g. finance, IT and human resources, but in the middle and front office, making use of shared assets and staff to meet multiple needs in the one facility, such as personal advisors navigating individuals across the range of educational, health and social interventions they need to become productive members of society.

To address all of these challenges requires a long term, well managed programme of transformation which in turn will require leadership and determination to see through to conclusion. Given the size of the budgetary challenge, however, there will also be a need for quick wins to go alongside investments which improve performance in the medium to long term whilst also keeping people engaged during a major period of organisational change.



# Conclusions and implications

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Although cities and local governments face different challenges, they can learn from each others' experiences, especially from international good practices, and from the private sector and so emerge from the global financial crisis stronger and better able to adapt to future challenges. But local government leaders must act now, and not let the window of opportunity close before they have taken full advantage.

To do this, cities and local governments must adopt a comprehensive approach, starting with a clear vision and supported by the enabling capabilities of leadership, culture and brand. Local government leaders must take charge of the situation they will find themselves in and develop a multi-tiered approach so that they can better respond to the challenging global economic and financial conditions that we anticipate in the next 12-18 months.

Cities and local governments must also look forward and act as intelligent investors. For growth not only to take off but be sustained, local governments must invest strategically and sustainably in the various 'capitals' needed by any city for long-term prosperity. Clearly, the priority should be projects with a high social and economic return, particularly in infrastructure, which assist private sector wealth creation. Importantly, cities and local governments should be wary of cutting investment plans to balance the books – this will not solve fiscal deficits, and will only serve to solve today's problem at the expense of creating new ones for tomorrow.

Cities and local governments cannot, however, act in isolation any more and must collaborate both cross-sector and regionally, to build 'joint capitals' such as intelligent transport systems, as well as across administrative boundaries, to join up critical public services like health and social care.

Most importantly, cities and local governments must continue to re-build the confidence of the private sector, which is the source of future growth and revenue (through local taxes and charges). There is a need for intelligent and authentic leadership and vision and for policies and mechanisms for collaboration appropriate for today's globalised economy.

**Local government leaders** therefore need to:

- get back to basics, prioritising between core and optional services and ask whether services and activities are needed to fulfil legal obligations, to meet local needs or simply because 'we've always done it this way' (and could therefore be stopped or done radically differently):

- focus on retaining talent, identifying the critical functions for local government and protecting the talent critical to delivering these functions;
- design and develop new service delivery models, particularly commissioning and early intervention and prevention models; and
- collaborate across agencies, private and voluntary sectors and also spatially, across geographies.

There are also some important implications for **central governments** which need to:

- provide a stable and sustainable framework within which local government leaders have the freedom to invest strategically and sustainably in the various 'capitals' needed by their cities for long-term prosperity; and
- put in place the mechanisms to facilitate collaboration more easily across geographical and administrative boundaries to assist in the creation of 'joint capitals'.

Finally, for **private and voluntary enterprises** the challenges are to:

- develop the business case for their investments in local markets by understanding better the implications of the 'make or buy' decision and the scale of the potential markets that may be created by the onset of public sector recession at a local level;
- build relationships with commissioners and understand better their needs now and in the future; and
- work with local government leaders to create a business environment attractive to business.

Local government leaders must therefore shift gear, from being reactive to events to acting now, with businesses, citizens and central government, to ensure that as the global economy takes off towards growth they are not left behind.

# Appendix: Approach

## Method

The research survey was undertaken by PricewaterhouseCoopers LLP. It covered the UK, Europe, Middle East, Asia, Australasia, Africa, South and North America. A combination of paper based, telephone and face to face interviews and e-surveys were sent to leaders in cities and local governments. The survey ran from September 2009 to the end of February 2010. The findings for this report were drawn from 58 completed surveys across the countries listed in Figure A1. The results were also split by Developed countries (33 responses) and Developing countries (25 responses). A further 215 cities and local governments responded to surveys in Brazil, Sweden and Netherlands which are included in separate reports for these countries.

**Figure A1**

By city and country

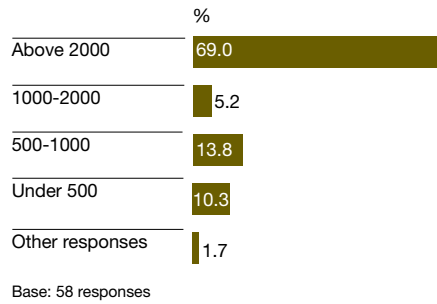
Country	Organisation
Belgium	Brussels Capital Region
Brazil	Prefeitura Municipal de Belo Horizonte
	Prefeitura Municipal de Campinas
	Prefeitura Municipal de Jundiai
	Prefeitura Municipal de Salvador
	Prefeitura Municipal de Santo André
	Prefeitura Municipal de São Paulo
Canada	City of Saskatoon
	City of Toronto
Chile	Las Condes Municipality
	Providencia Municipality
China	Shanghai – Shanghai Institute for International Studies (SIIS) – Foreign policy consult
	Shanghai – Shanghai Institute for International Studies (SIIS) – Research (International Relations)
	Shanghai – Shanghai Institute for International Studies – Think Tank
Czech Republic	Ostrava Municipality
Denmark	City of Aarhus
France	City of Bordeaux
	General Concil of Gironde 33
	General Concil Hauts de Seine 92
Germany	City of Essen
	Nürnberg
India	Bangalore
	Municipal Corporation of Greater Mumbai
Kenya	Municipal Council of Kisumu
	Municipal Council of Mumbasa

Country	Organisation
Latvia	Daugavpils City Council
	Valmiera Town Council
Luxembourg	City of Luxembourg
Netherlands	City of Dordrecht
	City of Roosendaal
	City of Rotterdam
	City of Utrecht
	City of Waalwijk
	City of Wijchen
New Zealand	New Plymouth District Council
Saudi Arabia	Jeddah Municipality
	Mecca Municipality
South Africa	City of Johannesburg
	eThekweni Municipality
	Kwadukuza Municipality
	Nelson Mandela Bay Municipality
	uMgungundlovu District Municipality
Spain	Bilbao City Council
	Diputacion Foral Alava
Sweden	Göteborgs Stad
	Helsingborg
	Landstinget Halland
	Landstinget i Värmland
	Uppsala kommun
Switzerland	City of Geneva
	City of Zurich
	Kanton Basel-Stadt
	Ville de Lausanne
United Arab Emirates	Western Region Municipality
United Kingdom	Bexley London Borough
	Birmingham City Council
	Greenwich Council
	London Borough of Camden

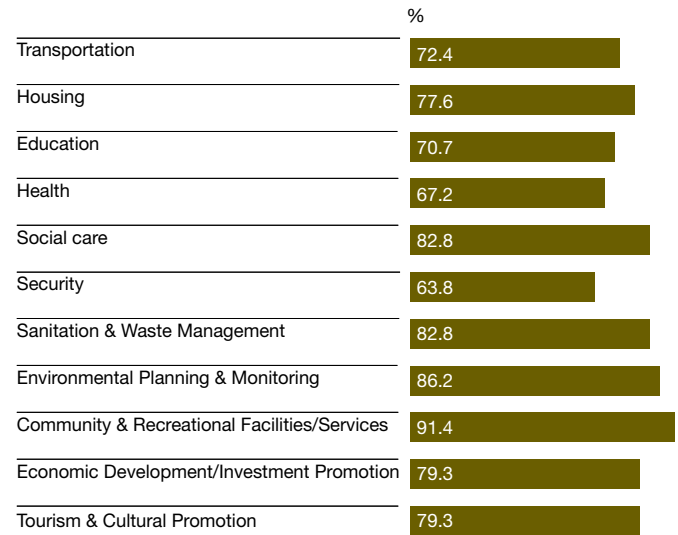
## Sample characteristics

The following charts set out the structure of our sample by size (measured by both value and employees) as well as the range of services provided.

**Figure A2**  
Size by employees

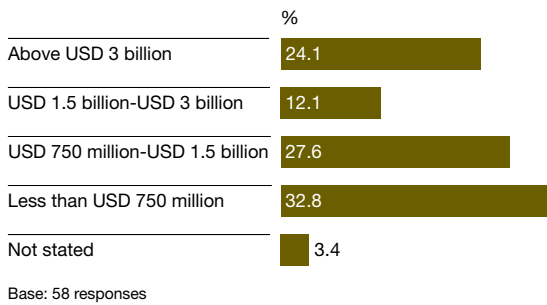


**Figure A4**  
Services provided by the organisation  
(Respondents were allowed to choose multiple responses)



Base: 58 responses; 'Other' excluded

**Figure A3**  
Size by budget (Annual budget for 2008 or 2008/9)



# Acknowledgements

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The following individuals in PricewaterhouseCoopers contributed to the production of this report.

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## About PricewaterhouseCoopers

PricewaterhouseCoopers' Global Government practice has been helping Government and public sector organisations locally, regionally, nationally and internationally for many years. We work with organisations across sectors as diverse as health, education, transport, home affairs, criminal justice, local government, housing, social welfare, defence and international development. Our people combine deep specialist expertise with a genuine understanding of the public sector.

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Designed by studioec4 20225 (04/10)